

Variable Geometry and the European Central Bank: How the ECB Can Assert Itself Against Attacks From Member States with Derogations

INTRODUCTION

Following World War II, European leaders undertook several economic and political initiatives in an attempt to create a stable economic environment, as well as to fill the political power vacuum between East and West.¹ Specifically, “the architects of the European Community (EC) sought to create on the historically fragmented continent of Europe an integrated economic market that would afford enterprise the benefits of harmonization and economies of scale, while bringing to the population as a whole a higher living standard.”²

Since the establishment in 1952 of the European Coal and Steel Community, the precursor to the present European Union (EU), the process of economic, legal and political integration has achieved extraordinary results.³ From a group of six states promoting free trade in the coal and steel sectors, the entity has grown into a union of fifteen members active in economic, political, social and cultural spheres.⁴ Despite the progress thus far, full integration, as desired by the original architects, will never be realized without a complete monetary union and a centralized monetary policy.

¹ See GEORGE A. BERMANN ET AL., CASES AND MATERIALS ON EUROPEAN COMMUNITY LAW 3 (1993). The first of these initiatives was a Benelux customs union among Belgium, the Netherlands and Luxembourg. See *id.* The Benelux Customs Convention became effective in 1948 and led ten years later to the creation of a common trading area. See *id.*

² *Id.* at 2. The European Community (EC) became the European Union (EU) when the Treaty on European Union, otherwise known as the Maastricht Treaty, came into force in November, 1993. See TREATY ESTABLISHING THE EUROPEAN COMMUNITY, Feb. 7, 1992, O.J. (C 224) 1 (1992), 31 I.L.M. 247 [hereinafter EC TREATY].

³ See BERMANN, *supra* note 1, at 2.

⁴ See *id.* The Treaty of Paris of April 18, 1951, establishing the European Coal and Steel Community, was signed by the three Benelux countries, France, Germany and Italy, and entered into force on July 25, 1952. See *id.* at 5.

In light of the objective of a complete monetary union, a revision of the Treaty of Rome was adopted in December, 1991 by the European Heads of State and Government meeting in Maastricht.⁵ The revision makes the European Monetary Union (EMU) one of the official goals of the Community, devises a strategy to achieve it and lays out the institutional framework by which EMU will be regulated.⁶ At the crux of monetary union lies the European Central Bank (ECB), the entity charged with maintaining price stability and general monetary order.⁷ The Delors Committee, a group composed of all EC central bank governors plus three outside experts, aptly stated that "a new monetary institution would be needed because a single monetary policy cannot result from independent decisions and actions by different central banks."⁸ Yet, the process of establishing a European central bank is not without impediments.

Because of the stringent deadline for creation of the third stage of monetary union and establishment of the ECB, it is conceivable that a majority of the Member States will be left out of the institutional structure.⁹ If this were the case, it is also conceivable that these Member States, via the Council of Ministers, would adopt legislation contrary to the prerogatives of the ECB.¹⁰ If this were to happen, the ECB would need to assert itself against such hostile attacks from Member States with derogations.¹¹

Part I of this note will discuss the framework for formation of the EMU. Part II will discuss the process by which the Council of Ministers will assess the convergence criteria of the Member States and the

⁵ See MICHELLE FRATIANNI ET AL., *THE MAASTRICHT WAY TO EMU* 1 (1992).

⁶ See *id.*

⁷ Protocol on the Statute of the European System of Central Banks and of the European Central Bank, Feb. 7, 1992, art. 2, 31 I.L.M. 331 [hereinafter Protocol].

⁸ FRATIANNI ET AL., *supra* note 5, at 3.

⁹ See EC TREATY art. 109j(3), (4).

¹⁰ See *id.* The Council is the collective head of state of the European Union, deciding external trade policies and concluding international agreements. See BERMANN, *supra* note 1, at 51. It also exercises primary legislative power within the Union. See *id.* The Council consists of representatives of Member State governments, voting in the name of their State with a voting strength crudely weighted according to the State's relative population size. See *id.* The Council thus resembles a head of state in status, a legislature in function and an assembly of constituent states in structure. See *id.*

¹¹ See EC TREATY art. 109j(3), (4). Member States which do not fulfill the entry criteria or are not politically minded to join the EMU will be given a derogation. See *id.* art. 109k(1). The Treaty states that a Member State with a derogation as well as that state's national central bank will be excluded from certain rights and obligations which arise from membership in the ESCB. See *id.* art. 109k(3).

transition to the third stage of EMU. Part III will address the governance of the European System of Central Banks (ESCB) and the ECB. Part IV will evaluate the objectives, functions and independence of the ESCB and the ECB. Finally, Part V will discuss how the ECB can assert itself against attack from Member States with derogations.

