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EUROSYSTEM

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# Introductory remarks

By Chiara Zilioli\*

It is a pleasure to see how over the years we have built up a network of interested people that follow our events with great interest and participation. Every year we note with pleasure and a bit of surprise that this network keeps increasing in size and extension.

Since 2015 the ECB has hosted a yearly legal conference, alternating, in even years, our **European System of Central Banks (ESCB) Legal Conferences**, which provide a platform for the discussion of technical topics of interest from a central bank and supervisory perspective, with, in odd years, our **ECB Legal Conferences** which focus on more institutional, constitutional and judicial issues.

To contribute to the green ECB objectives, with the aim of cutting our carbon emissions by half, the ECB has decided that only 50 % of all the meetings it organises, conferences included, will be in person, as virtual conferences help reduce our carbon footprint.

This is the reason why from now on our ESCB Legal conference every other year will be an online event. We are convinced that personal interaction is still superior in many respects, for example for brainstorming and networking in the margins of the event. On the other hand, a virtual conference has the advantage of enormously widening the potential outreach of our activities.

Therefore, balancing the various objectives, we decided to make use of the lessons learned and open the virtual doors of our **ESCB Legal Conference** to the public.

The common thread for the first three chapters of this book is that they concern developments for which COVID-19 acted as a catalyst, promoting, amplifying, or simply speeding up change. The common thread for the subsequent three chapters concerns the principle of the rule of law, which importance in the EU framework has been acknowledged by the Court of Justice of the European Union in the last years, and how this principle interacts with specific elements of the ECB's activities.

## 1 The COVID-19 crisis as a catalyst for change

The lockdown policies adopted to contain the virus in the past years have forced legal professionals, as everybody else, to dramatically change the way they access, produce and share information. Technical advancements have gone hand in hand with the steep increase in people's technical capabilities. Indeed, lawyers are not known for being either a particularly progressive or a tech savvy category of

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professionals. Yet many of us learned to sign documents electronically, plead virtually, and communicate with our stakeholders visually. As the computer became our means to interact with them, we were offered almost unlimited technical possibilities to demonstrate our thinking – which before had to be accessed through legal language, often considered obscure and arcane by non-lawyers. If our thinking can be visualised, visualisation techniques can be used to communicate and provide explanations using “*design thinking*” in the legal field as well. While this may in turn seem obscure and arcane to many lawyers right now, this is a growing trend which presents enormous advantages. Soon, mastering (legal) visualisation techniques will probably be as essential for a lawyer as using word processing software was in the 80s and 90s.

Legal professionals may be late adopters, but they have recognised the opportunity. Lawyers can exploit these developments for multiple purposes: to design better legal frameworks; to structure and better explain complex thinking and deal innovatively with their clients’ most complex problems; to prepare and conduct litigation; and to share and communicate knowledge and good practices. These are the techniques, the questions and opportunities that the first chapter examines.

Lawyers were certainly not the only ones whose habits were affected by the changes introduced as a consequence of the COVID-19 crisis. The implications of the new ways of interacting and working have been immense for the economy at large. Massive supply chain disruptions over the last couple of years have given rise to a new wave of reshoring. Due to other issues, such as current geopolitical tensions, it is also far from clear whether this is only going to be a temporary phenomenon.

## 2 The impact of the COVID-19 crisis on the financial sector

Changes in the economy have of course had an impact on monetary policy, and the changes in the discourse around inflation are in part a reflection of this reality. Monetary policy, or at least its degree of effectiveness, has also been affected by other changes within the financial sector. In this case, the COVID-19 crisis provided the occasion, rather than being the trigger, to test and understand the magnitude of certain trends of the past.

Over the past few years the role of the non-banking sector has increased. This has been visible, for example, in the way fire sales of assets held within the non-banking sector can affect the even and orderly transmission of monetary policy as well as financial stability. As the monetary policy framework is currently centred around credit institutions, several elements of this legal framework would need to be changed to make it possible to open central bank monetary policy facilities to non-bank entities. Several economic arguments warrant consideration of this policy option, in particular for money market funds. In this respect, a comparison with the experience of the New York Federal Reserve Bank with regard to the extension of its facilities to these entities is particularly relevant.

Financial disintermediation is a trend that goes beyond the wholesale sector and affects the retail sector as well. E-commerce has accelerated the increase in the use of electronic payments in the past decades. Such trends have accelerated further during the pandemic, due to lockdowns. Many people, often for the first time, were confronted with the need or simply had the time to consider the possibility of moving on from traditional payment in cash, owing to the alternative means of payment offered by modern technologies. The general public's growing adoption of digital forms of payments has been one of the key drivers for the central bank community to gear up their efforts to offer central bank digital currencies (CBDCs) as the anchor of a new digital payment environment. One of the functions of central bank money is indeed to serve as an anchor to the financial system as a whole, following the basic assumption of the convertibility at par (one to one) of commercial bank monies (e.g. bank deposits) in cash. It is thanks to this assumption that the general public trusts currencies over and beyond questions relating to operational, credit, liquidity and market risks in relation to the issuers of commercial money than it otherwise would. This, in turn, means that digital forms of privately and publicly issued money complement rather than oppose CBDCs, but also that the issuance of CBDCs is necessary to keep the trust of the general public in currency. Clearly, however, the relationship between digital commercial money, on the one hand, and central bank money, on the other, is central to keeping the stability of the system in the future and this question of "*interoperability*" is the focus of the discussion of the book's third chapter.

The issue of interoperability is not, however, exclusively confined to the domestic dimension and the relationship between CBDCs and commercial monies in the same denomination and currency area. Indeed, there is an international dimension to the issue as well. One of the catalyst moments which prompted an acceleration in the studies of CBDCs was the launch of a proposal, by an alliance of several market participants, known as "Libra" (later renamed "Diem"), a few years ago. Central banks were prompted to analyse in detail the technical and legal requirements of CBDCs due to the risks suddenly implied, in a concrete and actual manner, by global stablecoins; having the potential to disrupt the existing payment systems and the role of official currencies. In particular, one of the main concerns of central banks was to avoid that the wide use of stablecoins denominated in a third country currency (or even a third country CBDC) could limit the transmission of monetary policy and therefore monetary sovereignty. Remarkably, the main problem that "Libra" was supposed to address was that of payments across borders, which generally also means payments across currencies. Against that background, if the objective is to allow for cross-border payments in the new environment, interoperability between different CBDCs will be a key question to solve. Yet, the question of how CBDCs interact inevitably also has repercussions on the way CBDCs are designed for internal use, as a minimum in relation to questions such as the possibility for non-residents to hold CBDCs in their own domestic jurisdictions and the ways in which residents and non-residents alike can make use of CBDCs for payments in foreign jurisdictions. From a policy perspective the latter point is also relevant for the international role of certain major currencies, including the euro, while from a purely legal perspective, this problem raises numerous and interconnected questions of international and civil law that require a holistic analysis.



### 3 The rule of law

Let me now move to the last three chapters of the book. They do not relate to topics that have a connection with the COVID-19 crisis. Rather, their common thread is a principle that is very dear to the ECB: the rule of law, which also featured prominently in the programme of last year's ECB Legal Conference. Defending the rule of law is a formidable task. Last year, the Court of Justice delivered two historical judgements in cases brought by Hungary and Poland, revolving around the possibility and legitimacy of the attempt on the side of the EU legislator to define the principle of the rule of law. In broad terms, the Court of Justice held that the principles of legality, legal certainty, prohibition of arbitrariness of the executive powers, effective judicial protection, separation of powers, non-discrimination and equality before the law are all principles that have been acknowledged and confirmed as being part of the EU legal framework in its own jurisprudence, and it is therefore legitimate to have recourse to those principles to define the concept of the rule of law for the purposes of a specific regulation. Importantly, the Court of Justice rebutted the argument that the scope of application of the rule of law principle in the EU framework should be limited to the independence of the judiciary.

More than 2000 years ago, the Greek philosopher Aristotle, in his work "Politics", described the rule of law as the principle that no one is exempt from the law, no matter their position or their power, and that all people and organisations within a jurisdiction are held accountable to the same set of laws. This applies to the ECB as well. In reaction to the Commission's Communication on further strengthening the rule of law within the Union, the ECB published a document in 2019 where, from a central bank perspective, the focus was on the ways the principle of the rule of law and the instruments embedded in the Treaties should shield central banks from undue interferences with their independence within the EU legal framework.

The ECB and its lawyers are very attentive to the duty for our institution to comply with the Law with capital letters, beyond the narrow scope of the regulatory framework applicable to the ECB as a central bank or a banking supervisor, and even in those cases where rules as generally applicable would not normally apply to the ECB by virtue of our special status.

A comparison of the ECB's internal review procedure for contract award decisions with the legal framework for the review of such decisions in other EU, international and national organisations is particularly relevant in this context. In this regard, the ECB enjoys a particular status as an EU institution, exempted from national laws regulating the internal organisation and administration of public authorities and in particular from national budgetary or national procurement laws. The ECB is however subject to EU law, including EU procurement law. On the basis of and in the implementation of EU procurement law the ECB has established its own framework regulating various types of ECB tender procedures, as well as some exemptions for special types of contracts and other special cases. An important element of the principle of the rule of law is formal justice, at the core of which is the principle of equal treatment. Against this background, procedural justice ensures the correct application of legal rules and can complement the role of judicial adjudication in preserving the rights of those subject to

the legal rules. In this context, bodies reviewing administrative decisions, which have been on the rise in the EU in recent years, enhance such procedural justice as a second opportunity is given to the administration to reconsider whether it applied the relevant rules in the appropriate manner in a specific case. The appeal procedure before the ECB's Procurement Review Body (PRB) is a typical example of such a remedy offered to unsuccessful candidates and tenders to advance their rights, as a first recourse before turning towards judicial remedies. The PRB is set up as an internal body that is independent from the office carrying out the award procedure and is supported by the ECB's Directorate General Legal Services. The PRB has two main functions: first, it potentially deflates the number of cases that reach the stage of judicial adjudication, achieving judicial economy; second, it offers an additional chance for the ECB decision-making bodies to evaluate the appropriateness of their administrative decisions, thereby allowing the fullest implementation of the principle of good administration.

## 4 Banking supervision and other legal rules

Other material and substantive aspects of the rule of law pertaining to the effective protection of individual rights, and in particular human rights, are no less important. In this context, and as a consequence of fast technological developments and the growing use of personal data, the importance of protecting privacy and personal data is growing ever more critical. So much so that, building upon pre-existing jurisprudence of the Court of Justice, the right to the protection of personal data is part of the EU Charter of Fundamental Rights that all EU institutions are bound to abide by. Against this background, the Single Supervisory Mechanism (SSM) represents a fitting context to take stock of these trends and developments in practice. Because the SSM is itself a relatively recent institutional setup still in development, and also due to the fact that in pursuing its tasks as banking supervisor, the ECB receives personal data and has several arrangements in place to ensure compliance with the EU Data Protection Regulation (EUDPR), as is also the case with national supervisors that have to comply with the very similar provisions of the General Data Protection Regulation (GDPR). One practical situation in which supervisors have to comply with those requirements concerns personal data received in the context of fit and proper assessments. This is one of the most important tasks in prudential supervision. In accordance with Article 4(1), point (e) of the SSM Regulation, since November 2014, the ECB has the exclusive competence to review the suitability of members of the management body of significant credit institutions of Member States participating in the SSM.

A further aspect concerns potential conflict situations occurring between the obligations of supervisors under their professional secrecy regime and those under data protection rules. Against this very complex background, the Data Protection Officer plays a crucial role (in the ECB as in other institutions). It is an independent function, which the ECB's Directorate General Legal Services have the honour to host, and which is key in finding the appropriate balance between the often opposing needs of supervisory law, on the one hand, and data protection rules, on the other, in order to

show that reconciliation is possible in practice and that the two regimes are not necessarily mutually exclusive.

Another case of potential overlap and interaction between the banking supervision framework and a different set of rules concerns the legal framework on anti-money laundering (AML) and combating the financing of terrorism (CFT). This interaction has become more prominent in recent times due to several instances that gained the attention of the general public. In the last chapter the authors focus on the fascinating question of how it is possible to reconcile the exercise of the ECB's duty of diligence as an extension of the principle of good administration and its exclusive responsibility for taking supervisory decisions against the limitations deriving from the application of the principle of conferral, given that the legislator has explicitly excluded AML and CFT from the tasks conferred on the ECB by the SSM regulation. It demonstrates the issue of how authorities that have different but complementary and interlinked responsibilities must interact and cooperate. Needless to say, a point of reference for this discussion is provided by the clarifications which the General Court of the European Union has provided, particularly in its recent judgements in the *Versobank* and *AAB* cases. Moreover, the panel will also touch upon the recent developments in the applicable legal framework, such as the enhanced mechanisms aimed at ensuring a better cooperation between banking supervisors and AML/CFT authorities.

## 5 Looking ahead

The COVID-19 crisis which erupted in February 2020 has been the defining moment for everything that happened in the following two years. Sadly, I am afraid, the war Russia started against Ukraine in February 2022 will be remembered in the future as a defining moment for a period, which length is impossible for us to foresee. There are some who argue that academic independence requires distance from politics. While this is a very disputable assumption for any branch of science, it is one that is very difficult to argue in the case of law: the core of our discipline concerns rights and obligations of people and organisations, including Governments. Indeed, the rule of law is a principle that not only applies in national law and in EU law. Likewise, in international law there are laws that are agreed by all countries and that apply to all countries. This lies at the very core, and serves as the essential purpose of, international law and is reflected in the United Nations Charter, which refers to the obligation for Members to “settle their international disputes by peaceful means in such a manner that international peace and security, and justice, are not endangered” (Article 2(3)); and that all “Members shall refrain in their international relations from the threat or use of force against the territorial integrity or political independence of any state, or in any other manner inconsistent with the Purposes of the United Nations” (Article 2(4)). Every time a country initiates an armed conflict in another country's territory to solve an international controversy, international law is brutally violated – and this without even mentioning those cases where abject crimes are perpetrated against unarmed civilians: there we speak of crimes against humanity. The close interrelation between the domestic order and the international order is magisterially portrayed by the philosopher Immanuel Kant in his book “Perpetual Peace: A Philosophical Sketch”, credited by many as a key source of inspiration for the way

international law and the international order have been built over the course of the past century. The European Union, of which the ECB is part, is a great and successful experiment in the context of maintaining peace on our continent. Witnessing war again on European soil is something we all would have preferred to be spared from and our hopes are that by the time our next ESCB Legal Conference takes place, hostilities will have ceased and peace will have returned. And, who knows, maybe it will be possible to visit Lviv again, the beautiful Ukrainian city I visited two years ago and the city where both Hersch Lauterpacht and Raphael Lemkin, the two lawyers who identified in international law the crimes of genocide and crimes against humanity, grew up and studied. The beautiful book “East West Street” by Philippe Sands describes the events of that time. Let us hope that they will not repeat themselves today.

## Panel 1

# Visualisation and legal design thinking: the steady transformation of legal practice



# On visualisation and legal design thinking: the steady transformation of legal practice

By Hilde Hardeman\*

The rule of law is at the very core of the values on which the European Union and our societies are based. All of us contribute, in one way or another, to turning the rule of law into practice. This work – our work – is never finished. It affects everything and everybody, everywhere in our societies, at all times. Developments in the world around us make it even more obvious how important this really is. So how we shape our legal practice, in all its emanations, is crucial for every individual, our societies, our economy and our way of life.

The Publications Office of the European Union plays a systemic role in the decision-making processes of the European Union, and thus for the rule of law in the EU and beyond: it is the Publications Office that authenticates and publishes EU law to give it legal effect. It is thanks to our work that citizens get to know the law, can apply it and can use the opportunities it offers in their daily lives.

Democratic legitimacy, citizens' trust and, therefore, democratic resilience depend on how government and citizens, state and society interact. As publishers of the *Official Journal of the European Union*, we have a crucial role to play in bringing government and state to citizens and society, in a way that makes sense to them. Our aim is to provide widespread understanding of, and easy access to, the law applicable within the EU. This is essential for transparency and thus for citizens' trust, and also for the proper functioning of the internal market, our economy and our societies.

By making the entire corpus of law that applies in the EU findable and readable across language barriers, for both lay people and specialists, by making it seamlessly navigable and by allowing both humans and machines to interact with it, we aim to support citizens and businesses, as well as legal practitioners, courts and public administrations, not only in knowing the law, but in making the most of all of the opportunities the EU offers, with tangible benefits in everyday life.

The fact that we can make use of digital technology, for example artificial intelligence, creates opportunities that did not exist a few decades ago. This is an excellent development.

Artificial intelligence can help to increase the transparency of decision-making processes, demonstrate in practical ways how decision-making at the EU and national levels is closely intertwined and allow citizens and businesses a personalised view of what these decisions mean for them in real life, in their specific situation, with information in the language they speak and in a form they understand. Artificial

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intelligence helps us to achieve this through its unique capacity to map, classify, link and search the vast landscape of EU law and jurisprudence across language borders and jurisdictions. It also allows us to make information accessible in an inclusive way, including for people with disabilities, to fine-tune search mechanisms and to customise information to individual needs, in ways that human efforts alone could never achieve.

At the same time, the basics are as old as humankind, and as important today as they were when women and men first started to organise things between themselves using rules: the need for clear and easily understandable language, well-structured argumentation and visualisation.

That is precisely what this chapter is about. Frédéric Allemand, Filip Lulić and Marie Potel-Saville, three distinguished professionals, who work every day to show how visualisation and design thinking can help optimise legal practice, share with you their insights and experience. With visualisation and legal design thinking, they seek, each in their own way, to help citizens, economic operators, public servants, societal actors and scholars to understand and reap the benefits of the democratic, rule-of-law-based system we are so proud of and so attached to in every aspect of their lives.



# Lost in legal data visualisation? A legal scholar's view on the ECB-dedicated section in EUR-Lex

By Dr. Frédéric Allemand\*

## 1 Introduction

In collaboration with the ECB, the Publications Office of the European Union (hereinafter the "Office") has extensively redesigned the EUR-Lex website section dedicated to ECB legal acts and ECB-related documents. Unlike other sections, the ECB section introduces a new way of viewing legal acts and navigating through the corpus of ECB acts. At the ESCB Legal Conference in 2020, Per Nymand-Andersen (2020) emphasised the positive implications for active citizenship and effective legal research that better access to the law through digital technologies represents (Nymand-Andersen, 2020). Valérie Saintot (2020) also stressed that "developing a detailed understanding of the needs and interests of all parties involved - legislators, experts, academics and citizens - will enhance and facilitate progress in this new field for the greater good, enabling users to experience transparency and accountability in law-making".

Legal data visualisation as well as legal knowledge visualisation are increasingly attracting the attention of the legal community, given their potential to have a positive impact on legal education, access to and understanding of the law by citizens, and improved management and processing of legal data by businesses (especially law firms). In contrast, few academic publications in law rely on and integrate the visualisation of legal data or legal knowledge into their analyses. Even fewer studies examine the impact of these tools on legal research methodology. Is this lack of interest an indication of technological difficulties (insufficient computer literacy, expert tools not tailored to legal scholars)? IT Lawyer of the Year 2001 Professor Friedrich Lachmayer used a bridge metaphor to describe the relationships between informatics and law: "Legal informatics, which includes the visualisation of legal data, is about building a bridge between law and informatics. However, when it comes to the design of visualisation tools, informatics scholars expect too much from legal scholars, then the latter give up and the bridge collapses."<sup>1</sup> Could the problem be quite different and have to do with a specificity of law, namely the ontological formalism of a legal norm that denies these tools any interest in better understanding the law? (Zeno-Zencovich, 2018: 463)

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<sup>1</sup> Quoted in Čyras (2009).

To answer this question, my contribution focuses on the place of legal data visualisation tools in legal research through a concrete case, namely the updating of the "Euro" entry, which is to be published in the "Répertoire en droit européen" collection published by Dalloz, that I have to carry out. This entry, originally written in 2002 by Professor Jean-Victor Louis, deals with the monetary law of the European Union (EU). In addition to updating the references to the applicable legal acts and instruments, this new version must take account of changes in the content of the *lex monetae* and related legislation (protection of banknotes and coins, anti-counterfeiting measures, conversion and rounding procedures etc.) In this context, I have tried to integrate into my research methodology the visualisation tools made available by EUR-Lex. This study will therefore examine to what extent these tools correspond to the requirements and practices of legal research (2). After an analysis of EUR-Lex's new visual navigation system (3), I will compare my research needs with the possibilities offered by the visualisation tools (4).

## 2 The specificities of legal research

In everyday language, research refers to "the systematic investigation into and study of materials and sources in order to establish facts and reach new conclusions" (Oxford English Dictionary). Research is thus presented as a result and the process leading to that result. Appearing in the French language in the 12th century (and in the English language in the second half of the 16th century), it etymologically refers to the general action of "going through by searching" (from the Latin word *recercer*). In the 16th century, it took on a legal meaning to designate the conduct of an investigation into someone's actions.

The longstanding inclusion of the term "research" in the vocabulary of law does not mean that there is no epistemological debate about the existence and nature of "legal research". Law is a separate object of research "which belongs to the order of discourse and the normative order (of the duty to be), whose interpretation, hermeneutics, understanding, is a human activity" (Bioy, 2016). Legal training, oriented towards professionalism and not very open to interdisciplinarity, also leads to the researcher-lawyer not having any distance from their object of study: legal research is "in law", not "about law". This lack of critical distance is the source of a regular quarrel - largely meaningless - about the supposedly scientific nature of legal research compared to other scientific disciplines. As Dean Carbonnier (1979) noted: "If any body of reasoned and coordinated knowledge deserves this name (if only as opposed to empiricism), it is certain that there is a science of law... [i]t studies phenomena and formulates rules at the same time."<sup>2</sup> Indeed, the primary purposes of legal research are to work towards achieving progress in the law and acquiring systemic knowledge of the law, and, beyond that, to aim at a better integration of the law in society, legal security and social harmony (Terré, 2007). These cognitive and

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<sup>2</sup> Author's own translation. In French it reads as follows: "Si tout ensemble de connaissances raisonnées et coordonnées mérite ce nom (ne fût-ce que par opposition à l'empirisme), il est bien certain qu'il y a une science du droit. Différente des autres, ce n'est pas discutable ; peut-être même irréductible à toute autre, encore qu'on puisse lui trouver des analogies avec l'histoire (science conjecturale), et surtout avec les sciences du langage (qui, comme elle, étudient des phénomènes et formulent des règles tout à la fois)."

societal goals reflect the dual function of opinion and legitimisation of legislative action and jurisprudence that legal researchers perform (Jestaz and Jamin, 2004: 218).

Beyond the question of the nature and functions of legal research, the question of its relations with other disciplines of the humanities and social sciences has been raised for some thirty years. Without entering into this longstanding debate, I observe that there is a strong demand, both within and outside the legal community, for legal research to open up more widely to inter- and trans-disciplinarity (Roberts, 2017). Incidentally, lawyers are invited to take up research methods from other disciplines, and to no longer restrict their examination of “empirical data” to legal texts or case-law. In short, they must consider more broadly the context in which the law is produced and into which it is inserted.

These developments in legal research in general, and in EU law in particular, have a strong impact on the selection of data on which researchers base their reflections. If one considers only the field of EU law, legal material remains central. However, this material is not limited to the only sources of positive law in force and includes, where necessary, preparatory documents (green/white papers, legislative proposals, impact assessment reports, national parliamentary opinions on the respect of the principle of subsidiarity, legislative amendments of the European Parliament, political agreements of the Council), non-binding legal acts (Commission guidelines, the code of conduct of the Stability and Growth Pact and so on), repealed legal acts, and communication/information documents (press releases, parliamentary hearings, parliamentary questions, oral interventions, press articles).

To this must be added the works of legal scholars, in the form of monographs, commentaries, dictionaries, articles in peer-reviewed legal journals or, more simply, discussion or working papers. The intertwining of European and national law also requires the researcher to delve into national law and, in a related way, into the various national legal writings. This requirement for comparative legal research goes hand in hand with research that is multilingual in nature, due to the EU’s atypical linguistic regime and the juxtaposition of national legal systems and cultures, each of which has its own distinct legal-linguistic regime. Finally, the conduct of more interdisciplinary legal research also calls for legal analyses to be enriched with scientific works from other disciplinary fields (sociology, political economy, political science, philosophy of law, linguistics) or the taking into account of non-legal materials such as quantitative data (registers, statistical surveys) or qualitative data (interviews, case studies).

### 3 [EUR-Lex: an online gateway to EU law at the heart of legal research](#)

EUR-Lex is an online gateway providing access to EU law, the case-law of the Court of Justice, other EU public documents and electronic editions of the Official Journal of the European Union that are authentic. This service is provided by and under the responsibility of the Office. Established in 1969 as an interinstitutional office, the Office’s aim is to publish the publications of the institutions of the EU and the

European Atomic Energy Community under optimum conditions<sup>3</sup>. Consequently, the Office has exclusive competence to publish the Official Journal as well as other mandatory texts whose publication in the Official Journal is not a condition for their enforceability. It may also publish or co-publish non-mandatory publications entrusted to it under the prerogatives of each institution, in particular in the context of the institutions' communication activities.

The Office also develops, maintains and updates its electronic publishing services for the public. This task is technical in nature but has become essential since the paper version of the Official Journal was replaced by an electronic version in 2013.<sup>4</sup> It is “a fundamental principle of the Union's legal order that an act emanating from the public authorities may not be relied on as against individuals until such time as they have had the opportunity to acquaint themselves with it”.<sup>5</sup>

Administratively attached to the Commission, the Office is a common tool for the institutions and bodies that set it up (i.e. the European Parliament, the Council, the European Commission, the Court of Justice, the European Economic and Social Committee and the Committee of the Regions). Although formally established as an institution since the Treaty of Lisbon, the ECB is not one of the co-authors of the 2009 version of the Publications Office Decision (Decision 2009/496/EC). However, in accordance with European Anti-Fraud Office case-law, this decision applies to the ECB.

The scope of the Office's editorial powers is to be interpreted in conjunction with the regime governing the publication of acts of the institutions. A distinction is made between acts whose publication in the Official Journal is required pursuant to the general obligation contained in Article 297 TFEU (as well as to specific provisions of the Treaties, e.g. Article 287 TFEU) and other mandatory publications. The former concerns legislative acts adopted under the ordinary legislative procedure or a special procedure, as well as non-legislative acts of general application, namely those adopted in the form of regulations, directives which are addressed to all Member States, and decisions, where the latter do not specify to whom they are addressed. The latter concerns for example regulations and decisions without addressees adopted by the ECB under Article 132 of the Treaty on the Functioning of the European Union (TFEU) and Article 34 of the Statute of the European System of Central Banks and of the European Central Bank (Statute of the ESCB).

As regards other legal instruments, whether mandatory or non-mandatory, whose legal publication is not required by the Treaties, Article 15(1) TFEU requires that the institutions, bodies, offices and agencies of the EU conduct their work as openly as possible. Regulation (EC) No 1049/2001 of the Parliament and of the Council defines the principles, conditions and limits of the right of access to European Parliament,

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<sup>3</sup> Decision 2009/496/EC, Euratom of the European Parliament, the European Council, the Council, the Commission, the Court of Justice of the EU, the Court of Auditors, the European Economic and Social Committee and the Committee of the Regions, of 26 June 2009, on the organisation and operation of the Publications Office of the European Union (OJ L 168, 30.6.2009, p. 41).

<sup>4</sup> Council Regulation (EU) No 216/2013 of 7 March 2013 on the electronic publication of the Official Journal of the European Union (OJ L 69, 13.3.2013, p. 1).

<sup>5</sup> Case C-98/78, *Racke v Hauptzollamt Mainz*, EU:C:1979:14.

Council and Commission documents.<sup>6</sup> The other EU institutions, bodies, offices and agencies not listed in that Regulation are required to lay down in their rules of procedure the specific provisions governing access to their acts, in accordance with Regulation (EC) No 1049/2010.<sup>7</sup> In practice, publication requirements are also detailed in basic acts establishing EU bodies<sup>8</sup> or in interinstitutional agreements.<sup>9</sup> In the case of the ECB, it had already established the legal regime applicable to access to its administrative documents in a specific decision in 1998, supplemented in 1999 by its Rules of Procedure. These rules were amended in 2004 to take account of Regulation (EC) No 1049/2010.<sup>10</sup> ECB guidelines and instructions are legal instruments for internal use within the Eurosystem. Consequently, the ECB's Rules of Procedure do not provide for their systematic publication in the Official Journal, and leave it to the decision-making bodies, each within its area of responsibility, to decide whether or not to publish their acts,<sup>11</sup> taking into account their possible external legal effects (Zilioli and Selmayr, 1999). In practice, the ECB has published all its guidelines in the Official Journal (sometimes with a delay of one to two years from the date of adoption)<sup>12</sup>, in contrast to the situation with regard to the instructions of the Executive Board.

In this general context, legal information is only partially edited and made accessible via EUR-Lex. Without prejudice to Regulation (EC) 1049/2010, each EU institution and organ remains free to manage its documents and select the most appropriate communication channel. Unsurprisingly, numerous registers of legal acts are developed, managed and made available to the public by EU institutions, bodies and agencies in parallel with or in addition to EUR-Lex (see Table 1).

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<sup>6</sup> Regulation (EC) No 1049/2001 of the European Parliament and of the Council of 30 May 2001 regarding public access to European Parliament, Council and Commission documents (OJ L 145, 31.5.2001, p. 43).

<sup>7</sup> Article 15(3) TFEU.

<sup>8</sup> See, for example, Article 7 of 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); and Articles 10(4) and 13(2) of Regulation (EU) No 1093/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Banking Authority) (OJ L 331, 15.12.2010, p. 12).

<sup>9</sup> Points 24 to 26 of the Interinstitutional agreement of 13 April 2016 between the European Parliament, the Council of the European Union, and the European Commission on better law-making (OJ L 123, 12.5.2016, p. 1).

<sup>10</sup> Decision ECB/2004/3 of the European Central Bank of 4 March 2004 on public access to European Central Bank documents (OJ L 80, 18.3.2004, p. 42); and Decision ECB/2004/257/2 of the European Central Bank of 19 February 2004 adopting the Rules of Procedure of the European Central Bank (OJ L 80, 18.3.2004, p. 33). For an in-depth discussion, see Leino-Sandberg (2020).

<sup>11</sup> Article 17(7) and Article 17a of the ECB rules of procedure.

<sup>12</sup> See for example Guideline ECB/1999/NP11 of the European Central Bank of 22 April 1999 on the authorisation to issue national banknotes during the transitional period (OJ L 55, 24.2.2001, p. 71).

**Table 1**

**Non-exhaustive list of public registers of EU documents**

European Parliament	Council of the EU	European Commission	European Central Bank
Main register (written questions, written explanations of vote, joint motion for resolution, working documents, draft reports/opinions, texts adopted, agendas, minutes, records of attendance, coordinators, discharge, in-depth analysis etc.)	Main register (meeting documents, preparatory legislative documents, i.e. 4 column tables, press releases)	Main register (legislative proposals, impact assessments, delegated and implementing acts, Commission decisions, green papers, minutes of Commission meetings/DG meetings etc.)	Monetary policy decisions/statement/accounts
Legislative Observatory, OEIL (database for monitoring the EU decision-making process: legislative proposals, draft reports, texts adopted, contributions of the national parliaments etc.)	CASE (Central Archives Search Engine)	Competition cases register	Documents related to the Banking supervision (MoUs, supervisory guides, supervisory letters etc.)
IPEX (platform for mutual exchange of information between the national parliaments and the EP: EU draft legislative acts, consultations, national parliaments' positions)	Treaties and Agreements database	Comitology register	
CONNECT (EP's database of national parliament documents)	Intergovernmental conference (documents of the 2004 IGC and 2007 IGC)	Impact assessment register (impact assessment reports, regulatory scrutiny board opinions etc.)	
eMeeting (meeting documents of parliamentary committees, delegations, parliamentary assemblies)	Register of European Council conclusions	Infringement decisions register	
		Consultations register (calls, feedbacks, impact assessment reports, regulatory scrutiny board opinions)	
		Publications register (press release, agendas, national parliament opinion, planning and management opinions etc.)	

Source: Frédéric Allemand, on the basis of the EU institutions' websites

Information overlaps a lot from one register to another. The differences between registers lie mainly in the target audience and the search engines or visualisation features offered. The trend is towards a multiplication of registers, rather than their integration.<sup>13</sup> The ECB has taken the opposite approach to other institutions. From 1998 onwards the ECB maintained a section on its website relating to its legal framework, where legal acts published in the Official Journal (including consolidated versions drawn up under the responsibility of the Office), as well as other legal acts, such as opinions on EU acts and draft national regulations in its fields of competence, were accessible. The navigation between documents was basic and the search engine rather inefficient. Since 15 June 2020, all legal acts published by the ECB have migrated to EUR-Lex and are available in the “Browse by EU institutions” section.<sup>14</sup>

<sup>13</sup> For example, the European Parliament's IPEX and CONNECT registers, and the Committee of the Regions' REGPEX register, all provide access to the opinions of national parliaments under the subsidiarity principle. The IPEX register is the only one to offer a visualisation tool.

<sup>14</sup> For a comprehensive and stimulating presentation, see Saintot (2020).

EUR-Lex stands out for its organisation of legal information and for the facilitation of access to legal information that it publishes directly or collects from other registers. For each legal act, the “Document information” page displays all vertical relationships (amendments between documents, including repeals, corrections, implementing acts, delegated acts) and horizontal relationships (cross-references between documents) with other legal acts. The “Procedure” and “Internal procedure” pages provide access to preparatory documents and documents resulting from negotiations between institutions concerning legal acts adopted in accordance with an interinstitutional procedure, in particular the impact assessment carried out by the Commission, the reports of the regulatory scrutiny board, parliamentary work (legislative reports, parliamentary amendments) and discussions within the Council and its working groups, in addition to access to the usual documents (legislative proposal, final document adopted). This information environment is completed by mention of any judgments handed down by the Court of Justice concerning the interpretation or legality of the legal act (on the “Information on the document” page). However, it is regrettable that the opinions of the Advocates-General are not also mentioned, as they contribute to the development of EU law.<sup>15</sup> Finally, it is worth noting the possibility of a multilingual display of legal acts - a decisive feature in interpreting texts, in respect of which it should be remembered that the versions in all 23 official languages of the EU are authentic. In the case of ECB acts, the functionalities relating to “relationships between documents” are deactivated, given, on the one hand, the confidentiality of the deliberations of the ECB’s bodies and of the work carried on within the Eurosystem committees (including those of the legal committee)<sup>16</sup> and, on the other hand, the fact that the exercise of the ECB’s normative power does not form part of interinstitutional procedures.

The legal researcher can only welcome these functions, which help to set each legal act in a network of relationships with other acts. The implementation in March 2022 of the visualisation of relations constitutes notable and welcome progress in facilitating efficient analysis of texts.<sup>17</sup> However, this network of relations would benefit from being made more comprehensive and having its quality improved. For example, EUR-Lex provides only a partial link to information on the European Parliament’s Legislative Observatory document portal (see Table 2). There is no link to the amendments tabled by parliamentarians or to the negotiation documents in triologue. The opinions of national parliaments – in view of the application of the subsidiarity principle – are also missing.<sup>18</sup> It is also regrettable that as from the beginning of the eighth parliamentary term questions addressed by the members of the European Parliament to the other EU institutions are no longer published either in the Official

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<sup>15</sup> Opinion of AG Ruiz-Jacob Colomer, case C-466/00, *Arben Kaba*, case C-466/00, EU:C:2002:447, para. 115.

<sup>16</sup> Article 23 of the ECB’s Rules of Procedure. Those documents will be freely accessible after a period of 30 years unless decided otherwise by the decision-making bodies of the ECB.

<sup>17</sup> EUR-Lex, Discover the latest developments on EUR-Lex website, March 2022. Available at: [https://eur-lex.europa.eu/content/development/development\\_2022-01.html](https://eur-lex.europa.eu/content/development/development_2022-01.html). Accessed on October 15, 2022.

<sup>18</sup> To be exact, the documents related to the subsidiarity check are included among the documents from the Council register. A noteworthy difficulty here is that the “Procedure” page refers to these documents by their reference numbers and not by an indication of their content, whereas these details are to be found in the Council register.

Journal or on EUR-Lex. They are now published and accessible in a dedicated register on the European Parliament's website.<sup>19</sup>

**Table 2**

Comparison of content coverage between EUR-Lex and OEL (Proposal for a Regulation establishing minimum requirements for water reuse, COM(2018) 337 final - 2018/0169(COD)).

EUR-Lex	Legislative Observatory, OEL
	Committee draft report, PE628.362
	Amendments tabled in committee, PE629.751
	Amendments tabled in committee, PE630.372
	Amendments tabled in committee, PE630.658-Committee Opinion (AGRI), PE626.778
Committee Opinion (AGRI), AGRI_AD(2018)626778	Committee Opinion (AGRI), AGRI_AD(2018)626778
Committee report tabled for plenary (1st reading), A8-0044/2019	Committee report tabled for plenary (1st reading), A8-004/2019
Text adopted by Parliament (1st reading), P8_TA(2019)0071	Text adopted by Parliament (1st reading), T8-0071/2019
	Text agreed during interinstitutional negotiations, PE646.828
	Committee letter confirming interinstitutional agreement, PE646.829
	Committee draft report, PE650.390
Committee recommendation tabled for plenary (2nd reading), P9 A(2020)0098	Committee recommendation tabled for plenary (2nd reading), A9-0098/2020
Text adopted by Parliament (2nd reading), P9_TA(2020)0098	Text adopted by Parliament (2nd reading), T9-0056/2020

Source: Frédéric Allemand, on the basis of the EU institutions' websites

At first glance, the situation seems much better with regard to Council documents. On closer examination, however, a critical discrepancy can be observed: EUR-Lex does not include essential and structuring documents for the intra- and inter-institutional negotiation of legislative acts, i.e. the compromises made by Council presidencies, the position notes (proposals) of the national delegations, the opinions of the Council's Legal Service, the documents setting out the Council's general approach and those relating to the preparation of trialogues. Nor is there any linkage with the statements made on the occasion of the adoption of legislative acts. Although they have no legal value, these declarations contain elements of interpretation of the legislative acts to which they refer. In the absence of any methodological indication from EUR-Lex, it is difficult to know whether these differences in documentary coverage are the result of a specific selection policy or of interoperability problems between registers.

A similar question arises with regard to the list of academic writings on the decisions of the Court of Justice. Where they exist, the bibliographical references cited on the "Document information" page, in the section entitled "Doctrine", correspond only imperfectly to those mentioned for the same judgment on the Court of Justice's website.<sup>20</sup> That being said, legal research would benefit from scientific documentation being associated, as appropriate, with legal acts, on the model used for the judgments of the Court of Justice. In this respect, EUR-Lex could usefully draw on the EU

<sup>19</sup> European Parliament Plenary, Parliamentary questions, 2022. Available at: <https://www.europarl.europa.eu/plenary/en/parliamentary-questions.html>. Accessed on October 15, 2022.

<sup>20</sup> EUR-Lex lists 51 legal scholarly publications under the *Pringle* judgment, and CURIA 40.



institutions, which undertake substantial scientific research activity.<sup>21</sup> An interdisciplinary perspective would justify this documentation including references to legal scholarship, but also to contributions from other social sciences and humanities.

## 4 Using the legal information in the EUR-Lex section on ECB acts

Since June 2020, EUR-Lex has been testing a specific visualisation system for published ECB acts in the “Acts of the institutions” section. Clickable graphics present the acts by nature, date and subject area. This visualisation is intended to provide a new browsing experience for the user. Designed in collaboration between the Office's and the ECB's departments, this feature is part of the ECB's drive to improve access to its acts and transparency. On the research side, it is expected that the visualisation of legal data and information will provide inspiring insight into the state of the law and the ECB's exercise of its mandate and powers, thereby facilitating the identification of new research questions.

The updating of the euro section of the Dalloz Répertoire provided me with the opportunity to make intensive use of the new features of EUR-Lex in general and those implemented in the ECB acts section in particular. My analysis focused on legal acts in the field of “Banknotes and coins, means of payment and currency matters”, i.e. those based on Article 16 of the Statute of the ESCB and Article 128(1) and (2) TFEU. The user has two ways of navigating this corpus, namely textual (classic) and visual (new). The textual navigation covers all 452 ECB acts in this field over the period from 1998 to 2021. It includes binding and non-binding instruments (opinions, recommendations, letters), as well as documents concluded with other institutions or bodies (memoranda of understanding, international agreements). The visual navigation is limited to 95 binding legal acts, in this case decisions and guidelines adopted by the ECB. However, this number is still lower than the number of binding acts of an identical nature counted using the textual navigation system. The difference is explained by the inclusion of corrigenda in the number of legal acts. I concentrate below on the visual navigation mode, given its innovative nature and the needs of my analysis, which mainly focuses on binding acts.

The power to issue money is a prerogative of the monetary sovereign. This power is a practical symbol of monetary competence. Since the entry of the EU into Stage 3 of EMU, this competence is attributed exclusively to the EU for those Member States whose currency is the euro. According to Article 128 TFEU and Article 16 of the Statute of the ESCB, the ECB has the power to authorise the issue of euro banknotes and coins in the territory of the EU, which also includes the production, putting into circulation and withdrawal of euro banknotes and coins. The right to protect the

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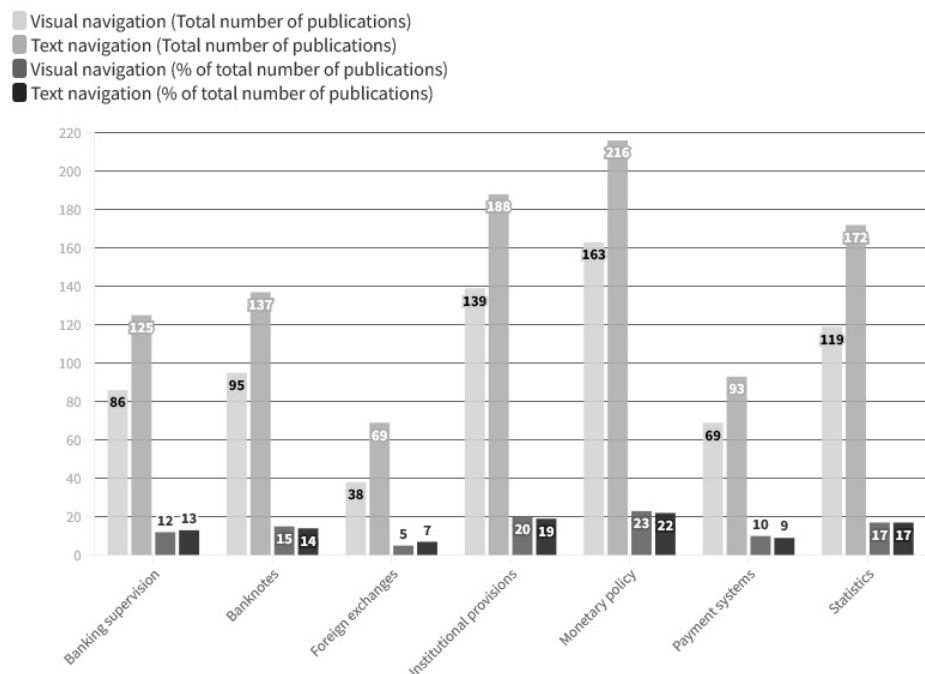
<sup>21</sup> The Commission has long developed a tradition of research to shed light and obtain inputs on the definition, content and effects of EU policies. In the field of European Monetary Union (EMU), see in particular the European Papers series, led by DG ECFIN. The European Parliament has increased its own scientific production since the 2010s: its “Research and Documentation” service produces a comprehensive range of content-rich and easy-to-read publications on major EU policies, issues and legislation. Since 2022, the General Secretariat of the Council has had an Analysis and Research Team. The ECB also supports an active research programme on economic and legal issues.

currency is a corollary of the right to mint. On this basis, the ECB has exclusive competence to define the general regime for the protection of the integrity of banknotes and to decide on the regime for the reproduction of banknotes and the exchange of mutilated or damaged banknotes.

Contrary to expectations, the legal, economic, social and political importance of cash (ECB, 2022) has not been reflected in any excessive legal activism by the ECB. The number of binding legal acts (95) is in line with the average number of acts published in all areas of ECB activity (101). The navigation mode used is irrelevant in this respect (see Chart 1). On average, four binding legal acts are adopted per year - the highest annual average is for monetary policy (7).

### Chart 1

Number of legal acts by topic and by navigation mode (1998-2021)

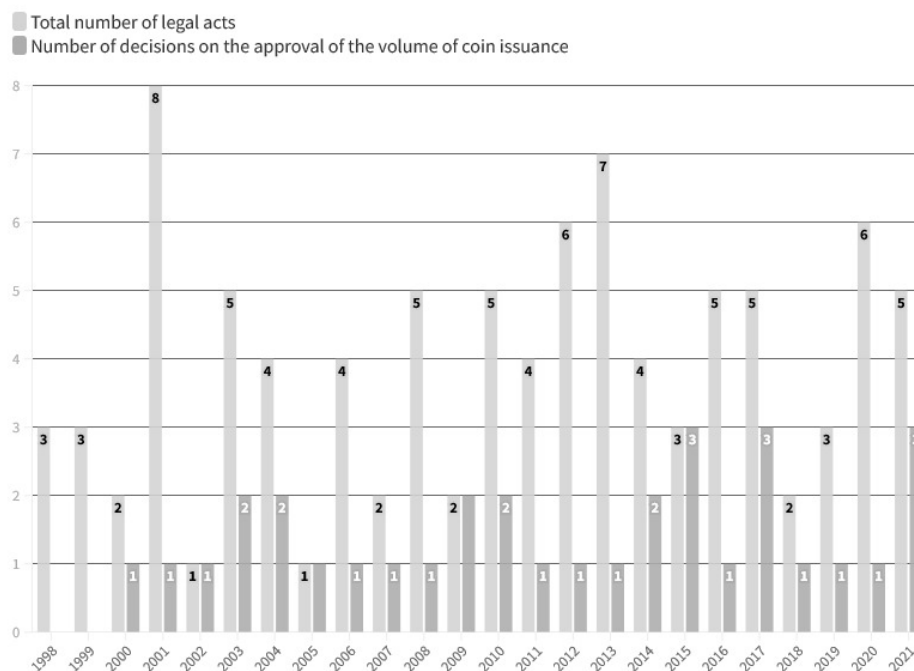


Source: Frédéric Allemand, on the basis of EUR-Lex

This legal activity has to be read in conjunction with the topics dealt with. One third (i.e. 33) of the ECB's acts on banknotes and coins relate to the annual authorisations of the volume of coins issued by the Member States. In some years, legal activity in this area is limited to approving the volumes of euro coins (see Chart 2).

## Chart 2

Total number of legal acts versus number of decisions on approval of the volume of coin issuance (1998-2021)



Source: Frédéric Allemand, on the basis of EUR-Lex

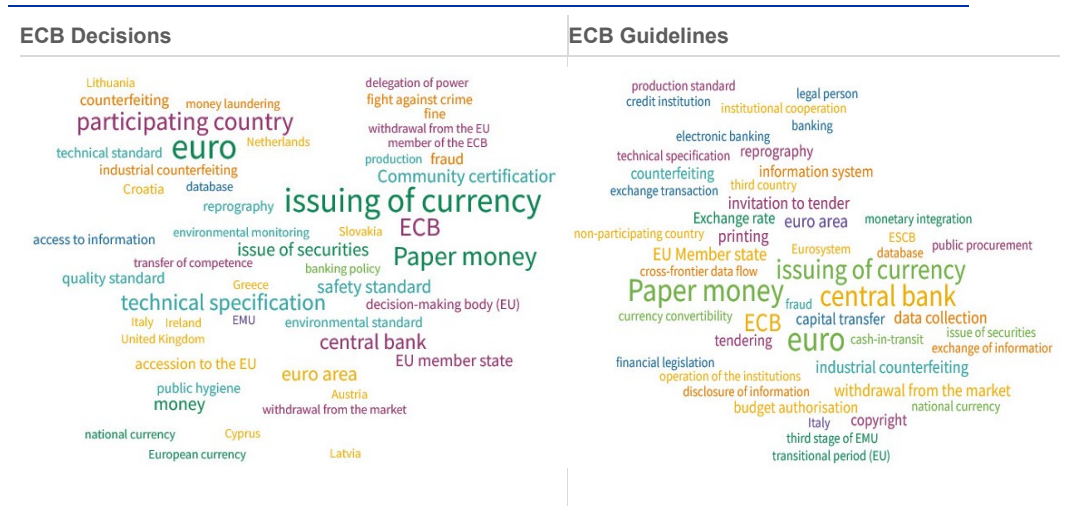
The visual navigation system does not allow for a detailed description of the specific topics covered by the legal acts, nor does it allow for an assessment of the proportion of the different types of legal acts adopted by the ECB in each area. This is unfortunate as, unlike in other areas, Article 128 TFEU and Article 16 of the Statute of the ESCB leave the ECB free to choose, among the different forms of legal instrument, those most appropriate for the exercise of its monetary policy powers. In order to obtain a more detailed view of the ECB's legislative activity, I therefore had to manually extract some metadata for each legal act in the corpus relating to euro banknotes and coins.<sup>22</sup> The extraction concerned in particular the fields relating to the title of the act, its legal bases, the numbering as attributed by the ECB, the form, the dates of the document, the act's entry into force, end of validity, addressees and relations with other legal acts, and the EUROVOC descriptors. As of 15 October 2022, the corpus under review includes 69 decisions (almost half of which relate to the authorisation of coin issuance volumes) and 26 guidelines.

In order to check whether certain matters relating to euro banknotes and coins show that the ECB has a preference for one form of instrument over another, I have attempted to reconcile three items of metadata, namely the legal bases of the acts, the nature of the addressees and the description of their content by the EUROVOC descriptors.

<sup>22</sup> EUR-Lex offers a web-based retrieval service which my limited computer knowledge did not allow me to use. See OPOCE (2012).

**Chart 3**

Number and intensity of occurrences by type of document (decisions, guidelines)



Source: Frédéric Allemand, on the basis on EUR-Lex

Not surprisingly, the descriptors related to paper money and currency issuance activities are similar with regard to the content of the decisions and guidelines. However, there are some differences: vocabulary related to the operational aspects of banknote production and the protection of banknotes against fraud is more often used in decisions. Guidelines, on the other hand, seem to favour vocabulary relating to institutional aspects, the administrative organisation of the currency issue and data exchange. It should be noted that the visualisation of descriptors associated with legal acts in the same corpus allows a pattern to emerge and, at the same time, the distinctiveness of certain acts to be revealed more effectively. The application of an unusual term to describe a legal act should immediately attract attention. Thus, the attentive and curious user will be surprised to see the descriptor "legal person" applied to Guideline EU/2017/2193 (ECB/2017/31) on the establishment of the Eurosystem Production and Procurement system, especially given that this term is not applied to Guidelines ECB/2004/18, ECB/2011/3, ECB/2013/49, ECB/2014/44 and (EU) 2021/2322 (ECB/2021/56), although they also deal with the same subject. In the course of further research, the user will note that new terms have been added to the EUROVOC descriptors for these guidelines since 2014. There is a strong emphasis on institutional aspects in the list of descriptors for the last two guidelines set out in Table 3. Some might see this as a whim of the staff responsible for selecting the descriptors, but that would be to forget that the choice of descriptors is based on a precise methodology and is nowadays a largely automated operation.<sup>23</sup> These developments reflect the profound changes undergone in the banknote printing market since the early 2000s, as well as the intense and difficult discussions within the Eurosystem between those NCBs that still have in-house printing services and those that have historically relied on private printing services.

<sup>23</sup> The European Commission's Joint Research Centre has developed a software package aiming to provide end users with a tool for the automatic annotation of documents with descriptors from the EuroVoc2 thesaurus: the JRC EuroVoc Indexer, aka JEX. See Steinberger, Ebrahim, Turchi (2012).

As for the analysis of the legal bases, it does not allow for any particular conclusion, given the variety of combinations listed (37). The use of Article 128(1) TFEU in conjunction with Article 16 of the Statute of the ESCB is the most frequent combination (29 times). It is also the only one used for the adoption of both decisions and guidelines. In all other cases, the differences in nature, effect and addressees between these categories of acts mean that the combinations used for their adoption are specific to them. It will come as no surprise that Article 14 of the Statute is only mentioned in relation to guidelines. However, the choice of a particular legal basis may sometimes be inconsistent over time: although they both deal with "accreditation procedures for manufacturers of euro secure items", Decision ECB/2013/54 refers to Article 128(1) TFEU among its legal bases, while Decision (EU) 2020/637 (ECB/2020/24) does not.

**Table 3**  
EUROVOC descriptors applied to ECB guidelines on the procurement of euro banknotes

Guidelines	Descriptors
ECB/2004/18	Paper money, central bank, ECB, euro, issuing of currency
ECB/2011/13	Paper money, central bank, ECB, euro, issuing of currency
ECB/2013/49	Paper money, invitation to tender, central bank, euro area, euro, issuing of currency
ECB/2014/44	Printing, paper money, invitation to tender, central bank, production standard, euro, issuing of currency
ECB/2017/31	Printing, paper money, legal person, tendering, central bank, operation of the institutions, euro, issuing of currency
ECB/2021/56	Printing, paper money, institutional cooperation, invitation to tender, tendering, central bank, euro, issuing of currency

Source: Frédéric Allemand, on the basis of the EU institutions' websites

## 5 Some provisional final conclusions

In a recent article, Michael Doherty (2020) recalls that "Law has traditionally been about words, and lawyers have been 'word people' and not 'picture people', though more recently the importance of images in the law is gradually increasing". Indeed, the challenge is not to produce pleasing images to embellish legal contributions whose editorial style is often denounced for its austere, pompous and outdated character.

The particular social function of law, the complexity of the legal situations to be regulated, and the epistemological knowledge to be used all shape the process of forming legal language. It is controlled by "an institution placed in a situation of hierarchical domination" (Didier, 1984), its vocabulary and syntax are codified and the definition of its terms is delegated to a community of experts. This is the opposite of everyday language. The wide dissemination of legal information via the Internet accentuates the gap between the two linguistic registers, and, in a related way, between awareness of the law and its knowledge by the public. "Somewhat illogically, we are supposed to know and follow rules that we cannot understand. Somewhat

illogically, in practice, the primary addressees of legal rules seem to be lawyers and/or judges - those who enforce compliance, not those who must comply. Unfortunately, those who must comply often 'discover' the applicable legal rule (or: develop a better understanding thereof) when it is too late: in the case of non-compliance." (Mik, 2020). This situation is not unique to law, and concerns all technical language. Mechanical repair manuals remain obscure to anyone without a minimum knowledge of mechanics. But law is not mechanics. "It is not for the lawyer, but for the litigants; it must be perceived by them. Judicial reasoning that cannot be followed or redone by the public is basically missing one of the characteristics of law."<sup>24</sup> (Carbonnier, 1966)

In this context, EUR-Lex and the ECB are to be congratulated for the initiative of a visual navigation mode through which to discover the ECB's legal acts. This does not change the complexity and technicality of their content. The scope of the tool remains limited, as I have experienced in the preparation of this contribution and in other research work. However, it is part of the necessary effort to improve knowledge of legal activities. It is to be hoped that this first step will be followed by many others in the years to come.

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<sup>24</sup> Author's own translation. The original text in French reads as follows: "Le Droit n'est pas fait pour le juriste, mais pour les justiciables; il doit être perçu par eux. À un raisonnement judiciaire qui ne peut être suivi, refait par le public, il manque, au fond, un des caractères du droit."

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# The big why of legal design and legal knowledge visualisation

By Filip Lulić\* and Valérie M. Saintot<sup>α</sup>

## 1 Introduction

The legal profession could be described as one of the more traditional professions. The way lawyers are educated and practice their craft has been stable for centuries. Law being essentially textual, jargon has amassed over time. While legal jargon is useful when it serves the purpose of being precise and specific, it can become a hurdle and counterproductive if used excessively and without a clear need. Technological developments and new wicked problems present a challenge to the entire society, but legal experts in particular are finding themselves more and more under pressure as they are the perceived guardians of the rule of law and curators of the “social contract”.

The Information Age has brought unprecedented technological developments, thereby opening doors to knowledge of all kinds and making it easily accessible via our devices. According to Wikipedia, the Information Age (also known as the Computer Age, Digital Age, Silicon Age, and New Media Age) is a historical period that began in the mid-20th century and is characterised by a rapid epochal shift from a traditional industry established during the Industrial Revolution to an economy primarily based on information technology. The Information Age was formed by capitalising on computer microminiaturisation advancements, which led to modernised information systems and internet communications as the driving force of social evolution.<sup>25</sup>

The legal profession adopted emails, computers and digital archives. However, this change did not amount to much more than the replacement of the analogue (paper) with the digital (files on a hard drive). Tech companies took note and started developing solutions aimed at the legal services market – and so the fast-growing field known as “legal tech” emerged. Legal tech can be defined as “software and technology which is used by law firms or legal teams to facilitate their processes and improve their effectiveness. The aim of legal tech is to simplify operations, optimise current workflows and improve the overall management of knowledge and information that exists in law firms or enterprises.”<sup>26</sup> AI-based solutions and blockchain technology are currently being explored in the legal tech field in order to adjust legal work to the digital domain in a more profound way.

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<sup>25</sup> [en.wikipedia.org/wiki/Information\\_Age](https://en.wikipedia.org/wiki/Information_Age)

<sup>26</sup> [www.lexology.com/library/detail.aspx?g=78c11ed9-0787-4b26-b062-3c6a1222d8e1](https://www.lexology.com/library/detail.aspx?g=78c11ed9-0787-4b26-b062-3c6a1222d8e1)

All this created pressure on lawyers to upgrade their traditional toolboxes and become more aware of the broader trends in the business world and more in tune with clients' needs. In particular, there is a need to ensure legal certainty, the proper valuation of legal risk and the mitigation of legal risk, and to increase the speed and transparency of legal proceedings.

One way for the legal profession to be more client-oriented is for legal professionals to apply user-centric design thinking principles to legal profession. The early systematisation and popularisation of this approach in the legal profession is widely attributed to Professor Margaret Hagan from Stanford Law School and Institute of Design. She started the Program for Legal Tech & Design in 2013, experimenting with the way design can make legal services more usable, useful and engaging.<sup>27</sup> The legal design movement quickly started spreading around the world and early subscribers started showcasing the benefits of this method, or better said – this mindset.

This article examines the way legal design can help bridge the gap between the law (and legislators or regulatory institutions) and its addressees (members of the broader society and market participants) in the Information Age and highlight the risks of failing to do so. Additionally, it explores a visual discipline similar on the surface to legal design – legal knowledge visualisation – and shows how it can support legal research and insight generation, outreach and knowledge sharing. Finally, this article offers several examples of legal design and legal knowledge visualisations from the practice of Directorate General Legal Services of the European Central Bank using a case study approach.

One final introductory note: this article brings a perspective based on the authors' experience as practitioners of legal design and legal knowledge visualisation techniques in their daily work. We invite the reader to explore the books that served us well when building legal design capabilities.<sup>28</sup> The reader should kindly note that since legal design is still a young discipline without any established agreement on its scope and limitations. Therefore, this article should be considered in this light and read as an opinion piece.

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<sup>27</sup> [law.stanford.edu/directory/margaret-hagan/](http://law.stanford.edu/directory/margaret-hagan/)

<sup>28</sup> Wagner, A. and Sherwin, R.K. (2014), *Law, Culture and Visual Studies*, Springer; Corrales Compagnucci, M., Haapio, H., Hagan, M., and Doherty, M. (2021), *Legal Design*, Edward Elgar Publishing Ltd.; Tafur, K. and Martins, M. (2022), *Legal Design*, Thomson Reuters Aranzadi.

## 2 What is legal design and legal knowledge visualisation?

### 2.1 Legal design

In her online book “Legal by Design”, Margaret Hagan defines legal design as “the application of human-centred design to the world of law, to make legal systems and services more human-centred, usable, and satisfying”.<sup>29</sup>

It is clear from this definition that we should first look in the direction of human-centred design and the technique commonly referred to as “design thinking”.

The design and consulting firm IDEO is often credited with coming up with the term “design thinking” to describe its approach in the late 1970s. However, on their own website they point out that design thinking is the product of a longer conversation, which started earlier in the 20th century. No matter the beginnings, we can confidently say that design thinking has seen global popularity and broader application only in the last 15 years or so.<sup>30</sup>

The main driver behind this approach is a question – how can we rethink the way we go about solving increasingly complex problems (often called “wicked problems”)? Design thinking is essentially a mindset and a five-step collaborative methodology, where each step is directly or indirectly derived from one of the main principles of good design: empathy, optimism, iteration, creative confidence, and experimentation. The steps are:

1. empathise (listening, being non-judgmental and trying to understand);
2. define (identifying roles, pain points, challenges and problems);
3. ideate (enabling creativity and openness, ranking proposals and prioritise);
4. prototype (making mock-ups, acting lean and failing fast); and
5. test (finding out what works, collecting feedback and iterating quickly).

Bringing this all together, Tim Brown (the executive chair of IDEO) defined design thinking as “a human-centred approach to innovation that draws from the designer’s toolkit to integrate the needs of the users, the possibilities of technology, and the requirements for business success”. What made design thinking more than just a way in which one design firm operates? According to IDEO, they were at the right place at the right time and recognised that the world is going through a technological shift that humans need to learn to navigate. Design thinking brings together what is desirable from a human point of view and what is technologically feasible and economically viable. It also allows people who aren’t trained as designers to use creative tools to address a vast range of challenges.<sup>31</sup>

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<sup>29</sup> [lawbydesign.co/legal-design/](http://lawbydesign.co/legal-design/)

<sup>30</sup> [designthinking.ideo.com/history](http://designthinking.ideo.com/history)

<sup>31</sup> [designthinking.ideo.com](http://designthinking.ideo.com)

Margaret Hagan and other pioneers understood that the legal profession was a prime candidate for the application of design thinking. And it is easy to see why – law governs interactions in a society, and it constantly needs to play “catch up” with the disruptions of rapid technological innovation. As one way to make its impact more effective, law can benefit from including the needs of the “end user” (to borrow the term from the IT world) in the creation process. We can imagine this idea as the correlation between choosing a user-friendly shape and form for law and legal products or services, and the likelihood of accomplishing the intended legal effects.

## 2.2 Legal knowledge visualisation

As explained above, legal design is focused on transforming legal products and services to be more human-centric. To do so, legal design relies on design thinking principles. Legal knowledge visualisation tends to be more oriented towards core legal and legislative knowledge. It combines conventional legal expertise with newer disciplines like data science and applied statistics to analyse and visually explore legal knowledge for the purpose of generating new insight and understanding, and opportunities to revisit legal analysis from a less established angle.

The purpose of legal knowledge visualisation is to help legal professionals with the management of their knowledge, their complex analytical work and the way they collaborate daily. It is also a highly meaningful way for legal professionals to explain and explore legal issues with their non-legal counterparts to establish a level playing field. Legal knowledge visualisation should not only be focused on the end product but on the process of “visualis-ING”, which helps to extract otherwise tacit and individual know-how and transform it into a collective and tangible building block. Human beings possess powerful cognitive capacities to use visual cues to further their thinking. Using visuals to augment individual and collective thinking is at the heart of legal knowledge visualisation.

In practice, it is not always easy to go from raw data to applicable knowledge. At this early stage in the development of the legal knowledge visualisation approach, we have come to differentiate between distinct types of legal visualisation building blocks: data, information and knowledge.<sup>32</sup>

### *Data*

“Data” means a collection of non-interpreted symbols or facts. Data are generated, among others, by any kind of digitally tracked behaviour and is often called the “oil of the Information Age” since a lot of business intelligence can be extracted from the interpretation of data. Applied to the legal profession, we can establish that law, case-law and legal opinions/advice are kept or published in digital formats and stored in (public or internal) databases, and obtaining such data is a relatively straightforward task. Additionally, most internal legal processes are run using tools that allow for different levels of data tracking and extraction. As a result, we can conclude that there

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<sup>32</sup> Saintot, V.M. and Di Matteo, G. (2022), “Helping lawyers to better visualize their knowledge: a formula and four scenarios”, Liquid Legal Institute, Springer.

are many legal data streams that we can tap into if we are interested in understanding these domains better.

Before visualising it, legal data (like any data) must be prepared by cleaning, parsing and coming up with criteria for assessment. During this process, the analyst already develops starting hypotheses that will be checked through the generation of a visual. However, data alone can only answer the basic questions of size and quantity. To offer deeper meaning, data need to be contextualised.

### *Information*

Information is data placed in connection with other factors and interpreted within the appropriate context.

Visualising legal information is particularly useful for the creation of visual output that stimulates dialogue and exchanges among legal professionals to form views and empower decision making. Formats such as infographics, diagrams or illustrations can quickly give the viewer the most salient point for discussion and netting of (contradicting) views. The process of visualising available legal information is a unique space to mobilise legal collective intelligence. Legal professionals can save precious time if they sketch the tenets of the legal challenges they are working on instead of articulating their findings and limitations in linear text. Furthermore, the format also lends itself to bringing in comments from experts in other disciplines, as it is rare that only legal information is needed to solve any given problem, or to stimulate creative or lateral thinking.

### *Knowledge*

Knowledge is obtained when information is processed through human cognition and experience. More topical expertise can be brought to the table to draw valid conclusions when legal information is visually accessible to one or many persons. Knowledge also has an experiential and practical dimension, that is to say, knowledge should pass the test of putting something to action in real life conditions.

Visualising knowledge is useful for sharing concepts and inviting others to engage in critical assessment and dialogue around the visuals produced. Knowledge visualisation is particularly useful for insight generation and observing (otherwise hidden) patterns – which is essential for both day-to-day work and research. Furthermore, visualisation is useful for outreach and communication on complex domains of legal activities in that they make otherwise abstract or obscure challenges simply and visually graspable. This, in turn, is a concrete step that adds to the goals of transparency and accountability, which are expected from public bodies in particular. Legal knowledge visualisation has the potential to directly contribute to rebuilding trust and to add credibility in the public discourse, which in this day and age represents a pressing need<sup>33</sup>.

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<sup>33</sup> Saintot, V.M. and Lulic, F. (2022), “Transforming our legal ecosystems”, Liquid Legal Institute, Springer.

## 3 What is information overload and how does it affect legal professionals?

### 3.1 What is information overload?

In the main, data are collected and stay hidden in the background, not visible to the average end user of digital devices. Knowledge requires learning and experience and lots of time to fine tune. That means that we must actively invest effort to get to either data or knowledge. But when it comes to information, that is not the case – quite the opposite.

In the Information Age, humans are producing as well as consuming information at astonishing rates. Here are some numbers to help us illustrate this defining trend:

- In 2011, the then CEO of Google, Eric Schmidt said that it now takes two days to create the amount of information created between the dawn of time and 2003<sup>34</sup> (widespread use of internet).
- In 2008, a study on Americans found that an average person gets exposed to and processes up to 34 GB of information a day through television, computers, cell phones, tablets, billboards, and many other gadgets.<sup>35</sup> The same study found that every year (from 1980 until 2008) the annual increase was about 5 %. If we assume that this increase stayed the same, in 2022 we are at 75 GB of daily processed information.
- Tests showed that the brain has a processing capability of between 60 – 120 bits per second during a specific task.<sup>36</sup> This means that the unconscious part of the brain is processing trillions of bits in the background, bringing to our attention only what is assessed as critical for decision making. Since the amount of information that needs to be assessed is constantly growing, the brain is struggling to keep up.

The human brain consumes a lot of energy. But the amount of energy that gets allocated to brain activities is roughly the same every day, regardless of the complexity of tasks. Furthermore, the capacity to replenish that energy is limited - mostly to sleep and rest, and, to a lesser extent, food. And while it is true that our brains are very plastic –, meaning that they can adapt to varying input relatively fast to enable effective decision making and problem solving– still, the rate at which the information intake is increasing is outpacing this rewiring ability of our brains.<sup>37</sup> The sheer amount of information that we are exposed to and need to process and elevate to decision-making level is causing us to burn our available daily allotment of brain energy (also called “neural energy”) earlier and earlier in the day, before we are able to

<sup>34</sup> [www.huffpost.com/entry/google-ceo-eric-schmidt-p\\_n\\_671513](http://www.huffpost.com/entry/google-ceo-eric-schmidt-p_n_671513)

<sup>35</sup> Bohn, R. E. and Short, J. E. (2009), “How much information? 2009 report on American consumers”. *Global Information Industry Center*, UC San Diego, CA.

<sup>36</sup> MIT Technology Review, available at [www.technologyreview.com/2009/08/25/210267](http://www.technologyreview.com/2009/08/25/210267)

<sup>37</sup> Jacob, K., Löwe, J., Manz, D., Schindler, D., Strathausen, R. and Walzl, B. (2022), “Lawyer Well-Being: Personal Health of Legal Professionals in Times of Disruption”, *LLI White Paper*, Weblaw.

sleep and replenish it. As a consequence, a well-documented set of negative effects is likely to manifest itself. This phenomenon is referred to as “information overload syndrome” or more colloquially – “infobesity”.

The phrase “information overload syndrome” has been around for some 60 years. Its creation is often associated with the work of the American social scientist Bertram Gross.<sup>38</sup> However, the syndrome has really intensified in the last 20 years through the rise of digital means for (hyper-)production, dissemination and consumption of information. It is safe to say that most people in modern societies are experiencing at least some of the effects of information overload.

According to the Information Overload Research Group (IORG), the negative effects of information overload are:<sup>39</sup>

- incorrect decisions,
- premature decisions,
- decision-making delays,
- decision fatigue,
- loss of productivity, and
- stress.

Additionally, the endless stream of information readily available all around us is a source of constant distraction, which interrupts and scatters our attention. Research has shown that the time that it takes an individual to return to what they were doing before an interruption is often far greater than the length of the interruption itself because the brain needs time to reorient itself to what it was doing before the interruption occurred.

There is no easy way to circumvent this issue, and the current approach – making each individual responsible for managing their own information exposure – simply means that most people will fail to properly identify the source of the problem, design an effective information filtering system and possess the discipline to follow it daily. Not to mention how peer pressure (“fear of missing out”) to keep scrolling down the endless information feed is a motivation factor that is far too powerful for most people to resist.

### 3.2 How is information overload affecting the legal profession?

Legal work, in principle, results in output made up of long and complex text with legal references and possibly overwhelming jargon. Because of that, it can be said that legislative, judicial and other legal documents require a high cognitive effort to analyse and use as a basis for action.

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<sup>38</sup> In his two-volume book *The Managing of Organizations: the Administrative Struggle*, published in 1964.

<sup>39</sup> [iorgforum.org/io-basics/](http://iorgforum.org/io-basics/)

As explained above, information overload is severely draining people's cognitive ability and legal documents are competing for attention with all the other sources of information, also in the C-suite. Here, one can say that legal documents, because of their impact on individuals, should be given priority in the distribution of cognitive resources. And that is true, to a certain extent. However, even if prioritised by the user, legal documents in their traditional format are not created in a way that speaks to the average individual who neither has the specific knowledge to properly dissect and evaluate the content nor has the time and available neural energy to invest in the task. The drop-off in attention is especially drastic when it comes to legislation.

By failing to recognise and adjust to the short attention span and scattered attention of addressees, lawmakers and other legal professionals are obfuscating the desired legal effect. The need to bridge the gap between the product of legal work and the general population is even greater when we consider another negative aspect of the abundance of information: the inability to determine what is true. An information war is raging on the Internet and, in recent years, we have come to know concepts like fake news and post-truth, which describe misinformation campaigns and the devaluation of facts in public communication.<sup>40</sup> Liberal democracies have always depended on professional journalism to provide people with reliable information for the deliberative public sphere.<sup>41</sup> This concept is now facing unprecedented challenges, which the last two US presidential elections and the Brexit referendum best exemplify.

While legal design and legal knowledge visualisation are not the ultimate solutions, applying this mindset immediately helps by putting the focus on product usability and the legal capabilities of the legal professionals who are involved. Empathy and creativity are essential parts of the process and, when combined with reliance on visual elements, they result in better understanding, acceptance and impact.

