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SUBJECT Points for consideration in the House of Representatives' plenary debate of the final report of the parliamentary inquiry committee on the financial system

Dear Ms van Miltenburg,

The credit crisis has made us aware of the implicit guarantees that governments have provided for systemic financial institutions. We pointed out the risks facing the Dutch government in 2012.¹ Since 2008, government capital injections have increased the national debt by more than €40 billion.² Similar measures have also been taken by other countries. The Organization for Economic Cooperation and Development (OECD) recently observed that the implicit government guarantees given for the banking system are still in place and are undesirable with a view to the sustainability of public finances.³ The financial markets need to be organised and supervised as effectively as possible if we are to control the risks to the best of our ability. For national parliaments to have access to the appropriate information, national audit institutions must therefore have the power to audit the supervision of financial markets. This is one of the few ways in which parliament can receive independent information on the performance of the supervisory authorities.

You will soon be holding the plenary debate of the final report of the parliamentary inquiry committee on the financial system. On the inauguration of the new House of Representatives in September 2012, we introduced you to our activities by means of a folder outlining recent audits carried out by the Court of Audit, the *Status report 2012* (House of Representatives, 2012-2013, 33 412, no. 1). The folder contains 38

¹ *Risks to public finances – insight and control*, House of Representatives, 2011–2012, 33 299, no. 2, p. 40 ff.

² See the Court of Audit's website on the credit crisis: <http://kredietcrisis.rekenkamer.nl>.

³ OECD (2012). *Implicit Guarantees for Bank Debt: Where Do We Stand?* See: <http://www.oecd.org/finance/financialmarkets/Implicit-Guarantees-for-bank-debt.pdf>.

fact sheets, one of which, fact sheet 8, considered the same matters as parliamentary paper 32 255 on the system in place to supervise the stability of financial markets.

By means of this letter, we wish to inform you of certain recent developments. We successively consider:

- the Court of Audit's access to the files of the supervisory authorities;
- recent developments in the ability of supreme audit institutions in the EU to audit supervisory authorities;
- two potential avenues for the House of Representatives to explore;
- the incomplete powers of the European Court of Auditors to audit the European Central Bank (ECB).

Court of Audit's access to the files of the supervisory authorities

Pursuant to section 91 of the Government Accounts Act 2001 (CW2001), the Court of Audit may audit the supervisory authorities such as the Netherlands Authority for the Financial Markets (AFM) and De Nederlandsche Bank (DNB). The power to audit DNB is specifically laid down in section 91.4 CW2001.

Nevertheless, the Minister of Finance and DNB are of the opinion that we do not have the power to examine individual files kept by the supervisory authorities. The minister and DNB base their opinion on the confidentiality provisions laid down in the Financial Supervision Act (sections 1.89 to 1.93b). This Act is based on two European directives:

- Directive 2006/48/EC relating to the taking up and pursuit of the business of credit institutions (articles 44-52);
- Directive 2009/138/EC on the taking up and pursuit of the business of insurance and reinsurance (articles 64-71).

The articles referred to above forbid persons who work or have worked for the supervisory authorities to provide confidential information to third persons.

We have been arguing for many years that these confidentiality provisions were not intended to deny the Court of Audit access to individual files kept by the supervisory authorities. The discussion has been running since 1994, when the House of Representatives asked us to audit the supervision of the collapsed insurance company, *Vie d'Or*. The former Insurance Supervisory Board and the Minister of Finance denied us access to the supervisory files on *Vie d'Or* pursuant to the

obligation of confidentiality laid down in the EU directives. We were therefore unable to perform the audit as requested. At the time, the Council of State also supported the legal interpretation of the Minister of Finance and DNB (House of Representatives, 1995-1996, 24 456, no. 3, appendix 1).

The House of Representatives' Committee on Government Expenditure indicated on 14 December 2010 that it wished to receive further information on the legal aspects of gaining access to DNB's files. We set out our opinion in a letter of 8 February 2011 (House of Representatives, 2010-2011, 32 255, no. 5).

Several months later, the Council of State, further to a request by the House of Representatives, reiterated its opinion on the matter (House of Representatives, 2010-2011, 32 255, no. 8). The Council again agreed with the Minister of Finance and DNB that the European legislation denied the Court of Audit access to the files kept by the supervisory authorities, DNB and AFM.

The situation has since changed to such an extent that the Minister of Finance has repeatedly stated in the past five years that he has no objection to the Court of Audit accessing the information concerned, provided such was not prevented by European legislation. This position was recently expressed in his response to our audit entitled *DNB's supervision of bank stability* (House of Representatives, 2011-2012, 32 255, no. 12).