I. BACKGROUND

A. *The Framework for the Formation of the European Monetary Union*

In the spring of 1989, the Delors Committee, composed of all EC central bank governors plus three outside experts, issued a report on a three-stage approach for the creation of the EMU.¹² The report recommended that economic and monetary union be achieved by a single process of development with three distinct stages.¹³ As the Delors Report envisaged, the first stage began on July 1, 1990.¹⁴ This stage included the increased coordination of monetary and economic policies among the Member States and the strengthening and standardization of the existing European Monetary System (EMS).¹⁵ Furthermore, Member States abolished all restrictions on the movement of capital between Member States and between Member States and third party countries.¹⁶

The second stage, which began on January 1, 1994, is a transitional stage intended to facilitate the eventual move to a common currency, the creation of a central bank and the implementation of a uniform monetary policy.¹⁷ The most important feature of this stage has been the establishment of the predecessor to the ECB, the European Mone-

¹² See JOHN B. GOODMAN, *MONETARY SOVEREIGNTY: THE POLITICS OF CENTRAL BANKING IN WESTERN EUROPE* 203 (1992).

¹³ See Coopers & Lybrand, *EC Commentaries, Economic and Monetary Union*, Aug. 15, 1995, at *4.2, available in LEXIS, World Library, Allnws File [hereinafter Coopers & Lybrand].

¹⁴ See DANIEL GROS & NIELS THYGESEN, *EUROPEAN MONETARY INTEGRATION* 344 (1992).

¹⁵ See Coopers & Lybrand, *supra* note 13, at *4.2. The EMS was established in 1978 as a direct response by the EC to the problems posed by the increasing instability of the dollar following the breakdown of the Bretton Woods system and the two oil shocks of the 1970s. See *id.* The primary goals of the EMS are to achieve a greater measure of monetary stability in the Community and to serve as an intermediate step towards monetary unification. See Marcello de Cecco & Alberto Giovannini, *Does Europe Need Its Own Central Bank?*, in *A EUROPEAN CENTRAL BANK? PERSPECTIVES ON MONETARY UNIFICATION AFTER TEN YEARS OF THE EMS* 1, 2 (Marcello de Cecco & Alberto Giovannini eds., 1989).

¹⁶ See Christopher A. Whytock, *Eurofed: Toward a European System of Central Banks and a European Central Bank*, available in WESTLAW, database JLR.

¹⁷ See EC TREATY art. 109c; RALPH J. MEHNERT, *USER'S GUIDE TO THE ECU* 16 (1992).

tary Institute (EMI), which will prepare for the third stage.¹⁸ The EMI, located in Frankfurt, serves to facilitate the transition to the third stage by advising EU institutions such as the Council and the Commission, and by generally assisting the individual Member States in their preparation for the third stage.¹⁹ The EMI has undertaken the creation of the regulatory, organizational and logistical framework necessary for the ESCB to perform its tasks in the third stage.²⁰ Furthermore, the EMI is helping national economies achieve the fulfillment of convergence criteria and is taking all necessary measures to correct persistent economic imbalances.²¹

The third stage, which must begin by January 1, 1999, will be marked by the transferral of all economic and monetary policy to EU institutions.²² Specifically, the EU Council will be given power to decide economic questions and impose constraints on national budgets.²³ The ECB also will decide all monetary issues including exchange market intervention measures in third currencies and acquisition and management of the official reserves of the Member States.²⁴ Furthermore, in the final stage, exchange rates will be irrevocably fixed, and a single currency will be introduced.²⁵

B. *Council Assessment of Convergence Criteria and the Move to the Third Stage*

During the second stage, the Commission and the EMI will report to the Council of Ministers on the progress made in the fulfillment by the Member States of their obligations regarding the achievement of economic and monetary union.²⁶ These reports will include an examination of the compatibility between each Member State's national

¹⁸ See EC TREATY art. 109f; MEHNERT, *supra* note 17, at 17.

¹⁹ See Coopers & Lybrand, *supra* note 13, at *6.2.

²⁰ See EC TREATY art. 109f(3); MEHNERT, *supra* note 17, at 17. The duties of the EMI are manifold. See Coopers & Lybrand, *supra* note 13, at *6.2. Specifically, the EMI will strengthen cooperation between the national central banks, strengthen the coordination of national monetary policies to ensure price stability, monitor the functioning of the present EMS, hold consultations on issues falling within the competence of the central banks and affecting the stability of the financial markets and facilitate the use of the ECU. See *id.*

²¹ See Coopers & Lybrand, *supra* note 13, at *4.2.