## 4 Case study: examples from the ECB Legal Services

### 4.1 Case study 1: How-to guide on EUR-Lex functionalities

#### PROBLEM

Improving the creation and management of topical collections of legal acts, while keeping them up to date and immediately usable to support output such as the drafting of new or amending legal acts, drafting legal advice, providing opinions, or creating legal acts in all the official languages of the EU.

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<sup>40</sup> Harjuniemi, T. (2022), "Post-truth, fake news and the liberal 'regime of truth' – The double movement between Lippmann and Hayek", *European Journal of Communication*, 37(3), pp. 269–283. doi.org/10.1177/02673231211046784

<sup>41</sup> McNair, B. (2012), *Journalism and democracy: An evaluation of the political public sphere*.



## SOLUTION

Creating a PDF guide with easy-to-follow steps, prominent and informative screenshots and direct links.

**Figure 1**

Screenshot of the How-to guide

**HOW-TO GUIDE: CUSTOM LEGAL ACT COLLECTIONS IN EUR-Lex**  
Create - Export - Store - Share

**Step 1**  
**Login to EUR-Lex**  
Only registered users can create folders and save/export items.

**Step 2**  
**Find the relevant legal act(s)**  
You can use any retrieval method you prefer, such as document number or browsing by type/year.

**Step 3**  
**Add the legal act to My items**  
On the legal act page view, use the "Save to My items" link in the left menu to choose a folder where you want the legal act to be saved (see screenshot 3).

**Step 4**  
**Create a folder or choose an existing one**  
The system prompts you to select a destination folder. For the first-time creation of a collection, select "Create new folder" and give it a name (see screenshot 4). If you want to add to a pre-existing folder, you will find all folders in a list in the drop-down menu after clicking the down arrow in the "Folder" field.  
Click "Save" when you are finished.

**Step 5**  
**Repeat steps 2-4 for each legal act**  
Find all the other legal acts that belong in your "background" collection and add them, one by one, to the folder you created (Note: remember to add them to the same project folder by using the drop-down arrow option, as described in Step 4).

**Step 6**  
**Go to the collection you just created**  
Your folder can be accessed from a drop-down list by clicking on your username in the top right corner and selecting "My items" (see screenshot 6).

**Step 7**  
**Select your folder and "Export" to get the collection in PDF format**  
Select your folder from the list. Once it opens, you will see all the legal acts you added to that folder. This is your collection of relevant legal acts. Check if everything is there and then click "Export" > "Export all" (located above the first legal act, on the right side of the grey bar). You can adjust export settings in the pop-up window if you have special needs, but default settings should work just fine too.

**Step 8**  
**Store and share**  
You will find the PDF in your Downloads folder. Check it and if it looks good, proceed with saving it to the project folder in DARWIN and share the link.

Created by: Filip Lulić (DG-L Knowledge Management team), January 2022  
filip.lulic@ecb.europa.eu

Source: DG Legal Services, ECB

## BENEFITS

- Format: PDFs are easy to store and disseminate. They are also easier to produce and update than videos are.
- Time: Faster retrieval of up-to-date legal references and less manual maintenance work.

- Efficiency: How-to guides are more efficient than individual training and purely textual manuals.

## 4.2 Case study 2: Topical tube map

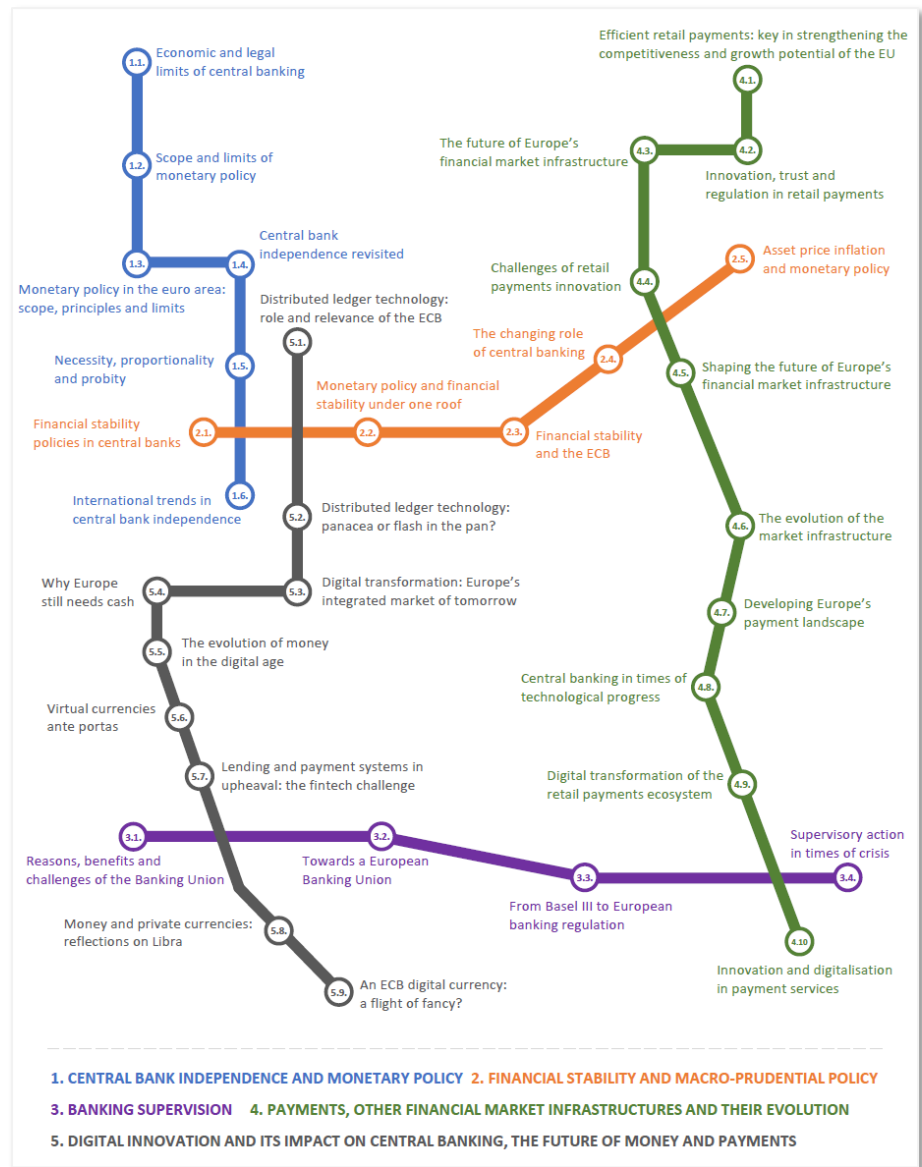
### PROBLEM

Offering a user-friendly way of browsing and navigating doctrinal pieces on different legal topics.

### SOLUTION

Using a recognisable visual metaphor of the underground tube (metro) map to enable users to find relevant topics and locate individual documents quickly (by including direct links to full articles in the PDF).

**Figure 2**  
Example of a topical tube map



Source: DG Legal Services, ECB

### BENEFITS

- Format: Intuitive, simple, sharable, and easy to edit and update.
- Time: Quick understanding of the content and topics covered. Fast access to desired content.
- Efficiency: Supports knowledge management and sharing.

## 4.3 Case study 3: Guidance on the procedure for recasts of legal acts

### PROBLEM

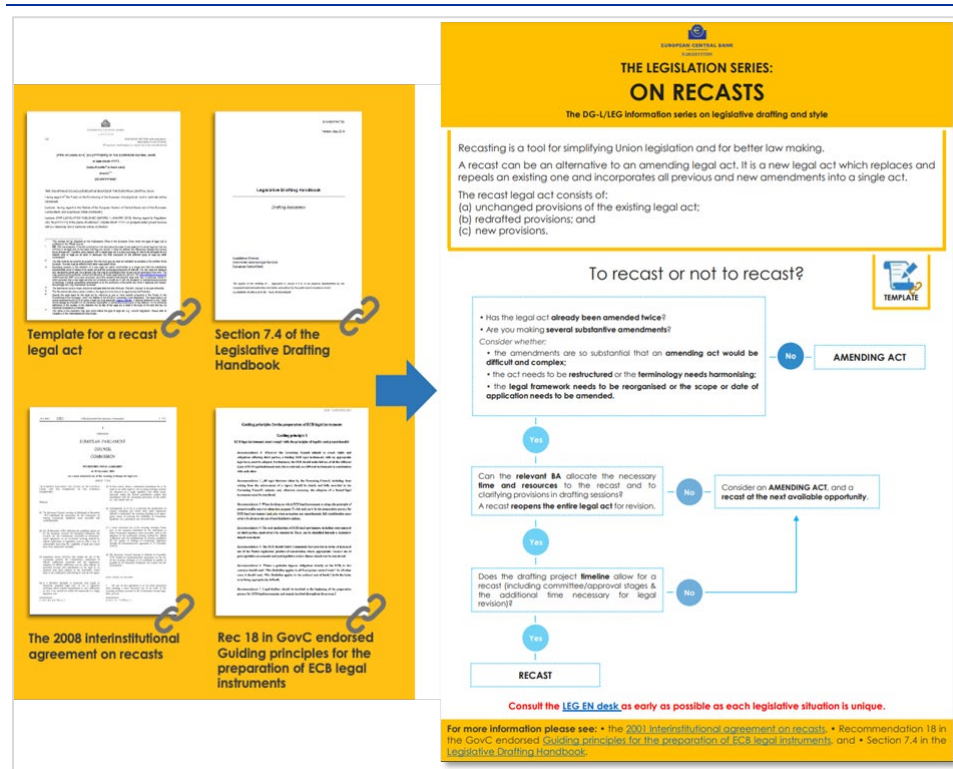
Users needed to be empowered to make a correct decision on whether to amend or recast a legal act without having to go through a set of detailed manuals (left part of figure 3 below) to identify guidelines on whether to recast or amend.

### SOLUTION

Concisely showing the main information for determining whether to recast (definition and scope) and providing a decision tree to make it easy for the user to find out if a recast is the appropriate tool for the job. Useful links to a contact point, recast template and detailed background documentation, which are all available at the discretion of the user, were added for efficiency.

**Figure 3**

From several textual guides to a one-page infographic



Source: DG Legal Services, ECB

### BENEFITS

- Format: One-page infographic (PDF).
- Time: Less time is needed for users to get to the most important information for their work.
- Efficiency: Knowledge sharing, correct use of legislative tools, and empowering users.

## 4.4 Case study 4: Visual navigation of the ECB legal framework (EUR-Lex)

### PROBLEM

Enhancing accessibility of the ECB's corpus of legal acts and instruments in EUR-Lex.

### SOLUTION

Analysis of the legal framework to select representative categories/topics of legal acts and create graphs with total/annual legislative activity. Additionally, built-in functionality to improve navigation – each bar is a clickable, dynamic link to a custom legal act compilation represented in the chart.

**Figure 4**

Part of the Visual Navigation tool from the ECB's EUR-Lex page



Source: eur-lex.europa.eu

## BENEFITS

- Format: Chart-based dashboard on EUR-Lex.
- Time: Users can explore different sub-corpora of legal acts in an intuitive way.
- Efficiency: The ECB legal framework is presented in a way that is accessible to non-experts. Charts are automatically updated when new legal acts are published and no manual maintenance is required.

For a detailed discussion on the Visual Navigation tool of the ECB legal framework and a broader view of enhancing access to EU law, please refer to the Panel 1 discussion of the ESCB Legal Conference 2020 – in particular V. Saintot's article “Establishing the foundation for visual navigation: the ECB legal framework in EUR-Lex” available [here](#).

## 5 Conclusion

This article was written in the aftermath of the global coronavirus pandemic, in the middle of an energy crisis and at the brink of a massive global recession, which is all happening at the same time as a number of societal transformations including – climate change and green transition, race, gender and identity movements, expansion of the virtual/digital domain, information overload and the crisis of truth – just to name a few. It is safe to say that the world is going through a major shift. The challenge lies in navigating changes on many levels simultaneously. Are we able to renegotiate so many clauses in the “social contract” at the same time, with enough wisdom to avoid the mistakes of the past?

Whatever the case may be, we know that legal professionals are involved in legislative, interpretative and advisory functions in all walks of society, and that means that lawyers play a key part as guardians of the rule of law. This article attempted to point out that legal professionals should acknowledge the complex societal challenges and upgrade their toolboxes to meet them with the logic of augmentation and not substitution.

The reason why we chose to focus on legal design and legal knowledge visualisation is because it enables a shift in mindset and daily practice by placing the focus on the collective and the ecosystem of stakeholders. Introducing an external perspective in the process of creating legal output is slowly building a bridge between abstract law and material reality. This bridge is needed if we are interested in restoring trust in public institutions, which is rapidly eroding.

Several conditions must be respected for visualisation and design to fulfil their promise. First, legal design must be practiced with honesty, humility and integrity. Otherwise, there is a risk of misusing it to keep doing more of the same, just in new clothes. Legal design must not be reduced to decoration and a friendly look and feel that is applied at the end of the production line to make the outcome look “pretty”. Second, legal design and visualisation are not about oversimplifying the complexity of

legal work. However, it is about questioning where this complexity is inevitable and where it is introduced for unjustifiable or self-serving reasons. Third, legal design and visualisation do not only help the end user, because practicing them inevitably leads to self-reflection. By following legal design and legal knowledge visualisation methodologies, legal professionals are transforming their craft. And it is not possible to transform the craft without transforming the practitioner. Legal design and legal knowledge visualisation invite legal professionals to develop compassion, empathy and perform regular checks of their inner motivations and values, and of their contribution to the broader society.

The disrupted times we live in stimulate us to acquire new and more sustainable methodologies to adapt and overcome the challenges that we face. Legal design and legal knowledge visualisation are tangible and transformative steps for legal professionals to rise to the occasion.

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## Panel 2

# Monetary policy operations with non-banks: legal, financial and comparative aspects





# On the monetary policy operations with non-banks: legal, financial and comparative aspects

By György Várhelyi\*

Non-bank intermediation and the increasing role that non-banks play in the transmission of monetary policy impulses has become obvious in the recent years. There is substantial evidence that non-banks take a more prominent role in credit provision in Europe and globally. Lending provided by non-banks, including FinTech companies, is steadily increasing and trends observed outside the EU show that Big Tech and other non-traditional lenders are successfully entering the lending market. Notwithstanding its increasing importance, at its current juncture, non-bank lending has not yet been harmonised across the EU, and this may create challenges for all stakeholders, including regulators.<sup>42</sup>

This overall trend which will probably stay with us for many years to come is not only relevant for regulators and banking supervisors but also for the monetary policy arm of central banking.

In addition to that growing phenomenon, the recent COVID-19 induced crisis has shown that non-bank financial intermediaries can exacerbate financial stability risks and thereby also impact orderly, and even transmission of, monetary policy. In such crisis periods, fire sales of assets held by these entities can lead to an impairment of the monetary policy transmission mechanism.<sup>43</sup> But, aside from crisis periods, it has also been argued that these intermediaries are, in a certain sense, more responsive to monetary policy measures that influence longer-term interest rates,<sup>44</sup> such as asset purchases.

Alongside asset purchases, short-term policy rates constitute an effective tool to steer interest rates in the euro area. The recent increases of the three key ECB interest rates serve as a potent example. But what is even more important is that short-term policy rate impulses sent out by the ECB should be transmitted evenly to the euro area economy, thereby providing another reason to assess the impact of non-banks in this context. The approval of the Transmission Protection Instrument by the ECB's Governing Council demonstrated the importance of an effective and even transmission of these policy rates across jurisdictions, especially when normalising

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<sup>42</sup> See European Banking Authority's, "Final Report on response to the nonbank lending request from the CfA on digital finance".

<sup>43</sup> See Speech by Isabel Schnabel, "The rise of non-bank finance and its implications for monetary policy transmission", 24 August 2021.

<sup>44</sup> See ECB Occasional Paper No 270 September 2021, "Non-bank financial intermediation in the euro area: implications for monetary policy transmission and key vulnerabilities".

the monetary policy stance in a post-COVID environment characterised by an ongoing war at our borders, a fomenting energy crisis and an inflation shock of unprecedented scale in recent times.

The open question remaining here is whether non-banks could be a useful channel for monetary policy transmission in the current swing of monetary policy normalisation. An example that immediately comes to mind in this respect is the so called “leaky floor” phenomenon. Non-banks have no access to central bank liquidity storage facilities and their market power vis-à-vis banks is limited, resulting in a remuneration on their bank deposits that is less favourable than the deposit facility rate (DFR). In the context of the Federal Reserve System Bech and Klee (2011)<sup>45</sup> showed that monetary policy normalisation – amid abundant excess liquidity – can potentially exacerbate this problem; increased policy rates may also entail increased spreads between DFR and deposit rates applied to non-banks by credit institutions (i.e., a case of “leaky floor”).

Against this background, non-banks seem relevant for monetary policy purposes both as regards longer and shorter-term interest rates. This was also underlined in the context of the ECB’s 2021 strategy review<sup>46</sup>, with the analysis conducted as part of the revision of the ECB strategy confirming non-banks’ relevance for the transmission of monetary policy.

The issue, however, remains that traditionally Eurosystem central banks interact only with credit institutions, and that, until now, the Eurosystem counterparty framework has been designed almost exclusively for credit institutions. The General Documentation Guideline<sup>47</sup> sets the relevant eligibility criteria which are all tailor-made for credit institutions.

The first requirement under Article 55 of the General Documentation Guideline is that the candidate counterparty is subject to minimum reserves. This first eligibility criterion already raises an issue for non-banks since Article 19.1 of the Statute of the European System of Central Banks and of the European Central Bank (the “Statute of the ESCB”) enables the ECB to subject only credit institutions to minimum reserves (to the exclusion of other types of market participants).

The second requirement is that the counterparty is covered by prudential supervision under the Capital Requirements Regulation and Directive (or other comparable requirements). Apart from certain large investment firms, this second requirement would also need to be revised in order to admit non-banks as counterparties.

The third requirement concerns financial soundness. Whilst financial soundness remains a broad concept it relies to a large extent, albeit not exclusively, on the compliance of the counterparty with minimum own funds requirements. Again, applying this to non-banks will be challenging.

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<sup>45</sup> Morten L. Bech and Elizabeth Klee, “The mechanics of a graceful exit: Interest on reserves and segmentation in the federal funds market”, *Journal of Monetary Economics*, 2011.

<sup>46</sup> See [An overview of the ECB’s monetary policy strategy article](#).

<sup>47</sup> Guideline (EU) 2015/510 of the European Central Bank of 19 December 2014 on the implementation of the Eurosystem monetary policy framework (General Documentation Guideline) (ECB/2014/60).

Finally, with respect to the specific instrument or operation, the counterparty must also fulfil all operational requirements specified in the contractual or regulatory arrangements applied by the home national central bank or the ECB. This could be a challenge for non-banks that do not have legal personality and, hence, may not be able to enter into direct contractual arrangements with Eurosystem central banks.

At this point, you might be right to think: what are we discussing then?

Here I feel it is necessary to recall that the recent unexpected shocks that hit European and global economies taught us that the monetary policy toolbox of Eurosystem central banks is extremely vast! Let me just mention the events in the past few years: the global financial and ensuing debt crisis, the COVID-19 pandemic, the increasing costs generated by global warming and Russia's unjustified aggression towards Ukraine. The distress caused by such events in European economies highlights that we are facing a fast-evolving world which requires constant reassessment of the economic and market conditions as well as a readiness to pull the appropriate tools from our toolbox.

Being a lawyer myself, I could not but also emphasise at this point that Article 18.1 of the Statute of the ESCB, defining the ECB's monetary policy instruments, explicitly envisages that credit operations may be conducted with credit institutions as well as with "other market participants".

To conclude, this ultimately leaves us with 3 questions to answer:

Should access of non-banks to central bank liquidity be part of the Eurosystem's toolbox in order to address a monetary policy need/objective?

Could access of non-banks to central bank liquidity be part of that toolbox in order to address a monetary policy objective?

How could access of non-banks to central bank liquidity be part of that toolbox in order to address a monetary policy objective? There are many available avenues, but would it be preferable to provide access to collateralised lending, i.e. on the asset side, or should such access be restricted to the deposit facility, i.e. liability side.

This is a very exciting discussion that we will be having today with our panel consisting of 3 prominent speakers!

Imène Rahmouni-Rousseau is the Director General of Market Operations at the ECB, in charge of implementing the single monetary policy for the euro area! Imène is also a member of the Bank for International Settlements Markets Committee and chairs the ECB Market Operations Committee. She is the author of several articles on financial markets and monetary policy implementation, most recently on the scarcity effect of quantitative easing on repo rates, published in the Journal of Financial Economics. Imène will discuss the monetary policy and financial stability case for granting access to non-banks. In other words, she will address the "should" and the "how".

Following Imène we have, Kerstin Schaepermann, a prominent lawyer and senior counsel at Clifford Chance, where she advises on cross-border banking and

investment services as well as the regulation of derivatives and financial market infrastructures. Kerstin will tell us whether we actually “could” provide for such access by describing some of the limitations resulting from the legal requirements.

Last but certainly not least, we will hear Marco Cipriani, the Head of Money and Payments Studies at the Federal Reserve Bank of New York. Marco has authored an extensive list of publications which I will not dare to cite in full. I would only mention that he has recently published an article on “The Money Market Mutual Funds Facility” in the Federal Reserve Bank of New York’s Economic Policy Review. Marco will present how the Federal Reserve Bank of New York has set up its Overnight Reverse Repo Facility or, how Marco will most certainly refer to it, ON RRP.

# Monetary policy operations with non-banks: financial, operational, and comparative aspects

By Imène Rahmouni-Rousseau\*

In recent years, there has been significant growth in the size of euro area non-bank financial intermediaries' (NBFIs) balance sheets. This has come at a time when the level of liquidity being intermediated in the euro area financial system has increased as a result of the expansion of the Eurosystem balance sheet. At the same time, NBFIs have no direct recourse to the Eurosystem balance sheet with access to monetary policy operations restricted to euro area credit institutions only.<sup>48</sup> However, amid the ever-growing euro area NBFIs sector, these financial intermediaries have become increasingly relevant in the transmission of monetary policy. Recent evidence of this is available from the role of NBFIs during bouts of market volatility, whereby the behaviour of NBFIs amplified the adverse feedback loops during the COVID-19 market turmoil. Meanwhile, it is also evident that NBFIs have become significant players in euro area money market transactions. As such, and as the Eurosystem makes further progress in normalising its monetary policy after a long period of low interest rates, it is an opportune time to take stock of the possible considerations around NBFIs access to the central bank balance sheet and how this could be done.

## 1 The increasing role of NBFIs in euro area money market activity

Detailed as follows are the primary factors which have given rise to NBFIs playing an increased role in euro area money markets, which are, of course, crucial for the implementation and transmission of monetary policy. In short, a greater level of central bank liquidity in the financial system has reduced credit institution's demand for exchanging liquidity among themselves, while a growth in the size of NBFIs resulted in a higher need for NBFIs to partake in money and capital markets in order to deposit funds and find respective investment opportunities.

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\* Director General of Market Operations at the European Central Bank. This contribution reflects the author's own views and not necessarily those of the European Central Bank.

<sup>48</sup> As defined in Article 4(1) of Directive 2006/48/EC and subject to fulfilling the eligibility criteria specified in Article 55 of Guideline (EU) 2015/510 of the European Central Bank of 19 December 2014 on the implementation of the Eurosystem monetary policy framework (ECB/2014/60) (OJ L 91, 2.4.2015, p. 3).

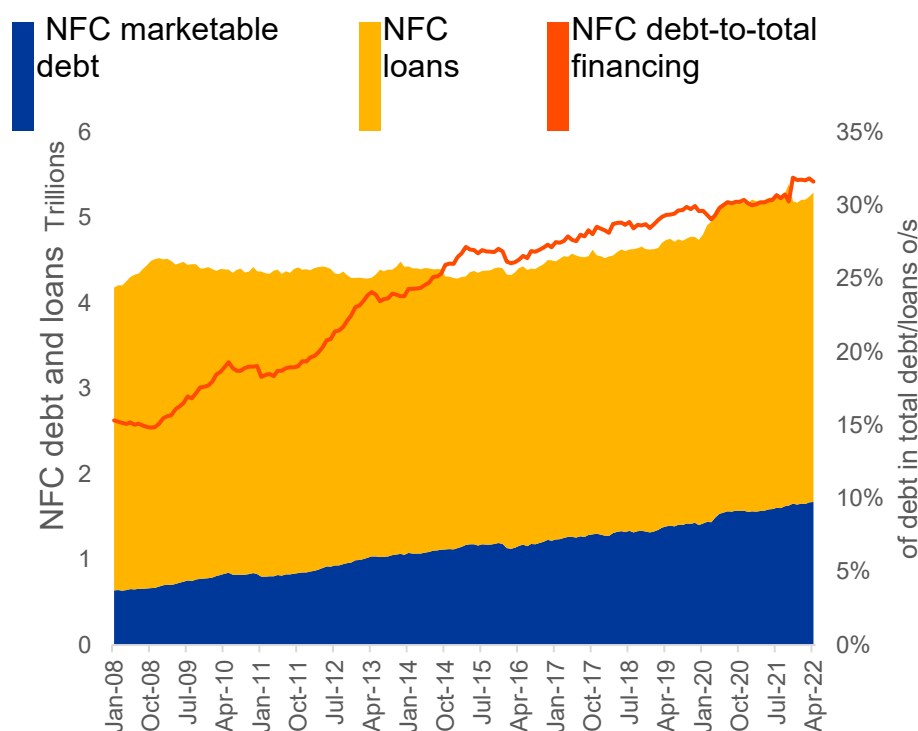
## 1.1 The growth in the NBFi sector

In recent years, a persistent increase in the size of the NBFi sector can be observed. This increase has been universal across NBFi sectors, including euro area investment funds (IFs), money market funds (MMFs), and insurance corporation and pension funds (ICPFs). Indeed, since December 2008, the size of these three sectors has increased from EUR 12 trillion to EUR 28 trillion in June 2022, driven both by flow and valuation effects. Further, it is worth noting that since the GFC, the pace of NBFi balance sheet growth has outpaced that of the banking sector resulting in an increase in the relative size of NBFis also.

There are significant differences in the business model, nominal size, and the number of NBFis in each sector. In terms of asset composition, while loans take a prominent role on the asset side for the banking sector, the asset side of the balance sheet of NBFis is dominated by debt securities, equity, and fund shares. As such, the importance of non-banks is also reflected in their expanding role in financing the real economy. **Chart 1** demonstrates that while non-financial corporate (NFC) financing still primarily comes from bank credit, NFCs have been increasingly turning toward credit markets for their financing (as depicted by the red line). In line with their expanding balance sheet size, NBFis are increasingly acting as the absorbers of such issuance – which not only increases their role in the real economy, but also their overall interconnectedness across financial markets.

**Chart 1**  
Euro area non-financial corporate finance composition

(LHS: EUR trillion, RHS: percentage of NFC debt outstanding/NFC loan)



Source: Statistical Data Warehouse

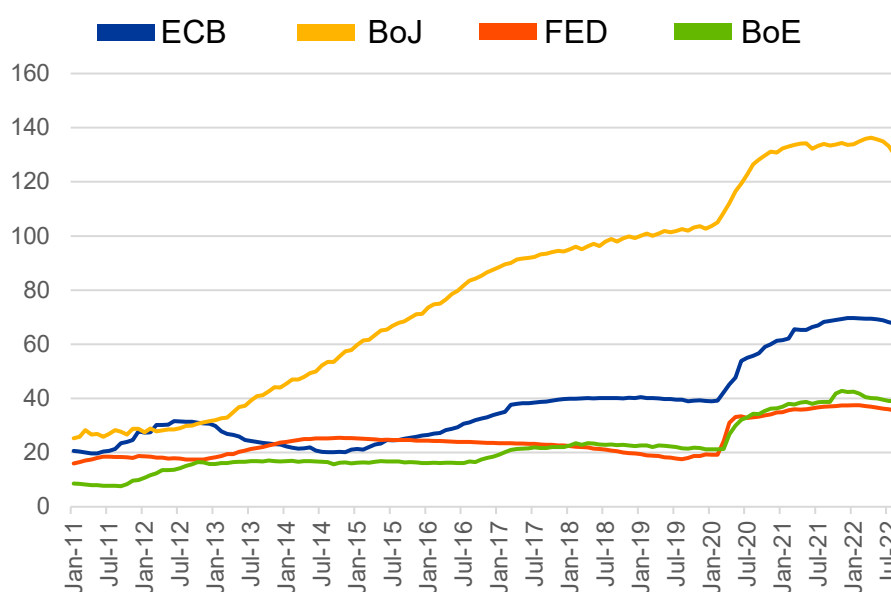
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## 1.2 Recent evolution in the Eurosystem balance sheet and European market structure

The past decade has also seen a significant increase in the size of most major central bank balance sheets. This can be observed both in nominal terms, but also when measured against respective Gross Domestic Product (GDP). As evident from **Chart 2**, this occurred in two distinct phases. First, in the aftermath of the Great Financial Crisis (GFC), central banks took a number of exceptional measures to ensure ample liquidity support was provided, including the conduct of large-scale asset purchases and longer-dated lending operations. This phase of balance sheet expansion was relatively gradual but took place over a prolonged period. Second, and more recently, there was the shorter but rapid expansion of central bank balance sheets in response to the financial and economic turmoil arising from the outbreak of COVID-19.

**Chart 2**  
Size of selected central bank balance sheets relative to GDP

(percentage, depicts the size of selected central bank balance sheets relative to respective GDP)



Source: Bloomberg

In both instances, the deployment of central bank balance sheets was a necessary step taken to ensure the appropriate monetary policy stance and to safeguard market functioning and preserve the orderly transmission of monetary policy. However, at the same time, this has also led to central banks having a significantly larger footprint across financial markets.

One way to measure this footprint in the euro area is the tracking of the growth in euro area excess liquidity over this period. Excess liquidity can be defined as any liquidity available in the banking system that exceeds banks' needs to fulfil minimum reserve requirements. Again, while this increase in excess liquidity in the euro area supported favourable financing conditions, it can also be said to have had a profound impact on European money market rates. In particular, it resulted in a movement away from the

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pre-GFC environment of liquidity deficit in the banking sector maintained by the Eurosystem (discussed further in Section 2), resulting in liquidity no longer being scarce among such institutions and reducing their demand for liquidity.

In parallel, an erosion of interbank transactions in the money market due to structural changes imposed by regulatory reform and higher level of risk aversion by credit institutions was also observed over this period. Such regulatory reform includes enhanced capital requirements, new liquidity provisions and the implementation of the Leverage Ratio. While the introduction of such regulation was necessary to strengthen the resilience of the banking system, a side effect was a reduction in the desire and ability of credit institutions to partake in euro area money markets, in particular for unsecured transactions. Indeed, constrained bank balance sheets, coupled with banks' higher level of risk aversion following the GFC, has led cross-border money market activity to decrease compared to 2007.

## 2 The role of the central bank balance sheet in financial intermediation

While the previous section discusses the factors which have driven the increased role of NBFIs in money markets, the following section considers how the Eurosystem balance sheet policy affects financial intermediation.

### 2.1 The specific role of credit institutions

In order to answer the question of whether we should expand monetary policy operation's access to NBFIs, it is first worth considering why the privilege of balance sheet access is granted to credit institutions – also referred to as “eligible monetary policy counterparties”. Eurosystem monetary policy is transmitted – first, across euro area financial markets and banks, and next, to the real economy. The Eurosystem has no direct interaction with the real economy, i.e., businesses and households.<sup>49</sup> In this manner, the ECB relies on the transmission, or pass through, of the Governing Council's monetary policy decisions to the real economy via the financial system (which includes both existing monetary policy counterparties and NBFIs). Therefore, it can be said that under the current constellation of monetary policy tools, the provision of balance sheet access to credit institutions is not a choice, but rather a necessity as this allows for the desired monetary policy stance to be passed through to the real economy.

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<sup>49</sup> It should be noted that with the introduction of the Corporate Sector Purchase Programme, direct interaction with the real economy was introduced given the purchasing of bonds in the primary markets. For further detail, please see: <https://www.ecb.europa.eu/mopo/implementation/app/html/cspp-qa.en.html>

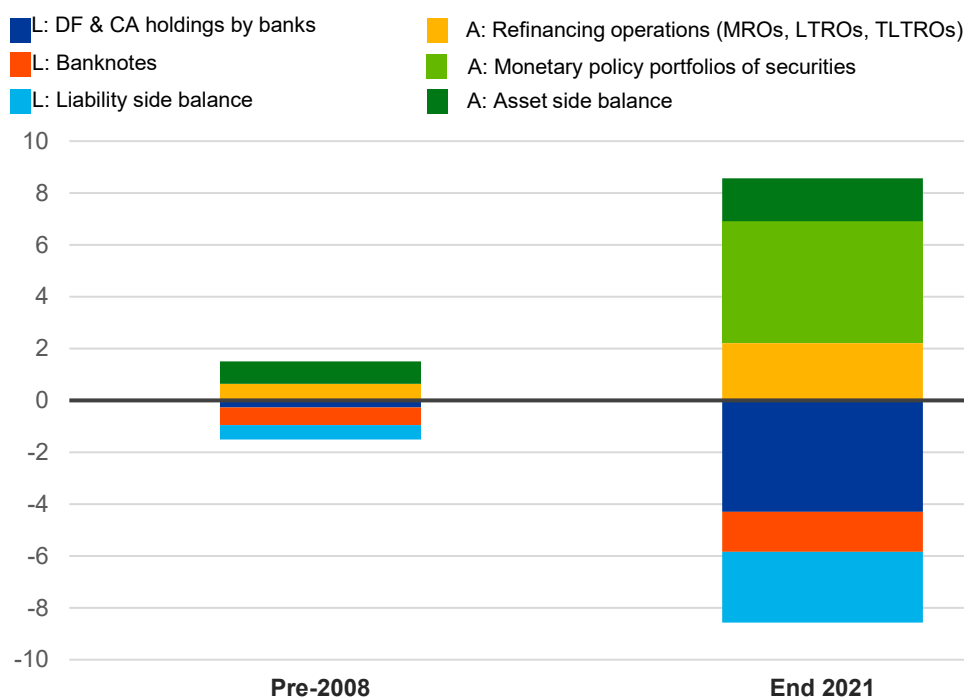
## 2.2 The current central bank balance sheet

Since the GFC, the size of the Eurosystem balance sheet has been amended significantly. In addition, the composition of the balance sheet has also been notably adjusted (**Chart 3**). First, pre-GFC, the provision of liquidity was conducted on a short-term basis (mainly via the weekly Main Refinancing Operations) and was also conducted on a quantity limited and auctioned basis, again with a view to ensuring the limited amount of liquidity needed for a clean transmission of monetary policy.

In recent years however, the current Eurosystem balance sheet is exemplified by outright portfolios and longer-term and targeted lending operations. Meanwhile, the provision of liquidity via the Main Refinancing Operations is now conducted on a full allotment basis, i.e. there is no explicit limit on the amount of liquidity any credit institution may receive (once they have adequate and sufficient collateral).<sup>50</sup>

**Chart 3**  
Stylised Eurosystem balance sheet

(EUR trillion, depicts a stylised example of the change in the Eurosystem balance sheet between end-2008 and end-2021)



Source: ECB

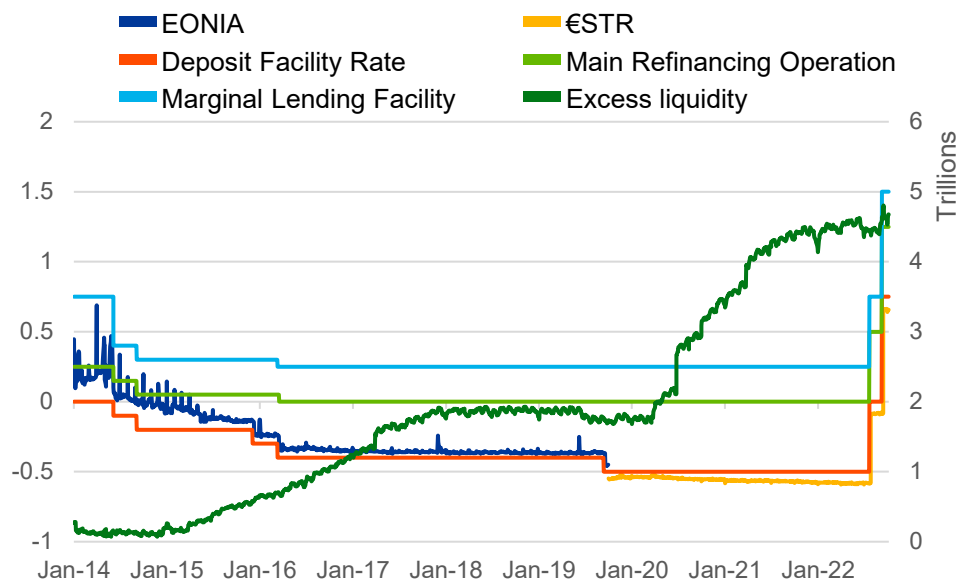
Beyond this, net asset purchases via the Eurosystem purchasing programmes have also introduced significant levels of liquidity into the euro area financial systems. Therefore, the provision of excess central bank liquidity significantly reduced the need for banks to transact liquidity among themselves.

<sup>50</sup> In the case of targeted longer-term refinancing operations (TLTROs), the level of lending is restricted by the applicable borrowing limits, as detailed here: <https://www.ecb.europa.eu/mopo/implement/omo/tltro/html/tltro-qa.en.html>

As a result, the marginal rate of borrowing in financial markets has become closer to the ECB's deposit rate, rather than the Main Refinancing Operation. **Chart 4** depicts this phenomenon, highlighting the downward movement of money market rates (in this case, EONIA and then €STR) from the Main Refinancing Operation (MRO) - the centre of the ECB's interest rate corridor – to the Deposit Facility Rate – the floor of the ECB's interest rate corridor amid the increase in excess liquidity.

**Chart 4**  
Eurosystem excess liquidity and money market rates

(RHS: percentage; LHS: EUR trillion)



Source: Bloomberg

NBFIs have no direct recourse to the Eurosystem balance sheet and cannot borrow or deposit money directly from the central bank. Instead, NBFIs must therefore turn to banks in order to fulfil their liquidity storage needs. The combination of the aforementioned factors (including increasing excess liquidity, reduced credit institution's participation in money markets, and an expansion in the NBFIs sector) now means that the intermediation role of banks, accepting deposits of non-banks to subsequently place them with the Eurosystem, has become the dominant trade in euro area unsecured money markets.

### 3 Considerations related to access to the asset side of the central bank balance sheet

As noted in Section 2 above, many of the post-GFC tools have significantly expanded the Eurosystem's asset side – from the introduction of large-scale asset purchases to the provision of longer-dated and targeted lending operations.

However, these amendments primarily affected the manner in which liquidity was provided from the Eurosystem to existing monetary policy counterparties (notwithstanding the purchasing of bonds in the CSPP in the primary market). As such, the provision of asset side access to NBFIs could be considered in terms of how it may complement such existing tools, and also as a means of providing liquidity specifically and directly to NBFIs if such a motivation arises.

### 3.1 Potential avenues for granting asset side access

In providing liquidity directly to NBFIs, it is important to differentiate the potential motivations behind providing such balance sheet access. There are two broad potential motivations, which would imply different types of facilities, namely:

1. Constantly available (i.e. standing) facility: The motivation behind such a facility would be to allow NBFIs to meet redemption requests on an ongoing basis through access to central bank liquidity. However, such a facility would significantly reduce money market activity and would also create very high moral hazard, as NBFIs would lack an incentive to prudently manage their liquidity buffers.
2. Backstop facility: The motivation behind such a facility would be to provide NBFIs with liquidity during crisis periods marked by sizable liquidity demand shocks due to unexpected and significant redemptions. In such instances, NBFIs could instead meet redemption requests through central bank liquidity only at a time when redemption pressures would, absent a backstop, lead to rapid and massive liquidation of assets, leading to self-fulfilling dynamics. This would provide relief in periods of high market stress and ensure the smooth transmission of monetary policy by maintaining financial stability. Such a facility should be priced in such a way that it is attractive during crisis periods, but it is not the preferred option in regular times.
3. Notably, while both facility types may allow for central bank liquidity to be used as an alternative to immediate asset sales, it should be noted that, ultimately and if redemptions do not reverse, NBFIs will likely be required to conduct asset sales given that central bank liquidity provision is finite in maturity. Therefore, even at the outset, it appears that the provision of a backstop facility would be a better business case given that NBFIs may only seek to receive central bank liquidity at times when immediate asset sales is not possible or would occur at heavily discounted prices, i.e., during crisis periods, with central bank liquidity provision following the lender-of-last resort logic.

### 3.2 The role of NBFIs during COVID-19

A good starting point for evaluating the motivation behind providing NBFIs access to the Eurosystem balance sheet is their role during the COVID-19-related market volatility. At this point, it is well-documented that the behaviour of some NBFIs sectors

during this period resulted in the amplification of risk-off moves, rather than acting as risk absorbers. Such a phenomenon was apparent even in lower risk markets, such as sovereign fixed income markets. For instance, in the United States, Eren and Woodridge (2021) highlight the pro-cyclical behaviour of NBFIs during March 2020, citing the role of leverage that had built up within specific sectors, and the subsequent rapid seeking of more liquidity holdings, as factors contributing to the downward pressure and high volatility observed in the US Treasury market at the time. Meanwhile, in the United Kingdom, evidence has also been provided in relation to the role of NBFIs in relation to the deterioration of sterling markets. Czech et. al (2021) detail the manner in which NBFIs' liquidity demand proved significant in affecting UK markets. In particular, it was noted that NBFIs' behaviour contributed to a large net liquidity demand in gilt repo markets, amounting to GBP 15 billion over the 'dash for cash' period. This, in turn, led to a deterioration in market fundamentals, including a short rise in gilt yield, bid-ask spreads and premiums on repo borrowings. The authors cite a number of factors influencing such behaviour, including the role of variation margin calls on derivatives as drivers of the increase in NBFIs' liquidity needs.

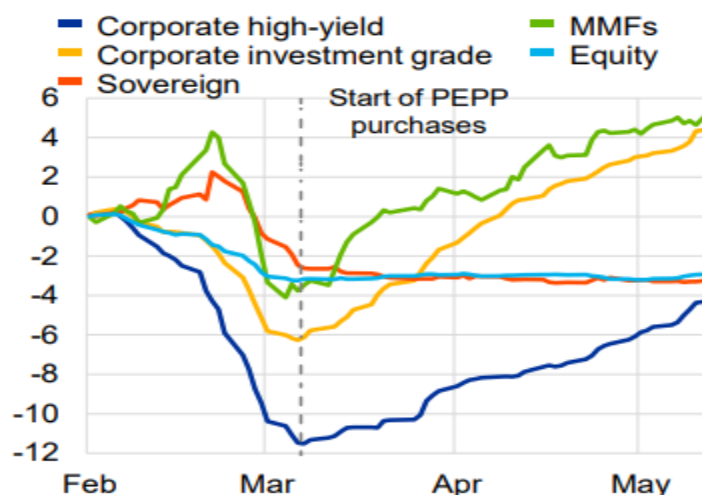
Similar conclusions have also been found in the euro area. ECB Executive Board member Isabel Schnabel highlighted, in particular, how regulation introduced in the NBFIs sector may not have fully reflected their increased role in euro area financial markets, giving rise to potential regulatory gaps. Further, Isabel Schnabel noted how NBFIs acted as amplifiers of market stress at this time, with a number of factors cited, including the increasing liquidity risk onboarded by NBFIs in recent years (the increased leverage assumed, in particular, by IFs with volatility-targeting investment strategies) and the marginalising requirements which increased liquidity requirements, thereby resulting in a spiral of forced selling (a so-called asset-price spiral). As such, encouragement is given to an amendment in the regulatory landscape that would result in NBFIs' regulation better reflecting the increased level of credit intermediation taking place outside the banking sector.

In order to counter the wide-spread financial shock and deterioration in financing conditions observed across the euro area in early 2020, the ECB took a number of decisive steps. This included the reactivation of swap lines with other central banks; a recalibration of the TLTRO III in order to increase borrowing incentives; a temporary easing of collateral requirements; and an expansion of asset purchases. In the latter case, this included both an expansion of the APP, which was extended by EUR 120 billion in 2020, and through the introduction of the PEPP, which ultimately reached an envelope of EUR 1,850 billion in March 2022. The PEPP in particular, as depicted in [Chart 5](#), was instrumental in reviving the commercial paper market and alleviating funding stress of corporations caused by fragility in MMFs.

**Chart 5**

Cumulative flows in euro area-domiciled funds

(percentages of assets under management)



Source: EPFR. Notes: Taken from speech by Executive Board member Schnabel, "COVID-19 and the liquidity crisis of non-banks: lessons for the future", November 2020.

Therefore, the key remaining question is the extent to which the direct provision of central bank liquidity could have complemented or substituted these monetary policy tools. Notably, in response to the bout of market volatility during the pandemic crisis, a number of major central banks took the step to provide direct liquidity to NBFIs. For example, the Bank of Canada introduced the Contingent Term Repo Facility (CTRF).<sup>51</sup> This was a liquidity providing operation offering Canadian dollar funding for one-month to eligible counterparties on a standing, bilateral basis against securities issued or guaranteed by the Government of Canada or a provincial government. In terms of NBFi access, both pension funds and insurance companies were able to partake in this operation.

### 3.3 Operational considerations

Beyond simply identifying a motivation behind the provision of NBFi balance sheet access, significant consideration would have to be given to the operational and financial aspects that such a decision would entail. The extension of liquidity to this sector would, of course, potentially expose the Eurosystem to the counterparty default risk of such institutions. In order to limit this potential credit risk, eligible monetary policy counterparties are required to meet a minimum set of criteria which are subject to ongoing review.

In this regard, access to Eurosystem monetary policy operations is permissible on the condition that the entity, in this case an eligible Eurosystem counterparty, meets all eligibility criteria, including the Eurosystem's concept of "financial soundness".

<sup>51</sup> Available at: <https://www.bankofcanada.ca/markets/market-operations-liquidity-provision/market-operations-program-s-and-facilities/contingent-term-repo-facility/>

Financial soundness refers, at a minimum, to the fulfilment of the (regulatory) “Pillar 1” own funds requirements. This includes risk-weighted capital ratios at all levels of capital, as well as the Leverage Ratio. Further, entities which are determined as failing or likely to fail (FOLTF) by the relevant supervisory or resolution authority are automatically limited in their access to Eurosystem monetary policy operations, and the ECB Governing Council may suspend, limit, or exclude an entity’s access to Eurosystem monetary policy operations based on any other information that raises substantial concerns about the counterparty’s financial soundness.

Therefore, before any provision of liquidity could be considered, a similar definition would have to be established for NBFIs. Notably, this definition should also allow for ongoing monitoring in this regard, in order to identify whether established thresholds/risk metrics have been breached by entities, in order to allow for similar FOLTF or financial soundness concerns, as detailed above.

Beyond this, holdings of ECB eligible collateral are unevenly distributed among NBFIs, meaning access to any potential lending facility would likely be practically available for some NBFIs only.

Finally, for instance the MMF Regulation contains provisions prohibiting the external support provided by third parties to MMFs, with potential similar restrictions existing in the various NBFi sectors. As such, significant operational, financial and legal considerations would need to be assessed before considering any asset side access to the balance sheet.

## 4 Liability side of the balance sheet

The opening-up of the liability side of the balance sheet to NBFIs would allow for non-banks to place deposits with the Eurosystem. As discussed in Section 2, the increase in liquidity intermediated in the euro area financial system has led to transactions between banks (with direct balance sheet access) and non-banks (with no direct balance sheet access) having become the dominant trade within unsecured money markets. As such, in an environment of very high excess liquidity where the intermediation capacity of banks is constrained, it is worth outlining considerations relative to the potential provision of such liability side access to non-banks.

### 4.1 Potential avenues for granting liability side access

Three main avenues could be considered: a standard deposit facility (akin to that available for existing monetary policy counterparties), a reverse repurchase facility (whereby collateral is provided back to the NBFi in exchange for the deposit), and the issuance of ECB debt certificates.

Some foreign central banks have taken the step to provide and operationalise these types of tools, with prominent examples being the Federal Reserve Bank of New

York's overnight reverse repo facility and the issuance of central bank bills or certificates by the Swiss National Bank and the Swedish Riksbank.

In the case of the Eurosystem, the specific decentralised multi-jurisdiction set up in which it operates requires a careful assessment of the operational and legal considerations around the possible use of these tools for the purpose of draining liquidity directly from NBFIs.

## 4.2 Potential motivation for opening up the liability side of the balance sheet

A motivation for providing liability side access to NBFIs could be to ensure that the Eurosystem retains control over short-term unsecured money market rates, which are the starting point for monetary policy transmission.

As such, the provision of liability side access could be seen as a manner of guaranteeing that a hard floor would be placed on euro area unsecured money market rates, and more specifically on €STR, which is the primary short-term (overnight) interest rate in the euro area.

In terms of pricing, [Chart 6](#) depicts the evolution of €STR alongside the ECB key interest rate from 2015 to 2022. Here, it is evident that €STR has traded below the Deposit Facility Rate for some time. Historically, while the Eurosystem operated in a liquidity deficit environment, money market rates in the euro area had typically traded in the centre of the interest rate corridor. However, more recently, money market rates have traded at a negative spread to the Deposit Facility Rate largely driven by transactions between existing monetary policy counterparties and non-banks.

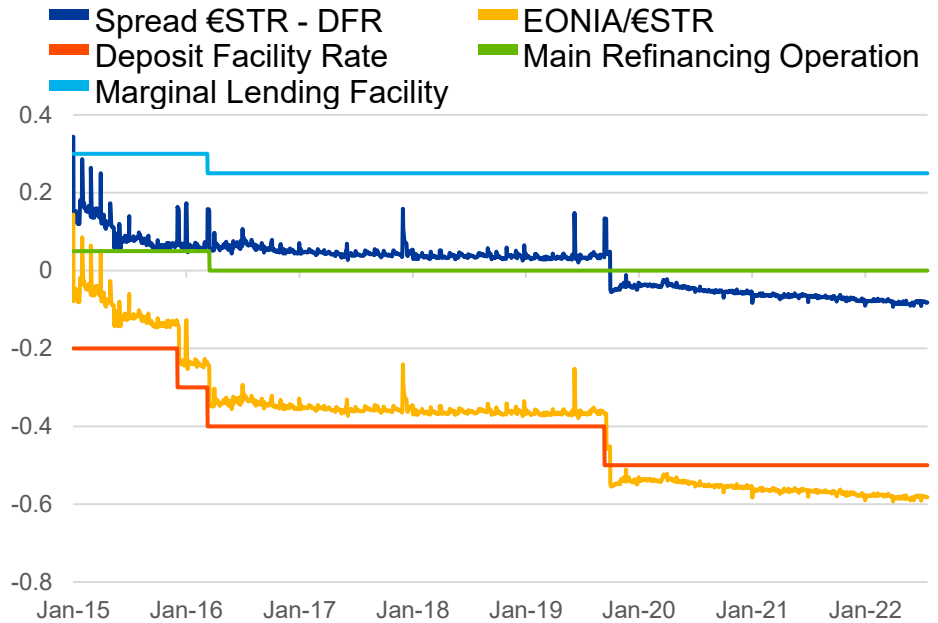
While this pricing is largely driven by the level of excess liquidity in the financial system, pricing in unsecured money market rates is also affected by other factors, including the differentiated access to Eurosystem monetary policy facilities available to different market participants. While existing Eurosystem counterparties can also park their funds with the ECB in the Deposit Facility (at the Deposit Facility Rate), non-banks need this service to be fulfilled by banks and the market. Therefore, and given that bank's balance sheets have been somewhat constrained by the growing liquidity they now hold, we can see that the rates counterparties offer to these non-banks are below the deposit DFR.



### Chart 6

ECB key interest rates and €STR (start-2015 to 21 July 2022)

(Percentage)



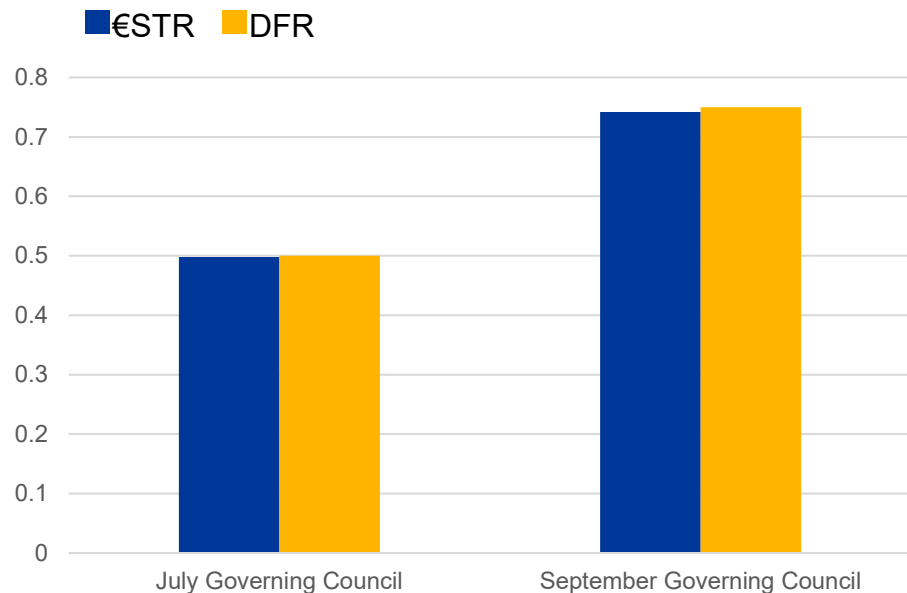
Source: Bloomberg

That said, **Chart 7** depicts the one-week change in €STR and the Deposit Facility Rate after the July and September 2022 monetary policy meetings of the Governing Council. Notably, the Governing Council delivered a 0.50 % increase in rates at the 21 July 2022 monetary policy meeting, and a 0.75 % increase in rates at the 8 September 2022 monetary policy meeting. Over this period, a smooth and immediate pass-through of these rate hikes has been observed. In both instances, the increase in €STR almost fully reflected both interest rate hikes. As such, it could be said that the negative spread is responsive to interest rate changes and is therefore controllable. However, the pass through of interest rate hikes to secured money market rates (repo) has been bumpier, and at times incomplete, which may create yet unexplored challenges to the transmission of monetary policy.

**Chart 7**

ECB key interest rates and €STR (21 July 2022 to 5 October 2022)

(Percentage)



Source: Bloomberg

## 5 Concluding remarks

In recent years, a variety of factors have led NBFIs to become the most active players in money markets, including a reduced demand for interbank liquidity among existing credit institutions and the general increase in size of the NBFIs sector. There is nothing to suggest that the recently observed continual growth in NBFIs will abate going forward, meaning that their importance in the transmission of monetary policy may only increase in time. Furthermore, during COVID-19 disruptions in March-April 2020, the behaviour of some NBFIs resulted in the amplification of risk-off moves, rather than acting as risk absorbers.

Conceptually at least, the provision of asset side access could be a way of directly providing liquidity to NBFIs in times of stress, which may in turn reduce tail risks associated with self-fulfilling adverse dynamics. Meanwhile, on the liability side of the balance sheet, the ability of NBFIs to place deposits with the central bank could provide an explicit floor to money market rates thereby strengthening their controllability.

However, there are many open financial, operational and legal questions over the feasibility and the best manner in which to expand access of Eurosystem monetary policy operations to NBFIs.

Therefore, it is prudent to continue to explore questions related to the potential provision of access to monetary policy operations both now and going forward, while

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recognising that the Eurosystem has so far effectively ensured a smooth transmission of its monetary policy impulses to unsecured rates under the current status quo.

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# Money market funds as counterparties of monetary policy operations – legal aspects

By Kerstin Schaepersmann\*

## 1 Introduction

Non-bank financial intermediation has risen significantly over the past decades. While credit intermediation by entities outside the traditional banking sector, also referred to as shadow banking, can support the economy by providing an alternative source of credit, enhancing market liquidity, maturity transformation and risk sharing,<sup>52</sup> it also poses different challenges.

On the one hand, challenges arise from the perspective of supervision of shadow banking to address risk of regulatory arbitrage, resulting in various regulatory changes since the publication of a report on shadow banking by the Financial Stability Board in 2011<sup>53</sup> and the EU Commission's Green Paper<sup>54</sup> in 2012 and subsequent communication in September 2013<sup>55</sup>, setting out its roadmap to limit the emergence of risks in the shadow banking sector. These include, in addition to enhanced transparency in derivatives and securities financing transactions, stricter requirements imposed on banks in their dealings with the shadow banking system, as evidenced by the introduction of a harmonised framework for alternative investment fund managers, and the adoption of more stringent rules for the investment by banks in securitisations.

On the other hand, the increase in non-bank finance has created new risks for monetary policy. In a downturn, as a result of the substantial liquidity and credit risks on the balance sheets of non-banks, their capacity to absorb losses can be affected, which in turn can result in systemic risks and an impairment of monetary policy transmission mechanisms of central banks, including the Eurosystem.

Traditionally, central bank funding under the monetary policy framework is directly provided only to credit institutions, which then intermediate the liquidity received to non-bank market participants. Already at the time of the global financial crisis, but also more recently in light of the impact that the COVID-19 pandemic had on the financial

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<sup>52</sup> See for example EBA Guidelines - Limits on exposures to shadow banking entities which carry out banking activities outside a regulated framework under Article 395(2) of Regulation (EU) No 575/2013 (EBA/GL/2015/20).

<sup>53</sup> Financial Stability Board, Shadow Banking: Strengthening Oversight and Regulation of 27 October 2011.

<sup>54</sup> European Commission, Green Paper Shadow Banking of 19 March 2012 (COM(2012) 102 final).

<sup>55</sup> European Commission, Communication from the Commission and the European Parliament, Shadow Banking – Addressing New Sources of Risk in the Financial Sector of 4 September 2013 (COM(2013) 614 final).

markets, it has become apparent that, in times of stress, this intermediation may be interrupted,<sup>56</sup> which may have implications for the market participants relying on such intermediation and on the functioning of the financial markets more generally.

Amongst the non-banks which have been particularly affected by, and showed vulnerabilities as a result of, events such as the global financial crisis and the market disruptions as a result of the COVID-19 pandemic, and which have been the focus of numerous studies and analyses<sup>57</sup> as regards their influence on the stability of the financial system, are money market funds (MMFs). As an alternative to bank deposits, because they offer diversification of investments, instantaneous liquidity and relative stability of value, they are closely linked to the banking sector and are an important source of corporate and government financing. As a result, runs on funds (i.e. high level of redemptions by investors in MMFs) combined with a lack of liquidity in private money markets in a financial crisis may have consequences not only on the functioning of the money markets, but also in the worst case on the real economy.

The aim of this paper is to examine certain legal aspects of the question whether access of non-banks in the form of MMFs to central bank funding in order to address a monetary policy objective could be part of the ECB's toolbox. The answer to this question needs to be looked at from two perspectives: (i) from the perspective of the rules governing the function and objectives of the ECB, namely the Treaty on the Functioning of the European Union (TFEU) and the Statute of the European System of Central Banks and of the European Central Bank (Statute of the ESCB) and the guidelines and decisions made on that basis (including the General Documentation Guideline<sup>58</sup>) and (ii) from the perspective of the rules and regulations governing the operation of MMFs.

This paper briefly puts into context the monetary policy measures currently available to the ESCB and then looks at a number of specific aspects of the MMF Regulation which need to be considered when assessing whether MMFs would be able to benefit from central bank funding on that basis.

## 2 Overview of the ECB's toolbox

From a monetary policy perspective, the primary objective of the Eurosystem is to maintain price stability.<sup>59</sup> The Eurosystem, which consists of the ECB and the National Central Banks (NCBs) of the countries which have adopted the euro, defines

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<sup>56</sup> Financial Stability Board (2020), Global Monitoring Report on Non-Bank Financial Intermediation 2020, p. 71.

<sup>57</sup> In the wake of the financial crisis, the European Systemic Risk Board (ESRB) published a study entitled "Money Market Funds in Europe and Financial Stability" (Occasional Paper No. 1, June 2012) and, more recently, the "Issues note on systemic vulnerabilities of and preliminary policy considerations to reform money market funds (MMFs)" of July 2021. The impact of the COVID-19 pandemic on MMFs and money markets is also addressed in the ECB's Occasional Paper Series No 270 as of September 2021 (Revised December 2021) "Non-bank financial intermediation in the euro area: implications for monetary policy transmission and key vulnerabilities".

<sup>58</sup> Guideline (EU) 2015/510 of the European Central Bank of 19 December 2014 on the implementation of the Eurosystem monetary policy framework (General Documentation Guideline) (ECB/2014/60) (OJ L 91, 2.4.2015, p. 3).

<sup>59</sup> Article 127(1) TFEU.

and implements monetary policy for the euro area according to this objective and in line with the mandate of the ECB.

The Eurosystem currently uses a range of instruments and procedures under its monetary policy framework through which it steers the short-term interest, being the operational target of the monetary policy.<sup>60</sup> As set out above, central bank funding under the monetary policy framework is traditionally directly provided only to credit institutions. In order to ensure equal treatment across the euro area, the current monetary policy framework allows for the participation of all euro area credit institutions as defined in the Capital Requirements Regulation (CRR),<sup>61</sup> i.e. institutions which take deposits or other repayable funds from the public and to grant credits for its own account, under uniform eligibility criteria specified by the Eurosystem. Under the General Documentation Guideline, credit institutions as eligible counterparties may access the Eurosystem's standing facilities and participate in Eurosystem open market operations. Pursuant to Article 18.1 of the Statute of the ESCB, all Eurosystem credit operations are conducted against eligible collateral aimed at protecting the Eurosystem against financial losses. Collateral may be in the form of marketable debt instruments and non-marketable assets specified in the General Documentation Guideline.

As part of a package of non-standard monetary policy measures, the ECB's asset purchase programme (APP) was initiated in mid-2014 to support the monetary policy transmission mechanism and provide the amount of policy accommodation needed to ensure price stability.<sup>62</sup> Under the APP, net purchases were conducted of a variety of assets, including bonds issued by central, regional and local governments, bonds issued by non-banks located in the euro area, eligible asset-backed securities (ABS) and eligible covered bonds issued by euro area credit institutions to help in achieving an inflation rate of 2 % over the medium term.

As a reaction to the COVID-19 pandemic, separate from and in addition to the net purchases under the APP, the ECB Governing Council introduced the pandemic emergency purchase programme (PEPP)<sup>63</sup> in March 2020 to counter serious risks to the monetary policy transmission mechanism and the outlook for the euro area. The terms of the PEPP allow for the outright purchase by the Eurosystem central banks of

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<sup>60</sup> See "The Eurosystem's instruments", available at [www.ecb.europa.eu/mopo/implement/html/index.en.html](http://www.ecb.europa.eu/mopo/implement/html/index.en.html)

<sup>61</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 amending Regulation (EU) No 648/2012 (OJ L 176, 27.6.2013, p. 1).

<sup>62</sup> See "Asset purchase programmes", available at [www.ecb.europa.eu/mopo/implement/app/html/index.en.html](http://www.ecb.europa.eu/mopo/implement/app/html/index.en.html) and the related decisions: (i) Decision (EU) 2020/188 of the European Central Bank of 3 February 2020 on a secondary markets public sector asset purchase programme (ECB/2020/9) (OJ L 39, 12.2.2020, p. 12), recasting Decision (EU) 2015/774 of the European Central Bank of 4 March 2015 on a secondary markets public sector asset purchase programme (ECB/2015/10) (OJ L 121 14.5.2015, p. 20), (ii) Decision (EU) 2016/948 of the European Central Bank of 1 June 2016 on the implementation of the corporate sector purchase programme (ECB/2016/16) (OJ L 157 15.6.2016, p. 28), (iii) Decision (EU) 2015/5 of the European Central Bank of 19 November 2014 on the implementation of the asset-backed securities purchase programme (ECB/2014/45) (OJ L 1, 6.1.2015, p. 4), and (iv) Decision (EU) 2020/187 of the European Central Bank of 3 February 2020 on the implementation of the third covered bond purchase programme (ECB/2020/8) (OJ L 39, 12.2.2020, p. 6), recasting Decision ECB/2014/40 of 15 October 2014 on the implementation of the third covered bond purchase programme (OJ L 335, 22.11.2014, p. 22).

<sup>63</sup> Decision (EU) 2020/440 of the European Central Bank of 24 March 2020 on a temporary pandemic emergency purchase programme (ECB/2020/17) (OJ L 091 25.3.2020, p. 1).

a range of eligible debt securities in the form of, inter alia, corporate bonds, covered bonds and ABS to the extent deemed necessary and proportionate to counter the threats posed by the extraordinary economic and market conditions on the ability of the Eurosystem to fulfil its mandate.

While the PEPP and the APP are not available to non-banks, the PEPP in particular helped ease liquidity tensions caused by the market turmoil as a result of the pandemic by primarily supporting the issuance of corporate CPs on the primary market from end of March 2020, which ultimately positively affected MMF net asset values.<sup>64</sup>

As set out above, whether, on the basis of the current legal framework, MMFs in the euro area may also be able to benefit from central bank support more directly is the focus of this paper.

### 3 Characteristics of MMFs

Before commenting on potential legal obstacles that require assessment in the context of the provision of central bank funding to MMFs in the euro area, it is worth giving a brief overview of the functions and types of MMFs under European law.

#### 3.1 European framework: MMF Regulation

The legal basis for the activities of MMFs in the European Union is laid down in the MMF Regulation<sup>65</sup>. According to the MMF Regulation, MMFs provide short-term financing for financial institutions, corporations and governments, which use their investments in MMFs as an efficient way to spread their credit risk and exposure, rather than relying solely on bank deposits. As a result, MMFs contribute to the financing of the economy of the EU.<sup>66</sup> The MMF Regulation came into effect in 2018 and was introduced as a result of "lessons learned" to make MMFs more stable and less vulnerable to runs, as was experienced during the financial crisis, during which MMFs faced massive redemption requests by investors, resulting in the generation of systemic risks.<sup>67</sup>

An MMF cannot be established, marketed or managed in the EU unless it has been authorised under the MMF Regulation and is a collective investment undertaking (fund) that (i) is authorised or requires authorisation as an undertaking for collective

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<sup>64</sup> See the Board of the International Organization of Securities Commissions (IOSCO) Thematic Note entitled "Money Market Funds during the March-April Episode" of November 2020 (OR03/2020) for a global overview.

<sup>65</sup> Regulation (EU) 2017/1131 of the European Parliament and of the Council of 14 June 2017 on money market funds (OJ L 169, 30.6.2017, p. 8).

<sup>66</sup> Recital 1 MMF Regulation.

<sup>67</sup> See Balz, K. (2008), "Money Market Funds: ESMA specifies requirements of EU Regulation", available at [www.bafin.de/SharedDocs/Veroeffentlichungen/EN/Fachartikel/2017/fa\\_bj\\_1712\\_Geldmarktfonds\\_en.html](http://www.bafin.de/SharedDocs/Veroeffentlichungen/EN/Fachartikel/2017/fa_bj_1712_Geldmarktfonds_en.html)

investment in transferable securities (UCITS) under the UCITS Directive<sup>68</sup> or is an alternative investment fund (AIF) under the Alternative Investment Fund Managers Directive (AIFMD);<sup>69</sup> (ii) invests in short-term assets; and (iii) has distinct or cumulative objectives offering returns in line with money market rates or preserving the value of the investment. As regards the legal form of MMFs, the UCITS Directive and the AIFMD both provide that the fund may be constituted in accordance with contract law (as a common fund managed by a management company), trust law (as a unit trust), or statute (as an investment company). The actual legal form of a UCITS or an AIF depends on the applicable national law under which it is established. The MMF Regulation specifies however that, where an MMF comprises more than one investment compartment, each compartment is regarded as a separate MMF for the purposes of, inter alia, the activities analysed in this paper.<sup>70</sup>

The MMF Regulation sets out rules for the operation of MMFs, in particular on the composition of the portfolio of MMFs, which may only invest in pre-defined eligible assets, namely money market instruments, asset-backed commercial paper, deposits with credit institutions, financial derivative instruments, repos and reverse repos fulfilling certain criteria and units or shares of other MMFs. In each case, these investments are subject to strict diversification requirements and concentration limits, aimed at ensuring the low risk and high quality of the relevant assets. An MMF must be set up as one of three distinct types: (i) Variable Net Asset Value MMFs (VNAV MMFs), whose value fluctuates with the value of their assets, (ii) public debt Constant Net Asset Value MMFs (CNAV MMFs), that must invest 99.5 % of assets in government debt instruments, reverse repos collateralised with government debt and cash and (iii) Low Volatility Net Asset Value MMFs (LVNAV MMFs), which can invest in a broader range of instruments, and, in particular at the start of the COVID-19 pandemic experienced substantial outflows. All MMFs can be short-term MMFs (with a maximum legal or residual maturity of their investments at 397 days), but only VNAV MMFs can be standard MMFs (which may also invest in money market instruments with a maximum legal or residual maturity of two years).

The MMF Regulation requires that an MMF establishes a prudent internal credit quality assessment procedure for determining the credit quality of its investments, which must be documented, as well as sound and prudent know-your-customer procedures. MMFs are also subject to maturity limitations in the form of a maximum allowable weighted average maturity (WAM) and weighted average life (WAL). They are also required to hold on an ongoing basis a minimum amount of liquid assets that mature daily or weekly in order to strengthen their ability to face redemptions and prevent their assets from being liquidated at heavily discounted prices. MMFs must also conduct stress testing at regular intervals as part of prudent risk management. Competent authorities have supervisory and investigatory powers to verify compliance with the MMF Regulation.

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<sup>68</sup> Directive 2009/65/EC of the European Parliament and of the Council of 13 July 2009 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS) (OJ L 302, 17.11.2009, p. 32).

<sup>69</sup> Directive 2011/61/EU of the European Parliament and of the Council of 8 June 2011 on Alternative Investment Fund Managers and amending Directives 2003/41/EC and 2009/65/EC and Regulations (EC) No 1060/2009 and (EU) No 1095/2010 (OJ L 174, 1.7.2011, p. 1).

<sup>70</sup> Article 8 MMF Regulation.



The respective manager of an MMF, which is, in the case of an MMF that is a UCITS, the UCITS management company, or the UCITS investment company in the case of a self-managed UCITS, and, in the case of an MMF that is an AIF, an AIFM or an internally managed AIF, is responsible for ensuring compliance by the MMF with the MMF Regulation.

## 3.2 Review of the MMF Regulation

The MMF Regulation is currently subject to review, on the basis of the European Securities and Markets Authority (ESMA) consultation report (MMF Regulation Consultation Report)<sup>71</sup> in March 2021 as well as ESMA's final report (MMF Regulation Final Report) in February 2022,<sup>72</sup> containing in particular policy proposals that the ESMA suggests putting forward in order to address the difficulties faced by MMFs in March 2020. In particular LVNAV MMFs in US dollars and some VNAV MMFs in euro were faced with large redemptions, as both were exposed to money market instruments issued by financial institutions and in particular commercial paper and certificates of deposit which suffered the greatest deterioration in liquidity during March 2020.<sup>73</sup> Although no EU MMF suspended redemptions or used liquidity fees on redemptions or redemptions gates as a result of the crisis, ESMA notes that the recommendations outlined within the MMF Regulation Final Report considers the lessons learnt during the COVID-19 crisis.

From a different perspective, it is worth noting that the European Banking Authority's (EBA) final report on criteria for the identification of shadow banking entities under the CRR<sup>74</sup> sets out draft regulatory standards as to which entities are considered shadow banking entities for the purposes of the reporting by credit institutions of their 10 largest exposures to shadow banking entities which carry out banking activities outside the regulated framework on a consolidated basis. In the report, the EBA notes on the one hand that, as a result of the MMF Regulation, MMFs are subject to specific authorisation procedures by competent authorities, and can invest only in certain activities, subject to regulatory requirements, including in terms of liquidity, concentration and diversification, as well as risk management requirements, and to a set of rules of maximum harmonisation that, in certain cases, are more stringent than those applied to UCITS or AIFs, which makes the framework under which MMFs operate more robust and safe. On the other hand, the EBA states that, in view of the ongoing review of the MMF Regulation to tackle the vulnerabilities shown by MMFs during the COVID-19 crisis and the ensuing workstreams on international and EU level to assess the situation and to identify policy options with the objective to enhance MMF resilience, it is appropriate to consider MMFs as shadow banking entities until such reforms are in place before reassessing the current policy stance.

