



UNIVERSITY OF AMSTERDAM



Amsterdam Centre for European Law and Governance

EMU Law **Professor René Smits**

23 September 2015

Principles and Foundations of European Union Law



Overview of the lecture

1. Basics: money, monetary unions, terms
2. Place of EMU law in EU law
3. Three elements and three stages of EMU
4. Economic policy coordination
5. Monetary policy
6. Banking Union
7. Outlook



1.A What is money?

- Store of value
- Means of payment
- Standard of account





1.B Money

- Official currencies: issued by central banks, legal tender status
- Parallel currencies: US dollar, Euro in third countries
- Bitcoin, local currencies (Sardex)



1.C What is the euro?

- Single currency of the EU (Euro Area), replacing legacy currencies (guilder, drachma, Deutschmark, French franc, etc.)
- A currency of its own, not deriving its value from other currencies
(like predecessor ECU, or IMF's SDR)
- 'Legal tender' (*wettig betaalmiddel, cours légal*) in 19 EU States
- Cash & banknotes versus bank [book] money (demand deposits)
(*monnaie scripturale, Unbarer Zahlungsverkehr, giraal geld*)



1.D What is 'monetary policy'?

- The set of measures by which a central bank influences money supply and interest rates in the economy

Objective:

- **ESCB**: 1) price stability 2) support of economic policies in EU (Euro Area)
 - **US Federal Reserve System**: maximum employment, stable prices, moderate long-term interest rates
 - **Swiss National Bank**: serving country as a whole
- TFEU does not define 'monetary' or 'economic policy'



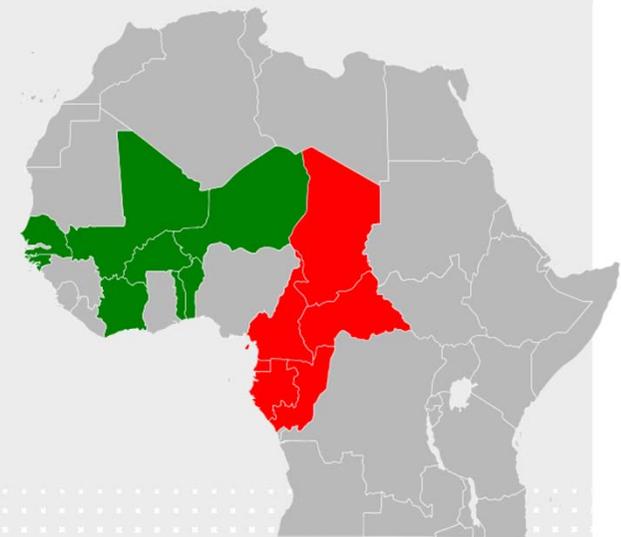
1.E What is ‘economic policy’?

- Everything else in terms of government (public) action affecting the economy
- Government (or EU institutions), not central bank actor
- TFEU does not define ‘monetary’ or ‘economic policy’
- ECJ in *Pringle Case* (ESM Treaty) does (to some extent) so by referring to the *objectives* of monetary policy and distinguishing these from those of economic policy, and then looking at monetary policy *instruments* (financial assistance is not a monetary policy instrument)

Case C-370/12 (*Pringle*), judgment of 27 November 2012

1.F Monetary unions

- EMU in EU
- CFA franc: West-African and Central-African currency unions with CFA franc linked to euro
- East African Community: Protocol signed 2013
- Pan-African monetary union: 2028
- Eastern Caribbean Currency Union





2. Place of EMU law in EU law

- ‘Traditionally’: full integration in EU law (primary, secondary)
- Since crises (GFC, euro area crisis): alternative legal basis – public international law, closely aligned with EU law: TSCG, or: Fiscal Compact Treaty; ESM Treaty, SRF Treaty // even private law: EFSF (Luxembourg law, English law)



3. Three elements and three stages of EMU

Three elements:

- Capital & Payments (63-66 and 75 TFEU, Protocol DK)
- Economic Union (120-126, 136-137 TFEU, Protocols)
- Monetary Union (127-135, 138, 219 TFEU, Protocols)

NB Institutional (134-135; 282-284 TFEU) & transitional (139-144 TFEU) provisions

Three stages:

- 1) Stage One (1990-1993) EEC Treaty applied
- 2) Stage 2 (1994-1999) EC Treaty amended in Maastricht applied
- 3) Stage 3 (1999-now) EC Treaty as amended by Lisbon Treaty: TFEU