²² See EC TREATY arts. 109j(3)-(4); Coopers & Lybrand, *supra* note 13, at *4.2; see also discussion *infra* part I(B).

²³ See Coopers & Lybrand, *supra* note 13, at *4.2.

²⁴ See *id.*

²⁵ See *id.*

²⁶ See EC TREATY art. 109j(1).

legislation and Articles 107 and 108 of the Treaty on European Union (TEU) and the Protocol on the Statute of the European System of Central Banks and of the European Central Bank (Protocol).²⁷ Furthermore, these reports will examine the achievement of sustainable convergence of national economies by reference to the fulfillment by each Member State of certain objective criteria.²⁸ These criteria call for the achievement of a high degree of price stability, the observance of the normal fluctuation margins provided for by the exchange rate mechanism of the EMS, the achievement of a budgetary position without an excessive deficit and meeting standards for long-term interest rate levels.²⁹

On the basis of these reports, the Council of Ministers, acting by a qualified majority on a recommendation from the Commission, will assess the progress of the Member States towards meeting the strict convergence criteria.³⁰ The Heads of State and Government will decide based on the assessments of the Council whether a majority of the Member States have fulfilled the necessary conditions for the adoption of a single currency and whether it is appropriate for the Union to enter the third stage of EMU.³¹ If the latter question is answered in the affirmative, the Council will also set the date for the beginning of the third stage.³² If by the end of 1997 the Council has not set the date for

²⁷ See *id.* Article 107 states the important principle that the ECB, the ESCB and the Member State central banks shall have independence in their decision-making and are not to take instructions either from Union institutions or from Member States. See *id.* art. 107. Article 108 states the each Member State shall ensure that its national legislation is compatible with the Treaty and the Protocol. See *id.* art. 108.

²⁸ See *id.* art.109j(1).

²⁹ See EC TREATY art. 109j(1). The achievement of a high degree of price stability is interpreted by the protocol on convergence criteria as meaning "an average rate of inflation, observed over a period of one year before the examination, that does not exceed by more than 1 percentage points that of, at most, the three best performing Member States in terms of price stability." *Id.* The observance of the normal fluctuations margins is interpreted by the protocol as meaning that the Member State has respected the normal margins "without severe tensions" and has not devalued "on its own initiative." *Id.* The protocol envisages specific long-term interest-rate levels: "over a period of one year before the examination, a Member State has had an average nominal long-term interest rate that does not exceed by more than two percentage points that of, at most, the three best performing member States in terms of price stability." Peter B. Kenen, *Can the EMU Fly?*, in GUILLERMO DE LA DENESA & PETER B. KENEN, *EMU PROSPECTS: TWO ESSAYS* 19, 26 (1995).

³⁰ See EC TREATY art. 109j(2). Qualified majority voting is addressed in Article 148 of the Treaty: "save as otherwise provided in this Treaty, the Council shall act by a majority of its members." *Id.* art. 148.

³¹ See *id.*

³² See *id.*

the beginning of the third stage, the stage will start automatically on January 1, 1999.³³

Member States which do not fulfill the entry criteria or are not politically minded to join the EMU will be given a derogation.³⁴ The Treaty clearly expresses that a Member State with a derogation as well as that state's national central bank will be excluded from certain rights and obligations within the ESCB.³⁵ Furthermore, the voting rights of a Member State with a derogation will be suspended with respect to a number of important provisions relating to the EMU, notably efforts to assure compliance with recommendations on the reduction of "excessive budget deficits" and decisions on recommendations for exchange rate policy.³⁶ On these matters, a qualified majority of the Council will be defined as two-thirds of the votes of Member States without a derogation.³⁷ Member States which have not met the convergence criteria but are politically ready to join EMU will have their derogation examined at least every two years, but they may request earlier examination.³⁸

The EMI will be liquidated on the date of entry into stage three, and its functions will be taken over by the ECB.³⁹ Article 44 of the Protocol of the ESCB states that the ECB will "take over those tasks of EMI that because of the derogations of one or more Member States still have to be fulfilled . . . ," and the ECB will have an advisory role in lifting derogations.⁴⁰ Furthermore, with the beginning of the third stage, the EMS agreement will be implicitly abrogated among the countries that lock their exchange rates irrevocably.⁴¹ Although the Treaty does not explicitly mention the position of Member States with a derogation, it

³³ See EC TREATY art. 109j(4).