<sup>71</sup> Consultation Report "EU Money Market Fund Regulation – legislative review" of 26 March 2021 (ESMA34-49-309).

<sup>72</sup> Final Report - ESMA opinion on the review of the Money Market Fund Regulation of 14 February 2022 (ESMA34-49-473).

<sup>73</sup> *ibid.*, p. 11. See also ESMA Report on Trends, Risks and Vulnerabilities No 1, 2021, p. 64.

<sup>74</sup> EBA, Final report - Draft Regulatory Technical Standards on criteria for the identification of shadow banking entities under Article 394(4) of Regulation (EU) No 575/2013 (EBA/RTS/2022/06) of 23 May 2022.

## 4 MMFs as eligible counterparties of ECB monetary policy instruments

As set out above, the first question that must be addressed in order to assess whether central bank funding may be made available to MMFs is whether this would be possible from the perspective of the rules governing the function and objectives of the Eurosystem.

### 4.1 Rules and regulations of the Eurosystem

As mentioned, traditionally, central bank funding under the monetary policy framework is directly provided only to credit institutions, which then intermediate the liquidity received to non-bank market participants.

Article 18.1 of the Statute of the ESCB provides that: "In order to achieve the objectives of the ESCB and to carry out its tasks, the ECB and the national central banks may: .... conduct credit operations with credit institutions and other market participants...", and hence, does not per se restrict the potential counterparties of credit operations to credit institutions.

The General Documentation Guideline reiterates the above principle by referring to "credit institutions and other market participants" in recital 7 and recital 17 is worded in a generic manner stating that "the implementation of the Eurosystem's monetary policy framework should ensure that a broad range of counterparties participate under uniform eligibility criteria" and that it needs to be ensured that "counterparties fulfil certain prudential and operational requirements". However, according to Article 55 of the General Documentation Guideline, the Eurosystem shall only allow participation by credit institutions as Eurosystem monetary policy counterparties if they (either the institution itself or a branch) are located in the euro area and they: (i) are subject to minimum reserve requirements; (ii) are subject to harmonised EU/EEA-supervision under Directive 2013/36/EU (CRD)<sup>75</sup> and the CRR or supervision under a comparable third country regime; (iii) are financially sound; and (iv) fulfil the operational requirements specified in the contractual or regulatory arrangements applied by the home NCB or the ECB with respect to the specific instrument or operation.

Minimum reserves to be held on accounts with the ECB and NCBs in pursuance of monetary objectives may, according to Article 19 of the Statute of the ESCB, be required from credit institutions but not from other parties, and only credit institutions are subject to supervision under CRD and CRR. While MMFs are subject to prudential supervision under the MMF Regulation (and under the UCITS Directive and AIFMD), it can therefore be concluded that under the current form of the General Documentation Guideline, direct participation by MMFs in the monetary operations set out thereunder would not be feasible.

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<sup>75</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, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC (OJ L 176, 27.6.2013, p. 338).

Taking into account the principles of Article 18.1 of the Statute of the ESCB, which does not limit potential counterparties of monetary operations to credit institutions, and the powers of the ECB under Article 18.2 of the Statute of the ESCB to establish general principles for open market and credit operations carried out by itself or the national central banks, including the announcement of conditions under which they stand ready to enter into such transactions, expanding the scope of eligible counterparties to non-banks is not per se excluded from a legal perspective.

Article 12.1 of the Statute of the ESCB authorises the ECB to formulate the single monetary policy of the EU and to issue the necessary guidelines to ensure its proper implementation. A bespoke set of guidelines addressing the specific nature of MMFs is therefore not prohibited if in line with the primary objective of the Eurosystem to maintain price stability.

## 4.2 Analysis of requirements under the MMF Regulation

The second question that needs to be addressed is whether the rules and regulations governing the operations of the MMF under the MMF Regulation contain any obstacles that would prevent the participation by an MMF in monetary policy operations, if monetary policy instruments in the form currently available to credit institutions were available to MMFs.

### 4.2.1 External support

Before looking at some individual aspects of eligible transactions that MMFs are allowed to undertake and how these could be reconciled with the requirements of the Eurosystem's monetary operations, a relevant aspect is an overarching principle of the MMF Regulation that could stand in the way of central bank funding of MMFs, namely the prohibition of external support.

The MMF Regulation stipulates a general prohibition of external support for MMFs. Article 35(2) MMF Regulation defines "external support" as "any direct or indirect support offered to an MMF by a third party, including a sponsor of the MMF that is intended for or in effect would result in guaranteeing the liquidity of the MMF or stabilising the NAV per unit or share of the MMF". As set out in the preamble to the MMF Regulation, the reason for such a prohibition is that providing support to an MMF with a view to maintaining either liquidity or stability, or de facto having such effects, increases the contagion risk between the MMF sector and the rest of the financial sector.

While the reference to a "third party" could, on its face, include any person and as a result also the Eurosystem, it is worth looking at the historical context of when the MMF Regulation was enacted and the purpose of the prohibition. Both in the proposal for the MMF Regulation (MMF Regulation Proposal)<sup>76</sup> and in the impact assessment

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<sup>76</sup> Proposal for a Regulation of the European Parliament and of the Council on Money Market Funds dated 4 September 2013 (COM(2013) 615).

accompanying the MMF Regulation Proposal (Impact Assessment),<sup>77</sup> external support from third parties was discussed under the term "sponsor support". While the MMF Regulation does not provide a specific definition as to what constitutes a sponsor of an MMF, the Impact Assessment identifies two types of sponsors: an asset manager of an MMF and the financial institution which offers or originates an MMF. This line of thought is continued in the recitals of the MMF Regulation, stating that entities in same group as the MMF, who would provide support because they have an economic interest in the management company managing the MMF or for reputational reasons, do not always commit explicitly to provide or guarantee the support to maintain the liquidity and the stability of their MMFs. Accordingly, there is uncertainty whether such sponsor support will be granted when an MMF needs it most, which contributes to uncertainty among market participants about who will bear the losses of an MMF in such circumstances and makes MMFs more vulnerable to runs. This is also because sponsors may not be prepared to face such situations because the "implied" guarantee is not recorded as an explicit guarantee that would require the build-up of capital reserves.

It is obvious that the Eurosystem, when directly or indirectly undertaking monetary policy operations with MMFs would have the intention to maintain the liquidity and stability of MMFs. However, on the basis of the above it can be argued that the prohibition to provide external support does not intend to capture any third party but only such parties which, as a consequence of their close link to an MMF, either as an affiliated entity or due to being involved in the setting up of an MMF, have an interest in stabilising the relevant individual MMF (although the wording of Article 35 MMF Regulation is not limited to individual support).<sup>78</sup> On the other hand, it has been suggested in the MMF Regulation Consultation Report that the current provisions on external support require amendments in order to face challenges such as the COVID-19 crisis.<sup>79</sup> Among the options discussed was central bank liquidity provision to MMFs.<sup>80</sup> From that it could be concluded that the current framework does not seem to be sufficient to allow central banks to provide liquidity directly to MMFs.

However, in light of the recitals of the MMF Regulation and the statements in the Impact Assessment outlined above, it appears reasonable to attribute the term "sponsor" to someone who generally has an individual economic or reputational interest in a particular MMF, giving such an MMF a priority treatment. The Eurosystem generally does not have such interests as it is guided by monetary policy and systemic stability and under its framework treats all eligible participants equally once their eligibility has been determined. Further, the purpose of Article 35 MMF Regulation,

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<sup>77</sup> Commission Staff Working Document Impact Assessment accompanying the proposal for a Regulation of the European Parliament and of the Council on Money Market Funds of 4 September 2013 (SWD(2013) 315).

<sup>78</sup> It should also be noted that the MMF Regulation proposal contained a provision allowing external support to individual MMFs other than CNAV MMFs in exceptional circumstances, namely where the MMF justifies and evidences the urgent need for support, that the support is limited in terms of amount and the time when it is made available and that the competent authority is satisfied that the provider of the external support is financially sound and has sufficient financial resources to withstand possible losses resulting from the external support granted without any adverse effects. However, this proposal did not make it into the final text.

<sup>79</sup> See No 129 et seq. of the MMF Regulation Consultation Report.

<sup>80</sup> *ibid*, No 66.

which is to ensure the resilience of MMFs in times of stress, is aligned with ECB's role as guarantor of systemic stability.<sup>81</sup>

Looking more closely at what "external support" effectively means, examples as stated in the non-exhaustive list set out in the MMF Regulation are cash injections from a third party, the purchase by a third party of assets of the MMF at an inflated price, the purchase by a third party of units or shares of the MMF in order to provide liquidity to the fund, the issuance by a third party of any kind of explicit or implicit guarantee, warranty or letter of support for the benefit of the MMF, or any action by a third party the direct or indirect objective of which is to maintain the liquidity profile and the NAV per unit or share of the MMF.

From these examples, it can be concluded that the term "support" implies a "non-market" element, e.g. that the transaction is entered into at off-market prices or terms, for reasons of a specific economic interest in the specific fund due to a close sponsor-like relationship rather than as a function or reflex of ensuring systemic stability as would be the case with the Eurosystem. Accordingly, if the Eurosystem enters into a transaction with the MMF which is in line with the standard market conditions that are available to all eligible counterparties participating in the relevant open market operations, it could be argued that this should generally not qualify as support within the meaning of Article 35 MMF Regulation.

This is supported by a public statement by ESMA made in July 2020 in the context of the COVID-19 pandemic in relation to the prohibition of providing external support to MMFs to promote coordinated action by the national competent authorities in response to these adverse events and to provide clarity to managers of MMFs.<sup>82</sup> At the time, measures of central banks, such as the purchase of corporate CPs, intermediated by credit institutions, indirectly also benefitted MMFs. ESMA clarified that MMFs may enter into transactions with third parties, including affiliated or related parties provided the requirements of Article 35 MMF Regulation are met. ESMA further stated that, for the purpose of examining whether a third party provides external support by purchasing assets of the MMF at an inflated price, transactions are not considered as external support "where they are executed at arm's length conditions". The Final Report of February 2022 does not lead to a different conclusion on the basis that ESMA does not suggest amending the contents of Article 35 MMF Regulation on the ban of external support, but only suggests adding in the clarifications contained in the ESMA public statement referred to above.

Accordingly, as long as monetary policy transactions by the Eurosystem are conducted via a standard tender procedure by entering into transactions by accepting bids submitted by counterparties after a public announcement<sup>83</sup> and hence on a

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<sup>81</sup> In its response to the MMF Regulation Consultation Report of 30 June 2021 (ESMA22-106-3439), the Securities and Markets Stakeholder Group agreed that a central bank intervention in its own market, such as the ECB's PEPP, should in no case be interpreted as an external support to MMFs, as central banks conduct monetary policy to achieve price stability (low and stable inflation) and help manage economic fluctuations.

<sup>82</sup> ESMA Public Statement - Actions to mitigate the impact of COVID-19 on the EU financial markets – External support within the meaning of Article 35 of the MMF Regulation of 9 July 2020 (ESMA34-39-1096).

<sup>83</sup> Article 2, point (92) and Article 4 General Documentation Guideline.

competitive basis to all eligible participants, such monetary policy transactions should not qualify as external support within the meaning of the MMF Regulation.

#### 4.2.2 Prohibited activities

As set out above, MMFs are subject to detailed rules to be observed when undertaking their operations, and certain activities are expressly restricted under the MMF Regulation. In addition to the prohibition of the investment in assets other than those which are expressly classified as eligible, the following activities are expressly prohibited: (i) the short sale of money market instruments, securitisations, ABCPs and units or shares of other MMFs, (ii) taking direct or indirect exposure to equity or commodities, (iii) entering into securities lending agreements or securities borrowing agreements, or any other agreement that would encumber the assets of the MMF and (iv) engaging in the borrowing and lending of cash.<sup>84</sup>

As a result, borrowing in the form of a loan under a facility in the form of a marginal lending facility under which participants can obtain overnight liquidity from the Eurosystem would not be possible for an MMF. As regards main refinancing operations (MROs), being a category of regular open market operations for providing liquidity to the banking system which under the current framework are the most important open market operations for the Eurosystem and are executed in a decentralised manner by the NCBs based on standard tenders, a differentiation must be made. MROs that are executed as a collateralised loan would be prohibited. Whether MROs as reverse transactions in the form of a repurchase agreement may be permissible under the framework of the MMF Regulation is analysed in the following section.

#### 4.2.3 Repurchase agreements

MMFs are permitted to conclude repurchase agreements to the extent that they fulfil the conditions specified in the MMF Regulation.<sup>85</sup> A "repurchase agreement" within the meaning of the MMF Regulation means any agreement in which one party transfers securities or any rights related to that title to a counterparty, subject to a commitment to repurchase them at a specified price on a future date specified or to be specified.

MROs are executed in the form of reverse transactions, which in turn are specific instruments to conduct open market operations, whereby an NCB buys or sells eligible assets under a repurchase agreement or conducts credit operations in the form of collateralised loans depending on the relevant contractual or regulatory arrangements applied by the NCBs.<sup>86</sup> The General Documentation Guideline specifies a repurchase agreement to be an arrangement whereby an eligible asset is sold to a buyer without any retention of ownership on the part of the seller, while the seller simultaneously

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<sup>84</sup> Article 9(2) MMF Regulation.

<sup>85</sup> Article 9(1), point (e) and Article 14 MMF Regulation.

<sup>86</sup> Article 2, point (80) General Documentation Guideline.

obtains the right and the obligation to repurchase an equivalent asset at a specific price on a future date or on demand, and hence is substantially aligned with the definition of a repurchase agreement under the MMF Regulation.

On the basis that the standard MROs are usually reverse repurchase transactions from the perspective of the Eurosystem (i.e. the Eurosystem receives securities and thereby provides liquidity to the market participants), the transaction constitutes a repurchase transaction from the perspective of the counterparty. In order to answer the question whether an MMF could enter into standard MRO transactions with the Eurosystem, it therefore needs to be analysed whether such MROs could be set up so that it would fulfil the eligibility criteria applicable to a repurchase agreement under the MMF Regulation.

A repurchase agreement in respect of securities that an MMF may conclude under the MMF Regulation must meet all of the following conditions:<sup>87</sup>

- The repurchase transaction must be used on a temporary basis, for no more than 7 working days, only for liquidity management purposes and not for investment purposes.<sup>88</sup> This timeframe corresponds in principle with Article 6(2) of the General Documentation Guideline, pursuant to which MROs are liquidity-providing operations, which normally have a maturity of one week.
- The counterparty receiving assets transferred by the MMF as collateral under the repurchase agreement is prohibited from selling, investing, pledging or otherwise transferring those assets without the MMF's prior consent. While the General Documentation Guideline does not expressly provide that prior consent by the counterparty of the Eurosystem under the MRO in the form of a reverse repo must be provided, it also does not appear to preclude that such a requirement could be agreed in the further contractual or regulatory arrangements to be concluded for the purposes of the agreement on the monetary policy operation (as provided by Article 1(3) and Article 180 of the General Documentation Guideline). Accordingly, an agreement on a requirement for the MMF to give its prior consent for dealing with any securities provided under the repurchase agreement appears to be possible in principle.
- The cash received by the MMF as part of the repurchase agreement does not exceed 10 % of its assets. This requirement does not exclude MROs but must be complied with by the MMF Manager.
- The MMF has the right to terminate the agreement at any time upon giving prior notice of no more than 2 working days. The General Documentation Guideline does not specify any such right to terminate the agreement at any time (but conversely also does not per se prohibit such a right), so that this would be a

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<sup>87</sup> Article 14 MMF Regulation.

<sup>88</sup> Exemptions apply in respect of deposits in accordance with Article 50(1), point (f) UCITS Directive (i.e. deposits with credit institutions which are repayable on demand or have the right to be withdrawn and maturing in no more than 12 months with credit institutions in an EU member state or in a third country which prudential rules have been considered equivalent) or eligible reverse repos under Article 15(6) MMF Regulation.

question of whether the implementing documentation can, taking into account the overall purpose of the measure, accommodate such a termination right.

Therefore, whereas theoretically, MROs could be designed so that they could meet the requirements of Article 14 MMF Regulation, in practice bringing MROs in line with such requirements poses challenges beyond feasibility from a purely legal perspective.

#### 4.2.4 Deposits

Under the MMF Regulation, a deposit with a credit institution is eligible for investment by an MMF if: (i) it is repayable on demand or is able to be withdrawn at any time, (ii) it matures in no more than 12 months, and (iii) the credit institution has its registered office in a Member State (or, if in a third country, is subject to equivalent prudential rules).

To determine whether an MMF could participate in a monetary instrument in the form of a deposit facility to make overnight deposits with the Eurosystem for the absorption of excess liquidity, the decisive question is whether the Eurosystem could be considered a credit institution as that term is used in the MMF Regulation, i.e. a credit institution as defined in Article 4(1), point (1) CRR as an undertaking the business of which is to take deposits or other repayable funds from the public and to grant credits for its own account. There is no binding EU-wide definition of the relevant terms comprising the definition, which therefore continues to be subject to different interpretations in the Member States.<sup>89</sup> Considering the wording of the definition, it can be argued that "undertakings" and "business" may be understood widely within the general meaning of the terms, and hence as any kind of activity, rather than only referring to activities with a commercial purpose. Similarly, in relation to the element "from the public", while in some cases deposits from other credit institutions or even professional market participants are not considered to be received from the public, others take the view that deposits or other repayable funds are considered to be taken from the public when they are received from legal or natural persons other than the credit institution itself. On that basis, the ECB and the NCBs which under Article 17 of the Statute of the ESCB open accounts for credit institutions, public entities and other market participants and accept assets as collateral, could be considered to be taking funds from the public. In addition, the CRD contains an express exemption declaring the provisions of that directive inapplicable to central banks<sup>90</sup> – as does the First Banking Directive in 1977, which in its recitals states that "exceptions must be provided for in the case of certain credit institutions to which this Directive cannot apply" - which shows that the definition of a credit institution in Article 4(1), point (1) CRR is not in itself sufficient to exclude such entities, since otherwise such an exemption would not have been required. Further, restricting the possibility of MMFs

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<sup>89</sup> See Opinion of the European Banking Authority on elements of the definition of credit institution under Article 4(1), point 1, letter (a) of Regulation (EU) No 575/2013 and on aspects of the scope of the authorisation of 18 February 2020 (EBA/OP/2020/15).

<sup>90</sup> Article 2(5) CRD IV.



to invest deposits with credit institutions only can also be seen as a reflection of the fact that only such entities are allowed to accept deposits.

On the other hand, it could be argued that the Eurosystem including the ECB and the NCBs do not conduct a "business" within the meaning of Article 4(1), point (1) CRR but exercise a sovereign or public function. Further, the interpretation of legislative materials preceding the MMF Regulation, such as the Impact Assessment, reveals that the legislator has made an informed decision of not transforming MMFs into special purpose banks (although this was also largely due to the fact that this would have had wider reaching consequences than just direct access to Eurosystem facilities by MMFs).<sup>91</sup> Also the fact that in the past central banks have only supported money markets indirectly, e.g. through the APP and PEPP, might indicate that the current legal framework seems not to allow a direct interaction with MMFs.

Finally, as mentioned above, various research has been undertaken, including as part of the MMF Regulation Consultation Report, with the aim of avoiding interventions by central banks, rather than furthering them and that ESMA is still of the view that the main objective of the review of the MMF Regulation should be to make MMFs more resilient to stressed market conditions without the need of (implicit) central bank support and to reduce their contribution to the building up of risk in the financial system.<sup>92</sup>

Accordingly, while the wording of the MMF Regulation may allow for the Eurosystem to qualify as credit institution and, as a result, to take deposits from MMFs, this might be seen as contrary to the legislators' intention and against the goals of future legislation.

## 5 Conclusion

While the analysis that has been and is being undertaken for reforms of the money market and the review of the MMF Regulation focuses on policy options that would address vulnerabilities within MMFs themselves and that are, inter alia, designed to ensuring the resilience and functioning of MMFs without the need for central banks to step in during crises, it is nevertheless worth considering further whether and in which circumstances central bank funding could be provided to MMFs taking into account the current framework for MMFs set out in the MMF Regulation.

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<sup>91</sup> In the Impact Assessment, transforming CNAV MMFs into special purpose banks was considered, amongst others to enable central banks to monitor their financing needs more closely and to be able to provide direct support to MMFs having liquidity problems (p. 23, 46). However, this option was not implemented in the final version of the MMF Regulation. It has been argued that subjecting MMFs to banking regulation would impact central bank monetary policies and the banking sector would be exposed to the risks of the MMF assets running into a contagion risk (p. 46). Also, MMFs not sponsored by banks would likely have to exit the business due to high additional operative costs and hence concentration in the sector would increase (p. 47). It was concluded that out of all the options that were considered, a conversion of MMFs to bank status appears to be the most incisive and represents the most challenging policy change. The impact of this option in terms of capital requirements and prudential supervision was considered as enormous and detrimental to the MMF sector (p. 51).

<sup>92</sup> MMF Regulation Consultation Report no. 79.

As demonstrated in this paper, central bank support for non-banks in the form of MMFs would not have to be ruled out completely from a purely legal perspective, although in a number of areas legislative action would be welcomed to enhance legal certainty and to make potential measures less vulnerable to challenges. This is, however, only one piece of the puzzle that, in order to form a complete picture, must be supplemented by considerations of, inter alia, the impact of the perception of the MMF sector's reliance on public sector support, the economic viability of MMF business models benefiting from the possibility to obtain public funding and on the goal of strengthening resilience in the MMF sector – and in the non-bank financial sector more broadly – to mitigate moral hazard.

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# Implementing monetary policy through non-banks: the ON RRP

By Marco Cipriani and Gabriele La Spada\*

## 1 Monetary policy implementation in the United States

### 1.1 Monetary policy implementation before the global financial crisis

US depository institutions – both domestic banks and branches of foreign banks – hold reserve balances (“reserves”) with the Federal Reserve System (“Federal Reserve”) to meet their liquidity needs. These reserves are borrowed and lent through uncollateralised loans, mostly overnight, called federal funds loans. The market for reserves is key for monetary policy implementation because the Federal Open Market Committee (FOMC)<sup>93</sup>, the committee responsible for regulating and directing open market operations of the Federal Reserve Banks, uses the effective federal funds rate (EFFR) – a daily summary statistic of the interest rate paid on federal funds loans – to communicate the monetary policy stance.<sup>94</sup>

Until the 2008 global financial crisis (GFC), the Federal Reserve communicated the stance of monetary policy by setting a specific target level for the effective federal funds rate. The EFFR was measured as the weighted average of the interest rate on federal funds loans reported to the Federal Reserve by federal funds brokers.

At that time, the amount of bank reserves at the Federal Reserve was relatively low (“reserve scarcity”), ranging from USD 40 to USD 50 billion between 2002 and 2008, and reserves did not pay an interest. As reserves were scarce and not remunerated, banks would actively trade in the federal funds market on a daily basis to meet their reserve requirements and liquidity needs; indeed, before the GFC, the daily volume in the federal funds market was around USD 220 billion (Afonso et al., 2014; Afonso et al., 2022).

To steer the EFFR towards its target, the Federal Reserve implemented a so-called “corridor system”. The Federal Reserve would adjust the amount of reserves

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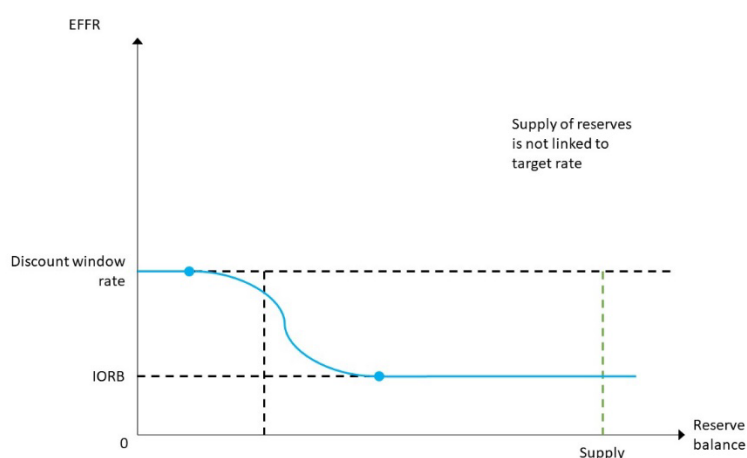
<sup>93</sup> The FOMC traditionally consists of all the members of the Board of Governors of the Federal Reserve, the president of the Federal Reserve Bank of New York and four of the remaining eleven Federal Reserve Bank presidents.

<sup>94</sup> Strictly speaking, the FOMC communicates the monetary policy stance via the “federal funds rate” – a conceptual rate. As a practical matter, the conceptual “federal funds rate” is measured by the EFFR, but the FOMC does not use the EFFR when communicating the policy stance.

available, the so-called “supply of reserves”, with relatively small daily open market operations (OMOs) to ensure that the federal funds rate would stay close to its target. When the Federal Reserve wanted to increase the supply of reserves, it would buy Treasuries, usually through repurchase agreements (repos), from primary dealers; these securities would then become an asset in the Federal Reserve’s balance sheet.<sup>95</sup> At the same time, the account of the primary dealer’s custodian bank at the Federal Reserve would increase by the value of the securities sold, adding to the amount of reserves available in the banking system; this increase in banks’ reserves would be an increase in liabilities in the Federal Reserve’s balance sheet, matching the increase in assets. Similarly, the Federal Reserve would reduce the amount of reserves by selling assets to primary dealers – usually through reverse repurchase agreements (reverse repos) – which, in turn, decreases the account of the dealer’s custodian bank at the Federal Reserve by the value of the securities purchased by the dealer.

In a scarce reserves environment, the supply of reserves intersects the steep part of banks’ reserve demand curve; even relatively small changes in the supply of reserve would imply material changes in the EFFR. By changing the supply of reserve, the Federal Reserve would steer the EFFR towards its target.

**Chart 1**  
Reserve demand



## 1.2 Monetary policy implementation after the global financial crisis

In the aftermath of the GFC, however, it became necessary to introduce several important changes to the Federal Reserve’s monetary policy implementation framework. Between 2008 and 2014, the Federal Reserve purchased large quantities of securities to stabilise the financial sector and support the economy in the aftermath of the crisis. As a result of this unprecedented balance sheet expansion, reserves

<sup>95</sup> Primary dealers are the trading counterparties of the Federal Reserve in the implementation of monetary policy; there are currently 25 primary dealers, including both banks and securities dealers. The assets purchased or sold by the Federal Reserve in OMOs are Treasuries and agency mortgage-backed securities.

exceeded USD 1 trillion in 2009 and reached USD 2.8 trillion in 2014. In such an environment of abundant reserves, small adjustments to the supply of reserves do not influence rates because reserves are so plentiful that the supply of reserves intersects the flat segment of banks' reserve demand curve.

Moreover, in 2008, the US Congress granted the Federal Reserve the authority to pay an "Interest on Reserve Balances (IORB)"<sup>96</sup>. Since then, the Federal Reserve has implemented monetary policy by changing the IORB in a so-called "floor system". In such a system, because banks can earn IORB on the balances in their Federal Reserve accounts, they are unwilling to lend in the federal funds market at a rate below the IORB.<sup>97</sup>

Since 2008, the Federal Reserve has communicated the monetary policy stance by setting a target range, instead of a target level, for the EFFR. Moreover, in 2016, it started computing the EFFR as the weighted median (as opposed to the average) of federal funds transactions reported directly to the Federal Reserve, through the FR2420 data collection, by institutions borrowing in the federal funds market.<sup>98</sup>

In 2019, the Federal Reserve formally adopted the ample reserves framework to implement monetary policy. In this system, an ample supply of reserves ensures that "control over the level of the federal funds rate and other short-term interest rates is exercised primarily through the setting of the Federal Reserve's administered rates, and in which active management of the supply of reserves is not required" (FOMC, 2019a and 2019b). Indeed, reserves are currently still very high, ranging between USD 3.1 and USD 3.9 trillion in 2022.

Chart 1 contrasts the implementation of monetary policy in a scarce and in an ample reserve regime. On the x-axis is the supply of reserves and on the y-axis the EFFR. The blue line represents banks' demand for reserves. If the supply of reserves crosses reserve demand on the steep segment of the reserve-demand curve, reserves are scarce, and monetary policy operates under a corridor system: even small changes in the supply of reserves move the interest rate, and the Federal Reserve affects the EFFR through daily OMOs that change the supply of reserves. In contrast, if the supply of reserves crosses reserve demand in the flat (or almost flat) segment of the reserve-demand function, reserves are ample, and monetary policy operates under a floor system, where the EFFR does not respond significantly to changes in the supply of reserves but is directly affected by changes in the IORB.

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<sup>96</sup> The 2006 "Financial Services Regulatory Relief Act" authorised the Federal Reserve Banks to pay interest on reserve balances starting in October 2011; in 2008, through the Emergency Economic Stabilization Act, Congress brought the date forward to October 2008. Until 2020, the Federal Reserve set two rates, the Interest on Reserve Balance Requirements (IORR) and the Interest on Excess Reserve Balances (IOER), though the two rates were set at the same level most of the time. In March 2020, the Federal Reserve eliminated banks' reserve requirements and proposed (and ultimately adopted) a single interest rate on reserve balances, the IORB.

<sup>97</sup> As we explain below, however, market frictions may push the EFFR below the ON RRP rate.

<sup>98</sup> See [https://www.newyorkfed.org/markets/opolicy/operating\\_policy\\_150202](https://www.newyorkfed.org/markets/opolicy/operating_policy_150202) and [https://www.newyorkfed.org/markets/opolicy/operating\\_policy\\_160106](https://www.newyorkfed.org/markets/opolicy/operating_policy_160106)

## 2 The ON RRP

### 2.1 Market frictions and the need of a floor

Since 2008, the EFFR has moved together with changes in its target range and remained close to the IORB, as shown in Chart 2. However, most of the time, the EFFR has been below the IORB, although as we mention above, banks have no incentive to lend their reserve balances below the IORB as they can get a higher interest by keeping them in their Federal Reserve accounts.

The reason is that depository institutions are not the only institutions trading in the federal funds market. Other institutions, such as government-sponsored enterprises (GSEs) and, in particular, Federal Home Loan Banks (FHLBs) hold accounts with the Federal Reserve.<sup>99</sup> These institutions have accounts with the Federal Reserve that do not qualify as reserves, and therefore do not earn the IORB. However, balances on these accounts can be used to lend in the federal funds market and become reserves when they are lent to banks. In particular, whereas 50 % of federal funds volume was among commercial banks before the GFC, FHLBs have provided more than 80 % of federal funds lending since 2008 (Afonso et al., 2014). Because FHLBs cannot earn IORB on their balances, they may be willing to lend them at lower rates, pushing the EFFR below the IORB.<sup>100</sup>

In theory, even if FHLBs do not have access to the IORB, in the absence of frictions, the EFFR should be equal (or very close to) the IORB when reserves are ample. The reason is that if banks are able to obtain funds from FHLBs significantly below IORB, they have an incentive to borrow from FHLBs and then hold these funds in their accounts at the Federal Reserve to earn the IORB, profiting from the spread; such borrowing increases demand for federal funds, which pushes the EFFR towards the IORB.

In practice, however, there are market frictions that introduce a wedge between the IORB and EFFR. In particular, banks are subject to regulatory and internal constraints based on balance-sheet size; therefore, they may be willing to borrow from FHLBs – which implies a balance-sheet expansion – to earn the spread only if the difference between the EFFR and the IORB is large enough.

Moreover, banks can also obtain overnight liquidity by borrowing from money market funds (MMFs), either in an unsecured way through Eurodollar transactions or in a secured way through repos, typically collateralised by Treasuries.<sup>101</sup> Both Eurodollar

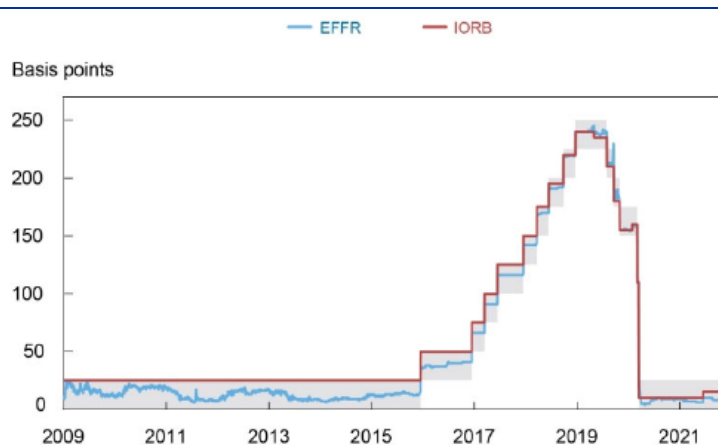
<sup>99</sup> A GSE is a quasi-governmental entity created by the US Congress to increase credit provision to specific sectors of the economy, for example the Federal Home Loan Mortgage Corporation (Freddie Mac). FHLBs are GSEs providing financial institutions support for housing finance. Debt issued by GSEs is commonly referred to as agency debt.

<sup>100</sup> All GSEs can lend in the federal funds market. In the remainder of the article, however, we will only refer to FHLBs because they are currently the main lender.

<sup>101</sup> A repo is a transaction in which the borrower sells a security to the lender, while agreeing to repurchase that same security at a specified price in the future. This is economically equivalent to a collateralised loan, where the difference between the purchase and the repurchase prices implies an interest rate.

and Treasury-backed overnight repos are not federal funds loans, and therefore do not enter into the computation of the EFFR; however, they are close substitutes, providing banks with liquidity that they can park as reserves with the Federal Reserve, earning IORB. The Eurodollar market and especially the repo market are much larger than the federal funds market; in 2015, for instance, daily average volume was around USD 140 billion for Eurodollar transactions and USD 600 billion for overnight Treasury-backed repos (Cipriani and Gouny, 2015). If rates in these markets print significantly below the EFFR, this impairs the transmission of monetary policy to short-term money rates.<sup>102</sup>

**Chart 2**  
EFFR and IORB



Source: FRED | Period: 9/23/2013 - 8/17/2022 | Frequency: Daily

To set a soft floor on the EFFR and other short-term rates, in 2013, the Federal Reserve introduced the Overnight Reverse Repo Facility (ON RRP).<sup>103</sup> The ON RRP allows MMFs, GSEs, banks, and primary dealers to place money (that is, to invest) overnight with the Federal Reserve at a fixed rate, the so-called ON RRP offering rate, via repurchase agreements backed by Treasuries.<sup>104</sup>

By allowing non-bank institutions to invest with the Federal Reserve via overnight repos at a fixed rate, the ON RRP provides a soft floor for the federal funds rate and for short-term rates in general. In fact, since the introduction of the ON RRP, the EFFR has almost never been below the ON RRP rate, as shown in Chart 3. The effectiveness of the ON RRP facility in controlling federal funds and other short-term rates was confirmed by the December 2015 lift-off, when the Federal Reserve tightened policy rates for the first time in a decade, and again in March 2022 when the

<sup>102</sup> In addition, if the Eurodollar and the repo rates print significantly below the EFFR, banks have an even lower incentive to borrow from FHLBs in the federal funds market, putting further downward pressure on the EFFR.

<sup>103</sup> The terms repo and reverse repo refer to the same transaction from different points of view. To the party selling the security with the agreement to buy it back (i.e., cash borrower in exchange for collateral) it is a repo. To the party buying the security and agreeing to sell it back (i.e., cash lender in exchange for collateral) it is a reverse repo.

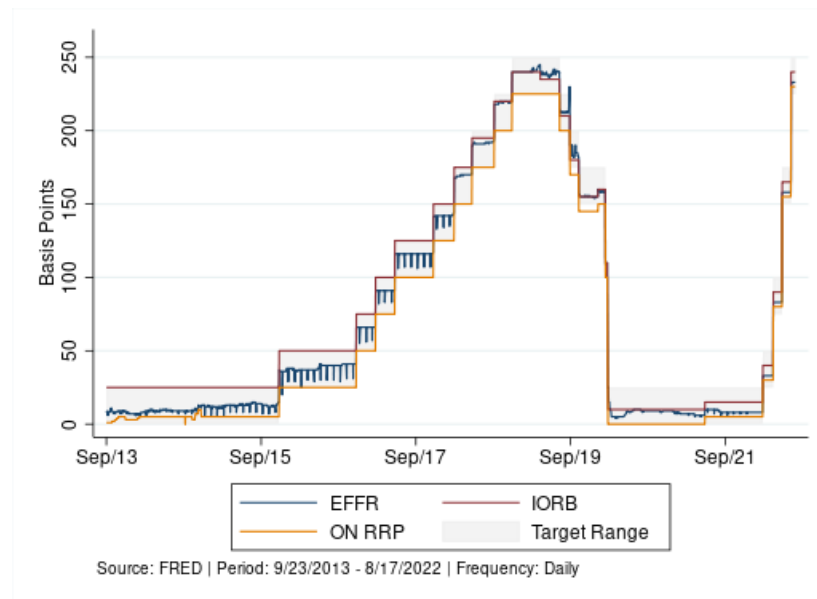
<sup>104</sup> A complete and up-to-date list of counterparties can be found at [https://www.newyorkfed.org/markets/rrp\\_counterparties](https://www.newyorkfed.org/markets/rrp_counterparties)



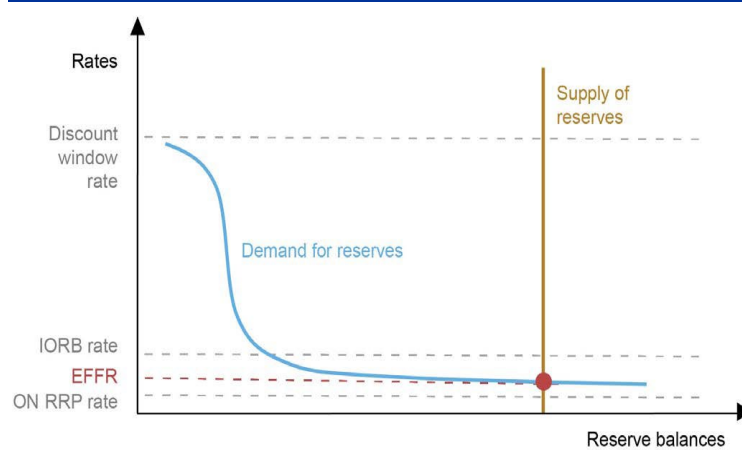
Federal Reserve started increasing rates in an environment of extremely abundant reserves.

In the current framework, the Federal Reserve changes its two administered rates – the IORB and ON RRP rates – together to implement monetary policy, and the reserve demand curve can be stylised as in Chart 4.

**Chart 3**  
EFFR, IORB and the ON RRP rate



**Chart 4**  
Reserve demand with ON RRP



## 2.2 The ON RRP setup

### 2.2.1 Legal authority

The legal authority for the establishment of the ON RRP comes from the Federal Reserve Act, Section 14(1):

*“Every Federal Reserve Bank shall have power [...] [t]o buy and sell, at home or abroad, bonds and notes of the United States [...].”*

Moreover, Section 12A(b) of the same Act stipulates that:

*“No Federal Reserve bank shall engage or decline to engage in open-market operations under section 14 of this Act except in accordance with the direction of and regulations adopted by the Committee.”*

Where the “Committee” is the FOMC. In accordance with this provision, each year the FOMC authorises the Federal Reserve Bank of New York to conduct domestic OMOs. As part of its policy decisions, the FOMC also periodically issues a domestic policy directive that covers ON RRP operations.

### 2.2.2 The mechanics of ON RRP operations

The Open Market Desk of the Federal Reserve Bank of New York (the “Desk”) conducts ON RRP operations daily, from 12:45 to 1:15 p.m.<sup>105</sup> The offering interest rate is pre-announced and set by the FOMC. The total daily investment in the ON RRP is capped at the total value of (most) Treasuries held outright in the System Open Market Account (SOMA) portfolio at the Federal Reserve Bank of New York, which are used as collateral in the transactions.<sup>106</sup>

Every day, any eligible counterparty can submit propositions for investing in the ON RRP up to the counterparty limit, which is currently set at USD 160 billion, and at a rate equal to or lower than the ON RRP offering rate.<sup>107</sup> If the total value of the propositions is below the aggregate limit – as it has almost always been the case – the interest rate on the transactions is the ON RRP rate set by the FOMC; if the aggregate limit is exceeded, awards are made at the rate at which the size limit is achieved, similarly to

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<sup>105</sup> The Desk can also conduct unscheduled repo operations as needed to maintain the federal funds rate within the target range, in accordance with the FOMC’s authorisations and directives.

<sup>106</sup> Securities that are not available for ON RRP operations include Treasuries held outright in the SOMA portfolio that are needed to conduct reverse repos with foreign official and international accounts, securities needed to support the securities lending operations conducted by the Desk and securities nearing maturity. Additionally, the Treasury securities serving as collateral for any outstanding term reverse repo operations would not be available to serve as collateral for ON RRP operations.

<sup>107</sup> The minimum proposition size is USD 1 million, and propositions must be submitted in increments of USD 1 million. All awards are allocated in USD 1 million increments.

a uniform price auction.<sup>108</sup><sup>109</sup> ON RRP trades settle on the tri-party repo (TPR) platform, on the books of BNY Mellon, the clearing bank of the platform.

## 2.3 ON RRP usage: past and present

In July 2013, Federal Reserve staff proposed establishing a reverse repo facility opened to a varied set of counterparties, including important non-bank lenders in money markets, to make it easier for the Federal Reserve to lift rates in an ample-reserve environment. Using reverse repos as a tool for monetary policy implementation was not new: as we discuss before, repos and reverse repos were used by the Desk before 2008 to temporarily add and drain reserves in the banking system. In this sense, the ON RRP was a *new twist* on an existing tool, expanding however the set of counterparties.

The FOMC authorised a testing exercise of the ON RRP in September 2013, to assess the facility's efficacy in controlling short-term rates. During this exercise, the FOMC directed the Desk to change the ON RRP rate and the counterparty caps in order to better understand how the facility would work. Between September 2013 and December 2014, the offering rate was moved up and down within a range from zero to ten basis points multiple times, and the counterparty cap was increased from USD 500 million to USD 30 billion. In September 2014, the FOMC also introduced a USD 300 billion overall limit for ON RRP daily take-up (FOMC, 2014b) and established the auction process described above to set the ON RRP rate if the overall limit is binding.<sup>110</sup>

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<sup>108</sup> The aggregate limit was more relevant prior to the rate liftoff of December 2015; indeed, the aggregate cap on the ON RRP was reached in September 2014. For this reason, from December 2014 to December 2015, the Desk also offered term reverse repos in addition to the ON RRP to add *capacity* to reduce the chances of the ON RRP aggregate limit being reached. The counterparty cap has been increased throughout the facility's existence.

<sup>109</sup> The Desk awards ON RRP propositions starting from the bidder submitting the lowest rate, giving this bidder the quantity requested; then the second-highest bidder and so forth until the aggregate ON RRP cap is reached; bids at the rate at which the cap is reached are awarded a pro-rata share. All bidders receive the same rate, equal to the lowest winning bid regardless of their actual bid.

<sup>110</sup> The explicit aggregate cap, fixed in USD terms, was abolished in December 2015; the only remaining aggregate cap is that related to the availability of securities described in the article (in addition to the counterparty caps).

**Chart 5**  
ON RRP take-up

(units, axis description)

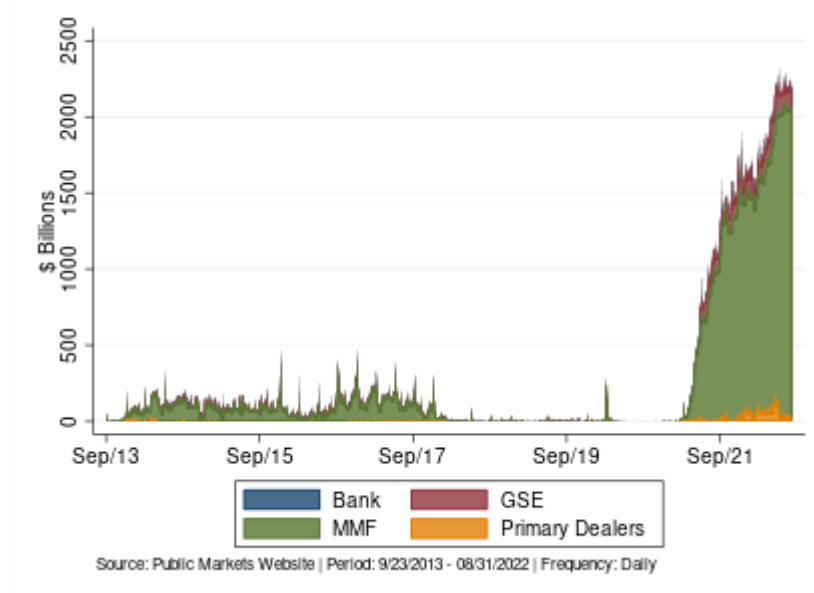


Chart 5 shows that, since the facility's inception, MMFs have consistently contributed to the vast majority of ON RRP take-up, accounting for roughly 89 % of the dollar value from September 2013 to August 2022. Moreover, ON RRP usage has varied greatly over time. We can identify three periods in the facility's existence.

During the testing period and the first half of the facility's existence, from September 2013 to December 2017, ON RRP take-up averaged USD 114 billion per day, with large spikes at quarter-ends (and smaller ones at month-ends). These spikes reflect sharp drops in the demand for overnight funding, which led MMFs, and to a lesser extent FHLBs, to invest their cash in the ON RRP. This drop in demand was due to regulatory reasons: some foreign banks compute regulatory leverage and capital ratios on quarter-end dates using a snapshot of their balance sheets at month-end. Because of this, they have an incentive to reduce borrowing at quarter-ends (the so-called "window-dressing"). Between September 2013 and December 2017, the average quarter-end ON RRP take-up was USD 284 billion, versus USD 111 billion on non-quarter-end dates.

These month-end decreases in banks' demand for short-term borrowing push money market rates down. If the demand for ON RRP around those dates exceeds the aggregate cap, the facility's award rate will be below the offering ON RRP rate because of the auction system described in Section 2.2; as a result, the ability of the ON RRP to act as a soft floor to the federal funds rate and support other short-term money rates would be impaired. Indeed, this is what happened at the September 2014 quarter end: ON RRP demand was USD 407 billion, above the aggregate USD 300 billion facility cap at that time; as a result, the award rate fell to zero basis points at the

end of the month and the rate on Treasury-backed repos fell below the ON RRP rate (Frost et al., 2015).<sup>111</sup>

From early 2018 to early 2021, on the other hand, ON RRP take-up was very low. Although the MMF industry had been increasing in size, both banks' demand for short-term borrowing (especially repos) and the supply of short-term Treasuries, another important investment in MMF portfolios, increased during that period; because of that, MMFs had less need to place their money with the ON RRP. The only exception were the early days of April 2020, when, at the beginning of the COVID-19 pandemic, government MMFs experienced sudden and large inflows as investors ran from prime to safer government MMFs (Cipriani and La Spada, 2020); faced with a sudden inflow of funds, government MMFs temporarily placed their money with the ON RRP.

In March 2021, ON RRP take-up started to increase again and has been increasing since then, reaching USD 2.4 trillion in September 2022, an unprecedented surge.<sup>112</sup> Afonso, Cipriani, and La Spada (2022) identify three main drivers behind this unprecedented increase in take-up. First, monetary policy tightening increases the size of the MMF industry, as investors flow from bank deposits – whose rates respond very sluggishly to policy-rate increases – to MMF shares, whose yields, in contrast, respond quickly and almost one-to-one to policy rate changes. Moreover, rising rates push MMFs to tilt their portfolios towards shorter-term securities such as overnight repos (and away from longer-term instruments) to reduce interest rate risk. Second, as the Federal Reserve expanded its balance sheet in response to the COVID-19 crisis, banks' balance sheet costs became more significant, reducing banks' demand for short-term borrowing; facing a reduced supply of short-term debt, MMFs shifted their investment toward the ON RRP. Similarly, as their balance sheet costs rose, banks had an incentive to shed deposits, which, in turn, flowed to MMF shares – their closest substitute – increasing MMF assets under management and therefore their ON RRP investment. Finally, the supply of T-bills also decreased during the same time period, giving MMFs fewer investment options and driving up the share of their assets invested in the ON RRP.<sup>113</sup>

### 3 The ON RRP versus emergency credit facilities

The ON RRP is not the only facility through which the Federal Reserve has interacted with MMFs. In particular, over the last 15 years, the Federal Reserve established two temporary facilities to assist MMFs meet heavy redemptions, stabilise the US

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<sup>111</sup> To strengthen rate control around month- and quarter-ends, in October 2014, the FOMC instructed the Desk to offer up to USD 300 billion in term (i.e., longer than overnight), reverse repo operations with the same set of counterparties used for ON RRP operations. The total reverse repo take-up on December 31 – the next quarter end – was USD 397 billion, of which USD 171 billion were in the ON RRP and USD 226 billion in the term reverse repos; likely because of these additional term offering, short-term interest rates generally stayed above the ON RRP offering rate at the end of December.

<sup>112</sup> In response to this increased demand for the ON RRP facility, in September 2021, the FOMC raised the counterparty limit from USD 80 to USD 160 billion.

<sup>113</sup> All these drivers have become more salient since 2016, after the Securities and Exchange Commission reform of the MMF industry, which caused a USD 1 trillion flow from prime to government MMFs, whose investment options are narrower (Cipriani and La Spada, 2021). Note also that not all of these drivers operated at the same time: for instance, take-up started growing well before monetary policy tightening.

short-term funding markets and support the provision of credit to the real economy during times of stress.

The most recent example is the Money Market Mutual Fund Liquidity Facility (MMLF), which was established by the Federal Reserve – with the approval of the Secretary of the Treasury and USD 10 billion in credit protection from the Exchange Stabilization Fund – in March 2020 to help prime and tax-exempt MMFs to meet the heavy redemptions suffered by these funds at the onset of the COVID-19 crisis.<sup>114</sup>

US prime MMFs lost USD 143 billion between 6 March and 26 March 2020, roughly 19 % of their assets under management; tax-exempt MMFs suffered similar outflows as a share of their assets under management. Around the same time, several money market rates increased sharply: the spreads of overnight AA-rated ABCP and AA-rated non-financial CP increased by 1.1 and 1.0 percentage points relative to the IORB; the effect on second-tier non-financial CP was even stronger, with the spread reaching 3.2 percentage points on March 17.

Through the MMLF, the Federal Reserve Board of Governors authorised the Federal Reserve Bank of Boston to make non-recourse loans to banks so that they could purchase assets from US MMFs; in turn, those assets collateralised the MMLF loans from the Federal Reserve Bank of Boston. Eligible assets included a wide range of money market instruments issued by the private sector and local governments, such as CP, ABCP, certificates of deposits and VRDNs, which had become highly illiquid in early March 2020. By lending to banks to purchase illiquid assets from MMFs, the MMLF improved the liquidity of MMF portfolios, helping them meet redemptions and disincentivising investors from running.

The facility ended its operations on 31 March 2021, by which time it had extended about USD 58 billion in credit. Even if the total value lent was much smaller than the size of the prime and tax-exempt MMF industry at that time (around USD 900 billion), the facility was very effective in reducing outflows from prime and tax-exempt MMFs and helped stabilise the US short-term funding markets at large (Anadu et al., 2022).

The MMLF design was based on that of a similar facility that the Federal Reserve had set up in September 2008, the Asset-Backed Commercial Paper Money Market Mutual Fund Liquidity Facility (AMLF). At that time, prime MMFs suffered another run, due to funds' exposure to the debt of distressed banks, during which they lost 18 % of their assets under management; as was the case the in 2020, the 2008 run destabilised money markets, with the spreads between overnight AA-rated ABCP and second-tier non-financial CP rates and the target EFRR reaching 3.6 and 3.8 percent points. The AMLF setup was similar to that of the MMLF, with the main difference being that banks could only use the funds to purchase ABCP, the main driver of funds' illiquidity at that time. Similar to the MMLF, the AMLF, which closed its operation in February 2010, was effective at abating investor outflows from prime MMFs and normalising market rates.

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<sup>114</sup> In the United States, government MMFs invest almost all their assets in US government and agency securities and in repos backed by those securities; prime MMFs can also buy private unsecured debt such as certificates of deposit (CDs), commercial paper (CP), and variable-rate demand notes (VRDNs), in addition to asset-backed commercial paper (ABCP); tax-exempt funds (also called municipal funds) mainly invest in short-term municipal, state, and local government debt, mainly in the form of VRDNs.

It is worth emphasising that the MMLF and AMLF are facilities different from a facility such as the ON RRP. First, the purpose of both the MMLF and the AMLF was to support the flow of credit to households and business, not monetary policy implementation.

Second, the MMLF and the AMLF were both credit facilities, offering liquidity to MMFs; in contrast, the ON RRP is an OMO through which MMFs invest at the Federal Reserve. For this reason, the MMLF and AMLF were assets in the Federal Reserve's balance sheet, whereas the ON RRP is a liability.

Third, through the ON RRP the Federal Reserve transacts directly with MMFs as they place money on its balance sheet. In contrast, through the MMLF and AMLF, the Federal Reserve made loans to banks, which used these loans to purchase assets from the MMFs.

Finally, in establishing the MMLF and AMLF, the Federal Reserve relied on a different section of the Federal Reserve Act, namely Section 13(3), which allows the Federal Reserve to lend on a secured basis in unusual and exigent circumstances, with prior approval of the Secretary of the Treasury.

## 4 The ON RRP and reserves

Changes in the ON RRP usage affect the aggregate level of reserves in the banking system: when an MMF invests in the ON RRP, it uses its deposits with its custodian bank, instructing the bank to place the cash in the ON RRP; to do this, the custodian bank uses its reserve balance at the Federal Reserve.

As we mentioned above, the ON RRP settles on the books of BNY Mellon, the TPR clearing bank. In contrast to typical TPR procedures, however, BNY Mellon does not keep the cash during the term of the transaction but rather transfers it to the Federal Reserve ON RRP account; as a result, when the ON RRP balance on the Federal Reserve's balance sheet increases, the amount of reserves in the banking system decreases by the same amount.

Chart 6 shows the impact of an ON RRP transaction on the Federal Reserve's balance sheet. In the example, an MMF invests USD 100 in the ON RRP, leading to a decline in reserve by USD 100, whereas the size of the Federal Reserve's balance sheet remains unchanged.

### Chart 6

#### ON RRP and reserves in the Federal Reserve's balance sheet

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##### Federal Reserve balance sheet

A		L	
Treasuries =		Reserves -100	
		ONRRP +100	

In other words, whereas only banks can hold reserve balances, the ON RRP allows a wider set of counterparties, including MMFs, to hold Federal Reserve liabilities. For this reason, the ON RRP allows the Federal Reserve to stimulate the economy by expanding its balance sheet – that is, through quantitative easing – without putting pressure on the balance sheets of banks (Cipriani et al., 2022).

In times of stress, the Federal Reserve may want to stimulate the economy by expanding its balance sheet through large-scale asset purchases and emergency lending facilities, as it did in 2008 and 2020. Both types of intervention operate through banks and their reserve accounts at the Federal Reserve. As Chart 7 shows, without the ON RRP, an increase in the Federal Reserve's balance sheet is likely to lead to a larger increase in banks' balance sheets. Since banks face both regulatory and internal constraints based on balance sheet size, balance sheet expansions by the Federal Reserve may make these constraints tighter. By allowing the Federal Reserve to expand its balance sheet through a wider set of institutions, the ON RRP alleviates this concern.

Indeed, this is what happened following the expansion of the Federal Reserve's balance sheet in response to the 2020 COVID-19 crisis: the increase in ON RRP take-up meant that the Federal Reserve was able to add stimulus to the economy through quantitative easing beyond the amount of reserves that the banking sector wanted to hold.



**Chart 7**

Federal Reserve's balance sheet expansion with and without ON RRP

Without ONRRP		With ONRRP	
A	L	A	L
Treasuries +100	Reserves +100	Treasuries +100	Reserves +50
			ONRRP +50

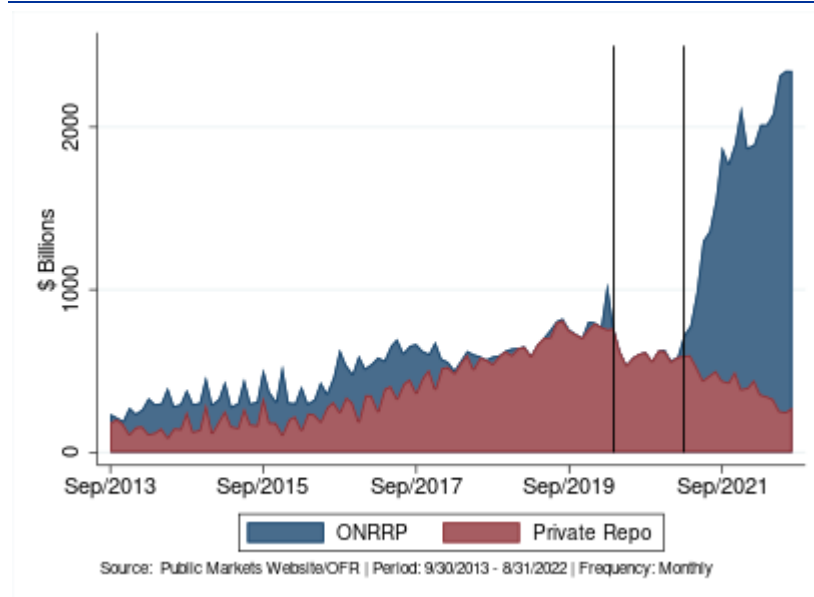
## 5 Considerations on financial intermediation and stability

When the ON RRP was proposed, both policymakers and academics raised concerns about its implication for financial stability and intermediation.

First, a larger ON RRP implies an expansion of the Federal Reserve's footprint in short-term funding markets. This may crowd out private financing, and especially banks' financing, as important money-market lenders such as FHLBs and MMFs place their cash directly, and earn an interest, with the Federal Reserve. For example, Chart 8 shows that, from March 2021 to August 2022, MMFs' private repo lending decreased by USD 320 billion, whereas their ON RRP take-up increased by USD 1.94 trillion. The crowding out of private short-term debt by the ON RRP could permanently affect financial intermediation in unintended ways: if large ON RRP usage is sustained for a prolonged time, it could atrophy the private short-term funding markets (FOMC, 2014a, 2014b; Frost et al., 2015). The experience of 2017-2019, however, is that the ON RRP organically declined as the Federal Reserve reduced its balance sheet and returns on alternative investments became more attractive; this evidence alleviates the concerns about crowding out private financing.

**Chart 8**

ON RRP and private repos held by MMFs



Second, the ON RRP can have important repercussions for financial stability. The ON RRP represents an extremely safe and overnight investment opportunity for MMFs and FHLBs. On the one hand, the Federal Reserve’s provision of this money-like asset to these money market lenders with cash management needs may displace private money, which is riskier and more exposed to run risk (Stein, 2012; Greenwood, Hanson, and Stein, 2013; Krishnamurthy and Vissing-Jorgensen, 2013; Carlson et al., 2014). Because of this, the ON RRP may reduce the risk of runs in the financial system, and it could do this better than short-term Treasury securities as government creation of short-term safe assets implies a greater rollover risk to the government.

On the other hand, if the caps on the facility’s usage are very large, so that they are unlikely to be binding, the ON RRP may have disruptive effects on financial stability by facilitating flight-to-quality episodes during periods of distress. In particular, by providing an outside safe option at a fixed rate, the ON RRP could increase the likelihood of a run by money market investors. Whereas the price of other safe assets, such as Treasuries, increases with market demand in times of stress, thereby reducing flight-to-quality incentives, the ON RRP rate does not, as long as the aggregate cap is large enough; for this reason, it could experience sudden and very large increases in usage during periods of market stress. Indeed, the concern of potentially exacerbating flight-to-quality episodes was one of the reasons why the ON RRP was subject to more stringent aggregate caps when it was originally opened.

It is worth noticing that a flight-to-quality to the ON RRP did not materialise in April 2020 when prime MMFs were subject to very heavy redemptions. Funds mainly flowed from prime to government funds, without ON RRP take-up increasing during the run. There was an uptick in ON RRP take-up after the run as government funds invested the cash they had received from investors leaving prime funds.

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## Panel 3

# Towards legal interoperability of retail central bank digital currencies: a comparative law perspective



# Legal interoperability and retail CBDCs: taming the multiverse of (payments) madness

By Jess Cheng and Joseph Torregrossa\*

In the context of central bank digital currencies (CBDCs), interoperability is often prioritised as a critical technical functionality, but its legal dimensions are largely unexplored. This note contributes to the discussion by introducing the concept of “legal interoperability” in the domestic payment system and its relevance to the retail CBDC context, particularly as the necessary legal foundation for transferability and convertibility. Based on lessons from the past, this note will also provide pragmatic considerations for the future, with an emphasis on safety and efficiency.

## 1

### Introduction

The ability to seamlessly move like Doctor Strange across these different dimensions in the domestic payment system — that is, various payment networks and forms of money — is critical to the overall system’s efficiency.

In the 2022 film Doctor Strange and the Multiverse of Madness, the eponymous protagonist experiences an array of alternate realities, traveling (at times unwillingly) from universe to universe. Moments after a hyper-destructive downtown battle with a cyclopiian octopus, Doctor Strange and his ragtag team of heroes gather at a downtown pizzeria, where their existential dilemma in the multiverse (that is, multiple worlds and multiple character identities that simultaneously exist) is neatly presented:

America Chavez: I can travel the Multiverse.

Doctor Stephen Strange: What?

The Sorcerer Supreme: You can physically move from one multiverse to another?

Doctor Strange: How?

America Chavez: That’s the problem. I don’t know how. I can’t control it. Only happens when I’m really, really afraid.”

In the payment space, while there are no monsters rampaging through “alt-worlds”, there are various planes of existence, so to speak, in the form of various payment networks (such as automated clearinghouse or ACH services, wires, checks, and

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instant payments) and various networks of money (such as deposits with commercial banks and cash, as well as potentially a central bank digital currency or CBDC).

How a given jurisdiction's payment "multiverse" is constructed depends in large part on the law. As explained in a note by the authors:

"Take a close look at something that is widely used by the general public as "money" – a Federal Reserve note, a deposit with a bank, a balance with a nonbank payment company (such as PayPal or Venmo), or perhaps even a cryptocurrency – and ask what it means to use it as a store of value and a medium of exchange. That question is, in essence, a legal one. Who (if anyone) stands behind the associated commitments and what rules (if any) govern it? For a Federal Reserve note, the associated obligations are undertaken by a trusted party, with the arrangement governed by reliable and time-tested rules. On the opposite end of the spectrum are certain stablecoins and other cryptocurrencies for which the legal rights and obligations are unpredictable, obfuscated, or idiosyncratic, with untested rules."<sup>115</sup>

The ability to seamlessly move like Doctor Strange across these different dimensions in the domestic payment system – that is, various payment networks and forms of money – is critical to the overall system's efficiency. Legal considerations are paramount in that regard, as explained by the authors:

"A sound legal framework is an important foundation for network effects within the payment system. It can bring certainty and clarity to a payment arrangement, resulting in greater consistency and predictability to the parties' payments activity; this, in turn, removes inefficiencies and provides an incentive for more parties to join the system. The ability of different arrangements to interoperate, including from a legal standpoint – that is, for users to smoothly and efficiently choose between arrangements subject to different legal frameworks, while being confident the arrangement will, like money, serve as a way to make a payment – could bring further efficiencies to users."<sup>116</sup>

As the world considers the future evolution of money in the form of a "general purpose" or "retail" CBDC (that is, a CBDC intended to be held and used by consumers and businesses for day-to-day transactions, including as payment for small-value goods and services) – and in particular the legal foundation for cross-border CBDC arrangements – it is necessary to consider how the system currently works and why that is, as well as how the concept of "legal interoperability" is already reflected in today's domestic payment system, as this note will cover.

## 2 Central bank digital currencies

A CBDC that is widely available to the general public would therefore be a new third type of central bank money.

A number of central banks around the world, including the Federal Reserve in the United States, have been exploring the potential benefits and risks of CBDCs from a variety of angles, including through technological research and experimentation.

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<sup>115</sup> Cheng and Torregrossa (2022) (hereinafter, the "Lawyer's Perspective Note").

<sup>116</sup> *ibid.*



The Bank for International Settlements (BIS) refers to CBDC as “a digital payment instrument, denominated in the national unit of account, that is a direct liability of the central bank.”<sup>117</sup> Today, in the United States and most other jurisdictions, money in the form of a direct liability of the central bank (i.e. “central bank money”) exists in two forms: (1) Cash (physical banknotes that are widely available to the general public) and (2) balances in central bank accounts (deposits that are electronically recorded on the central bank’s books, for which only certain statutorily specified financial institutions are eligible to hold). A CBDC that is widely available to the general public would therefore be a new third type of central bank money, likely with some combination of the defining features of the two currently existing types of central bank money.

In a recent Bank for International Settlements survey of central banks, “Gaining momentum – Results of the 2021 BIS survey on central bank digital currencies” (the “BIS Survey”), of the 81 central banks surveyed, 90 % of central banks reported that they are exploring CBDCs, with more than half now developing them or running concrete experiments.<sup>118</sup> The survey notes that more and more central banks are in the “advanced stages” of exploring a CBDC, with 26 % currently developing a CBDC or running a pilot and 62 % conducting experiments or proofs-of concept.

## 2.1 The role of the private sector

Although CBDCs would be a new form of central bank money, the private sector would nevertheless be expected to have an important role to play. For example, preliminary analysis by the Federal Reserve Board of Governors suggests that a potential US CBDC, if one were created, “would best serve the needs of the United States” by being “intermediated”, among other things.<sup>119</sup>

Under this intermediated model, the general public would hold CBDC and transact in CBDC through private-sector financial institutions, which potentially could include banks as well as nonbank financial institutions. In this arrangement, the Federal Reserve would provide CBDC-related financial services only to these private-sector financial institutions (rather than becoming a retail bank that directly services the

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<sup>117</sup> BIS Annual Economic Report (2021).

<sup>118</sup> Kosse and Mattei (2022).

<sup>119</sup> Board of Governors of the Federal Reserve System (2022).

general public), with the financial institutions in turn having customer relationships with members of the general public.<sup>120</sup>

The Federal Reserve Board of Governors has provided further preliminary commentary on an “intermediated” model for a US CBDC: “The Federal Reserve Act does not authorize direct Federal Reserve accounts for individuals, and such accounts would represent a significant expansion of the Federal Reserve’s role in the financial system and the economy. Under an intermediated model, the private sector would offer accounts or digital wallets to facilitate the management of CBDC holdings and payments. Potential intermediaries could include commercial banks and regulated nonbank financial service providers, and would operate in an open market for CBDC services. Although commercial banks and nonbanks would offer services to individuals to manage their CBDC holdings and payments, the CBDC itself would be a liability of the Federal Reserve. An intermediated model would facilitate the use of the private sector’s existing privacy and identity-management frameworks; leverage the private sector’s ability to innovate; and reduce the prospects for destabilizing disruptions to the well-functioning U.S. financial system.”<sup>121</sup>

Such an approach is consistent with the various CBDC models under consideration among other central banks: “Most central banks are considering a retail CBDC architecture that involves the private sector ... [T]here are generally two ways in which central banks can distribute a CBDC to the public – either directly (a one-tiered model) or indirectly, via private sector intermediaries (a two-tiered model). In the one-tiered model, the central bank would not only operate the interbank CBDC system but also provide the CBDC account and wallet services directly to the public. In the two-tiered model, the central bank and trusted private sector intermediaries would work together.”<sup>122</sup>

## 2.2 Interoperability and legal dimensions

From a practical standpoint, customers of different CBDC intermediaries would ideally be able to readily transfer CBDC balances between each other, if a CBDC were to serve as a widely accessible means of payment.<sup>123</sup> As the Federal Reserve has noted, “[t]he ability to transfer value seamlessly between different intermediaries

<sup>120</sup> *ibid.*, an alternative to this model could be an arrangement where the general public holds a liability issued by financial institutions, with financial institutions backing these customer claims one-to-one with balances at the central bank, such as the Federal Reserve. This model could leverage the concept of a securities entitlement under Article 8 of the US Uniform Commercial Code. In the context of a CBDC, the holder of a CBDC would have an “entitlement” – that is, a *sui generis* package of rights and interests – against their private-sector CBDC intermediary, and that intermediary would be obliged to back these claims one-to-one with balances at the central bank. For example, a US CBDC intermediary would have the obligation to maintain a balance with the Federal Reserve equal to its total entitlements to customers. Like the holder of a securities entitlement under Article 8, a CBDC holder in this arrangement could look only to its CBDC intermediary to assert any claims or exercise any rights. Provided that the regulatory framework ensures that these intermediaries’ liabilities are always fully backed by a balance at the central bank, these liabilities could share many of the characteristics of a CBDC arrangement where the general public has a direct relationship with the central bank. However, under such an approach, the liabilities would not be central bank money, as holders would not have a direct claim they could assert against the central bank, only against the CBDC intermediary.

<sup>121</sup> *ibid.*

<sup>122</sup> BIS Annual Economic Report (2021).

<sup>123</sup> Board of Governors of the Federal Reserve System (2022).

makes the payment system more efficient by allowing money to move freely throughout the economy.”

The BIS describes this concept more broadly as “interoperability”, emphasising its importance among central banks: “Another new survey question showed that most central banks (76 %) working on a retail CBDC are exploring interoperability with existing payment system(s). Interoperability can encourage the adoption of CBDCs and enable the coexistence of central bank and commercial bank money. Payment system interoperability enables banks and other payment service providers (PSPs) to make payments across systems without participating in multiple systems. This would allow end users to seamlessly move their money in and out of their CBDC accounts, for example from and to their commercial bank accounts using a credit card or electronic money transfer.”<sup>124</sup>

Prior literature tends to frame interoperability in operational and functional terms, referring to it as “technical, semantic and business compatibility that enables a system to be used in conjunction with other systems.”<sup>125</sup> However, interoperability includes important legal dimensions – in particular, to support transferability and convertibility of CBDC within a jurisdiction’s domestic payment system, as well as for cross-border CBDC payments, as a foundational matter.

The importance of a sound legal framework underpinning any potential CBDC arrangement in the US context is discussed further in a note by one of the authors: “A principal role of the Federal Reserve in the U.S. financial system is to be the guardian of public confidence in money; thus a sound legal framework is a key precondition. It serves as the bedrock that enables users of a general-purpose CBDC and the market more broadly to be confident that the instrument they use to transfer value is robust and reliable, functions smoothly and securely, and comes with clear rules and protections for the payment recipient and for the consumer. Any cracks would undercut the public's trust in the CBDC.”<sup>126</sup>

Indeed, like other jurisdictions, the legal framework underpinning the US payment system has evolved over time, and any issuance of a CBDC would be a significant change. A retail CBDC would more effectively yield public benefit if it results in new services and products that are well understood and safely constructed, and that “interoperate” well with existing forms of money, particularly from a legal standpoint. Along these lines, in its 2022 report to the G20, the BIS has identified five evaluation criteria for analysing various CBDC arrangements: (1) do no harm, (2) enhancing efficiency, (3) increasing resilience, (4) assuring coexistence and interoperability with non-CBDC systems, and (5) enhancing financial inclusion.<sup>127</sup> To meet these criteria, it is critical to understand the core tenets of safety and efficiency inherent in the US payment system's current design – in particular, the legal foundations for the critical tenet that “one dollar” has a singular meaning of “one dollar” in whatever form it takes.

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<sup>124</sup> BIS Annual Economic Report (2021).

<sup>125</sup> CPMI, BISIH, IMF, World Bank Group (2022).

<sup>126</sup> Cheng, Lawson, Wong (2021).

<sup>127</sup> CPMI, BISIH, IMF, World Bank Group (2022).

## 3

## Payment system safety and efficiency

A central bank's bridging role in the domestic payment system provides customers of different commercial banks with an efficient means to make payments to each other, underpinned by a legal framework that allows these individual bank "networks" to "interoperate."

Today, a given jurisdiction's payment system reflects a public-private partnership, working in two tiers. The central bank provides accounts and services to commercial banks and certain other financial institutions. They, in turn, provide financial services to consumers and businesses, subject to regulation and supervision by financial authorities.