Recent developments in the ability of supreme audit institutions in the EU to audit supervisory authorities

We refer your House to two recent developments in the ability of supreme audit institutions in the EU to audit supervisory authorities.

1. Comparative audit of supreme audit institutions in EU member states to audit financial supervisors in their own countries

Since the outbreak of the financial crisis, questions have been asked in many European countries about the quality of the supervision of the banking industry exercised by the supervisory authorities. The presidents of the supreme audit institutions of the EU accordingly decided in October 2011 to carry out a joint audit entitled *Access of Supreme Audit Institutions to the main financial supervisors in EU Member States*, in which the supreme audit institutions analysed and tested their ability to audit the supervisory authorities in their home countries. Thirteen of the 17 supreme audit institutions and the European Court of Auditors took part in the

exercise. We have enclosed the joint report as adopted on 19 October 2012 by the *Contact Committee of the Supreme Audit Institutions of the European Union* with this letter for your information.

The report concludes that:

- seven supreme audit institutions do not have an audit mandate;
- six supreme audit institutions, one being the Netherlands Court of Audit, have a mandate to audit national supervisory authorities;
- four of these six supreme audit institutions actually have access to individual files kept by the national supervisory authorities;
- the Netherlands Court of Audit does not have such access to individual supervisory files. Our counterpart in Poland also does not have such access, albeit for other reasons.

It can be concluded from the enclosed report that four supreme audit institutions of EU member states have a mandate and access to the files of the supervisory authorities. The national implementation of the two EU directives referred to earlier in this letter apparently does not prevent those supreme audit institutions from accessing supervisory files in the member states. The European Commission, moreover, does not object to such access. The Court of Audit is the only supreme audit institution in the EU to have a mandate *without* access to supervisory files. This stance is justified on the grounds of two European directives, which of course should have identical application in all member states.

The report also discloses that it had not been the intention of the European directives to limit the powers of supreme audit institutions. The English-language report, as already noted, has been enclosed with this letter and can also be found on the Court of Audit's website on EU economic governance.⁴ The table below shows the main audit findings.

⁴ See: http://www.courtofaudit.nl/english/Publications/Topics/EU_governance_to_combat_the_economic_and_financial_crisis, under the heading 'The European system for financial supervision'.

Main findings of the audit, Access of Supreme Audit Institutions to the main financial supervisors in EU member States (19 October 2012)

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SAI	Main financial supervisor	Mandate SAI to audit financial supervisor	Actual access SAI to audit bank files of supervisors	Test SAI on completeness of files
Denmark	Danish Financial Supervisory Authority	Yes	Yes, with condition of confidentiality	Full access based on previous audits
Estonia	Financial Supervision Authority	No	No	-
Finland	Financial Supervisory Authority	No	No	-
France	Financial Markets Authority & Prudential control Authority	Yes	Yes, with condition of confidentiality	All files had an index and were complete.
Germany	Federal Financial Supervisory Authority	Yes	Yes, with condition of confidentiality	Index equals actual number of documents in files
Italy	Bank of Italy	No	No	-
Latvia	Financial and Capital Market Commission	No	No answer, so no request at banks.	-
Lithuania	Bank of Lithuania	No	No	-
Netherlands	Bank of the Netherlands	Yes	No	-
Poland	Polish Financial Supervision Authority	Yes	Partially. No data concerning bank secrecy	Question not applicable according to Polish SAI
Portugal	Bank of Portugal	No	No	-
Slovakia	National Bank of Slovakia	No	No	-
Sweden	Financial Supervisory Authority	Yes	Yes, with condition of confidentiality	Full access based on previous audits
ECA	European Banking Authority	Yes	Yes, agreed to confidentiality	No index, only digital files

2. Amendment of the EU bank supervision directive (CRD IV)

The European bank supervision directive ('Capital Requirements Directives IV', CRD IV) will be amended this year. The European Commission's current proposal allows certain information on bank supervision to be made available to supreme audit institutions (article 60). In response to the second report of the parliament inquiry committee into the financial system, the Minister of Finance stated that a draft provision had been included in CRD IV, partly on the initiative of the Netherlands, '... in which it is proposed that parliamentary inquiry committees and the Court of Audit

may examine confidential supervisory information in order to exercise their audit roles effectively' (House of Representatives, 2012-2013, 31 980, no. 77, p. 15).⁵

What next? Two potential avenues for the House of Representatives to explore

In view of the recent developments described above, we believe your House can ask the Minister of Finance to explore two avenues that would allow the Court of Audit to access individual supervisory files of the supervisory authorities. Only then can the Court of Audit carry out independent audits of supervisory files so as to inform parliament of the performance of the supervisory authorities.

