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The statutory authority of the European Central Bank and euro-area national central banks over TARGET2-Securities*

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I. Introduction

As an academic as well as a banking and securities regulator, the dedicatee of this volume has made significant contributions to the integration of European financial markets. Accordingly, the topics of his publications reflect the ongoing integration process of European financial markets and of European securities markets, in particular. While, at the outset, his interests focused on securities regulation in Europe,[1] he has recently turned to studying the various initiatives to render clearing and settlement in Europe more efficient.[2] Indeed, while safe and efficient clearing and settlement systems are universally acknowledged as being an essential factor in the creation of an integrated European financial market,[3] numerous obstacles still exist that render cross-border securities transactions costly and less efficient than ultimately possible.

TARGET2-Securities (in financial jargon 'T2S') is one of the most advanced steps towards a more efficient and sound clearing and settlement infrastructure for the European securities market. The project

* May 2008. Any subsequent developments could not be taken into account.

[1] E. Wymeersch, 'Securities Market Regulations in Europe' in A.M. George, and I.H. Giddy (eds.), *International Finance Handbook* (New York: Wiley, 1982), 1–51; *idem*, 'Europese Effectenreglementering', in J. R. Schaafsma and E. Wymeersch (eds.), *Bescherming van beleggers ter beurze, Vereniging Handelsrecht* (Zwolle: W.E.J. Tjeenk Willink, 1986), 271–392; *idem*, 'The EEC and the Eurosecurities Markets', *Singapore Conference on International Business Law* (1987).

[2] E. Wymeersch, 'Securities Clearing and Settlement: Regulatory Developments in Europe', in G. Ferrarini and E. Wymeersch (eds.), *Investor Protection in Europe*, (Oxford University Press, 2006), 465 et seq.

[3] See the European Commission, *Financial Services: Implementing the Framework for Financial Markets: Action Plan* (1999), http://ec.europa.eu/internal_market/finances/docs/actionplan/index/action_en.pdf).

undertaken by the Eurosystem, i.e., the European System of Central Banks (ESCB) known as 'the European Central Bank (ECB) and the national central banks (NCBs) of those Member States whose currency is the euro'[4], aims at creating a settlement service for securities transactions linked to the existing Europe-wide cash settlement system known as TARGET2. The project is praised as being 'ground-breaking'[5] or even as an 'opportunity to jointly shape the future',[6] but has also met with severe criticism,[7] sometimes to the point of outright rejection.

One of the controversial issues raised almost at the outset was whether European law confers the statutory authority on the euro-area central banks (CBs), i.e. the ECB and the euro-area NCBs, to develop a securities settlement infrastructure. Although those denying the Eurosystem's legal power – in practice critics doubted the ECB's power in particular – have become fewer and most market participants seem to accept the Eurosystem's initiative, the question of whether the euro-area CBs can claim a sufficient legal basis for setting up and operating such a facility remains essential for the realization of the entire project.

This chapter, in seeking to provide a definite answer, is organized as follows. Starting with a brief overview of the other initiatives in the field of clearing and settlement (Section II), it goes on to give a brief description of TARGET2-Securities and to explain some pertinent key features (Section III). The main section (Section IV) then examines whether the euro-area CBs are empowered to implement TARGET2-Securities. It first sets out basic assumptions offering *inter alia* some clarifications as to the relationship between the ESCB and the Eurosystem, on the one hand, and the interplay between the Eurosystem and the ECB/NCBs, on the other hand. Building on that analysis, it then examines in some detail the relevant provisions that might confer the authority on the euro-area CBs to set up and operate TARGET2-Securities. The essay ends by offering some concluding remarks (Section V).

[4] Hence, the term 'Eurosystem' is not only a shorthand for 'the ECB plus the euro-area NCBs', but denotes a particular version of the ESCB. As to this interpretation, see infra IV.A. in more detail.

[5] M. Godeffroy, 'Ten frequently asked Questions about TARGET2-Securities' (available at www.ecb.int/paym/t2s/defining/outgoing/html/10faq.en.html).

[6] J. Tessler, 'An Opportunity to jointly shape the Future', *TARGET2-Securities Newsletter* No. 2, August 2007, 3 (available at www.ecb.int/paym/t2s/pdf/T2S_Newsletter_070829.pdf).

[7] E.g., J. Mérère, 'The Devil is in the Detail', *Finanzplatz* (January 2007), 18.

II. Overview of other initiatives in the field of clearing and settlement[8]

Taking existing EU legislation as a starting point, some directives contain provisions relevant for certain aspects of securities clearing and settlement activities. This is particularly true for the Settlement Finality Directive (SFD) of 1998,[9] but also for the Collateral Directive of 2002,[10] and – to a certain extent – the (recast) Banking Directive of 2006[11] and the (recast) Capital Adequacy Directive of 2006.[12] Even some provisions of the Markets in Financial Instruments Directive (MiFID)[13] have an effect on the clearing and settlement infrastructure, e.g. Article 34, which gives a right of access to an investment firm in one Member State, on a non-discriminatory basis, to the clearing and settlement system of another Member State. However, these provisions do not constitute a comprehensive framework for securities clearing and settlement activities, but rather form a partial patchwork regulating only specific problems.

The European Commission, following its Financial Services Action Plan of 1999,[14] set up a group of financial market experts, chaired by Alberto Giovannini, to analyse the status quo of the European financial market. The Giovannini Group, in its first report on clearing and settlement within the EU, identified fifteen barriers rendering cross-border securities transactions inefficient (often called Giovannini barriers), and, in its second report on the same topic, suggested a set of actions to eliminate these barriers.[15] Building

[8] For more details see Wymeersch, 'Securities Clearing and Settlement', (note 2, above), 470–83; K.M. Löber, 'The Developing EU Legal Framework for Clearing and Settlement of financial Instruments', *European Central Bank, Legal Working Paper Series*, No. 1, February 2006; H. Beck, 'Clearing und Settlement im Fokus europäischer Rechtspolitik', in K.P. Berger, G. Borges, H. Heermann, A. Schlüter, and U. Wackerbarth (eds.), *Zivil- und Wirtschaftsrecht im Europäischen und Globalen Kontext* (Berlin: De Gruyter, 2006), 669–95.

[9] Directive 98/26/EC [1998] OJ L 166/45.

[10] Directive 2002/47/EC [2002] OJ L 168/43.

[11] Directive 2006/48/EC [2006] OJ L 177/1.

[12] Directive 2006/49/EC [2006] OJ L 177/201.

[13] Directive 2004/39/EC [2004] OJ L 145/1.

[14] European Commission, *Financial Services: Implementing the Framework for Financial Markets: Action Plan* (note 3, above).