### 3.1

### The tiered structure of money

With respect to the various forms of "money" widely used by the general public, this tiered structure is reflected in the balance sheets of the central bank and commercial banks. Booked on the central bank balance sheet are the forms of money that are liabilities of the central bank – for example, physical banknotes and master account balances of commercial banks with the Federal Reserve. Parties can transact in central bank liabilities with confidence in their acceptance and lack of credit risk.

Regarding physical banknotes, for example, the Lawyer's Perspective Note explains further: "Historically, federal statutes had specified a formal gold or silver content for the dollar, but these statutes were rendered obsolete when the United States abandoned the domestic gold standard with the passage of the Gold Reserve Act of 1934 and demonetized silver in the 1960s. Although the dollar as a standard unit of value has been defined in the past in terms of a gold or silver content, today there is no requirement that the monetary system of the United States consist of gold and silver coin or of currency backed by gold or silver. Rather, a Federal Reserve note is readily able to be exchanged for goods and services because, as a legal matter, it is an obligation of the United States and backed by the full faith and credit of the U.S. government. This confidence is reinforced by the Federal Reserve Act's prescription that whenever currency is issued by the Federal Reserve, the issuing Federal Reserve Bank (Reserve Bank) posts collateral equal to 100 per cent of the value of the notes issued."<sup>128</sup>

Moreover, the more parties use and transact in these physical banknotes, the more useful it becomes, and in a virtuous circle, more parties will in turn seek to use physical banknotes in more transactions — a phenomenon known as "network effects", which can in turn bring efficiencies. The legal framework plays an important role in reinforcing the efficiencies from network effects, as the authors have discussed in the Lawyer's Perspective Note: "The stability and uniformity in the legal treatment of various denominations of U.S. currency also leads to efficiencies and a type of network effect. If a merchant accepts a \$100 bill today from a customer, it does not need to assess whether that \$100 bill will need to be converted to some other form, possibly at some discounted rate, when it tries to use it to, say, pay wages to its employees tomorrow. Nor does the merchant face the risk that its holdings of Federal Reserve notes would be greater or less depending on the exact type of note it holds (a

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<sup>128</sup> Cheng and Torregrossa (2022).

hundred \$1 bills or a single \$100 bill). Each U.S. dollar is "money good" in the literal sense, so payments in physical dollars happen without friction."<sup>129</sup>

Of course, holdings of physical banknotes by the general public for their routine transactions are relatively small. Rather, it is deposits at private-sector commercial banks that are by far the more prevalent form of money held and widely used by the public. A deposit with a bank is a liability of that bank. If a depositor has an account with a bank, that means the depositor has a right to assert a claim against the bank for the value of the deposit. Importantly, a depositor holds a contract right in the form of a promise to pay from the bank to the depositor, rather than any property right to specific bank assets.

Thus, in a number of ways from both a legal and a practical standpoint, bank deposits could be viewed as a "network of money" in the domestic payment that is separate from physical banknotes like Federal Reserve notes and other liabilities on a central bank's balance sheet. From a legal standpoint, as the authors have explained in the Lawyer's Perspective Note: "The law treats a bank deposit ... differently from a Federal Reserve note ... A Federal Reserve note is payable in its face amount to the bearer on demand, which means that an individual lawfully in possession of the note may be regarded as the owner of the note. Like other bearer instruments, an individual who loses a Federal Reserve note or has it stolen may suffer financial loss. The Federal Reserve will not replace it; if currency is stolen, the individual's recourse is generally limited to pursuing a civil or criminal action against the thief. In contrast, a bank deposit is a contractual relationship that a depositor has with their bank. For individuals, this relationship carries certain legal protections, like the consumer protections against errors and fraud under the Electronic Fund Transfer Act. If a payor were to wire money through its bank to a payee who maintains an account with a different bank, what happens is not a transfer of property from the hands of payor to payee, as it would be in a payment of Federal Reserve notes. Rather, it is a shifting of bank liabilities: the payor's claim against its bank decreases and the payee's claim against its bank increases, in the amount of the payment ..."<sup>130</sup>

Conceptually, when one uses physical banknotes such as Federal Reserve notes to purchase a good or service, one could be said to be using the "central bank network", so to speak, whereas when one makes payment from one's deposit account at a commercial bank (such as by using a debit card), one could be said to be using the "commercial bank network", so to speak.

## 3.2 The role of the central bank

Importantly, while deposit claims against commercial banks and Federal Reserve notes could each be viewed as distinct "networks" of money, subject to different legal frameworks, they nevertheless "interoperate" such that both function as money to a generally equal degree in practice. This bridge between different networks of money

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<sup>129</sup> *ibid.*

<sup>130</sup> *ibid.*

exists in large part because of the role a given jurisdiction's central bank plays in the domestic payment system.

As the authors have explained in the Lawyer's Perspective Note: "[T]he Federal Reserve, through commercial banks, helps enable the public to convert bank deposits into cash, and vice versa. When individuals or businesses want cash, they obtain it by drawing on their deposits at commercial banks. The banks, in turn, can obtain their cash from the Federal Reserve, at which banks may maintain their own deposit accounts known as "master accounts." When individuals or businesses no longer want the cash they have on hand, they can deposit the excess in banks, and the banks can subsequently deposit any excess with the Federal Reserve. This "elasticity" of the currency supply was a primary objective of the Congress when it passed the Federal Reserve Act in 1913."<sup>131</sup>

Thus, central banks like the Federal Reserve buttress the interoperability between the "commercial bank network" of money and the "central bank money network" of money by supporting their conversion – that is, providing services to commercial banks that withdraw or deposit cash, which indirectly helps enable members of the general public to convert bank deposits into physical banknotes, and vice versa.

Beyond supporting the interoperability of the "commercial bank network" and the "central bank network" of money through this conversion mechanism, central banks like the Federal Reserve play another important bridging role in their domestic payment system's interoperability. Within the "commercial bank network" of money, customers of different commercial banks could each be viewed using separate "sub-networks" of money, so to speak. For example, all customers that have deposit accounts at Alpha Bank could be viewed as users of the "Alpha Bank sub-network" of commercial bank money, whereas all customers that have deposit accounts at Beta Bank are users of the "Beta Bank sub-network" of commercial bank money. Each bank is easily capable of executing transfers on its own books between its own customers – an on-us, intrabank transfer.

Yet, what if a payor who maintains a deposit account at Alpha Bank seeks to make payment to a payee who maintains a deposit account at Beta Bank? Alpha Bank would debit the deposit account of its customer, and Beta Bank would credit its customer's deposit account – but how would Alpha Bank and Beta Bank communicate and settle with each other?

Here, the central bank plays an important bridging role that supports the interoperability of these commercial bank "sub-networks" of money by enabling transferability, through central bank-operated payment services such as the Federal Reserve's Fedwire Funds Service. Specifically, Alpha Bank would pay Beta Bank through the Federal Reserve, which would typically process a transaction by receiving instructions from Alpha Bank, delivering instructions to Beta Bank, and settling the amount of a transaction by effecting changes to the banks' master account

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<sup>131</sup> *ibid.*

balances.<sup>132</sup> Viewed through the lens of "network effects" and "interoperability", the accounts and payment services that the Federal Reserve provides help to bridge these individual commercial bank "sub-networks" and allow them to "interoperate" by enabling safe and efficient payment transfers to flow between commercial banks. This interoperability, in turn, enhances the networks effects for each commercial bank that a single one would not be able to achieve on its own.

Taken together, the Federal Reserve's bridging role in this context – that is, by supporting transferability between the "sub-networks" of commercial bank money or a given payment instrument – provides customers of different commercial banks with an efficient means to make payments to each other, underpinned by a legal framework that allows these individual bank "networks" to "interoperate."

Of course, the central bank is not necessarily unique in this context of supporting transferability. The private sector plays an important complementary role in connecting commercial bank "sub-networks". As highlighted in the Lawyer's Perspective Note: "It is important to note that other private-sector payment systems can play a similar bridging role. Even still, to help ensure that they function safely and efficiently, these systems may rely on prefunded Reserve Bank balances to back or effect interbank settlement. The reliance of these private-sector arrangements on the Federal Reserve underscores the important and unique role the central bank plays in the U.S. payment system: it brings network efficiencies as well as safety, in the form of settlement on the central bank's balance sheet. At the same time, central bank money does not stifle responsible innovation by crowding out or supplanting private-sector institutions that offer their own advantages in meeting customer needs."<sup>133</sup>

In short, a retail domestic payment system today essentially operates as an array of various networks, consisting of the "central bank network" of money in the form of physical banknotes and the "commercial bank network" of money in the form of deposit account balances. The latter is scattered across individualised "sub-networks" of commercial bank money, operated by each bank. Whether it is supporting the convertibility between these different networks of widely used money or the transferability across different sub-networks of commercial bank money, the central bank and its payment services (such as ACH, wires, checks, and instant payment services operated by the central bank) serve as the "hub" that links everything together.

It is thus no insignificant matter when a central bank like the Federal Reserve expands the scope of the commercial banks and financial institutions that it connects – that is, expanding the breadth of convertibility and transferability that it enables. For example, in the United States, Congress amended the Federal Reserve Act in 1980 to broaden the Federal Reserve's authority to make all depository institutions eligible for master accounts with and financial services from a Federal Reserve Bank. This expansion brought more financial institutions, particularly thrifts and credit unions, into the Federal Reserve "network." The result of that historic instance was the creation of

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<sup>132</sup> In particular, this would entail a decrease to the Reserve Bank's liability to Alpha Bank as reflected in its master account balance and an increase to the Reserve Bank's liability to Beta Bank as also reflected in its master account balance.

<sup>133</sup> Cheng and Torregrossa (2022).

nationwide reach for the domestic ACH system, particularly because the Federal Reserve could interoperate with other private-sector clearinghouses. Thus, not only did the central bank expand the scope of financial institutions for which it could enable transferability, it could also exchange messages with other ACH operators. The end-result was a level of network effects in the ACH network that a single operator might never have achieved on its own. Thus, even today, the use case for a 50-year-old system like ACH is still compelling, particularly for recurring payments, because the reach of the domestic network is so broad through this interoperability.

Historically in the United States, Congress has over time expanded the scope of the Federal Reserve “network”, with this expansion motivated not only by efficiency but also by safety and at times other policy considerations, as illustrated in Table 1.

**Table 1**  
Policy-driven expansion of the Federal Reserve “network”

Year	Milestone
1913	Congress created the Federal Reserve System, giving the Reserve Banks the authority to establish deposit accounts for Reserve Bank members and a nationwide cheque-clearing system (as well as to issue Federal Reserve notes). In doing so, Congress put the Reserve Banks at the centre of what was then a fractured payment system, in order to, among other things, improve its functioning to make the system more efficient and eliminate interbank settlement risk to make the system more stable.
1917	The Federal Reserve Act was amended to authorise the Reserve Banks, for collection purposes, to accept deposits of cash and cheques from any bank or trust company, regardless of whether the institutions were members of the Federal Reserve System. This amendment in essence served to create deeper reach for the ‘network’ with respect to the Reserve Banks’ cheque-collection service, helping to meet Congress’s goal of universal par clearing of cheques.
1978	The ‘network’ was further expanded when Congress added US branches and agencies of foreign banks to the list of institutions that expressly could access Reserve Bank accounts and services, in connection with the policy goal of treating branches and agencies of foreign banks like their domestic counterparts. This expansion of the network also came with expanded oversight of the activities of these branches and agencies by the federal banking agencies.
1980	Congress again reconsidered the scope of the ‘network’, in connection with the revisions to the Federal Reserve’s monetary policy authorities. With the passage of the Monetary Control Act 1980, Congress expressly made all depository institutions — entities that are almost all subject to federal oversight — eligible to access Reserve Bank master accounts, payment services and the discount window. In a balancing of various policy trade-offs (including giving thrifts and credit unions direct access to the Federal Reserve ACH network, without having to rely on commercial correspondent banks), these same institutions also became subject to Federal Reserve authority to set reserve requirements — a critical monetary policy tool of the time.
2010	The ‘network’ was expanded further, with the policy goal of promoting financial stability. In connection with the financial crisis and the adoption of the Dodd-Frank Wall Street Reform and Consumer Protection Act, Congress further expanded the scope of the ‘network’ to designated financial market utilities, which would also become subject to federal oversight when so designated by the Financial Stability Oversight Council.

Quoted from the Lawyer’s Perspective Note

These historical points of comparison and the central bank’s role today as a network “hub” are informative as the world looks ahead and considers retail CBDCs,

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particularly interoperability among intermediaries' platforms and customer bases – as well as the legal underpinnings.

### 3.3 The concept of legal interoperability

Critical to the interoperability of commercial bank networks today is the legal framework that underpins it. As the authors have explained in the Lawyer's Perspective Note: "Different forms of electronic interbank transfers (for example, an ACH payment or a wire transfer) may have different underlying legal bases and may be conducted in different ways from an operational standpoint, but each is in essence a shift in bank liabilities and corresponding interbank settlement based on instructions communicated between banks, allowing banks like Alpha Bank and Beta Bank to pay each other."<sup>134</sup>

In other words, from a legal perspective and considering the US payment system as a whole today, whether it is a transaction involving ACH, a wire transfer, or even cash – these different forms of payment have different underlying legal bases and may be conducted in different ways from an operational standpoint, but each enables the discharge of an underlying obligation, the essence of what it means to make a payment, to pay a debt. It is this critical concept that could be viewed as "legal interoperability" in the domestic payment system – this ability for users to smoothly and efficiently choose between arrangements subject to different legal frameworks, while being confident the arrangement will, like all forms of money, serve as a way to make a payment.

In particular, this "legal interoperability" is a necessary foundation for the critical transferability and convertibility functions of the central bank discussed earlier. A central bank enables transferability by supporting the interoperability of individual commercial bank "sub-networks" of money through central bank-operated payment services such as ACH, wires, checks, and instant payment services. In this context, "legal interoperability" is embodied in commercial rules and contract terms that are not necessarily identical but are at least consistent and clear, providing legal certainty, on important aspects of the arrangement (such as the funds transfer mechanism, settlement finality, and the handling of error or delay, fraud, and theft).

As discussed earlier, the central bank also plays a critical role in supporting interoperability through enabling convertibility between networks of widely used money, currently deposits with commercial banks and physical banknotes and, possibly in the future, a retail CBDC. Commercial banks that receive central bank services to withdraw or deposit cash (and perhaps, one day, retail CBDC) will seek legal clarity and certainty that the central bank will support conversion at par. In this way, "legal interoperability" supports fungibility across networks of widely used money.

Taken together, these forms of "legal interoperability" bring even more efficiencies to users of the payment system, as it amplifies the network effects of each individual network. Though complex, the domestic payment system is able to function smoothly

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<sup>134</sup> *ibid.*

and safely largely because of the central bank's role as a network hub that supports safe and efficient interoperation of the system's component parts. From a legal perspective, although different legal bases underpin different arrangements, a given jurisdiction's payments law as a whole – that is, commercial law, the regulatory regime, and the supervisory framework – provides certainty and predictability that "one dollar" has a singular meaning in whatever form it takes.

### 3.4 Looking ahead

Today, as jurisdictions are considering new forms of money, namely retail CBDCs, threshold questions such as the legal characterisation of a CBDC, particularly if it is a sui generis asset, and the role of intermediaries' platforms will have important implications. Beyond first order considerations such as whether there is clear legal authority to issue a retail CBDC (that is, whether any issuance would be consistent with the central bank's mandates, functions, and powers as enshrined in the central bank law), critical first steps toward building a robust legal framework to underpin a CBDC include addressing critical legal issues:

“Anti-money laundering, countering the financing of terrorism, and addressing sanctions evasion. It is critical that such a legal framework, as a precondition, includes approaches to combatting money laundering and countering the financing of terrorism so as to mitigate the risk that the CBDC could become a favoured medium for illicit activities, particularly given the ease and speed at which potentially large amounts of money could be transferred. As a point of comparison, illicit activities in connection with virtual currencies are not just limited to direct use in transactions to commit crime or to support terrorism (such as buying and selling illicit things), but also include use by bad actors to launder their illicit proceeds or hide financial activity from authorities (such as law enforcement, national intelligence, tax, or economic sanctions authorities).

At the same time, it will be essential to consider how privacy is respected and how personal data is protected in a CBDC arrangement. Legal requirements vary, depending on the role a particular party plays in handling or processing a payment transaction—whether the party is a bank, service provider to a bank, affiliated party, or communication provider. Depending on the design of a CBDC and the extent of the central bank's role in the arrangement, the central bank could have access to an unprecedented scale of granular transaction information; possibly, transactional data could be available to certain third parties (like banks and service providers) or, in the extreme, to everyone. This close linkage between money and data contrasts with physical banknotes, which do not carry with them transaction data that can be connected to a specific person and their history of financial dealings.

Legal roles and responsibilities. Furthermore, a general-purpose CBDC may call for the central bank to step into roles and responsibilities with respect to the general public that are generally shouldered today by private-sector banks vis-à-vis their customers. As a consequence, it would become vital to address issues concerning the risks to be managed by the central bank under applicable law, including the gamut of

legal responsibilities associated with the CBDC (namely with respect to anti-money-laundering, economic sanctions, privacy, and data security) that may be allocated to it.

In addition, a legal framework should equitably allocate loss for instances when things go awry – such as operational failures like error or delay, fraud, theft, or bankruptcy and insolvency – with clarity and predictability to reinforce public trust and market confidence in a CBDC. With respect to wholesale payments today, payments law provides loss allocation regimes that are calibrated to incentivise parties to take steps to minimise the chance of the loss occurring in the first place (for example, assign the risk of loss to the party in the best position to control it) or minimise the loss borne by individual transacting parties (for example, spread the burden of the loss). However, for a CBDC expected to be used by individuals and businesses, the question of how loss should be allocated will raise important questions beyond who is most able to manage the risk – what allocation is realistic and, importantly, fair?”<sup>135</sup>

In the United States, like other jurisdictions, investment securities went through a similar digital transition decades ago, moving away from paper to electronic records. Traditionally, securities were tangible, namely paper documents that incorporated rights, and the law of securities has been transformed to keep pace with dematerialisation.<sup>136</sup>

However, there is an important distinction in the realm of money, where interoperability is critical to the safety and efficiency of the payment system as a whole. A retail CBDC would not necessarily serve the payment system well if it results in new services that are poorly understood by the general public and that does not “interoperate” well with the existing forms of money, particularly from a legal standpoint.

Thus, a critical policy and legal consideration from a domestic standpoint would be how to most effectively integrate any retail CBDC into the existing payment system. In 2003, the Committee on Payment and Settlement Systems of the Bank for International Settlements concluded that an extreme outcome where a retail CBDC displaces all commercial bank money and the central bank acts as the sole issuer of money would unlikely be sufficiently stable or efficient to endure.<sup>137</sup> These concerns continue today, though the Fed CBDC Paper noted that these concerns could possibly be mitigated by CBDC design choices, such as having a CBDC be non-interest-bearing and subject to quantity limits (i.e., limits on the amount of CBDC that could be held by a single holder).

Rather, the questions of the day around CBDC tend to focus on interoperability at the domestic level – such as how to calibrate the public-private partnership in a CBDC arrangement, how to enable CBDC transferability between users of different intermediaries, and how to support conversions between CBDC and existing forms of money, for example. These are not necessarily new problems. The central bank’s

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<sup>135</sup> Cheng, Lawson and Wong (2021).

<sup>136</sup> Garrido, Liu, Sommer and Viancha (2022).

<sup>137</sup> CPSS (2003).

historic role as a “network hub” has long served as a strong foundation for interoperability in the domestic payment system, and useful lessons could be leveraged from the historic evolution of payment systems and the policy considerations at each decision point.

## 4 Conclusion

In introducing a new “dimension” of money into the payments multiverse, the lessons of the past and core tenets of efficiency and safety inherent in the domestic payment system’s current design can help inform policy decisions.

This note has whipped through various planes of existence in the multiverse of payments. In introducing a new “dimension” of money – in the form a retail CBDC, with new types of intermediaries with novel roles and responsibilities – into the payments multiverse, the lessons of the past and core tenets of efficiency and safety inherent in the domestic payment system’s current design can help inform policy decisions. Rather than reinvent the wheel, consider instead reinforcing the network effects and continuing to build upon the “legal interoperability” – which provides a stable foundation of legal clarity and certainty to underpin convertibility and transferability across the system’s widely-used forms of money. This legal foundation and the network effects enabled by it currently serve the domestic payment system well. Such an approach would enable the financial system and the public that the system serves to have greater choice in the safest and most efficient means to hold money and pay.

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# Legal interoperability of retail CBDCs: initial considerations

By Panagiotis Papapaschalis\*

Interoperability is a technical notion with which experts in financial market infrastructures (FMIs) have been conversant for the past few decades. However, interoperability between legal tender cash issued by different central banks has been a moot issue. Banknotes and coins being physical, material things (*res*), their exchange could only take place physically, i.e. through tendering to a credit institution or a *bureau de change* – a tedious business. Digitalisation of legal tender cash submits the latter to issuance, clearing and settlement through an *infrastructure* of some sort, thus rendering interoperability an advantageous option, and a constitutive part of the business case for digitalisation.

## 1 Legal Interoperability: definition, relevance, desirability

In an EU context, the notion of interoperability has only found its way in FMI-related legal texts relatively recently, in 2009. Thus, the amended Settlement Finality Directive<sup>138</sup> defines interoperable systems as “two or more systems whose system operators have entered into an arrangement with one another that involves cross-system execution of transfer orders”. In the same vein, three years later, the European Market Infrastructure Regulation<sup>139</sup> defines, in the context of a particular FMI, central clearing counterparties, an interoperability arrangement as “an arrangement between two or more CCPs that involves a cross-system execution of transactions”. Therefore, at this early stage, the emphasis has been on a (technical and legal) arrangement between two system operators, ensuring that transactions introduced in one system could settle in the other. However, the law did not specify the elements of such an arrangement or the need for its standardisation.

Two years further down the road, but solely as regards central securities depositories (CSDs) and securities settlement systems, the CSD Regulation<sup>140</sup> requires (Article 48) that interoperable securities settlement systems and CSDs, which use a common

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<sup>138</sup> Directive 98/26/EC of the European Parliament and of the Council of 19 May 1998 on settlement finality in payment and securities settlement systems (OJ L 166, 11.6.1998, p. 45). The definition of interoperability was introduced in 2009, by means of Directive 2009/44/EC of the European Parliament and of the Council of 6 May 2009 amending Directive 98/26/EC on settlement finality in payment and securities settlement systems and Directive 2002/47/EC on financial collateral arrangements as regards linked systems and credit claims (OJ L 146, 10.6.2009, p. 37).

<sup>139</sup> Regulation (EU) No 648/2012 of the European Parliament and of the Council of 4 July 2012 on OTC derivatives, central counterparties and trade repositories (OJ L 201, 27.7.2012, p. 1).

<sup>140</sup> Regulation (EU) No 909/2014 of the European Parliament and of the Council of 23 July 2014 on improving securities settlement in the European Union and on central securities depositories and amending Directives 98/26/EC and 2014/65/EU and Regulation (EU) No 236/2012 (OJ L 257, 28.8.2014, p. 1).

settlement infrastructure, “establish identical moments of: (a) entry of transfer orders into the system; [and.] (b) irrevocability of orders”. Hence, and while the onus of achieving interoperability is left to the operators of the relevant systems, mere cross-system execution of transactions no longer suffices.

Lastly, in the context of payments and the interlinking of online payment service providers (PSPs), the second Payment Services Directive<sup>141</sup> (recital 93 and Article 98) explicitly entrust the European Banking Authority with the task “to specify the requirements of common and open standards of communication to be implemented by all account servicing payment service providers that allow for the provision of online payment services. This means that those open standards should ensure the interoperability of different technological communication solutions”. The ensuing regulatory technical standards<sup>142</sup> emphasise the importance of standardisation (through standards of communication developed by international or European organisations) for achieving interoperability of different communication solutions. With this further evolutionary step, agreements between operators no longer suffice – adherence to broader standards is key.<sup>143</sup>

Particularly this last development shows the increasing relevance of interoperability in the context of retail central bank digital currencies (CBDCs). Under the plausible assumption that they will be deployed as schemes<sup>144</sup>, “establish[ing] a set of common operational rules and technical standards that intermediaries would need to follow in order to provide digital ... solutions to end users”, retail CBDCs will already need to cater for internal interoperability. Interoperability among retail CBDCs is but a subsequent step, enabling payments among different currencies to and from intermediaries belonging to different schemes.

Finally, interoperability of retail CBDCs is not only desirable because it connects, but also because it adds value through its ability to segregate. Recent events such as the war in Ukraine and the subsequent complexity of disconnecting individual Russian banks from SWIFT’s network showcase this<sup>145</sup>.

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<sup>141</sup> Directive (EU) 2015/2366 of the European Parliament and of the Council of 25 November 2015 on payment services in the internal market, amending Directives 2002/65/EC, 2009/110/EC and 2013/36/EU and Regulation (EU) No 1093/2010, and repealing Directive 2007/64/EC (OJ L 337, 23.12.2015, p. 35).

<sup>142</sup> Commission Delegated Regulation (EU) 2018/389 of 27 November 2017 supplementing Directive (EU) 2015/2366 of the European Parliament and of the Council with regard to regulatory technical standards for strong customer authentication and common and secure open standards of communication, C/2017/7782 (OJ L 69, 13.3.2018, p. 23).

<sup>143</sup> For a discussion on the trend toward broader standardisation, spreading from the financial sector to the manufacturing and retail sectors, Bank of Japan, Interoperability and Standardization in Financial Services in the Digital Age, 04.2022 available at: <https://www.boj.or.jp/en/research/brp/psr/data/psrb220427.pdf> p. 11 et seq.

<sup>144</sup> Panetta, F., Building on our strengths: the role of the public and private sectors in the digital euro ecosystem, Introductory statement, at the Committee on Economic and Monetary Affairs of the European Parliament, 29 September 2022, available at: <https://www.ecb.europa.eu/press/key/date/2022/html/ecb.sp220929~91a3775a2a.en.html>

<sup>145</sup> Compare e.g. the measures applying to disconnection from SWIFT versus the total prohibition of export of euro banknotes, in Articles 5h and 5u of Council Regulation (EU) No 833/2014 of 31 July 2014 concerning restrictive measures in view of Russia’s actions destabilising the situation in Ukraine (OJ L 229, 31.7.2014, p. 1).

## 2 Assumptions and exclusions

This paper assumes a retail CBDC, i.e. a liability of a central bank, irrespective of its legal nature or medium, that has legal tender status in order to be interoperable with other CBDCs in their native jurisdictions. Moreover, this analysis focuses on interoperability among retail CBDCs, and not the mere use of a domestic CBDC abroad or the interoperability between CBDC and (i) cash of the same currency or (ii) other, privately issued digital assets. As with cash, use of a domestic CBDC abroad is in principle legally feasible on a *voluntary* basis (contractual freedom). It may also be rendered mandatory depending on the personal (as opposed to purely territorial *lex monetae*) scope of a CBDC attributed by the *lex fori*. However, this does not require any interoperability arrangement.

Interoperability between a CBDC and its corresponding cash must be guaranteed by the issuing central bank because it is a means to achieve *full fungibility*, i.e. conversion at par between concurrent yet different manifestations of legal tender, and to enable the funding of CBDC accounts or wallets through cash.

Interoperability between a CBDC and private means of payment boils down to a question of access of providers to the digital currency infrastructure – an issue hinted upon in the previous heading but requiring a separate analysis in its own right.<sup>146</sup>

## 3 Designing interoperable CBDCs

### 3.1 A general central bank obligation to make currencies interoperable?

Interoperability of CBDCs may, in a global context, contribute to further liberalisation of capital flows or, in the EU context, achievement of the free movement of capital.

However, at present, there is no concrete legal obligation for central banks to render their digital currencies interoperable. A decision on the desired degree of interoperability thus has to be reached in view of each individual central bank's mandate and competences, in particular with regard to monetary policy and the operation of financial market infrastructures. To the extent that interoperability can lead to large sums of a CBDC held or spent outside the native jurisdiction or currency area, the financial stability of both such jurisdictions could be at stake. This renders the involvement of both central banks – and, potentially, the concurrent involvement of authorities (co-)responsible for financial stability – necessary.

Moreover, in the EU context, unlimited and unconditional EU-wide interoperability of a digital euro could be considered an infringement of the Treaties, to the extent it

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<sup>146</sup> See, e.g. UK Finance, Designing Interoperability for a potential UK CBDC, 07.2022, available at: <https://www.ukfinance.org.uk/policy-and-guidance/reports-and-publications/designing-interoperability-potential-uk-cbdc> p. 5 et seq. defining both interoperability and fungibility more broadly; Brunnermeier, M.K., James, H., Landau, J.P., The Digitalization of Money, NBER Working Paper No. 26300, 09.2019, available at: [https://www.nber.org/system/files/working\\_papers/w26300/w26300.pdf](https://www.nber.org/system/files/working_papers/w26300/w26300.pdf) p. 17 et seq. discussing the problem of large private platforms being reluctant to interoperate.



circumvents the convergence criteria imposed therein on Member States with a derogation to accede to the euro area<sup>147</sup>.

To sum up, interoperability can be neither mandatory nor unilateral – but must be based on competence and consensus.

## 3.2 Potential designs: conceptual models

The Bank for International Settlements (BIS) Innovation Hub has presented a seminal report on CBDC interoperability<sup>148</sup>, distinguishing between the following conceptual models for the design of interoperable CBDCs:

- (a) the compatible model: individual CBDC systems using common standards, such as message formats, cryptographic techniques and data requirements, to reduce the operational burden on PSPs for participating in multiple systems;
- (b) the interlinked model: individual CBDC systems being linked (bilaterally or through a single access point<sup>149</sup>) with a set of technical and contractual agreements that not only facilitate communication and exchange of data, but can also facilitate compliance, foreign currency provision and settlement;
- (c) the single system model: individual CBDCs using a single common technical infrastructure and potentially also a common rulebook.

## 3.3 Potential designs: legal archetypes

Translating the above concepts into legal architecture, and after having established that interoperability can be neither mandatory nor unilateral, two archetypal legal designs are envisageable:

*First*, a multilateral agreement establishing either a single global point of issue for all retail CBDCs and a contingent central node, through which the exchange of retail CBDCs takes place, or merely such a central node. A single global point of CBDC issue (akin to a single CSD for all the world's securities) is unprecedented<sup>150</sup>.

<sup>147</sup> Article 140(1) TFEU and Protocol (13) to the TFEU.

<sup>148</sup> Bank of International Settlements, Committee on Payments and Market Infrastructures, Report to the G20: Options for access to and interoperability of CBDCs for cross-border payments, 07.2022, available at: <https://www.bis.org/publ/othp52.pdf>. The options were, however first presented in Auer, R., Haene, P. and Holden, H., Multi-CBDC arrangements and the future of cross-border payments, BIS Paper, no 115, March 2021; for a list of examples based on these models, see World Economic Forum, White Paper: Defining Interoperability, 11.2021, available at: [https://www3.weforum.org/docs/WEF\\_Defining\\_Interoperability\\_2021.pdf](https://www3.weforum.org/docs/WEF_Defining_Interoperability_2021.pdf) at pp. 9-10.

<sup>149</sup> For a description of such an arrangement see Christodorescu, M. et al., Universal Payment Channels: An Interoperability Platform for Digital Currencies, 09.2021, available at: <https://doi.org/10.48550/arXiv.2109.12194> pp. 5-8.

<sup>150</sup> See Bank of International Settlements, Committee on Payments and Market Infrastructures, Report to the G20: Central bank digital currencies for cross-border payments, 07.2021, available at: <https://www.bis.org/publ/othp38.pdf> at p. 3, optimistically describing this state of affairs as an opportunity to start with a “clean state”.

However, the inspiration for a mere central node exists (albeit not in a retail context). Continuous Linked Settlement (CLS) already settles foreign exchange transactions individually in gross terms, with payments settled payment versus payment via national central bank accounts. This archetype corresponds to both the single system and part of the interlinked models above.

*Second*, bilateral contractual arrangements through which two central banks issuing CBDCs fix the modalities and limits of granting access to (at least one of) their CBDC infrastructures. A fitting example already exists in the field of instant payments, where the ECB and the Sveriges Riksbank concluded a cooperation agreement offering Sweden access to the Eurosystem's TARGET Instant Payment Settlement (TIPS) to support the Swedish instant payment service, called RIX-INST<sup>151</sup>. This archetype corresponds to part of the interlinked model above.

The compatible model does not correspond to any of the archetypes as it seems to be based on soft agreements and best-efforts undertakings. Central banks voluntarily concert to a given standard – but are not legally obliged to continuously adhere to it. Also, this system does not lead to true interoperability, since it merely facilitates PSP participation in multiple systems through reduction of the operational burden but does not eliminate this requirement.

### 3.4 Feasibility – legal impediments

Generally speaking, the more numerous the parties to a negotiation, the more difficult it is to reach a (meaningful) agreement, unless one party has a dominant position and is able to impose its terms. Corporate seats or centres of operations and the law applicable to the arrangement are bound to become bones of contention, as they give one of the jurisdictions physical control over premises and judicial control via its legal system.<sup>152</sup> Even under the assumption that a meaningful agreement on the functioning of the platform is reached, attributing governance and control in the medium to long term and catering for crisis situations affecting some jurisdictions more than others may prove challenging<sup>153</sup>. If one adds to the above the fact that a single point of issue or a central node may become, from a cyber-security viewpoint, a *single point of failure*, the difficulties and requirements of establishing a multilateral arrangement can be well understood.

Bilateral arrangements on the other hand are easier to reach. Contractual freedom allows for tailor-made agreements between various parties, reflecting each party's

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<sup>151</sup> [https://www.ecb.europa.eu/press/pr/date/2020/html/ecb.pr200403\\_1~302d8928e3.en.html](https://www.ecb.europa.eu/press/pr/date/2020/html/ecb.pr200403_1~302d8928e3.en.html). TIPS may also interoperate to secure DVP of assets in a DLT platform; see La Rocca, R., et al. Integrating DLTs with market infrastructures: analysis and proof-of-concept for secure DVP between TIPS and DLT platforms in Banca D'Italia; and Mercati, infrastrutture, sistemi di pagamento Nr 26, 07.2022, available at: <https://www.bancaditalia.it/pubblicazioni/mercati-infrastrutture-e-sistemi-di-pagamento/approfondimenti/2022-026/index.html?com.dotmarketing.htmlpage.language=102>

<sup>152</sup> Zetsche, D., et al., DLT-Based Enhancement of Cross-Border Payment Efficiency – a Legal and Regulatory Perspective, BIS Working Papers No 1015, 05.2022, available at: <https://www.bis.org/publ/work1015.htm> at p. 14.

<sup>153</sup> Similarly, see Bank of International Settlements, Committee on Payments and Market Infrastructures, Report to the G20: Options for access to and interoperability of CBDCs for cross-border payments, 07.2022, available at: <https://www.bis.org/publ/othp52.pdf> at p. 25.

needs and negotiating clout. Feasibility, however, comes at the cost of fragmentation of interoperability arrangements, which reduces their efficiency.

Moreover, and besides the abovementioned commonplaces affecting practical feasibility, a number of legal impediments also needs to be bypassed. The most salient thereof are discussed below.

### 3.4.1 Central bank mandate(s)

Above it was already hinted that a decision on the desired degree of interoperability has to be reached in view of a central banks' mandate and competences<sup>154</sup>. This echoes recent research by the International Monetary Fund on CBDCs<sup>155</sup> according to which “[w]hether the issuance of CBDC falls under the mandate of a central bank requires an analysis of the central bank law’s provisions concerning two aspects of its mandate, namely its functions (sometimes also called “tasks” or “duties”) –“what” a central bank must do to achieve its objectives – and its powers – “how” a central bank can act to implement its functions.” If a central bank cannot even *establish* a CBDC, for instance, because its statutes include a narrow function to issue *banknotes and coins* and no power to issue *currency*, then examining whether its CBDC can be rendered interoperable would be a moot point. If it is concluded that a central bank may issue CBDC, care needs to be taken that its *payment system function* extends beyond interbank systems<sup>156</sup>. Needless to say, for multilateral interoperability, the above checks must be performed on, and, if need be, legislative amendments must be made to, the mandate of all participating central banks.

### 3.4.2 Legal nature of CBDCs

Due to the novelty of CBDCs and the variety of their future design options, the jury is still out on their legal nature. Will *account-based* CBDCs be a direct, contractual claim on a central bank, transferred by assignment? Will *token-based* CBDCs be (quasi) res, transferred by a change in possession? Or, alternatively, will CBDCs as digital representations of cash be simply characterised as a central bank liability<sup>157</sup>, subject to a *sui generis* regime? Different jurisdictions may reach different conclusions on the legal nature of CBDCs. If this is the case, e.g. if a token-based CBDC is to be rendered

<sup>154</sup> See G7 Finance Ministers and Central Bank Governors' Statement on Central Bank Digital Currencies (CBDCs) and Digital Payments, 10.2021, available inter alia at:

[https://www.bundesfinanzministerium.de/Content/EN/Downloads/G7-G20/2021-10-13-g7-central-bank-digital-currencies.pdf?\\_\\_blob=publicationFile&v=4](https://www.bundesfinanzministerium.de/Content/EN/Downloads/G7-G20/2021-10-13-g7-central-bank-digital-currencies.pdf?__blob=publicationFile&v=4) para. 4 which states that: “[a]ny CBDC must support, and ‘do no harm’ to, the ability of central banks to fulfil their mandates for monetary and financial stability.”

<sup>155</sup> Bossu, W., Itatani, M., Margulis, C., Rossi, A., Weenink, H. and Yoshinaga, A., Legal Aspects of Central Bank Digital Currency: Central Bank and Monetary Law Considerations, IMF Working Paper WP/20/254, available at:

<https://www.imf.org/en/Publications/WP/Issues/2020/11/20/Legal-Aspects-of-Central-Bank-Digital-Currency-Central-Bank-and-Monetary-Law-Considerations-49827> para. 24 et seq.

<sup>156</sup> *ibid.*, para. 52.

<sup>157</sup> Sveriges Riksbank, E-Krona pilot Phase 2, April 2022, available at: <https://www.riksbank.se/globalassets/media/rapporter/e-krona/2022/e-krona-pilot-phase-2.pdf>. See also UK Finance, Designing Interoperability for a potential UK CBDC, 07.2022, available at: <https://www.ukfinance.org.uk/policy-and-guidance/reports-and-publications/designing-interoperability-potential-uk-cbdc> p. 16, with a broader set of options for CBDC issuance.

interoperable with an account-based CBDC, the contractual documentation on interoperability, be it bilateral or multilateral, should recognise these differences and respect all relevant exchange modalities, particularly as regards settlement finality/final settlement<sup>158</sup> and distribution of liability.<sup>159</sup>

### 3.4.3 National legal requirements

National legal requirements can either be general or pertain specifically to the design of a CBDC. An example of such a CBDC design requirement could be holding and/or transaction limits. If one jurisdiction has implemented holding and/or transaction limits on its CBDC, cross-border payments to and from another CBDC, the value of which fluctuates, risks violating those limits. A ‘waterfall’ arrangement whereby a CBDC above a certain threshold is automatically transferred to the holder’s commercial bank account may solve the problem of exceeding the holding limit – but not the transaction limit.

A general legal requirement that may become pertinent is data protection. In some jurisdictions privacy is a fundamental right<sup>160</sup>, the processing of personal data is subject to the principles of lawfulness, purpose limitation and data minimisation<sup>161</sup> and transfers of personal data to third countries are in principle conditional upon a finding of adequacy of the third country’s privacy law and practice<sup>162</sup>. It can safely be assumed that the CBDC of such jurisdiction would strive to ensure maximum privacy and data protection. Other jurisdictions, on the contrary, may design their CBDC on the principle of full data transparency and control by the central bank or another state agency. Legal interoperability without an adequacy finding is still possible if other appropriate safeguards are put in place, but it will always be conditional on the availability of enforceable data subject rights and effective legal remedies<sup>163</sup>. Therefore, a fully-fledged rule of law analysis of such a jurisdiction may become necessary if any personal data is to be transferred. Compliance with anti-money laundering legislation would be another example, whereby the same cross-CBDC transaction would trigger different levels of customer due diligence in the respective jurisdictions involved.<sup>164</sup>

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<sup>158</sup> See e.g. Skingsley, C., et al. Can multilateral platforms improve cross-border payments? 07.2022, available at: <https://www.bis.org/cpmi/publ/bb17.pdf> at p. 5.

<sup>159</sup> Jung, H., Jeong, D., Blockchain Implementation Method for Interoperability between CBDCs, *Future Internet* 2021, 13, 133, available at: <https://doi.org/10.3390/fi13050133> p. 12, for lack of clarity as regards distribution of liability in a decentralised model.

<sup>160</sup> E.g. Article 8 of the EU Charter of Fundamental Rights.

<sup>161</sup> E.g. Article 5 Regulation (EU) 2016/679 of the European Parliament and of the Council of 27 April 2016 on the protection of natural persons with regard to the processing of personal data and on the free movement of such data, and repealing Directive 95/46/EC (GDPR) (OJ L 119, 4.5.2016, p. 1).

<sup>162</sup> E.g. Article 45 GDPR.

<sup>163</sup> E.g. Article 46 GDPR.

<sup>164</sup> In the same vein see Ortino, M., *The Functions of Law and of Digital Platforms in the Payment System*, *European Business Law Review* 33, no. 7 2022 p. 1094, concluding that “interoperability and data portability in the payment system, including CBDCs, can be guaranteed only if they are regulated by adequate legal and regulatory mandatory requirements”.

### 3.4.4 Freedom to operate

Interoperability arrangements are technology intensive. Whether central banks develop own technology for the issuance and interoperability of CBDCs, or rely on third party IPR and standards<sup>165</sup>, interoperable CBDCs require international freedom to operate. Challenges in one jurisdiction, for instance concerning patent infringements, coupled with cease-and-desist orders, would not only affect the CBDC of that jurisdiction, but also those interoperable with it.

## 4 Conclusions

Interoperability of retail CBDCs may be a desirable feature, but it is neither necessary for the functioning of a CBDC within its native jurisdiction, nor does it come without legal complexity. Currently most central banks focus on designing and setting up their own digital currencies, which will likely use different technology.<sup>166</sup> However, there is merit in exposing and overcoming technical and legal obstacles to interoperability ex ante and early on, rather than trying to tackle them ex post, i.e. only when the various, diverging, CBDCs have gained momentum. In so doing, it must be kept in mind that: (a) inspiration from FMI law and regulation is precisely that, an inspiration only; (b) novel legal issues would need to be addressed, with the legal nature of CBDCs prominently figuring among them; and, (c) the evolution of legal doctrine must align itself with the political will to create (interoperable) CBDCs – and the technological capacity to do so.

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<sup>165</sup> For a presentation of the various technical standards relevant to CBDCs, see World Economic Forum, White Paper: Defining Interoperability, 11.2021, available at: [https://www3.weforum.org/docs/WEF\\_Defining\\_Interoperability\\_2021.pdf](https://www3.weforum.org/docs/WEF_Defining_Interoperability_2021.pdf) at pp 13-17. In the EU standardisation through harmonised standards issued by private bodies squarely falls within the ambit of judicial review, van Waeyenberge, A., Restrepo Amariles D.; James Elliott Construction: a "new(ish) approach" to judicial review of standardisation, E.L. Rev. 882 2017 p. 7-8; more nuanced in Eliantonio, M. Medzmariashvili, M., Hybridity Under Scrutiny: How European Standardization Shakes the Foundations of EU Constitutional and Internal Market Law'. Legal Issues of Economic Integration 44, no. 4 2017 p. 334.

<sup>166</sup> VISA Economic Empowerment Institute, Cross-border payments for Central Bank Digital Currencies via Universal Payment Channels, 2021, available at: <https://usa.visa.com/content/dam/VCOM/global/ms/documents/veei-cross-border-payments-for-cbdcs.pdf> p. 9.

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# Legal interoperability of the digital euro: prospects and challenges

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Many central bank digital currency (CBDC) projects are moving from conceptual analysis regarding objectives and legal basis<sup>167</sup> to practical design. As some countries have already introduced their own CBDC and others are actively preparing to (potentially) do so,<sup>168</sup> a key issue currently under discussion is the interoperability of CBDCs.<sup>169</sup> Policymakers are beginning to understand that rendering CBDCs interoperable – at the domestic level and potentially also cross-border – raises not only thorny technical issues, but also a range of fundamental legal questions. The purpose of this chapter is to hint at some of these questions and to discuss why they are important.

## 1 What is CBDC legal interoperability? And why is it important?

The Bank for International Settlements (BIS) describes interoperability as the “technical, semantic and business compatibility that enables a system to be used in conjunction with other systems”.<sup>170</sup> While this definition does not mention the enabling role of the law explicitly, it implies that there needs to be a certain level of legal compatibility of “systems” to interoperate smoothly. Applied to retail CBDCs (rCBDCs),<sup>171</sup> it also implies that such rCBDCs constitute “systems” that need to be enabled to interoperate with other existing (and potentially also future) “systems”. This need to interoperate stems from the objectives rCBDCs are to serve. At the domestic level, rCBDCs must interoperate with other systems of money of the same currency to serve as an interchangeable means of payment (and potentially also store of value). At the international level, there is a need – or at least a desirability – for rCBDCs to interoperate with other rCBDC systems (and their wider payment ecosystems)

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<sup>167</sup> For the digital euro see e.g. Grünewald, Zellweger-Gutknecht and Geva (2021).

<sup>168</sup> Overview available at <https://cbdctracker.org/>

<sup>169</sup> See e.g. the recent non-paper by France, Germany, Italy, Spain and the Netherlands on a digital euro, 9 September 2022, available at <file:///C:/Users/U287170/AppData/Local/Temp/bijlage-non-paper-digitale-euro.pdf>: “To the extent possible, a digital euro could be made interoperable with other central bank digital currencies in order to reap the potential benefits of faster, cheaper and safer cross-border transactions (cross-currency use) and to be used by residents from outside the euro area (cross-border use).”

<sup>170</sup> Bank for International Settlements (2022), p. 5.

<sup>171</sup> This chapter focuses on retail CBDC (rCBDC), i.e. a CBDC issued for use by the public at large.



denominated in another currency to facilitate cross-border payments<sup>172</sup> and safeguard the international role of and demand for the domestic currency.<sup>173</sup>

## 1.1 The domestic level

In today's national payment systems, different forms or "systems" of money used by the general public interoperate. In many jurisdictions, including the United States and the euro area, payments are based on a tiered or hybrid model: the central bank plays a key role in providing the monetary base in the form of central bank deposits for commercial banks and cash (banknotes) for the public at large, while commercial banks and other private-sector payment services providers provide customers with payment solutions (e.g. debit and credit cards) on the basis of commercial bank money (deposits).<sup>174</sup> By their legal nature, commercial bank deposits are individual private entities' debts and are thus associated with a default risk of the issuing bank. Cash, on the other hand, represents a liability of the central bank and a risk free means of payment and store of value.

A key feature of this tiered or hybrid model is that commercial bank deposits (i.e. private money) are freely convertible to cash (i.e. public money) and vice versa. This guaranteed mutual convertibility ensures that all monetary objects denominated in a specific currency circulate at par, independent of whether they are private or public money, thus ensuring the uniformity of money. Cash serves as an anchor in the monetary system and maintains the banking system's stability in the medium and long term.<sup>175</sup> From the perspective of the public at large, the systems "cash" and "commercial bank deposits" are interoperable. At least under normal market conditions, both deposits held with commercial banks and cash function as "money" more or less interchangeably – although each with their advantages and disadvantages in terms of privacy, convenience and risk of loss/theft, amongst others. Citizens may choose which form of money they want to use to transact a payment, without encountering much friction if the transaction crosses "systems".

With rCBDC, a new "system" of money enters the scene. Jurisdictions that consider introducing a rCBDC typically aim to provide the public with a digital equivalent and complement to cash. A stated key motivation for the adoption of a digital euro, for example, is the declining use of cash and the prospect that this use may decline even further in the future,<sup>176</sup> which may weaken the function of cash as the anchor to other forms of money, in particular commercial bank deposits. If a digital euro is to share that

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<sup>172</sup> See e.g. Auer, Haene and Holden (2021); Bindseil and Pantelopoulos (2022), pp. 48-50. CBDC interoperability thus falls squarely within the G-20's endeavour to address existing challenges in the cross-border payments market, including high costs, low speed, limited access and insufficient transparency, and the roadmap to enhance cross-border payments the G-20 endorsed in October 2020. See Financial Stability Board (2020).

<sup>173</sup> An interoperable digital euro would also be supportive to the objectives of the EU's Retail Payment Strategy, in particular its Pillar 3 ("Efficient and interoperable retail payment systems and other support infrastructures"). See Communication from the Commission – A retail payments strategy for the EU, 24.9.2020, COM(2020) 592 final.

<sup>174</sup> For the United States see Cheng and Torregrossa (2022).

<sup>175</sup> Zellweger-Gutknecht, Geva and Grünwald (2021), pp. 298-299.

<sup>176</sup> E.g. European Central Bank (2020), pp. 10-11.

anchor function with cash, it needs to interoperate just as smoothly – or at least similarly smoothly – with commercial bank deposits as cash does. Users of the digital euro should, in principle, at all times and without friction be able to change “systems” by transferring digital euros to their commercial bank accounts or, vice versa, by withdrawing funds from their commercial bank accounts and transferring them to their digital euro accounts or digital wallets.<sup>177</sup> Just as with cash deposits or withdrawals, users’ funds would switch from being public money, i.e. a liability of the central bank, to being private money, i.e. a liability of their commercial bank, or vice versa, respectively. In principle, this conversion between rCBDC and commercial bank deposits would happen at par, i.e. a user withdrawing 100 euros from her bank account will receive 100 digital euros on her digital euros account or wallet. However, limits imposed on the holdings of digital euros and other means, proposed by some to mitigate the risks of structural disintermediation and digital runs,<sup>178</sup> would affect the digital euro’s free convertibility.<sup>179</sup>

## 1.2 The international level

At the international level, interoperability refers to the ability to transfer rCBDC across borders and convert it into rCBDC (or other forms of fiat money) denominated in another currency.<sup>180</sup> In this dimension, the challenge is less one of integrating rCBDC as a new system into existing and already interoperable systems, as is the case at the domestic level, but more one of creating rCBDC systems and arrangements “connecting” them to allow for cross-border payments using rCBDC. In this rather unexplored territory, we can look to two precedents for inspiration and useful guidance. A first set of precedents are the arrangements in place for cross-border (and partially also cross-currency) wholesale payments and settlement, including the continuous linked settlement (CLS), the Trans-European Automated Real-time Gross settlement Express Transfer system (Target2) securities and the TARGET Instant Payment Settlement (TIPS) systems. A second precedent could be seen in the continuing experimentation with wholesale multi-CBDC (mCBDC) arrangements.<sup>181</sup> These precedents hint not only at potential high-level models for “connecting” different rCBDC systems, through compatibility or interlinking of different domestic rCBDC systems or even a joint rCBDC system,<sup>182</sup> but also at the many potential legal and operational challenges that cross-border interoperability of rCBDC would entail.<sup>183</sup>

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<sup>177</sup> This assumes full mutual convertibility also of banknotes and digital euros, which is desirable but not necessarily a given.

<sup>178</sup> See e.g., Bindseil (2020).

<sup>179</sup> An artificial scarcity of the digital euro will likely increase its value compared to other forms of money that are available without limits. In periods of stress, convertibility at par may thus not hold up.

<sup>180</sup> The possibility for countries to grant non-residents access to their domestic rCBDC is different from creating actually interoperable systems and thus not covered specifically in this chapter. It finds guidance in the international legal framework that has developed on how countries should treat international payments and transfers and relies on the distinction of residence and non-residence.

<sup>181</sup> See Committee on Payments and Market Infrastructures (CPMI), BIS Innovation Hub, International Monetary Fund (IMF) and World Bank (2022), in particular pp. 38-39.

<sup>182</sup> For a discussion of these models see Deutsche Bundesbank (2022), pp. 72-77; Omlor and Birne (2022), pp. 1790-1792.

<sup>183</sup> See CPMI, BIS Innovation Hub, IMF and World Bank (2021 and 2022).

As rCBDCs are being developed as a domestic means of payment, their potential future role as a vehicle for cross-border transactions should be kept in mind. Early reflection on potential operational and legal impediments is vital to ensure efficient cross-border interoperability once rCBDCs have been successfully adopted in several jurisdictions. It also mitigates the risk that rCBDCs do cross-border harm.<sup>184</sup> The recently announced joint exploration by the BIS and the central banks of Israel, Norway and Sweden of rCBDC cross-border interoperability (“Project Icebreaker”) will provide first insights into the operational and technological feasibility of interlinking different domestic rCBDC systems through a joint “hub”.<sup>185</sup>

## 2 Legal interoperability of the digital euro: what is needed?

A key premise for the successful adoption of an rCBDC is its legal interoperability at the domestic level. The remainder of this chapter thus focuses on what is needed to render the digital euro legally interoperable. The digital euro is unique in the sense that it combines a domestic with an international dimension. It is “domestic” in the sense that it concerns one unit of account – the euro – and one central hub or balance sheet – the European Central Bank (ECB) together with the national central banks (NCBs). It is international in that it operates in a regulatory and legal environment that is only partially harmonised and where financial institutions are largely supervised at Member State level.

### 2.1 Creating a digital euro “system”

As an initial step, the digital euro will require a system of its own for its entire “life cycle” – from its issuance to its production, distribution as well as storage and transfer. Much of the ultimate design of the digital euro remains open for the time being, which renders a detailed legal analysis of this system difficult. However, in a likely scenario, the ECB will opt for an intermediated “tiered” model that avoids a direct (contractual) relationship between the central bank and the public and in which financial intermediaries and/or wallet providers handle payments in digital euro – whether in the form of tokens or account balances – on behalf of and for the account of the ECB. Under such a model, the ECB will provide the core (back-end) infrastructure, while keeping commercial banks and other payment service providers or intermediaries in charge of running the infrastructure, providing customer-facing appliances and conducting customer authentication, amongst other services.

A technical rulebook<sup>186</sup> will formalise the roles and responsibilities of the ECB as the likely operator of the core system, commercial banks and potentially other service providers and intermediaries, establishing a governance structure and uniform rules

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<sup>184</sup> “Do no harm” is one of the foundational principles identified for rCBDCs. See BIS (2020), p. 10.

<sup>185</sup> ‘Project Icebreaker: Central banks of Israel, Norway and Sweden team up with the BIS to explore retail CBDC for international payments’, available at [www.bis.org/about/bisih/topics/cbdc/icebreaker.htm](http://www.bis.org/about/bisih/topics/cbdc/icebreaker.htm)

<sup>186</sup> See BIS (2020), p. 6.

for the digital euro system.<sup>187</sup> The rulebook will define standards regarding the terms and basic features of participating private entities' processes and applications as well as identify which applications are mandatory or an optionality. Participating private entities will have to implement those requirements and ensure that their processes and applications are interoperable with the core system provided by the ECB. The costs that this creates for them will depend on the extent to which they can rely on existing solutions and systems, e.g. those for interbank payments.

While much of the creation of this digital euro system falls within the competence of the ECB, input by other EU institutions, in particular the co-legislators, will be necessary to render the system legally interoperable. On the basis of Article 128(1) of the Treaty on the Functioning of the European Union (TFEU), the ECB is competent to issue a digital equivalent to euro banknotes, with incidental powers to determine the digital euro's technological design and the technical modalities of its issuance, distribution and transfer.<sup>188</sup> It may adopt legal acts of its own to fulfil its issuance function.<sup>189</sup> Were the digital euro to serve solely as a means of payment, which the ECB is considering in order to control the amount of digital euro in circulation and, hence, any adverse effects on bank intermediation,<sup>190</sup> its legal basis is less straight-forward. In this case, the digital euro's adoption might be based on Article 127(2), fourth indent, TFEU, i.e. the ECB's core task to promote the smooth operation of payment systems to fulfil its primary objective of price stability, and Article 22 of the Statute<sup>191</sup> in combination with Article 128(1) TFEU.

Article 133 TFEU, on the other hand, assigns the EU co-legislators with the role of laying down, on the basis of secondary law acts, "the measures necessary for the use of the euro as the single currency". The delineation of which legal issues pertain to the *issuance* of a digital euro and which are necessary for the *use of the euro as the single currency* might not always be a straightforward one. Counterfeiting may be an example of a legal issue that pertains to both. The euro is currently subject to an elaborate legal framework against its counterfeiting, consisting of Council legal acts and ECB decisions.<sup>192</sup> New rules to protect from counterfeiting and public misperception and that would cater for the digital nature of the digital euro,<sup>193</sup>

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<sup>187</sup> A key question to be decided by the ECB is which categories of supervised entities are to be allowed to offer digital wallets or accounts in digital euros. From a competition law perspective and for reasons of safety and resilience, there might be a need for the ECB to ensure that market power by single providers of wallets (in a token-based setting) remains limited in the distribution of the digital euro.

<sup>188</sup> See Grünewald, Zellweger-Gutknecht and Geva (2021), pp. 1040-1045. Digital Euro Association (2022), p. 11, in contrast, argue that "it is preferable for the ECB to be given an explicit legal mandate on which to issue the digital euro".

<sup>189</sup> Examples pertaining to tangible banknotes include Decision ECB/2013/10 of 19 April 2013 on the denominations, reproduction, exchange and withdrawal of euro banknotes (OJ L 118, 30.4.2013, p. 37) as well as Decision ECB/2020/24 of 27 April 2020 on accreditation procedures for manufacturers of euro secure items and euro items (OJ L 149, 12.5.2020, p. 12) and Decision ECB/2010/14 of 16 September 2010 on the authenticity and fitness checking and recirculation of euro banknotes (OJ L 267, 9.10.2010, p. 1).

<sup>190</sup> European Central Bank, (2022), pp. 9-10.

<sup>191</sup> Statute of the European System of Central Banks and of the European Central Bank.

<sup>192</sup> In particular, Council Regulation (EC) No 1338/2001 of 28 June 2001 laying down measures necessary for the protection of the euro against counterfeiting (OJ L 181, 4.7.2001, p. 6) and Decision ECB/2010/14.

<sup>193</sup> The current anti-counterfeiting framework is geared towards tangible attributions of the euro. See e.g. Council Regulation (EC) No 2182/2004 of 6 December 2004 concerning medals and tokens similar to euro coins (OJ L 373, 21.12.2004, p. 1): "Medals and tokens" are "metallic objects (...), which have the appearance and/or technical properties of a coin" (Article 1(c)).

including for private digital assets referring to “euro” or “digital euro”,<sup>194</sup> will likely need to be the result of close coordination between the ECB and the Commission. Other legal issues might be of such elevated societal importance that involvement of the co-legislators is required from a democratic point of view – privacy being the prime example.

When the euro was introduced in the form of tangible banknotes (and coins), the role of the EU legislature (then the Council alone) was to provide legal certainty for individuals and companies and to ensure a smooth substitution of national currencies with the euro.<sup>195</sup> Ensuring such “legal interoperability” might be its key task again in the context of the introduction of a digital euro.<sup>196</sup> The EU co-legislators will have a central role to play in aligning the EU’s broader legal framework with the novelty of a digital euro.<sup>197</sup>

## 2.2 Necessary amendments to the EU’s legal framework

As part of the ongoing investigation phase, the digital euro project, in collaboration with the Commission, is looking into the amendments to the EU’s legal framework that might be needed before the digital euro is introduced.<sup>198</sup> This exercise is key to ensuring interoperability. From a legislative point of view, a starting question will be whether a separate “digital euro regulation” is needed to introduce legal rules that are specific to the digital euro and/or to what extent existing EU legislation can be amended to cater for the digital euro. Due to limited public information on the digital euro’s ultimate design, this question is difficult to answer at this stage. This chapter thus confines itself to highlighting some key areas of EU legislation that will likely require reconsideration in anticipation of the introduction of a digital euro.

### 2.2.1 Prudential regimes for private entities participating in the system

Whatever the ultimate design of the digital euro might be, the digital euro system will likely include intermediaries or service providers other than licensed commercial banks (credit institutions). One way of ensuring that these entities, such as wallet providers, are brought within the reach of adequate prudential rules and supervision

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<sup>194</sup> See also Digital Euro Association (2022), p. 11.

<sup>195</sup> See Council Regulation (EC) No 1103/97 of 17 June 1997 on certain provisions relating to the introduction of the euro (OJ L 162, 19.6.1997, p. 1) (“1st Euro-Regulation”), pertaining to the continuity of contracts and ECU-denominated obligations as well as conversion and rounding; Council Regulation (EC) No 974/98 of 3 May 1998 on the introduction of the euro (OJ L 139, 11.5.1998, p. 1) (“2nd Euro-Regulation”), introducing euro banknotes and coins over a transitional period and regulating the substitution of national currencies; Council Regulation (EC) No 2866/98 of 31 December 1998 on the conversion rates between the euro and the currencies of the Member States adopting the euro (OJ L 359, 31.12.1998, p. 1), determining the conversion rates at which, up to today, banknotes and coins denominated in national currencies may be converted into euro.

<sup>196</sup> However, the context is different now as no new single currency is introduced, but a different monetary object denominated in the unit of account of that currency.

<sup>197</sup> In January 2021, the Commission and ECB agreed to work together to analyse various design options and the broader legal implications of the introduction of the digital euro. See e.g. Communication from the Commission – The European economic and financial system: fostering openness, strength and resilience, 19.1.2021, COM(2021) 32 final, pp. 10-12 (Key action 6).

<sup>198</sup> The Commission has announced a legislative proposal on a digital euro for early 2023.

would be to subject them to the regime applicable to “payment institutions” according to the Payment Services Directive (the “PSD2”).<sup>199</sup> For that purpose, payment services in digital euros, for example services enabling digital euros to be “placed” in a commercial bank account or for digital euro “withdrawals” from such account, would need to be included in the PSD2’s definition of payment services.<sup>200</sup> A fundamental question is whether any entity could in principle seek authorisation as a “payment institution” in digital euro, or whether that circle of entities would be *a priori* selective in one way or another.<sup>201</sup> Depending on the ultimate design of the digital euro, some payment services may require “payment institutions” to hold an account with the ECB/NCBs, which the Eurosystem may want to offer only to a selected circle of entities.<sup>202</sup> There might also be different categories of “payment institutions”. While some might be authorised to only store and transfer, others might also be authorised to convert, i.e. bring into circulation and sterilise, digital euros.

However, existing prudential regimes may also have to be amended. The introduction of a digital euro may necessitate amendments to banks’ licensing requirements, as transposed into national law on the basis of the Capital Requirements Directive (CRD)<sup>203</sup> (in particular Articles 8 and 10-14) and any technical standards adopted on the basis thereof. For example, the execution of payments in and the storage of digital euro will likely have to be included expressly in banks’ programme of operations provided for in Article 10 CRD. Moreover, prudential supervisors will have to be assured that any financially material risks with regard to digital euro operations of banks are properly managed and that the processes and applications used are safe, reliable and resilient.<sup>204</sup>

The framework for bank recovery and resolution<sup>205</sup> might also be affected by the issuance of a digital euro. Unlike commercial bank deposits, digital euros in accounts or wallets provided by commercial banks will not be subject to resolution powers, in particular bail-in, applied by resolution authorities. They are liabilities of the ECB, not of commercial banks that only facilitate their storage and transfer. However, bank

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<sup>199</sup> Directive (EU) 2015/2366 of the European Parliament and of the Council of 25 November 2015 on payment services in the internal market (OJ L 337, 23.12.2015, p. 35).

<sup>200</sup> Annex I to the PSD2. For an analysis of the extent to which digital euro payments would already fall within the scope of the *Zahlungsdiensteaufsichtsgesetz (ZAG)*, the German transposition of the PSD2, see Omlor and Birne (2020), pp. 9-10. Moreover, the principle of coexistence and interoperability suggests that, to the extent possible and appropriate, the same rules should apply to all euro payments, likely including the information requirements and the rights and obligations between payment service providers and payment service users, as set out in the PSD2.

<sup>201</sup> However, such pre-selection may raise concerns from a competition law perspective and would need to be justified by relevant public interests.

<sup>202</sup> Article 17 of the Statute allows the ECB and the NCBs to “open accounts for credit institutions, public entities and *other market participants*” (emphasis added).

<sup>203</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 (OJ L 176, 27.6.2013, p. 338).

<sup>204</sup> Given that these operations concern central bank money, the supervision of banks’ digital euro operations are only partially a prudential concern. National competent authorities will likely have to “share” supervision over banks’ digital euro operations with the ECB in one way or another.

<sup>205</sup> Directive 2014/59/EU of the European Parliament and of the Council of 15 May 2014 establishing a framework for the recovery and resolution of credit institutions and investment firms (OJ L 173, 12.6.2014, p. 190); Regulation (EU) No 806/2014 of the European Parliament and of the Council of 15 July 2014 establishing uniform rules and a uniform procedure for the resolution of credit institutions and certain investment firms in the framework of a Single Resolution Mechanism and a Single Resolution Fund (OJ L 225, 30.7.2014, p. 1).

processes and applications that allow for the transfer and storage of digital euros may affect banks' resolvability as they may become "critical functions". Safeguards may be needed to ensure that they can be separated from other operations of a bank in the event of the bank's failure.

### 2.2.2 Settlement finality and collateral

The Settlement Finality Directive<sup>206</sup> ensures that transfer orders in euro payments, amongst others, are finally settled, i.e. become irrevocable and unconditional at the point of settlement. It was passed to reduce systemic and legal settlement risks in payment and securities settlement systems, in particular those arising from the insolvency of financial institutions participating in these systems. It also provides for the enforceability of the netting of transfer orders, despite the insolvency of a participant. Finality of payments in digital euros will have fundamentally different legal implications than in the case of interbank payments in commercial bank money, as they concern central bank money, which can ultimately always be settled. A key legal issue will be the segregation of both types of "monies" where the systems and/or participants in the systems overlap (e.g. account segregation in the case of an account-based design).

Depending on the digital euro's design, the Eurosystem may provide account balances for intermediaries other than supervised financial institutions against eligible assets as collateral. In that case, the Financial Collateral Directive (FCD)<sup>207</sup> may have to be amended to include such intermediaries and to ensure that the protection afforded by the FCD, i.e. access to the collateral security at all time without the collateral giver's participation and guaranteed realisation, applies to them as well.

### 2.2.3 Financial crime controls and privacy

Another broad area for reconsideration concerns the balancing between the need to be compliant with anti-money laundering (AML) and countering the financing of terrorism (CFT) requirements, on the one hand, and laws on data protection and privacy rights, on the other. To ensure integrity in today's financial system, banks and other payment service providers verify identity and validate compliance with the AML/CFT requirements of the 5th AML-Directive<sup>208</sup> when customers open accounts and transact high-value payments. A token-based digital euro design permitting anonymous transactions would allow for cash-like usability with strong privacy, while amplifying the AML/CFT risks associated with cash.<sup>209</sup> A digital euro design that

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<sup>206</sup> Directive 98/26/EC of the European Parliament and of the Council of 19 May 1998 on settlement finality in payment and securities settlement systems (OJ L 166, 11.6.1998, p. 45).

<sup>207</sup> Directive 2002/47/EC of the European Parliament and of the Council of 6 June 2002 on financial collateral arrangement (OJ L 168, 27.6.2002, p. 43).

<sup>208</sup> Directive (EU) 2015/849 of the European Parliament and of the Council of 20 May 2015 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing (OJ L 141, 5.6.2015, p. 73).

<sup>209</sup> Unlike with cash, no "portability limitations" apply to transactions in digital euro. See BIS (2021), p. 82, stating that "[i]dentification at some level is ... central in the design of CBDCs".

renders transactions fully transparent to authorities, on the other hand, while addressing AML/CFT concerns, might not align with users' privacy rights and preferences. Indeed, the ECB's public consultation on a digital euro found that anonymity was by far the greatest concern among EU citizens, suggesting that there might be resistance to the use of digital IDs.<sup>210</sup>

In search of a balance between the conflicting objectives of privacy and traceability, the ECB has experimented with so-called "anonymity vouchers", a technical solution to allow payments of small amounts within a given period and with a high level of privacy.<sup>211</sup> Users spend these vouchers if they want to transfer digital euro without revealing information to the AML authority, thus limiting the amount of digital euro that can be transferred anonymously by the number of vouchers issued by the AML authority to each user.<sup>212</sup> This implies a system in which only small-value transactions in digital euro could be made anonymously, while transaction monitoring would apply to payments beyond a certain threshold.<sup>213</sup> Other technical solutions may ensure that only intermediaries, not the ECB or NCBs, have access to transaction data on a need-to-know basis.<sup>214</sup> Any such data governance arrangement would not only have to be set out in the ECB's technical rulebook for the digital euro system,<sup>215</sup> but would also have to be adequately brought in line with the requirements of the 5th AML-Directive, including its future amendments,<sup>216</sup> as well as relevant data protection regulations.<sup>217</sup>

## 2.3 Understanding potential legal impediments from Member States' diverging private law regimes

It is not only EU law that has an impact on the digital euro's interoperability. Member States' legal frameworks and traditions may vary considerably in their likely treatment of the digital euro under private law. While the legal status of "accounts" is better understood and developed, much less clarity exists under a token-based design of the

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<sup>210</sup> ECB (2021). See also the Commission's proposal to establish a more harmonised approach to digital identification across the EU, which may impact the AML-regime as well: Proposal for a Regulation of the European Parliament and of the Council amending Regulation (EU) No 910/2014 as regards establishing a framework for a European Digital Identity, 3.6.2021, COM(2021) 281 final.

<sup>211</sup> There are other innovative technologies that allow policy makers to find an optimal balance between the near-complete anonymity of cash and full information regarding existing digital payment transactions. For the experiments of the Bank of Israel with a digital shekel see Bank of Israel (2022), pp. 18-21.

<sup>212</sup> ECB (2019), p. 6.

<sup>213</sup> The question of where precisely to set this threshold remains. And would several payments to the same recipient within a specified timeframe (e.g. one week) count as one payment for the purposes of determining whether the threshold was reached?

<sup>214</sup> Chaum, Grothoff and Moser (2021) propose a scheme of one-sided privacy, which allows the buyer to remain anonymous while rendering the seller's incoming transactions available to competent authorities (e.g. law enforcement) upon request.

<sup>215</sup> See paragraph 2.1. ECB (2022), pp. 6-8.

<sup>216</sup> For the legislative package proposed by the Commission see: [https://finance.ec.europa.eu/publications/anti-money-laundering-and-countermeasures-financing-terrorism-legislative-package\\_en](https://finance.ec.europa.eu/publications/anti-money-laundering-and-countermeasures-financing-terrorism-legislative-package_en)

<sup>217</sup> These include, in particular, Regulation (EU) 2016/679 of the European Parliament and of the Council of 27 April 2016 on the protection of natural persons with regard to the processing of personal data and on the free movement of such data (General Data Protection Regulation) (OJ L 119, 4.5.2016, p. 1); Regulation (EU) 2018/1725 of the European Parliament and of the Council of 23 October 2018 on the protection of natural persons with regard to the processing of personal data by the Union institutions, bodies, offices and agencies and on the free movement of such data (OJ L 295, 21.11.2018, p. 39).



digital euro.<sup>218</sup> As book money, an account-based digital euro would qualify as an intangible, transferable through debits and credits of the account on which it is held. Because it would be traceable, like existing current accounts on the books of central banks, there is no need to afford private law privileges (i.e. its *bona fide* acquisition) to an account-based digital euro.<sup>219</sup> A token-based digital euro, on the other hand, lacking such history and common understanding, fits less easily into traditionally recognised private property law categories or definitions.

Accordingly, differing levels of property rights might be applied to it in different EU jurisdictions, also affecting the question of which law applies in cross-border transactions. Some Member States may treat it similarly to a banknote, subjecting it to rules to protect its *bona fide* acquisition, others may treat it like a fully-fledged intangible without any private law privileges. Across the EU, there is no common understanding on whether intangible objects may qualify as property at all.<sup>220</sup> Some Member States rely on broad definitions of “things” that encompass intangible objects.<sup>221</sup> The civil codes of other Member States define “things” more narrowly as physical objects,<sup>222</sup> requiring legal recognition of the status of specific intangible objects as “things”.

