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European Economic and Monetary Union: Will the EMU Ever Fly The Euro: A New Single Currency for Europe: Legal Framework

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EUROPEAN ECONOMIC AND MONETARY UNION: WILL THE EMU EVER FLY?

Roger J. Goebel*

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INTRODUCTION

No other issue is of greater importance to the European Union today than whether and how Economic and Monetary Union (EMU) will be attained. If EMU can be successfully achieved, not only will it produce substantial economic and monetary benefits, but its success will have great political and psychological significance. A strong EMU is apt to promote further efforts toward a federal union. Conversely, if EMU fails or if there are protracted delays in its attainment, if too many Member States remain permanently outside the monetary union, or if some states suffer serious economic and social disruption as a consequence of joining the monetary union, then such shortfalls will adversely affect the present level of political integration in the European Union.

The title of this article represents a pun, but a pun with a point that responds to the tensions between these dreams of EMU's success and fears of its failure. The emu is a large Australian bird, but, like the better-known ostrich, the emu does not fly. However, it can run very fast. The point is, that during the early stages of planning for the EMU there were some very high-flying aspirations for what it might attain, and what its attainment might mean for the political future of the European Union. Since then, these aspirations have been considerably chilled by political and economic realities. Still, one can reasonably hope that when the EMU structure is in place, it, like the Australian emu, will run very fast—that, while it may not achieve the highest goals imagined by some proponents, the EMU will function well at a more modest but realistic level.

The goal of an Economic and Monetary Union, sometimes also called the European Monetary Union, has been a central preoccupation of the European Community for many years. In fact, the idea of substantial economic and monetary coordination dates to the origin of the Community, and a proposal for a monetary union was advanced as early as 1971. In its description of the current monetary union plan and progress toward its attainment, this Article will deal initially in Part I with the goals which have inspired the current efforts to attain EMU, namely the perceived benefits of an integrated Community monetary system regulated by a central bank system, together with a single Community currency, eliminating trans-border currency costs and promoting further market integration within the common market.
Next, this Article will outline the historical development of EMU, describing in Part II the initial 1970 plans and the success of the 1979 European Monetary System. Part III continues this historical review with a sketch of the vital catalyst, the 1989 Delors Report, the succeeding Commission studies, and the work of the 1990-1991 Rome Intergovernmental Conference that prepared the text of the Treaty provisions on EMU. Also necessary to situate EMU in its historical context is Part IV which deals with the early progress toward free movement of capital, a goal now attained through a 1988 directive and EC Treaty Article 73, introduced in 1994. Free movement of capital is an essential pre-condition for EMU.

The core of this Article lies in Parts V and VI. Part V sets out the three-stage approach to EMU, pragmatically gauged for progressive development, and describes in some detail the role, powers and structure of the European Central Bank and the European System of Central Banks. Part VI builds on this by reviewing a series of constitutional and legal issues concerning the Treaty structure, notably the need for independence of the central bank system, the "democratic deficit" represented by the meager role accorded to the European Parliament, the essential need for effective judicial review to achieve a "rule of law" for EMU, and the question whether the central bank system ought to work to achieve high employment in addition to trying to achieve its Treaty goal of price stability.

The final Parts of this Article move to the current scene. Part VII describes the second stage of progress toward EMU, 1994-1998, and the current role of the European Monetary Institute. This Part's most important feature is its analysis of the complex monetary convergence criteria which Member States must satisfy in order to join in the third stage of EMU, and its evaluation of current progress of the states in that regard. Part VIII sets out the key policy decisions taken by the European Council in 1995-1997 to further the development of EMU, and describes some related legislative measures, notably the recent regulations that embody the "Stability and Growth Pact." The final Part covers the plans and studies for the new single currency, the euro, and some essential legislation to enable its introduction.