4.A Economic policy coordination

- Neither exclusive, nor shared: Article 5 TFEU
- Coordination among Member States in Ecofin
- Plus Euro Group (and Euro Working Group)
- New economic governance competences



Jeroen Dijsselbloem
President, Euro Group



Valdis Dombrovskis
(Euro, Social Dialogue)



Pierre Moscovici
Economic and
Financial Affairs,
Taxation and Customs



4.B Economic policy coordination

Article 119 (1) TFEU:

“(...) the activities of the Member States and the Union shall include, as provided in the Treaties, the adoption of an economic policy which is based on the close coordination of Member States’ economic policies, on the internal market and on the definition of common objectives, and conducted in accordance with the principle of an open market economy with free competition.”

Article 119 (3) TFEU :

“These activities of the Member States and the Union shall entail compliance with the following guiding principles: stable prices, sound public finances and monetary conditions and a sustainable balance of payments. ”



4.C Economic policy coordination

Article 120 TFEU:

Member States shall conduct their economic policies **with a view to contributing to the achievement of the objectives of the Union**, as defined in Article 3 of the Treaty on European Union, and in the context of the **broad guidelines** referred to in Article 121(2). The Member States and the Union shall act **in accordance with the principle of an open market economy with free competition, favouring an efficient allocation of resources**, and in compliance with the principles set out in Article 119 ”



4.D Economic policy coordination

Article 121 TFEU:

- “Member States shall regard their economic policies as a matter of common concern and shall coordinate them within the Council, in accordance with the provisions of Article 120”
- BEPGs: draft by Ecofin Council – on Commission recommendation – to European Council
- European Council discusses draft – Ecofin adopts
- Commission monitors – Council recommends



4.E Recommendation vs. proposal

Article 293 TFEU:

1. “Where, pursuant to the Treaties, the Council acts on a **proposal** from the Commission, it may amend that proposal **only by acting unanimously**, except in (...)”
2. “As long as the Council has not acted, the Commission may alter its proposal at any time during the procedures leading to the adoption of a Union act.”



4.F Economic union: prohibitions

- Prohibition of monetary financing (Article 123)
- Prohibition of privileged access (Article 124)
- 'No bail-out' clause (Article 125)



4.G Coordination / economic policy

- **Multilateral surveillance procedure – Broad Economic Policy Guidelines** (BEPGs) (Art. 121 TFEU) // Employment Guidelines (Art. 148 TFEU)
- **Excessive deficit procedure** (Art. 126 TFEU)
- **Specific coordination among € area States** (Art. 136 TFEU - new since 'Lisbon')
- **Own economic policy measures of the EU and EU financial assistance to Member States** (basis for strategic reserves of oil and gas) (Art. 122 TFEU)



4.H Stability & Growth Pact

- Comes on top of TFEU coordination requirements
- Based on resolution and secondary legislation
- Introduced in 1997, amended in 2005, again in 2011
- Instead of avoidance of excessive budget deficits: over medium time, budgetary balance or surplus: MTBO for each Member State
- Annual Stability / Convergence Programmes to be submitted
- Sanctions (Article 126(11) TFEU): fines, periodic penalty payments