There is a need to understand which potential legal impediments may arise for the interoperability of the digital euro due to Member States’ diverging private law regimes. This will facilitate a better understanding of the unique features of digital euro tokens and the development of uniform principles according to which their legal status could be harmonised, to some extent, across the EU. The SFD may serve as a historical example. It introduced the principle of settlement finality to contribute to the efficient and cost-effective operation of cross-border payment and securities settlement arrangements. To comply with the requirements of the SFD, Member States amended their private law regimes where necessary, in particular by implementing “carve outs” for payment and settlement systems from certain national bankruptcy law provisions.<sup>223</sup>

Looking beyond the EU’s jurisdiction, international consensus on key principles regarding the private law treatment of rCBDC and the applicable law would reduce

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<sup>218</sup> See Bossu, Itatani, Margulis, Rossi, Weenink and Yoshinaga (2020), p. 9. See, however, Zellweger-Gutknecht (2021), pp. 33-34, who argues that “account balances” and “tokens” might not be so fundamentally different, given that tokens are also fully debited (invalidated) and credited (created) with each transaction. See in the same sense already [www.stlouisfed.org/on-the-economy/2020/october/tokens-accounts-why-distinction-matters](http://www.stlouisfed.org/on-the-economy/2020/october/tokens-accounts-why-distinction-matters)

<sup>219</sup> Instead, the *nemo plus iuris* rule would apply. See Bossu, Itatani, Margulis, Rossi, Weenink and Yoshinaga (2020), p. 9. See, however, Zellweger-Gutknecht (2021), p. 40.

<sup>220</sup> See also Digital Euro Association (2022), pp. 10-11.

<sup>221</sup> See e.g. § 285 of the Austrian Allgemeines bürgerliches Gesetzbuch (ABGB): “Alles, was von der Person unterschieden ist, und zum Gebrauche der Menschen dient, wird im rechtlichen Sinn eine Sache genannt.”

<sup>222</sup> See e.g. § 90 of the German Bürgerliches Gesetzbuch (BGB): “Sachen im Sinne des Gesetzes sind nur körperliche Gegenstände.” and Article 2 of the Dutch Burgerlijk Wetboek (BW) Boek 3: “Zaken zijn de voor menselijke beheersing vatbare stoffelijke objecten.”

<sup>223</sup> For example, according to the Dutch Bankruptcy Act, a declaration of bankruptcy has retroactive effect to the beginning of the day on which it was pronounced (Articles 23 and 35 Bankruptcy Act). This provision would have created problems for euro payment finality. To comply with the requirements of the SFD, the Dutch legislator introduced a derogation provision, exempting payment and settlement systems as well as participating financial institutions from this retroactive effect to allow “for a complete execution of orders in the system or rights and duties which arise for a participant due to or in connection with its participation in the system.” (Article 212b Bankruptcy Act).

existing uncertainties and unpredictabilities, facilitating cross-border interoperability. Such key principles could ultimately be enshrined in an international code of legislation, similar to the Hague and Geneva Securities Conventions<sup>224</sup> that provide a modern international legal regime for intermediated securities. Even if the success of these Conventions has remained limited when it comes to their application in practice, these are the fora in place for coordination in international private law matters. The ongoing UNIDROIT project on digital assets and private law, covering digital assets generally, could provide a starting point.

### 3 Conclusions

Developments around the introduction of a digital euro and rCBDC elsewhere in the world are unfolding at a fast pace. For rCBDCs to reach their full potential in driving payments innovations while maintaining the anchor function of public money, they must be interoperable to the largest extent feasible – both at the domestic and international level. This chapter has addressed, on a fundamental level, what is needed to render a digital euro interoperable at the domestic level. Apart from creating a digital euro system, domestic interoperability will require embedding this new system in the EU's broader legal framework. This involves a difficult legal balancing in terms of the scope of private entities allowed to participate in the system and their supervision or oversight as well as regarding the right and preference of users for privacy while ensuring the integrity of the system. Moreover, this chapter has argued, there is a need to better understand the potential legal impediments from Member States' possibly differing treatment of the digital euro under private law, at least under a token-based design.

As these necessary steps are being addressed by policymakers in the EU, the focus should not be on the domestic level alone. Differences in designs and legal requirements of rCBDCs may prove an impediment to successful cross-border interoperability between them. It is thus absolutely key that international discussion on rCBDC design and cross-border rCBDC experimentation take place at this early stage of rCBDC development.

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<sup>224</sup> Hague Convention on the law applicable to certain rights in respect of securities held with an intermediary (5 July 2006); UNIDROIT Convention on substantive rules for intermediated securities (9 October 2009).

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## Panel 4

Comparison of the ECB's internal review procedure for contract award decisions with the legal framework for the review of such decisions in other EU, international and national organisations



ESCB Legal Conference 2022 – Panel 4  
Comparison of the ECB's internal review procedure for contract award decisions with the legal framework for the review of such decisions in other EU, international and national organisations

# The importance of good communication for avoiding conflict

By Martin Benisch\*

This panel offers a comparison of the ECB's internal review procedure for contract award decisions with the legal framework for the review of such decisions in other EU institutions, and in international and national organisations. The starting point will be the ECB's internal review procedure for contract award decisions (i.e. the Procurement Review Body, PRB), a mechanism that does not exist in any other EU institution. This will include a stocktaking after 15 years of PRB decisions, an assessment of the impact of recent case-law on review procedures and the requirements to obtain interim relief from the Court of Justice of the European Union, as well as an assessment of practical problems, for example in terms of language regime.

The panellists are:

- Isabell Koepfer, Adviser, Legal Services, European Central Bank;
- Laura André, Member of the Legal Service, European Commission; and
- Jeff Dirix, Senior Advisor, Head of Group, Legal Department, Nationale Bank van België / Banque Nationale de Belgique.

The presentations will deal with several aspects of managing the relationship between the bidders and the contracting authority. This includes information on how successful a specific body was in the past 15 years in reviewing complaints of tenderers in procurement procedures who considered themselves not treated or heard correctly during the procedure. It addresses how other institutions deal with questions of bidders and arrange for a proper review process. And finally, it elaborates on how the dialogue between the contracting authority and the tenderer continues even after an award decision has been taken.

A common theme in all of these presentations is the importance of communication in the relationship between the contracting authority and the tenderers during, but also after, the selection process has ended.

This raises the following questions. Why is it indeed beneficial – for contracting authorities and tenderers – to communicate with the counterparty in a transparent manner and to keep doing so throughout the process? What role does communication play in the relationship between contracting authorities and tenderers?

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To put it bluntly, assuming that all legal obligations have been complied with, why would contracting authorities want to communicate and rethink their own position rather than simply going through with their decision unilaterally? Why would bidders be at all interested in communicating with the contracting authority and continuing the dialogue even after their bid has been rejected in a procurement procedure?

There must be a benefit for both parties in staying in contact, in keeping the communication channels open, and in taking the time to explain their own perspective.

The obvious reason for the interest in such communication is reducing the level of misunderstanding, which is the major cause of conflict.<sup>225</sup> The achievement of such understanding is largely dependent on information and communication.<sup>226</sup>

What does perfect communication look like in the first place? Touitou defines seven “C”s that effective information has to comply with.<sup>227</sup> According to this, information must be:

1. complete, it must address all concerns of the receiver;
2. concise, hence exact and straightforward;
3. clear, i.e. avoiding complex grammar;
4. courteous, so be respectful and polite, for instance by answering promptly and by avoiding expressions that hurt or belittle;
5. concrete, thus, specific and definite, not vague;
6. considerate of the needs of the audience; and
7. correct, the most obvious one, referring to the absence of lies and false representation.

This list of features of perfect communication signals that a lot can go wrong in communication, so also when bidders and contracting authorities communicate in a tender process. Applying all Touitou’s requirements, from the first to the last, information can be forgotten or go missing, it can be too bulky with the risk of relevant aspects being overlooked, it can be ambiguous, delayed or offensive, too vague, or not meeting the expectations of the receiver or it can simply be false. This confirms the clear need for all participants in procurement processes to make use of all efforts to keep all involved parties, contracting authorities on the one side and bidders on the other, informed in a consistent manner, subject, of course, to what is permissible in the procurement procedure at hand.

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<sup>225</sup> Touitou, T.C., Communication, Conflict and Crisis Management, EJBMR, European Journal of Business and Management Research, Vol. 5, No. 4, August 2020, p. 1.

<sup>226</sup> *ibid.*, p. 1.

<sup>227</sup> *ibid.*, p. 4.



The European Commission, in its Public Procurement Guidance for Practitioners<sup>228</sup>, requests that potential tenderers are allowed, provided that this is foreseen in the tender documents, to contact the contracting authority to ask for clarifications. The Commission also recommends that reliable communication channels are available to all potential tenderers and that clear timeframes and cut-off dates are set. The Commission finds it beneficial to all parties to create and maintain an open and constructive relationship between the contractor and the contracting authority, also during the phase of implementing the contract. They highlight that such regular and smooth communication will enable knowledge-sharing, common understanding and a greater ability to anticipate possible problems or risks.

All efforts for transparent and constructive communication cannot avoid the risk that communication fails, resulting in a conflict. Should this then be the end of communication and of the exchange of information?

Let's first take a closer look at the nature of conflict. Touitou provides three possible perspectives on conflict.<sup>229</sup> It can be:

- a negative phenomenon that needs to be avoided;
- a natural occurrence in every organisation of humans that needs to be accepted and managed; or
- an imperative that should even be encouraged to avoid an organisation becoming static, apathetic and unresponsive to the need for change.

Procurement practitioners would probably subscribe to the first or, as realists, the second perspective, so trying to avoid conflict or, when it nevertheless does happen, live with it and try to manage it well. However, even the third perspective on conflict has value in the field of procurement. Conflict, when carried out in an orderly and functional manner, has the potential to ensure that all aspects of a public procurement procedure are considered. For instance, it ensures that the contracting authority is not overlooking opportunities by reducing the scope of the procurement in too detailed a manner or asking for services that are quite impossible to provide.

Now imagine that the tender process is concluded, and bids have been rejected. What is the role of information and communication then or – one step further – in the case of imminent judicial conflict?

The UK Ministry of Defence<sup>230</sup> considers that in terms of conflict management much depends on the quality of the debrief, hence how well the reasons why bidders were not successful are explained. The Ministry asked contracting authorities whether such debrief was always offered. The UK authorities confirmed that it depended on the contract value threshold but that it was generally best practice to offer a debrief for all procurement procedures, where possible. Respondents suggested that a firm

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<sup>228</sup> European Commission (2018). Public Procurement Guidance for Practitioners, p. 88 and 106.

<sup>229</sup> Touitou, T.C., Communication, Conflict and Crisis Management, EJBMR, European Journal of Business and Management Research Vol. 5, No. 4, August 2020, p. 4.

<sup>230</sup> Butler, L.R.A. (2020). Governing compliance with public procurement law: a view from the UK Ministry of Defence, Robert Allen, P.P.L.R., Public Procurement Law Review, 5, pp. 301-333.

indication of the information prescribed by the regulations would generally be sufficient. They reported that previous research has also identified the importance of rewinding the procedure or reinstating a supplier as a direct corrective action that is likely to prevent a supplier from instituting a legal challenge.

Academics confirm that good debriefing defuses protests, also by giving contractors a better understanding of, and control over, the risk of improperly losing the award.<sup>231</sup>

- Information helps suppliers to reassess and understand changes necessary to improve the performance of their business offer.
- Information also makes suppliers “tender-ready or contract-ready”<sup>232</sup> and makes future bids more successful.
- An evaluation of access of small and medium enterprises (SMEs) to public procurement procedures in the EU reported that “no debriefing” was one of the top four biggest problems that companies face when participating in public procurement procedures.
- Evans concludes that meaningful feedback and clear communication allow SMEs to understand why they lost and why another company won.
- Finally, all this has a strong potential to reduce the risk of litigation.<sup>233</sup>

Arrowsmith concludes that there is a very important mechanism for enforcing public procurement rules and a key feature of many modern procurement systems: a robust system of review and remedies before a national review body.<sup>234</sup> She also identifies three hurdles that particularly hinder the use of such a review system:

- fear of retaliation by the procuring entity or other public/private purchasers;
- financial and resource costs of bringing proceedings; and
- lack of awareness of legal rights or of violations.

Therefore, she calls for the resolution of disputes prior the conclusion of a contract wherever possible and for the provision of rapid hearings. She thus lobbies for an effective remedy rather than denying such a remedy.<sup>235</sup>

The above has shown what sound communication should consist of (the 7 “Cs”), why good and comprehensive feedback of the final decision is an essential element at all stages of a procurement procedure, even after the contract award, and how communication is contributing to the benefit of all parties involved.

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<sup>231</sup> Speidel, R.E. (1972). *Judicial and Administrative Review of Government Contract Awards*, [https://heinonline.org/HOL/Page?public=true&handle=hein.journals/lcp37&div=8&start\\_page=63&collection=journals&set\\_as\\_cursor=0&men\\_tab=srchresults](https://heinonline.org/HOL/Page?public=true&handle=hein.journals/lcp37&div=8&start_page=63&collection=journals&set_as_cursor=0&men_tab=srchresults), 37 *Law & Contemp. Probs.*, p. 63.

<sup>232</sup> Evans, C., & Cahill, D. (2019). *Feedback and Supplier Debriefing: The Unloved Child of SME-Friendly Procurement Practice*. *Public Contract Law Journal*, 48(4), pp. 710-711.

<sup>233</sup> *ibid.*, p. 712.

<sup>234</sup> Arrowsmith, S. (2018). *The law of public and utilities procurement: regulation in the EU and UK* (3rd ed.). Sweet & Maxwell, p. 926.

<sup>235</sup> *ibid.*, p. 927.

And that is why it is indeed beneficial to communicate in a transparent manner and to keep communicating throughout the process.

# The ECB's internal appeal procedure for contract award decisions

By Isabell Koepfer\*

## 1 Introduction

The European Central Bank (ECB) enjoys a particular status as a European Union (EU) institution and is as such exempt from national budgetary and national procurement laws. The ECB is however subject to EU law, including to EU procurement law. Against this background the ECB has, for its procurement needs, established its own legal framework for tender procedures. The legal framework includes an internal appeal procedure before the Procurement Review Body (PRB) which – having been established in 2007 – happens to celebrate its 15th anniversary in 2022.

ECB procurement rules allow unsuccessful candidates and tenderers in public tender procedures to contest the ECB's award and rejection decisions through an appeal before the PRB. The appeal procedure was created as a means to further strengthen the rule of law and the principle of good administration, two principles that are of great importance to the ECB. Procedural justice is an important building stone of the concept of rule of law, at the core of which lies the principle of equal treatment. Procedural justice helps to ensure the correct application of legal rules and can complement the role of judicial adjudication in preserving the rights of those which are subjects to those legal rules. Review bodies of administrative decisions are designed to enhance procedural justice as they offer the opportunity to the administration to review and, if need be, to reconsider a previous decision. The appeal procedure before the PRB is a typical example of such a remedy.

This year's anniversary of the internal appeal procedure presents a good opportunity to take a closer look at this procedure again and assess its merits over the past 15 years. This article proceeds, by way of background and context, by briefly explaining the status of the ECB as an EU institution and its implications for the applicability of procurement laws, providing an overview on the ECB procurement rules as well. Further, the article will particularly highlight those aspects of the procurement procedure that enable a candidate or tenderer to subsequently exercise legal remedies, including the internal appeal procedure. Important in this context is the communication between the tenderers and the contracting authority after the issuance of an award decision as foreseen in the ECB procurement rules, the legal remedies available to tenderers, in particular pre-contractual remedies, as well as the standstill period, a feature which allows the tenderers the opportunity to raise objections, request information, and also file an application with the Court of Justice of the

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European Union. Indeed, all these features are key for the application of the principles of transparency and good administration, and the right to an effective remedy, especially due to the broad margin of appreciation of contracting authorities.

## 2 Legal status of the ECB

The ECB, as an EU institution, has the autonomous power to lay down rules for its internal organisation and administration. By virtue of this general principle of public international law, the ECB is exempt from national laws on the internal organisation and administration of public authorities, and in particular from national budgetary or procurement laws.<sup>236</sup> This general privilege is reflected in national laws which provide for the exemption of international organisations from a particular field of law.<sup>237</sup> EU procurement directives<sup>238</sup> are also not applicable to ECB procurements as they are addressed to Member States, not to Union institutions.<sup>239</sup> Furthermore, the ECB is not bound by the rules set out in Title V of the Financial Regulation for contract award procedures conducted by Union institutions, because the ECB has its own budget which is separate from that of the European Union.<sup>240</sup>

This does not mean, however, that the ECB is entirely free and without limitations to establish its own procurement regime. The principles of the Treaties, and in particular the free movement of goods, the freedom of establishment and the freedom to provide services apply to public tender procedures carried out by Union institutions, even if they are not subject to EU procurement directives.<sup>241</sup> Furthermore, the award of contracts by public authorities within the EU must respect the principles deriving therefrom and which have been established by the Court of Justice, such as equal treatment, non-discrimination, mutual recognition, proportionality<sup>242</sup> and transparency. Since the ECB's award and rejection decisions in tender procedures are subject to judicial review by Union courts, the ECB also needs to observe the relevant procurement jurisprudence of the Court of Justice.<sup>243</sup>

Within such boundaries, the ECB has, as a legislator, established its own legal framework for procurement procedures: first by way of internal guidelines and, as of 2007, on the basis of binding ECB decisions adopted by the Executive Board and

<sup>236</sup> Koepfer (2016), p. 290; von Lindeiner (2016); Gruber and Benisch (2007), p. 11.

<sup>237</sup> For instance, according to Section 109(1) No 1b of the German Act against Restraints of Competition (Gesetz gegen Wettbewerbsbeschränkungen – GWB), international organisations are not subject to German procurement rules.

<sup>238</sup> Directive 2014/24/EU of the European Parliament and of the Council of 26 February 2014 on public procurement and repealing Directive 2004/18/EC (OJ L 94, 28.3.2014, p. 65); Directive 2014/23/EU of the European Parliament and of the Council of 26 February 2014 on the award of concession contracts (OJ L 94, 28.3.2014, p. 1).

<sup>239</sup> Case T-553/11, *European Dynamics Luxembourg v ECB*, EU:T:2014:275, para. 110.

<sup>240</sup> Article 2(b) of Regulation (EU, EURATOM) No 966/2012 of the European Parliament and of the Council of 25 October 2012 on the financial rules applicable to the general budget of the Union and repealing Council Regulation (EC, Euratom) No 1605/2002 (OJ L 298, 26.10.2012, p. 1) (the "Financial Regulation").

<sup>241</sup> Case C-324/98, *Telaustria and Telefonadress*, EU:C:2000:669, paras. 60-62. See also Arrowsmith (2014), pp. 7-26; von Lindeiner (2016).

<sup>242</sup> See Case C-213/07, *Michaniki*, EU:C:2008:731, para. 48; recital 1 and Article 18(1) of Directive 2014/24/EU; Arrowsmith (2014), pp. 7-24 and 25.

<sup>243</sup> Article 40 of the ECB procurement rules.

published in the *Official Journal of the European Union*.<sup>244</sup> In 2016, the ECB overhauled its procurement rules and adopted Decision ECB/2016/2 laying down the Rules on Procurement<sup>245</sup> (the “ECB procurement rules”), which to a large extent is modelled according to the EU procurement directives and the case-law of the Court of Justice.

The ECB procurement rules require that all procurements carried out by the ECB respect the principles of transparency, proportionality, publicity, equal access and equal treatment, non-discrimination and fair competition.<sup>246</sup> Furthermore, recital 4 of the ECB procurement rules states explicitly that the ECB respects the general principles of procurement as reflected in Directive 2014/24/EU and the Financial Regulation. Another important aspect of public procurement is that it involves the spending of public money. As a result, the ECB, as a public institution, is accountable for its actions and is committed to the principle of cost-efficiency. It thus seeks the best value for money for the products, works and services that it procures.

## 3 Legal framework

The ECB procurement rules apply to the award of supply, services, works and concession contracts. The tender procedure to be followed depends on the estimated contract value thresholds and the items to be procured. The applicable contract value thresholds refer to the applicable thresholds in the EU procurement directives.<sup>247</sup> Contracts with an estimated value equalling or exceeding the applicable threshold amount are awarded by public tender procedure. Contracts with an estimated value below the threshold amounts are awarded through a simplified procedure set out in Chapter III of the ECB procurement rules. Contracts with an estimated value below EUR 20 000 may be awarded directly to one supplier without a tender procedure.<sup>248</sup>

### 3.1 Types of procedures

The ECB procurement rules provide for the same public tender procedures as Directive 2014/24/EU: the open (Article 10 of the ECB procurement rules), restricted (Article 11) and negotiated (Article 12) procedures, competitive dialogue (Article 13) and innovation partnership (Article 14).<sup>249</sup> The ECB procurement rules also include special rules on electronic procurement, such as electronic auctions, electronic

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<sup>244</sup> Decision ECB/2007/5 of the European Central Bank of 3 July 2007 laying down the Rules on Procurement (OJ L 184, 14.7.2007, p. 34). The legal basis is Article 11(6) of Protocol (No 4) on the Statute of the European System of Central Banks and of the European Central Bank (the “Statute of the ESCB”). Decision ECB/2007/5 was amended by Decision ECB/2009/2 of the European Central Bank of 27 January 2009 (OJ L 51, 24.2.2009, p. 10), Decision ECB/2010/8 of the European Central Bank of 27 July 2010 (OJ L 238, 9.9.2010, p. 14) and Decision ECB/2012/10 of the European Central Bank of 19 June 2012 (OJ L 178, 10.7.2012, p. 14).

<sup>245</sup> Decision ECB/2016/2 of the European Central Bank of 9 February 2016 laying down the rules on procurement (OJ L 45, 20.2.2016, p. 15). See von Lindeiner (2016).

<sup>246</sup> Article 3 of the ECB procurement rules.

<sup>247</sup> Article 4(3) of the ECB procurement rules.

<sup>248</sup> Article 37 of the ECB procurement rules.

<sup>249</sup> For further details on detailed procedural rules see von Lindeiner (2016).

catalogues and the dynamic purchasing system. The ECB has gradually rolled out an electronic tendering system which allows tenderers to submit offers electronically. It has aligned its rules with the general requirements set out in Article 22 of Directive 2014/24/EU in conjunction with Annex IV thereto.

Contracts with an estimated value below the threshold amounts<sup>250</sup> and services pursuant to Article 6(2) in conjunction with Annex I of the ECB procurement rules are awarded through a simplified procedure – the so-called three or five quote procedure.<sup>251</sup> The Article 6(2) services are those listed in Annex XIV to Directive 2014/24/EU, and include health, social and related services, educational and cultural services, hotel and restaurant services, legal services, investigation and security services.<sup>252</sup> These categories of services have by their very nature a limited cross-border dimension. Only contracts for such services that equal or exceed EUR 750 000 are subject to full EU-wide transparency and require the publication of a contract notice in the *Official Journal*.<sup>253</sup>

### 3.2 Exemptions for special types of contract and exceptional cases

Certain types of contracts fall outside the scope of the ECB procurement rules.<sup>254</sup> While these categories of contract are exempt from the ECB procurement rules, this does not automatically mean that such contracts may be awarded directly to any supplier. The conclusion of such contracts must either follow a specific procedure (e.g. employment contracts) or be conducted in accordance with a selection process that ensures the best value for money.

Furthermore, the ECB procurement rules contain certain exceptions on the basis of which the ECB may deviate from specific procedural requirements or award a contract directly to one supplier.<sup>255</sup> These exceptions concern, for instance, situations where, for unavoidable reasons (i.e. of a technical, artistic or legal nature), the contract can only be awarded to one particular supplier; or situations where, for reasons of extreme

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<sup>250</sup> There is no publication requirement, thus the ECB has the discretion to select the tenderers to be invited, following proper market research and taking into account any possible cross-border interest. Up to a contract value of EUR 50 000, the number of tenderers to be invited is three, and above this value it is five. The process is a one-phase procedure that is largely similar to an open procedure, except that the ECB is free to stipulate the applicable time limits and can choose to conduct negotiations with the tenderers.

<sup>251</sup> Chapter III of the ECB procurement rules.

<sup>252</sup> The three/five quote procedure for Article 6(2) services with a publication requirement is similar to a simplified negotiated procedure. The publication of a contract notice usually leads to expressions of interest from suppliers who are invited to participate in the tender procedure on the basis of selection criteria. Other suppliers that meet the same criteria may also be invited to participate. The deadline for the submission of expressions of interest and tenders can be set at the reasonable discretion of the ECB.

<sup>253</sup> See recital 114 of Directive 2014/24/EU.

<sup>254</sup> See Article 2(3), (4) and (6) of the ECB procurement rules. These include, for instance, cooperation agreements between the ECB and other public institutions, contracts for the acquisition or rental of land or buildings, employment contracts, certain research and development contracts, arbitration and conciliation services, in-house contracts and contracts subsidised directly by the ECB under certain conditions. Furthermore, contracts relating to the legal representation of the ECB during or in preparation for court or arbitration proceedings and contracts for exclusive services of notaries, trustees and court officials are also exempt from the scope of the ECB procurement rules. The selection of experts serving as members of high-level advisory boards assisting the ECB in the fulfilment of its tasks is subject to a special procurement procedure.

<sup>255</sup> Article 6(1) of the ECB procurement rules.

urgency that could not have been foreseen by the ECB, the time limits for a procurement procedure cannot be met.<sup>256</sup>

These exceptions are to a large extent based on the cases set out in Article 32(2) of Directive 2014/24/EU. While the Directive restricts these situations to a negotiated procedure without prior publication, the ECB procurement rules allow more leeway, ranging from changing procedural requirements in the procurement process to a direct award to one supplier, if appropriate. Where possible, the ECB must ensure competition between several suitable suppliers.<sup>257</sup>

## 4 Communication of the outcome of the tender procedure

Correct communication of the outcome of the tender procedure to candidates and tenderers is very important to avoid objections and the exercise of remedies by unsuccessful candidates and tenderers. Article 34 of the ECB procurement rules specifies the respective notification requirements of the ECB.

Firstly, the ECB must communicate its award decision in writing and without undue delay to all candidates and tenderers whose applications or tenders are rejected.<sup>258</sup> The ECB notifies all concerned candidates and tenderers whose applications or tenders are rejected of the reasons for rejecting their application or tender as well as the duration of the standstill period referred to in Article 34(2). The notification of the award decision is sent within the so-called standstill period: at least 10 days prior to the signature of the contract by the ECB if the notification is sent by fax or electronic means and at least 15 days prior to the signature of the contract if other means of communication are used. Furthermore, any unsuccessful tenderer that has made an admissible tender can request the ECB in writing for the name of the successful tenderer as well as the characteristics and relative advantages of the successful tender. The ECB may decide to withhold certain information where its release would affect other suppliers' legitimate commercial interests, would hinder the application of the law, might prejudice fair competition between suppliers or would otherwise be contrary to the public interest.

### 4.1 Statement of reasons – legal requirements

Article 34(3) of the ECB procurement rules is modelled according to the corresponding provision in Article 113(2)) of the Financial Regulation that applies to the other Union

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<sup>256</sup> Further exceptions exist for contracts which have been classified as secret by the ECB or where special security measures are required, such as research and development contracts in the field of banknote security; for supply contracts where the relevant products are manufactured purely for the purpose of research, experimentation, study or development; in relation to purchases out of supplier bankruptcy and in the case of additional products acquired under a supply contract where a change of supplier would lead to disproportionate difficulties in operation and maintenance.

<sup>257</sup> In order to ensure transparency, the ECB publishes annually a list of contracts with a value above EUR 50 000 that have been awarded on the basis of non-public tender procedures or awarded to one particular supplier by way of exception under Article 6(1) of the ECB procurement rules, indicating the value and the subject matter of the contracts and the names of the successful tenderers.

<sup>258</sup> Article 34(1) of the ECB procurement rules.



institutions. The provision is in line with the relevant provisions in Directive 89/665/EEC<sup>259</sup> (Article 2a) in connection with Directive 2014/24/EU (Article 55), which require that all concerned candidates and concerned tenderers whose applications and tenders are admissible are notified of the reasons for rejecting their application or tender (“a summary of the relevant reasons”) as well as the duration of the standstill period.

In terms of scope of the information to be provided to an unsuccessful tenderer, the judgment of the General Court in the case *EUIPO v European Dynamics* from 3 May 2018<sup>260</sup> outlines the basic requirements for the statement of reasons to be provided by contracting authorities in outcome letters. In the case at issue, the contracting authority EUIPO provided in the outcome letter to the unsuccessful tenderer European Dynamics a comparative table setting out the number of points awarded to that tenderer and the number of points to the three tenderers that obtained the highest scores. Upon request, EUIPO provided a further extract of the evaluation report with a comparative table (quantitative, no written comments) comprising the qualitative scores of European Dynamics’ tender and the successful tenderers, on the basis of three criteria, as well as the names of the successful tenderers and a comparative table with the scores obtained for the two financial criteria and their respective weighting. However, EUIPO did not provide the relevant scores attributed to further sub-criteria of the three quality criteria. Therefore, the Court concluded that EUIPO had not entirely met the requirements concerning the obligation to state the reasons for the outcome of the evaluation of the tender.

The Court stated that:<sup>261</sup>

- the contracting authority cannot be required to communicate to an unsuccessful tenderer, first, in addition to the reasons for rejecting its tender, “a detailed summary of how each detail of its tender was taken into account” when the tender was evaluated and, second, in the context of notification of the characteristics and relative advantages of the successful tender, a detailed comparative analysis of the successful tender and of the unsuccessful tender;<sup>262</sup>
- the contracting authority is not obliged to provide an unsuccessful tenderer, upon written request from that tenderer, with a full copy of the evaluation report;<sup>263</sup>
- according to settled case-law of the Court, the statement of reasons required under the second paragraph of Article 296 TFEU must be assessed in the light of the circumstances of each case, in particular the content of the measure in question and the nature of the reasons given.<sup>264</sup>

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<sup>259</sup> Council Directive 89/665/EEC of 21 December 1989 on the coordination of laws, regulations and administrative provisions relating to the application of review procedures to the award of public supply and public works contracts (OJ L 395, 30.12.1989, p. 33) (the “Remedies Directive”).

<sup>260</sup> Case C-376/16P, para. 53 et seq.

<sup>261</sup> Case C-376/16P, para. 57 et seq.

<sup>262</sup> Case C-629/11PP, not published, EU:C:2012:617, para. 22 and the case-law cited therein.

<sup>263</sup> *ibid.*, para. 22.

<sup>264</sup> *ibid.*, para. 23 and the case-law cited therein.

More specifically in relation to the level of information provided by the contracting authority, the Court found that the comparative tables enabled European Dynamics to have an overall view of the points awarded to their tender and to those of the successful tenderers in relation to both the qualitative and the financial criteria, and of their effect on the final overall score. Settled case-law does not, in principle, require a specific weighting to be attached to every negative or positive comment in the evaluation.

However, where the procurement documents contain specific quantified weightings attached to criteria or sub-criteria, the principle of transparency requires a quantified evaluation to be given in respect of those criteria or sub-criteria.<sup>265</sup> It must be possible for the affected candidates and tenderers or a court either to understand the respective weightings of those (sub-)criteria in the evaluation, that is to say, in the determination of the total score, or to establish a correlation between the specific negative comments and the deductions of points that impacted that total score.

It follows that a decision must enable a tenderer to understand the reasons why its tender has been rejected and to identify the characteristics and relative advantages of the successful tenderers and must enable the EU judiciary to verify the legality of the assessment contained therein.

## 4.2 Previous notification regime

The current notification regime has been in place since the last revision of the ECB procurement rules in 2020. The predecessor notification scheme under Decision ECB/2016/2<sup>266</sup> foresaw a different and quite complex two step-procedure.

According to Article 34(3) of Decision ECB/2016/2, rejected candidates and tenderers could, within 15 days of receipt of the award decision, request the ECB to provide the reasons for rejecting their application or tender and to provide copies of all documents relating to the evaluation of their application or tender. Unsuccessful tenderers whose tender was admissible could also ask for the name of the successful tenderer as well as the key characteristics and relative advantages of their tender. To accommodate unsuccessful candidates and tenderers' right of access to evaluation documents, there was a standstill period of 10 or 15 days between the award and signature of contracts, which was extended in the event of additional requests for information. In some cases this led to a high administrative burden and delays in the subsequent contract award, which was one of the reasons why this notification regime was eventually revised by the current Decision ECB/2020/10.

Enhanced transparency considerations vis-à-vis unsuccessful tenderers provided another reason to revise the previous notification regime. One such consideration was the aim to give unsuccessful tenderer more information already with the outcome letter instead of only upon request. These endeavours coincided with new developments in EU case-law aiming to reinforce the right to an effective remedy. In its order in

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<sup>265</sup> Case C-376/16P, para. 63 et seq.

<sup>266</sup> Decision ECB/2016/2.

the *Vanbreda* case<sup>267</sup>, the General Court opened a new era for interim measures as it eased the conditions for the establishment of urgency and, moreover, introduced an objective criterion – that of the existence of a strong prima facie case. In the case at issue, the Court sustained an application for interim measures, concluding that it suffices that the applicant would suffer serious – instead of also irreparable – harm, in order to preserve the principle of effective judicial protection. Furthermore, the Court clarified that the provisions of the Remedies Directive are considered as reflecting and concretising the general principle of the right to an effective remedy and are therefore attributed the status of EU primary law. This is of particular importance for a Union institution such as the ECB, as the Remedies Directive does not apply to public procurement procedures of Union institutions.

In its order in the *Vanbreda* case, the General Court took an innovative approach while acknowledging the inefficiency of past case-law.<sup>268</sup> Over the years, the Court had developed strict case-law relating to the condition of urgency: “[u]rgency must be assessed in the light of the need for an interlocutory order in order to avoid serious and irreparable damage to the party seeking the interim relief.”<sup>269</sup> At the same time, according to settled case-law, “damage of a pecuniary nature cannot, save in exceptional circumstances, be considered as irreparable, financial compensation is generally capable of restoring the position of the person suffering the damage to what it had been before.”<sup>270</sup> The combination of the above two conclusions in settled case-law systematically led all interim relief applications submitted in the context of public procurement – being inherently linked to pecuniary damage – to fail the above test.

Contrary to its previous case-law, the Court stated in *Vanbreda* that the requirement to demonstrate irreparable harm could be satisfied only with excessive difficulty because of systemic reasons (para. 157). It therefore considered that such an outcome was irreconcilable with the obligation to provide for effective interim legal protection and the need for effective protection of the financial interests of the EU (para. 158).

## 5 Remedies and internal appeal procedure

As a further instrument to strengthen the legal remedies of candidates and tenderers, the ECB procurement rules allow unsuccessful candidates and tenderers in public tender procedures to contest the ECB’s award and rejection decisions through an appeal before the PRB.

The PRB is an internal body composed of senior managers and is independent from the office carrying out the award procedure. The review body has two main functions: Firstly, it offers an additional remedy whose purpose is to ensure that the lawfulness of the administrative decision is verified by a body separate from the one that took the decision, thereby giving due consideration to the principle of good administration.

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<sup>267</sup> Order of the General Court of 23 April 2015 in case C-35/15 P(R) *Vanbreda*.

<sup>268</sup> Korogiannakis (2017).

<sup>269</sup> Judgment in case C-180/01 P-R *Commission v NALOO* [2001] ECR I-5737, para. 52.

<sup>270</sup> Judgment in case C-213/91 R *Abertal and Others v Commission* [1991] ECR I-5109, para. 24.

Secondly, it aims for judicial economy, potentially decreasing the number of cases which reach the stage of judicial adjudication.

The appeal procedure is outlined in Article 39 of the ECB procurement rules and further specified in the internal mandate of the PRB. The mandate contains further rules on the adoption of decisions and specifies the role of the secretariat which assists the PRB in the performance of its tasks.

## 5.1 Conditions for lodging an appeal

According to Article 39(1) of the ECB procurement rules, candidates and tenderers in public tender procedures under Chapter II of the ECB procurement rules may challenge in writing the ECB's decision to reject their application or tender within 10 days of receipt of the notification, in accordance with Article 34(1) or the first sentence of Article 34(3) of the ECB procurement rules. The appeal has suspensive effect in relation to the award of the contract.

The appeal must include all supporting information and reasoned objections with the exception of any objections that are precluded in accordance with Article 28(2) of the ECB procurement rules. This provision bars certain objections relating to the incomplete, inconsistent or illegal nature of tender documentation and objections relating to infringements of the applicable procurement rules by the ECB or another candidate or tenderer, if they are not raised in time. It gives the ECB the opportunity to correct or supplement the requirements or remedy the irregularity, if need be. Objections which are not communicated to the ECB in time may not be raised at a later stage. Candidates and tenderers are precluded from raising them in the ECB appeal procedure and in proceedings before the Court of Justice.<sup>271</sup> The preclusion rule has recently been confirmed by the General Court in its judgment of 5 October 2022.<sup>272</sup>

If the appeal is admissible and well-founded, the PRB will annul the decision of the ECB and will either order the tender procedure or parts of it to be repeated or will take a final decision itself. If the appeal is inadmissible or unfounded, the PRB will reject the appeal. The PRB notifies the appellant in writing of its decision within one month following the receipt of the appeal. The decision must state the reasons on which it is based.

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<sup>271</sup> In *European Dynamics Luxembourg v ECB*, the General Court ruled that the preclusion rule in the former Article 21(2) of Decision ECB/2007/5 only relates to the tender procedure itself and does not extend to court proceedings. The General Court drew its conclusion from the unclear wording of the title and the text of the provision, see case T-553/11, *European Dynamics Luxembourg v ECB*, EU:T:2014:275, paras. 102-105; see Koepfer (2016), p. 296. The current Article 28 has been revised accordingly. The wording of the former Article 21(2) of Decision ECB/2007/5 (now superseded by Article 28(2) of Decision ECB/2016/2) read as follows: "If candidates or tenderers consider that the ECB's requirements laid down in the contract notice, the invitation to tender or supporting documents are incomplete, inconsistent or illegal or that the ECB or another applicant/tenderer has infringed the applicable procurement rules, they shall notify their objections to the ECB within 15 days. If the irregularities affect the invitation to tender or other documents sent by the ECB, the time limit shall start to run from the date of receipt of the documentation. In other cases, the time limit shall start to run from the moment the candidates or tenderers become aware of the irregularity or could reasonably have become aware of it. The ECB may then either correct or supplement the requirements or remedy the irregularity as requested, or reject the request indicating the reasons therefor. Objections which were not communicated to the ECB within 15 days may not be raised at a later stage."

<sup>272</sup> Case T-761/20, *European Dynamics Luxembourg v ECB*, para. 101.

If the appeal is rejected, an additional standstill period of at least 10 days prior to the signature of the contract by the ECB, if the notification is sent by fax or electronic means, or at least 15 days prior to the signature of the contract, if other means of communication are used, applies. The PRB notifies the appellant about the duration of the standstill period.

Following the conclusion of the appeal procedure, the appellant may seek legal relief from the General Court. Article 40(3) of the ECB procurement rules allows action to be brought before the Court only following an appeal decision.<sup>273</sup> The deadline for submission to the Court is two months from receipt of the appeal decision by the appellant.

Since the appeal procedure is only admissible in public tender procedures under Chapter II of the ECB procurement rules, claims in all other tender procedures can be brought directly before the General Court.

## 5.2 Scope of review by the PRB

The PRB examines whether the appeal is admissible and whether the decision of the ECB to reject the application or tender was taken in line with the ECB procurement rules and the general principles of EU procurement law.

Under settled case-law of the Court of Justice, the ECB, as any Union institution, has broad discretion in assessing the factors to be taken into account for the purpose of deciding to award a contract following an invitation to tender. This discretion extends to both the selection and the evaluation of the award criteria. Accordingly, a review of a contested decision is limited to checking compliance with the procedural rules and the duty to give reasons, verifying the correctness of the facts found and ensuring that there is no serious and manifest error of assessment or misuse of powers.<sup>274</sup>

### 5.2.1 Statement of reasons

Concerning the general requirements for the duty to state reasons, the General Court, in its 5 October 2022 judgment in *European Dynamics v ECB*, referred to settled case-law<sup>275</sup> according to which “the statement of reasons required by Article 296 TFEU must be appropriate to the measure at issue and disclose in a clear and unequivocal fashion the reasoning followed by the institution which adopted the measure, in such a way as to enable the persons concerned to ascertain the reasons for it and to enable the competent court to exercise its power of review. The requirements to be satisfied by the statement of reasons depend on the circumstances

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<sup>273</sup> The General Court appears to have accepted the approach by which the ECB established this mandatory requirement for admissibility in case T-553/11, *European Dynamics Luxembourg v ECB*, EU:T:2014:275 and case T-761/20, *European Dynamics Luxembourg v ECB*.

<sup>274</sup> Judgment of the General Court of 23 May 2014, *European Dynamics v ECB*, T-553/11, para. 229 and the case-law cited therein; judgment of the General Court of 26 January 2017, *TV1 v Commission*, T-700/14, paras. 44 and 90.

<sup>275</sup> Case T-761/20, *European Dynamics Luxembourg v ECB*, para. 119 et seq.

of each case, in particular the content of the measure in question, the nature of the reasons given and the interest which the addressees of the measure or other parties concerned by it, for the purposes of the fourth paragraph of Article 263 TFEU, may have in obtaining explanations. It is not necessary for the reasoning to go into all the relevant facts and points of law, since the question whether the statement of reasons meets the requirements of Article 296 TFEU must be assessed with regard not only to its wording but also to its context and to all the legal rules governing the matter in question.”<sup>276</sup>

In addition, it should also be borne in mind that the obligation to state adequate reasons, laid down in Article 296 TFEU, is an essential procedural requirement that must be distinguished from the question whether the reasoning is well founded, which goes to the substantive legality of the measure at issue.<sup>277</sup>

In the case at issue, the ECB as contracting authority excluded European Dynamics (the applicant) from a tender procedure for attempting to unduly influence the decision-making in the procurement procedure pursuant to Article 30(5)(g) of the ECB procurement rules. European Dynamics had sent letters to representatives of the ECB outside the foreseen procurement channels, including the President of the ECB. Following the exclusion and dismissal of the appeal by the PRB, European Dynamics brought an action before the General Court. The applicant sought the annulment of the decision of the ECB to exclude the applicant from the tender procedure at issue, the annulment of several related decisions and corresponding damages in the amount of EUR 23,29 million.

The Court dismissed the action of European Dynamics and followed the ECB’s view that the exclusion under Article 30(5)(g) of the ECB procurement rules was justified, because such letters were aimed at putting pressure on the recipients to intervene in said procedure, in particular, in the enquiry into the abnormally low nature of the applicant’s offer.<sup>278</sup> The Court found that the exclusion on this ground was proportionate and compliant with the ECB’s obligations to state reasons, and that the PRB had not misused its powers when rejecting the applicant’s appeal. Consequently, the Court also rejected the applicant’s claim for damages.

Concerning the duty to state reasons, the applicant claimed that the ECB did not state the exact reasons why the letters that the applicant had sent to the ECB were considered as intimidating. The Court came nevertheless to the conclusion that it was possible to understand the reasons for which the ECB considered the respective letters to unduly influence the decision-making process in the procurement procedure at issue.<sup>279</sup>

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<sup>276</sup> See Case C-279/08 P, *Commission v Netherlands*, EU:C:2011:551, para. 125 and the case-law cited therein.

<sup>277</sup> See Case C-367/95 P, *Commission v Sytraval and Brink’s France*, EU:C:1998:154, para. 67; Case C-17/99, *France v Commission*, EU:C:2001:178, para. 35; and Case C-521/09 P, *Elf Aquitaine v Commission*, EU:C:2011:620, para. 146.

<sup>278</sup> Case T-761/20, *European Dynamics Luxembourg v ECB*, para. 88.

<sup>279</sup> *ibid.*, para. 126.

Furthermore, the Court stated that in public procurement the obligation to state reasons pertaining to a decision may be fulfilled in several stages<sup>280</sup> and must be assessed in the light of the information available to the applicant at the time when the action was brought.<sup>281</sup>

## 5.2.2 No misuse of powers

According to settled case-law, the concept of misuse of powers refers to cases where an administrative authority uses its powers for a purpose other than that for which they were conferred on it. A decision may amount to a misuse of powers only if it appears, on the basis of objective, relevant and consistent factors, to have been taken for purposes other than those stated.<sup>282</sup>

In the above-mentioned case *European Dynamics v ECB*, the applicant claimed that the PRB put forward new arguments in its appeal decision and expanded the allegedly unfounded arguments relied on by the ECB's Procurement Committee in its exclusion decision. Accordingly, by not merely "reviewing" the lawfulness of that decision and examining the arguments put forward only by the applicant, the PRB had taken on the role of the contracting authority and exceeded the limits of its discretion, solely for the purpose of excluding the applicant from the procurement procedure at issue.

The Court followed the views of the ECB and ruled that the PRB is not required, in the context of its duty to state reasons, to confine itself to substantiating or supplementing the evidence relied on by the Procurement Committee but is entitled to set out its own considerations in responding to those arguments.<sup>283</sup> These observations imply a certain leeway for the PRB to improve and specify the reasoning of a contested decision.

## 5.3 Rules of procedure of the PRB

The appeal procedure is further specified in the mandate of the PRB. It is an ECB internal document that is not open to the public. The mandate contains further procedural rules, for instance, how decisions are adopted, absences of PRB members and conflicts of interests, and specifies the role of the secretariat which assists the PRB in the performance of its tasks.

The PRB is supported by the ECB's Directorate General Legal Services. It assists the PRB in the performance of its tasks; in particular, it provides PRB members with the relevant tender documentation and liaises with the Procurement Committee to clarify

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<sup>280</sup> *ibid.*, para. 121; see to that effect and by analogy, judgment of 19 March 2010, *Evropaiki Dynamiki v Commission*, T-50/05, EU:T:2010:101, para. 133 and the case-law cited therein, and judgment of 22 May 2012, *Sviluppo Globale v Commission*, T-6/10, not published, EU:T:2012:245, para. 29.

<sup>281</sup> Judgment of 25 February 2003, *Strabag Benelux v Council*, T-183/00, EU:T:2003:36, para. 58; and judgment of 25 February 2003, *Renco v Council*, T-4/01, EU:T:2003:37, para. 96.

<sup>282</sup> Case T-761/20, *European Dynamics v ECB*, para. 133; judgment of 23 May 2014, *European Dynamics Luxembourg v ECB*, T-553/11, EU:T:2014:275, para. 323 and the case-law cited therein.

<sup>283</sup> Case T-761/20, *European Dynamics v ECB*, para. 13.

facts; furthermore, it summarises the facts underlying the appeal, provides a preliminary legal assessment and prepares a first draft of the appeal decision.

## 5.4 Effectiveness of the remedy

The ECB receives on average five appeals per year. Since the establishment of the PRB in 2007, more than 70 appeals have been submitted to the PRB, approximately 10 % were upheld, the majority either rejected or settled by presenting the appellant with additional information that it had not asked for previously. On substance the appeals mainly relate to the evaluation of the tenders (e.g. assignment of scores) and compliance with selection criteria (e.g. requirements of reference projects).

The PRB appeal procedure has proven to be “an effective remedy” and “a robust internal review mechanism”, as confirmed by the General Court<sup>284</sup> and the European Court of Auditors<sup>285</sup>. The General Court evaluated the ECB’s PRB appeal procedure as follows: the ECB appeal procedure “is not merely a conciliation mechanism whose purpose is to reach an out of court settlement, but is an effective remedy whose purpose is to ensure that the lawfulness of the decision to reject the applicant’s application or bid is verified by a body separate from the one which made the initial rejection decision and giving rise to a decision open to judicial review.”<sup>286</sup>

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<sup>284</sup> Case T-553/11 *European Dynamics Luxembourg v ECB*, EU:T:2014:275, para. 32.

<sup>285</sup> European Court of Auditors (2016), Observation 80, p. 43.

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# Legal remedies against public procurement decisions from a national law perspective

By Jeffrey Dirix\*

## 1 Introduction

This contribution closes this series of articles on legal protection in public procurement. Where the two previous contributions focus on remedies against procurement decisions by two institutions of the European Union (EU), namely the European Central Bank (ECB) and the European Commission, and hence on applicable EU law,<sup>287</sup> this piece examines the legal options for tenderers to contest decisions made by national contracting authorities. Consequently, it approaches the topic from another angle, i.e. national public procurement law and, more specifically, Belgian public procurement law.<sup>288</sup>

First, this contribution highlights the legal framework applicable to decisions by national contracting authorities, including the legal remedies available against such decisions. Since (legal protection in) public procurement is to a large extent harmonised within the EU, the relevant EU directives are first discussed, followed by the Belgian law transposing those directives.

Second, this contribution gives an overview of contracting authorities' obligations under Belgian law to inform tenderers of their procurement decisions. Transparent communication is after all a prerequisite for effective legal protection.

Third, it provides an overview of the rules governing the standstill period after notification of the award decision, during which the contract cannot be concluded. Such standstill is necessary to allow unsuccessful tenderers to exercise their right to pre-contractual remedies.

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<sup>287</sup> See the provisions relevant for legal protection against procurement decisions of the ECB and the European Commission included in the Treaty on the Functioning of the European Union, in Decision (EU) 2016/245 of the European Central Bank of 9 February 2016 laying down the rules on procurement (ECB/2016/2) (OJ L 45, 20.2.2016, p. 15) and in Regulation (EU, Euratom) 2018/1046 of the European Parliament and of the Council of 18 July 2018 on the financial rules applicable to the general budget of the Union amending Regulations (EU) No 1296/2013, (EU) No 1301/2013, (EU) No 1303/2013, (EU) No 1304/2013, (EU) No 1309/2013, (EU) No 1316/2013, (EU) No 223/2014, (EU) No 283/2014, and Decision No 541/2014/EU and repealing Regulation (EU, Euratom) No 966/2012 (OJ L 193, 30.7.2018, p. 1).

<sup>288</sup> The author is a legal expert and staff member of the Nationale Bank van België/Banque Nationale de Belgique, which is a national central bank within the Eurosystem and a national competent authority within the Single Supervisory Mechanism.

Fourth, it discusses the legal remedies available in respect of procurement decisions by contracting authorities. Specific review procedures under Belgian law are examined in the context of the general principles set out in EU law. The focus is specifically on pre-contractual remedies as being arguably the most effective form of legal protection in the context of public procurement.

Finally, with reference to the fifteenth anniversary of the establishment of the ECB's Procurement Review Body as the trigger for this series of articles, this contribution looks at the possibilities under national law for internal review of procurement decisions. In the absence of a formal legal framework on internal review procedures under Belgian law, the contribution examines alternative methods that contracting authorities can explore on a voluntary basis to increase transparency and monitor the legal soundness of their procurement decisions with the aim of avoiding unnecessary litigation with tenderers.

## 2 Legal framework

EU law sets out minimum harmonised public procurement rules.<sup>289</sup> This contribution focuses on the rules applicable to “classic” sectors, i.e. the provisions included in Directive 2014/24/EU (“the Public Procurement Directive”). These rules were transposed into Belgian law by the Act of 17 June 2016 on public procurement (“the Public Procurement Act”) and the Royal Decree of 18 April 2017 on procurements in the classic sectors.

The standards for legal protection in public procurement are also based on EU law. For the classic sectors, see Council Directive 89/665/EEC<sup>290</sup> (“the Remedies Directive”). See also, for the utilities sector, Council Directive 92/13/EEC<sup>291</sup>. Both Directives have been substantially amended by Directive 2007/66/EC<sup>292</sup>. As noted above, this contribution focuses on the provisions applicable to the “classic” sectors.

Under this EU legal framework Member States must take the necessary measures to ensure that decisions taken by contracting authorities can be appealed effectively and swiftly. These obligations were transposed into Belgian law by the Act of 17 June 2013 on the statement of reasons, transparency obligations and legal protection concerning public procurement, utilities procurement and concession contracts (“the Transparency and Remedies Act”).

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<sup>289</sup> See in that regard (for the classic sectors) Directive 2014/24/EU of the European Parliament and of the Council of 26 February 2014 on public procurement and repealing Directive 2004/18/EC (OJ L 94, 28.3.2014, p. 65) and (for the utilities sectors) Directive 2014/25/EU of the European Parliament and of the Council of 26 February 2014 on procurement by entities operating in the water, energy, transport and postal services sectors and repealing Directive 2004/17/EC (OJ L 94, 28.3.2014, p. 243).

<sup>290</sup> Council Directive 89/665/EEC of 21 December 1989 on the coordination of the laws, regulations and administrative provisions relating to the application of review procedures to the award of public supply and public works contracts (OJ L 395, 30.12.1989, p. 33).

<sup>291</sup> Council Directive 92/13/EEC of 25 February 1992 coordinating the laws, regulations and administrative provisions relating to the application of Community rules on the procurement procedures of entities operating in the water, energy, transport and telecommunications sectors (OJ L 76, 23.3.1992, p. 14).

<sup>292</sup> Directive 2007/66/EC of the European Parliament and of the Council of 11 December 2007 amending Council Directives 89/665/EEC and 92/13/EEC with regard to improving the effectiveness of review procedures concerning the award of public contracts (OJ L 335, 20.12.2007, p. 31).

This (EU and national) framework on legal protection provides for pre-contractual and post-contractual remedies. Where the former are intended to correct infringements of public procurement rules in the course of the tendering procedure and, in any case, before the contract is concluded, the latter aim to declare unlawfully concluded contracts ineffective and/or to provide compensation after the conclusion of such contract. In the framework of this contribution, the focus is mainly on pre-contractual remedies.

However, this contribution first looks at the transparency obligations for contracting authorities in respect of their procurement decisions. Transparency is a prerequisite for effective pre-contractual legal protection.<sup>293</sup> See in that regard recital 6 of Directive 2007/66/EC:

“The standstill period should give the tenderers concerned sufficient time to examine the contract award decision and to assess whether it is appropriate to initiate a review procedure. When the award decision is notified to them, the tenderers concerned should be given the relevant information which is essential for them to seek effective review. The same applies accordingly to candidates to the extent that the contracting authority or contracting entity has not made available in due time information about the rejection of their application.”

### 3 Transparency obligations under Belgian law

Article 55(1) of the Public Procurement Directive provides that contracting authorities must as soon as possible inform each candidate and tenderer of their procurement decisions. It gives the unsuccessful tenderers the opportunity to take note of the decision, as well as of the reasons for that decision.<sup>294</sup> The following section looks at the way in which this principle has been transposed by the Belgian legislator.

In general, the Belgian legislator has opted for a system in which a single decision report is drawn up for each procurement decision. Subsequently, in cases where candidates and tenderers should only be informed about their own situation (cf. *infra*), extracts from this report are communicated. In other instances, unsuccessful candidates and tenderers should be given the opportunity to compare their situation with that of the tenderer(s)/candidates selected. In that case, the entire decision report is sent out. Consequently, the Belgian legislator went beyond the obligation set by Article 2a(2) of the Remedies Directive to provide “a summary” of the relevant reasons when communicating an award decision to each tenderer and candidate. The Belgian

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<sup>293</sup> In the same vein the Court of Justice of the European Union has held that “complete legal protection presupposes, first, an obligation to inform tenderers of the award decision” (Case C-212/02, *Commission v Austria*, EU:C:2004:386, para. 21) and that “it is only once a concerned candidate or tenderer has been informed of the reasons for its elimination from the public procurement procedure that it may come to an informed view as to whether there has been an infringement of the applicable provisions and as to the appropriateness of bringing proceedings” (Case C-406/08, *Uniplex*, EU:C:2010:45, para. 31). See also Dor, V. (2020) *La motivation, l’information et les recours en matière de marches publics*, Kluwer, p. 50.

<sup>294</sup> See Dujardin J., Van Damme, J., Vande Lanotte, J. and Mast, A. (2021), “De rechtsbescherming inzake overheidsopdrachten en concessies”, in *Overzicht van het Belgisch administratief recht*, Kluwer, No 254.

legislator's objective in this regard was to avoid contradictory documents or misinterpretations.<sup>295</sup>

First, when conducting two-stage procedures with a preliminary selection phase, Belgian contracting authorities have the obligation to inform unsuccessful candidates, immediately after taking the selection decision, of the reasons for the rejection of their application.<sup>296</sup>

For two-stage procedures where the contracting authority has limited the number of selected candidates by ranking them based on certain selection criteria, additional transparency obligations apply. In such cases the contracting authority should send the entire selection report to all unsuccessful candidates, including the names of the candidates or tenderers, whether selected or not, and the legal and factual reasons justifying their selection or non-selection (including the reasons underlying the ranking of the applications).<sup>297</sup>

Second, a contracting authority should inform all unsuccessful tenderers, immediately after taking the award decision, of the reasons for the rejection of their tender.<sup>298</sup> In addition, the contracting authority has the obligation to send the entire decision report to those tenderers that have submitted an admissible tender.<sup>299</sup> This report should include the name(s) of the successful tenderer(s) and of those tenderers whose bids, although admissible, were not selected. It should also state the legal and factual reasons for the award decision, including the characteristics and relative advantages of the selected bid.<sup>300</sup>

Third, when a contracting authority decides not to award a contract, it should, immediately after taking this decision, send the decision report to any candidate or tenderer that was still involved in the procedure.<sup>301</sup> This report should state the legal and factual reasons for the decision not to award the contract and, where applicable, mention the new award procedure that will follow.<sup>302</sup>

By means of exception, information regarding procurement decisions cannot be shared if the release of such information would impede law enforcement or would otherwise be contrary to the public interest, would prejudice the legitimate commercial

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<sup>295</sup> See De Koninck C., Flamey, P. and Bosquet, J. (2010), "Rechtsbescherming inzake overheidsopdrachten na de wet van 23 december 2009" (2010), in *Rechtskundig Weekblad*, 2009-2010, issue 40, No 11-13.

<sup>296</sup> Article 7, section 1, 1° of the Transparency and Remedies Act.

<sup>297</sup> Article 7, section 1, 2° of the Transparency and Remedies Act. See also Article 5, 6° of the Transparency and Remedies Act.

<sup>298</sup> Article 8, sections 1, 1° and 2° of the Transparency and Remedies Act.

<sup>299</sup> Article 8, section 1, 3° of the Transparency and Remedies Act.

<sup>300</sup> Article 5, 9° of the Transparency and Remedies Act.

<sup>301</sup> Article 9 of the Transparency and Remedies Act.

<sup>302</sup> Article 5, 10° of the Transparency and Remedies Act.

interests of a particular economic operator, whether public or private, or might prejudice fair competition between economic operators.<sup>303</sup>

For low value contracts up to a maximum of EUR 140 000 the transparency obligations are less strict. Contracting authorities can limit their communication to informing candidates and tenderers of the result of their decisions. Only after a candidate or tenderer has made a request to that effect does the obligation arise to communicate the reasons for the procurement decision within 15 days following such request.<sup>304</sup> However, a contracting authority can also decide to apply the more stringent transparency obligations for contracts above the threshold of EUR 140 000 to such low value contracts on a voluntary basis.<sup>305</sup>

## 4 The standstill period

After notifying the (unsuccessful and the successful) tenderers of the award decision,<sup>306</sup> Belgian contracting authorities are required to observe a standstill period of 15 days.<sup>307</sup> During this standstill period the contract cannot be concluded.<sup>308</sup> This therefore gives unsuccessful tenderers the opportunity to assess the award decision and, potentially, apply for a review procedure.<sup>309</sup>

If an unsuccessful tenderer applies for review by starting a suspension procedure (see *infra*) within 15 days of notification, the standstill will be extended until the review body has given its judgment.<sup>310</sup> In this way, unsuccessful tenderers benefit from effective

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<sup>303</sup> Article 10 of the Transparency and Remedies Act. It should be noted that in the context of litigation the competent review body (e.g. the Belgian Council of State, cf. *infra*) should also ensure confidentiality of certain (commercial) information included in the procurement files submitted to its judgment. When deciding to what extent and in what way the confidentiality and secrecy of such information must be ensured, the competent body should take into account the requirements of effective judicial protection, of the rights of defence of the parties and of a procedure respecting the right to a fair trial. See Article 26 of the Transparency and Remedies Act. See also De Koninck, C., Flamey, P. and Bosquet, J. (2010), "Rechtsbescherming inzake overheidsopdrachten na de wet van 23 december 2009", in *Rechtskundig Weekblad*, 2009-2010, Issue 40, No 54.

<sup>304</sup> Article 29/1, sections 1 and 2 of the Transparency and Remedies Act. See also De Koninck, C., Flamey, P. and Bosquet, J. (2010), "Rechtsbescherming inzake overheidsopdrachten na de wet van 23 december 2009", in *Rechtskundig Weekblad*, 2009-2010, Issue 40, No 7.

<sup>305</sup> The Nationale Bank van België/Banque Nationale de Belgique, for example, consistently applies the provisions applicable above the threshold also to low value contracts. A contracting authority might decide to do so to enhance transparency and to anticipate the information requests that might otherwise follow. Furthermore, this approach might be beneficial from the perspective of procedural simplicity, by allowing the application of the same notification procedures regardless of the contract value. Finally, this approach is mandatory when a contracting authority voluntarily applies the contractual standstill for low value procurements (cf. *infra*).

<sup>306</sup> Under Belgian law contracting authorities should carry out a dual notification, simultaneously via registered mail and via fax or electronic means. See Article 9/1 of the Transparency and Remedies Act.

<sup>307</sup> See Article 11 of the Transparency and Remedies Act. In this respect, the Belgian legislator went beyond the minimum standstill period of 10 days applicable if fax or electronic means are used to notify the tenderers that is provided for in Article 2a(2) of the Remedies Directive.

<sup>308</sup> See also Article 8, section 2 of the Transparency and Remedies Act.

<sup>309</sup> See *supra* the reference to recital 6 of Directive 2007/66/EC. See De Koninck, C., Flamey, P. and Bosquet, J. (2010), "Rechtsbescherming inzake overheidsopdrachten na de wet van 23 december 2009", in *Rechtskundig Weekblad*, 2009-2010, Issue 40, No 21.

<sup>310</sup> Article 11 of the Transparency and Remedies Act.

pre-contractual review and, if the review body finds that the award decision is flawed, keep intact their chances of winning the procurement.<sup>311</sup>

No standstill is required for procedures with an estimated contract value below the EU threshold amounts.<sup>312</sup> Hence, the effectiveness of pre-contractual remedies is significantly greater for procedures above these thresholds than for those below them.

However, for works contracts of a value exceeding 50 % of the EU threshold amount, contracting authorities should nevertheless observe the standstill.<sup>313</sup> The same goes for contracts with an initial estimated value below the threshold but with an actual value upon award of more than 20 % above the threshold.<sup>314</sup> In this way, contracting authorities are discouraged from making an artificially low estimate of the contract value.<sup>315</sup>

Furthermore, no standstill is required (i) for procedures that are exempt from prior publication under EU law, (ii) if there is only one tenderer,<sup>316</sup> and (iii) for contracts based on a framework agreement.<sup>317</sup>

Nevertheless, a contracting authority can decide to apply a standstill period in any event for procurement procedures even if they are exempt from this obligation. In this way, by enhancing the effectiveness of a pre-contractual remedy a contracting authority may avoid long and costly post-contractual litigation, e.g. a claim for damages.<sup>318</sup>

## 5 External review procedures under Belgian law

This section gives an overview of the review procedures that are available to unsuccessful tenderers. Both pre-contractual and post-contractual legal protection mechanisms are highlighted.

Specific attention is given to pre-contractual review procedures because, first, they allow a tenderer that has suffered harm as a result of an unlawful decision to continue to compete for the contract in question. Second, such pre-contractual review usually results in legal certainty in the short term, avoiding lengthy legal disputes. Third, pre-contractual remedies may benefit the society as a whole by rectifying situations where contracts might otherwise be awarded to tenderers that did not submit the most

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<sup>311</sup> Dor, V. (2020) *La motivation, l'information et les recours en matière de marchés publics*, Kluwer, p. 67.

<sup>312</sup> Currently EUR 5 382 000 for works contracts and EUR 215 000 for supply and service contracts.

<sup>313</sup> Article 30 of the Transparency and Remedies Act.

<sup>314</sup> Article 3 of the Transparency and Remedies Act.

<sup>315</sup> See De Koninck, C., Flamey, P. and Bosquet, J. (2010), "Rechtsbescherming inzake overheidsopdrachten na de wet van 23 december 2009", in *Rechtskundig Weekblad*, 2009-2010, issue 40, No 5.

<sup>316</sup> This exception only applies if there are no candidates concerned, meaning that there are no candidates still involved in the tender procedure for which the contracting authority has not made available information about the rejection of their application before the notification of the contract award decision.

<sup>317</sup> Article 12 of the Transparency and Remedies Act.

<sup>318</sup> De Koninck, C., Flamey, P. and Bosquet J. (2010), "Rechtsbescherming inzake overheidsopdrachten na de wet van 23 december 2009", in *Rechtskundig Weekblad*, 2009-2010/40, No 5 and Dor, V. (2020) *La motivation, l'information et les recours en matière de marchés publics*, Kluwer, p. 71.

economically advantageous offer and can avoid claims for damages against contracting authorities.<sup>319</sup> Consequently, one might consider that pre-contractual review is the most effective form of legal protection.

Within 15 days following the notification of an allegedly flawed procurement decision<sup>320</sup> any person who has or has had an interest in obtaining a particular contract and who has been or is likely to be prejudiced by this decision can apply for its suspension.<sup>321</sup> Consequently, the standstill period and the time limit for applying for pre-contractual review are aligned.

The competent review body can also (i) order other interim measures to rectify the alleged violation or prevent harm and (ii) order interim measures necessary for the enforcement of its judgment.<sup>322</sup>

In respect of procurement decisions by Belgian administrative authorities<sup>323</sup> the Belgian Council of State is competent to rule on applications for suspension. Some contracting authorities – for example private hospitals and educational institutions – do not qualify as administrative authorities.<sup>324</sup> Review of procurement decisions by such authorities can be sought before the Belgian judicial courts.<sup>325</sup> This contribution, however, focuses on the procedure before the Council of State.<sup>326</sup>

Applications submitted to the Council of State need not demonstrate urgency or serious or irreparable harm.<sup>327</sup> There is also no need, for admissibility purposes, for proof that the tender submitted is the most economically advantageous one. The suspension procedure is accordingly an accessible form of review.<sup>328</sup>

If, after a prima facie evaluation<sup>329</sup>, the Council of State finds that the case is based on serious grounds or an apparent illegality, it will suspend the procurement decision.<sup>330</sup>

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<sup>319</sup> De Koninck, C., *Thematische fiche rechtsbescherming inzake overheidsopdrachten*, 2021, [www.mercatus.kluwer.be](http://www.mercatus.kluwer.be)

<sup>320</sup> Article 23, section 3 of the Transparency and Remedies Act.

<sup>321</sup> Article 15 of the Transparency and Remedies Act. Unsuccessful tenderers have an “interest” within the meaning of this provision. See Vermeire, L. and Vos, I. (2015), “Rechtsbescherming inzake overheidsopdrachten bij de Raad van State: een eerste stand van zaken na de rechtsbeschermingswet van 17 juni 2013 en de hervorming van de Raad van State in 2014”, in *Tijdschrift voor Bestuurswetenschappen en Publiekrecht*, 2015/6, No 26 and Dor, V. (2020) La motivation, l’information et les recours en matière de marchés publics, Kluwer, pp. 113-116.

<sup>322</sup> Article 15 of the Transparency and Remedies Act. One example of a possible interim measure might be an order to allow a candidate whose application was wrongly rejected to continue to participate to the tender procedure by submitting an offer. Another example would be an order by the review body to the contracting authority to take a new decision.

<sup>323</sup> Article 14, section 1 of the coordinated laws on the Council of State of 12 January 1973.

<sup>324</sup> De Koninck, C., Flamey, P. and Bosquet, J. (2010), “Rechtsbescherming inzake overheidsopdrachten na de wet van 23 december 2009”, in *Rechtskundig Weekblad*, 2009-2010, issue 40, No 49.

<sup>325</sup> Article 24 of the Transparency and Remedies Act.

<sup>326</sup> The Council of State has confirmed on several occasions that it is competent to hear cases brought against procurement decisions of the Nationale Bank van België/Banque Nationale de Belgique. See, for example, Council of State, Case 52.701, 5 April 1995, *Van Roey*.

<sup>327</sup> Dor, V. (2020) La motivation, l’information et les recours en matière de marchés publics, Kluwer, pp. 118-119.

<sup>328</sup> Cf. Vermeire, L. and Vos, I. (2015), “Rechtsbescherming inzake overheidsopdrachten bij de Raad van State: een eerste stand van zaken na de rechtsbeschermingswet van 17 juni 2013 en de hervorming van de Raad van State in 2014”, in *Tijdschrift voor Bestuurswetenschappen en Publiekrecht*, 2015/6, No 15 and 27.

<sup>329</sup> Dor, V. (2020) La motivation, l’information et les recours en matière de marchés publics, Kluwer, pp. 132-133.



Nevertheless, the Council of State should respect the contracting authority's margin of discretion in procurement matters. Accordingly, the Council of State must limit its proceedings to a legality review and cannot take a final decision in place of the contracting authority.<sup>331</sup>

The legal pleas submitted by the applicant may refer to discriminatory technical, economic or financial specifications, to abuse of power or to infringements of (i) EU and national public procurement law, (ii) applicable constitutional, statutory and regulatory provisions as well as general principles of law, and (iii) the tender documents.<sup>332</sup>

In addition, the legal pleas and arguments put forward by the applicant can only be accepted (i) if the infringement or irregularity could influence or has influenced the disputed decision or the decision-maker's competence or (ii) if it has deprived the applicant of a guarantee.<sup>333</sup> An unsuccessful tenderer might for example argue that its bid was wrongly declared inadmissible or that the tender documents are flawed.

In the same vein, the ranking of the tenders can be relevant when assessing the admissibility of a plea. For example, an applicant who submitted an admissible tender that was only ranked sixth will bear the burden of proof of demonstrating that, if the grounds they put forward are found to be serious, this could lead to a new assessment with their tender appearing as the most advantageous.<sup>334</sup>

Furthermore, the Council of State may take into account the probable consequences of a suspension or other interim measures for all interests likely to be harmed, as well as the public interest, and may decide not to grant such measures when their negative consequences could exceed their benefits. A decision not to grant suspension or interim measures on such grounds will not prejudice any other claim of the person seeking such measures.<sup>335</sup>

However, the Council of State applies this balancing of interests clause with caution.<sup>336</sup> The Council has decided only on rare occasions not to suspend the

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<sup>330</sup> Article 15 of the Transparency and Remedies Act.

<sup>331</sup> Dujardin J., Van Damme, J., Vande Lanotte, J. and Mast, A. (2021), "De administratieve en juridictionele beroepen", in *Overzicht van het Belgisch administratief recht*, Kluwer, 2021, No 1184.

<sup>332</sup> Article 14 of the Transparency and Remedies Act.

<sup>333</sup> Article 14, section 1 of the coordinated laws on the Council of State of 12 January 1973; Vermeire, L. and Vos, I. (2015), "Rechtsbescherming inzake overheidsopdrachten bij de Raad van State: een eerste stand van zaken na de rechtsbeschermingswet van 17 juni 2013 en de hervorming van de Raad van State in 2014", in *Tijdschrift voor Bestuurswetenschappen en Publiekrecht*, 2015/6, No 25.

<sup>334</sup> Vermeire, L. and Vos, I. (2015), "Rechtsbescherming inzake overheidsopdrachten bij de Raad van State: een eerste stand van zaken na de rechtsbeschermingswet van 17 juni 2013 en de hervorming van de Raad van State in 2014", in *Tijdschrift voor Bestuurswetenschappen en Publiekrecht*, 2015/6, No 32 - 33 and the cited case-law of the Council of State.

<sup>335</sup> Article 14 of the Transparency and Remedies Act. The Belgian legislator has thus made use of the option provided in Article 2(5) of the Remedies Directive.

<sup>336</sup> Dor, V. (2020) *La motivation, l'information et les recours en matière de marchés publics*, Kluwer, pp. 123-125.

disputed decision based on such grounds.<sup>337</sup> In this regard, Belgian legal doctrine refers to pre-contractual and preventive legal protection in procurement matters as a general principle of EU law. Therefore, the balancing of interests clause should be interpreted strictly and only applied in overriding situations.<sup>338</sup>

The suspension procedure against a procurement decision before the Council of State is both effective and rapid. A judgment generally follows within the month after submission of the application.

