



## DRAFT GUIDELINE ON PRECAUTIONARY FINANCIAL ASSISTANCE

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AGREED DRAFT

# **European Stability Mechanism**

## **Guideline on Precautionary Financial Assistance**

### **Article 1**

#### ***Aim and scope***

The objective of precautionary financial assistance is to support sound policies and prevent crisis situations by allowing ESM Members to secure the possibility to access ESM assistance before they face major difficulties raising funds in the capital markets. ESM precautionary financial assistance instruments provide support to ESM Members with sound economic fundamentals which could be affected by an adverse shock beyond their control.

### **Article 2**

#### ***Types of precautionary financial assistance***

1. Precautionary financial assistance may be provided via a Precautionary Conditioned Credit Line (PCCL) or via an Enhanced Conditions Credit Line (ECCL). A PCCL and an ECCL can be drawn via a loan or a primary market purchase. Both types of credit line shall have an initial availability period of one year and shall be renewable twice, each time for six months and based on the procedure in Article 3(9).
2. Access to a PCCL shall be based on eligibility criteria and limited to ESM Members where the economic and financial situation is fundamentally sound and whose government debt is sustainable. As a rule, ESM Members need to meet quantitative benchmarks and comply with qualitative conditions related to EU surveillance. An assessment shall be made on whether a potential beneficiary ESM Member qualifies for a PCCL on the basis of the criteria provided for in Annex III to the ESM Treaty:
  - (a) Respect of the quantitative fiscal benchmarks, as reported by the European Commission. The ESM Member shall not be under excessive deficit procedure and needs to meet the three following benchmarks in the two years preceding the request for precautionary financial assistance:
    - i. a general government deficit not exceeding 3 % of GDP,
    - ii. a general government structural budget balance at or above the country-specific minimum benchmark,<sup>1</sup>
    - iii. a debt benchmark consisting of a general government debt-to-GDP ratio below 60 % or a reduction in the differential with respect to 60 % over the previous two years at an average rate of one twentieth per year;

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<sup>1</sup> The minimum benchmark is the level of the structural balance providing a safety margin against the 3 % budget deficit to GDP threshold established by the EU Treaties under normal cyclical conditions. It is mainly used as one of three inputs into the calculation of the minimum MTO.

- (b) Absence of excessive imbalances, as assessed by the European Commission. The ESM Member should not be identified as experiencing excessive imbalances under EU surveillance;
  - (c) A track record of access to international capital markets, where relevant, on reasonable terms, as assessed by the Managing Director;
  - (d) A sustainable external position, as assessed by the European Commission; and
  - (e) Absence of severe financial sector vulnerabilities putting at risk the ESM Member's financial stability, as assessed by the relevant authorities under EU law.
3. The beneficiary ESM Member shall ensure a continuous respect of the eligibility criteria after the PCCL is granted, which shall be monitored in accordance with Article 5.
  4. In line with Article 14(1) of the ESM Treaty and Annex III to the ESM Treaty<sup>2</sup>, access to an ECCL shall be open to ESM Members that are not eligible to the PCCL because of non-compliance with some of the eligibility criteria but whose general economic and financial situation remains sound and whose government debt is sustainable. Subject to Article 13(3) of the ESM Treaty, the beneficiary ESM Member shall agree on an MoU detailing policy conditionality, aimed at addressing the remaining weaknesses, and requiring a continuous respect of the eligibility criteria which were considered met when the credit line was granted. The MoU shall be fully consistent with the measures of economic policy coordination provided for in the TFEU, including the Stability and Growth Pact. The respect of the MoU shall be monitored in accordance with Article 5.