[15] The Giovannini Group, *Cross-Border Clearing and Settlement Arrangements in the European Union, Brussels* (November 2001); *idem*, *Second Report on EU Clearing and Settlement Arrangements*, Brussels, April 2003, http://ec.europa.eu/internal_market/financial-markets/docs/clearing/second_giovannini_report_en.pdf.

on the second Giovannini report, the European Commission in its Second Consultative Communication on Securities Clearing and Settlement[16] proposed the preparation of a framework Directive on Clearing and Settlement and the establishment of three groups of experts: the Clearing and Settlement Advisory and Monitoring Expert Group (CESAME), the Legal Certainty Group (LCG) and the Fiscal Compliance Expert Group (FISCO).[17]

In the meantime, since the former goal of removing the Giovannini barriers within a time period of three years has proved to be unrealistic, the European Commission has reversed its approach. Instead of pursuing the preparation of a framework Directive, the Commission has asked the market participants to agree on a Code of Conduct[18] that contains specified commitments of trading and post-trading infrastructure providers. According to the European Commission's report to the ECOFIN in July 2007,[19] the Code of Conduct has already had a positive impact. However, this does not imply that further activities are unnecessary. Quite the contrary, the FISCO report of October 2007[20] will serve the Commission as a basis for further discussions with Member States on future EU initiatives to simplify and modernize tax procedures applied to financial assets. Likewise, the LCG report, due in mid-2008, is expected to outline proposals for substantial EU legislation – probably either in the form of a Directive or a Regulation – dealing with substantive legal aspects of clearing and settlement.

A working group was established by the European System of Central Banks (ESCB) in collaboration with the Committee of European Securities Regulators (CESR) to elaborate common standards or recommendations for securities settlement systems and to enhance the safety

[16] *Clearing and Settlement in the European Union – The way forward,* Communication from the Commission to the Council and the European Parliament, COM(2994) 312 final.

[17] For further information on the expert groups, see http://ec.europa.eu/internal_market/financial-markets/clearing/index_en.htm.

[18] European Code of Conduct for Clearing and Settlement of 7 November 2006, http://ec.europa.eu/internal_market/financial-markets/docs/code/code_en.pdf.

[19] Improving the Efficiency, Integration and Safety and Soundness of Cross-border Post-trading Arrangements in Europe, Report to the ECOFIN, 25 July 2007, http://ec.europa.eu/internal_market/financial-markets/docs/clearing/ecofin/20070725_ecofin_en.pdf.

[20] The Fiscal Compliance Experts' Group, *Solutions to Fiscal Compliance Barriers Related to Post-trading within the EU, Second Report 2007*, http://ec.europa.eu/internal_market/financial-markets/clearing/compliance_en.htm.

and efficiency of cross-border securities clearing and settlement activities within the EU. Building on the CPSS/IOSCO recommendations,[21] but seeking to adapt these global recommendations to European circumstances, the group elaborated the Standards for Securities Clearing and Settlement within the European Union,[22] nineteen standards aimed at rendering securities clearing and settlement systems within the European Union safer, more efficient and sound.[23]

Still further initiatives within Europe are undertaken by the European Financial Markets Lawyers Group (EFMLG), a group established in 1999 following a Eurosystem initiative and composed of European lawyers working for major credit institutions active in the European financial market. The EFMLG's work aims at promoting the harmonization of EU financial market activities through legal initiatives. In its report 'Harmonisation of the legal Framework for Rights evidenced by book-entries in respect of certain financial Instruments in the European Union'[24] the EFMLG observed barriers to cross-border securities transactions similar to those identified by the Giovannini Group. The EFMLG formulated recommendations calling for further EU legislation in the form of directives and supporting the (as it was called at the time) EU Securities Account Certainty Project, proposed by the Giovannini Group.

Looking beyond Europe, some global initiatives show parallels to the work currently being undertaken in the EU, e.g. the 'Convention on the Law Applicable to certain Rights in respect of Securities held with an Intermediary'[25] concluded by the Hague Conference in 2002 and signed by two signatories – Switzerland and the US – in 2006 (dealing with matters that are addressed albeit differently within the EU by the SFD and other EC legal acts). Another initiative is UNIDROIT's project on Intermediated Securities. The original text of the 'Preliminary draft

[21] CPSS/IOSCO, *Recommendations for Securities Settlement Systems*, November 2001, www.bis.org/publ/cpss46.pdf.

[22] The ESCB-CESR Standards for Securities Clearing and Settlement in the European Union, www.ecb.int/pub/pdf/other/escb-cesr-standardssecurities2004en.pdf.

[23] Critical, then, Bundesverband Deutscher Banken, *Europäische Wertpapiermärkte – Konsolidierung des Rechtsrahmens*, Berlin, January 2006, 34.

[24] European Financial Markets Lawyers Group, *Harmonisation of the legal Framework for Rights evidenced by book-entries in Respect of certain financial Instruments in the European Union*, European Central Bank, June 2003.

[25] Hague Conference on Private International Law, 'Convention on the Law Applicable to Certain Rights relating to Securities held with an Intermediary', 5 July 2006, www.hcch.net/index_en.php?act=conventions.text&cid=72.

Convention on harmonized substantive Rules regarding Securities held with an Intermediary' of 2004 was further developed during the international negotiation process that took place between May 2005 and May 2007. In September 2008, a diplomatic conference is planned to be held in Geneva to adopt a 'Convention of substantive rules regarding intermediated securities'.[26]

III. TARGET2-securities: main features of the project[27]

On 7 July 2006, the ECB's Governing Council announced that the Eurosystem is evaluating opportunities to provide settlement services for securities transactions. Having drafted the project's rough features, the Eurosystem launched feasibility studies which came to the conclusion that the project was operationally, legally, economically and technically feasible.[28] A first consultation paper, that framed the cornerstones of TARGET2-Securities by setting up twenty principles and sixty-seven high-level proposals, was published in March 2007[29] on which market participants could comment by June 2007.[30] Working groups, designed to allow a variety of institutions to participate, elaborated the user requirements which were fully articulated by the end of 2007.[31] A second public consultation was launched in December 2007. Market participants were invited to comment on the TARGET2-Securities user requirements

[26] For the Preliminary Draft and further information on Study 78 on intermediated securities, see www.unidroit.org/english/workprogramme/study078/item1/main.htm.

[27] As to the following, cf. Godeffroy, 'Ten frequently asked questions about TARGET2-Securities' (note 5, above); ECB, *TARGET2-Securities, The Blueprint* (8 March 2007), www.ecb.int/pub/pdf/other/t2sblueprint0703en.pdf; ECB, *T2S Progress Report* (26 October 2007), www.ecb.int/pub/pdf/other/t2s-progressreport200710en.pdf.

[28] The feasibility studies are available at www.ecb.int/paym/t2s/decisions/html/nextphase.en.html.

[29] ECB, *T2S Consultation Paper: General Principles and high-level Proposals for the User Requirements* (26 April 2007), www.bundesbank.de/download/zahlungsverkehr/t2s_us_070426.pdf.

[30] For an overview of the market participants' reactions see I. Terol, 'How have the Principles and Proposals been reviewed after the Consultation?', presentation, T2S info session 29 August 2007, www.ecb.int/paym/t2s/pdf/outgoing/t2s_infosession_070829_presentation1.pdf.