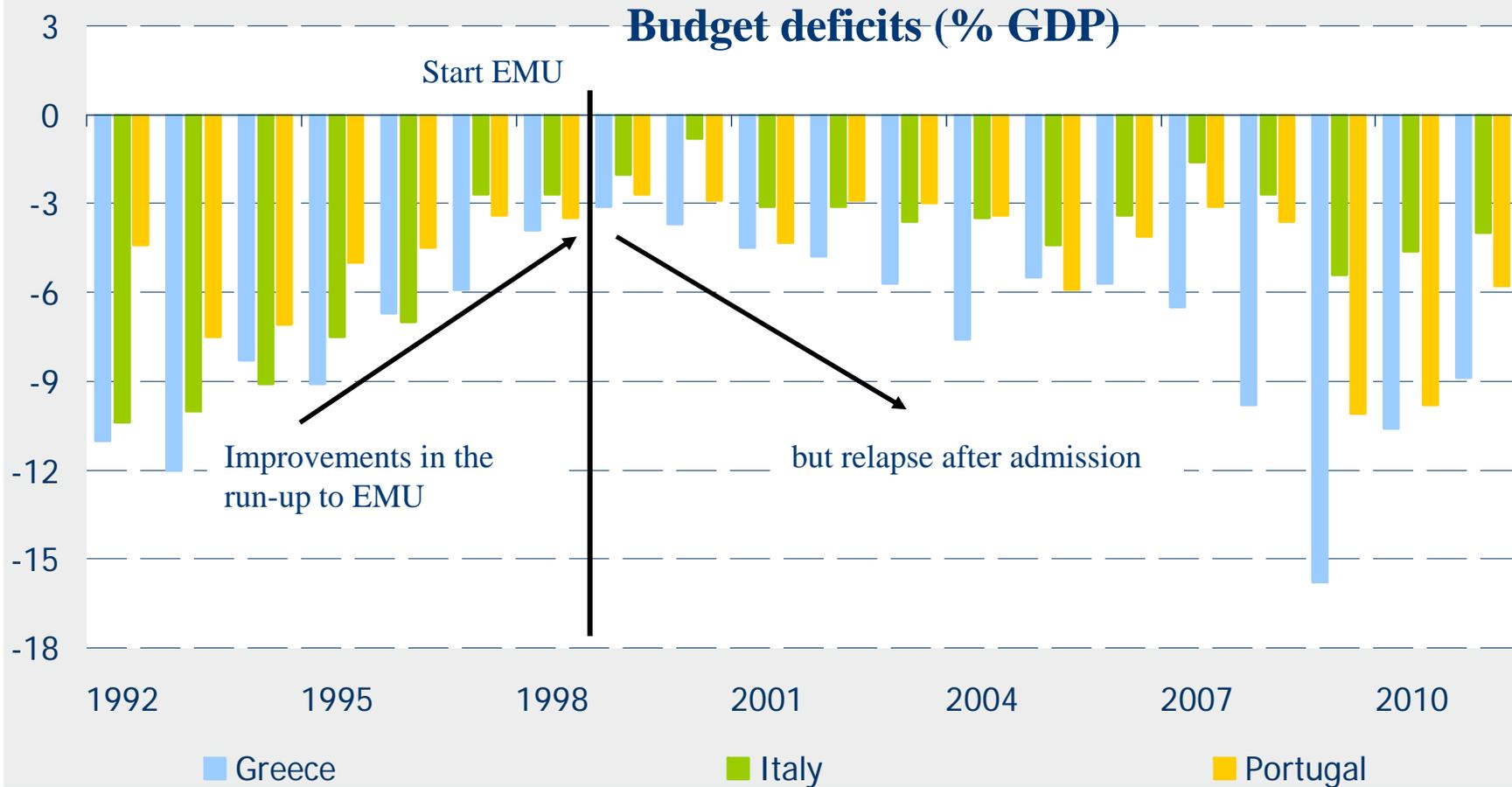


4.1 Sovereign debt *cum* banking crisis

- First ten years of EMU: markets hardly distinguished between sovereign risk of Germany or Greece: ‘spreads’ over ‘*Bunds*’ were minimal
- After Lehman collapse, spreads started to rise
- After George Papandreou acknowledged gap in Greek budget (twice as large): rates spiked
- ‘Contagion effect’: other Member States affected, as well
- Since then, fear, speculation and distrust in solution capacities policy makers
- E(M)U’s weaknesses stand exposed before market