### **Article 3**

#### ***Procedures for granting precautionary financial assistance***

1. An ESM Member may address a request for precautionary financial assistance to the Chairperson of the Board of Governors, indicating whether a PCCL or an ECCL is to be considered.<sup>3</sup> In the PCCL request (the Letter of Intent), the ESM Member shall commit to continuous compliance with the eligibility criteria provided for in Annex III of the ESM Treaty and referred to in Article 2 above, while highlighting the main elements of its policy intentions.
2. Before submitting a request for precautionary financial assistance, the ESM Member is invited to consult on a confidential basis with the Managing Director on its potential access to a PCCL or an ECCL. Such consultations will be carried out together with the Commission in liaison with the ECB, treating the ESM Member's interest in precautionary financial assistance as confidential.
3. On receipt of a request for precautionary financial assistance, in line with Article 13 of the ESM Treaty, both i) the Managing Director and ii) the European Commission in liaison with

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<sup>2</sup> Annex III refers to the term sheet on the reform of the ESM endorsed by the Euro Summit statement of 14 December 2018 specifying inter alia that "the ECCL instrument will continue to be available as foreseen in the current ESM guideline".

<sup>3</sup> This should be done taking into account Recital 8 of the ESM Treaty.

the ECB, shall be entrusted by the Chairperson of the Board of Governors to together discharge the following tasks:

- (a) to assess the existence of a risk to the financial stability of the euro area as a whole or of its Member States;
- (b) to assess whether general government debt is sustainable and whether, in case of a draw down, stability support can be repaid. Wherever appropriate and possible, such an assessment may be conducted together with the IMF;
- (c) to assess the actual or potential financing needs of the ESM Member concerned.

In addition, both i) the Managing Director and ii) the European Commission in liaison with the ECB, shall be requested to assess together, whether the ESM Member concerned meets the conditions for accessing a PCCL or an ECCL as set out in Article 2(2) and 2(4), respectively.

4. Moreover, the Chairperson of the Board of Governors shall entrust the European Commission with the task to assess whether the policy intentions included in the ESM Member's request for a PCCL are fully consistent with the measures of economic policy coordination provided for in the TFEU, in particular with any act of European Union law, including any opinion, warning, recommendation or decision addressed to the ESM Member concerned.
5. On the basis of the request of the ESM Member and the assessments referred to in paragraphs 3 and 4, the Managing Director shall prepare a proposal for financial assistance consistent with the aforementioned assessments and taking into account the financial situation of the ESM. On this basis and in accordance with Article 13(2) of the ESM Treaty, the Board of Governors may decide to grant, in principle, precautionary financial assistance to the ESM Member concerned in the form of a PCCL or an ECCL and approve its aggregate amount in accordance with Article 13(2) of the ESM Treaty.
6. If a decision is adopted pursuant to paragraph 5, the Board of Governors shall, in accordance with Article 13(3) of the ESM Treaty, entrust:
  - a. i) The Managing Director and ii) the European Commission in liaison with the ECB, together and, wherever possible, also together with the IMF, with the task of negotiating, with the ESM Member concerned, an MoU detailing the policy conditions attached to the ECCL, in line with Article 2(4). No MoU shall be negotiated in the case of a PCCL.
  - b. The Managing Director with the task of preparing, in parallel, a proposal for a financial assistance facility agreement (FFA), including the financial terms and conditions of the precautionary financial assistance, to be adopted by the Board of Governors. For the PCCL, these terms will include a proposed Maximum Maturity of not more than 5 years from the date of the first disbursement under the facility, considering the assessments set out in paragraph 3(b) and 3(c).

7. In case of an ECCL, the MoU shall be signed on behalf of the ESM by the European Commission and the Managing Director, subject to compliance with the conditions set out in paragraph 6(a) and approval by the Board of Governors.
8. The Managing Director shall sign the FFA, subject to approval by the Board of Directors.
9. Upon request from the ESM Member, based on a proposal by the Managing Director and an updated financing needs assessment conducted pursuant to paragraph 3(3)(c), subject to the beneficiary ESM Member's compliance with the conditionality attached to precautionary financial assistance, as assessed pursuant to Article 5(3), the Board of Governors may decide, by mutual agreement, to renew the credit line by extending its availability period. Extension of an ECCL shall require an updated MoU. The request for extension of the availability period should be submitted sufficiently in advance to allow its timely approval before the credit line expires.