[31] ECB, *T2S – The User Requirements* (12 December 2007), www.ecb.int/ecb/cons/shared/files/T2S_urd_chapters.pdf; a summary of the user requirements can be found at www.ecb.int/ecb/cons/shared/files/T2S_urd_management_summary.pdf. For a description of the TARGET2-Securities governance structure cf. TARGET2-Securities Newsletter No. 1, June 2007, www.ecb.int/paym/t2s/pdf/T2S_Newsletter.pdf, 3 *et seq.* or the (shorter) overview at www.ecb.int/paym/t2s/defining/html/index.en.html.

and the methodology for the assessment of the economic impact of the project by April 2008.[32] The ECB assumes the project will be concluded by 2013, at the latest.[33]

The objective of TARGET2-Securities is to maximize safety and efficiency in the settlement of euro-denominated securities transactions. The main features of the project, as so far determined, are as follows:

TARGET2-Securities will be a single, purely technical platform providing harmonized IT settlement services to central securities depositories (here below referred to as 'CSDs') based on the TARGET2 platform,[34] a technical platform for the settlement of payment instructions. It will be established as well as fully owned by the Eurosystem[35] and technically operated on behalf of four of the Eurosystem NCBs (Bundesbank, Banque de France, Banca d'Italia and Banco de España).[36] TARGET2-Securities will allow the simultaneous (real-time) booking of both legs of a transaction in securities , i.e. the payment in (exclusively) central bank money and the transfer (of title) of the securities on a single IT-platform (integrated model). In more detail:

The ECB/Eurosystem will not operate as a CSD[37] since it will not legally maintain securities accounts for CSDs,[38] or even less for banks that are clients of such a CSD. Instead, the account and legal relationships remain exclusively between CSDs and their clients, i.e. the banks holding securities accounts with the CSDs also manage the account relationships among the different CSDs (the legal arrangements between CSDs will, however, be affected by the harmonized terms and conditions governing the settlement services provided by TARGET2-Securities)[39]. From this it follows that cross-border and cross-CSD securities transactions will still be effected by book entries in securities

[32] ECB Press Release of 18 December 2007, www.ecb.int/press/pr/date/2007/html/pr071218.en.html.

[33] Speech by G. Tumpell-Gugerell, Member of the Executive Board of the ECB at the *Journal of Financial Transformation* dinner London, 27 September 2007, www.ecb.int/press/key/date/2007/html/sp070927.en.html.

[34] *General Principles* (note 29, above), 4, principle 2.

[35] ECB Press Release 7 July 2006, www.ecb.int/press/pr/date/2006/html/pr060707.en.html; *General Principles* (note 29, above), 4, principle 1.

[36] Questions and Answers on TARGET2-Securities, 8 March 2007, www.ecb.int/press/pressconf/2007/html/is070308.en.html#t2s.

[37] *General Principles* (note 29, above), 4, principle 3.

[38] *General Principles* (note 29, above), 5, principle 4.

[39] *General Principles* (note 29, above), 7, principle 15.

accounts held by CSDs' clients with CSDs or by CSDs with one another. Moreover, the question of whether the T2S's booking of a security from one account to another perfects a transfer of title, and at what point in time it does so, lies outside the scope of TARGET2-Securities, and is determined solely by the national law(s) applicable to the transaction. In this respect TARGET2-Securities will neither alter the present situation nor will national legislative adaptations be necessary for the implementation of TARGET2-Securities (even if legal harmonization would be desirable to improve integration).[40] However, T2S may increase (even in the absence of legal harmonization of substantive law) the predictability of and legal certainty on the completion of the legal transfer, due to the transfer order finality on both sides of a cross-system transaction and the standardized simultaneous settlement in T2S in the accounts of both CSDs involved resulting in the legal exchange of cash and securities.

What the ECB/Eurosystem will provide is the TARGET2-Securities platform, i.e. the integrated IT-platform allowing for the simultaneous booking of cash transactions in cash accounts held with the Eurosystem central banks by CSDs or their customers, as well as securities transactions in securities accounts held with the CSDs. The database functionality required will be restricted to the basic role of collocating and electronically storing account-related data in a common technical location.[41] All CSDs are eligible under equal-access conditions[42] to participate in TARGET2-Securities,[43] but not required to do so. TARGET2-Securities will operate on a non-profit-making basis.[44] As regards the relationship between cash transactions and securities transactions, TARGET2-Securities is planned to operate following the so-called Delivery versus Payment (DVP) model 1, which in T2S means simultaneous real-time delivery versus payment settlement in central bank money for domestic *and* cross-border transactions of securities.[45]

[40] TARGET2-Securities, *Legal Feasibility Study* (8 March 2007), 6. Admittedly, the study assumes that the soundness and efficiency of TARGET2-Securities could be strengthened by further harmonization in this respect (available at www.ecb.int/pub/pdf/other/t2slegalfeasibility0703en.pdf).

[41] TARGET2-Securities, *Legal Feasibility Study* (note 40, above), 1.

[42] *General Principles* (note 29, above), 7, principle 14, principle 12.

[43] *General Principles* (note 29, above), 7, principle 13.

[44] *General Principles* (note 29, above), 8 principle 18.

[45] TARGET2-Securities, *Legal Feasibility Study* (note 40, above), 2.

IV. Legal assessment

A. Basics

The starting point for a legal analysis of TARGET2-Securities is a seeming puzzle. On the one hand, as mentioned above, the Eurosystem is said to be the full owner and operator of TARGET2-Securities, whereas, on the other hand, critics have disputed the legal authority of the ECB (and the NCBs) to operate the system.

These divergences obviously beg the question whether the Eurosystem is a separate actor from the ECB and the NCBs, or whether the term is just an abbreviation for denoting the ECB and the NCBs. The problem is compounded by the fact that the EC Treaty as well as the Statute of the European System of Central Banks and of the European Central Bank ('ESCB/ECB Statute') only deal with the ESCB but do not employ the term Eurosystem at all. Moreover, both the EC Treaty as well as the ESCB/ECB Statute invest the ESCB with tasks and, in order for these tasks to be carried out, confer certain legal powers on the ECB and the NCBs.

Against this backdrop, any meaningful discussion of the question whether the EC Treaty and/or the ESCB/ECB Statute actually confer the legal authority required on the actor owning and operating TARGET2-Securities presupposes some prior clarifications as to the nature of the Eurosystem and its relationship with the ESCB on the one hand and the ECB on the other hand.

1. ESCB and the Eurosystem

The Eurosystem according to the definition given in Article 9 Sentence 2 of the Rules of Procedure of the ECB[46] means 'the European Central Bank (ECB) and the national central banks of those Member States whose currency is the euro'. By contrast, the EC Treaty and the ESCB/ECB Statute only refer to the European System of Central Banks defined by Article 107 (1) EC Treaty as being 'composed of the ECB and of the central banks' of all Member States.