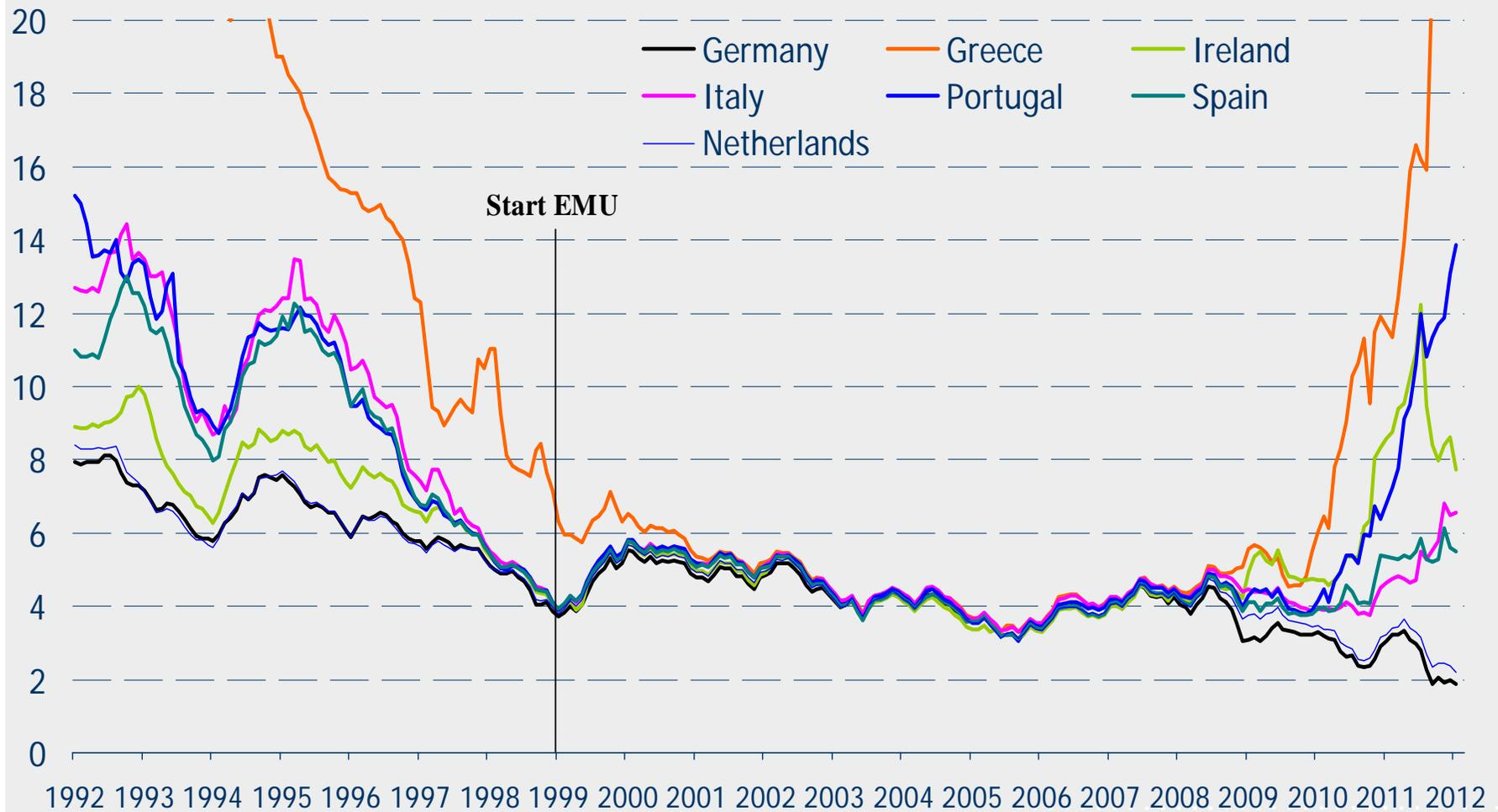


Governments went back to old habits





“On/off” market discipline





Previous slides from: The Eurozone Crisis: Causes and Solutions

Klaas Knot
President, De Nederlandsche Bank

Asia Society, Hongkong
15 October 2012



4.J Economic governance strengthening: main elements

- ‘European Semester’: aligned budgetary cycle
- ‘Six-pack’: reinforcing Stability & Growth Pact, introducing Excessive Imbalances Procedure, strengthening Member States’ budgetary frameworks
- ‘Two-pack’: draft budgets monitored by Commission; ‘enhanced surveillance’ for Member State in difficulties
- Fiscal Compact Treaty (TSCG): balanced budget rules



4.K Economic governance strengthening: approach

- Disciplinary and contentious approach
- Sanctions strengthened and brought forward
(earlier phase of EDP/SGP application, EIP, statistical fraud)
- Practice: flexibility
(Making the best use of the flexibility within the existing rules of the Stability & Growth Pact, COM(2015) 12 final, 13 January 2015)
- Practice: incisive policy prescriptions through conditionality for 'programme States' (Greece)

ECB President Mario Draghi, London, 26 July 2012:

- “**Within our mandate**, the ECB is ready to do whatever it takes to preserve the euro.
And believe me, it will be enough.”
- “To the extent that the size of these sovereign premia hampers the functioning of the monetary policy transmission channel, they come within our mandate.”