³⁴ See *id.* art. 109k(1). Two protocols were adopted at Maastricht to accommodate the specific problems of EMU for the United Kingdom and Denmark. The first protocol allows the UK government to consult its parliament before deciding on whether to move to a single currency. See Coopers & Lybrand, *supra* note 13, at *7.3. Similarly, the second protocol provided Denmark with an exemption from the EMU provisions of the Treaty. See *id.* According to this protocol, the Danish government will notify the Council of its position concerning participation in the third stage of EMU before the end of 1996. See *id.*

³⁵ See EC TREATY art. 109k(3). Specifically, "a derogation . . . shall entail that the following articles do not apply to the Member State concerned: Articles 104c(9) and (11); 105(1), (2), (3) and (5); 105(a); 108a; 109 and 109a(2)(b)." *Id.*

³⁶ See *id.* art. 109k(5); GROS & THYGESEN, *supra* note 14, at 424.

³⁷ See EC TREATY art. 109k(5); GROS & THYGESEN, *supra* note 14, at 424.

³⁸ See EC TREATY art. 109k(2).

³⁹ See GROS & THYGESEN, *supra* note 14, at 424.

⁴⁰ Protocol, *supra* note 7, art. 44.

⁴¹ See GROS & THYGESEN, *supra* note 14, at 424.

strongly suggests that an EMS-like arrangement will link the currencies of the non-participants to the common currency of the participants in full EMU.⁴² Article 109m states that until the beginning of the third stage, or for as long as a Member State has a derogation, national exchange rate policy shall be treated as a matter of common interest.⁴³

C. *The Governance of the European System of Central Banks and the European Central Bank*

The ESCB will be composed of the ECB and the national central banks of the Member States who have joined the final stage.⁴⁴ The ECB will have two decision-making bodies: the Executive Board and the Governing Council.⁴⁵ The Executive Board will have six members: a President, a Vice President and four other members of recognized standing and professional expertise in monetary or banking matters.⁴⁶ The Board members will be appointed, by common accord, by the Member governments for an eight-year non-renewable term.⁴⁷ The appointments will be on the basis of a recommendation from the Council of Ministers and after consultations with the European Parliament and the Governing Council of the ECB.⁴⁸

The Governing Council will contain the six members constituting the Executive Board and the governors of the national central banks of the Member States.⁴⁹ The terms of office shall be no less than five years, and all members of the Council will have one vote.⁵⁰ The decision to give each member one vote is significant in light of the objectives of both the EMU and the ECB:

Weighted voting could have fostered the thinking that governors were primarily representing national interests and not equal members of a collegiate body charged with formulating

⁴² See *id.*

⁴³ See EC TREATY art. 109m; GROS & THYGESEN, *supra* note 14, at 424–25.

⁴⁴ See Protocol, *supra* note 7, art. 1; GROS & THYGESEN, *supra* note 14, at 397.

⁴⁵ See Protocol, *supra* note 7, art. 9.3; GROS & THYGESEN, *supra* note 14, at 397.

⁴⁶ See Protocol, *supra* note 7, arts. 11.1–2; GROS & THYGESEN, *supra* note 14, at 397.

⁴⁷ See Protocol, *supra* note 7, art. 11.2; GROS & THYGESEN, *supra* note 14, at 397.

⁴⁸ See Protocol, *supra* note 7, art. 11.2; GROS & THYGESEN, *supra* note 14, at 397.

⁴⁹ See Protocol, *supra* note 7, art. 10.1; GROS & THYGESEN, *supra* note 14, at 397.

⁵⁰ See Protocol, *supra* note 7, arts. 10.2, 14.2. However, there are some instances when members will have more than one vote. See *id.* art. 10.3. Specifically, “for any decisions taken under Articles 28, 29, 30, 32, 33 and 51, the votes in the Governing Council shall be weighted according to the national central banks’ shares in the subscribed capital of the ECB.” *Id.*

a common policy. Alliances of a few large members could then de facto have come to dominate decision-making.⁵¹

The Governing Council will act by simple majority with the President having the casting vote in the event of a tie.⁵² The Governing Council will normally meet monthly, but in any event at least ten times per year.⁵³

The responsibilities of the Governing Council and the Executive Board are enunciated in Article 12.1 of the Protocol of the ESCB.⁵⁴ According to this article of the Protocol, the Governing Council shall formulate the monetary policy of the Community including, as appropriate, decisions relating to intermediate monetary objectives, key interest rates and the supply of reserves in the system, and shall establish the necessary guidelines for their implementation.⁵⁵ The Executive Board shall implement monetary policy in accordance with the decisions and guidelines laid down by the Governing Council.⁵⁶ The national central banks will act in accordance with the guidelines and instructions of the Executive Board.⁵⁷