However, this neither implies that the Eurosystem lacks a legal foundation in primary community law nor that the ESCB and the Eurosystem form two different organizations existing alongside one another. In particular, it would be misleading to conceive of the Eurosystem as a subset of the ESCB. Rather, it is more appropriate to say that the EC Treaty as

[46] Decision ECB/2004/2 [2004] OJ L 080/33.

well as the ESCB/ECB Statute – despite the definition given by Article 107 (1) EC Treaty – attribute two different meanings to the term 'ESCB'. Depending on the Article in question, the term 'ESCB' must be construed either in the sense of Article 107 (1) EC Treaty as 'the ECB and the NCBs of all Member States' or, as is most often the case, in the sense of Article 9 Sentence 2 of the Rules of Procedure of the ECB, i.e. as 'the ECB and the euro-area NCBs'. Moreover, the term 'Eurosystem' does not denote any distinct organization existing apart from the ESCB but denotes the ESCB in its latter quality, i.e. the ESCB comprising the ECB and euro-area NCBs.

Art. 122 (3) and (4) EC Treaty and Art. 43 (1), (3) and (4) ESCB/ECB Statute determine for the provisions of the EC Treaty and the ESCB/ECB Statute respectively whether those provisions address the ESCB in the sense of Art.107 (1) EC Treaty or in the sense of the 'Eurosystem'. The reading depends on whether those provisions according to the definition given by Art. 122 (3) and (4) EC Treaty and Art. 43 (1), (3) and (4) ESCB/ECB Statute refer to (the NCBs of) all Member States or only to (the NCBs of) euro-area Member States.

2. Legal nature of the ESCB/Eurosystem

The ESCB/Eurosystem, as is universally admitted, has no legal personality of its own. This follows *a contrario* from Article 107 (2) EC Treaty and Article 9.1 ESCB/ECB Statute which, both, award legal personality only to the ECB.

Most commentators even assert that the ESCB/Eurosystem has no existence of its own, i.e. that it does not exist as a separate organization. Instead, the ESCB/Eurosystem is labelled as being an institutional framework of rules establishing a link between the ECB and the (euro-area) NCBs,[47] or even reduced to the status of being nothing more than an abbreviation denoting the ECB and the (euro-area) NCBs.[48]

On the other hand, according to the ECB's presentation, TARGET2-Securities will be fully owned and operated by the Eurosystem. In line with this, recital 4 of the ECB's guideline on a Trans-European Automated Real-time Gross settlement Express Transfer system (TARGET2) provides for the ECB, '[a]cting on the Eurosystem's behalf', to enter into a

[47] H.K. Scheller, *The European Central Bank – History, Role and Functions*, 2nd edition (Frankfurt: ECB, 2006), 42.

[48] W. Kahl and U. Häde, 'Art. 107 EC Treaty' in C. Callies and M. Ruffert, *Das Verfassungsrecht der Europäischen Union*, 3rd edition (Munich: Beck, 2007), No. 2 (with further references).

contract with a service provider.[49] Both documents strongly hint at the ECB's willingness to accept the Eurosystem as an organizational actor in its own right, even though these statements would not be in line with the primary Community law just described if they meant to attribute to the Eurosystem a legal personality of its own.

Indeed, primary Community law, i.e., the provisions of the EC Treaty and those of the ESBC/ECB Statute, the latter being a Protocol to the EC Treaty and therefore also part of primary Community law,[50] is rather ambiguous as to the nature of the ESCB/Eurosystem.

At a first glance, the ESCB/Eurosystem seems to form an organizational entity, being endowed with certain tasks, members, and decision-making bodies which, for the lack of a legal personality of its own, cannot as such enter into any legal relationship with third parties, i.e., non-members. According to this interpretation, the tasks are set out in Article 105 (2) EC Treaty as well as in Article 3 ESCB/ECB Statute, whereas Article 107 (1) EC Treaty determines membership. With regard to the system's own decision-making bodies, Article 107 (3) EC Treaty entrusts the decision-making bodies of the ECB with governing the ESCB/Eurosystem, as well. Thus, while the ESCB/Eurosytem arguably lacks institutions ('*Organe*') of its own, it is governed (cf. Art. 105 (1) EC Treaty) internally through the pertinent decision-making bodies of the ECB. Whereas, the operational tasks are carried out by the central banks forming part of the Eurosystem (Art 9.2., Art 16 et seq. ESCB/ECB-Statute) putting, under the principle of decentralization, an emphasis on the NCBs with regard to the fulfilment of operational tasks (Art 12.1 (3) of the ESCB-Statute). Put differently, with regard to inner-organizational decisions the ESCB/Eurosystem – as opposed to the ECB – takes decisions by relying on the latter's decision-making bodies. By contrast, with regard to activities vis-à-vis third parties, Articles 18 *et seq.* ESCB/ECB Statute confer the power to act on the ECB and euro-area NCBs as legal persons.

Serious doubts still remain. Even if one were to conceive of the ESCB/Eurosystem as an organizational entity in its own right, the existence

[49] Guideline ECB/2007/2 [2007] OJ L 237/1.

[50] R. Smits, 'Art. 105 EC Treaty', in H. von der Groeben and J. Schwarze (eds.), *Vertrag über die Europäische Union und Vertrag zur Gründung der Europäischen Gemeinschaft, commentary*, 4 vols., 6th edn (Baden-Baden:, Nomos, 2003), vol. III, No. 20; B. Kempen, 'Article 105 EC-Treaty', in R. Streinz (ed.), *EUV/EGV Vertrag über die Europäische Union und Vertrag zur Gründung der Europäischen Gemeinschaften, commentary (*Munich: Beck, 2003), No. 15 (referring to Article 311 EC-Treaty).

of such a system would not entail any practical consequences, at all. To begin with, any decisions taken on behalf of the ESCB/Eurosystem are at the same time decisions taken by the ECB, since the latter's decision-making bodies also govern the ESCB/Eurosystem. Article 110 (1) EC Treaty is testimony to this, since it explicitly stipulates that, in order to carry out the tasks entrusted to the ESCB, the ECB shall make regulations, take decisions and make recommendations. Moreover, the actions of the system's members, i.e. of the ECB and the NCBs, are not governed by the decision-making bodies of the ESCB/Eurosystem, but by those of the ECB. With respect to the NCBs, Article 14.3 ESCB/ECB Statute provides for the ECB (by way of its decision-making bodies) to issue guidelines and instructions for the NCBs to follow when acting in their capacity as an integral part of the ESCB/Eurosystem.

On balance, then, in line with the prevailing interpretation, the ESCB – and the same holds true for the Eurosystem, as well – is to be understood as shorthand meaning 'the ECB and the (euro-area) NCBs'. Hence, for present purposes, whether any actor is empowered to implement TARGET2-Securities is to be discussed solely with respect to the ECB and the euro-area NCBs.