5.A ESCB

- ESCB = ECB + NCBs // Eurosystem = ECB + 'in' NCBs

- **Objectives:**

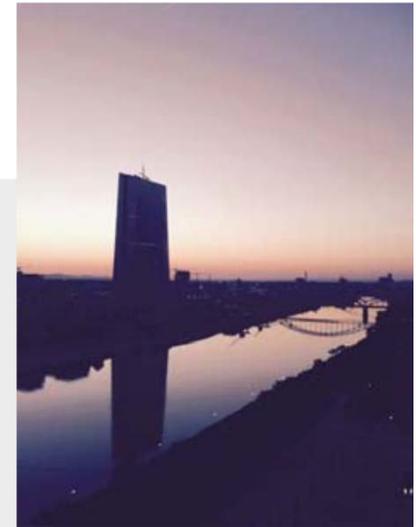
- price stability (primary)
- support of the general economic policies in the Union (secondary)

- **Main tasks:**

1. - to define and implement the monetary policy of the Union
2. - to conduct foreign exchange operations consistent with Article 219 TFEU
3. - to hold and manage the official foreign reserves of the Member States
4. - to promote the smooth operation of payment systems

- **Other tasks:**

5. - consultation on draft EC and national legislation
6. - issue of bank notes
7. - authorization of issue of coins
8. - 'contribute to the smooth conduct of policies pursued by the competent authorities relating to the prudential supervision of credit institutions and the stability of the financial system'
9. - statistical functions
10. - possible own supervisory task





5.B Independence

- ‘...neither the ECB, nor a national central bank, nor any member of their decision-making bodies shall seek or take instructions from Community institutions or bodies, from any government of a Member State or from any other body...’. [Article 130 TFEU and Article 7 ESCB Statute]
- **Institutional independence**
- **Personal independence**
- **Functional independence**
- **Financial independence**



5.C Accountability

■ **Mutual representation in decision making bodies**

ECOFIN Council President and a member of the Commission may participate in the Governing Council and General Council meetings. No right to vote. Only the ECOFIN Council President may submit a motion for deliberation to the Governing Council [Article 284(1) TFEU, Article 45(2) ESCB Statute] // Participation of the ECB President in ECOFIN Council meetings [Article 284(2) TFEU]

■ **Appearance before the European Parliament**

ECB President and other members of Executive Board can be heard before the European Parliament, at the request of the EP [Article 284(3) TFEU]; ECB President is to present the annual report to the European Parliament (as well as to the ECOFIN Council)

■ **Judicial control**

The acts or omissions of the ECB are subject to judicial control by the ECJ [Article 35 ESCB Statute and relevant provisions of TFEU]

■ **Specific attribution of powers**

ESCB is subject to the principle specific attribution of powers or conferral [Article 5 TEU]

■ **Reporting requirements**

Reporting through periodic publications [Article 284(3) TFEU and Article 15 ESCB Statute]



5.D Monetary policy (1)

- Conventional and unconventional methods (largely based on Article 18 ESCB Statute)
- Negative interest rates
- Widening of collateral
- Lending in foreign currencies
- Long-Term Refinancing Operations (LTROs)
- *Targeted* LTROs (T-LTROs): inexpensive funding to banks on condition of on-lending to private sector
- Forward guidance and transparency



5.E Monetary policy (2)

- Bond purchasing programmes: Securities Market Programme (SMP), Covered Bonds Purchasing Programme (CBPP), Asset-Backed Securities Purchase Programme (ABSPP)
- Quantitative Easing (QE): Expanded Asset Purchase Programme (“adds the purchase programme for public sector securities to the existing private sector asset purchase programmes to address the risks of a too prolonged period of low inflation. It consists of CBPP3, ABSPP, and Public Sector Purchase Programme (PSPP)”)
- Rationale behind QE: pushing inflation back to below but close to 2% per annum and taking assets for investment out of the market, so that banks will look for other lucrative investments: loans to private sector



5.F Monetary policy (3)

- Outright Monetary Transactions (OMTs)
- Announced September 2012, legal acts prepared not adopted
- ECB announcement: “outright transactions in secondary sovereign bond markets that aim at safeguarding an appropriate monetary policy transmission and the singleness of the monetary policy” // “A necessary condition for Outright Monetary Transactions is strict and effective conditionality attached to an appropriate European Financial Stability Facility/European Stability Mechanism (EFSF/ESM) programme.” // “The Governing Council will consider [OMTs] to the extent that they are warranted from a monetary policy perspective as long as programme conditionality is fully respected, and terminate them once their objectives are achieved or when there is non-compliance with the macroeconomic adjustment or precautionary programme.”