When an application for suspension has been submitted, the standstill period is extended until the Council of State has given its judgement. If a contracting authority concludes the contract despite the standstill, a suspension of the award decision by the Council of State will automatically lead to the suspension of the contract execution.<sup>339</sup>

After an award decision has been suspended by the Council of State, the applicant should in principle within the time limits provided by law apply for annulment of the decision or, if the contract has already been concluded in violation of the standstill, submit a claim to declare the contract ineffective (see *infra*). If no such application or claim is submitted, the suspension of the award decision (and/or the contract) will be lifted by the Council of State.<sup>340</sup>

However, after the suspension of a procurement decision by the Council of State, a contracting authority will often revoke the decision at issue. In this way the contracting authority can avoid an extended period of litigation and legal uncertainty.<sup>341</sup> Taking into account the judgment of the Council of State, the contracting authority can subsequently take a new award decision or decide not to award the contract and possibly retender.

An application for annulment of a procurement decision<sup>342</sup> should be submitted within 60 days following the notification.<sup>343</sup> Again, the Council of State is the competent review body for procedures against procurement decisions by administrative authorities and the judicial courts for proceedings against decisions by other contracting authorities (cf. *supra*).<sup>344</sup>

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<sup>337</sup> In Case 188.958 of 18 December 2008, *Sanofi Pasteur MSD*, the Council of State considered that the disadvantage suffered by the applicant by losing the opportunity to carry out the assignment at issue – the supply of vaccines – was outweighed by the risks of vaccination programs being interrupted in case of a suspension of the award decision. Hence, priority was given to the public interest regarding public health. See also Vermeire, L. and Vos, I. (2015), “Rechtsbescherming inzake overheidsopdrachten bij de Raad van State: een eerste stand van zaken na de rechtsbeschermingswet van 17 juni 2013 en de hervorming van de Raad van State in 2014”, in *Tijdschrift voor Bestuurswetenschappen en Publiekrecht*, 2015/6, No 41.

<sup>338</sup> Besides the vaccine case, legal doctrine points also at urgently necessary dike works after a flood as a possible example. See De Koninck, C., Flamey, P. and Bosquet, J. (2010), “Rechtsbescherming inzake overheidsopdrachten na de wet van 23 december 2009”, in *Rechtskundig Weekblad*, 2009-2010/40, No 35.

<sup>339</sup> Article 13 of the Transparency and Remedies Act.

<sup>340</sup> Article 13 of the Transparency and Remedies Act.

<sup>341</sup> De Koninck, C., Flamey, P. and Bosquet, J. (2010), “Rechtsbescherming inzake overheidsopdrachten na de wet van 23 december 2009”, in *Rechtskundig Weekblad*, 2009-2010/40, No 31.

<sup>342</sup> Article 14 of the Transparency and Remedies Act.

<sup>343</sup> Article 23, section 2 of the Transparency and Remedies Act.

<sup>344</sup> Article 24 of the Transparency and Remedies Act.

In the framework of an annulment procedure against a procurement decision by an administrative authority the Council of State makes a final assessment of the applicant's legal pleas and arguments. In the event of annulment, the decision is annulled with retroactive effect.<sup>345</sup>

Furthermore, any person with an interest in obtaining a contract with a value above the EU thresholds<sup>346</sup> can, if that contract has already been concluded by the contracting authority, bring an action before the judicial courts<sup>347</sup> requesting that the contract be declared ineffective.<sup>348</sup>

Ineffectiveness was introduced in public procurement law by Directive 2007/66/EC to "combat the illegal direct award of contracts" and as "the most effective way to restore competition and to create new business opportunities for those economic operators which have been deprived illegally of their opportunity to compete".<sup>349</sup> However, in practice we see that this procedure is rather rarely used by unsuccessful tenderers as opposed to the suspension procedure.<sup>350</sup>

The introduction of this new procedure by the European Legislator was in line with earlier case-law of the Court of Justice of the European Union rejecting a purely civil law approach whereby wrongfully concluded public contracts were considered inviolable – on the basis of the *pacta sunt servanda* principle – and such infringements could only give rise to compensation in the form of damages.<sup>351</sup>

The court will declare a contract ineffective in the following situations:<sup>352</sup>

- The contracting authority has concluded a contract without prior publication at EU level although such publication was required by law.<sup>353</sup>
- The contracting authority has concluded a contract in violation of the standstill period and (i) this infringement has deprived the tenderer of the possibility to pursue pre-contractual remedies and (ii) this infringement is combined with a violation of the EU Procurement Directive affecting the tenderer's chances of securing the contract.

<sup>345</sup> Cf. Dujardin J., Van Damme, J., Vande Lanotte, J. and Mast, A. (2021), "De administratieve en jurisdictionele beroepen", in *Overzicht van het Belgisch administratief recht*, Kluwer, 2021, No 1187.

<sup>346</sup> This also applies to works contracts with a value exceeding 50 % of the EU threshold amount (see Article 32 of the Transparency and Remedies Act) and contracts with an initial estimated value below the EU threshold but with an actual value upon award of more than 20 % above the threshold (see Article 3 of the Transparency and Remedies Act).

<sup>347</sup> The Council of State is not competent to rule on requests to declare a contract ineffective.

<sup>348</sup> A time limit of 6 months applies to this procedure. See article 23, section 5 of the Transparency and Remedies Act.

<sup>349</sup> See recitals 13 and 14 of Directive 2007/66/EC.

<sup>350</sup> Dor, V. (2020) *La motivation, l'information et les recours en matière de marchés publics*, Kluwer, p. 145.

<sup>351</sup> Joined Cases C-20/01 and C-28/01, *Commission v Germany*, EU:C:2003:220; and Case C-503/04, *Commission v Germany*, EU:C:2007:432. See also De Koninck, C., Flamey, P. and Bosquet, J. (2010), "Rechtsbescherming inzake overheidsopdrachten na de wet van 23 december 2009", in *Rechtskundig Weekblad*, 2009-2010/40, No 1.

<sup>352</sup> Article 17 of the Transparency and Remedies Act.

<sup>353</sup> However, this is not applicable if the contracting authority (i) considers that the award of a contract without prior publication of a contract notice is permissible under EU law, (ii) has published a notice for voluntary ex ante transparency expressing its intention to conclude the contract, and (iii) has not concluded the contract before the expiry of a period of at least 10 calendar days following the date of the publication of this notice. See Article 18 of the Transparency and Remedies Act.

- The contracting authority has concluded a contract based on a framework agreement but without respecting the procedures provided by law.

When declaring a contract ineffective the competent court can decide to annul all contractual obligations with retroactive effect or limit the scope of annulment to those obligations that still have to be performed.<sup>354</sup> In the latter case, the court also imposes a fine on the contracting authority.<sup>355</sup>

The court may decide not to declare the contract ineffective, even though it has been awarded illegally on the grounds previously mentioned, if it finds, after having examined all relevant aspects, that overriding reasons of public interest require that the effects of the contract should be maintained.<sup>356</sup> The Belgian legislator indicated, by example, that the court should refuse to declare ineffective a contract for certain purchases of medicines, such as vaccines, by hospitals, where this would immediately jeopardise patient care.<sup>357</sup>

In such case, the court will instead impose alternative penalties, i.e. the imposition of a fine on the contracting authority or the shortening of the duration of the contract.<sup>358</sup>

With regard to this balancing of interests the following principles apply:

- Economic interests in the effectiveness of the contract may only be considered as overriding reasons if in exceptional circumstances ineffectiveness would lead to disproportionate consequences.
- However, economic interests directly linked to the contract concerned cannot constitute overriding reasons relating to a general interest. Economic interests directly linked to the contract include, inter alia, costs resulting from delay in execution of the contract, costs resulting from the launching of a new procurement procedure, costs resulting from a change of the economic operator performing the contract and costs entailed in legal obligations resulting from the ineffectiveness of the contract.

Finally, a claim for damages can be submitted<sup>359</sup> both in the course of an annulment procedure before the Council of State and in the form of a standalone procedure before the judicial courts.<sup>360</sup>

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<sup>354</sup> Article 19 of the Transparency and Remedies Act.

<sup>355</sup> Article 22 of the Transparency and Remedies Act.

<sup>356</sup> Article 20 of the Transparency and Remedies Act.

<sup>357</sup> See the explanatory memorandum annexed to the Act of 23 December 2009 inserting a new chapter on the statement of reasons, information and remedies in the Public Procurement Act, DOC 52-2276/001, pages 36-37, <https://www.dekamer.be/FLWB/pdf/52/2276/52K2276001.pdf>. See also De Koninck, C., Flamey, P. and Bosquet, J. (2010), "Rechtsbescherming inzake overheidsopdrachten na de wet van 23 december 2009", in *Rechtskundig Weekblad*, 2009-2010/40, No 42 and Dor, V. (2020) La motivation, l'information et les recours en matière de marchés publics, Kluwer, pp. 139-141.

<sup>358</sup> Article 22 of the Transparency and Remedies Act.

<sup>359</sup> Article 16 of the Transparency and Remedies Act.

<sup>360</sup> Article 24 of the Transparency and Remedies Act.

## 6 Internal review mechanisms

This last section examines the internal review possibilities for unsuccessful tenderers. The procedure before the ECB's Procurement Review Body is an example of an organised form of internal review.<sup>361</sup> Such internal review procedure may be offered with the object of guaranteeing an independent second assessment on the regularity of the outcome of the procurement and settling controversies without litigation.<sup>362</sup>

In the same vein, Article 1(5) of the Remedies Directive, which was introduced by Directive 2007/66/EC, provides that "Member States may require that the person concerned first seek review with the contracting authority".

However, when transposing Directive 2007/66/EC the Belgian legislator did not include this organised internal review procedure in the Belgian legal framework.<sup>363</sup> Hence, no organised internal review procedures apply to decisions made by contracting authorities in Belgium.

No reasons for this omission were made explicit in the explanatory memorandum attached to the draft law, and the issue was not commented upon in Belgian legal doctrine. Therefore, we have no clarity as to the reasons for not making use of this option provided by the Remedies Directive.<sup>364</sup>

However, in the absence of organised internal review procedures, Belgian contracting authorities can explore and implement alternative approaches with the same objectives of increasing transparency, accountability and good governance and avoiding unnecessary litigation.

First, during the standstill period unsuccessful tenderers can request additional information.<sup>365</sup> In that context, tenderers can refer to the general law principle of public access to official documents.<sup>366</sup>

Second, when receiving a complaint from an unsuccessful tenderer regarding a procurement decision during the standstill period, a contracting authority can on a voluntary basis make a thorough assessment of such complaint. To enhance the objectivity of such additional assessment, the contracting authority might involve an "independent" department.<sup>367</sup>

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<sup>361</sup> Article 39 of Decision (EU) 2016/245 of the European Central Bank of 9 February 2016 laying down the rules on procurement.

<sup>362</sup> Von Lindeiner, F., Bitti, G. and Hermans, M. (2019), "The European Central Bank and EU procurement law: a comparative outlook", in *Legal Working Paper Series 18*, 2019, point 3.4.1, available via <https://www.ecb.europa.eu/pub/pdf/scplps/ecb.lwp18~b5e787176e.en.pdf>.

<sup>363</sup> In some other areas of law, the Belgian legislator did provide for internal review procedures, e.g. internal review of decisions from educational institutions and internal review of public access decisions.

<sup>364</sup> The legislator may have considered the external pre-contractual remedies sufficient. Furthermore, the complex Belgian State structure might have been seen as an obstacle. Alternatively, budgetary considerations may have been behind this decision, given that organising internal review procedures also entails additional costs for the contracting authorities.

<sup>365</sup> Such requests are of course without prejudice to applicable confidentiality rules, see *supra*.

<sup>366</sup> See Article 32 of the Belgian Constitution and the Public Administration Act of 11 April 1994.

<sup>367</sup> At the Nationale Bank van België/Banque Nationale de Belgique, the legal department is involved in such proceedings. However, other departments might also qualify, e.g. internal audit or compliance.

If the complaint is considered unfounded, the contracting authority can start a dialogue with the tenderer involved with the aim of convincing them of the legality and validity of the decision at issue and avoiding follow-up litigation.

However, if the contracting authority finds merit in the complaint, it can revoke the disputed procurement decision.<sup>368</sup> Thereafter, it can take a new decision rectifying the previous error or decide not to award the tender and possibly retender.

Proceedings such as these constitute a form of voluntary administrative review. Under Belgian public law doctrine the possibility of requesting an administrative authority to review a decision it has taken constitutes a general principle of law.<sup>369</sup>

As voluntary administrative review does not in itself extend the standstill or the time limit for the submission of an application for suspension, the interactions between the contracting authority and the tenderer will be subject to strong time pressure. Therefore, the Belgian legislator might consider amending the Transparency and Remedies Act in the future by granting contracting authorities the possibility to extend the standstill and suspend the time limit for applying for suspension on a voluntary basis.<sup>370</sup>

Third, even after an unsuccessful tenderer has applied for suspension, the contracting authority can still explore ways to enhance transparency, accountability and good governance. Consequently, a contracting authority might make a thorough assessment of the application for suspension, not only in view of preparing its defence but also to objectively evaluate the applicant's arguments. The contracting authority might involve its legal department and/or an external law firm.

Again, if the contracting authority finds merit in the applicant's arguments, it can decide to revoke its decision. In that case, the suspension procedure becomes devoid of purpose and the review body - the Council of State for decisions by administrative authorities, see *supra* – will not examine the case further.<sup>371</sup>

Thereafter, the contracting authority can take a new decision correcting its previous error or decide not to award the tender and possibly retender.

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<sup>368</sup> During the standstill, the contract cannot yet be concluded. If the contracting authority, on the basis of an additional assessment in that period, finds that the award decision is flawed, the latter can be revoked. See Article 85 of the Public Procurement Act and Dor, V. (2020) *La motivation, l'information et les recours en matière de marchés publics*, Kluwer, p. 57-58. Cf., Dujardin J., Van Damme, J., Vande Lanotte, J. and Mast, A. (2021), "De administratieve en juridictionele beroepen", in *Overzicht van het Belgisch administratief recht*, Kluwer, 2021, No 1187-1191.

<sup>369</sup> This principle also applies in the absence of an explicit statutory or regulatory provision. See Dujardin J., Van Damme, J., Vande Lanotte, J. and Mast, A. (2021), "De administratieve en juridictionele beroepen", in *Overzicht van het Belgisch administratief recht*, Kluwer, 2021, No 1166-1172.

<sup>370</sup> Cf., Dor, V. (2020) *La motivation, l'information et les recours en matière de marchés publics*, Kluwer, p. 62.

<sup>371</sup> For an example of a case where the Nationale Bank van België/Banque Nationale de Belgique decided on its own initiative to revoke an award decision after assessing an application for suspension that was submitted by an unsuccessful tenderer, see Case 251.610 of 24 September 2021, *Seris Technology*. Subsequently, the Nationale Bank van België/Banque Nationale de Belgique made a new award decision based on a modified ranking of the tenders. In the context of a new suspension procedure brought by the now unsuccessful tenderer that was previously ranked first, the Council of State upheld this second decision of the Nationale Bank van België/Banque Nationale de Belgique. See Case 253.941 of 8 June 2022, *Siemens*.

## 7 Conclusion

This contribution has assessed the issue of legal protection in procurement matters from a national law perspective.

The applicable EU directives and Belgian law transposing those directives provide for a robust system where contracting authorities must observe a standstill period after notifying unsuccessful tenders of an award decision and the underlying reasons for that decision. An accessible, effective and rapid suspension procedure before the Council of State is available as a pre-contractual remedy. In addition, contracts that are awarded illegally can be declared ineffective.

Therefore, transparency and standstill obligations coincide with effective review procedures. As a result, a tenderer who has suffered prejudice within the tendering process can keep intact their prospects of securing the contract by applying for pre-contractual review. In addition, lengthy litigation and legal uncertainty can be avoided.

An unsuccessful tenderer is entitled to start a procedure against a procurement decision made by the ECB before the ECB's Procurement Review Body. This amounts to a form of organised internal administrative review that can enhance transparency, accountability and good governance. Furthermore, unnecessary litigation can be avoided in that way.

In the same vein, the Remedies Directive allows Member States to provide for such organised internal administrative review. However, the Belgian legislator did not make use of that option.

Nonetheless, a Belgian contracting authority can on a voluntary basis provide for some form of internal administrative review, both before and after a suspension procedure has been started. Therefore, also in the absence of explicit statutory or regulatory provisions, contracting authorities have possibilities to strengthen their procurement procedures and avoid lengthy and costly litigation.

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## Panel 5

# The General Data Protection Regulation and its relevance for banking supervision



# On the General Data Protection Regulation and its relevance for banking supervision

By Klaus Lackhoff\*

As was mentioned by Chiara Zilioli in her opening speech, the European Union is built on the rule of law. And fundamental rights are at the heart of a legal order built on the rule of law – they are the fundament of such a legal order. Consequently, the whole legal order built on them must be thought through from the perspective of fundamental rights.

Accordingly, fundamental rights must, within the applicable limits, be respected by all legal acts created within the legal framework of the EU. Legislative acts like regulations and individual decisions, for example, must comply with them.

Data protection is a fundamental right enshrined in Article 8 of the Charter of Fundamental Rights of the European Union (the “Charter”). Article 8 of the Charter is in principle a *lex specialis* to Article 7 of the Charter, protecting the privacy of private life and of communication and this provision in turn matches Article 8 of the European Convention of Human Rights.

Consequently, banking supervisors – including the ECB – must comply with the rules of data protection enshrined in the Charter. For national banking supervisors, the national legal system may establish even additional obligations.

The data protection related obligations of public authorities are further elaborated, in particular, in two regulations.

The first is [Regulation \(EU\) 2016/679](#), more commonly known as the General Data Protection Regulation (the GDPR). This Regulation establishes the data protection framework applicable to organisations established in the EU, as well as to organisations based outside the EU that intentionally offer goods or services to the EU or monitor the behaviour of individuals within the EU.

The second is [Regulation \(EU\) 2018/1725](#) (the EUDPR). This Regulation establishes the rules applicable to the processing of personal data by EU institutions, bodies, offices and agencies. These rules are similar though not always identical to the rules of the GDPR. However, whenever the provisions of the EUDPR follow the same principles as the GDPR, those two sets of provisions should, according to the case law of the Court of Justice of the European Union, be interpreted homogeneously, in particular because the scheme of the EUDPR should be understood as equivalent to the scheme of the GDPR (see recital 5 of the EUDPR).

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A first dimension of the relationship between data protection and banking supervision is, consequently, how banking supervisors can ensure compliance with the obligations under the data protection rules.

Such compliance may sometimes be challenging, for example if in an on-site inspection individual credit files will be reviewed. Such compliance may also require adjustments to standard processes but, as we will see, it is possible.

In this context we will also see how the diverging interests of the data subjects whose data are concerned and the supervisors – being controllers and processors under the EUDPR and GDPR – are balanced by the law or have to be balanced in a concrete case.

A second dimension to the relationship between data protection and banking supervision may not be as obvious.

Banking supervisors are subject to confidentiality obligations. The professional secrecy regime is established as counterpart to the broad obligations of supervised entities to provide information to supervisors. It requires banking supervisors to keep confidential not publicly known data, the disclosure of which is likely to adversely affect either the proper functioning of the system for banking supervision, or the interest of the person who provided the information or a third party (for the ECB as banking supervisor see Article 27 of the Single Supervisory Mechanism Regulation).

Therefore, the professional secrecy regime shall protect among other things the legitimate interests of supervised entities and may as such be demanded by fundamental rights like the freedom to conduct a business. This right enshrined in Article 16 of the Charter also protects commercial secrets against interference by banking supervisors, among others.

In most situations, the obligation of supervisors to keep certain information confidential and the obligations under data protection rules coincide. However, there may also be cases where a data subject may invoke rights under the GDPR or EUDPR which would require a supervisor not to comply with professional secrecy rules. This may for example be the case where an individual asks for access to personal data stored with the supervisor and which the supervisor received from an institution.

As should be clear from this brief introduction, data protection rules may raise tricky questions. However, we are lucky to have with us Karolina Mojzesowic, Sandrine Letocart and Maarten Daman – experienced speakers that will be able to navigate us through these difficult waters. In order to tackle the two above mentioned dimensions, the first speaker of this panel, Karolina Mojzesowic, will first introduce the basic principles and definitions of the data protection Regulations as well as the most relevant rights of the individual under this legislation. Thereafter, Sandrine Letocart will discuss the professional secrecy obligations of banking supervisors and potential conflicts with rights of data subjects. Finally, Maarten Daman will provide a view on the issue of how banking supervisors can ensure compliance with the data protection rules and manage the challenges connected therewith, as well as a view on the role of the Data Protection Officer in this environment.

# Professional secrecy and the rights of data subjects under the EU data protection framework

By Sandrine Letocart\*

The protection of personal data is an area of EU law that has received considerable and increasing attention over the last decade. It is enshrined in two provisions of primary law of general application, four legal acts of secondary EU law are exclusively devoted to the protection of personal data<sup>372</sup> and the topic occupies a non-negligible place in other acts of secondary law.<sup>373</sup> A similar trend can also be observed with respect to the agenda of EU Courts.<sup>374</sup>

Technological development is undoubtedly a driver behind this evolution. By facilitating the collection and treatment of personal data, technology has brought the collection and use of personal data to a broader scale in quantitative and qualitative terms, thereby increasing the need for protection. But other factors, of a more structural nature, also explain the importance of the topic in EU law. Indeed, the protection of personal data is intimately related to the exercise of the four free movement freedoms, which underpin the internal market.<sup>375</sup> Some scholars even see

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<sup>372</sup> The *General Data Protection Regulation* (Regulation (EU) 2016/679 of the European Parliament and of the Council of 27 April 2016 on the protection of natural persons with regard to the processing of personal data and on the free movement of such data, OJ L 119, 4.5.2016, p. 1); the EU Institutions Data Protection Regulation (Regulation (EU) 2018/1725 of the European Parliament and of the Council of 23 October 2018 on the protection of natural persons with regard to the processing of personal data by the Union institutions, bodies, offices and agencies and on the free movement of such data, OJ L 295 of 21.11.2018, p. 39); the *Police and Justice Data Protection Directive* (Directive (EU) 2016/680 of the European Parliament and of the Council of 27 April 2016 on the protection of natural persons with regard to the processing of personal data by competent authorities for the purposes of the prevention, investigation, detection or prosecution of criminal offences or the execution of criminal penalties, and on the free movement of such data, OJ L 119 4.5.2016, p. 89); and the *Directive on privacy and electronic communications* (Directive 2002/58/EC of the European Parliament and of the Council of 12 July 2002 concerning the processing of personal data and the protection of privacy in the electronic communications sector, OJ L 201, 31.7.2002, p.37) spanning together over 200 pages of legislation.

<sup>373</sup> See, for example, Articles 40 to 43 of the *Anti-Money Laundering Directive* (Directive (EU) 2015/849 of the European Parliament and of the Council of 20 May 2015 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing, OJ L 141 5.6.2015, p. 73), and Articles 56, 81 and 93 of the *Clinical Trials Regulation* (Regulation (EU) No 536/2014 of the European Parliament and of the Council of 16 April 2014 on clinical trials on medicinal products for human use, OJ L 158 27.5.2014, p. 1).

<sup>374</sup> See, notably, the chapter devoted to the protection of personal data in the Annual Report 2021 on the Judicial Activity of the Court of Justice of the European Union, available at this address: <https://curia.europa.eu/jcms/upload/docs/application/pdf/2022-07/qd-ap-22-001-en-n.pdf>. The research and documentation directorate of the Court of Justice also published no fewer than four notes on this topic over the last five years.

<sup>375</sup> See, for example, recital 3 of the Data Protection Directive (Directive 95/46/EC of the European Parliament and of the Council of 24 October 1995 on the protection of individuals with regard to the processing of personal data and on the free movement of such data, OJ L 281, 23.11.1995, p. 31).

the protection of personal data as a precondition for the full exercise of other fundamental rights.<sup>376</sup>

It is therefore topical that the 2022 edition of the ESCB Legal Conference devoted a panel discussion to the legal aspects of the protection of personal data, and proposed to examine its relevance for banking supervision, which is also a topic of current interest and a cornerstone of the protection of the integrity of the single currency and the internal market.<sup>377</sup> In this context, the present contribution analyses the interaction between the right to the protection of personal data and the duty of professional secrecy of supervisory authorities.

## 1 The rights of data subjects

The right to the protection of personal data is a fundamental right whose recognition in the EU legal order is established in Article 8 of the Charter of Fundamental Rights of the European Union<sup>378</sup> and Article 16 of the Treaty on the Functioning of the European Union.<sup>379</sup> The Charter lays down conditions for the processing of personal data and identifies the basic rights of data subjects, i.e. the right to access personal data which have been collected concerning them and the right to have it rectified (Article 8(2) of the Charter). To ensure the effectiveness of these rights, data subjects are also entitled to being informed that personal data concerning them is being processed. These rights and the corresponding obligations apply to EU institutions, and to the Member States when they are implementing EU law (Article 51 of the Charter) or, in other words, when they carry out activities falling within the scope of EU law (Article 16(2) of the Treaty).

The content of the right to data protection is further spelled out in several legal acts of secondary law.<sup>380</sup> In particular, the EU data protection framework is contained in two EU regulations adopted on the basis of Article 16(2) of the Treaty: the General Data Protection Regulation (GDPR) and the European Union Data Protection Regulation (EUDPR)<sup>381</sup>. The EUDPR subjects the processing of personal data by EU institutions and bodies to similar rules as those laid down in the GDPR.

As an EU institution, the European Central Bank (ECB) is bound by Article 8 of the Charter and is subject to the EUDPR. In this context, the ECB has certain obligations vis-à-vis subjects of personal data. Notably, the ECB must proactively inform data subjects that it is processing personal data concerning them when such data were

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<sup>376</sup> See Rouvroy A. and Pouillet Y. (2009), “The Right to Informational Self-determination and the Value of Self-Development: Reassessing the Importance of Privacy for Democracy”, in *Reinventing data protection?* edited by S. Gutwirth, et al., Springer Science & Business Media, p. 76. An unsettling aspect of this view is that, to a certain extent, it is based on the premise of the inefficiency of the protection of these other fundamental freedoms.

<sup>377</sup> See e.g. recitals 2 and 3 of the SSM Regulation (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>378</sup> OJ C 326, 26.10.2012, p. 393.

<sup>379</sup> OJ C 202, 07.06.2016, p. 47.

<sup>380</sup> See above, footnotes 2 and 3.

<sup>381</sup> See above, footnote 2.

obtained from a third party (Article 16 EUDPR). Under Article 17 EUDPR, data subjects have the right to access their personal data. This means that, on the request of data subjects, the ECB as data controller must inform them whether it processes personal data concerning them. In the affirmative, the ECB must inform these data subjects of the type of personal data it processes<sup>382</sup>, the purpose of this processing<sup>383</sup> and of the content of the personal data<sup>384</sup>. In this latter respect, while the data subject's right of access applies to "raw" personal data used as a factual basis for the analysis carried out by the administration (in particular, to allow them to check the accuracy of such personal data), this right of access does not extend to the analysis and the assessment subsequently produced by the administration.<sup>385</sup>

## 2 The duty of professional secrecy

At the same time, as an authority competent for the prudential supervision of credit institutions, the ECB is bound by a duty of professional secrecy that prevents the disclosure of confidential information. To avoid misunderstandings, note that this contribution does not address possible conflicts between data protection and banking secrecy, which is defined as the prohibition for banks to disclose information concerning their clients.<sup>386</sup>

The legal basis for the supervisory authorities' duty of professional secrecy is Article 53 of the Capital Requirements Directive (CRD).<sup>387</sup> This provision is made applicable to the ECB by the reference contained in Article 27(1) of the SSM Regulation to "relevant acts of Union law".

Article 53 of Capital Requirements Directive and Article 27(1) of the SSM Regulation impose a duty of professional secrecy on natural persons,<sup>388</sup> but it is clear that this

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<sup>382</sup> In this respect, reference to generic categories is sufficient, such as: contact details, education, working experience, shareholdings, business activities and criminal records. The obligation to provide such information also aims to allow the data subject to verify the legality of the processing.

<sup>383</sup> I.e. in this case, that the processing is done for the purpose of the exercise of the tasks conferred on the ECB by the SSM Regulation. The obligation to provide such information aims to allow the data subject to verify the legality of the processing.

<sup>384</sup> This obligation aims to allow the data subject to exercise their right to rectification.

<sup>385</sup> Judgment of 17 July 2014, *YS and others*, C-141/12, EU:C:2014:2081, paras. 39 to 48, and the Opinion of Advocate General Kokott, para. 59. Compare with the different solution in the judgment of 27 December 2017 (*Nowak*, C-434/16, EU:C:2017:994). However, it appears from the opinion of the Advocate General that, in that latter case, the assessment was physically inseparable from the personal data (paras. 62 and 63).

<sup>386</sup> In certain legal orders, banking secrecy is directly imposed by law (e.g. in France, Article L511-33 of the French Monetary and Financial Code). In other jurisdictions, banks are not subject to a duty of professional secrecy in the strict sense (i.e. a prohibition of disclosure imposed by law and criminally sanctioned). Rather, they are subject to a duty of discretion derived by the case-law from the duty of confidentiality inherent to the contractual relationship between a bank and its clients (e.g. in Belgium, Cass., 28 October 1978, Pas., 1979, I, p. 237; J.T., 1979, p. 371) or resulting from express provisions in the banks' general terms and conditions (e.g. in Germany, No. 2(1) of the template of the terms and conditions developed by the Association of German Banks).

<sup>387</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 (OJ L 176, 27.6.2013).

<sup>388</sup> Article 53(1) CRD applies to "all persons working for or who have worked for the competent authorities and auditors or experts acting on behalf of the competent authorities". Article 27(1) of the SSM Regulation imposes a duty of professional secrecy on "Members of the Supervisory Board, staff of the ECB and staff seconded by participating Member States". See also in primary law Article 37 of the ESCB Statute and Article 339 TFEU.

duty also directly binds the supervisory authority *itself*, and not merely through the natural persons identified in these provisions.<sup>389</sup> In the same vein, while the text of Article 53 of the Capital Requirements Directive refers to information received in the performance of supervisory tasks, the duty of professional secrecy extends to information produced in this context (e.g. supervisory assessments and supervisory decisions).<sup>390</sup>

The duty of professional secrecy only covers information that is confidential. However, the concept of confidential information is not defined in the Capital Requirements Directive or other relevant EU legislation.<sup>391</sup> The formula defining this concept was coined by the Court of justice in the *Baumeister* case. According to the *Baumeister* test, confidential information is “information held by the competent authorities: (i) which is not public and (ii) the disclosure of which is likely to adversely affect the interests of the person who provided that information or of third parties, or the proper functioning of the system [for banking supervision]”.<sup>392</sup>

This duty of professional secrecy flows from a duty to protect legitimate interests entrusted to supervisory authorities.<sup>393</sup> The primary aim of professional secrecy is therefore not to safeguard the private commercial interests of the banks concerned; it first and foremost pursues the objective of general public interest to preserve the proper functioning of the system for banking supervision. As a matter of fact, the absence of confidentiality is liable to compromise the smooth transmission of confidential information from banks to their supervisors and between supervisory authorities and, thereby, impair the proper performance of the supervisor’s task of monitoring entities subject to banking supervision. These considerations were stressed by the Court of justice in a string of rather recent preliminary rulings.<sup>394</sup>

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<sup>389</sup> For a textual confirmation, see e.g. Article 53(2), first subparagraph, CRD and the provisions on exchange of information between authorities in Articles 56 to 61 CRD, which are conceived as exceptions to the duty of professional secrecy. See also *Baumeister*: “the aim of professional secrecy is to impose on the competent authorities the obligation to refuse, as a general rule, to disclose confidential information” (Judgment of 19 June 2018, *Bundesanstalt für Finanzdienstleistungsaufsicht v Ewald Baumeister*, C-15/16, EU:C:2018:464 paras. 44 and 45).

<sup>390</sup> This is implicitly confirmed in *Baumeister* (para. 35): the duty of professional secrecy covers information whose disclosure would adversely affect “the proper functioning of the system for [banking supervision]”. See also in paragraph 56 the reference to the protection of “information relating to the supervision methodology and strategy employed by the competent authorities”.

<sup>391</sup> In this respect, see the plea for the adoption of a uniform professional secrecy standard by Smits, R. and Badenhoop, N. (2019), “Towards a Single Standard of Professional Secrecy for Financial Sector Supervisory Authorities: A Reform Proposal”, *European Law Review*, Issue 44:3, pp. 295-318.

<sup>392</sup> While the *Baumeister* case concerned the interpretation of Article 54 MIFID, the application of the same test to define “confidential” information in the context of Article 53 CRD, which has a similar wording, was implicitly confirmed in a subsequent judgement of the Court of Justice of the same year (*Buccioni*, C-594/16, paras. 29 and 30) and more recently by the General Court in a judgment of 6 October 2021 (*Organización de Consumidores y Usuarios v ECB*, T-15/18, paras. 121 to 128).

<sup>393</sup> Koupepidou, E. (2020), “Introduction to the panel on transparency versus confidentiality of supervisory decisions, documents and information”, *ESCB Legal Conference*, p. 219 et seq.; see also Farinhas, C. (2019), “Access to confidential information in the financial and banking sectors: judgements of the Court of Justice”, in Altmann, Baumeister, UBS and Buccioni *Law and Financial Markets Review*, 13(4), pp. 204 and 207; Smits, R. and Badenhoop, N. op.cit. footnote 19, p. 307.

<sup>394</sup> Judgment of 11 December 1985, *Commune de Hillegom v Cornelis Hillenius*, C-110/84, EU:C:1985:495, para. 27; Judgment of 12 November 2014, *Altmann and Others*, C-140/13, EU:C:2014:2362 paras. 31-33; Judgment of 19 June 2018, *Bundesanstalt für Finanzdienstleistungsaufsicht v Ewald Baumeister*, C-15/16, EU:C:2018:464 paras. 31-35; Judgment of 13 September 2018, *Enzo Buccioni v Banca d'Italia*, C-594/16, EU:C:2018:717 paras. 27-29; Judgment of 13 September 2018, *UBS Europe SE*, C-358/16, EU:C:2018:715 paras. 36-38.



### 3 The intersection of the rights of data subjects and the duty of professional secrecy of supervisory authorities

Against this background the question of the interaction between the general public interest protected by professional secrecy and the fundamental right of data subjects to be informed about the processing of their personal data and to access such data arises. Are they antagonistic and, if so, how can they be reconciled? In other words, in cases where compliance with the rights of information and the right of access of data subjects would imply the disclosure of information protected by professional secrecy, does professional secrecy tump data protection, or is it the other way around?

This question is not purely theoretical. Even though the primary subjects of prudential supervision are not data subjects, but legal persons, supervisory authorities nevertheless process a fair amount of personal data, for instance for the purpose of assessing the suitability of shareholders or proposed acquirers of qualifying holdings or for fit and proper assessments concerning members of the management body.<sup>395</sup>

No exception limiting the right to data protection is contained in Article 8 of the Charter.<sup>396</sup> However, fundamental rights do not constitute unfettered prerogatives, and their exercise may be restricted, provided that the restriction pursue objectives of general interest and that they do not involve, in the light of the objectives pursued, a disproportionate and intolerable interference that impairs the very substance of the guaranteed rights.<sup>397</sup> These limits, identified in the case law before the adoption of the Charter, were incorporated in its Article 52(1), which subjects restrictions to fundamental rights to the following conditions: the restriction is provided for by law, respects the essence of the rights it affects, pursues an objective of general interest recognised by the EU and is proportionate and necessary to meet this objective.

If the aforementioned conditions are fulfilled, secondary EU law may lay down exceptions to the fundamental right of protection of personal data. In this respect, the objective of Article 53 CRD is of a general interest that is recognised by EU law. However, this provision does not seem to meet the condition of being a restriction ‘provided for by law’ within the meaning of Article 52(1) of the Charter, since this condition was interpreted by the Court as requiring “that the legal basis which permits the interference with those rights must itself define the scope of the limitation on the exercise of the right concerned [and] lay down clear and precise rules governing the scope and application of the measure in question and imposing minimum safeguards”.<sup>398</sup>

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<sup>395</sup> An exemplative list of personal data processed by the ECB in the performance of the prudential supervisory tasks conferred on it by the SSM Regulation is contained in recital 5 of Decision ECB/2021/42 (Decision (EU) 2021/1486 of the European Central Bank of 7 September 2021 adopting internal rules concerning restrictions of rights of data subjects in connection with the European Central Bank’s tasks relating to the prudential supervision of credit institutions, OJ L 328 of 16.9.2021, p. 15).

<sup>396</sup> Compare with the right to access an administrative file (as part of the right to good administration), which is expressly limited by the protection of “*the legitimate interests of confidentiality and of professional and business secrecy*” (Article 41(2), point (b), of the Charter).

<sup>397</sup> Judgment of 13 September 2018, *UBS Europe SE*, C-358/16, EU:C:2018:715, para. 62 and the case-law cited.

<sup>398</sup> Judgment of 16 July 2020, *Facebook Ireland and Schrems*, C-311/18, EU:C:2020:559, paras. 175 and 180, and the case-law cited.

In addition, the CRD does not exclude information covered by professional secrecy from the scope of the EU data protection framework, on the contrary. As a matter of fact, Article 62 CRD establishes that the processing of personal data in accordance with that Directive is subject to the obligations that flow from data protection legislation<sup>399</sup> thereby confirming that the ECB is subject to the obligations that flow from the EUDRP, including in the performance of its prudential supervisory tasks. The reference in Article 62 to “the processing” of personal data should not be interpreted as a limitation of the application of the EU data protection framework, whereby the provisions concerning the rights of data subjects in Chapter III GDPR and EUDPR would, by contrast, be excluded. Such a distinction between processing and the rights of data subjects is not supported by the EU data protection framework whose *ultima ratio* is precisely to ensure the protection of the rights of data subjects with regard to the processing of their personal data.<sup>400</sup>

Under Article 27(1) of the SSM Regulation, the ECB’s duty of professional secrecy in the performance of its supervisory tasks is governed by Article 37 of the Statute of the ESCB and by “relevant acts of Union law”, which notably covers the CRD. Article 27(2) of the SSM Regulation makes a similar reference to “relevant Union law” with respect to the conditions under which the ECB may exchange of information with other authorities in the performance of its prudential supervisory tasks. It cannot be concluded from the absence of a reference in Article 27 of the SSM Regulation to data protection rules that the EU legislator intended to exclude the performance of the ECB’s prudential supervisory tasks from the scope of the EU data protection framework. As a matter of fact, Article 62 CRD is inserted in the section of this directive entitled on exchange of information and professional secrecy, so that it is implicitly covered by Article 27 of the SSM Regulation. This interpretation is confirmed by recital 81 of the SSM Regulation, which clearly states that the EU data protection framework is “fully applicable to the processing of personal data by the ECB for the purposes of [the SSM Regulation]”.

By contrast, all the conditions identified in Article 52(1) of the Charter are met by the EUDRP, which contains specific provisions laying down in a precise manner the restrictions that may be applied to the rights of data subjects.<sup>401</sup> Article 16(5), point (d), contains a specific exception according to which the controller’s obligation to inform data subjects that it is processing data collected by third parties (as opposed to data obtained directly from the data subject) does not apply where such data must remain confidential subject to an obligation of professional secrecy regulated by EU law, including a statutory obligation of secrecy. However, the EUDPR does not contain a general exception excluding from the scope of the EUDPR personal data that might be processed by the ECB in the performance of the prudential supervisory tasks conferred by the SSM Regulation or that might be covered by the ECB’s professional secrecy.

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<sup>399</sup> Article 62 CRD, in conjunction with Article 94 GDPR and Article 99 EUDPR, respectively.

<sup>400</sup> On the extensive interpretation of the concept of ‘processing’ and of the scope of application of the EU data protection framework, see the opinion of Advocate General Bobek in case [C-245/20](#), *Autoriteit Persoonsgegevens*, EU:C:2021:822, paras. 55 to 65.

<sup>401</sup> See notably the following provisions of the EUDPR: Articles 16(5), 17(4), 19(3), and Article 25.

It follows from the provisions of the Charter, the CRD, the SSM Regulation and the EUDPR, that supervisory authorities cannot, as a general exception, oppose their duty of professional secrecy to data subjects seeking to enforce their rights under the EU data protection framework. However, this conclusion should not give rise to concerns for supervisors mindful to preserve the mutual trust in the respect of confidentiality, which is a key element for the proper functioning of the system for prudential supervision.

As a matter of fact, the right of access of data subjects covers data concerning natural persons only, and data subjects can only claim access to data concerning themselves. In the light of the definition of confidential information protected by supervisory authorities' professional secrecy duty,<sup>402</sup> it is not clear in which cases the disclosure to a natural person of data concerning itself could adversely affect: the interests of the person who provided the data, the interests of third parties, or the proper functioning of the system for banking supervision. In addition, the right of access of data subjects should in principle not extend to the assessment that is based on the accessible "raw" personal data.<sup>403</sup>

## 4 Reconciling professional secrecy and the rights of data subjects

However, in case a conflict nevertheless exists between professional secrecy and the data subjects' right of access, the EU data protection framework offers tools to reconcile data protection obligations on the one hand and professional secrecy on the other.<sup>404</sup>

As a matter of fact, Article 25 EUDPR allows the adoption of restrictions on the rights of data subjects, subject to certain conditions that largely mirror those set out in Article 52(1) of the Charter.<sup>405</sup> These restrictions must pursue one of the objectives of general interest listed in Article 25(1), which notably refers to the safeguarding of important objectives of general public interest of the EU or a Member State (in particular their economic or financial interests) and of regulatory functions connected with the exercise of an official authority (points (c) and (g), respectively).

The ECB implemented this option by adopting Decision ECB/2021/42.<sup>406</sup> Under Article 3(1) of this Decision, the rights of data subjects may be restricted where the exercise of those rights would jeopardise or adversely affect the performance of the ECB's supervisory tasks under the SSM Regulation, including the proper functioning of the supervisory system. This corresponds to the last part of the *Baumeister* test, i.e. the protection of the proper functioning of the system.<sup>407</sup> At the same time, Article 3(1), point (a), of Decision ECB/2021/42 seems a bit broader than part of the

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<sup>402</sup> See above, section 2.

<sup>403</sup> See above, section 1 *in fine*.

<sup>404</sup> In addition to the specific exception in Article 16(5), point (d), EUDPR, see above, section 3.

<sup>405</sup> See above, section 3.

<sup>406</sup> Decision (EU) 2021/1486 of the European Central Bank, see above, footnote 395.

<sup>407</sup> See above, paragraph 10.

*Baumeister* test. As a matter of fact, the term “including” used in that provision seems to indicate that the existence of an adverse effect on the functioning of the system is only an example of adverse effect on the performance of the ECB’s supervisory tasks. Article 3(1), point (b), of Decision ECB/2021/42 provides for the possibility to restrict the rights of data subjects when their exercise would jeopardise or adversely affect the safety and soundness of credit institutions and the stability of the financial system within the EU and each Member State.

By contrast, Decision ECB/2021/42 does not cover the part of the *Baumeister* test referring to the protection of the individual interest of the person who provided the data or a third party. This should not raise concerns as it is difficult to imagine in which circumstance the disclosure to a data subject of data concerning themselves would affect the interests of the data subject or third parties and, therefore, be considered to breach the duty of professional secrecy.<sup>408</sup> However, if this were to be the case, the ECB could resort to the exception in Article 17(4) EUDPR, subject to demonstrating that the rights of the person who provided the data or those of third parties would be affected by disclosure. The bar is higher than a simple adverse effect on the interests that would allow to refuse the disclosure of information protected by professional secrecy under the *Baumeister* test.

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<sup>408</sup> See above, paragraph 20.

Koupepidou, E. (2020), "Introduction to the panel on transparency versus confidentiality of supervisory decisions, documents and information", *ESCB Legal Conference*.

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Opinion of Advocate General Bobek in case [C-245/20](#), *Autoriteit Persoonsgegevens*, EU:C:2021:822.

# Data protection and banking supervision: like oil and water?

By Maarten G.A. Daman\*

Data protection is a fundamental right of the Union<sup>409</sup>. The same holds true for the distinct right of privacy, which – regrettably – is often mistakenly confused with data protection.<sup>410</sup> As a consequence, the institutions and bodies of the European Union, such as the European Central Bank (ECB) as banking supervisor, and the Member States when they are implementing EU law, such as national competent authorities (NCAs) whose supervisory powers are based on Union law, must respect the fundamental right to data protection, observe its principles and promote the application thereof.<sup>411</sup> This means that any legislative act, any interpretation thereof and any administrative decision must respect and be in the spirit of the right to data protection. In other words, they must withstand challenges before the Court of Justice of the European Union, known for its broad, data subject-friendly interpretation of the right to data protection.

Data protection principles apply to the ECB legal framework, notably the SSM Regulation<sup>412</sup> and the legal acts adopted by the ECB, such as the SSM Framework Regulation,<sup>413</sup> the Fees Regulation,<sup>414</sup> as well as its decisions, with or without a legal or natural person as addressee. Furthermore, data protection principles apply to ECB guidance, opinions, and administrative acts, such as granting or denying a right of access. At national level, the same holds true for NCAs.

The fundamental right to data protection equally applies to legal acts in EU banking law, such as the Single Rulebook,<sup>415</sup> the Capital Requirements Regulation<sup>416</sup> and Directive<sup>417</sup>, the Single Resolution Mechanism Regulation<sup>418</sup>, the Deposit Guarantee Scheme Directive<sup>419</sup> and the Financial Conglomerates Directives.<sup>420</sup>

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<sup>409</sup> Article 8 of the Charter of Fundamental Rights of the European Union.

<sup>410</sup> *ibid.*, Article 7.

<sup>411</sup> Article 51 TFEU.

<sup>412</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.

<sup>413</sup> Regulation (EU) No 468/2014 of the European Central Bank of 16 April 2014 establishing the framework for cooperation within the Single Supervisory Mechanism between the European Central Bank and national competent authorities and with national designated authorities (ECB/2014/17).

<sup>414</sup> Regulation (EU) No 1163/2014 of the European Central Bank of 22 October 2014 on supervisory fees (ECB/2014/41).

<sup>415</sup> The Interactive Single Rulebook (ISRRB) of the European Banking Authority (EBA) is a useful online tool.

<sup>416</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 amending Regulation (EU) No 648/2012.

<sup>417</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, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC.

In view of the legal pre-eminence and hierarchy of the fundamental right to data protection in the EU, the question arises whether data protection risks undermining the effective supervision of credit institutions. This article argues that the available exceptions and restrictions to data protection rights sufficiently cater for a reconciliation between data protection and banking supervision interests: transparency and professional secrecy are not mutually exclusive but complementary objectives. However, finding such a balance necessitates a careful case-by-case assessment in which Data Protection Officers (DPOs) play a key role as intermediators.

## 1 Exceptions to data subject rights

The fundamental right to data protection is not an absolute right. Any limitation on the exercise of the rights and freedoms recognised by the Charter must be provided for by law and must respect the essence of those rights and freedoms.<sup>421</sup> Limitations may be made to those rights and freedoms only if they are necessary and genuinely meet objectives of general interest recognised by the EU or the need to protect the rights and freedoms of others.<sup>422</sup> The Court has added that “the requirement that any limitation on the exercise of fundamental rights must be provided for by law implies that the legal basis which permits the interference with those rights must itself define the scope of the limitation on the exercise of the right concerned.”<sup>423</sup> In other words, the mere fact that banking supervision is undoubtedly an objective in the general interest of the EU, does not suffice to limit and interfere with data protection rights.

### 1.1 Unfounded and excessive data subject requests

Whilst data subjects enjoy a wide array of rights, the corresponding obligations of a controller must be interpreted in the light of fairness and proportionality. Therefore, a controller may refuse to act on data subject requests if they are found to be manifestly

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<sup>418</sup> Regulation (EU) No 806/2014 of the European Parliament and of the Council of 15 July 2014 establishing uniform rules and a uniform procedure for the resolution of credit institutions and certain investment firms in the framework of a Single Resolution Mechanism and a Single Resolution Fund and amending Regulation (EU) No 1093/2010.

<sup>419</sup> Directive 2014/49/EU of the European Parliament and of the Council of 16 April 2014 on deposit guarantee schemes.

<sup>420</sup> Directive 2002/87/EC of the European Parliament and of the Council of 16 December 2002 on the supplementary supervision of credit institutions, insurance undertakings and investment firms in a financial conglomerate and amending Council Directives 73/239/EEC, 79/267/EEC, 92/49/EEC, 92/96/EEC, 93/6/EEC and 93/22/EEC, and Directives 98/78/EC and 2000/12/EC of the European Parliament and of the Council.

<sup>421</sup> Article 52(1) of the Charter.

<sup>422</sup> *ibid.*

<sup>423</sup> Opinion 1/15 (*EU-Canada PNR Agreement*) of 26 July 2017, para. 139 and the case-law cited; Judgment of 17 December 2015, *WebMindLicenses*, C-419/14, para. 81; Judgment of 16 July 2020, *Facebook Ireland and Schrems*, C-311/18, para. 172.

unfounded or excessive, in particular because of their repetitive character.<sup>424</sup> However, data subjects do not have to justify or provide reasons for their request. The Court has ruled that a balance must be struck between the data subject's rights enshrined in Chapter III of the General Data Protection Regulation (GDPR),<sup>425</sup> and the burden which the obligations represent to the data controller.<sup>426</sup> In the Opinion of Advocate General Pitruzzella, a fair balance leans toward greater attention being paid to the protection of the data subject's data and privacy, as is made clear by the requirement that, in order to refuse to act on a data subject's request for access, the "controller shall bear the burden of demonstrating the manifestly unfounded or excessive character of the request."<sup>427</sup>

Excessiveness depends on a variety of elements: the specifics of the sector in which the controller operates,<sup>428</sup> the degree to which changes occur in the controller's data base,<sup>429</sup> whether a refusal may cause substantial damage to the individual,<sup>430</sup> the period covered,<sup>431</sup> and, in the author's view, the quantity and degree of sensitivity of personal data. There is a correlation between the risks to data subjects, for example due to the degree of changes to personal data or the presence of "special categories of personal data" and the likelihood of excessiveness: the higher the risk, the narrower the exception should be applied. For instance, repetitive requests to access personal data in the framework of a fit and proper assessment are less likely to be considered excessive during the process, when regular changes occur and "special categories of data" are present (e.g. criminal record). However, repetitive requests are more likely to be considered excessive when the assessment has been concluded and changes to personal data are unlikely to materialise and, ideally, non-essential personal data (e.g. criminal record) has been erased. However, the mere fact that a request relates to a lot of personal data does not imply that such a request is excessive per se. As mentioned above, the burden of proof for the manifestly unfounded or excessive character of a request lies with the controller who is accountable. This requires case-by-case analysis, justification and documentation by the controller, who bears the burden of proof, with the advice of a DPO.

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<sup>424</sup> Article 14(5) of Regulation (EU) 2018/1725 of the European Parliament and of the Council of 23 October 2018 on the protection of natural persons with regard to the processing of personal data by the Union institutions, bodies, offices and agencies and on the free movement of such data, and repealing Regulation (EC) No 45/2001 and Decision No 1247/2002/EC (EUDPR).

<sup>425</sup> Regulation (EU) 2016/679 of the European Parliament and of the Council of 27 April 2016 on the protection of natural persons with regard to the processing of personal data and on the free movement of such data, and repealing Directive 95/46/EC.

<sup>426</sup> Judgment of 7 May 2009, *Rijkeboer*, C-553/07, para. 64.

<sup>427</sup> Article 14(5) EUDPR and Opinion of Advocate General Pitruzzella of 9 June 2022 in the pending Case C-154/21.

<sup>428</sup> European Data Protection Board (2022), 'Guidelines 01/2022 on data subject rights - Right of access' [https://edpb.europa.eu/system/files/2022-01/edpb\\_guidelines\\_012022\\_right-of-access\\_0.pdf](https://edpb.europa.eu/system/files/2022-01/edpb_guidelines_012022_right-of-access_0.pdf), p. 4.

<sup>429</sup> *ibid.*, p. 4.

<sup>430</sup> Information Commissioner's Office, 2022, Guide to law enforcement processing - Manifestly unfounded & excessive requests, Version: v0.6.

<sup>431</sup> The Financial Court of Berlin-Brandenburg held that a request concerning any type of data over a period of more than 50 years is excessive (FG Berlin-Brandenburg - 16 K 2059/21).



## 1.2 Exceptions where the controller must adhere to certain transparency obligations when the personal data are obtained from the data subject

Where personal data relating to a data subject are collected from the data subject, the controller shall, at the time when personal data are obtained, provide the data subject with a long list of information, such as purpose, recipients and retention period. However, the controller does not need to provide information to data subjects in cases where the individual already has this information.<sup>432</sup> In the author's view, the burden of proof lies with the controller and not the data subject. For example, if a manager of a credit institution was provided with a privacy statement containing all necessary information in relation to granting a banking licence, the Single Supervisory Mechanism (SSM) would not have to provide the information again when requesting additional information for the same process. However, in case of doubt, the SSM would have to provide proof that the manager received the privacy statement.

## 1.3 Exceptions where the controller must adhere to certain transparency obligations when the personal data are not obtained from the data subject

Where personal data have not been obtained from the data subject, the controller can rely on additional exceptions.

To start with, if the provision of such information proves impossible or would involve a disproportionate effort, reflecting the principle of proportionality, balance must be struck between a data subject's interests and the burden placed upon a controller. For example, when a Joint Supervisory Team (JST) obtains a loan tape of a credit institution, it would be impossible, or at least disproportionate, to notify all data subjects across the EU. The same objective can be achieved by requiring the credit institution to notify its customers that their data may be shared with the SSM. In addition, the SSM as controller must take appropriate measures to protect the data subject's rights and freedoms and legitimate interests, including making the information publicly available, for instance by publishing a privacy statement on its website.<sup>433</sup>

Next, if the provision of such information to data subjects is likely to render impossible or seriously impair the achievement of the objectives of that processing, the controller can exceptionally choose not to provide the information to a data subject. To rely on this exception controllers must demonstrate that the provision of the information alone would nullify the objectives of the processing. Moreover, reliance on this exception presupposes that the data processing satisfies all data protection principles (legality, proportionality, etc).<sup>434</sup> For example, the ECB's whistleblowing mechanism would be seriously impaired if the ECB were to (immediately) inform alleged wrongdoers.

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<sup>432</sup> Article 15(4) EUDPR.

<sup>433</sup> *ibid.*, Article 16(6).

<sup>434</sup> Article 29 Data Protection Working Party Guidelines on transparency under Regulation 2016/679, p. 31.

Similarly, reporting suspicious transactions in the framework of anti-money laundering and countering the financing of terrorism (AML/CFT) legislation, including the future European reporting system for material AML/CFT weaknesses (EuReCA), would be seriously impaired if data subjects were to be informed as soon as they are entered into the database.<sup>435</sup> However, this must be re-evaluated over time in consultation with the DPO. Again, the controller must take appropriate measures to protect the data subject's rights and freedoms and legitimate interests.

Another exception is the case where obtaining or disclosing information is expressly laid down by EU law, which provides appropriate measures to protect the data subject's legitimate interests.<sup>436</sup> This vaguely formulated exception should be interpreted restrictively. For instance, the SSMR entrusts the ECB with the task of creating a whistleblowing mechanism.<sup>437</sup> Thus, obtaining whistleblower reports is expressly laid down by EU law (criteria 1). However, the Article does not provide for appropriate measures to protect the data subject's interests (cumulative criteria 2). Therefore, it should not be used as the legal basis not to inform the individuals mentioned by the whistleblower (as we will see, there are other means to do so). Some controllers argue that the obligation for controllers to interpret these obligations in line with the GDPR/EUDPR already provides appropriate measures of protection. In the author's view, however, this would not be in the spirit of data protection legislation and leaves too much room for interpretation and too little transparency for data subjects.

Finally, there is an exception where personal data must remain confidential subject to an obligation of professional secrecy regulated by EU law, including a statutory obligation of secrecy.<sup>438</sup> In many Member States this, for example, relates to personal data falling under a lawyer-client relationship (but not corporate lawyers), the anonymity of journalistic sources or medical confidentiality. Members of the European System of Central Banks (ESCB) governing bodies (e.g. the Supervisory Board), staff of the ECB and national central banks are required, even after their duties have ceased, not to disclose information of the kind covered by the obligation of professional secrecy.<sup>439</sup> This does not provide a blank cheque for banking supervisors to ignore the duty to inform data subjects, rather, it creates a possibility to occasionally apply an exception where personal data must remain confidential. In cases where a supervisory authority receives a whistleblowing report containing personal data of bank managers, the supervisory authority could argue that the accused persons should not be informed in the interest of the investigation.<sup>440</sup>

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<sup>435</sup> Based on Article 9a(1) and (3) of the EBA Regulation.

<sup>436</sup> Article 16(5), point (c), EUDPR.

<sup>437</sup> Article 23 SSMR.

<sup>438</sup> Article 16(5), point (d) EUDPR and Article 14(5), point (d), GDPR. See also "The impact of the General Data Protection Regulation on the banking sector: Data subjects' rights, conflicts of laws and Brexit", L. Baker, *Journal of Data Protection & Privacy*, Volume 1(2), 2017, pp. 137-145(9).

<sup>439</sup> See Article 38 of the Statute of the European System of Central Banks and of the European Central Bank. This is further detailed in Article 27 of the SSMR, which obliges the ECB to also ensure that service providers related to the discharge of supervisory duties are also subject to equivalent professional secrecy requirements.

<sup>440</sup> Article 23 SSMR specifically refers to the "protection of personal data". European Data Protection Supervisor (EDPS) Guidelines on processing personal information within a whistleblowing procedure (17 December 2019), p. 8.

However, this exception does not apply indefinitely and needs to be re-evaluated regularly with the advice of a DPO.

It is worth noting that DPOs, who, by law, potentially have access to all personal data in an organisation, are also bound by secrecy or confidentiality concerning the performance of their tasks.<sup>441</sup> For example, where a DPO advises a JST and obtains personal data of a bank employee in the course of the advisory activity, the DPO does not have to inform the employee.

## 1.4 Right of access

The right of access encompasses the right to obtain certain information (purpose, categories of data, recipients, etc.) and to obtain a copy of personal data. It is a right distinct from the right of access to documents.<sup>442</sup> The right of access to personal data has two principal limitations:

- The request must relate to personal data in the possession of the controller. It may be that the personal data were deleted or that the information requested is not yet known, for example, where the controller has not yet actually identified the recipients of personal data.<sup>443</sup> Limiting the right of access in relation to a specific time period, for instance to one year, when data are stored for a much longer period, does not constitute a fair balance between the interest of the data subject and the corresponding obligations of the controller.<sup>444</sup>
- The provision of a “copy” (to be interpreted broadly so as to also include on-site access), shall not adversely affect the rights and freedoms of others.<sup>445</sup> This does not mean that personal data of others must be excluded per se, but only if the data adversely affect other individuals. Requesting a copy of personal data from a spouse, for example their bank account, would adversely affect them.<sup>446</sup> The controller must be able to factually demonstrate that the rights and freedoms of others would be adversely affected in the concrete situation and weigh the interests of all participants taking into account the likelihood and severity of the risks present in the communication of the data.<sup>447</sup> Needless to say, it does not liberate the controller to implement the right of access but instead obliges the

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<sup>441</sup> Article 44(5) EUDPR; Article 29 Working Party Opinion 1/2006 on the application of EU data protection rules to internal WB schemes in the fields of accounting, internal accounting controls, auditing matters, fight against bribery, banking and financial crimes. (1 February 2006), p. 13.

<sup>442</sup> Article 15 TFEU and Regulation (EC) No 1049/2001 of the European Parliament and of the Council of 30 May 2001 regarding public access to European Parliament, Council and Commission documents, see in particular Article 4(1)(b) where privacy and the integrity of the individual, in particular data protection legislation, is an exception to the right to access documents.

<sup>443</sup> See the pending case before the Court of Justice whether a request regarding the third parties to whom the data are disclosed implies that a data subject should receive information regarding the specific recipients to whom personal data are disclosed, or does it suffice to provide information solely regarding the categories of recipients of such disclosures: Case C-154/21, *RW v Österreichische Post AG*.

<sup>444</sup> Judgment of 7 May 2009, *Rijkeboer*, C-553/07, para. 66.

<sup>445</sup> Article 17(4) EUDPR.

<sup>446</sup> *Tietosuojavaltuutetun toimisto - OP Ryhmä*, Case 3075/182/2018.

<sup>447</sup> European Data Protection Board (2022), ‘Guidelines 01/2022 on data subject rights - Right of access’ [https://edpb.europa.eu/system/files/2022-01/edpb\\_guidelines\\_012022\\_right-of-access\\_0.pdf](https://edpb.europa.eu/system/files/2022-01/edpb_guidelines_012022_right-of-access_0.pdf), p. 51.

controller to leave out or render illegible those parts that may have negative effects on the rights and freedoms of others.<sup>448</sup>

“Others” refers to any individual other than the person requesting access, including the controller and processor.<sup>449</sup> For instance, when granting access to personal data of a JST report, personal data of members of staff of the supervisory authority should be omitted, if access to their personal data would adversely affect them.

## 1.5 Right to erasure

The right to erasure can be denied, for example, in order to exercise the right of freedom of expression and information (e.g. requesting a newspaper to delete a name in a press article in the online archive)<sup>450</sup> or for the establishment, exercise or defence of legal claims.<sup>451</sup> In addition, the controller can also reject the request for erasure in order to comply with a legal obligation to which the controller is subject or for the performance of a task carried out in the public interest or in the exercise of official authority vested in the controller.<sup>452</sup> Banking supervision, by definition, is a task carried out in the public interest of the EU and is naturally exercised on the basis of a legal obligation to which the supervisory authority is subject. Yet, this does not imply that a supervisory authority can categorically reject requests for erasure. If the data were obtained from the data subject, for instance in the framework of a fit and proper assessment, the candidate could withdraw their application and request the deletion of the personal data in the application file. The supervisory authority would then have to demonstrate that it has a legal obligation to retain the personal data after the withdrawal by an applicant.

## 2 Restrictions to data subject rights

Unlike exceptions, restrictions do not apply by default but require “legislative measures” (GDPR) or “legal acts” (EUDPR).<sup>453</sup> Under the GDPR, where it refers to a legal basis or a legislative measure, this does not necessarily require a legislative act adopted by a parliament.<sup>454</sup> The Court of Justice and the European Court of Human Rights have stressed that it is essential that a legislative measure or legal act seeking to restrict the scope of data subject rights or of controller’s obligations is sufficiently clear in its terms to give individuals an adequate indication of the circumstances in and

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<sup>448</sup> *ibid.*

<sup>449</sup> *Ibid.*, p. 50.

<sup>450</sup> *Gegevensbeschermingsautoriteit*, Decision 104/2022 of 16 June 2022.

<sup>451</sup> Article 19(3), point (a), and 19(3), point (e), EUDPR.

<sup>452</sup> Article 19(3), point (b) EUDPR.

<sup>453</sup> EDPB Guidelines 10/2020 on restrictions under Article 23 GDPR, 2020; C. Etteldorf, “EDPB Guidelines on Restrictions under Article 23 GDPR”, 2021, 7 *Eur Data Prot L Rev* 564.

<sup>454</sup> Recital 41 GDPR.

conditions under which controllers are empowered to resort to any such restrictions (foreseeability).<sup>455</sup>

The EUDPR creates the possibility to adopt legal acts on the basis of the Treaties or, in matters relating to the operation of Union institutions and bodies, internal rules laid down by the latter to restrict “the application” of most data subject rights. The right to object and the right not to be subject to a decision based solely on automated processing cannot, however, be restricted.<sup>456</sup>

The GDPR, on the other hand, creates the possibility for EU or national law to which the data controller or processor is subject to restrict, by way of a legislative measure, “the scope of the obligations and rights’ of all data subject rights”.<sup>457</sup>

Under both legal umbrellas, restrictions must respect the essence of fundamental rights and freedoms and must be necessary and proportionate measures in a democratic society to safeguard a specified list of interests. The power conferred upon Member States may be exercised only in accordance with the requirement of proportionality, according to which derogations and limitations in relation to the protection of personal data must apply only in so far as is strictly necessary.<sup>458</sup> In the next part, this article will present the grounds for restrictions that are most relevant for banking supervision.

## 2.1 Other important objectives of general public interest of the Union or of a Member State’s right to erasure

The ECB can restrict most data subject’s rights to safeguard “other important objectives of general public interest of the Union or of a Member State ... or an important economic or financial interest of the Union or of a Member State, including monetary, budgetary and taxation matters”.<sup>459</sup>

## 2.2 Monitoring, inspection or regulatory functions

The ECB can also restrict most data subject’s rights to safeguard “a monitoring, inspection or regulatory function connected, even occasionally, to the exercise of official authority” in relation to the abovementioned “other important objectives of general public interest of the Union or of a Member State”.<sup>460</sup>

The ECB acts in the public interest of the EU as a public authority entrusted with carrying out, for supervisory purposes, specific tasks in relation to all credit institutions

<sup>455</sup> European Court of Human Rights, 14 September 2010, *Sanoma Uitgevers B.V. v The Netherlands*, no 38224/03, para. 83; EDPB Guidelines 10/2020 on restrictions under Article 23 GDPR, 2020, para. 17.

<sup>456</sup> Article 25 EUDPR.

<sup>457</sup> Article 23 GDPR; C. Etteldorf, “EDPB Guidelines on Restrictions under Article 23 GDPR”, 2021, 7 Eur Data Prot L Rev 564.

<sup>458</sup> Judgment of 6 October 2020, *La Quadrature du Net and Others v Premier ministre and Others*, joined cases C-511/18, C-512/18 and C-520/18, para. 210.

<sup>459</sup> Article 25(1), point (c), EUDPR.

<sup>460</sup> Article 25(1), point (g), EUDPR.

established in the Member States participating in the SSM. Such tasks include monitoring, inspection or regulatory functions connected with the exercise of official authority related to the prudential supervision of credit institutions.<sup>461</sup>

### 3 A scattered landscape of restrictions

As shown above, there are important divergences between the EUDPR and GDPR when it concerns restricting data subject's rights.<sup>462</sup>

The material scope differs: the EUDPR restricts "the application" compared to the GDPR which restricts "the scope of the obligations and rights". Also, the EUDPR does not allow a restriction of the right not to be subject to a decision based solely on automated processing which is possible under the GDPR. The safeguards also slightly differ where the EUDPR has additional grounds: (i) objectives of the foreign and security policy of the EU; and (ii) internal security of Union institutions and bodies, including electronic communications. There is also a small difference in the safeguarding of monitoring, inspection or regulatory functions which also applies to "breaches of ethics for regulated professions" which is not the case under the EUDPR.

The ECB's processing of personal data is governed by the EUDPR which allows the ECB to adopt its own restriction decisions. The GDPR, on the other hand, is complemented by national provisions and allows Member States to implement specifications or restrictions on certain rules set out in the GDPR. As a consequence, NCAs cannot pass restriction decisions and need to rely on Member State laws to restrict data subject rights. That leads NCAs to rely more on the application of exceptions instead of restrictions. For example, Member States have adopted different conditions that permit the processing of personal data relating to criminal convictions, which is relevant, for example, for fit and proper assessments. Another example is that some Member State laws allow restriction of access and erasure rights of credit registers, such as in Spain.<sup>463</sup>

The lack of harmonisation may, in practice, lead to different treatment of individuals depending on the applicable restrictions. For example, a request to access personal data in a fit and proper assessment of a new board member of a credit institution in Member State A may be restricted, whereas the request for access by a board member in Member State B may not be restricted. The same applies for a new board member requesting access to personal data at two different Union institutions.

The situation is particularly challenging in cases of joint controllership between the ECB and NCAs and/or between NCAs from various Member States:

- Data subjects have the right to address any controller who is party to a joint-controllership agreement. Indeed, the EUDPR and GDPR stipulate that "the data subject may exercise his or her rights under this Regulation in respect of and

<sup>461</sup> Recital 6 of Decision (EU) 2021/1486 of the European Central Bank of 7 September 2021.

<sup>462</sup> EDPB Guidelines 10/2020 on restrictions under Article 23 GDPR, 2020.

<sup>463</sup> Law No 44/2002 of 22 November on "Central de Información de Riesgos".

against each of the controllers”. Therefore, data subjects would have the right to address at their choice the ECB and any NCA for exercising their data subject rights. The joint-controllership agreement could not prevent this, given that Article 26(3) EUDPR/GDPR stipulate that data subjects enjoy such a right “irrespective of the terms of the arrangement”. The consequences are that data subjects, e.g. members of the management bodies of credit institutions whose fitness and propriety were assessed, could exercise their data subject rights at any NCA and at the ECB (“forum shopping”). Nothing would prevent data subjects opting for the NCA whose national legislation is the least restrictive or to exercise their rights at various NCAs and the ECB simultaneously, potentially leading to different outcomes due to different national provisions and leading to different outcomes before national courts.

- Moreover, for each NCA and the ECB a different data protection supervisory authority would be responsible. This can also lead to a fractured interpretation of exceptions and restrictions among such NCAs, which triggers further legal uncertainty.<sup>464</sup> Data subjects would have the right to lodge a complaint vis-à-vis any of the data protection authorities (DPAs), potentially opting for the strictest one.
- The existence and level of administrative fines vary. The GDPR leaves the sanctions regime of public administration to national laws which leads to a fractured approach, whereas under the EUDPR, the EDPS can impose administrative fines on the ECB.<sup>465</sup>
- Finally, the liability of controllers varies significantly between the ECB and the NCAs. The EUDPR does not specifically deal with non-compliance liability and merely states in Article 65 that “any person who has suffered material or non-material damage as a result of an infringement of this Regulation shall have the right to receive compensation (...).” The GDPR, on the other hand, contains more detailed and far-reaching rules on compensation and liability. The GDPR also established, in Article 65(4), that “where more than one controller or processor, or both a controller and a processor, are involved in the same processing and where they are (...) responsible for any damage caused by processing, each controller or processor shall be held liable for the entire damage in order to ensure effective compensation of the data subject.”

The divergence of potential restrictions to data subject rights amongst the ECB and NCAs is not satisfactory. It raises questions about equal treatment of EU citizens when the same personal data, processed for the same purposes, of the same individual, is treated differently merely because of the responsible entity. When the supervision of the internal market for banking services is harmonised to increase its effectiveness, the restrictions to the fundamental right should be harmonised as well, thereby ensuring a level playing field of protection of fundamental rights. It would boost data protection across the EU and also facilitate banking supervision.

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<sup>464</sup> C. Ettlendorf, “EDPB Guidelines on Restrictions under Article 23 GDPR”, 2021, 7 Eur Data Prot L Rev 564.

<sup>465</sup> Article 66 EUDPR.

## 4 The position of Data Protection Officers: what we have learned thus far

DPOs can play an important role in balancing the interest of banking supervision and data protection. By now, after almost half a decade since the entry into force of the GDPR and the EUDPR, the existence and *raison d'être* of DPOs in organisations is acknowledged. The DPO acts primarily as an independent counsellor (“to advise”) and ambassador (“to inform”) of data protection, as well as a liaison with the supervisory authority. Under the EUDPR, a DPO may, on their own initiative or at the request of others, also investigate matters and occurrences directly relating to data protection.

The designation and tasks of a DPO rarely cause a problem anymore, whereas the position of DPOs to carry out their tasks proves to be more controversial in practice. The European Data Protection Board’s topic for its second coordinated enforcement action in 2023 will concern the designation and position of DPOs.<sup>466</sup> This means that national data protection authorities will prioritise this topic, leading to targeted follow-up on both the national and the EU level, as well as new guidance on the position of DPOs.

This article will focus on two key areas that are particularly important for DPOs in banking supervision.