B. Statutory power of the ECB/euro-area NCBs over TARGET2-Securities

Before embarking on a detailed analysis of whether the EC Treaty and/or the ESCB/ECB Statute confer the legal authority to set up and operate TARGET2-Securities on the ECB and the euro-area NCBs, it seems worthwhile to briefly point out that the settlement of securities transactions is a not uncommon function of central banks. Currently, for example, the central banks of the United States, Japan, Belgium, Greece and Portugal are active in this field.[51] In addition, in the last twenty years the central banks of France, the UK, Spain,[52] Italy, Ireland, the Netherlands and Finland (as major shareholders) were involved in securities settlement but gave up their involvement in the context of the de-mutualization and privatization of their securities exchanges during the 1990s.

[51] G. Tumpel-Gugerell, 'Speech at the EU Commission's Conference on The EU's new Regime for Clearing and Settlement in Europe', 30 November 2006, Brussels, www.ecb.int/press/key/date/2006/html/sp061130_1.en.html.

[52] Godeffroy, 'Ten frequently asked Questions about TARGET2-Securities', (note 5, above).

Admittedly, the involvement of other central banks in the settlement of securities does not predicate anything about whether any of the actors just mentioned is empowered to execute such actions given the current legal regime. However, it illustrates by way of example that this field of activity is not alien to the operation of a central bank (some of which are in fact euro-area NCBs). Indeed, in comparison with TARGET2-Securites, most of these central banks assert a much more substantive role in securities settlement, e.g. the US Fedwire System also acts as CSD.[53]

1. Principle of limited transfer of powers to the ECB/euro-area NCBs

The starting point for an analysis of whether the EC Treaty and/or the ESCB/ECB Statute confer the authority to implement TARGET2-Securities on the euro-area CBs, i.e. the ECB and the euro-area NCBs is the principle of limited transfer of powers.

The EC does not possess comprehensive jurisdiction, but can only act insofar as sovereign rights have been transferred by Member States in accordance with the principle of limited transfer of powers from Member States to the EC ('*compétence d'attribution*'). The principle of limited transfer is not only applicable as far as the regulatory power of the EC is concerned (Article 5 (1) EC Treaty), but also with respect to the EC institutions ('*Organe*') (Article 7 (1) EC Treaty). Thus, each institution can only act insofar as it has been assigned authority.[54]

The ECB is arguably not an institution of the EC (see Article 7, Article 8 EC Treaty) since it was established and given a legal personality of its own by Article 107 (2) EC Treaty.[55] Its exact legal nature is controversial.[56] However, since its powers are formed on a similar basis to an institution of the EC,[57] any action by the ECB requires a basis of authorization, i.e. a legal basis. This applies for any kind of action – lawmaking as well as other forms of acting. From this it follows that for the ECB

[53] E.M. Jaskulla, 'Zukünftige Regelung des Clearing und Settlement von Wertpapier- und Derivategeschäften in der EU', *Zeitschrift für europarechtliche Studien*, (2004), 497, at 509.

[54] R. Geiger, *Vertrag über die Europäische Union und Vertrag zur Gründung der Europäischen Gemeinschaft, commentary*, 4th edn (Munich: Beck, 2004), Art. 7 EC Treaty, No. 15.

[55] Case C-11/00: *Commission v. ECB ('OLAF')* [2003] ECR I-7215, para. 92.

[56] Cf. amongst several others U. Häde, 'Zur rechtlichen Stellung der Europäischen Zentralbank', *Wertpapiermitteilungen* (2006), 1605 *et seq.*

[57] C. Schütz, 'Die Legitimation der Europäischen Zentralbank zur Rechtsetzung', *Europarecht* (2001), 291–2; A. Decker, Die Organe der Europäischen Gemeinschaft', *Juristische Schulung* (1995), 883–4.

to be empowered to set up and operate TARGET2-Securities requires a provision that goes beyond empowering the EC in general by vesting the ECB in particular with the authority to undertake such a project.

Moreover, since the euro-area NCBs are an integral part of the ESCB and, as such, act in accordance with the guidelines and instructions of the ECB to carry out the tasks entrusted to the ESCB/Eurosystem (Article 14.3 ESCB/ECB Statute) the principle of limited transfer of powers applies to the euro-area NCBs, when acting as an integral part of the ESCB/Eurosystem, too.

2. Criteria for the choice of a legal basis

The legal basis is to be chosen according to objective, legally verifiable circumstances, especially the purpose and content of the legally relevant act.[58] Given the features of TARGET2-Securities described above, any legal provision that may serve as a legal basis for the euro-area CB's authority for TARGET2-Securities has to empower the ECB/euro-area NCBs to carry out payments for securities transactions and to book securities held by CSDs from one account into another in order to settle securities transactions.

Since the Statute of the ECB, as part of the ESCB/ECB Statute, forms a part of primary Community law,[59] one or several Articles of the Statute may empower the ECB/euro-area NCBs to establish and operate TARGET2-Securities.

3. Provisions in the EC Treaty?

Neither Articles 56 *et seq*. EC Treaty nor Articles 94 *et seq*. EC Treaty supply a legal basis for any action on the part of the ECB in general, or for the setting up of TARGET2-Securities in particular.

In contrast, Article 105 (2) EC Treaty has been invoked as a legal basis. Indeed, as just mentioned, Article 105 (2), fourth indent, of the EC Treaty and Article 3.1, fourth indent, of the ESCB/ECB Statute attribute to the ESCB the basic task *inter alia* of 'promot[ing] the smooth operation of payment systems'. However, these provisions only define the framework of the ESCB's activities.[60] The specific operations that the ESCB and – since the ECB and the NCBs form part of and may carry out functions

[58] Case 45/86, *Commission v. Council APS* [1987] ECR-1493, para. 11.

[59] Supra IV.A.2. at note 50, above.

[60] R. Smits, *The European Central Bank, Institutional Aspects* (The Hague: Kluwer Law International, 1997), 179.

of the ESCB – the ECB and the euro-area NCB's respectively are empowered to pursue tasks as regulated in the ESCB/ECB Statute.[61] These detailed provisions would be circumvented, if Article 105 (2) EC-Treaty on its own could serve as a legal basis for TARGET2-Securities.

4. Article 18.2 ESCB/ECB Statute?

Pursuant to Article 18.2 ESCB/ECB Statute, the ECB is to establish general principles for open market operations and credit operations carried out by itself or the NCBs.