5.G Monetary policy (4)



- Challenge before German Constitutional Court
- Reference to CJEU, with clear indication of BVerfG views (OMTs incompatible with EU law)
- AG: discretion ECB “The Courts, when reviewing the ECB’s activity, must therefore avoid the risk of supplanting the Bank, by venturing into a highly technical terrain in which it is necessary to have an expertise and experience which, according to the Treaties, devolves solely upon the ECB”
- Court: ECB determines which instruments to employ in interest of price stability objective



5.H Gauweiler quotes (1): transmission argument

“The ability of the ESCB to influence price developments by means of its monetary policy decisions in fact depends, to a great extent, on the transmission of the ‘impulses’ which the ESCB sends out across the money market to the various sectors of the economy. Consequently, if the monetary policy transmission mechanism is disrupted, that is likely to render the ESCB’s decisions ineffective in a part of the euro area and, accordingly, to undermine the singleness of monetary policy. Moreover, since disruption of the transmission mechanism undermines the effectiveness of the measures adopted by the ESCB, that necessarily affects the ESCB’s ability to guarantee price stability. Accordingly, measures that are intended to preserve that transmission mechanism may be regarded as pertaining to the primary objective laid down in Article 127(1) TFEU. The fact that a programme such as that announced in the press release might also be capable of contributing to the stability of the euro area, which is a matter of economic policy (see Pringle, para. 56), does not call that assessment into question. Indeed, a monetary policy measure cannot be treated as equivalent to an economic policy measure merely because it may have indirect effects on the stability of the euro area (see, by analogy, Pringle, para. 56).”



5.1 Gauweiler quotes (2): selectivity of OMT

“As regards the selective nature of the programme announced in the press release, it should be borne in mind that the programme is intended to rectify the disruption to the monetary policy transmission mechanism caused by the specific situation of government bonds issued by certain Member States. In those circumstances, the mere fact that the programme is specifically limited to those government bonds is thus not of a nature to imply, of itself, that the instruments used by the ESCB fall outside the realm of monetary policy. ”



5.J Gauweiler quotes (3): OMT are not economic policy measure

“It is, of course, possible that a government bond-buying programme may, indirectly, increase the impetus to comply with those adjustment programmes and thus, to some extent, further the economic-policy objectives of those programmes. However, such indirect effects do not mean that such a programme must be treated as equivalent to an economic policy measure, since it is apparent from Articles 119(2) TFEU, 127(1) TFEU and 282(2) TFEU that, without prejudice to the objective of price stability, the ESCB is to support the general economic policies in the Union. ”

“(…) the fact that the purchase of government bonds on the secondary market subject to a condition of compliance with a macroeconomic adjustment programme could be regarded as falling within economic policy when the purchase is undertaken by the ESM (see Pringle, para. 60) does not mean that this should equally be the case when that instrument is used by the ESCB in the framework of a programme such as that announced in the press release. ”



5.K Gauweiler quotes (4): adequate reasoning and proportionality

- “(...) explanations provided by the ECB that the programme is based on an analysis of the economic situation of the euro area, according to which, at the date of the programme’s announcement, interest rates on the government bonds of various States of the euro area were characterised by high volatility and extreme spreads. According to the ECB, those spreads were not accounted for solely by macroeconomic differences between the States concerned but were caused, in part, by the demand for excessive risk premia for the bonds issued by certain Member States, such premia being intended to guard against the risk of a break-up of the euro area. // that special situation severely undermined the ESCB’s monetary policy transmission mechanism in that it gave rise to fragmentation as regards bank refinancing conditions and credit costs, which greatly limited the effects of the impulses transmitted by the ESCB to the economy in a significant part of the euro area” // [no] manifest error of assessment.” // “a programme such as that announced in the press release does not infringe the principle of proportionality”