D. *The Objectives, Functions and Independence of the ESCB and the ECB*

The ESCB will have three specific objectives.⁵⁸ As enunciated in the Protocol, the primary objective of the ESCB, which will be composed of the ECB and the national central banks, will be to maintain price stability.⁵⁹ Furthermore, without adversely affecting the objective of price stability, the ESCB shall support the general economic policies of the Community.⁶⁰ The ESCB also will act consistently with free and competitive markets.⁶¹

⁵¹ GROS & THYGESEN, *supra* note 14, at 397.

⁵² See Protocol, *supra* note 7, art. 10.2.

⁵³ See *id.* art. 10.5.

⁵⁴ See *id.* art. 12.1.

⁵⁵ See *id.*; GROS & THYGESEN, *supra* note 14, at 398.

⁵⁶ See Protocol, *supra* note 7, art. 12.1; GROS & THYGESEN, *supra* note 14, at 398.

⁵⁷ See Protocol, *supra* note 7, art. 12.1; GROS & THYGESEN, *supra* note 14, at 398.

⁵⁸ See Protocol, *supra* note 7, art. 2.

⁵⁹ See *id.* Unfortunately, there is not a precise definition yet of what is meant by price stability. Thygesen suggests three possible measures: (a) an index of average prices for traded goods and services in the EC; (b) a weighted index of consumer prices; and (c) an average of value-added deflators in the production of tradeables. See Charles Goodhart, *A European Central Bank*, in EUROPEAN BANKING 12, 27 (Andy Mullineux ed., 1992).

⁶⁰ See Protocol, *supra* note 7, art. 2.

⁶¹ See *id.*

In order to avoid political influence and therefore achieve these common objectives, the ECB will function as an independent entity.⁶² In general, central bankers argue that they are able to work more efficiently when they are insulated from partisan political influence.⁶³ Moreover, there is some empirical evidence that countries with a more independent central bank, like Germany, have succeeded in maintaining price stability better than those with central banks that are more subject to the control of their central government, such as the UK.⁶⁴ The Protocol of the ESCB explicitly provides for an independent central bank.⁶⁵ Article 7 of the Protocol states that neither the ECB nor the national central banks will seek or take instructions from EU institutions or member governments, and that member governments will not try to influence the ECB.⁶⁶ Consequently, although the president of the Council of Ministers and a member of the Commission may attend meetings of the ECB Governing Council, they will not be allowed to vote.⁶⁷

A prominent feature of an independent bank is that it generates its own revenue and does not rely on fiscal authority for its operations.⁶⁸ The ECB will be constructed in this regard like a private bank.⁶⁹ Each national central bank will provide capital and will transfer foreign assets to the ECB, and the property of the ECB will be exempt from all forms of requisition or expropriation.⁷⁰ The ECB will earn income on specifically designated assets and will distribute it to the member banks according to their capital shares.⁷¹ The ECB will, in sum, be financially independent.⁷²

In addition to the institutional independence of the ECB, the personal independence of central bankers from the administrations in

⁶² See *id.* art. 7. "Note, however, that independence does not make the central bank an apolitical institution." FRATIANNI ET AL., *supra* note 5, at 33–34 n.15. Charles Goodhart has pointed out that an independent central bank is forced to defend its policies continuously against pressure groups and in public debates and to seek coalitions in the political arena; a dependent central bank enjoys the government's protection against direct political attack. See *id.* In this sense, the position of independent central banks is more political than that of dependent central banks. See *id.*

⁶³ See Goodhart, *supra* note 59, at 24.

⁶⁴ See *id.*

⁶⁵ See Protocol, *supra* note 7, art. 7.

⁶⁶ See *id.*; FRATIANNI ET AL., *supra* note 5, at 34.

⁶⁷ See EC TREATY art. 109b; FRATIANNI ET AL., *supra* note 5, at 34.

⁶⁸ See FRATIANNI ET AL., *supra* note 5, at 36.

⁶⁹ See *id.*

⁷⁰ See Protocol, *supra* note 7, arts. 28–30; FRATIANNI ET AL., *supra* note 5, at 36.

⁷¹ See Protocol, *supra* note 7, art. 32; FRATIANNI ET AL., *supra* note 5, at 36.