### 4.1 The DPO must be involved in a timely manner

The respective organisation shall ensure that the DPO is involved, properly and in a timely manner, in all issues which relate to the protection of personal data.<sup>467</sup>

Early involvement of the DPO is key to achieve privacy by design in any organisation. The DPO must be involved from the earliest stage possible in all issues relating to data protection and this should be standard procedure within the organisation’s governance. The DPO should, for example, be part of the relevant working groups dealing with data processing activities within the organisation and participate regularly in meetings of senior and middle management.<sup>468</sup> In some instances, it is obvious that a DPO needs to be consulted, for example, if a banking supervisor is confronted with a data subject request, data breach or data protection impact assessment. But DPOs should also be involved in all other cases where personal data is at stake, for example, when supervisors intend to request additional data not collected under the harmonised EU reporting framework in order to analyse specific developments in supervised institutions’ risk profiles; when planning to share credit quality review data from on-site inspections; when testing artificial intelligence for assessing the fitness and propriety of members of the management body; or when planning to make use of public cloud computing.

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<sup>466</sup> See EDPB press article of 14 September 2022, “EDPB adopts statement on European Police Cooperation Code & picks topic for next coordinated action”.

<sup>467</sup> Article 44(1) EUDPR.

<sup>468</sup> Article 29 Data Protection Working Party, WP 243 rev.01, Guidelines on Data Protection Officers (“DPOs”).



All relevant information must be passed on to the DPO in a timely manner to allow them to provide adequate advice. The opinion of the DPO must always be given due weight. In case of disagreement, it is recommended to document the reasons for not following the DPO's advice.<sup>469</sup>

The Luxembourg DPA fined a controller because the DPO of the group company was not sufficiently involved in the subsidiary company in Luxembourg. Even if the DPO was participating in numerous meetings at group level and regularly organised meetings with its local points of contact, that was not sufficient to demonstrate the direct, formal and permanent involvement of the DPO at operational level in Luxembourg.<sup>470</sup>

Involving a DPO is not only a noble act of good administration but can also pay off financially. The Italian DPA lowered the amount of the sanction because the controller had involved the DPO and complied in good faith with the DPO's opinion.<sup>471</sup>

The Belgian DPA ruled that the DPO must be consulted before a decision is made, be allowed to make an independent data protection risk assessment (which must be taken into account) and then be informed of the final decision. The DPO acts as advisor and is not responsible for the decision. However, if the controller only informs a DPO of the outcome of a decision, it will undermine the role of a DPO and be in breach of data protection law.<sup>472</sup> In practice, it is not always understood that the controller, i.e. the SSM and NCAs, are responsible for compliance and not the DPOs.

## 4.2 The controller must support the DPO

A DPO can only support an organisation in finding the right balance between data protection and the need for professional secrecy in banking supervision, when a DPO has the necessary support for such a complex task. Therefore, the organisation must support the DPO by providing the resources necessary to carry out those tasks and access to personal data and processing operations, and to maintain their expert knowledge.<sup>473</sup>

### 4.2.1 The first element: providing necessary resources

Organisations must provide the resources necessary to carry out the tasks of a DPO.<sup>474</sup> To start with, a DPO needs to be provided with one of the most precious resources: time. Only DPOs who are given sufficient time to fulfil their duties can be

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<sup>469</sup> *ibid.*

<sup>470</sup> *Décision de la Commission nationale siégeant en formation restreinte sur l'issue de l'enquête n°[...] menée auprès de la Société A*, Délibération, 31 May 2021, number 18FR/2021.

<sup>471</sup> *Garante per la protezione dei dati personali, Ordinanza ingiunzione nei confronti del Comune di Greve in Chianti* 2 July 2020, number 9440025.

<sup>472</sup> Gegevensbeschermingsautoriteit, Decision 18/2020, 28 April 2020.

<sup>473</sup> Article 44(2) EUDPR.

<sup>474</sup> Article 44(2) EUDPR and Article 38(2) GDPR.

effective in advising their organisation.<sup>475</sup> This is particularly important where the DPO is appointed on a part-time basis or is also responsible for other tasks.<sup>476</sup>

Often, one full-time equivalent does not suffice and the DPO must be provided with additional staff. A 2020 report found that over half of the DPOs across national central banks (NCBs) and NCAs were either a team or a DPO supported by a team.<sup>477</sup> The following elements will determine the necessary number of staff:

- Level of risk to the rights and freedoms of natural persons: The necessity to conduct a data protection impact assessment (DPIA) indicates a high risk to data subjects and requires by law the involvement of the DPO, for example, the use of new technologies such as artificial intelligence in banking supervision and (“Suptech”) fit and proper assessments of individuals.
- Sensitivity of processing activities: for example, the processing of criminal records or marital status of banking managers are sensitive personal data that necessitate the involvement of the DPO to ensure appropriate safeguards are taken.
- Quantity of processing activities: the number of processing activities has steadily increased over the last years. The number of processing activities amongst NCBs/ NCAs vary immensely, ranging from 16 to 550.<sup>478</sup>
- Complexity of underlying IT systems: the use of cloud services, interconnected IT systems and blockchain are examples where a DPO is needed to advise to ensure compliance.
- Number of cross-border transfers of personal data: the transfer of personal data to third countries, for example, foreign banking supervision authorities, have become increasingly difficult and have come under the scrutiny by the Court of Justice.

Apart from time and staff to fulfil their duties, DPOs must also be given adequate support in terms of financial resources (e.g. to request external legal advice) and infrastructure (office and equipment). Lastly, it is important that the designation of the DPO is officially communicated to staff so that their existence and function is known within the organisation and data subjects can directly reach out to their DPO.<sup>479</sup> In 2021, a Luxembourg public entity was fined because the contact details of the DPO

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<sup>475</sup> In 2021, a Luxembourg public entity was fined because its DPO could allocate 70 % of the working time to data protection matters and was ordered to rectify the situation within six months: *Décision de la Commission nationale siégeant en formation restreinte sur l'issue de l'enquête n°[...] menée auprès de l'établissement public A, Délibération*, 15 October 2021, number 38FR/2021.

<sup>476</sup> Article 29 Data Protection Working Party, WP 243 rev.01, Guidelines on Data Protection Officers ('DPOs'), p. 14.

<sup>477</sup> A. Magdziarz and B. Pardo, "The GDPR in European Central Banks and Competent Authorities", 2020, p. 50.

<sup>478</sup> It is noteworthy that, in jurisdictions where the NCA is separate from the NCB, the number of processing activities reported for the NCA were significantly lower than the number reported for the NCB: A. Magdziarz and B. Pardo, "The GDPR in European Central Banks and Competent Authorities", 2020, p. 16.

<sup>479</sup> See Article 44(4) and 38(4) EUDPR which grant data subjects the right to directly contact their DPO. See also Article 29 Data Protection Working Party, WP 243 rev.01, Guidelines on Data Protection Officers ('DPOs'), p. 14.

were not easy to find and only accessible in English.<sup>480</sup> At NCB/NCA level, approximately half of the DPOs report a high level of awareness about their functions in the institution they represent.<sup>481</sup>

#### 4.2.2 The second element: access to personal data and processing operations

It is of paramount importance that a DPO has the necessary access to core business areas, for example staff responsible for granting authorisation requests, as well as support services, such as IT security and human resources, so that DPOs can receive essential support, input and information.<sup>482</sup> For example, a DPO can consult IT security when assessing IT systems in the framework of a DPIA. The active and visible support of the DPO's function by senior management is a key element to support a DPO as well.<sup>483</sup>

#### 4.2.3 The third element: maintaining expert knowledge

DPOs should be given the opportunity to stay up to date on developments within data protection, to participate in necessary training and to obtain qualifications with the aim to constantly increase their level of expertise.<sup>484</sup> Only one third of DPOs of NCBs and NCAs have been issued a certification by their national DPAs or a private certification.<sup>485</sup>

## 5 Conclusion

Data protection is a fundamental right but not an absolute right. Consequently, there are sufficient options available to protect the need for secrecy and confidentiality in banking supervision and to strike a balance between the right to protect personal data and the legitimate interests of banking supervisors. The GDPR and EUDPR create a framework that allows for balance between transparency and professional secrecy. However, the burden of proof and responsibility lies with the controller of the personal data. Also, restrictions are always of a temporary nature, should last only as long as is strictly necessary, proportionate and justified, whereas the fundamental right to personal data is long-lasting.

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<sup>480</sup> *Décision de la Commission nationale siégeant en formation restreinte sur l'issue de l'enquête n°[...] menée auprès de l'établissement public A, Délibération*, 15 October 2021, number 38FR/2021.

<sup>481</sup> A. Magdziarz and B. Pardo, "The GDPR in European Central Banks and Competent Authorities", 2020, p. 50.

<sup>482</sup> Article 29 Data Protection Working Party, WP 243 rev.01, Guidelines on Data Protection Officers ('DPOs'), p. 14.

<sup>483</sup> *ibid.*, p. 14.

<sup>483</sup> *ibid.*

<sup>484</sup> *ibid.*, pp. 13-14.

<sup>485</sup> A. Magdziarz and B. Pardo, "The GDPR in European Central Banks and Competent Authorities", 2020, pp. 51-52.

DPOs play an important role in ensuring that banking supervisors strike the right balance between data protection and banking supervision needs, especially when advising on the application of exceptions and restrictions. The law provides DPOs with the necessary independence and a mandate, tasks and tools to take on the role of intermediary. However, practice shows that many organisations, both private and public, do not always involve their DPO in a timely manner or provide them with sufficient resources. This bears reputational and legal risks for banking supervisors who are accountable for data protection.

So, are data protection and the need for professional secrecy and confidentiality in banking supervision like oil and water. It is true that both pursue different interests and could obliterate each other. However, as in real life, both are needed and when they complement each other they maximise their value.

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*Sanoma Uitgevers B.V. v the Netherlands*, no 38224/03 (2010), ECtHR, 14 September 2010, para. 83.

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## Panel 6

The NCAs' duty of assistance and the ECB's duty of diligence when assessing AML-CFT aspects relevant for the ECB's supervisory tasks





ESCB Legal Conference 2022 – Panel 6  
The NCAs' duty of assistance and the ECB's duty of diligence when assessing AML-CFT aspects relevant for the ECB's supervisory tasks

# On the National Competent Authorities' duty of assistance and the ECB's duty of diligence when it, in performing its supervisory tasks, has to assess anti-money laundering and counter-terrorism financing

By Carmen Hernández Saseta\*

Under the SSM Regulation<sup>486</sup> the ECB is exclusively competent to perform specific tasks in prudential supervision. At the same time, anti-money laundering and counter-terrorism financing (AML/CFT)-related supervisory tasks have not been conferred on the ECB and remain with competent authorities at national level.<sup>487</sup> Notwithstanding this, significant points of contact exist between AML/CFT supervision and the ECB's supervisory tasks. For example, AML/CFT-related findings can be relevant to assess the suitability of a board member in fit-and-proper proceedings or of a proposed acquirer of qualifying holdings in a bank. The ECB is also exclusively competent to withdraw the authorization of credit institutions for serious breaches of AML/CFT rules.

Within the Single Supervisory Mechanism, competent authorities, including the ECB, should discharge their responsibilities in full respect of the distribution of tasks decided by the legislator. At the same time, appropriate integration of AML/CFT issues into prudential supervision should be ensured.

It has come to light on several occasions during the last few years that applying this in practice may involve certain difficulties on the legal side. Some disputes have reached the Court of Justice of the European Union. The *Versobank*<sup>488</sup> and *ABB*<sup>489</sup> cases concern actions for annulment against ECB decisions to withdraw the authorisation of credit institutions for, among other reasons, breaches of AML/CFT provisions. In these cases, the General Court has made important considerations that help to clarify the delineation of competences between the ECB, the National Competent Authorities (NCAs) and, where different, AML/CFT supervisors.

In this panel, we will have the opportunity to discuss these issues with three knowledgeable and experienced lawyers that will offer diverse perspectives on the

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<sup>486</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>487</sup> Recital 28 of the SSM Regulation.

<sup>488</sup> See Joined Cases T-351/18 and T-584/18, *Ukrseļhosprom PCF LLC and Versobank AS v ECB*.

<sup>489</sup> Case T-797/19 *Anglo Austrian AAB and Belegging-Maatschappij "FarEast" v ECB*, EU:T:2022:389.

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matter. I have had the pleasure to work with them on numerous occasions. I hold each of them in high esteem, not only professionally but also personally. I am thrilled to share this (virtual) table with them today.

Let me introduce each of them, in the order of their appearance, before we start the discussion.

## The panellists

Audrone Steiblyte, member of the Legal Service of the European Commission. Since 2013, she has been directly involved in the creation and development of the Banking Union. Her fields of expertise include bank supervision, bank resolution, capital requirements, European Supervisory Authorities, as well as sustainable finance. Audrone has represented the European Commission in more than 350 court cases before the Court of Justice of the European Union (CJEU). She has published in the field of EU law, with specific emphasis on banking law, free movement of capital as well as EU cohesion policy and structural instruments. Audrone will walk us through the general framework of distribution of competences between the ECB and NCAs, paying special attention to the ECB's power to withdraw banking licences due to AML/CFT breaches. Audrone will also refer to the important insights provided by the General Court's recent judgments on the underlying principles of cooperation between the NCAs and the ECB when assessing AML/CFT aspects relevant for the ECB's supervisory tasks. Finally, Audrone will also touch upon the recent legislative developments and how those developments are progressively strengthening cooperation between competent authorities.

Giorgia Marafioti, Senior Legal Counsel in the Supervisory Law Division of the ECB's Directorate General Legal Services. Since 2017, she has been providing legal advice to the ECB's banking supervision arm and representing the ECB before the CJEU in several cases relating to banking supervision. Prior to joining the ECB, Giorgia worked for the Banking Supervision Department of Banca d'Italia and, previously, for a prestigious international law firm focusing on corporate and banking law issues and international arbitration. In the panel, Giorgia will provide interesting reflections on the role of the ECB when it comes to integrating AML/CFT issues into prudential supervision.

Giorgia will review how the ECB, when examining AML/CFT aspects, complies with the principle of good administration, and with the duty of diligence, without overstepping its powers. Giorgia will pay special attention to the scope of the ECB's duty of diligence in license withdrawal procedures based on serious infringements of AML/CFT provisions and will give account of relevant clarifications on this matter provided by recent judgments of the General Court.

Rafael Martínez-Lozano, a senior lawyer in the Regulatory and Supervisory Advice Division at the Banco de España's Legal Department. He advises on legal issues relating to supervision and resolution of credit institutions, including on the drafting of related legislation. He also worked for the Supervisory Law Division of the ECB's

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Directorate General Legal Services between 2017 and 2019, providing legal advice on topics related to the Single Supervisory Mechanism framework. Prior to joining the Banco de España's Legal Department, Rafael worked for a leading law firm in Spain where his practice was focused on public law and regulated sectors.

Rafael will first remind us about the risks that AML/CFT issues bring for the prudential supervisor. He will then explain the particularities of the Spanish framework for supervision of AML/CFT risks which provides an unusual arrangement within the SSM where the NCA it is not the AML/CFT supervisor, which adds another level of complexity to the system. Finally, Rafael will present the main challenges that the special characteristics of the Spanish system presents in relation to the competence to withdraw authorisations due to very serious breaches of AML/CFT provisions.

# Integration of AML/CTF risks into prudential supervision – the cooperation framework between the ECB and NCAs

By Audrone Steiblyte\*

This article briefly covers the three following topics: (i) exclusive European Central Bank (ECB) powers in a decentralised cooperation framework between the ECB and the national competent authorities (NCAs); (ii) NCAs' supportive function in dealing with anti-money laundering (AML) and countering the financing of terrorism (CFT) breaches leading to authorisation withdrawal; and (iii) main AML/CFT related legislative developments in Directive 2013/36/EU<sup>490</sup> (the "CRD").

## 1 Exclusive ECB powers in a decentralised cooperation framework

Regulation (EU) No 1024/2013<sup>491</sup> (the "SSM Regulation") provides that when the ECB exercises its exclusive competences as prudential supervisor, ensuring compliance with the relevant EU law, it is assisted by the NCAs.

In its turn, the General Court confirmed in the *Versobank* judgment<sup>492</sup> that the powers which were not conferred on the ECB remained vested in the NCAs.

The Single Supervisory Mechanism (SSM) centralises functions related to prudential supervision within the ECB and provides for a decentralised implementation by the NCAs, yet always under the supervision of the ECB, to which NCAs provide their cooperation and assistance.<sup>493</sup>

It was held in the *Landeskreditbank Baden-Württemberg* judgment that direct prudential supervision by the NCAs under the SSM was envisaged by the Council of the European Union as a mechanism to assist the ECB rather than as the exercise of autonomous competence.<sup>494</sup>

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\* Member of the Legal Service of the European Commission since 2002. The views expressed are those of the author and do not necessarily reflect those of the European Commission.

<sup>490</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, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC (OJ L 176, 27.6.2013, p. 338).

<sup>491</sup> See Article 6(8) of 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>492</sup> Case T-351/18 and T-584/18, *Versobank v ECB*, EU:T:2021:669, para. 114.

<sup>493</sup> See Article 6(2) and (3) of the SSM Regulation.

<sup>494</sup> Case T-122/15, *Landeskreditbank Baden-Württemberg v ECB*, EU:T:2017:337, para. 58.

While the ECB exercises “direct” prudential supervision of significant credit institutions,<sup>495</sup> the prudential supervision of less significant institutions is part of the above-mentioned decentralised exercise of power by the NCAs.

The decentralised prudential supervision of less significant institutions is, however, overseen and supervised, as a last resort, by the ECB, whose task is to ensure the proper functioning and effectiveness of the prudential supervision system and the consistent and uniform application of prudential rules in all participating Member States.

In the words of the General Court, “the ECB carries out ‘indirect’ supervision of less significant institutions and, in that context, NCAs provide their cooperation and assistance to the ECB. In addition, the same NCAs remain competent in respect of matters not covered by the SSM Regulation: consumer protection, markets in financial instruments, AML/CFT, and the fight against corruption.”<sup>496</sup>

In other words, rather than having a distribution of powers between the ECB and the NCAs in the performance of the tasks referred to in Article 4(1) of the SSM Regulation, the Regulation establishes that the exclusive powers delegated to the ECB are implemented within a decentralised framework.

## 2 Competences for treating AML/CFT breaches in the authorisation withdrawal process

In the area of AML/CFT, dating from the establishment of the SSM a possible tension between the competences that belong to the NCAs on one hand and the ECB on the other hand could be observed. That aspect has also now been addressed in the case-law of the Union courts.

Recitals 28 and 29 of the SSM Regulation list, among the “supervisory tasks not conferred on the ECB” and which should remain with the national authorities – “the prevention of the use of the financial system for the purpose of money laundering and terrorist financing and consumer protection”.

However, it follows from the combined reading of Article 4(1) and Article 6 of the SSM Regulation that the power to withdraw authorisations from credit institutions is reserved exclusively for the ECB.

It is therefore evident that the assisting role of the NCAs is particularly important in the withdrawal of authorisations process, due to AML/CFT concerns. The NCAs are responsible for assisting the ECB in the preparation and implementation of any acts relating to the exercise of the ECB’s supervisory tasks and that includes, in particular, the ongoing day-to-day assessment of a credit institution’s situation and any related on-site verifications.

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<sup>495</sup> See Article 6(4), second subparagraph, of the SSM Regulation.

<sup>496</sup> See *Versobank v ECB*, para. 131.

Within the decentralised exercise of exclusive powers in relation to withdrawal of authorisation, the NCAs supervising less significant institutions are required to fulfil their duty to provide cooperation and assistance to the ECB, as provided for in Article 6(2), second subparagraph, and in Article 6(3) of the SSM Regulation by; (i) carrying out the necessary physical checks and inspections; (ii) entering into communication with the credit institution in question in order to resolve problems at an early stage, including by consulting the relevant financial supervisory authority in its role as the national resolution authority; and (iii) preparing a draft decision on the withdrawal of authorisation, pursuant to Article 14(5) of the SSM Regulation.

In the area of authorisation withdrawal the cooperation between the ECB and NCAs is expressed, in accordance with Article 14(5) of the SSM Regulation, by the obligation to consult the relevant NCA in the event that the ECB withdraws the authorisation on its own initiative and by the possibility for the NCA to propose an authorisation withdrawal to the ECB.

Although the Member States remain competent to implement the AML/CFT provisions, the ECB has exclusive competence to withdraw authorisation, for all credit institutions, irrespective of their size, even where such competence is based on the grounds set out in Article 67(1)(d), (e) and (o) CRD, to which Article 18 of that Directive explicitly refers. Article 14(5) of the SSM Regulation lays down, as a condition for the withdrawal of authorisation, the existence of one or more grounds justifying withdrawal under Article 18 CRD. Thus, the applicants challenging the withdrawal of banking authorisations in court cannot question the ECB's competence to adopt the withdrawal decisions based on AML/CFT breaches.

Article 67 CRD provides for the withdrawal of authorisations where credit institutions fail to comply with AML/CFT requirements, thus compliance with AML/CFT obligations is in principle required in the context of prudential supervision, since the use of the financial system for money laundering purposes is likely to threaten the stability, integrity and reputation of the financial system and of the single market.<sup>497</sup>

However, the question arises as to whether the ECB may adopt a decision withdrawing authorisation because of the infringement of AML/CFT provisions alone? Would the ECB have sufficient competence for that?

The answer is yes.

Article 18(f) CRD provides that a banking authorisation may be withdrawn if a credit institution commits at least one of the breaches provided for in Article 67(1) CRD.<sup>498</sup> For example, when the authority identifies a serious breach of the national provisions adopted pursuant to the AML/CFT Directive.<sup>499</sup> In exercising its competence related

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<sup>497</sup> See also in that regard the judgment in *Versobank v ECB*, para. 185.

<sup>498</sup> See also in that regard Case T-797/19, *Anglo Austrian AAB v ECB*, EU:T:2022:389, para. 33.

<sup>499</sup> Directive (EU) 2015/849 of the European Parliament and of the Council of 20 May 2015 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing, amending Regulation (EU) No 648/2012 of the European Parliament and of the Council, and repealing Directive 2005/60/EC of the European Parliament and of the Council and Commission Directive 2006/70/EC (OJ L 141, 5.6.2015, p. 73).

to the withdrawal of authorisations, the ECB is obliged to apply, inter alia, the national law provisions transposing the CRD.<sup>500</sup>

In the *Versobank* judgment the General Court rejected arguments that, owing to the division of powers between the NCAs and the ECB together with the principle of proportionality, the full range of other available measures (fines, prohibition on carrying out certain types of activity, and criminal proceedings) must first be exhausted before an authorisation is withdrawn on the grounds of infringement of the AML/CFT legislation.<sup>501</sup>

Furthermore, in the *Anglo Austrian AAB* judgment the General Court recognised that it was sufficient if the national authority adopts an administrative decision establishing a serious breach of AML/CFT law and there is no requirement that a judgment or a decision with *res judicata* effects should recognise the responsibility of a credit institution for the breach.<sup>502</sup>

Another important aspect also clarified by the General Court in the *Anglo Austrian AAB* judgment<sup>503</sup> is that from the moment when the national administrative decision becomes final (i.e. it is no longer possible to challenge the decision in the national court), the question of prescription in relation to the facts established in that decision may no longer be raised. Hence, the ECB is legally entitled to rely on the factual aspects set out in such a final administrative decision.

In other words, the fact that the AML/CFT breaches are old or have been corrected has no bearing on the existence of the credit institution's liability. In the *Anglo Austrian AAB* judgment the Court examined the situation where the relevant national law did not impose a time limit to be observed for taking into account earlier decisions establishing liability. Nor did it require that serious breaches be interrupted or still exist when the decision to withdraw authorisation was adopted, especially since, in this case, the breaches were only discovered a few years before the adoption of the contested decision.

One of the most important policy related aspects established in the *Anglo Austrian AAB* judgment is linked to the general objective of safeguarding the European banking system. The General Court takes a firm stance concerning corrected AML/CFT breaches and states that if such corrected breaches could no longer justify a withdrawal of authorisation, credit institutions that have committed serious breaches would be permitted to continue their activities as long as the competent authorities fail to demonstrate once again that they have committed new breaches.

Where the national authorities establish serious breaches of the national law provisions adopted pursuant to the AML/CFT Directive and propose to the ECB the withdrawal of the banking authorisation, it is apparent from Article 14(5), second subparagraph, of the SSM Regulation and from Article 83(2) of the SSM Framework

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<sup>500</sup> In accordance with Article 4(3) of the SSM Regulation.

<sup>501</sup> See the judgment in *Versobank v ECB*, para. 191.

<sup>502</sup> See the judgment in *Anglo Austrian AAB*, para. 51.

<sup>503</sup> See the judgment in *Anglo Austrian AAB*, para. 71.



Regulation<sup>504</sup>, that the ECB is required to take full account of the grounds put forward by the NCA to justify that withdrawal.

The division of powers between the NCAs of the participating Member States and the ECB under the SSM in practice requires that the facts constituting breaches of AML/CFT legislation are established by national authorities, often specialised in the area, like the financial intelligence units (FIUs), whereas the legal assessment of whether those facts justified a withdrawal of authorisation and the assessment of proportionality were reserved for the ECB. The ECB therefore has to rely on its own assessment of compliance with the national provisions relevant in that regard.

When the ECB considers undertaking its own assessment of the facts and the legal grounds of the case in order to exercise its discretion (“may withdraw”), this assessment is to be distinguished from the investigation and the determination of relevant facts. The ECB is not obliged, in the case of less significant credit institutions, to carry out its own investigation, but may validly rely on the factual findings provided to it by the NCA.

It should be noted that an EU institution having to rely on the findings made by another institution situated at a different level (or even legal order) is not a novel situation. In the *Fininvest* judgment<sup>505</sup> the Court of Justice looked into the so-called “composite procedures” which are initiated by the national authority but at the end of which an EU institution, more specifically the ECB, takes a final decision, eventually making the analysis of the national authority its own. Where an EU institution exercises the final decision-making power alone, without being bound by the act of the national authority, it is for the EU courts to rule on the legality of the final decision adopted by the EU institution and also to examine any defects vitiating the preparatory acts and proposals of the national authority that could affect validity of the final decision. The Court underlined in the judgment that it is essential to have a single judicial review in order to avoid any risk of diverging assessments of the final decision, in particular where that final decision follows the view expressed in the preparatory acts and proposals.

The judgment in the *Fininvest* case was an important victory for the SSM. The mechanism at issue is built upon close cooperation between national supervisors and the ECB. The key element of such cooperation are the composite procedures as examined in the *Fininvest* judgment.

Since the adoption of the SSM Regulation and the CRD in 2013 the EU courts have provided important insights on the underlying principles of cooperation between NCAs and the ECB when assessing AML/CFT aspects relevant for the ECB’s supervisory tasks. Further developments in jurisprudence are, of course, expected at the very least because the judgment in *Versobank* has been appealed and the same could happen as regards the *AAB* judgment.

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<sup>504</sup> Regulation (EU) No 468/2014 of the European Central Bank of 16 April 2014 establishing the framework for cooperation within the Single Supervisory Mechanism between the European Central Bank and national competent authorities and with national designated authorities (SSM Framework Regulation) (ECB/2014/17) (OJ L 141, 14.5.2014, p. 1).

<sup>505</sup> See Case C-219/17, *Silvio Berlusconi and Finanziaria d’investimento Fininvest SpA (Fininvest)*, EU:C:2018:1023.

### 3 Legislative developments

Since 2013, the Commission, via its legislative proposals amending the CRD, and the EU co-legislators have established new rules in the area of AML/CFT that further strengthen NCAs' assistance in the ECB's supervisory work.

The so-called CRD V amendment<sup>506</sup> adopted in June 2019 strengthened the cooperation obligations between NCAs, FIUs and authorities entrusted with the public duty of supervising credit and financial institutions under the AML/CFT Directive.<sup>507</sup> All those authorities must now, within their respective competences, provide each other with information relevant for their respective tasks under the CRD, the CRR<sup>508</sup> and the AML/CFT Directive.

In particular, where the evaluation of the governance arrangements, the business model, or the activities of an institution, gives the banking supervisor reasonable grounds to suspect that money laundering or terrorist financing is being, or has been, committed or there is an increased risk thereof, the supervisor is subject to a legal obligation to immediately notify the AML/CFT authority. The banking supervisor and the AML/CFT authority will then produce their common assessment to be immediately sent to the European Banking Authority.

The CRD VI proposal<sup>509</sup>, adopted by the Commission in October 2021 and currently being examined by the co-legislators, attempts to introduce further AML/CFT tools that are considered essential for maintaining stability and integrity in the financial system.

Banking supervisors are consistently required to factor in money laundering and terrorist financing concerns into their relevant supervisory activities.

The CRD VI proposal specifically focuses on the acquisition or divestiture of qualifying holdings, material transfers of assets and liabilities, mergers and divisions as well as the authorisation of third-country branches. All these operations are considered to be material for the functioning of credit institutions and therefore, in order to ensure that NCAs can intervene before one of these material operations is undertaken, they are notified *ex ante*. Following the legislative proposal, that notification should, in particular, be accompanied by information necessary for the NCAs to assess the planned operation from a prudential, an anti-money laundering and a countering the financing of terrorism perspective.

The NCAs would be required to assess whether money laundering or terrorist financing is being, or has been, committed or attempted, or that the proposed acquisition could increase the risk thereof.

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<sup>506</sup> Article 117(5) of Directive (EU) 2019/878 of the European Parliament and of the Council of 20 May 2019 amending Directive 2013/36/EU as regards exempted entities, financial holding companies, mixed financial holding companies, remuneration, supervisory measures and powers and capital conservation measures (OJ L 150, 7.6.2019, p. 253).

<sup>507</sup> Directive (EU) 2015/849.

<sup>508</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 amending Regulation (EU) No 648/2012 (OJ L 176, 27.6.2013, p. 1).

<sup>509</sup> COM(2021) 663 final.

The proposal also sets out conditions for the refusal or withdrawal of a third-country branch's authorisation and those conditions, inter alia, cover situations related to AML/CFT breaches.

A final compromise between the European Parliament and the Council on the text of the CRD VI is not, however, expected until the end of 2022.

## 4 Conclusion

The exclusive supervisory powers conferred on the ECB by the SSM Regulation did not specifically include responsibilities in the area of AML/CTF, as those responsibilities were left with the relevant NCAs. The *Versobank* and *ABB* judgments provided dividing lines between the assistance of NCAs and the decision-making discretion of the ECB when establishing and assessing AML-CFT breaches in the authorisation withdrawal process. Those judgments also confirmed the autonomous value of the AML/CFT related breaches in justifying withdrawal of authorisations,

An explicit legal basis for integrating AML/CTF risks into prudential supervision came into effect in June 2019 with the CRD V amendments and provided the ECB with solid grounds for looking into AML/CTF risks when carrying out prudential supervision. Given the importance of AML/CFT policy in the EU the Commission's proposal for the CRD VI clearly aims at further strengthening the synergies between AML/TFC monitoring and prudential supervision.

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# The scope of the ECB's duty of diligence when examining AML/CFT aspects in the exercise of prudential supervision

By Giorgia Marafioti\*

## 1 Introduction

The prevention of the use of the financial system for the purpose of money laundering is expressly excluded<sup>510</sup> from the scope of tasks conferred on the European Central Bank (ECB) by the SSM Regulation<sup>511</sup>, which at the same time provides for a duty of the ECB to cooperate with authorities in charge of ensuring compliance with “anti-money laundering and counter financing of terrorism (AML/CFT)” legislation.<sup>512</sup>

Even though it is not competent to supervise compliance with AML/CFT legislation, the ECB integrates AML/CFT concerns systematically when performing its supervisory tasks.<sup>513</sup> The EU legal framework, in fact, expressly requires prudential supervisors to take into account “money laundering and terrorist financing (ML/TF)” risks in the exercise of specific prudential tasks, notably when granting authorisations,<sup>514</sup> when assessing acquisitions of qualifying holdings,<sup>515</sup> and when

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<sup>510</sup> Recital 28 SSM Regulation.

<sup>511</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>512</sup> Recital 29 SSM Regulation.

<sup>513</sup> See Recital 20 of Directive (EU) 2019/878 of 20 May 2019 amending Directive 2013/36/EU as regards exempted entities, financial holding companies, mixed financial holding companies, remuneration, supervisory measures and powers and capital conservation measures (OJ L 150, 7.6.2019, p. 253), pursuant to which “competent authorities should consistently factor money laundering and terrorist financing concerns into their relevant supervisory activities, including supervisory evaluation and review processes, assessments of the adequacy of institutions' governance arrangements, processes and mechanisms and assessments of the suitability of members of the management body, inform accordingly on any findings the relevant authorities and bodies responsible for ensuring compliance with anti-money laundering rules and take, as appropriate, supervisory measures in accordance with their powers under Directive 2013/36/EU and Regulation (EU) No 575/2013.”

<sup>514</sup> ML/TF risks are considered in the processes of authorisation, particularly in the assessment concerning governance and internal control mechanisms (see Article 10 of Directive 2013/36/EU, which however contains no express reference to ML/TF risk), as well as the suitability of shareholders (see Article 14(2) of Directive 2013/36/EU, cross-referring to the criteria set out in Article 23(1) of Directive 2013/36/EU). According to the Joint ESAs Report on the withdrawal of authorisation for serious breaches of AML/CFT rules (ESAs 2022 23), paragraph 24, it would be opportune “that all sectoral acts should be amended to provide that – as one of the conditions for granting authorisation – competent authorities expressly consider the applicant's exposure to ML/TF risk, and be satisfied that the envisaged arrangements, processes and mechanisms enable sound and effective ML/TF risk management and compliance with AML/CFT requirements. For this purpose, cooperation and information exchange between prudential supervisors and AML/CFT supervisors should be ensured.”

<sup>515</sup> Article 23(1)(e) of Directive 2013/36/EU of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC (OJ L 176, 27.6.2013, p. 338).

conducting fit and proper assessments.<sup>516</sup> Moreover, AML/CFT concerns may come into relevance in the context of ongoing supervision, whereas lack of compliance with AML/CFT provisions may constitute a symptom of unsound governance and internal control mechanisms of a credit institution,<sup>517</sup> and, in the event of serious AML/CFT breaches, may justify the withdrawal of its authorisation.<sup>518</sup>

It is therefore essential that the ECB duly accounts for AML/CFT aspects in the exercise of prudential supervision. It is equally essential that, when doing so, the ECB remains within the remit of its competences and does not exceed the boundaries of the tasks conferred on it by the SSM Regulation. The delicate balance of these two aspects brings into play two relevant principles of EU law. On one side, the principle of care, requiring EU institutions to perform a full and impartial assessment of all relevant facts before exercising their powers. On the other hand, the principle of conferral, providing that the European Union can act only within the limits of the competences conferred upon it by the Member States.

This will be the focus of this contribution, which will review how the ECB, when examining AML/CFT aspects, complies with the principle of good administration, and in particular with the duty of diligence, without overstepping its powers. The topic will be introduced in Section 2 by considering the main elements of the principle of care developed by the case-law of EU courts. This will pave the way for some reflections, in Section 3, on the scope of the ECB's duty of diligence when assessing AML/CFT aspects relevant for the exercise of its prudential supervisory tasks. Section 4 will focus in particular on the scope of the ECB's duty of diligence in licence withdrawal procedures based on serious infringements of AML/CFT provisions and will give account of relevant elaborations on this matter provided by two recent judgments of the General Court.

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<sup>516</sup> Article 91 of Directive 2013/36/EU. See also Joint ESMA and EBA Guidelines on the assessment of the suitability of members of the management body and key function holders under Directive 2013/36/EU and Directive 2014/65/EU (EBA/GL/2021/06).

<sup>517</sup> See EBA Final Report on Guidelines on internal governance under Directive 2013/36/EU (EBA/GL/2021/05), para. 19, pursuant to which “[t]he EBA Guidelines on internal governance clarify, in line with Directive 2013/36/EU, that identifying, managing and mitigating money laundering and financing of terrorism risk is part of sound internal governance arrangements and credit institutions’ risk management framework.” See also EBA Opinion on how to take into account ML/TF risks in the Supervisory Review and Evaluation Process (EBA/Op/2020/18) and EBA Revised Guidelines on common procedures and methodologies for the supervisory review and evaluation process (SREP) and supervisory stress testing under Directive 2013/36/EU (EBA/GL/2022/03).

<sup>518</sup> Article 18(f) in conjunction with Article 67(1)(o) of Directive 2013/36/EU.

## 2 The duty of diligence as an element of the principle of good administration

The notion of “duty of diligence” or “duty of care”<sup>519</sup> became widely acknowledged following the landmark judgment delivered in 1991 by the Court of Justice in the *Technische Universität München*<sup>520</sup> case. The formulation developed in this judgment, often reiterated in subsequent case-law, identifies the duty of care as “the duty of the competent institution to examine carefully and impartially all the relevant aspects of the individual case”<sup>521</sup> when adopting its decisions. EU courts consider the duty of diligence to be inherent in the principle of good administration<sup>522</sup> and have consistently ruled that this duty applies also when an institution exercises discretionary administrative powers. In fact, in the Court’s view, compliance with the duty of diligence is all the more important in procedures for the adoption of decisions entailing a broad discretion, as in these cases the institutions’ power of appraisal is circumscribed by the principle of care.<sup>523</sup> This aspect is very closely related to the central feature of the duty of diligence as a tool for EU courts to review the correctness of complex technical assessments without encroaching upon the discretionary powers granted to institutions.<sup>524</sup>

Many eminent scholars have investigated the central role played by the duty of diligence in calibrating the intensity of judicial review of discretionary acts, underlining how this duty has become a tool for EU courts to revise the factual bases of administrative decisions, insofar as “it concerns the process of collecting the

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<sup>519</sup> The terminology used by EU courts to refer to the notions of “care” and “diligence” has not been consistent across case-law: references have been made, inter alia, to the “duty of care” (see e.g., Case T-167/94, *Nölle v Council and Commission*, EU:T:1995:169, para. 73), the “duty of diligence” (see e.g., Case T-108/08, *Davidoff v OHMI*, EU:T:2011:391, para. 19), and the “duty of diligent and impartial examination” (see e.g., Case C-290/07 P, *Commission v Scott*, EU:C:2010:480, para. 90). For an overview of the terminology used by EU courts to refer to the principle of care, see Mihaescu (2015), pp. 394-405. The author notes that the principles of care and diligence may to a great extent be applied in an interchangeable way but that a distinction between the two may be identified in the fact that “the EU Courts’ case-law highlights that more often than not the principle of diligence is interpreted in conjunction with the ‘reasonable time’ requirement and therefore the compliance by the administration with its duty to act diligently is often assessed as being dependent on the passage of time that it had taken in order to perform the tasks assigned to it” (Mihaescu (2015), pp. 403-404). For the purposes of the present contribution, the terms “duty of diligence” and “duty of care” will be used in an equivalent manner.

<sup>520</sup> Case C-269/90, *Technische Universität München v Hauptzollamt München-Mitte*, EU:C:1991:438.

<sup>521</sup> Case C-269/90, *Technische Universität München v Hauptzollamt München-Mitte*, para. 14, Case T-285/03, *Agraz and Others v Commission*, EU:T:2005:109, para. 49, Case T-369/06, *Holland Malt v Commission*, EU:T:2009:319, paras. 195-196, Case T-167/94, *Nölle v Council and Commission*, para. 73, Case T-212/03, *MyTravel Group v Commission*, EU:T:2008:315, para. 49.

<sup>522</sup> See Case C-47/07 P, *Masdar (UK) Ltd v Commission*, EU:C:2008:726, paras. 92-93, Case C-556/14 P, *Holcim (Romania) SA v European Commission*, EU:C:2016:207, para. 80, Case C-337/15 P, *European Ombudsman v Claire Staelen*, EU:C:2017:256, para. 34, Case T-286/09, *IntelCorp. v Commission*, EU:T:2014:547, para. 359, Case T-153/19, *European Union Copper Task Force v Commission*, EU:T:2021:688 para. 67.

<sup>523</sup> Case C-269/90, *Technische Universität München v Hauptzollamt München-Mitte*, para. 14, Case T-285/03, *Agraz and Others v Commission*, para. 49, Case C-405/07 P, *Netherlands v Commission*, EU:C:2008:613, para. 56.

<sup>524</sup> See Case T-333/10, *Animal Trading Company (ATC) BV and Others v European Commission*, EU:T:2013:451, para. 84, where the Court notes that “compliance with the duty of the Commission to gather, in a diligent manner, the factual elements necessary for the exercise of its broad discretion as well as the review thereof by the European Union Courts are all the more important because the exercise of that discretion is only subject to a limited judicial review of the merits, confined to examining whether a manifest error has been committed. Thus, the obligation for the competent institution to examine carefully and impartially all the relevant elements of the individual case is a necessary prerequisite to enable the European Union Courts to ascertain whether the elements of fact and of law on which the exercise of that broad discretion depends were present.”

information needed to appraise the relevant factual and legal aspects of a given situation, and the manner in which such information is assessed”.<sup>525</sup> One of these scholars, Professor Hofmann, considers that the approach of EU courts in reviewing compliance with the duty of care requirement encompasses two steps: first, it is examined whether the institution has collected all relevant facts necessary for the adoption of a measure; second, it is examined whether such facts are capable of sustaining the decision, i.e. whether the final act can logically be based on and is consistent with the facts it relies on.<sup>526</sup>

Two elements can therefore be identified in the duty of care requirement.<sup>527</sup> The first dimension is the so-called “factual element” connected to the “fact-collection” activity underlying administrative decisions, whereby in principle all relevant facts substantiating a decision must be collected by the decision-making authority. EU courts have considered that when performing this activity an institution must conduct a diligent and impartial examination so that it has at its disposal, when adopting the final decision, “the most complete and reliable information possible for that purpose”.<sup>528</sup> Compliance with this dimension of the duty of diligence therefore requires that evidence collected for the purposes of the decision contains all the information which must be taken into account in order to assess a complex situation (i.e. the most complete information possible), but also that such evidence is factually accurate and consistent (i.e. the most reliable information possible). This element of the duty of care requirement is an essential pre-condition for the quality of the overall decision-making process, and of the final decision,<sup>529</sup> and fosters the impartiality of administrative action, in line with the broader principle of good administration as laid down in Article 41 of the Charter of Fundamental Rights of the European Union.

The second dimension of the duty of care requirement is the so-called “cognitive element”, which entails a diligent and impartial assessment of the evidence collected, which must substantiate the conclusions drawn from it in the final decision. The Court’s review, in this respect, encompasses the way the institution has assessed the evidence, by scrutinising whether the decision is compatible with the factual and legal elements it is based on.<sup>530</sup> For decisions entailing a broad discretion, compliance with

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<sup>525</sup> Mendes (2017), pp. 155-156.

<sup>526</sup> Hofmann (2020), pp. 87-112.

<sup>527</sup> Hofmann (2020) observes that the two aspects of the principle of care reviewed by EU courts can already be identified in Case 6/54, *Nederlands v High Authority*, to which the origins of the approach to the definition of the duty of care by the case-law date back.

<sup>528</sup> Case C-290/07 P, *Commission v Scott*, para. 90.

<sup>529</sup> See, along these lines, the recent judgment in Joined Cases C-65/21 P and C-73/21 P to C-75/21 P, *SGL Carbon v Commission*, EU:C:2022:470, para. 32, where the Court notes that “[a]dmittedly, the fact that all the relevant facts of the individual case have been taken into account carefully and impartially is not, of itself, sufficient to prevent the institution concerned from committing a manifest error of assessment. Nevertheless, a breach, by that institution, of its duty of diligence is the most common reason for such an error.”

<sup>530</sup> Mendes (2017) notes that this notion of duty of diligence developed by the case-law converges with the line of case-law concerning the standard of judicial review of administrative discretion, initiated with the judgment in the *Tetra-Laval* case, as both lines of case-law “enable the Court to scrutinize the information on the basis of which the act was adopted, the way the decision-maker has collected and treated that information and to assess the plausibility of the conclusion it took therefrom. On this basis, the reviewing court is capable of assessing the plausibility of the decision in view of the facts that grounded the choices ultimately made”. (Mendes (2017), p. 159). In this respect, see e.g. Case T-257/07, *France v Commission*, EU:T:2011:444, paras. 84-89, and Case C-525/04 P, *Spain v Lenzing*, EU:C:2007:698, paras. 56-58, where EU courts bring together the standard of judicial review of discretionary decisions and the duty of diligence.

this second element of the duty of diligence is all the more important, according to the Court, “because the exercise of that discretion is only subject to a limited judicial review of the merits, confined to examining whether a manifest error has been committed”.<sup>531</sup>

The duty of diligence is therefore a general obligation which EU institutions must comply with throughout the process leading to the exercise of their administrative powers and the adoption of their decisions. It should be noted, though, that the scope of such an obligation cannot be defined in general terms and must be assessed on a case-by-case basis. The duty of care is thus, to use the words of Advocate General Szpunar in the recent case *SGL Carbon v Commission*, an obligation of “variable contours”,<sup>532</sup> since its scope is shaped by the provisions determining the powers and the discretion of an administration in a particular case. This is a relevant point for our discussion because it suggests that the scope of the ECB’s duty of diligence not only cannot be at odds with the boundaries of the ECB’s competences but is also shaped by them.

These considerations lead us to some reflections on the scope of the ECB’s duty of diligence when assessing AML/CFT aspects relevant to its supervisory tasks.

### 3 The ECB’s duty of diligence when assessing AML/CFT aspects in the exercise of its supervisory tasks

The objective of reducing ML/TF risks in credit institutions is separate from, but closely connected to, the objective of prudential supervision, to ensure credit institutions’ safety and soundness and the stability of the financial system at large.<sup>533</sup> Therefore, prudential supervisors of credit institutions, including the ECB in its supervisory capacity, integrate AML/CFT concerns systematically when performing their prudential tasks.

In cases where AML/CFT aspects are relevant for the purposes of the adoption of an ECB supervisory decision, the input of national AML authorities plays a key role, since

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<sup>531</sup> Case T-333/10 *Animal Trading Company (ATC) BV and Others v European Commission*, para. 84. On the topic of judicial review of supervisory discretion, see Ioannidis (2021).

<sup>532</sup> Advocate General Szpunar notes that: “the duty of diligence, being a general obligation of the EU administration, is one of variable contours. In practice, in each type of administrative intervention, the taking into consideration of all the relevant circumstances should be preceded by an analysis of the scope of the administration’s powers and of its discretion, as determined by the provisions applicable to the particular case. That is true, in particular, as regards the administration’s adoption of delegated or implementing acts of general scope, or of individual acts. In that situation, the scope of the administration’s duty of diligence is determined by the provisions applied in the particular case, which determine the scope of the powers of the administration and its discretion. On the basis of those provisions, the administration identifies all of the relevant circumstances to be taken into account. It is impossible to analyze the administration’s duty of diligence without taking account of the concrete situation governed by those provisions.” See opinion of Advocate General Szpunar in Joined Cases C-65/21 P and C-73/21 P to C-75/21 P, *SGL Carbon v Commission*, paras. 54-55.

<sup>533</sup> See Joined Cases T-351/18 and T-584/18, *Ukrseľhosprom PCF LLC and Versobank AS v ECB*, EU:T:2021:669, para. 185, according to which compliance with AML-CFT obligations “is clearly relevant in the context of prudential supervision, since, as underlined in recitals 1 and 2 of Directive 2005/60, the use of the financial system for money laundering purposes is likely to threaten the stability, integrity and reputation of the financial system and of the single market”. See also Commission Communication COM/2018/645 final, Strengthening the Union framework for prudential and anti-money laundering supervision for financial institutions.



the elements ascertained by such authorities constitute facts on which the ECB relies in order to substantiate its own decision.

In this regard, it should be noted that the EU legislator has expressly decided that supervision of compliance with AML/CFT provisions is not conferred on the ECB under Article 4(1) SSM Regulation and should remain with the relevant national authorities.<sup>534</sup> Therefore, the ECB cannot carry out AML/CFT-related supervisory tasks or enforce AML/CFT legislation: if this were done, the ECB would encroach on the competence of national authorities and thus breach EU law. In concrete terms, this means that whenever AML/CFT aspects come into relevance for the adoption of its decisions, the ECB needs to rely on facts established by the relevant AML authority.

The boundaries to the ECB's powers stemming from the allocation of competences under the SSM Regulation raise relevant questions concerning the scope of the ECB's duty of diligence when assessing AML/CFT aspects in the exercise of its supervisory tasks.

An attempt to better define this scope can be made building upon the two dimensions of the duty of care requirement mentioned in Section 2 of this contribution.

In the "fact-collection" phase, since the ECB lacks the competence to (re-)investigate or (re-)establish for itself the facts submitted by the AML authority or to draw from them any conclusion on lack of compliance with AML/CFT legislation, the reliability of such facts may only be assessed by verifying whether they appear to be well-founded, sufficiently specific, accurate and consistent. For this purpose, the ECB should take into account all relevant aspects of the concrete case, including how and where the determinations of the AML authority have been made, having regard for example to whether they are laid down in binding legal acts, on-site inspection reports, or preliminary assessments. In order to comply with the duty to collect the most complete and reliable information possible, in line with the applicable case-law, the ECB should also request additional information or evidence to the AML authority if the relevant facts do not appear to be clear or sufficiently specific. An analogy could be drawn with the scope of the duty of care of the Council when adopting restrictive measures upon information provided by the Sanctions Committee of the United Nations or by authorities of a third country. According to the case-law in this field, the Council is not required to carry out, systematically or on its own initiative, its own investigations or checks for the purpose of obtaining additional information from such authorities. At the same time, in order to discharge its duty of care, the Council is required to assess, on the basis of the circumstances of the case, whether it is necessary to seek the disclosure of additional evidence from the Sanctions Committee or the third country authorities if it transpires that the evidence already supplied is insufficient.<sup>535</sup>

Different considerations become relevant as concerns the scope of the ECB's duty of diligence when performing the legal assessment of the factual and legal elements of the case in order to conclude whether the adoption of a certain decision is warranted. In this phase, the scope of the ECB's duty of diligence is not constrained by the

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<sup>534</sup> Recitals 15 and 28 SSM Regulation.

<sup>535</sup> See, e.g., Case T-107/15, *Uganda Commercial Impex v Council*, EU:T:2017:628, paras. 53-54 and para. 62, Case T-545/13, *Al Matri v Council*, EU:T:2016:376, paras. 57 and 68.

boundaries to the ECB's powers because this assessment only rests on prudential considerations, which entirely fall within the ECB's competence. The ECB in fact enjoys full discretion in assessing which conclusions, if any, are to be drawn from AML/CFT findings for the purposes of potential prudential supervisory actions.

The two dimensions of the duty of care requirement become intertwined during the right to be heard phase, when the persons who are the subject to the administrative proceedings have the possibility to make known their observations on the draft ECB decision. The link between the duty of care and respecting other procedural rights, notably the right to be heard, has been consistently established by the relevant case-law,<sup>536</sup> which requires institutions not only to hear, but also to examine carefully and impartially, the points raised by the parties to the administrative procedure.<sup>537</sup> The right to be heard under Article 24 SSM Regulation and Article 31 SSM Framework Regulation<sup>538</sup>, constituting an essential procedural guarantee in the process for the adoption of ECB supervisory decisions, seems to play an even more important role when an ECB decision is based on the findings of AML authorities, i.e. on facts which have not been investigated by the ECB itself. During the right to be heard phase, in fact, the ECB discloses the draft decision to its addressee, enabling it to provide its comments and examine whether any exculpatory evidence provided by it raises material doubts as to whether the facts on which the draft decision is based are erroneous. This phase, therefore, is an important test for the ECB to verify whether the findings provided by the AML authority, and the ECB's conclusions based on them, are well founded in the light of the observations presented by the party concerned. The outcome of this test indirectly has a bearing on the evidentiary value of the facts on which the decision is based and, consequentially, on the ECB's compliance with its duty of diligence in taking those facts into account. For instance, if no evidence is provided by the party concerned to contest those findings, their reliability appears confirmed and even strengthened, which in turn seems to advocate in favour of the ECB considering them established facts.

## 4 The ECB's duty of diligence in licence withdrawal procedures based on serious infringements of AML/CFT provisions

A concrete example of how the two dimensions of the duty of care requirement interact when the ECB examines AML/CFT aspects in the exercise of its supervisory tasks can be found in licence withdrawal procedures based on serious breaches of AML/CFT provisions.

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<sup>536</sup> See Case C-269/90, *Technische Universität München v Hauptzollamt München-Mitte*, para. 14 and para. 25, Case T-413/03, *Shandong Reipu Biochemicals v Council*, EU:T:2006:211, para. 63, Case T-633/11, *Guangdong Kito Ceramics and Others v Council*, EU:T:2014:271, para. 43.

<sup>537</sup> See Case T-358/17, *Mohamed Hosni Elsayed Mubarak v Council of the European Union*, EU:T:2018:905, para. 153, Case C-349/07, *Sopropé*, EU:C:2008:746, para. 50, Joined Cases C-584/10 P, C-593/10 P and C-595/10 P, *Commission and Others v Kadi*, EU:C:2013:518, para. 114.

<sup>538</sup> Regulation (EU) No 468/2014 of the European Central Bank of 16 April 2014 establishing the framework for cooperation within the Single Supervisory Mechanism between the European Central Bank and national competent authorities and with national designated authorities (OJ L 141, 14.5.2014, p. 1).

In this respect, it should be noted that in the Single Supervisory Mechanism (SSM) legal framework the ECB has the exclusive competence to withdraw authorisations of all credit institutions, irrespective of their size.<sup>539</sup>

From the perspective of EU administrative law, the withdrawal of a licence qualifies as a composite procedure,<sup>540</sup> where the national competent authority (NCA) submits a preparatory act,<sup>541</sup> and the ECB alone exercises the final decision-making power, taking into account the justification put forward by the NCA<sup>542</sup> but without being bound by its proposal.<sup>543</sup>

According to Article 83 SSM Framework Regulation, in making the decision on whether to accept or reject the draft withdrawal proposal submitted by the NCA, the ECB must take into account: (i) its own assessment of the circumstances justifying the withdrawal of authorisation; (ii) the NCA's proposal; (iii) consultations held with the relevant NCA; and (iv) any comments provided by the credit institution in the exercise of its right to be heard.

The legal framework, therefore, while allowing the ECB to exercise full discretion on the decision to withdraw a licence, expressly requires it to take into account certain factors when doing so, thereby setting the standard of the ECB's duty of care in the context of licence withdrawal procedures. This provision plays an even more important role in the context of licence withdrawal procedures concerning less significant institutions, as in these cases the ECB typically is not directly involved in the supervision of the entity<sup>544</sup> until such time that the situation deteriorates and closer interactions between the ECB and the relevant NCA start. In these cases, relevant factors in the supervisory history of the bank – including for example supervisory actions undertaken by the NCA and opportunities given by the NCA to the bank in order to remedy the situation – constitute key aspects that the ECB must take into account in order to comply with the principles of duty of care and of proportionality.

In its two recent *Versobank* and *AAB Bank* judgments, the General Court ruled on two cases of withdrawal of authorisation on account of serious breaches of AML/CFT legislation. In these judgments the General Court had the opportunity to provide its view on the interpretation of the legal framework concerning the division of powers between national authorities and the ECB in licence withdrawal procedures based on infringements of AML/CFT provisions. These findings of the Court paved the way for it

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<sup>539</sup> Articles 4(1)(a) and Article 14(5) SSM Regulation.

<sup>540</sup> On the topic of composite procedures in the SSM, see Brito Bastos (2019), pp. 1355-1378; Brito Bastos (2021); and Di Bucci (2021).

<sup>541</sup> Pursuant to Article 82 SSM Framework Regulation, the process to withdraw an authorisation may also start on the initiative of the ECB, which in this case must consult with the NCA of the Member State where the credit institution is established before adopting the licence withdrawal decision.

<sup>542</sup> Article 14(5), second subparagraph, SSM Regulation.

<sup>543</sup> See Case C-219/17, *Silvio Berlusconi and Fininvest SpA v Banca d'Italia and IVASS*, EU:C:2018:1023, para. 55.

<sup>544</sup> The SSM centralises functions relating to prudential supervision with the ECB, while providing for decentralised implementation of some tasks by the NCAs, under the supervision of the ECB, to which they provide their cooperation and assistance. In particular, within the SSM, the ECB is exclusively competent to exercise the tasks under Article 4(1)(a) and (c) SSM Regulation with regard to all institutions, irrespective of their significance status, and to carry out the direct prudential supervision of significant credit institutions, while NCAs carry out direct prudential supervision of less significant institutions.

to assess the ECB's duty of diligence in licence withdrawal procedures, having regard to the specific facts and relevant factors supporting each of the two contested decisions.

#### 4.1 The General Court judgment in the *Versobank* case

On 6 October 2021 the General Court delivered its judgment<sup>545</sup> in the action for annulment against the ECB decision withdrawing the licence of Versobank AS, a less significant institution falling under the direct supervision of Finantsinspektion (the Estonian Financial Supervisory Authority, FSA).<sup>546</sup> The contested decision was also based on the ground for licence withdrawal under Article 18(f) in conjunction with Article 67(1)(o) of Directive 2013/36/EU, having regard to the FSA's findings of repeated and serious AML/CFT breaches committed by the bank.

Two aspects of this judgment, which elaborates on a wide range of relevant issues,<sup>547</sup> appear of particular interest for the purposes of the present contribution.

The first aspect relates to the General Court's findings on the delineation of competences between the FSA and the ECB as concerns the withdrawal of Versobank's authorisation. These findings address the applicants' claim that the ECB does not have the power to adopt a licence withdrawal decision on the ground of infringements of AML/CFT provisions, because it lacks competence on such matters, and that by withdrawing Versobank's authorisation based on this ground the ECB infringed the FSA's powers in the AML/CFT field.

In order to address this claim, the Court preliminarily notes the provisions governing the division of powers between the ECB and NCAs within the SSM,<sup>548</sup> focusing in particular on the role of NCAs in carrying out direct supervision of less significant institutions and in assisting the ECB when the latter exercises its tasks under Article 4(1)(a) and (c) SSM Regulation towards these institutions. As concerns, more specifically, the task of withdrawing an authorisation, the Court notes that the cooperation between the ECB and NCAs is expressed as an option of the NCAs to propose such a withdrawal to the ECB, which must carry out its own examination as to whether there are circumstances justifying it and thus take a decision on the proposed licence withdrawal.<sup>549</sup> Finally, the General Court notes that national authorities remain competent in respect of matters not covered by the SSM Regulation, including the

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<sup>545</sup> Joined Cases T-351/18 and T-584/18, *Ukrseļhosprom PCF LLC and Versobank AS v ECB*. An appeal against the first instance ruling to the Court of Justice is pending as Case C-803/21 P.

<sup>546</sup> In the Estonian legal framework, the FSA is responsible for both prudential matters (thereby acting as NCA within the meaning of Article 2(2) SSM Regulation) and for compliance with AML/CFT obligations.

<sup>547</sup> The judgment touches upon, inter alia, the interplay between the SSM and the Single Resolution Mechanism, the proportionality assessment underlying the adoption of a licence withdrawal decision, and the judicial review of EU courts following the internal administrative review of an ECB decision. On this last topic, see Witte (2022), pp. 45-60.

<sup>548</sup> Joined Cases T-351/18 and T-584/18, *Ukrseļhosprom PCF LLC and Versobank AS v ECB*, paras. 114-153.

<sup>549</sup> *ibid.*, paras. 140-141.

supervision of compliance with AML/CFT provisions, and that the ECB has a duty of cooperation vis-à-vis such national authorities.<sup>550</sup>

Having regard to the abovementioned provisions governing the allocation of powers within the SSM, and in particular Article 4(1)(a) and Article 14(5) SSM Regulation, the Court notes that the ECB has the exclusive competence to withdraw authorisations of all credit institutions established in the SSM, irrespective of their size, in the cases set out in the relevant EU law. Since, pursuant to Article 18(f) in conjunction with Article 67(1)(o) of Directive 2013/36/EU, the authorisation of a credit institution may be withdrawn when the latter is found liable for a serious breach of the national provisions adopted pursuant to Directive 2005/60/EC<sup>551</sup>. It follows that the ECB is competent to withdraw an authorisation on the ground of AML/CFT infringements as well.<sup>552</sup>

The Court considers that in the present case the ECB exercised this competence in accordance with the relevant legal framework and did not infringe the FSA's powers in the AML/CFT field. In fact, Versobank's compliance with AML/CFT provisions was monitored through several investigations carried out by the FSA.<sup>553</sup>

In the light of the above, the Court concludes that "[i]t was therefore without disregarding the division of powers between the NCAs of the participating Member States and the ECB under the SSM that, in the present case, the facts constituting breaches of the AML/CFT legislation were established by the FSA, whereas the legal assessment of whether those facts justified withdrawal of authorisation and the assessment of proportionality were reserved for the ECB".<sup>554</sup>

The findings of the Court concerning the delineation of the FSA's and the ECB's powers are closely related to the second aspect of the judgment which is relevant for our purposes, namely the Court's consideration of the ECB's duty to conduct a careful and impartial assessment of the relevant aspects of the case.

The Court's findings in this regard address the applicants' claim that the ECB simply relied on the FSA's conclusions without carrying out its own examination of the relevant facts of the case.<sup>555</sup> This claim is rejected by the Court with an argument which brings together the principle of care and the principle of conferral. The premise on which the Court's reasoning rests is that, in light of the abovementioned considerations on the allocation of powers and the cooperation between the ECB and the FSA, the ECB was indeed entitled to rely on the information included in the FSA's proposal in order to substantiate its decision.<sup>556</sup> Based on this premise, the Court further develops its argument with reference to specific facts included in that proposal,

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<sup>550</sup> *ibid.*, paras. 131 and 142.

<sup>551</sup> Directive 2005/60/EC of the European Parliament and of the Council of 26 October 2005 on the prevention of the use of the financial system for the purpose of money laundering and terrorist financing (OJ L 309, 25.11.2005, p. 15); no longer in force (date of end of validity: 25 June 2017); repealed, replaced, and to be read as a reference to Directive (EU) 2015/849 (OJ L 141, 5.6.2015, p. 73); compare Article 66 of Directive (EU) 2015/849.

<sup>552</sup> Joined Cases T-351/18 and T-584/18, *Ukrselhosprom PCF LLC and Versobank AS v ECB*, paras. 184-190.

<sup>553</sup> *ibid.*, para. 193.

<sup>554</sup> *ibid.*, para. 197.

<sup>555</sup> *ibid.*, para. 214.

<sup>556</sup> *ibid.*, para. 220, cross-referring to paras. 194-198.

namely the FSA's findings of breaches "which have not been properly challenged by the second applicant",<sup>557</sup> and considers that these findings "had to be treated by the ECB as established facts and as not requiring, for that reason, a review by the ECB".<sup>558</sup> The conclusion reached by the Court takes account of the fact that, as already mentioned, when it comes to AML/CFT breaches the ECB must rely on the findings of the AML authority. This, however, cannot offset the ECB's obligation to comply with the principle of care; a relevant indication in this direction can be found in the prominence given by the Court to the fact that, in the present case, the breaches had not been properly challenged by the bank,<sup>559</sup> an element which corroborates the reliability of the FSA's findings. It is therefore only after having concluded that these findings constituted a complete and reliable set of information that the ECB *had to* consider them as established facts, and "rightly confined itself to verifying whether they indeed constituted grounds justifying the withdrawal of authorisation".<sup>560</sup>

These considerations lead us to the part of the judgment where the Court reviews the ECB's compliance with the duty to perform a diligent and impartial assessment of the evidence collected in order to conclude whether the grounds for adoption of the decision are met. The Court deals with this aspect by addressing several pleas which sought to cast doubts on the ECB's assessment<sup>561</sup> without however substantively challenging the ECB's conclusion that the ground for licence withdrawal based on serious AML/CFT infringements was met. These parts of the judgment include extensive and detailed references to the supervisory history of interactions between the FSA and Versobank in the years preceding the licence withdrawal<sup>562</sup>, giving an account of the persistent and structural nature of the AML/CFT breaches and of the fact that the bank did not duly remedy them, despite several opportunities to do so and several warnings from the FSA. In light of these elements, described and analysed in the statement of reasons of the contested decision, the Court rejects the applicants' pleas that the ECB committed an error of assessment when considering that the relevant grounds for withdrawing Versobank's licence were met.

## 4.2 The General Court judgment in the *AAB Bank* case

On 22 June 2022, the General Court delivered its judgment<sup>563</sup> in the action for annulment against the ECB decision withdrawing the licence of Anglo Austrian Bank (AAB) AG, a less significant institution falling under the direct supervision of

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<sup>557</sup> *ibid.*, para. 219.

<sup>558</sup> *ibid.*, para. 219.

<sup>559</sup> The circumstance that the applicants did not properly challenge the facts on which the decision was based and did not provide any evidence to demonstrate that the information provided by the FSA was misleading is remarked in several parts of the judgment (see, for instance, paras. 218, 221, 233, 257 and 289).

<sup>560</sup> Joined Cases T-351/18 and T-584/18, *Ukrseļhosprom PCF LLC and Versobank AS v ECB*, para. 219.

<sup>561</sup> See for instance Sections 3 and 4 of the judgment (paras. 226-296), addressing the applicants' claims that certain aspects of the case were not duly taken into account and that the ECB committed certain errors of assessment.

<sup>562</sup> See, e.g., Joined Cases T-351/18 and T-584/18, *Ukrseļhosprom PCF LLC and Versobank AS v ECB*, para. 278.

<sup>563</sup> Case T-797/19 *Anglo Austrian AAB and Belegging-Maatschappij "FarEast" v ECB*, EU:T:2022:389. An appeal against the first instance ruling to the Court of Justice is pending as Case C-579/22 P.

Österreichische Finanzmarktaufsicht (the Austrian Financial Market Authority, FMA).<sup>564</sup>

The *AAB Bank* judgment offers interesting elaborations on several legal issues revolving around the topic of withdrawal of banking authorisations, such as the interpretation of EU law provisions laying down the cases when an authorisation may be withdrawn,<sup>565</sup> the proportionality assessment supporting a licence withdrawal decision,<sup>566</sup> and the procedural rights applicable in the administrative procedure leading to a withdrawal of authorisation, including the right to good administration enshrined in Article 41 of the Charter.<sup>567</sup> The present contribution will focus on the part of the judgment dealing with this last aspect, where the Court addresses the applicants' claim that the ECB did not comply with its duty to determine, examine and assess carefully and impartially all the relevant matters of the case because it relied on facts ascertained by the FMA rather than carrying out its own investigations of such facts.<sup>568</sup>

The Court approaches this claim by drawing a distinction between the two grounds for withdrawal on which the contested decision was based.

As concerns the ground relating to serious AML/CFT infringements,<sup>569</sup> the Court notes in the first place that national law provisions transposing Article 67(1)(o) of Directive 2013/36/EU must be interpreted in accordance with the delineation of competences envisaged under the SSM Regulation: it follows that, contrary to the applicants' claim, the legal framework does not require the ECB to establish for itself that a credit institution has committed a serious infringement of AML/CFT provisions and that the ECB must rely on decisions of national authorities to that effect.<sup>570</sup> The Court further notes that in the present case the ECB has demonstrated the existence of the relevant facts justifying the withdrawal of authorisation on account of serious AML/CFT infringements by relying on decisions of the FMA, on rulings of national courts, on reports of the bank's internal audit function and on its own assessment of the relevant documentation. Therefore, the ECB did not simply refer to the breaches laid down in the FMA's proposal, but it ascertained, for the purposes of the examination of the facts and evidence available, that the bank had been found liable for serious AML/CFT breaches.<sup>571</sup>

As concerns the ground relating to the failure to have in place appropriate and robust governance arrangements<sup>572</sup> – a matter that, contrary to AML/CFT aspects, falls squarely within the competences of the ECB pursuant to Article 4(1)(e) SSM

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<sup>564</sup> In the Austrian legal framework, the FMA is responsible for both prudential matters (thereby acting as NCA within the meaning of Article 2(2) SSM Regulation) and for compliance with AML/CFT obligations.

<sup>565</sup> Case T-797/19 *Anglo Austrian AAB and Belegging-Maatschappij "FarEast" v ECB*, paras. 20-162.

<sup>566</sup> *ibid.*, paras. 163-201.

<sup>567</sup> *ibid.*, paras. 251-273.

<sup>568</sup> *ibid.*, para. 251.

<sup>569</sup> Ground for licence withdrawal under Article 18(f) of Directive 2013/36/EU in conjunction with Article 67(1)(o) of Directive 2013/36/EU.

<sup>570</sup> Case T-797/19 *Anglo Austrian AAB and Belegging-Maatschappij "FarEast" v ECB*, para. 258.

<sup>571</sup> *ibid.*, para. 259.

<sup>572</sup> Ground for licence withdrawal under Article 18(f) of Directive 2013/36/EU in conjunction with Article 67(1)(d) of Directive 2013/36/EU.

Regulation — the Court notes that the ECB did not simply refer to the breaches laid down in the FMA's licence withdrawal proposal but it verified for itself the breaches of prudential provisions ascertained by the FMA,<sup>573</sup> i.e. it based its decision on its own assessment of compliance with national provisions transposing Article 74 of Directive 2013/36/EU.<sup>574</sup> The Court also notes that the ECB was entitled to rely on decisions of the FMA for this purpose.<sup>575</sup>

These findings of the Court, while confirming on the one hand that the ECB is subject to the duty to examine and assess carefully and impartially all the matters of fact relevant to the withdrawal of authorisation, on the other hand suggest that compliance with such duty is to be assessed against the scope of the ECB's competences. Thus, according to the interpretation of the Court, for matters falling within its competences, the ECB is entitled to base its assessment on the information provided by national authorities, while for matters outside of its competences, like AML/CFT aspects, the ECB must base its assessment on the facts established by such authorities. Once again, therefore, similarly to the *Versobank* judgment, the Court's review of the ECB's compliance with the principle of care takes fully into account the boundaries to which the ECB is subject when exercising its tasks.

In the light of the above considerations, the Court concludes that the ECB cannot be criticised for having omitted to carefully examine and assess all aspects relevant to the withdrawal of AAB Bank's authorisation.<sup>576</sup>

## 5 Conclusion

The EU legal framework requires the ECB to appropriately account for ML/TF aspects when exercising its own responsibilities and tasks as prudential supervisor. For this purpose, the ECB must leave the assessment of compliance with AML/CFT provisions to national AML authorities, which are competent in that field, but is still required to conduct a diligent and impartial examination of the findings of such authorities when it relies on them to substantiate its own decisions.

This conclusion is supported, as concerns the exercise of the task of withdrawal of authorisation, by the findings of the General Court in the *Versobank* and *AAB Bank* cases. In these judgments, the Court ruled that the ECB is subject to a duty to examine and assess carefully and impartially all the matters of fact relevant to the licence withdrawal decision and provided relevant indications on how the scope of such a duty can be reconciled with the principle of conferral.

While these judgments offer a valuable interpretation of how the ECB should integrate AML/CFT concerns in licence withdrawal procedures, relevant clarifications on this topic could still be provided by the Court of Justice in the appeal proceedings. Moreover, the judgments leave open the point concerning the scope of the ECB's duty

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<sup>573</sup> Case T-797/19 *Anglo Austrian AAB and Belegging-Maatschappij "FarEast" v ECB*, para. 267.

<sup>574</sup> *Ibid.*, para. 266.

<sup>575</sup> *ibid.*, para. 271.

<sup>576</sup> *ibid.*, para. 272.



of diligence in the exercise of other supervisory tasks, such as for instance, the assessment of qualifying holding acquisitions. Interesting questions which arise in this respect concern, for instance, the scope of the ECB's assessment of criteria under Article 23(1)(e) of Directive 2013/36/EU, related to the suspicion of money laundering or terrorist financing or an increased risk thereof, and the standard of reliability for evidence substantiating such criteria.<sup>577</sup> Further reflection seems to be warranted on these aspects, which deserve particular attention also in the light of the practical implications they may have on the interaction between the ECB and national authorities in the context of qualifying holding procedures.

In conclusion, although the *Versobank* and *AAB Bank* cases do not provide a direct answer to these open questions, it seems to me that the findings of the Court in these judgments, read together with the case-law on the duty of diligence, indicate a clear direction to address them.