I. THE GOALS OF AN ECONOMIC AND MONETARY UNION

The attainment of an Economic and Monetary Union will transform the European Community,¹ and its over-arching structure, the European Union,² in a

¹ The European Community, often called the EC or simply the Community and formally designated as the European Economic Community (EEC) until 1993, was created by the Treaty Establishing the European Economic Community, signed at Rome (and hence often called the Rome Treaty) on March 25, 1957. 298 U.N.T.S. 11.
² The Treaty on European Union (TEU), signed at Maastricht on February 7, 1992 (and hence often called the Maastricht Treaty), effective November 1, 1993, created a structure called the European Union. The European Community, renamed as such by the TEU, is by far its most important component part, but the European Union also includes two other so-called "pillars:" Article J on Common Foreign and Security Policy, and Article K on Cooperation in Justice and Home Affairs. The TEU, together with the Treaty Establishing the European Community (EC Treaty)
more fundamental manner than any development since the substantial achievement of the internal market program. Indeed, the 1995 Green Paper on the Introduction of the Single Currency depicted EMU as the “logical and essential complement” to the common market. The recent impetus toward EMU undoubtedly stems in large measure from the generally satisfactory progress to date in attaining a single market.

The goal of EMU has three components: (1) an integrated Community monetary system; (2) an institutional structure, with a European Central Bank at its center; (3) a single currency, the euro, replacing present national currencies in all the participating Member States. Each will be described in greater detail later, but some preliminary notes should be made.

An integrated Community monetary system with a European Central Bank at its core offers the prospect of both greater monetary stability and a large monetary marketplace. As will be seen later, the Member States have followed sharply different national economic and monetary policies in the past. The necessity to meet rather high economic and monetary standards in order to participate in the monetary union has compelled virtually all the Member States to adopt much stricter monetary policies, in effect, putting their financial households in order. If, as can be safely assumed, the European Central Bank adopts stable monetary policy programs and has the power to implement them, with a minimum of political interference from Member State governments and Community institutions, then the prospect is one of a more solid monetary structure for all the participating States.

Since Member States participating in the monetary union will no longer be able to resort easily to deficit financing, their rate of economic growth is apt to be steadier, and they will be more likely to attract international and domestic investment. A reduction in deficit spending and a lowering of long-term debt will bring the corollary of less frequent need to float state loans and the obtention of lower interest rates for state debt. The private sector will benefit because financial and commercial enterprises should be able to float bonds and borrow long-term funds in a more liquid market, again at lower rates.

With regard to the adoption of the single currency, the euro, the Commission estimates that use of a single currency will save the Community annually around 20-25 billion ECU, or approximately 0.3-0.4% of GDP, through the elimination of currency-related transaction costs (i.e., the expense of changes in currency when transacting commercial and personal affairs across frontiers within the

in its present form, is printed in its entirety in 1992 O.J. (C 224) 1 and 31 I.L.M. 247 (1992). The provisions on economic and monetary union are an integral part of the EC Treaty. Hence, throughout the text of this article, reference will usually be made to the European Community, or the Community, rather than to the European Union.

Community). Business will no longer need currency options, futures or insurance to hedge against shifts in national currency value when transacting trans-border financial and commercial affairs within the Community. On the other hand, as planning for the introduction of the euro moves ahead, private financial sector and other sources are estimating more precisely the transition costs in abandoning current currencies and shifting to a single currency. The final cost is probably incalculable, but it may well represent tens of billions of dollars—perhaps over a hundred billion dollars in the aggregate. In addition, there will be serious adjustment shocks when governments, financial institutions, businesses and private parties must cope with the change-over to an unfamiliar single currency. It is certainly within the realm of possibility that transition costs will exceed savings in transaction costs during the initial years of monetary union.

But there is a further and more important economic benefit flowing from a single currency, namely, the achievement of far greater price and cost transparency in all trans-border financial, commercial and private transactions. Thus, purchasers of raw materials and supplies, intermediate distributors of products, persons providing services, and consumers of goods, services or credit will all be able easily and quickly to compare prices or expenses when dealing with domestic and foreign parties. This will considerably facilitate the business operations of large financial institutions and multinational corporations, which have, not surprisingly, become strong supporters of the efforts to attain EMU. Yet overall, smaller enterprises may derive greater benefit than larger ones from this increased price and cost transparency, since smaller enterprises tend to have less expertise in conducting trans-border affairs.

Prospects of greater market integration, especially in the financial services sector, are bound to lead to enhanced merger and acquisition activity, resulting in the disappearance of many smaller or less efficient enterprises. The Commission estimates that several Member States are “over-banked,” possessing too many banks or other financial institutions in proportion to their general population and overall level of commercial activity. The wave of trans-border and domestic financial sector mergers and acquisitions that increased sharply in 1996-1997 may be expected to continue. Although manifestly leading to a more efficient financial sector, this process will also produce far more powerful market players, whose conduct will have to be carefully monitored by Community and national competition authorities, as well as by financial regulatory bodies.