⁷² See FRATIANNI ET AL., *supra* note 5, at 36.

office is necessary to achieve the common objectives of the ECB.⁷³ To this end, individual central bankers cannot be removed from office for the design and execution of monetary policy.⁷⁴ Additional means to ensure independence are nonrenewability of terms, so that members of the ECB Executive Board will not be tempted to defer to the government in power, and staggering of terms, so that all the members are not appointed by the same administration.⁷⁵ Appointments are staggered by giving members of the initial Executive Board different terms of office.⁷⁶ The president of the first Executive Board will have a term of eight years, the vice-president a term of four years and the other members of the board terms of between five and eight years.⁷⁷

The ESCB will undertake five main tasks: define and implement the monetary policy of the EU; conduct foreign exchange operations in accordance with the prevailing exchange rate regime of the EU; hold and manage the official foreign reserves of the Member States; ensure the smooth operation of payment systems; and participate as necessary in the formulation, coordination and execution of policies relating to the prudential supervision of credit institutions and the stability of the financial system.⁷⁸ In addition to these tasks, the ECB shall have certain advisory functions.⁷⁹ Specifically, the ECB shall be consulted on any proposed EU act in its field of competence and by national authorities regarding any draft legislative provision in its field of competence.⁸⁰ The ECB's fields of competence are generally considered to entail all monetary, prudential, banking and financial matters.⁸¹ Furthermore, the ECB may submit opinions to the appropriate EU institutions or bodies or to national authorities on matters in its fields of competence.⁸²

In meeting its objectives and carrying out its general functions, the ESCB will have specific monetary operations and functions.⁸³ The

⁷³ See *id.* The ECB is "institutionally independent" because, as stipulated by Article 7 of the Protocol, it will not seek or take instructions from EU institutions or Member States. Protocol, *supra* note 7, art. 7.

⁷⁴ See *id.* art. 14.2; FRATIANNI ET AL., *supra* note 5, at 37.

⁷⁵ See Protocol, *supra* note 7, arts. 11.2, 50; FRATIANNI ET AL., *supra* note 5, at 37.

⁷⁶ See Protocol, *supra* note 7, art. 50; FRATIANNI ET AL., *supra* note 5, at 37.

⁷⁷ See Protocol, *supra* note 7, art. 50; FRATIANNI ET AL., *supra* note 5, at 37.

⁷⁸ See Protocol, *supra* note 7, arts. 3.1, 3.3.

⁷⁹ See *id.* art. 4.

⁸⁰ See EC TREATY art. 105(4); Protocol, *supra* note 7, art. 4.

⁸¹ See Goodhart, *supra* note 59, at 16.

⁸² See EC TREATY art. 105(4); Protocol, *supra* note 7, art. 4.

⁸³ See Protocol, *supra* note 7, ch. IV.

Governing Council will have the exclusive right to authorize the issuance of lender tender within the EU.⁸⁴ The ECB will be entitled to require credit institutions to hold minimum reserves on accounts with the ECB and with national central banks.⁸⁵ The Governing Council also will lay down the regulations concerning the calculation and determination of the required minimum reserves.⁸⁶ The ECB and the national central banks will be entitled to establish relations with banks and financial institutions in third party countries, and with international bodies such as the International Monetary Fund (IMF).⁸⁷ The ESCB will be entitled to acquire and sell, spot and forward all types of foreign exchange assets and gold.⁸⁸ The bank will also conduct all types of banking transactions with third countries, including borrowing and lending.⁸⁹ Each national central bank will transfer to the ECB its foreign reserve assets, other than Member State currencies and ECUs.⁹⁰ The Governing Council shall decide upon the proportion to be called up by the ECB following its establishment and the amounts called up at later dates.⁹¹ Each national central bank will be credited with a claim equivalent to its contribution, and the Governing Council will determine the amount in which national central banks are remunerated.⁹² The ECB may accept the pooling of IMF reserve positions and special drawing rights (SDRs).⁹³

In order to carry out the functions of the ESCB, the ECB will make regulations, take decisions, deliver opinions and make recommendations.⁹⁴ The acts or omissions of the ECB shall be open to review or

⁸⁴ See *id.* art. 16; Goodhart, *supra* note 59, at 17.

⁸⁵ See Protocol, *supra* note 7, art. 19.1; Goodhart, *supra* note 59, at 17.

⁸⁶ See Protocol, *supra* note 7, art. 19.1; Goodhart, *supra* note 59, at 17.

⁸⁷ See Protocol, *supra* note 7, art. 23; Goodhart, *supra* note 59, at 17.

⁸⁸ See Protocol, *supra* note 7, art. 23; Goodhart, *supra* note 59, at 17.