Avenue 1: Reinterpretation of the two European directives relating to the taking up and pursuit of the business of credit institutions and relating to the taking up and pursuit of insurance and reinsurance

The joint audit conducted by the supreme audit institutions found that the European directives do not prevent the Court of Audit gaining access to the files of the supervisory authorities. This appears to be simply a matter of national interpretation. We therefore recommend that you revise this interpretation of European legislation so that it is consistent with that of the countries whose supreme audit institutions do have access to individual files of the supervisory authorities. This first avenue has the benefit that it can take effect immediately without needing to revise regulations already in place.

Avenue 2: Amendment of the European bank supervision directive (CRD IV)

Both the Minister of Finance and DNB expect the forthcoming amendment of CRD IV to clarify the current situation. The European Commission has proposed that provisions be included in the capital directive regarding the access of supreme audit institutions to credit institutions. The proposed provisions lay down that under certain conditions member states can grant their supreme audit institutions access to files on the prudential supervision of financial institutions. One of the conditions is that a precisely defined control or audit mandate must be included in national legislation. As the Court of Audit already has such a statutory mandate, the new European directive would remove any objections the minister and DNB might have.

Pursuant to section 87 CW2001, the Court of Audit may, in so far as it regards this as being necessary for the performance of its duties, inspect all goods, records, documents and other information carriers in such manner as it may determine, in all

⁵ The President of DNB employs words of a similar tenor in appendix 1 to the parliamentary paper concerned.

central government sectors. In contrast to this relatively low barrier to inspect information, there is a relatively high barrier to publishing confidential information. In response to an audit by the Court of Audit of a gift made by DNB (also known as the *Victory Boogie-woogie* audit), the Minister of Finance informed the House of Representatives about the Court of Audit's powers as laid down in section 87 CW2001 and about the publication of confidential information.⁶

The answer to the question 'What's next?' seems obvious to the Court of Audit. Avenue 1 can be explored nationally, regardless of the pace and nature of European developments. The current regime of the CW2001 provides sufficient guarantees that the denial of access can be withdrawn with due care.

Incomplete powers of the European Court of Auditors to audit the European Central Bank (ECB)

The report enclosed with this letter also considers the position of the European Court of Auditors. The financial supervisor shown in the table above is the European Banking Authority (EBA),⁷ not the European Central Bank. The European Commission proposed in September 2012 that the ECB become the main supervisor of banks in the EU.⁸ Responsibility for supervision would thus be shifted from the national authorities (in the Netherlands, DNB) to the ECB. National supervisory authorities, it is proposed, would continue to exercise supervisory tasks but would be subject to the authority of the ECB. The Council of Ministers agreed to the introduction of a European supervisory mechanism for banks, with a central role for the ECB, on 13 December 2012.⁹

To safeguard the information position of the European parliament and the member states, the European Court of Auditors should be able to audit the supervision exercised by the ECB. The European Court of Auditors' current mandate does not allow it to do so. This creates an audit gap at European level: arrangements are not in place for the independent audit of the ECB's organisation and exercise of its supervisory tasks and authority.

⁶ A the time, section 54 CW. House of Representatives, 1999-2000, 26 248, no. 2 (report), no. 11 (agreements).

⁷ See page 11 of the enclosure.

⁸ *Proposal for a Council regulation, conferring specific tasks on the European Central Bank concerning policies relating to the prudential supervision of credit institutions*, COM(2012) 511 final.

⁹ See http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ecofin/134265.pdf.

We would ask your House to urge the Minister of Finance to insist in Brussels that the European Court of Auditor's powers be enlarged. This would be consistent with the recent coalition agreement, in which countries are required to hold each other to their agreements effectively and to strengthen control mechanisms where necessary. A comprehensive system of supervision and supervisors also requires a comprehensive system of audit and audit institutions.

Closing comment

The Court of Audit will continue to follow developments in the effectiveness of financial supervision. We will inform you of any relevant new developments and would be pleased to provide further clarification of this letter if you wish.

We will forward a copy of this letter to the President of the Senate and to the Minister of Finance. We will inform by same mail the Minister of Foreign Affairs, the State Secretary for Finance, the Vice-President of the Council of State, the President of De Nederlandsche Bank, the President of the Netherlands Authority for the Financial Markets and the President of the European Court of Auditors.

Netherlands Court of Audit

Saskia J. Stuiveling,
President

Ellen M.A. van Schoten,
Secretary-General

Enclosure: Report on the access of supreme audit institutions to the main financial supervisors in the EU member states