6. A 'Banking union': overview

- 'Banking union' = joint supervision by ECB and NCAs with ECB in the lead, plus EU-level resolution of banks, single rule book and deposit insurance; hence:
 - ✓ Single Supervisory Mechanism (ECB + NCAs) – Regulation 1024/2013
 - ✓ Single Resolution Mechanism – Regulation 806/2014 (and Agreement on the Single Resolution Fund [mutualisation of banks' own contribution to resolution])
 - ✓ Single rulebook: CRR 575/2013 and CRD IV 2013/36 (+ BRRD, FICOD ...)
 - ❑ Harmonised deposit insurance: Deposit Guarantee Directive 2014/49



6.B ‘Banking union’: rationale

- Rationale: breaking sovereign doom loop
- Euro Area Summit, 29 June 2012: “We affirm that it is imperative to break the vicious circle between banks and sovereigns.”

https://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ec/131359.pdf

- Backtracking - Joint Statement of the Ministers of Finance of Germany, the Netherlands and Finland, 25 September 2012:
“the ESM can take direct responsibility of problems that occur under the new supervision, **but legacy assets should be under the responsibility of national authorities**”

https://www.eerstekamer.nl/eu/overig/20121001/gezamenlijke_verklaring_van_de/document

6.C 'Banking union': SSM = ECB + NCAs

- Based on SSM Regulation (1024/2013)
- ECB's role in banking supervision in Euro Area:
 - direct and full for 123 significant banks / banking groups
List: https://www.bankingsupervision.europa.eu/ecb/pub/pdf/list_sse_lsi.en.pdf?7cfe8aed9fcde86121744f574159bd25
 - direct and limited (licensing and authorisation of shareholders) for all banks
 - indirect for all banks
- See, also: SSM Framework Regulation (468/2014; ECB/2014/17)



Supervisory Board, new ECB organ



6.D ECB supervisory powers (1)

Article 1 Regulation 1024/2013 (SSM Regulation):

This Regulation confers on the ECB **specific tasks** concerning **policies relating to the prudential supervision of credit institutions**, with a view to contributing to **the safety and soundness** of credit institutions and **the stability of the financial system** within the Union and each Member State, with full regard and duty of care for the unity and integrity of the internal market based on equal treatment of credit institutions with a view to preventing regulatory arbitrage.



6.E ECB supervisory powers (2)

Articles 4, 5 and 6 Regulation 1024/2013 (SSM Regulation)

- ❑ ECB directly supervises significant banks (Art. 6(5)); NCAs other banks (Art. 6(6))
- ❑ ECB authorises all banks and shareholders in all banks (Art. 4(1) (a) and (c); Arts. 14, 15)
- ❑ ECB responsible for effective and consistent functioning of SSM (Art. 6(1))
- ❑ ECB issues regulations, guidelines, general instructions to NCAs (Art. 6(5) (a))
- ❑ ECB may decide to directly supervise NCA-supervised banks (Art. 6(5) (b))
- ❑ ECB exercises oversight over the functioning of the SSM (Art. 6(5) (c))
- ❑ ECB always has direct investigative powers (Art. 6(5) (d), Arts. 10-13)
- ❑ ECB may request NCAs ad hoc or continuous information (Art. 6(5) (e))
- ❑ ECB issues Framework Regulation setting out SSM functioning (Art. 6(7))
- ❑ ECB may directly apply macro-prudential tools (Art. 5(2))

6.F NCA powers

- ❑ Direct supervision of non-significant banks (Art. 6(6))
- ❑ National-law derived powers of information gathering and on-site inspection (Art. 6(6))
- ❑ Preparation of decisions on authorisation of banks and shareholders (Arts. 14 and 15)
- ❑ Application of macro-prudential tools (Art. 5(1))
- ❑ All in close cooperation with ECB, with prior submission of material supervisory decisions
- ❑ Other supervision, i.e. not mandated to ECB/SSM





6.G Supervisory Board

- New organ of the ECB, introduced by Article 26 SSM Regulation
- Chair and Vice-Chair, 4 ECB representatives and NCAs from 19 States
- Vice-Chair is also Executive Board Member and,

as such, member of the
Governing Council



SB prepares supervisory decisions
for Governing Council
'no objection' procedure
< *Danièle Nouy, Chair*
Sabine Lautenschläger, Vice-Chair >



6.H Transparency and accountability

- Far-reaching accountability mechanisms in MoU with Ecofin Council and Interinstitutional Agreement with EP
- Due respect for professional secrecy and business secrets
- Chair-to-Chair confidential oral discussions behind closed doors
- EP gets “a comprehensive and meaningful record of the proceedings of the Supervisory Board that enables an understanding of the discussions, including an annotated list of decisions” and GC objections to SB draft decisions to be reported
- Cooperation with a Parliamentary inquiry regulated in advance



Accountability breeds
response-ability.