⁸⁹ See Protocol, *supra* note 7, art. 23; Goodhart, *supra* note 59, at 17.

⁹⁰ See Protocol, *supra* note 7, art. 30.1; Goodhart, *supra* note 59, at 17. The ECU is an artificial European monetary unit. See BERMANN, *supra* note 1, at 1196. The value of the ECU is fixed as a composite of a "basket" of Member State currencies with weighted values one to another. See *id.* A macroeconomic calculation of the proportionate strength of the national economy underlying each State's currency is used in allocating weights to different currencies. See *id.*

⁹¹ See Protocol, *supra* note 7, art. 30.1; Goodhart, *supra* note 59, at 17.

⁹² See Protocol, *supra* note 7, art. 30.3; Goodhart, *supra* note 59, at 17.

⁹³ See Protocol, *supra* note 7, art. 30.5; Goodhart, *supra* note 59, at 17.

⁹⁴ See EC TREATY art. 108a(1); Protocol, *supra* note 7, art. 34.1. The Treaty and Protocol define the various acts in this way: "A regulation shall have general application. It shall be binding in its entirety and directly applicable in all Member States. Recommendations and opinions shall have no binding force. A decision shall be binding in its entirety upon those to whom it is addressed." EC TREATY art. 108a(2).

interpretation by the European Court of Justice (ECJ).⁹⁵ In specific circumstances Member States, the Council, the Commission, the European Parliament (EP) and natural or legal persons will have standing to bring suit before the ECJ.⁹⁶ Furthermore, the ECB may institute proceedings before the ECJ in these same circumstances.⁹⁷ A decision of the ECB to bring an action before the ECJ will be taken by the Governing Council.⁹⁸

II. DISCUSSION

Since the establishment of the European Coal and Steel Community in 1952, economic integration has been actively sought by the Member States.⁹⁹ Yet, full integration as desired by the original architects will never be realized without a monetary union and a centralized monetary policy to provide stability and strength. Not unlike other states who have from time to time hastily pursued a governmental objective, the Member States of the EU have at times hastily pursued the objective of complete monetary union. Specifically, by requiring Member States to achieve strict convergence criteria for initiation into the third stage of economic and monetary union and by adopting a final and resolute deadline of January 1, 1999 for the establishment of this third stage, the Member States themselves have created a regime which may not be attainable.¹⁰⁰ Fortunately, the Member States have considered the legal ramifications of establishing a full monetary union by January 1, 1999.¹⁰¹ As a result, the Member States have provided specific provisions in the Treaty and the Protocol to deal with those situations which may arise if monetary union includes only several participating Member States.¹⁰² These provisions furnish the ECB with the means to assert itself against attack from Member States with derogations.¹⁰³

⁹⁵ See Protocol, *supra* note 7, art. 35.1.

⁹⁶ See EC TREATY art. 173; see also discussion *infra* part II. For a complete discussion of the doctrine of direct effect, that is the instance when a natural or legal person has standing to sue an EU institution or a Member State, see generally BERMANN, *supra* note 1, at 166.

⁹⁷ See EC TREATY art. 173; see also discussion *infra* part II.

⁹⁸ See *id.* art. 35.5.

⁹⁹ See generally BERMANN, *supra* note 1, at 2.

¹⁰⁰ See EC TREATY art. 109j.

¹⁰¹ See *id.* art. 173.

¹⁰² See *id.*

¹⁰³ See *id.*

The Treaty on European Union provides that the Heads of State and Government will deem whether or not it is appropriate for the EU to enter the third stage of EMU.¹⁰⁴ If by the end of 1997 the date for the beginning of the third stage has not been set, the third stage will start automatically on January 1, 1999.¹⁰⁵ It is conceivable that by the end of 1998 only a few Member States will have met the convergence criteria. Regardless, even if only two of the Member States have fulfilled the necessary conditions by the end of 1998, EMU will be required to proceed.¹⁰⁶ Consequently, a situation may arise where only two Member States have transferred power over their monetary regimes from their national central banks to the EU institutions.¹⁰⁷ The rest of the Member States would be given derogations.¹⁰⁸ Member States with derogations as well as the national central banks of those states would be excluded from certain rights and obligations which arise from membership in the ESCB.¹⁰⁹

If this situation were to occur, it is conceivable that Member States with derogations, who essentially would be left out of the institutional framework of the monetary union, would be unsatisfied with certain aspects of the ECB's monetary policy. As a result, these Member States might attempt to pass and implement legislation through the Council of Ministers in the hope of changing monetary policy to suit their own particular needs. Such legislation would be hostile to the prerogatives of the ECB. For example, the Member States with derogations could pass a directive decreasing the level of capital which national central banks are required to maintain. Such action by the Council could vitiate a prior ECB directive stipulating the level of reserve requirements of national central banks. This scenario appears possible because only qualified majority voting, as opposed to unanimous consent by Member States, would be required for this type of legislation.¹¹⁰

If the Member States with derogations adopt banking legislation contrary to the ECB's prerogatives, the ECB could undertake measures to prevent such hostile action. To do this, the ECB would have to seek

¹⁰⁴ See *id.* art. 109j(3).