#### **Article 4**

##### ***Activating a credit line***

1. The activation of the credit line shall be at the initiative of the beneficiary ESM Member. The ESM Member may request the draw-down of funds at any time during the availability period of the credit line according to the agreed terms. It shall inform the ESM at least five business days in advance of its intention to draw funds, depending on the intended size.
2. The maximum amount under a single disbursement shall be set in the FFA.

#### **Article 5**

##### ***Monitoring***

1. Both i) the Managing Director and ii) the European Commission in liaison with the ECB, together and, wherever possible, also together with the IMF, shall, in accordance with Article 13(7) of the ESM Treaty, be entrusted with monitoring compliance with the conditionality attached to the credit line.
2. The beneficiary ESM Member shall give its full cooperation to the institutions monitoring compliance pursuant to paragraph 1. It shall, in particular, provide all the information that the institutions deem necessary for the monitoring of conditionality and financial due diligence in a manner compatible with the applicable legal framework.
3. Both i) the Managing Director and ii) the European Commission in liaison with the ECB, shall be entrusted together with conducting periodic reviews to verify the beneficiary ESM Member's compliance with the conditionality attached to precautionary financial assistance. Where an ECCL is granted or a PCCL drawn, the review missions may in principle be combined with the enhanced surveillance missions under the EU legal framework.
4. The findings of the compliance reviews under paragraph 3 shall be reported to the Board of Directors. For a PCCL, a report shall verify continuous respect of the eligibility criteria as

specified in Article 2, whereas for an ECCL it shall verify compliance with the policy conditions detailed in the MoU. In case of non-compliance with the applicable conditionality, the compliance report shall assess the reasons for non-compliance and provide information for the BoD to decide whether the PCCL or the ECCL continues to be adequate taking into account the policy commitments provided by the ESM Member in the supplemental MoU or the amended IoI. The enhanced surveillance report by the European Commission may also be shared with the Board of Directors.

5. A report in accordance with paragraph 4 shall be submitted to the Board of Directors every three months for an ECCL and after a PCCL has been drawn, every six months for an undrawn PCCL and after the first drawing on the credit line.
6. In case the compliance report concludes that the ESM Member continues to respect the eligibility criteria for the PCCL or comply with the conditionality attached to the ECCL, the credit line shall be deemed to be maintained by the Board of Directors, unless the Managing Director or any Director requests a decision of the Board of Directors by mutual agreement whether the credit line should be maintained, in which case the Managing Director shall promptly convene the Board of Directors or solicit a vote without a meeting on the requested decision.
7. If the compliance report concludes that the ESM Member no longer respects the eligibility criteria for the PCCL, or no longer complies with the conditionality attached to the ECCL, access to the credit line shall be deemed to be discontinued by the Board of Directors, unless the Board of Directors decides by mutual agreement to maintain the credit line. For this purpose, the Managing Director shall promptly convene the Board of Directors or solicit a vote without a meeting on the decision. If the ESM Member has drawn funds under the credit line before the Board of Directors receives a report concluding that the ESM Member does not comply with the conditionality attached to the precautionary financial assistance, an additional margin shall apply, in line with the pricing guideline, unless the Board of Directors assesses on the basis of the report that non-compliance is due to events beyond the control of the ESM Member.

## **Article 6**

### ***Expiration and Cancellation***

1. A precautionary credit line expires at the end of the availability period, if the Board of Directors does not decide to maintain the credit line in accordance with Article 5(6) and (7), or if the undisbursed amounts have been cancelled by the beneficiary ESM Member in accordance with the terms specified in the FFA.
2. The ESM Member may address a new request for further ESM stability support, including in the form of a credit line or a loan.

**Article 7**

***Warning system***

The ESM shall establish an appropriate warning system, in accordance with Article 13(6) of the ESM Treaty, to ensure that the ESM receives any repayments due by the ESM Member under the stability support in a timely manner.

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