- Stephen R. Covey





6.I 'Banking union' accountability arrangements (1)

ECB-EP Interinstitutional Agreement

- “the conferral of supervisory tasks implies a significant responsibility for the ECB to contribute to financial stability in the Union, using its supervisory powers in the most effective and proportionate way”
- “any conferral of supervisory powers to the Union level should be balanced by appropriate accountability requirements” EP and Council “legitimised institutions representing the citizens of the Union and the Member States”
- Specification of reporting requirements
- Information hotline and FAQs at ECB with feedback of questions on SSM
- Specification of public and confidential hearings before EP
- Specification of responding to EP questions
- Confidentiality requirements for confidential information
- Safeguards for confidentiality of ECB documents
- Cooperation of ECB with EP Investigations ('Committee of Inquiry')
- Involvement in selection and appointment Supervisory Board and removal of Chair or Vice-Chair Supervisory Board (Article 26(4) SSM Regulation)



6.J ‘Banking union’ accountability arrangements (2)

ECB-(Ecofin) Council MoU

- “the conferral of supervisory tasks implies a significant responsibility for the ECB to contribute to financial stability in the Union, using its supervisory powers in the most effective and proportionate way”
- “any conferral of supervisory powers to the Union level should be balanced by appropriate accountability requirements”: EP and Council “legitimised institutions representing the citizens of the Union and the Member States”
- Covers accountability to Ecofin Council and Euro Group
- Similar reporting requirements as vis-à-vis the EP, plus some extra’s
- Specification of responding to Euro Group questions
- Confidentiality of ECB documents
- Involvement in selection and appointment Supervisory Board and removal of Chair or Vice-Chair Supervisory Board (Article 26(4) SSM Regulation)



6.K

LOLR = ELA

- Lender of Last Resort assistance (LOLR)
- Emergency Liquidity Assistance (ELA):
 - providing liquidity support
 - in exceptional circumstances
 - to a temporarily
 - illiquid
 - credit institution (CA)
 - which cannot obtain liquidity through either the market or participation in monetary policy operations
- *ECB Monthly Bulletin*, February 2007, pp. 73-84
“The EU arrangements for financial crisis management”
- Plus: provision of liquidity to sector as a whole



6. L ELA under ESCB responsibilities

- “private sector solution is preferable whenever possible”
- “the provision of ELA is within the discretion of the national central bank, which will consider the relevant factors that may justify the access to this lending of last resort” (‘constructive ambiguity’)
- “the Eurosystem also has procedures in place regarding the provision of ELA to individual credit institutions in the euro area, which are under the responsibility of the national central banks (NCBs)”
- *ECB Monthly Bulletin, February 2007*

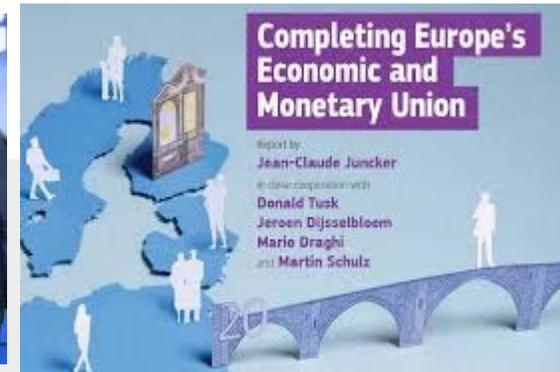


ECB's ELA Procedures 17 October 2013

The **procedures** underlying the Governing Council's role pursuant to Article 14.4 of the Statute of the European System of Central Banks and of the European Central Bank with regard to the provision of ELA to individual credit institutions

At:

https://www.ecb.europa.eu/pub/pdf/other/201402_elaprocedures.en.pdf?e716d1d560392b10142724f50c6bf66a



7. Outlook

- Banking union third element: single deposit insurance
- [Five Presidents' Report](#)
- Eurobills, Eurobonds - Euro Area Treasury
- Partial EU-funding of national unemployment benefits so that automatic stabilisers work across the Euro Area ([Glienicker Gruppe](#))
- Various crises: avoided Grexit, refugees, imminent Brexit?
- Cultural aspect of European integration (language [labour market], media space, European people)