¹⁰⁵ See EC TREATY art. 109j(4).

¹⁰⁶ See *id.*

¹⁰⁷ See Coopers & Lybrand, *supra* note 13, at *4.2.

¹⁰⁸ See EC TREATY art. 109k(1).

¹⁰⁹ See *id.* art. 109k(3).

¹¹⁰ See *id.* art. 148.

judicial recourse from the ECJ. The ECB would undertake this measure by invoking Article 173 of the Treaty, which provides:

[The European Court of Justice shall] have jurisdiction in actions brought by a member state, the Council or the Commission on grounds of lack of competence, infringement of an essential procedural requirement, infringement of this Treaty or any rule of law relating to its application of misuse of powers. The Court shall have jurisdiction under the same conditions in actions brought by the European Parliament and by the ECB for the purpose of protecting their prerogatives.¹¹¹

Therefore, in accordance with Article 173, the ECB may bring suit against the Council of Ministers if the Council, in enacting the banking legislation, infringed an essential procedural requirement.¹¹²

In such a case, the ECB could argue that infringement of an essential procedural requirement occurred when the Council failed to consult the ECB about the proposed banking legislation. Article 105(4) of the Treaty provides that "the ECB shall be consulted on any proposed Community act in its field of competence."¹¹³ If the banking legislation is in the field of competence of the ECB, the Council of Ministers will have infringed an essential procedural requirement.¹¹⁴

The field of competence of the ECB will include monetary, prudential, banking and financial matters.¹¹⁵ Consequently, any legislation dealing with the reserve requirements for capital of national central banks will necessarily be within the field of competence of the ECB. As a result, such legislation enacted without the consent of the ECB would be struck down as violative of Article 173 of the Treaty.¹¹⁶

Although the Member governments have provided specific provisions in the Treaty and the Protocol to deal with situations that could arise if monetary union includes only several participating Member States, the Treaty should be amended to allow for a delay in establishing a full monetary union.¹¹⁷ For example, the Treaty could stipulate that the third stage of EMU will begin when either a majority or

¹¹¹ *Id.* art. 173.

¹¹² *See id.*

¹¹³ EC TREATY art. 105(4).

¹¹⁴ *See id.*

¹¹⁵ *See id.* art. 105; Goodhart, *supra* note 59, at 16.

¹¹⁶ *See* EC TREATY art. 173.

¹¹⁷ *See id.*

two-thirds of the Member States have met the convergence criteria. If the Treaty is not amended in such a manner, Member States with derogations, in the event that they have a qualified majority of the Council, will be able to adopt and implement legislation hostile to the prerogatives of the ECB. Hostile action taken by Member State governments in this regard will subsequently force the ECB to assert itself by means of legal recourse from the ECJ, an event which will generally cause inefficient and sometimes ineffective European monetary policy decision-making. By amending the Treaty to allow for a delay if the convergence criteria is not achieved by a majority of the Member States, however, impediments to efficient and effective monetary policy decision-making, such as the Council trying to pass legislation contrary to the prerogatives of the ECB, will be eliminated.

CONCLUSION

It is conceivable that a majority of the Member States, being unable to meet the strict convergence criteria, will be left out of the institutional structure of the third stage of EMU. If this were to occur, it is also conceivable that these Member States, via the Council of Ministers, could adopt legislation contrary to the prerogatives of the ECB. If this legislation were to pass, the ECB could undertake measures to prevent such hostile action by Member States with derogations. Specifically, the ECB could invoke Article 173 of the Treaty and argue that infringement of an essential procedural requirement occurred when the Council failed to consult the ECB about the proposed banking legislation. Because banking legislation is in the field of competence of the ECB, the ECJ would strike down the legislation as violative of Article 173. Yet, hindrances to achieving efficient and effective common European monetary policy decision-making, caused by Member States with derogations, can only be fully eliminated by amending the Treaty to allow for a delay in establishing a full monetary union.

Jonathan A.C. Wise