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<sup>577</sup> In this respect, it should be considered that the assessment of a proposed qualifying holding acquisition strongly relies on forward-looking considerations and is therefore supported by a different type of evidence compared, for example, to a licence withdrawal decision, which is based on the examination of relevant facts that happened in the past. Moreover, Article 23(2) of Directive 2013/36/EU provides that the competent authority may oppose a proposed acquisition if there are "reasonable grounds" for doing so; this wording seems to suggest that a decision opposing the acquisition of a qualifying holding could be adopted by the ECB also based on less conclusive evidence than that required for a licence withdrawal decision.

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# Legal challenges of considering anti-money laundering/countering the financing of terrorism (AML/CFT) risks in prudential supervision. The particular point of view of a national competent authority (NCA) that is not the national AML/CFT authority

By Rafael Martín Lozano\*

## 1 Introduction

Money laundering (ML) and terrorist financing (TF) damage the economy and society in many different ways. ML facilitates and perpetuates crime and supports criminals, while TF facilitates terrorist attacks all over the world. Together, they undermine the trust of citizens in financial institutions, negatively affect market integrity and threaten the stability of the financial system.<sup>578</sup>

Cases of recent breaches of anti-money laundering (AML) rules in the banking sector have shown that banks' involvement in ML can hamper a bank's reputation, pose significant risks to its sound management and funding and affect relations with its customer. Not only that, on a larger scale, these breaches are a threat to banks themselves and indeed to their viability (e.g. liquidity crisis due to a run on deposits). It is clear that breaches of AML or counter-terrorist financing (CTF) provisions may be symptoms of unsound governance and internal control mechanisms.

Definitely, the way credit institutions design government arrangements, internal control functions and sound management processes to properly govern AML and CFT are relevant to prudential supervisors. This has been acknowledged by EU legislators, who have taken a number of steps to clarify and strengthen the important link between AML/CFT and prudential issues in banks' life cycle. Among them, the Capital

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<sup>578</sup> See the European Banking Authority's (EBA) Factsheet on Anti-Money laundering and countering the financing of terrorism. February 2020.

Requirements Directive (CRD)<sup>579</sup> has been amended to require prudential supervisors to act on AML/CFT information.<sup>580</sup>

In this regard, risks related to AML/CFT issues should be considered in some of the most relevant prudential supervisory procedures. In particular, when granting a banking licence, assessing whether the bank's managers are fit for the job, when reviewing how the business model risks are evaluated, how client and counterparty risks are overseen and managed in the everyday operations of the bank, in assessing acquisitions of qualifying holdings, and finally, whether and when a bank's licence should be withdrawn due to AML/CFT breaches. Where the prudential supervisor finds reasonable grounds to suspect that ML/TF is, or has been, committed or attempted, or that there is increased risk thereof, the CRD requires prudential supervisors to adopt measures to mitigate that risk. In the case of certain supervisory procedures such as fit and proper or qualifying holding, those measures could include rejecting applications; in the case of ongoing reviews, prudential supervisors have to notify the EBA and the bank's AML/CFT supervisor immediately.

With the establishment of the Single Supervisory Mechanism (SSM), prudential responsibilities for significant credit institutions and, for certain tasks (authorisation and withdrawal of licences, and assessment of qualifying holdings<sup>581</sup> acquisitions) for all credit institutions in the Banking Union, were transferred to the European Central Bank (ECB). The ECB, like all prudential supervisors, has to take AML/CFT concerns into account in its prudential supervisory activities. However, when acting in its supervisory capacity, the ECB is not the AML/CFT authority.<sup>582</sup> The transfer of prudential supervisory powers to the ECB introduced an additional institutional layer for cooperation and coordination, adding interaction with the ECB to the interaction between domestic AML/CFT supervisors and prudential authorities.<sup>583</sup> As covered later in this article, this complexity could be even more acute in frameworks, such as the Spanish one, in which the national AML/CFT authority and the national prudential authority are not within the same institution.

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<sup>579</sup> Directive (EU) 2019/878 of the European Parliament and of the Council of 20 May 2019 amending Directive 2013/36/EU as regards exempted entities, financial holding companies, mixed financial holding companies, remuneration, supervisory measures and powers and capital conservation measures (OJ L 150, 7.6.2019, p. 253).

<sup>580</sup> Opinion of the European Banking Authority on communications to supervised entities regarding money laundering and terrorist financing risks in prudential supervision, July 2019, (EBA-Op-2019-08 24). The amendments introduced an explicit cooperation obligation between prudential authorities and AML/CFT authorities and Financial Intelligence Units (FIUs) and removed confidentiality barriers to effective information exchange between those authorities. Furthermore, CRD V clarifies the possibility for prudential supervisors to use available prudential tools to address AML/CFT concerns from a prudential perspective. It provides more details on the assessment of the internal controls and risk management systems during the authorisation process. It also introduces an explicit power to remove members of the management board in case of concerns related to their suitability, including from an AML/CFT perspective. Moreover, CRD V also mentions explicitly the AML/CFT dimension in the context of the supervisory review and evaluation process (SREP), requiring competent authorities to take necessary measures using the tools and powers at their disposal should AML/CFT concerns be significant from a prudential perspective. There is also an obligation for competent authorities to notify the EBA and the authority responsible for AML/CFT supervision where they identify weaknesses in the governance model, business activities or business model, which give reasonable grounds to suspect ML or TF.

<sup>581</sup> In line with recital 22 of the SSM Regulation this would not be the case in the context of a bank resolution.

<sup>582</sup> Recital 28 of the SSM Regulation.

<sup>583</sup> Report from the Commission to the European Parliament and the Council on the assessment of recent alleged money laundering cases involving EU credit institutions. Brussels, 24.7.2019. COM (2019) 373 final.

Against this background, while supervision of financial institutions' compliance with AML/CFT requirements remains an exclusive competence of the national AML/CFT authorities, to keep banks safe and sound, it is essential that supervisors responsible for AML/CFT and prudential supervisors further enhance information exchange and work very closely with each other. However, despite the fact that there are evident points of contact between AML/CFT supervision and prudential supervision, for the sake of reducing legal risks, it is necessary to draw a line and delineate the competences of AML/CFT supervisors and prudential supervisors, including the ECB. In other words, answers to the questions on: (i) where the competences of prudential supervisors end and those of other AML/CFT authorities begin; and (ii) how each authority should rely on the facts shared by the other in order to exercise their own competences, become crucial.

In this regard, in its judgment *Ukrseľhosprom PCF LLC and Versobank AS v European Central Bank*<sup>584</sup> the General Court of the European Union has shed new light on these questions. In particular, the division of powers between the ECB and national AML/CFT authorities as concerns the withdrawal of authorisations for the infringement of AML/CFT rules. This issue was also recently covered by the General Court of the European Union in its judgment *Anglo Austrian AAB Bank AG and Belegging-Maatschappij "Far-East" BV v European Central Bank*,<sup>585</sup> which also touches upon the withdrawal of a banking licence based on AML/CFT breaches.

The purpose of this article is to provide some insights on the main legal challenges stemming from AML/CFT risks and how they are embedded in the prudential supervision faced by a prudential national authority that is not the AML/CFT supervisory authority (i.e. the Banco de España). It will also reflect on how recent court cases will bring some new guidance on how to face those legal challenges.

## 2 Particularities of the Spanish framework on the supervision of AML risks

The current Spanish arrangement on the supervision of AML/CFT risks is unusual among the participant countries of the SSM. Unlike most of the other Member States, the AML/CFT supervisory powers are not allocated within the prudential supervisors.

The Commission for the Prevention of Money Laundering and Monetary Infringements (CPBCIM) is the NCA for AML/CFT pursuant to Law No 10/2010, of April 28, on the Prevention of Money Laundering and the Financing of Terrorism (Law No 10/2010). The CPBCIM is a collegiate body under the umbrella of the Ministry of Economic Affairs and Digital Transformation. It is composed of representatives from a wide variety of Spain's relevant authorities, including policy makers, the Ministry of Economic Affairs, public prosecution, police, civil guard, customs and tax authorities,

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<sup>584</sup> Joint Cases T-351/18 and T-584/18, *Ukrseľhosprom PCF LLC and Versobank AS v European Central Bank*, EU:T:2021:669.

<sup>585</sup> Case T-797/19, *Anglo Austrian AAB AG, formerly Anglo Austrian AAB Bank AG and Belegging-Maatschappij "Far-East" BV v European Central Bank*, EU: T:2022:389.

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intelligence services, data protection authorities and financial entities' prudential supervisors (the Banco de España, the Directorate-General for Insurance and Pension Funds (DGSFP), and the National Securities Exchange Commission (CNMV)). The CPBCIM is responsible for developing and implementing AML/CFT policies, facilitating domestic coordination and cooperation at the policy and operational level.

Two bodies support the CPBCIM in the performance of its mandate: the Secretariat and the Executive Service for the Prevention of Money Laundering and Monetary Infringements (SEPBLAC).

Regarding the supervision of the fulfilment of the obligations derived from the AML/CFT framework, Spain has a dual-track supervisory regime, where the AML/CFT supervisory tasks are the responsibility of SEPBLAC's Executive Service, which carries out its supervisory activities regarding financial institutions in cooperation with prudential supervisors.

SEPBLAC is organically and functionally attached to the CPBCIM. However, a large part of the staff is provided by the Banco de España. It is worth mentioning that it is also the Financial Intelligence Unit (FIU). SEPBLAC coordinates and cooperates closely with prudential supervisors when performing its supervisory functions. The cooperation mechanisms and exchange of information between those authorities are covered by the provisions of Law No 10/2010.

Firstly, Law No 10/2010 provides that any authority or civil servant who finds out facts that may constitute an indication or evidence of ML or TF, whether during inspections carried out on the entities subject to their supervision, or in any other way, must report them to SEPBLAC.<sup>586</sup> In particular, it is stated that the Banco de España, the CNMV and the DGSFP must inform SEPBLAC when in the exercise of their supervisory tasks they uncover possible breaches of the AML/CFT obligations.

Regarding supervisory tasks, Law No 10/2010 allows prudential supervisors to perform certain supervisory tasks regarding AML/CFT with respect to the financial entities under their prudential supervision, provided that a bilateral Memorandum of Understanding (MoU) is signed between the CPBCIM and the prudential authority.<sup>587</sup>

The first MoU between the CPBCIM and the Banco de España was signed in 2005, and was updated in 2008, 2013 and March 2021.

The MoU empowers the Banco de España to exercise certain AML/CFT supervision functions. The Banco de España's powers in this area are limited to the supervision of AML/CFT obligations related to due diligence, internal control and reporting of information, with respect to those regulated entities under its supervision.<sup>588</sup> This means that, due to the MoU, both SEPBLAC and the Banco de España may carry out

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<sup>586</sup> Article 48(1) of Law No 10/2010.

<sup>587</sup> Article 44(2)(m) of Law No 10/2010.

<sup>588</sup> While SEPBLAC is in charge of the supervision of the whole catalogue of obliged entities detailed in Article 2 of Law No 10/2010 (which implements into national law Article 2 of the AML Directive), the Banco de España's tasks are limited to the financial entities subject to prudential supervision.

AML/CFT inspections of banks. However, while the Banco de España may identify AML/CFT breaches, the power to decide and impose the relevant measures lies with CPBCIM. The Banco de España may only issue non-binding recommendations to address the findings and submit proposals to the CPBCIM. Finally, if the Banco de España identifies possible suspicious transactions, the Banco de España should report them to SEPBLAC, as the FIU.

On the other hand, the MoU also governs the specificities of cooperation between SEPBLAC and the Banco de España regarding AML/CFT tasks. It covers the coordination between both institutions in their planning and in their inspection tasks, through the preparation of an annual plan of the inspections to be carried out as previously agreed in a coordinated way and whose approval lies with the CPBCIM. It also establishes a fluid exchange of information between the Banco de España, SEPBLAC and the CPBCIM (both on a regular basis and through ad hoc exchanges).

In March 2021, a new MoU was signed,<sup>589</sup> which further clarifies the role of the Banco de España and deepens supervisory cooperation and coordination between SEPBLAC and the Banco de España. The new MoU also takes into consideration the establishment of the SSM and the growing international cooperation activity. It is worth mentioning upfront that, as the ECB has no competence on AML/CFT issues, the AML/CFT supervisory tasks entrusted to the Banco de España through the MoU cover not only Less Significant Institutions, but also Significant Institutions under the direct prudential supervision of the ECB.<sup>590</sup> Obviously, this scenario increases the complexity of the necessary cooperation between the relevant authorities.

In this regard, the MoU provides that SEPBLAC and the Banco de España will share with each other in advance the information to be reported to the ECB in the context of the Multilateral Agreement signed between the ECB and the AML/CFT national authorities in January 2019.<sup>591</sup> In particular, the Banco de España will inform SEPBLAC in advance of the relevance of the information to be shared with the ECB for the performance of the ECB's supervisory tasks. Taking into account the specificities of the Spanish framework, both SEPBLAC and the Banco de España were designated as points of contact at the same level for the purpose of the Multilateral Agreement.

It is worth mentioning that a specific department was created within the Banco de España and under the umbrella of the Directorate General Supervision for carrying out the AML/CFT supervisory tasks entrusted by the MoU and for enhancing the cooperation with the SEPBLAC. In this regard, this new department serves as a

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<sup>589</sup> Decision, dated 22 March 2021, of the Directorate General of the Treasury and Financial Policy, publishing the MoU between the Banco de España and the Commission for the Prevention of Money Laundering and Monetary Offences, for the coordination of their respective roles on supervision and inspection of AML/CFT.

<sup>590</sup> The Banco de España is also the supervisor of other financial institutions subject to the AML/CFT framework, which are also covered by the MoU. However, this contribution is mainly focused on credit institutions.

<sup>591</sup> The Agreement can be found at: [https://www.sepblac.es/wp-content/uploads/2019/01/agreement\\_between\\_cas\\_and\\_the\\_ecb.pdf](https://www.sepblac.es/wp-content/uploads/2019/01/agreement_between_cas_and_the_ecb.pdf)

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contact point for the cooperation between SEPBLAC and the Banco de España in its capacity as prudential supervisor.

To sum up, when the Banco de España carries out AML/CFT inspections, it may directly issue recommendations to banks to overcome any AML/CFT deficits. This is done on the basis of inspections reports. However, if the Banco de España considers that the deficiencies imply breaches of AML/CFT regulations, it should draft a report to the CPBCIM proposing to: (i) issue a binding request; and/or to (ii) open a sanctioning procedure. In any event, the CPBCIM, based on the findings detected, may, on its own initiative, adopt any measure without a proposal from the Banco de España. SEPBLAC could equally carry out AML/CFT inspections over entities supervised by the Banco de España.

It is worth noting that if the Banco de España considers that those breaches of AML obligations have a prudential impact on the credit institutions concerned, it will be for the Banco de España or the ECB, in their capacity as prudential supervisors, to take the appropriate prudential measures regarding those credit institutions.

When it comes to the sanctioning regime for breaches of AML/CFT obligations, Law No 10/2010 provides for a broad range of sanctions that may be applied if an obliged entity fails to meet its responsibilities. The competence to impose sanctions largely rests with the CPBCIM, where the sanctioned proceedings are conducted by the Secretariat of the CPBCIM. Proposed sanctions are then considered by the CPBCIM, following which, sanctions for serious or very serious breaches will be adopted by the Minister of Economic Affairs, or the Council of Ministers, respectively.

According to Law No 10/2010, when the entity subject to sanctioning proceedings requires administrative authorisation to operate, a prior report from the competent prudential authority is required for serious or very serious breaches on the potential impact of the proposed sanctions on the stability of the institution subject to the proceedings.<sup>592</sup> Therefore, if the proceedings are carried out against a credit institution a report from the Banco de España (for less significant institution) or the ECB (for significant institutions) would be required for serious or very serious infringements.

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<sup>592</sup> Article 61(3) of Law No 10/2010.



### 3 Main legal challenges faced by the Banco de España as a prudential supervisor in the field of AML/CFT issues

#### 3.1 Potential overlapping powers between the AML/CFT authority and the Banco de España in the field of governance and internal risk control, particularly as concerns imposing binding requirements on banks

As explained above, AML/CFT risks have an impact on prudential supervision. In particular, the risks of the use of the financial system for ML or TF are relevant for prudential supervisors and are taken into consideration in the supervisory procedures related to acquisitions of qualifying holdings in supervised entities, grants and withdrawals of authorisations to credit institutions, and suitability assessments of existing or prospective managers of supervised entities, as well as in the context of the SREP.<sup>593</sup>

Therefore, it is in the interest of prudential supervisors to ensure that the institutions under their prudential supervision maintain a high degree of compliance not only with the specific regulations governing credit institutions, which they are responsible for overseeing, but also with the AML/CFT framework, insofar as such compliance may affect the risk profile and viability of institutions under their supervision.

In this regard, under the complex Spanish framework, the MoU between the CPBCIM and the Banco de España provides that the latter may supervise, along with SEPBLAC, the compliance with AML/CFT obligations related to due diligence, internal control, reporting and custody of relevant documents in relation to entities under their scope of prudential supervision. When detecting shortcomings in those obligations, the Banco de España is entitled to issue recommendations to the entities, while issuing binding requirements is within the remit of the CPBCIM, upon a proposal from SEPBLAC or the Banco de España.

Therefore, the Banco de España may determine whether certain breaches of AML/CFT legislation have taken place. Frequently, a breach of AML/CFT obligations also indicates shortcomings of a prudential nature related to the compliance function, internal control or governance arrangements. Consequently, there may be situations in which powers stemming from both frameworks could be applied (prudential and AML/CFT), at least as regards the general aspects of the internal controls of institutions.

Against this background and following the principles of respecting the scope of competence, cooperation and coordination among both institutions stemming from the MoU, when the Banco de España finds evidence of weak internal control due to AML/CFT risks, it should firstly report to SEPBLAC and the CPBCIM the facts

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<sup>593</sup> Opinion of the European Central Bank of 16 February 2022 on a proposal for a directive and a regulation on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing (CON/2022/5).

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constituting shortcomings in the area of AML/CFT. After that, the CPBCIM should assess the facts reported by the Banco de España and, if it finds it appropriate, issue the relevant request to the institution. Lastly, if the Banco de España considers that those facts also have a prudential impact not covered by the request of the AML/CFT authority, it may issue another request based on its prudential powers.

Under this approach, the Banco de España would bring its actions more strictly into line with the framework of cooperation provided for in the MoU signed with the CPBCIM.

This current practice, although complex, seems to be compatible with the stance of the General Court of the European Union in the recent court cases mentioned in the introduction.<sup>594</sup> In a nutshell, one of the main takeaways from the judgments is that whilst the determination of facts constituting breaches of AML/CFT legislation falls within the competence of the AML/CFT supervisor, the legal assessment and the proportionality of the prudential measures resulting from that breach are reserved for the prudential supervisor. The court cases endorse the prudential supervisor's competence to, on the basis of AML/CFT deficiencies, assess their prudential impact and impose the prudential measures it deems appropriate and proportionate to address the risks.

### 3.2 Allocation of the competence to withdraw the authorisation due to very serious breaches of AML/CFT obligations

In the Spanish legal framework, the withdrawal of the licence due to very serious breaches of AML/CFT obligations is only provided for as a sanction in Law No 10/2010, but not explicitly provided as a ground for withdrawal in the Spanish transposition of the CRD.<sup>595</sup>

Indeed, Article 56(1)(c) of Law No 10/2010 provides, as a sanction for serious breaches of AML/CFT obligations, the withdrawal of the administrative authorisations for those entities that require them to operate. Pursuant to Article 61(3) of Law No 10/2010 the competence to impose such a sanction is within the remit of the Council of Ministers, at the proposal of the Minister for Economic Affairs and Digital Transformation with the prior report of the supervisory authority.

In principle, this scheme is in line with the AML Directive.<sup>596</sup> Indeed, the aforementioned Article 61(3) of Law No 10/2010 implements the provisions of Article 58(2) of the AML Directive, which allows Member States to determine which national

<sup>594</sup> A thorough assessment of these court cases can be found in Giorgia Marafioti's contribution.

<sup>595</sup> It should be noted that Law No 10/2014, that transposes the CRD into the Spanish legal framework, does not include among the list of serious infringements the one provided for in Article 67(1)(o) CRD (i.e. when an institution is found liable for a serious breach of the national provisions adopted pursuant to the AML/CFT Directive). One plausible reason could be that the Spanish legislator has understood that this infringement is already provided for in Law No 10/2010.

<sup>596</sup> Directive (EU) 2015/849 of the European Parliament and of the Council of 20 May 2015 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing, amending Regulation (EU) No 648/2012 of the European Parliament and of the Council, and repealing Directive 2005/60/EC of the European Parliament and of the Council and Commission Directive 2006/70/EC.

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authority will be the NCA for AML/CFT tasks, including the imposition of the sanctions provided therein (among them, "the withdrawal or suspension of such authorisation" as provided for in Article 59(2)(c) of the AML Directive). In this regard, it should also be noted that Article 58(5)(b) of the AML Directive provides that the AML/CFT authorities may exercise their powers to impose sanctions directly or in collaboration with other authorities.

In the transposition to the Spanish framework, the AML/CFT authority (the CPBCIM) will not impose the sanction directly, but instead it will be imposed by the Council of Ministers, upon a proposal from the Minister of Economic Affairs following a report from the prudential supervisor. According to this procedure, the allocation of the competence to impose such a sanction to the Council of Ministers would be the option chosen by the Spanish legislator, within the margin of discretion provided by the AML Directive.

It is worth noting that the allocation of this competence under the Spanish legal framework departs from the prevailing standard in other SSM jurisdictions. In addition, this national regime raises doubts as regards the distribution of competences as established by the European legislator in the SSM Regulation.<sup>597</sup> Indeed, the distribution of competences within the SSM derived from Article 4(1)(a) and Article 14 of the SSM Regulation specifically states that the ECB is the competent authority to decide on the withdrawal of authorisations for credit institutions.

In this regard, the ECB maintains that it is the exclusive competent authority to authorise and withdraw the banking licence of both significant and less significant credit institutions, also in cases of withdrawal due to serious breaches of AML/CFT rules pursuant to Article 18(f)<sup>598</sup> and Article 67(1)(o)<sup>599</sup> CRD.

This interpretation of the ECB has recently been confirmed by the General Court of the European Union in two cases relating to the withdrawal of authorisation from credit institutions due to serious breaches of AML/CFT rules: *Ukrsehosprom PCF LLC and Versobank AS v European Central Bank* and *Anglo Austrian AAB Bank AG and Belegging-Maatschappij "Far-East" BV v European Central Bank*.

Moreover, it should be highlighted that in its judgment *Ukrsehosprom PCF LLC and Versobank AS v European Central Bank*, the General Court of the European Union has provided important clarifications on the delineation of responsibilities between the AML/CFT authorities and the ECB, as prudential supervisor. In particular, the General Court upheld that whilst the facts constituting breaches of the AML/CFT legislation fall within the competence of the AML/CFT supervisor, the legal assessment of whether

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<sup>597</sup> Council Regulation (EU) No 1024/2013 of 15 October 2013 entrusting the ECB with specific tasks in respect of policies relating to the prudential supervision of credit institutions.

<sup>598</sup> Article 18(f) CRD provides that "The competent authorities may only withdraw the authorisation granted to a credit institution where such a credit institution: (...) (f) commits one of the breaches referred to in Article 67(1)".

<sup>599</sup> Article 67(1) provides for the list of infringements, which includes when "an institution is found liable for a serious breach of the national provisions adopted pursuant to Directive 2005/60/EC".

those facts justified withdrawal of authorisation and the assessment of proportionality are reserved for the ECB.<sup>600</sup>

Against this background, although there has not been a withdrawal of an authorisation of credit institutions due to serious breaches of AML/CFT rules in the Spanish jurisdiction, this legal conflict could be overcome by invoking the primacy of EU law and the direct effect of EU Regulations (i.e. the SSM Regulation) over national law transposing directives.

However, in order to avoid weakening the legal basis of withdrawal decisions that by their own nature run a high risk of being challenged before the courts, the national legislator could solve this misalignment in a manner consistent with EU law as interpreted and applied by the ECB. In our view, this would require the amendment of both Law No 10/2010 and Law No 10/2014 transposing the CRD, in order to include among the list of serious infringements that may lead to the withdrawal of a banking licence, the one provided for in Article 67(1)(o) CRD.

### 3.3 Concerning the AML authority report in qualifying holding (QH) procedures and licensing procedures

As explained in the introduction, risks related to AML/CFT have to be considered in many prudential supervisory processes. Therefore, it is essential that both supervisors responsible for AML/CFT and prudential supervisors increase their information exchange and work very closely with each other, particularly in a framework where those competences are not with the same institution (i.e. as is the situation in Spain) and in the common procedures, where the final decision rests with the ECB.

With regard to QH procedures, the prudential competent authorities — in cooperation with the AML/CFT supervisor — will assess whether there are reasonable grounds to suspect that, in connection with the proposed acquisition, ML or TF is being, or has been, committed or attempted, or that the proposed acquisition could increase the risk thereof. When this is the case, the competent authority is empowered to oppose such an acquisition and adopt the relevant measures to freeze the voting rights attached to such QHs.

With regard to authorisation, in accordance with Article 10 in combination with Article 74 CRD, the prudential competent authorities must refuse to grant a licence where it is not satisfied “that the arrangements, processes and mechanisms referred to in Article 74(1) enable sound and effective risk management by that institution”. These grounds for refusal also include ML/TF risk controls, considering that: (i) as specified in the EBA Guidelines on a common assessment methodology for granting authorisation,<sup>601</sup> ML/TF risk is part of the risks to be assessed for granting the licence; and (ii) in keeping with the internal governance framework, risk management covers all risks,

<sup>600</sup> Joined cases T-351/18 and T-584/18, *Ukrseľhosprom PCF LLC and Versobank AS v European Central Bank*, para. 197.

<sup>601</sup> Available at <https://www.eba.europa.eu/regulation-and-policy/other-topics/guidelines-authorisationcredit-institutions>

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including ML/TF risk. In addition, the EBA Guidelines on authorisation make specific reference to ML/TF risk in respect of areas of the business plan analysis, internal governance, information and communication technology and cyber security risk, capital and liquidity.

Since in the Spanish framework the AML/CFT and prudential authorities are different bodies, the approach followed so far in the Banco de España, as prudential supervisor, has been to rely on the judgment of the AML/CFT authority when assessing the AML/CFT risk. To this end, prudential regulations require the AML/CFT authority's report when applying for banking licences and in QH procedures.

However, the Spanish national framework also has some distorted aspects with respect to EU law. In particular, the first additional provision of Royal Decree No 304/2014, which develops Law No 10/2010, establishes that a report from SEPBLAC is not mandatory in procedures for authorising credit institutions and in the assessment of the QH of acquisitions and increases in shareholdings: (i) when the person or entity subject to the procedure is not considered an obliged subject pursuant to the AML/CFT legislation; and (ii) in subsequent changes of the chain of intermediate entities through which a holder implements a previously authorised qualifying holding.

This provision clashes with the prudential framework governing the procedures for the authorisation and acquisition of the QHs of credit institutions, which does not waive the obligation to assess the AML/CFT risks and requires a report from SEPBLAC on this matter. It should be recalled that, these national procedures are largely a transposition of the CRD.

The Banco de España's stance has been to not replace or supplement this assessment and request such a report despite it not being mandatory under Law No 10/2010, as the competence to assess such risk lies with SEPBLAC. This misalignment is particularly relevant in the procedures relating to credit institutions, in which the ECB would be the competent prudential authority to decide on the authorisation and on the QH based on a proposal from the Banco de España. Indeed, the proposals to be submitted to the ECB should not be submitted without assessing the AML/CFT risks, and this should not be deviated from just because SEPBLAC's report is not considered mandatory, nor because the Banco de España is not entitled to replace such assessment as it lacks competence on the matter.

In view of the above and for legal certainty reasons, an amendment to the current framework repealing the exemptions on the required AML/CFT reports from SEPBLAC would be welcomed.

## 4 Upcoming EU legislative developments in the AML/CFT field

It is evident that ML/TF crimes respects no borders and cannot be fought in isolation. Weakness in one area of the single market opens up the entire single market to abuse.

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However, so far, the EU approach to AML/CFT was mainly based on a minimum harmonisation directive with a strong focus on national law and direct supervision of financial institutions by AML/CFT NCAs.

The EBA, with the European Securities and Markets Authority (ESMA) and the European Insurance and Occupational Pensions Authority (EIOPA), has been working on developing AML/CFT policy for competent authorities and financial institutions in the EU. A series of joint AML/CFT standards, guidelines and opinions have developed the way competent authorities and financial institutions should approach AML/CFT risks. In 2019, the European legislator consolidated the AML/CFT mandates of all three European supervisory authorities within the EBA. It also gave the EBA a clear legal duty<sup>602</sup> to contribute to preventing the use of the financial system for the purposes of ML/TF to lead, coordinate and monitor the AML/CFT efforts of all EU financial services providers and competent authorities.

However, more steps towards convergence and consistency on the approach followed by EU AML/CFT authorities are needed. In this regard, the AML/CFT issue has caught the attention of EU legislators.<sup>603</sup> In its Communication “Towards better implementation of the EU’s anti-money laundering and countering the financing of terrorism framework” of July 2019, the European Commission introduced the measures needed to ensure a comprehensive EU policy on AML/CFT. In line with the above Communication, on 7 May 2020 the Commission published its “Action Plan for a comprehensive Union policy on the prevention of money laundering and terrorist financing”, where it sets out its point of view on a future AML/CFT framework that promotes the integrity of the EU financial system. The Commission’s Action Plan is built on six pillars: (i) effective implementation of existing rules; (ii) a single EU rulebook; (iii) an EU-level supervision; (iv) a support and cooperation mechanism for FIUs; (v) enforcing use of information to enforce criminal law; (vi) strengthening the international dimension of the EU AML/CFT framework.

From a legal point of view, the proposal of an AML/CFT legislative package is of interest. This package is currently being discussed by the European Parliament and the Council, and it will include, among others, the following legal initiatives:

1. **Regulation establishing a new EU authority (the “AMLA”):** This proposal provides for the creation of a new EU authority that will change AML/CFT supervision in the EU and enhance cooperation among FIUs. The AMLA will become the centrepiece of an integrated AML/CFT supervisory system, consisting of the AMLA itself and the national authorities with an AML/CFT

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<sup>602</sup> In particular, the EBA carries out its task by: (i) leading the development of AML/CFT policy and supporting its effective implementation by competent authorities and financial institutions across the EU to foster an effective risk-based approach to AML/CFT with consistent outcomes; (ii) coordinating across the EU and beyond by fostering effective cooperation and information exchange between all relevant authorities in a way that supports the development of a common understanding of ML/TF risks, strengthens risk-based AML/CFT supervision, ensures that emerging risks are dealt with promptly across the single market and ensures effective oversight of cross border financial institutions; and (iii) monitoring the implementation of EU AML/CFT policies and standards to identify vulnerabilities in competent authorities’ approaches to AML/CFT supervision and to take steps to mitigate them before ML/TF risks materialise.

<sup>603</sup> Communication from the Commission on an Action Plan for a comprehensive Union policy on preventing money laundering and terrorist financing 2020/C 164/06 (C/2020/2800).

supervisory mandate. This system is aimed to ensure the private sector correctly and consistently applies EU rules.

2. The current powers and tasks of the EBA in the AML/CFT area will be transferred to this new authority, which is supposed to be established in 2023. The AMLA will exercise direct supervision over financial institutions that operate in a significant number of Member States and/or have high risk profiles. Irrespective of such criteria, AMLA may take over supervision of an individual financial entity in the event of relevant AML/CFT concerns.
3. **Regulation on AML/CFT with directly applicable rules:** the new regulation seeks to harmonise certain AML/CTF rules at EU level. This is to be achieved by replacing those sections of the national AML/CFT laws that relate to customer due diligence, obliged entities and beneficial owners with a set of directly binding rules on all the Member States. It also includes an EU-wide €10,000 limit on cash payments.
4. **New AMLD 6:** this directive will replace AML Directive currently in force, which contains provisions that will be included in national legislation, such as rules on cooperation between national supervisors and financial intelligence units in the Member States. The new directive will also update the rules on common registries such as the beneficial owner registry.

## 5 Main conclusions and some reflections

Concerning the Spanish allocation of AML/CFT tasks, centralising in only one national authority all AML/CFT tasks (namely the FIU and the supervision of all AML obliged entities) may have some advantages, such as that of providing consistent domestic supervision.

However, this framework increases complexity and hinders coordination between the relevant authorities. Moreover, it has become more and more apparent that there is a close link between AML/CFT obligations imposed on financial institutions and prudential risks.

Bearing this in mind, allocating the competences of supervision of AML/CFT obligations related to internal controls and governance to prudential supervisors would allow advantage to be taken of the proven synergies that exist between AML/CFT and prudential supervision, thereby also contributing to institutional efficiency. This proposal would not only reduce the coordination and cooperation issues described in the main legal challenges but would align the Spanish framework with the predominant institutional architecture that is in place in nearly all EU countries.

Nevertheless, the recent court cases will also help to enlighten the blurred delineation of competences between AML/CFT and prudential authorities. In particular, they endorse the approach that the relevant prudential supervisor must rely on the facts as investigated by the AML/CFT authorities, while drawing prudential conclusions from

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these facts would, however, be a competence of the prudential supervisor. Indeed, the competence for investigating AML/CFT breaches, and determining whether a breach has occurred lies solely with the AML/CFT authority, as part of its fact-finding competences. The AML/CFT authority may also use its own powers to respond to its findings, for example by imposing a fine. Once such breaches have been established by the AML/CFT authority, the prudential supervisor may take these established facts as given and use its powers. Any measures adopted by the prudential supervisor should, however, always be applied from a prudential perspective and not from a crime avoidance perspective.

Leaving aside the particularities of the Spanish framework, from a wider perspective, the upcoming legislative changes based on the European Commission's Action Plan will increase harmonisation. Indeed, with clear regulatory guidance and stronger supervisory powers, further legislative harmonisation will address current EU Member State divergences and strengthen enforcement of AML/CFT compliance. In addition, the future AMLA will establish an integrated system of AML/CFT supervision across the EU, based on common supervisory methods and convergence of high supervisory standards, leading to a common approach within the EU to fighting ML and TF.

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# Concluding remarks

By Chiara Zilioli\*

The main themes of the 2022 ECB Legal Conference and of this book are on the one hand the legal developments in response to the pandemic, and on the other hand, the practical application by the ECB of the rule of law. The first theme, i.e. the legal developments in response to the pandemic, were analysed through the lenses of, first, the evolution of legal practice with the use of visualisation and legal design, second, the potential conduct of monetary policy operations with non-banks, and third, the development of central bank digital currencies. The second theme, i.e. the practical application by the ECB of the rule of law was considered by virtue of, first, the procurement framework, second, the data protection framework and, finally, the tension between the ECB's duty to carefully and impartially examine all elements when assessing AML-CFT aspects relevant to the performance of its supervisory tasks and the duty of other competent authorities to assist the ECB in fulfilling those tasks.

## 1 Overview of the contributors

The first part of this book deals with **“Visualisation and legal design thinking: the steady transformation of legal practice”**. **Frédéric Allemand** illustrated how legal design has effectively improved his work and its relevance to legal research. He emphasised that while the visualisation of legal data and legal knowledge is becoming more and more important in the provision of legal services, they have not yet been adequately used by legal scholars and have not been satisfactorily examined in the field of legal research. Frédéric then took EUR-Lex as an example and concluded that, while the database is complete, its visualisation tools could be improved to better address the needs of legal scholars.

**Filip Lulić** explained that legal knowledge visualisation combines legal expertise with data science and statistics and aims at analysing and visually displaying legal knowledge by the use of various tools. He noted that information overload affects the legal profession because on the one hand legal documents are very complex and text-heavy, and on the other, end users have a limited attention span; therefore information overload threatens the objectives of mitigating risks and maintaining legal certainty. Legal design and knowledge visualisation can counteract the negative consequences of information overload by lowering the cognitive effort needed to process the information contained in legal documents.

**Marie Potel-Saville**, whose contribution is unfortunately not included in this book, analysed during the conference how legal design can strengthen the rule of law by

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explaining that the lack of readability or usability of legal documents can threaten their application. Marie focused on the role of neuroscience in legal design, an approach that follows a methodology based on user centricity. She noted that information overload causes stress to the human brain and distorts its learning ability. By designing information within our cognitive limits, legal design can bridge the gap between law and its users. In doing so, legal design can lead to greater efficiency, user empowerment, better decision-making, better access to justice, and can have a systemic impact.

The second part of the book focuses on “**Monetary policy operations with non-banks: legal, financial and comparative aspects**”. **Imène Rahmouni-Rousseau** explained that in the last decade the role of non-banks in the financial markets has increased, as has their importance for the transmission of monetary policy. Imène considered whether and in which manner non-banks could be given direct access to the central bank balance sheet and concluded that arguments can be made for access to both the asset and the liability sides of the balance sheet of central banks. However, she noted that it is important to consider whether such access is necessary and proportionate, to examine whether the legal framework allows for such access to be granted and to ensure that such access has a sound monetary policy justification.

**Kerstin Schaepersmann** analysed the extent to which existing legal framework permits non-banks to participate in monetary policy operations, focusing her analysis on the perspective of money market funds (MMFs), a sub-group of non-banks which were particularly affected by the global financial crisis and the one induced by the COVID-19 pandemic. She pointed out that there are limitations that need to be overcome not only in the monetary policy framework, as this framework is addressed almost exclusively to banks, but also in the MMF-specific legislation which, to enable MMFs to take part in Eurosystem monetary policy operations, should be clarified for the sake of legal certainty.

**Marco Cipriani** provided an overview of the way in which the New York Federal Reserve System set-up a dedicated facility for non-banks. He focused on the application of the Overnight Reverse Repo Facility (ON RRP), which allows eligible institutions to lend to the Federal Reserve while receiving US treasuries. In this respect he explained how the ON RRP allows the Federal Reserve to maintain control over short-term money market rates and how allowing a large range of institutions to hold liabilities with the Federal Reserve alleviates pressure from banks when the Federal Reserve expands its balance sheet.

The third part of the book deals with the topic of “**Legal interoperability of retail central bank digital currencies**”. **Ross Leckow**, who unfortunately could not contribute to this book, presented during the conference the concept of cross-border interoperability of central bank digital currencies (CBDCs) from an international perspective. He explained that an international legal framework has been developed that governs the treatment of payments and transfers and that the principles underlying this framework provide useful guidance on how payments and transfers with CBDC should be regulated. Ross drew attention to the principle of “do no harm”, explaining that the introduction of CBDC must not prejudice important public policy

objectives, such as the conduct of monetary policy or financial stability. He then explained how cross-border interoperability can be achieved under different CBDC models and concluded that while the cross-border use of CBDCs is still under development, interoperability is an important element that needs to be accompanied by legal and technical improvements.

**Jess Cheng** provided an overview of the concept of legal interoperability in the US payment system. She noted that although different legal bases underpin different arrangements, US payment law provides the certainty and predictability that "one dollar" has a singular meaning in whatever form it takes. She also touched upon the complementary roles of the public and private sector in the issuance of central bank and commercial bank money respectively and discussed how new forms of money (for example stable coins or CBDCs) can interoperate with existing forms of money. Jess finally noted that the legal characterisation of a CBDC, particularly if it is a *sui generis* asset, has important implications and that a critical consideration remains to be executed on how CBDC can be integrated in the existing payment system.

**Panagiotis Papapaschalis** then addressed the issues of cross-currency interoperability from an EU law point of view. He noted that while interoperability is mainly a technical concept, it has found its way into EU law. Panagiotis examined elements of legal design of cross-currency interoperability, which could include introducing a single, global point of issue for all retail CBDCs (taking T2S as a precedent), using a central node (as in the case of CLS) or establishing bilateral arrangements between retail CBDC-issuing central banks. Noting that there is no general obligation in the legal framework to make different currencies interoperable, he addressed the potential legal impediments to an efficient cross-currency interoperability, such as differences in the governance and design of CBDCs and conflicting legal and regulatory requirements.

Lastly, **Seraina Gruenewald** provided some high-level take-aways on the topic of legal interoperability. She explained that interoperability is important from a domestic and from an international perspective and elaborated on the measures that need to be put in place in order to achieve interoperability of the digital euro. Accordingly, these could include the adoption of a technical rulebook establishing a governance structure and uniform standards, which in her view falls largely within the ECB's competence on the basis of Article 128(1) TFEU, as well as amendments in the key areas of EU law, such as in the prudential regime for intermediaries and digital euro payment service providers and the settlement finality and collateral. Seraina concluded by discussing the importance of understanding potential obstacles that may arise for the interoperability of the digital euro due to Member State's diverging civil law regimes and private law traditions, stressing the need for harmonisation at EU level.

The fourth part of this book concerns the comparison of the **"ECB's internal review procedure for contract award decisions with other similar procedures in other EU bodies and international and national organisations"**. **Isabel Koepfer** presented the ECB's internal review procedure for contract award decisions. Isabel explained that while the ECB is not subject to national procurement laws, it is bound by the EU Treaties and the principles of procurement established by the relevant case-law, such as the principles of equal treatment, proportionality and transparency,

as well as by its own framework in the area of procurement. She then described the possible remedies that are available to tenderers, with particular focus on the Procurement Review Body of the ECB, the effectiveness of which has been acknowledged by the General Court of the Court of Justice of the European Union (CJEU) and the European Court of Auditors.

Although she could not provide her written contribution for this book, in the course of the conference **Laura André** focused on the communication between the tenderers and the contracting authority after the issuance of an award decision as foreseen in Regulation (EU, Euratom) 2018/1046 (the “Financial Regulation”). She pointed to the recommendation made by the CJEU that contracting authorities should proactively provide all tenderers with the information needed to understand the reasoning of the award decision. The communication with tenderers and duty to state reasons are important to fulfil the right to an effective remedy and the principle of transparency, especially due to the broad margin of appreciation of contracting authorities. Laura concluded by drawing attention to the standstill period, which is a feature of the procedure that allows the tenderer the opportunity to, inter alia, raise objections, request information and file an application with the Court provided that serious harm can be demonstrated. All these features are key for the application in practice of the principle of transparency, the right to an effective remedy and the principle of good administration, which support the rule of law.

**Jeff Dirix** examined the matter of internal review from a national law perspective, and in particular from the Belgian procurement law standpoint. He noted that in Belgium the contracting authority immediately and proactively shares information with tenderers with the aim of enabling them to understand the outcome of the decision of the authority, even when it decides not to award a contract. He then described the legal remedies which are available under Belgian law, with special focus on pre-contractual external remedies, which avoid unnecessary litigation with tenderers.

The fifth part of this book concerns the “**General Data Protection Regulation and its relevance for banking supervision**”. **Karolina Mojzesowicz** kicked off the discussion by describing the EU legal framework on data protection. In particular, she provided an historical background to the adoption of Regulation (EU) 2016/679 (General Data Protection Regulation (GDPR)), which was necessitated by an exponential growth in the generation of personal data and explained its interaction with Regulation (EU) 2018/1725 (EUDPR) which concerns the processing of personal data by the Union institutions, bodies, offices and agencies. In her presentation, Karolina highlighted that the legal framework applies only to personal data. Accordingly, if data are truly and irreversibly anonymised the relevant data protection rules cease to be applicable. Finally, she provided an overview of the range of rights afforded by the legal framework to the data subjects and the corresponding obligations of controllers. Karolina’s contribution is not included in this book.

Building on the previous presentation, **Sandrine Letocart** investigated how the rights of data subjects interact with the duty of professional secrecy imposed by EU law on supervisory authorities. This duty aims to protect not only the private interests of banks but also pursues an objective of general public interest. Sandrine clarified that, in the exercise of their tasks, supervisors will receive personal data. She considered whether

there are frictions between the duty of professional secrecy and the rights of data subjects to access information and to be informed and explored how such conflicts, if any, can be resolved.

**Maarten Daman** focused on the fact that transparency and professional secrecy are not mutually exclusive but complementary objectives. He noted that while the right to data protection is a fundamental right of the EU, it is not an absolute one, and as such it is subject to limitations. These exceptions and restrictions can be used to reconcile the obligation to protect personal data with the tasks in the field of banking supervision. In addition, data subjects enjoy a wide range of rights, and the corresponding obligations of the controllers must be interpreted in the light of fairness and proportionality. Maarten also noted that the divergences in the GDPR and EUDPR in the restriction of the rights of data subjects can lead to a differential treatment of individuals and concluded by explaining the role of Data Protection Officers (DPOs) in ensuring compliance with the GDPR and EUDPR.

In the sixth part of the book, on the **“NCAs’ duty of assistance and the ECB’s duty of diligence when assessing anti-money laundering and countering the financing of terrorism (AML-CFT) aspects relevant for the ECB’s supervisory tasks”**, **Audrone Steiblyte** sets the scene by explaining that the ECB exercises exclusive powers in the area of prudential supervision which are implemented in a decentralised manner through the assistance provided by national competent authorities (NCAs). At the same time, the powers that were not conferred on the ECB remain vested in the NCAs. AML and CFT-related supervisory tasks and the enforcement of the relevant legislation are not among the competences conferred on the ECB. The assisting role of the NCAs is thus particularly important in cases where there are points of contact between AML/CFT supervision and ECB competences, for example in cases of withdrawal of authorisations due to AML/CFT concerns. While the framework foresees cooperation between the ECB and NCAs, the ECB has exclusive competence to withdraw the authorisation on grounds related to AML/CFT. This has also been confirmed by the General Court in the judgements in the *Versobank* and *AAB* cases. Given the importance of the AML/CFT policy in the EU, Audrone draws attention to the Commission’s proposal on the reform of CRD VI which aims at further strengthening the synergies between AML/CFT monitoring and prudential supervision.

**Giorgia Marafioti** considers that in the light of the close connection between AML/CFT supervision and prudential supervision, the ECB integrates AML/CFT concerns when performing its supervisory tasks. The boundaries to the ECB’s powers stemming from the allocation of competences under the SSM Regulation raise relevant questions concerning the scope of the ECB’s duty of diligence whenever AML/CFT aspects become relevant for the adoption of a supervisory decision. Giorgia explained that the ECB must respect the balance between the principle of conferral and the principle of good administration, and in particular the duty of diligence. A concrete example of the scope of the ECB’s duty of diligence can be found in licence withdrawal procedures based on serious breaches of AML/CFT provisions. Even when the ECB relies on findings established by another authority, which retains competence in a certain field, the duty of care principle still requires it to conduct a

diligent and impartial examination of those findings. On the basis of the case-law and in particular recent cases in the field of banking supervision, Giorgia explores the ECB's duty of care whenever AML/CFT aspects become relevant for the adoption of a supervisory decision, building upon the two dimensions of the "due care" requirement. While the General Court has provided important clarifications that are relevant for the adoption of withdrawal decisions, questions concerning other supervisory powers remain open.

Last but not least, [Rafael Martín Lozano](#) presented the legal challenges in the consideration of AML/CFT risks in the performance of prudential supervision, focusing on the NCA's point of view. He explained that AML/CFT risks have a prudential impact at each stage of a bank's life cycle and expressed the view that the transfer of prudential supervisory powers to the ECB introduced an additional institutional layer for cooperation and coordination between domestic AML/CFT supervisors and prudential authorities. This complexity may be more acute in certain legal frameworks, such as the Spanish one, in which the national AML/CFT authority is different from the prudential supervisor. Rafael stressed that it is essential that supervisors responsible for AML/CFT and prudential supervisors increase information exchange and work very closely with each other and that it is necessary, for the sake of reducing legal risks, to delineate the competences of AML/CFT supervisors and prudential supervisors, including the ECB. Finally, he noted that the current approach in the area of AML/CFT has been based on a minimum harmonisation directive with a strong focus on national law and that the EU legislator is now taking steps towards greater convergence and consistency in the application of the AML/CFT framework.

## 2 Some acknowledgements

The 2022 ECB Legal Conference would not have been possible without our panellists and contributors, who generously contributed their expertise in lively discussions.

Sincere thanks are due to Antonio Riso, who organised this year's Conference. Antonio has worked very hard to put this programme together; during the preparation stage, to maintain the contacts with speakers and chairs, and in the course of the conference, to make sure that everything was running smoothly. Antonio was supported in the preparation of the Conference by two colleagues in the Legal Services Section – Tončica Radovčić and Monica Bermudez Leyva. They always go the extra mile to ensure the smooth and efficient running of these events.

Last but not least, I would also like to thank the many other colleagues in Legal Services and in technical support, who ensured the conference ran well, and in particular Javed Ghafoor, our colleague from the IT team who helped us solve many technical challenges with the WebEx event these two days.

The ECB Legal Conference 2022 included on average 200 participants with peaks at 250 and around 588 visualisations. It has been a rich debate and I hope it will contribute to the development of ideas, exchanges, and studies on the legal topics that were discussed in the course of the Conference.





# Programme

## Monday, 5 September 2022

10:30 Online registration opens

11:00 **Welcome address and opening of the Conference**

Chiara Zilioli, Director General Legal Services, European Central Bank

11:30 **Panel 1**

**Visualisation and legal design thinking: the steady transformation of legal practice**

Society continues to evolve in its relationship to information. In the face of developments such as pervasive competition for our attention, changing ways in which citizens access information and law students are taught and learn, and digitalisation of legal transactions, there is an opportunity and a need for lawyers to understand and adopt new approaches to the practice of the law. It is a fact that visualisation and design thinking have become widely accepted approaches to help innovate, analyse, collaborate and persuade. Legal professionals may be late adopters but they have recognised the opportunity, even though more exploration is still needed. Lawyers can exploit these developments for multiple purposes: to design better legal frameworks; to deal innovatively with their clients' most complex problems; to prepare and conduct litigation; and to share knowledge and good practices. The panel will consider the historical perspective (the law beyond words); the user's perspective (human-centred legal design); and the client orientation perspective. The legal departments of the European Central Bank and of the national central banks and national competent authorities can benefit from exploring these new trends and perhaps find in them inspiration to make better use of the collective legal intelligence that they promote.

**Chair**

Hilde Hardeman, Director General, Publication Office of the European Union

**Panellists**

Filip Lulić, Legal Analyst, Legal Services, European Central Bank

Frédéric Allemand, Manager of the RESuME project, Faculty of Law, Economics and Finance, University of Luxembourg

Marie Potel-Saville, Founder & CEO, Amurabi SAS

Discussion with questions from the audience

13:00 End of Panel 1

Lunch break

15:00

**Panel 2**

**Monetary policy operations with non-banks: legal, financial and comparative aspects**

The recent crisis has further highlighted the importance of non-bank intermediation and the increasing role that non-banks play in the transmission of monetary policy impulses. The panel will discuss the legal, economic and financial stability aspects of granting access for non-banks to monetary policy operations both on the asset and the liability side of the Eurosystem central banks' balance sheets. The discussion will benefit from the experience of the New York Federal Reserve in setting up and implementing its Overnight Reverse Repo Facility (ON RRP).

**Chair**

György Várhelvi, Lead Legal Counsel, Legal Services, European Central Bank

**Panellists**

Imène Rahmouni-Rousseau, Director General Market Operations, European Central Bank

Kerstin Schaeppersmann, Counsel, Clifford Chance

Marco Cipriani, Head of Money and Payments Studies, Federal Reserve Bank of New York

Discussion with questions from the audience

15:45

End of Panel 2

16:00

**Panel 3**

**Towards legal interoperability of retail central bank digital currencies: a comparative law perspective**

In the context of central bank digital currencies (CBDCs), interoperability is an important technical functionality that merits consideration from the legal perspective. The panel will discuss interoperability largely in the retail CBDC context and, based on lessons from the past, will attempt to provide conjectures about the future. The discussion will cover both the domestic context (exchangeability between CBDCs and cash; interoperability between intermediaries' platforms) and the international context (exchangeability between CBDCs and cash; interoperability between CBDCs). The panel will also touch upon the different civil law treatment of the two CBDC systems (account based/claim and token-based/quasi in rem) as well as the ramifications of that treatment for legal interoperability.

**Chair**

Otto Heinz, Head of Division, Legal Services, European Central Bank

**Panellists:**

Panagiotis Papapaschalis, Senior Lead Legal Counsel, Legal Services, European Central Bank

Ross Leckow, Acting Head of BIS Innovation Hub - Strategy and Legal at Bank for International Settlements, BIS

Jess Cheng, Senior Counsel, Federal Reserve Board

Seraina Gruenewald, Professor European and Comparative Financial Law, Radboud University

17:30

Discussion with questions from the audience

End of Conference Day 1

## Tuesday, 6 September 2022

08:30 Online registration opens

### Welcome address – Day 2

Chiara Zilioli, Director General Legal Services, European Central Bank

09:00 Panel 4

### Comparison of the ECB's internal review procedure for contract award decisions with the legal framework for the review of such decisions in other EU, international and national organisations

The discussion will compare the ECB's internal review procedure for contract award decisions (i.e. the Procurement Review Body) with the legal framework for the review of such decisions in other EU, international and national organisations. It will include a stocktaking after 15 years of decisions of the PRB; an assessment of the impact of recent case law on review procedures and the requirements for obtaining interim relief from the Court of Justice of the European Union; as well as practical problems that arise, for example in terms of the language regime.

#### Chair

Martin Benisch, Head of Section, Legal Services, European Central Bank

#### Panellists:

Isabell Koepfer, Adviser, Legal Services, European Central Bank

Jeff Dirix, Senior Advisor, Head of Group, Legal Department, Nationale Bank van België / Banque Nationale de Belgique

Laura Andre, Member of the Legal Service, European Commission

Discussion with questions from the audience

10:30 End of Panel 4

Coffee break

11:00 Panel 5

### The General Data Protection Regulation and its relevance for banking supervision

Data protection is a current topic and the implications of the General Data Protection Regulation (GDPR) and the EU Data Protection Regulation (EUDPR) still require elucidation for banking supervisors and banking supervision. To this end, the panel will explore the obligations under the GDPR and EUDPR and how they interact with professional secrecy obligations, and will also discuss issues that have arisen in the day-to-day work of supervisors as regards the application of the data protection legislation. These include, among others, personal data access requests by managers of credit institutions, potential conflicts between such requests and professional secrecy obligations, and the handling of unauthorised disclosure of personal data.

#### Chair

Klaus Lackhoff, Head of Section, Legal Services, European Central Bank

#### Panellists

Maarten Daman, Data Protection Officer, European Central Bank

Sandrine Letocart, Principal Legal Counsel, Legal Services, European Central Bank

Karolina Moizesowicz, Deputy Head of Unit, Directorate General Justice and Consumers, European Commission

Discussion with questions from the audience

12:30 End of Panel 5

Lunch

14:30 Panel 6

**The NCAs' duty of assistance and the ECB's duty of diligence when assessing AML-CFT aspects relevant for the ECB's supervisory tasks**

Article 6(3) of the SSM Regulation provides for the general responsibility of national competent authorities (NCAs) to assist the ECB in relation to the tasks conferred on it by the SSM Regulation. The assistance provided by NCAs is particularly important in the field of common procedures, especially regarding less significant credit institutions, as well as the assessment of aspects related to anti-money laundering/combating the financing of terrorism (AML-CFT), as the prevention of the use of the financial system for the purposes of money laundering is not within the SSM remit. The judgement of the General Court of 6 October 2021 in joined cases T-351/18 and T-584/18 (*Ukrseľhosprom PCF LLC and Versobank AS v European Central Bank*) provides important clarifications on the division of powers between the ECB and NCAs regarding the withdrawal of authorisations for the infringement of AML-CFT requirements. The panel will discuss the scope of the ECB's powers to assess matters related to AML-CFT requirements, as well as how the ECB ensures compliance with the duty of diligence when relying on assessments made by NCAs or competent authorities on AML-CFT related matters, and the practical difficulties that the ECB may encounter when implementing this approach.

**Chair**

Carmen Hernandez, Head of Section, Legal Services, European Central Bank

**Panellists**

Giorgia Marafioti, Senior Legal Counsel, Legal Services, European Central Bank

Rafael Martín Lozano, Legal Counsel, Legal Department, Banco de España

Audrone Steibyte, Member of Legal Service, European Commission

Discussion with questions from the audience

16:00 End of Panel 6

16:15 **Concluding remarks and closing of the Conference**

Chiara Zilioli, Director General Legal Services, European Central Bank

16:30 End of the ESCB Legal Conference 2022

# Biographies

## 1 Frédéric Allemand

Frédéric Allemand is a researcher in law at the Faculty of Law, Economics and Finance of the University of Luxembourg, and an associate researcher at the Polytechnic University of Valenciennes. He lectures on European economic law, public finance and EU legislative procedures at Sciences Po Paris, Sciences Po Rennes, the Institut national du service public, and the University of Lille.

Before joining the University of Luxembourg, Mr Allemand spent five years as a researcher then as coordinator of the European Integration Studies Department at the Centre Virtuel de la Connaissance sur l'Europe – a Luxembourg-based public research centre. He also worked in the ECB's legal department, in the French Secretariat-General for European Affairs, in the French Senate and for several European and French think tanks.

Mr Allemand is a graduate of Sciences Po Paris and also holds a PhD in public law. He specialises in EU law and economic governance law. He has authored more than seventy scholarly publications, mainly on the Economic and Monetary Union. Since 2017 he is editor-in-chief of the *Revue de l'euro*, an interdisciplinary open access journal on Economic and Monetary Union.



## 2 Martin Benisch

Since May 2022, Martin Benisch is acting Head of the Legislation Division (LEG) and, since 2015, Head of the Banknotes Procurement and Accounting Law Section (BPAL).

- LEG is in charge of all translations and revision of ECB and banking supervision (SSM) legal acts. It consists of a team of Lawyer-Linguists that cover all 24 official languages of the European Union.
- BPAL covers institutional law issues related to contract and procurement, banknotes, accounting and audit, privileges and immunities, tax law and intellectual property rights. Martin has also worked in the Legal Department of the Deutsche Bundesbank.

In 1994, he joined the predecessor of the ECB, the European Monetary Institute and became ECB staff from the outset in 1998. Martin has the First and Second State Exam (Universität Bayreuth, OLG Bamberg) and an LL.M. from the Vrije Universiteit Brussel on international and comparative law.





### 3

## Jess Cheng

Jess Cheng is a partner in Wilson Sonsini Goodrich & Rosati's New York office. She was formerly senior counsel at the Federal Reserve Board of Governors, where she specialised in a broad spectrum of payment system issues, including policy analysis of digital assets, stablecoins, and central bank digital currencies and oversight of the Federal Reserve's payment services, including the FedNow Service. Prior to that, she was counsel at the International Monetary Fund, where she advised on the strategic direction of the Fund's fintech work agenda and provided technical assistance to advance law reform in central bank legislation. Previously, she was deputy general counsel at Ripple (a San Francisco-based fintech company specialising in distributed ledger technology-based cross-border payment solutions), counsel and officer at the Federal Reserve Bank of New York, and an associate at the New York law firm Wachtell, Lipton, Rosen & Katz. She holds a BA in economics from Yale University and a JD from Columbia Law School. She currently serves as the Vice Chair of the American Bar Association Business Law Section's Uniform Commercial Code Committee.



## 4 Marco Cipriani

Marco Cipriani is the head of the Money and Payments Studies Department of the Federal Reserve Bank of New York Research Group. His research interests include experimental finance, financial markets microstructure, non-bank financial institutions, and social learning in financial markets.

Before joining the Federal Reserve Bank of New York, Marco was a senior economist at the International Monetary Fund and an Associate Professor of Economics at George Washington University. Marco holds a Ph.D. from New York University.



## 5 Maarten Daman

Maarten Daman has been Data Protection Officer (DPO) of the European Central Bank (ECB) and the European Systemic Risk Board (ESRB) since September 2020. Before joining the ECB in 2016, he worked for the International Court of Justice, the principle judicial organ of the United Nations, the European Police Office (EUROPOL) and as genocide researcher in Rwanda.

Maarten has lectured at the University of Copenhagen and is a reservist Legal Advisor of the Belgian Armed Forces.

Maarten holds a LL.M. in international public law (cum laude) from the University of Edinburgh and a master's in law (magna cum laude) from the University of Antwerp.



## 6

### Jeff Dirix

Jeff Dirix works as a senior legal counsel and head of the Corporate Law Division in the Legal Department of the National Bank of Belgium (NBB). He joined the NBB in 2011, immediately after finishing his law studies at the university of Leuven (KU Leuven). In 2017, Jeff was seconded to the ECB on a short-term basis where he worked for the Institutional Law Division of the Directorate General Legal Services.

Jeff has experience in various areas of law, in particular institutional law, corporate governance, accounting law, fiscal law, public access law and public procurement law.

Within the Eurosystem, Jeff is member of the LEGCO Task Force on VAT issues and of the Ethics and Compliance Conference.

Besides his job as legal counsel of the NBB, Jeff is active as a musician (pianist and conductor). Among other musical activities, he is the conductor and cofounder of The Bank Notes, a choir of NBB staff members.



## 7

### Seraina Grünewald

Seraina Grünewald is full professor and holds the Chair for European and Comparative Financial Law at Radboud University Nijmegen in the Netherlands. She is a member of the Academic Board of the European Banking Institute (EBI), a member of the Sustainable Finance Lab in the Netherlands and affiliated as an academic fellow with the interdisciplinary University Research Priority Programme Financial Market Regulation at the University of Zurich.

She is a well-known expert in the field of financial and monetary law, with a focus on central banking, bank resolution, banking union and sustainable finance, and is frequently invited to present at international and European authorities, including at the IMF, the ECB, the European Stability Mechanism and the Single Resolution Board.

Her research has benefited from the ECB Legal Research Programme as well as scholarships from the Swiss National Science Foundation and the Swiss-American Society. In 2020, she co-authored a comprehensive study on the legal foundations of the digital euro.



## 8 Hilde Hardeman

Hilde Hardeman is Director-General of the Publications Office of the EU as of 1 December 2021. Prior to that, she served as Head of the European Commission's Service for Foreign Policy Instruments. She joined the Commission in 1994 and, since then, she

- held the position of Deputy Head of Cabinet to the Commission's Vice-President for Jobs, Growth, Investment and Competitiveness;
- headed the Commission President's briefing team;
- and was in charge of the units for relations with Russia, Ukraine, Moldova and Belarus.

Hilde Hardeman holds a PhD in Slavic philology and history from the University of Leuven, which she obtained after studies at Leuven, Stanford University and the École des hautes études en sciences sociales in Paris. She was visiting professor at the College of Europe.



## 9

### Carmen Hernandez

Carmen Hernández Saseta works as Head of Section at the Supervisory Law Division of the Directorate General Legal Services of the European Central Bank. She joined the ECB in 2013 from Bank of Spain to assist in the preparatory phase and implementation of the Single Supervisory Mechanism.

Prior to working at the legal departments of the ECB and Bank of Spain she developed a career in the private sector, practising as a lawyer in the fields of EU and competition law at one of the leading firms in Spain.



## Isabell Koepfer

Isabell Koepfer is currently an Adviser in the Banknotes, Procurement and Accounting Section within the ECB's Institutional Law Division. Isabell joined the ECB in 2007 and has 20 years' work experience in contract and procurement law. She has previously worked for GIZ (Gesellschaft für internationale Zusammenarbeit), a German government owned organisation in the field of international cooperation for sustainable development and at the international law firm Allen & Overy LLP.

Isabell studied at the University Nanterre (Paris), the University of London (SOAS) and Wolfgang-Goethe University Frankfurt am Main. She has a postgraduate in EU law from the University of London and obtained a PhD in environmental law from the Wolfgang-Goethe University Frankfurt am Main.





## Klaus Lackhoff

Klaus Lackhoff has been Head of Section in the Supervisory Law Division of the ECB's Directorate General Legal Services since June 2015. His section deals in particular with issues related to the Capital Requirements Regulation.

Before joining the ECB in 2015, he worked for more than 15 years at an international law firm. He advised on a broad range of financing transactions and on banking supervisory issues and was involved in the ECB's preparations for its supervisory tasks in the Single Supervisory Mechanism (SSM) and the drafting of the SSM Framework Regulation.

Klaus has earned a Doctor juris from the University of Münster, with a thesis on the freedom of establishment, an LLM from the University of Iowa, with a paper titled "Restrictions on State Interference with Commerce in the U.S.A. and the EC", and a master's degree in European law from the University of Saarbrücken.



## 12 Sandrine Letocart

Sandrine Letocart is Principal Legal Counsel in the ECB's Supervisory Law Division. She has worked at the ECB since 2005 in various roles, notably in the Legislation Division, as Secretary to the Legal Committee and was seconded to the ESCB International and Coordination Unit of the National Bank of Belgium.

Sandrine held academic positions of teaching assistant at the Université Libre de Bruxelles (Company Law) and at Sorbonne University Abu Dhabi (European law, Company Law). She started her professional life at the Brussels Bar, working in one of the largest independent law firms in Belgium providing legal advice in various fields of business law.

Sandrine has a master's degrees in law and in business law from the Université Libre de Bruxelles and a holds a degree in European Law from the Universiteit van Amsterdam.



## Filip Lulić

Filip Lulić is currently a part of the Legal Knowledge Management Team of the ECB's Directorate General Legal Services. There he mainly works on the department's digitalisation agenda, bridging the gap between law and IT in projects like developing knowledge hubs, legal taxonomies, automated workflows and legislative databases.

Filip Lulić holds a Master of Laws degree from University of Rijeka, Croatia. After working for several companies in the private sector, he moved to Frankfurt to join Legal Services of the European Central Bank. Over the years, he specialised in managing legal tech and AI projects.

Filip is a keen practitioner of legal design thinking and knowledge visualisation techniques, and also publishes articles in the domain, speaks at conferences, and shares his know-how in a community of practice he facilitates.



## Giorgia Marafioti

Giorgia Marafioti is Senior Legal Counsel in the Supervisory Law Division of the ECB's Directorate General Legal Services. Since 2017, she has been providing legal advice to the ECB's banking supervision arm and representing the ECB before the CJEU in various cases relating to banking supervision. Prior to joining the ECB, she spent four years in the Banking Supervision Department of Banca d'Italia.

Ms Marafioti started her career in an international law firm, where she focused on corporate and banking law issues and international arbitration. She graduated from the Luiss University in Rome and she is admitted to practice in Italy.



## 15 Rafael Martín Lozano

Rafael Martín Lozano is a senior lawyer serving in the Regulatory and Supervisory Advice Division in the Banco de España's Legal Department since March 2014. He advises on legal issues relating to supervision and resolution of credit institutions, including on the drafting of related legislation. He also worked for the Supervisory Law Division of the ECB's Directorate General Legal Services between 2017 and 2019, providing legal advice on topics related to the Single Supervisory Mechanism framework.

Prior to joining the Banco de España's Legal Department, Rafael worked for Garrigues law firm from 2009 to 2014, where his practice was focus on public law and regulated sectors, providing legal advice to companies and public administrations. He holds an executive master's in business law and graduated in law and business administration at Comillas Pontifical University in Madrid.



## 16 Panagiotis Papapaschalis

Panagiotis Papapaschalis is currently Senior Lead Legal Counsel at the Directorate General Legal Services of the European Central Bank, dealing with, among others, financial market infrastructures, fintech and cybersecurity.

Prior to that, he worked as: (i) Senior Counsel (on secondment) in the International Monetary Fund's Legal Department, dealing with, among others, technical assistance on central bank, banking and financial market infrastructure legislation, and as Legal Team Leader with the European Securities and Markets Authority.

He holds two LLM degrees in financial law (Aristotle University, Greece and Fordham University, USA) and is admitted to practice in New York, Greece, and England and Wales.



## Imène Rahmouni-Rousseau

Imène Rahmouni-Rousseau is the Director General of Market Operations at the ECB, in charge of implementing the single monetary policy for the euro area, together with the national central banks of the Eurosystem. Her responsibilities include lending operations and collateral, asset purchase programmes, and foreign exchange reserve management, as well as market monitoring and intelligence.

Imène sits in the BIS Markets Committee and chairs the ECB Market Operations Committee and the Bond Market Contact Group. She was previously the Director of Markets at Banque de France, the French central bank, and worked for five years at the Bank for International Settlements in Basel, where she led the vulnerability analysis team of the Financial Stability Board Secretariat.

She is the author of a number of articles on financial markets and monetary policy implementation, most recently on the scarcity effect of quantitative easing on repo rates, published in the Journal of Financial Economics. Imène has also co-chaired a 2018 BIS Markets Committee report on monitoring of fast-paced markets and co-authored several articles on financial innovation (CDOs, hedge funds, ETFs, shadow banking..). She holds a master's degree in economics and finance from Ecole Centrale de Paris (1997) and from Sciences Po Paris (1998).

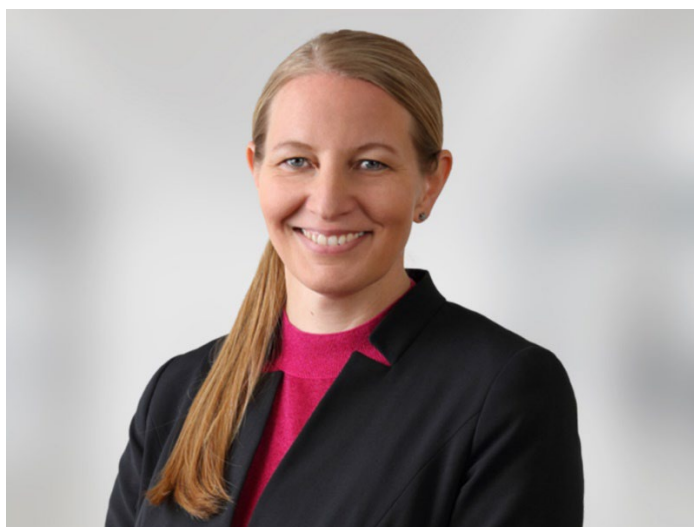


## Kerstin Schaepersmann

Kerstin Schaepersmann is a counsel in the Frankfurt office of Clifford Chance.

With more than 15 years of experience, she specialises in German and European banking and capital markets laws, with a particular emphasis on regulatory law, including the regulation of derivatives and financial market infrastructures. She has also advised on numerous securitisation and other structured finance transactions, including for the purposes of regulatory capital management and on issuances eligible as collateral for Eurosystem credit operations.

She studied law at the Universities of Trier and Lund/Sweden from 1995 to 2000 and completed the Second State Examination in 2002. After starting her career with Clifford Chance in 2003, she completed a secondment at KfW and is now a counsel in the Frankfurt office of Clifford Chance.





## Audrone Steiblyte

Audronė Steiblytė has been a member of the Legal Service of the European Commission since 2002, currently working in the area of State aid with particular focus inter alia on banks, insurance and financial services.

Between 2013 and 2022, in her capacity as member of the Legal Service, she was directly involved in the creation and development of the banking union and her field of expertise covered banking supervision, bank resolution, capital requirements, European supervisory authorities, as well as sustainable finance.

Previously a lecturer at Mykolas Riomeris University and a government official she was directly involved in the EU accession negotiations for Lithuania. She represented the European Commission in more than 350 court cases before the CJEU. She published in the field of Union law, with specific emphasis on banking law, free movement of capital as well as Union cohesion policy and structural instruments.



## György Varhelyi

György K. Várhelyi is Lead Legal Counsel in the ECB's Directorate Legal Services and an agent of the ECB before the CJEU. He focuses on financial law-related matters such as the legal aspects of the ECB's monetary policy implementation, including non-standard measures. He previously worked as an attorney at law with Skadden, Arps, Slate, Meagher and Flom LLP and then in investment banking at BNP Paribas. He was in charge of equity and equity-linked capital market transactions and M&A activities in and outside Europe. Mr Várhelyi has been admitted to the Paris Bar Association. He graduated from the Magistère and holds an LLM in commercial and corporate law from the University Panthéon-Assas Paris II.



## Chiara Zilioli

Chiara Zilioli has dedicated her entire working life to the European integration project. In 1989 she joined the Legal Service of the Council of Ministers in Brussels, moving to the Legal Service of the European Monetary Institute in 1995 and subsequently to the ECB as Head of Division in Legal Services in 1998, where she was appointed Director General in 2013.

Ms Zilioli holds an LLM from Harvard Law School and a PhD from the European University Institute. Since 1994 she lectures at Goethe University Frankfurt, at its Institute for Law and Finance and at the European College of Parma, Parma University. In 2016 she was appointed Professor of Law at Goethe University Frankfurt. She has published numerous articles and four books. She is also a member of the Parma Bar Association.

Chiara Zilioli has been married to Andreas Fabritius for more than 30 years; they have four children.



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