For obvious reasons, this provision on its own does not authorize the ESCB to set up TARGET2-Securities: general principles within the meaning of Article 18.2 are legally non-binding rules i.e. rules that do not bind third parties (except euro-area NCBs),[62] not a technical platform. The general principles referred to in this provision include *inter alia* the preconditions which market participants willing to enter into transactions with the ECB or euro-area NCBs have to fulfil in order to qualify as an eligible counterparty[63] and set out the criteria under which the ECB and euro-area NCBs enter into binding relationships and execute transactions with such eligible counterparties. Thus, establishing these principles, on the one hand, provides important information to the market and, on the other hand, serves to limit the power of the ECB/euro-area NCBs to discriminate among market participants in selecting counterparties to operations pursuant to Article 18.2. It also provides for the binding framework under which the ECB and euro-area NCBs conduct transactions, including the eligible ways of settling such transactions, for instance, regarding the cross-border settlement of collateralized credit.[64]

5. Article 18.1 in conjunction with Article 17 ESCB/ECB Statute?

According to Article 18.1 second indent ESCB/ECB Statute, the ECB and euro-area NCBs may conduct credit operations with market participants,

[61] Kempen, 'Article 105 EC-Treaty', in Streinz (note 50, above), Art.107 EC-Treaty', No. 8, 15; Smits, 'Article 105 EC-Treaty', in von der Groeben and Schwarze (eds.) (note 50, above), No. 4, 5; Smits, *The European Central Bank,* (note 60, above), 179.

[62] Smits, *The European Central Bank* (note 60, above), 274; cf. also the examples given in Weenink, 'Art. 18 ESCB Statute', in von der Groeben and Schwarze (eds.) (note 49, above), No. 41 *et seq.*

[63] Weenink in von der Groeben and Schwarze (eds.) (note 50, above), No. 41.

[64] See e.g. Chapters 3 and 6 of the General Documentation on the Eurosystem monetary policy instruments and procedures, September 2006 (Annex 1 to Guideline ECB/2000/7 as amended) (available at www.ecb.int/pub/pdf/other/gendoc2006en.pdf).

with lending being based on adequate collateral. By way of clarification, Article 17 ESCB/ECB Statute authorizes the ECB and NCBs to 'accept assets, including book-entry securities, as collateral'.[65] The term 'assets' is rather wide, and thus covers any legal method of transferring securities,[66] including *inter alia* the pledging of securities, the fiduciary transfer of claims on third parties and the institution of a lien.[67]

Even read in conjunction, Articles 18.1 and 17 do not provide for a legal basis for TARGET2-Securities in its entirety. As a purely technical platform, the system will not alter the existing securities accounts structure. CSDs will still hold accounts with each other, whereas other market participants will hold accounts with a CSD. As a consequence, the ECB under TARGET2-Securities acts on behalf of the CSDs even if, in a purely technical sense, holders of a securities account with a CSD could send their settlement orders directly to the settlement platform. In contrast, the ECB and NCBs, when carrying out the tasks entrusted to the ECB by conducting lending operations based on accepting adequate collateral with market participants, act for themselves when taking book-entry securities. From this it follows that Articles 18.1 and 17 cannot serve as a legal basis for the TARGET2-Securities project insofar as the establishment and operation of a securities settlement platform on behalf of market participants, i.e. CSDs, are concerned.

Arguably, the situation is somewhat different as far as the lending by the ECB and euro-area NCBs based on collateral in the form of book-entry securities is concerned (which is required for all central bank credit operations). Admittedly, Articles 18.1 and 17 do not explicitly state whether the ECB/euro-area NCBs are empowered to establish and operate technical facilities aimed at facilitating the secure and efficient settlement of lending against collateral transactions. However, the Eurosystem does have a vital interest in the efficient and secure functioning of securities settlement systems since, otherwise, its ability to pursue monetary policies by lending against collateral transactions will be severely hampered. Therefore, one may indeed interpret Article 18.1 in conjunction with Article 17 to the effect that *a fortiori* the ECB/

[65] It has been argued that the legal basis for the cash leg of the system or the collateralization of central bank credit by securities could be found in Article 17. However, this approach disregards the complex structure of TARGET2-Securities. In any case, it does not supply a legal basis for the entire project.

[66] Weenink, 'Art. 17 ESCB Statute', in von der Groeben and Schwarze (eds.) (note 50, above), No. 11.

[67] Smits, *The European Central Bank,* (note 60, above), 263.

euro-area NCBs are empowered to set up the technical (IT) infrastructure required for the purpose of effectively operating lending against collateral transactions. Put differently, the establishment and operation of a platform providing services conducive to the more effective conduct of the Eurosystem's credit operations falls within the mandate of the ECB and the NCBs (notwithstanding the fact that such operations are currently conducted without such a platform having been established, albeit in a less effective and less secure manner). On the other hand, this interpretation only holds true for those book-entry securities which the ECB and the euro-area NCB's are willing to accept as collateral, at least in principle.

6. Article 23 ESCB/ECB Statute?

Article 23 ESCB/ECB Statute empowers the ECB and euro-area NCB's to acquire and sell spot and forward all types of foreign exchange assets – including securities as clarified by the regulation itself – as well as to hold and manage the assets and conduct all types of banking transactions in relations with third countries.

It has been argued that the provision furnishes a legal basis for TARGET2-Securities, because the ECB and the euro-area NCB's have been granted such a wide scope of operations in the external field and therefore authority cannot be denied to the ECB/euro-area NCBs domestically. Admittedly, the ECJ has developed external powers of the EC by drawing a parallel to its internal powers as an example of implied powers.[68] According to this ruling, the EC is not only entitled to conclude international treaties if the EC Treaty explicitly stipulates a regulatory power to do so, but also if the EC has the corresponding inner authority.[69] However, as regards the ECB and the euro-area NCBs, their internal powers are regulated in Articles 17–22 ESCB/ECB Statute and thus implied powers can only be derived from these detailed regulations. Article 23 only refers to external operations as its headline and its content expressively state.

Still, it would be inconsistent if the regulation granted external powers to the ECB/euro-area NCBs to a much greater extent than internal

[68] A. Haratsch, C. Koenig and M. Pechstein (eds.), *Europarecht*, 5th edn (Tübingen: Mohr-Siebeck, 2006), 430.

[69] Case 22/70: *Commission v. Council* (*AETR)* [1971] ECR 263, para. 72 *et seq.*; Joined Cases 3, 4 and 6/76: *Kramer* [1976] ECR 1279, para. 30, 33.

powers.[70] Therefore, Article 23 ESCB/ECB Statute indicates that the provisions dealing with the internal powers, i.e., Articles 17–22 ESCB/ECB Statute are to be construed extensively.

7. Article 22 ESCB/ECB Statute

Pursuant to Article 22 ESCB/ECB Statute, (i) '[the] ECB and national central banks may provide facilities',[71] and (ii) 'the ECB may make regulations, to ensure efficient and sound clearing and payment systems within the Community and with other countries'. With respect to 'facilities', the provision empowers the ECB as well as the euro-area NCBs.

a. Providing facilities for a securities settlement system on the basis of Article 22? According to the ECB, the term 'clearing and payment systems' in Article 22 also refers to securities settlement systems because of the following arguments:[72]

- the inclusion of the term 'clearing system' would not have been necessary if Article 22 referred only to payment systems;
- the potential for a major disturbance in a CSD's operation, that could spill over to payment systems and endanger their smooth functioning, is likely to have increased in recent years because of the increased importance of secured lending as money market instruments, the increased use of securities collateral to control risks and increase liquidity in payment systems through collateralized intraday credit lines, and the rapid growth of securities settlement volumes'.[73]

[70] Smits and Gruber, 'Art. 23 ESCB Statute', in von der Groeben and Schwarze (eds.) (note 50, above), No. 24; Smits, *The European Central Bank,* (note 60, above), 312.

[71] According to some commentators, the euro-area NCBs are empowered with respect to payment systems operating within their country, whereas the ECB is empowered with respect to payment systems operating cross-border within some or even all Member States of the ESCB (cf. Smits and Gruber, 'Art. 22 ESCB Statute', in von der Groeben and Schwarze (eds.) (note 50, above), No. 21). However, neither the EC Treaty nor the ESCB/ECB Statute explicitly stipulate that there is a geographic limitation to the powers of NCBs, if they act on behalf of the Eurosystem.

[72] For most of the following arguments see ECB, 'The role of the Eurosystem in payment and clearing Systems', *ECB Monthly Bulletin* (April 2002), 52, www.ecb.int/pub/pdf/mobu/mb200204en.pdf.

[73] See Bank for International Settlements, *Cross-border Securities Settlement* (Basle, 1995), 6. Also, in the Introduction of the CPSS/IOSCO Recommendations for securities settlement systems it is pointed out that 'securities settlement systems (SSSs) are a crucial component of the financial markets' and that 'weaknesses in SSSs can be a source of systemic disturbances to securities markets and to other payment and settlement systems'.

- real-time cross-system DVP in central bank money can only be achieved in a single integrated set-up and nobody but the Eurosystem as the sole statutory provider of euro central bank money is able to provide this service;
- the application of the term 'system' for payment systems as well as securities settlement systems in the Settlement Finality Directive.[74]

However, none of these arguments is convincing.[75] To begin with, 'clearing' is understood as a mechanism for transferring value in a particular way, usually by way of 'netting'. Strictly speaking, 'clearing' excludes the settlement phase as well as systems where no clearing is used, such as 'gross' settlement systems where value is transferred immediately via accounts held with the settlement agent. In addition, a large variety of clearing systems exist in the financial market infrastructure, but they are also used in many other (non-financial) areas of the economy. Put more generally, 'clearing' is not a specific feature of securities transfer systems. Second, even granting that Article 22 vests the ECB with the power to make Regulations in the Community law sense of the word,[76] the (purported) necessity for a uniform legal treatment of delivery versus payment systems cannot override the lack of a pertinent legal basis, but simply prevents the realization of a system which – and this is crucial in this context – is not mandated by the ESCB/ECB Statute. In addition, TARGET2-Securities has no bearing on the legal framework, i.e. the set of legal rules governing cross-border securities transactions. Third, the use of a word in secondary and (!) subsequent EU legislation does not allow any inference as to the meaning of the same word used in preceding primary EU law. Moreover, Article 22 explicitly qualifies the systems meant by adding the word 'payment'.

In order to refute these arguments, it is sometimes said that, because of the close functional relationship between payment systems and securities clearing and settlement systems, the ECB/euro-area NCBs will only be able to carry out the ESCB's task of contributing to the stability of the financial system (Article 3.3 ESCB/ECB Statute) to perfection if they have

[74] Directive 98/26/EC (note 9, above).

[75] As to the following, in the same sense, see C. Keller, Regulation of Payment Systems', *Euredia (*2002), 455, 460–3.

[76] Some authors even argue that the term 'clearing' in Art. 22 is not specific enough to grant any authority for taking measures to promote the operation of 'securities settlement and payment systems'; cf. A. von Bogdandy and J. Bast, 'Scope and Limits of ECB Powers in the Field of Securities Settlement', *Euredia* (2006), 365, 382.

also powers with respect to securities systems.[77] However, this argument neglects the distinction enshrined in Article 3 ESCB/ECB Statute between the ESCB's basic task of promoting the smooth operation of payments systems (Art. 3.1 fourth indent) and its more limited role of contributing to the stability of the financial systems (Article 3.3). Article 22 empowers the ECB and the euro-area NCBs 'to ensure efficient and sound clearing and payment systems', i.e. attributes authority only in regard of its basic task to promote the smooth operation of payment systems.

Finally, to clutch at straws, one may want to point to Article 2 (1) of the German statute implementing The Headquarters Agreement between the Government of the Federal Republic of Germany and the European Central Bank concerning the seat of the European Central Bank.[78] According to this provision, the ECB participates as the central depository for securities in the commercial intercourse of the CSDs. However, the agreement is not a binding interpretation of the EC Treaty or the ESCB/ECB Statute respectively. The regulation just shows that the Member State, Germany, acted on the assumption of an ECB authority for the settlement of securities transactions.

b. Designing TARGET2-Securities as a (facility for a) payment system Since Article 22 does not cover securities settlement systems as such, the ECB/euro-area NCBs would only be empowered to establish TARGET2-Securities if, at least given a certain design, the system would qualify as a facility for a payment system.

(i) The meaning of 'payment systems' in Article 22 is hardly ever spelled out in any detail. The ECB provides the following useful definition: 'a set of instruments, banking procedures and, typically, interbank funds transfer systems which facilitate the circulation of money'.[79] Put differently, payments systems combine legal regulations, technical norms and standards, and hardware for the primary goal of facilitating the transfer of money.[80]

[77] Smits and Gruber, 'Art. 22 ESCB Statute', in von der Groeben and Schwarze (eds.) (note 50, above), No. 21.

[78] Gesetz zu dem Abkommen vom 18 September 1998 zwischen der Regierung der Bundesrepublik Deutschland und der Europäischen Zentralbank über den Sitz der Europäischen Zentralbank, 19 December 1998, BGBl. II 1998, 2995.

[79] ECB, 'The role of the Eurosystem in payment and clearing Systems', *ECB Monthly Bulletin,* (April 2002), (note 72, above), 47.

[80] The term 'payment' contained in Art. 22 is thus not limited to its meaning in Art. 56 (2) EC, where payments constitute the consideration within the context of an underlying

(ii) Article 22 does not limit the power of the ECB/euro-area NCBs to provide facilities for payment systems of a particular design. Indeed, the wording to 'provide facilities' in order 'to ensure efficient and sound clearing and payment systems …' does not even require that the facility has to be part of a payment system.

Admittedly, existing payment systems, e.g. TARGET, do not interlink the transfer of payments and the corresponding transfer of securities. However, payment systems could also be designed to provide for 'contingent' payment messages by participants, i.e. messages to effectuate the cash transfer only on condition that the corresponding book entries in the participants' securities accounts have already been made or will, at least, be made simultaneously. The operator of such a payment system could even choose whether to allow orders to the effect that a payment is only to be made provided that the transfer of title with respect to the securities in question has taken effect or, less demanding on the operator, whether just to allow orders subject to the condition that the respective book entries have been made, regardless of their effect with respect to the ownership of the securities.

Regardless of the final design, for the ECB/euro-area NCBs to provide (facilities for) such a payment system would fall within the scope of Article 22. Clearly, such a system would contribute to the smooth operation of payments systems, at least with respect to linked payments/(cross-border/cross-CSD)securities transactions.

(iii) TARGET2-Securities lends itself to be designed as such a second-generation payment system[81] for at least two reasons. First, while CSDs would continue to serve as such and would still hold securities settlement accounts with one another, the ECB would not act as a CSD but would operate the technical platform for the clearing and settlement of the securities transactions taking place, including those between the CSDs. Second, the booking on a single technical platform would facilitate the interlinking of the settlement of the cash leg and the securities leg of a transaction. The design of TARGET2-Securities according to the increasingly common

transaction, but it also includes money transfers forming part of the 'movement of capital' in the sense of Art. 56 (2) EC; see von Bogdandy and Bast, 'Scope and Limits of ECB Powers in the Field of Securities Settlement', (note 76, above), 371.

[81] Likewise, the Legal Committee of the Eurosystem (Legal Feasibility Study (note 40, above), 2 (dating from 20 December 2006) states that 'T2S is conceived as a feature that supplements the operation of TARGET2,' i.e. a payment system.

model[82] for securities settlement systems – DVP, i.e. booking is only carried out after payment has been made – does not constitute a restriction, because what is envisaged is delivery-versus-payment model 1, which means settlement in real time of the cash leg of a securities transaction in central bank money alongside *simultaneous* settlement of the securities leg (a novelty for cross-system transfers which can only be provided through the active involvement of central banks as the sole supplier of central bank money). Thus, the delivery of securities takes place simultaneously with the payment and is – as a consequence – compatible with the model of a 'contingent' payment.[83]

(iv) It has been argued that Article 22 ESCB/ECB Statute can only serve as a legal basis for TARGET2-Securities if current securities settlement systems are either inefficient or unsound, but neither the wording of the regulation nor its intention justify such a restrictive interpretation. Both also cover actions by the ECB/euro-area NCBs destined to improve even further the workings of an already largely sound and efficient clearing and payment system as well as actions intended to prevent currently sound and efficient systems from becoming inefficient or unsound. However, even those who postulate this additional requirement come to the conclusion that it is met, due to the inefficiency of the current systems.

(v) The final question of whether Article 22 even empowers the ECB/euro-area NCBs to establish and operate the particular part of an IT platform where the booking of the securities is carried out can also be answered in the affirmative. This follows from the fact that the easiest, most effective and most secure way to promote the smooth operation of an Eurosystem payment system which allows for contingent payment orders, i.e. for the payment orders of CSDs to be executed on condition that the corresponding securities transaction has taken place or takes place simultaneously, is for the ECB/euro-area NCBs to operate a technical platform which allows the ECB/

[82] See Standard No. 7 of the ECB-CESR Standards for Securities Clearing and Settlement in the European Union (note 22, above).

[83] It could even be argued that a payment system permits payment messages on the condition that the corresponding book entries in the securities account will be made in the future. However, this conflicts with the principle of settlement finality since future cancellations of payments could be necessary.

euro-area NCBs to effectuate the book entries in the CSDs' securities accounts as well – exactly the gist of TARGET2-Securities.[84]

The upshot is that a legal basis for TARGET2-Securities can be derived from the term 'payment system' in Article 22 ESCB/ECB Statute having regard to the euro-area CBs' role as defined by Articles 105 (5) EC Treaty, Article 3.3 ESCB/ECB Statute.

8. Principle of subsidiarity pursuant to Article 5 (2) EC Treaty

Since Article 22 is a concurrent competence,[85] Article 5 (2) EC Treaty applies. Due to the regulation's transnational character, this requirement is not problematic.

9. Principle of competential proportionality pursuant to Article 5 (3) EC Treaty

According to the ECJ, the principle of competential proportionality is only violated by manifestly inapt measures, apparently erroneous evaluations or if it is obvious that a less encumbering measure proposed by the persons involved is equally effective,[86] which is not the case in this context.

V. Conclusion

The question whether the euro-area CBs, i.e., the ECB and the euro-area NCBs, have authority to develop TARGET2-Securities can be answered in the affirmative. The legal basis, which is required according to the principle of a limited transfer of powers from EU Member States to the ECB/euro-area NCBs, is furnished by Article 22 ESCB/ECB Statute having regard to the ECB's role, as defined by Articles 105 (5) EC Treaty, Article 3.3 ESCB/ECB Statute.

However, because of the limited competence of the Eurosystem under Art 22 ESCB/ECB Statute (referring only to facilities for payment and clearing systems) TARGET2-Securities should not constitute a facility

[84] However, as it has been argued correctly, this does not include the legal authority that would permit the ECB to constrain CSDs to use exclusively TARGET2-Securities.

[85] C. Eser, *Die Außenkompetenz Europäischen Zentralbank im Spannungsfeld zur Europäischen Gemeinschaft in der Endstufe der Wirtschafts- und Währungsunion* (Regensburg:, 2005), 134; Smits and Gruber, 'Art. 22 ESCB Statute', in von der Groeben and Schwarze (eds.) (note 50, above), No. 17.

[86] Case 280/93: *Germany v. Council ('Bananenmarktordnung')* ECR [1994] I-5039, para. 90 *et seq.*

for a securities settlement system, but should qualify as a variation or a feature ancillary to the operation of a payment system. This should be possible, because Article 22 ESCB/ECB Statute does not limit the euro-area CBs' power to provide facilities for payment systems of a particular design. Although existing payment systems do not interlink the transfer of payments and the corresponding transfer of securities, payment systems could also be designed to provide for 'contingent' payment messages by participants, i.e. messages to effectuate the cash transfer only on condition that the corresponding book entries in the participants' securities accounts have already been made or will be made simultaneously. Thus, the initial design of TARGET2-Securities as a mechanism enabling the delivery-versus-payment model 1, i.e. settlement in real time of the cash leg of a securities transaction in central bank money alongside simultaneous settlement of the securities leg, would fall within the ambit of Article 22 ESCB/ECB Statute. Alterations of and additions to the initial model are of no relevance as long as TARGET2-Securities will be a functionality that is ancillary and subordinate to the main operation of the Eurosystem, i.e. to the running of its payment system TARGET2. However, if TARGET2-Securities were to provide a comprehensive service to CSDs comprising the full post-trade production chain (similar to a 'Single Settlement Engine' as conceived by other market participants) this might be considered tantamount to a circumvention of Art 22 ESCB/ECB Statute. Given that, TARGET2-Securities should limit itself to a technical module allowing the coordination of book entries by the CSD and by the Eurosystem to ensure delivery versus payment (DvP). As a minimum, this would require TARGET2-Securities to take recourse to TARGET2 for the settlement of the cash legs. Otherwise, the required supportive character of TARGET2-Securities vis-à-vis TARGET2 would be in doubt.

SECTION 2

Transatlantic perspectives