On the global monetary stage, a successful EMU will also play a leading role. Use of the euro for international trade and as a reserve currency will be far more substantial than is the present use of individual national currencies, even

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4 Id. at 3.

the German mark. Moreover, the existence of a European Central Bank with a mandate for price stability and a strong currency is quite apt to promote the desirability of the use of the euro in international transactions. The euro may become a serious competitor for the U.S. dollar in global transactions, especially in the international oil and commodities markets and in trans-border credit and financial operations.

Finally, a successful EMU will have a great impact on the political aspect of the European Community. One of the most essential types of sovereign power, namely the control over monetary policy, will be transferred to a Community institution. It is true that, as we shall see in Part V, the institution, the European Central Bank, will be independent of the traditional Community political institutions, namely the Commission, Council and Parliament. Nevertheless, power over monetary policy will rest with a Community entity. Such a transfer of vital power necessarily diminishes the role of national governments to a significant degree.

The transfer of monetary power to the European Central Bank and the creation of a single common currency are bound also to produce significant psychological consequences. Citizens of the Member States will perceive more readily the extent, importance and hopefully the value of European integration. Replacement of national currency and coins by the euro will represent a far more meaningful symbol of Union integration than the current European passport or the Union flag can ever be. Migrant workers and professionals in particular will see tangible benefits from the use of the euro, since they will more readily be able to compare income levels and the cost of living in different Member States, as well as to transfer funds to a new place of residence or back to their home or family.

Thus far, it has been assumed that the Community will successfully attain Economic and Monetary Union. Although the prospect for its success are increasingly bright, this is not a guaranteed result. To some degree, the plan for EMU represents an audacious gamble. If successful, the economic, monetary and political benefits will be enormous. But if the progress is stalled, if too many Member States remain permanently outside of EMU, or if a monetary shock destabilizes the entire structure once created, the adverse impact on the Community would be serious, perhaps very grave. American economists in particular were initially highly skeptical of the merits of EMU and concerned about its potential risks. While they have become less pessimistic in view of recent progress, still it must be said that EMU does bring significant risks as well as benefits.

The current mood in the European Community is one of guarded optimism. As will be described in Part VII, the current prospects are that eleven Member States will launch the monetary union in 1999, with a reasonable likelihood that the four others will join by 2002, the date set for the introduction of the euro as legal tender, or shortly thereafter.

Before closing this Part, a word is appropriate on the role of the highest political leadership of the Member States, gathered together in the body designated as the European Council. Ever since 1969, when President Pompidou
of France took the initiative of urging summit meetings, the Heads of State and Government of the Member States have been meeting two to four times a year to discuss major issues confronting the Community (or the Union), setting policy guidelines and issuing important declarations of principle. By the late 1970s, these summit meetings became known as European Council sessions.6

With the adoption of the important series of EC Treaty amendments known as the Single European Act, effective July 1, 1987, the European Council acquired Treaty status.7 The current relevant provision, Article D of the Treaty on European Union (TEU), includes the President of the Commission in the European Council meetings of Heads of State and Governments. Article D states the role of the European Council to be to "provide the Union with the necessary impetus for its development and [to] define the general political guidelines thereof."8

The role of the European Council in deciding upon the key aspects of the proposed structure of EMU, and in promoting its steady evolution toward reality, has been an unusually marked one. As we shall see in later Parts, successive meetings of the European Council have resulted in crucial policy decisions, or achieved critical compromise breakthroughs on intransigent issues, in shaping the progress toward EMU. Moreover, the TEU itself specifies that a number of fundamental decisions in moving toward EMU, especially that of the designation of the Member States that will join in its final stage in 1999, are to be taken by the Council, the Community's principal legislative body, meeting in the unusual composition of the Heads of State and Government, instead of its more customary composition of finance ministers or foreign affairs ministers.

Indeed, in the prospective creation of a monetary union, not only should great tribute be paid to the vision of Commission President Jacques Delors, but also to the vision and political will of Chancellor Kohl of Germany and President Mitterand of France, who together provided the principal leadership in the planning. Also playing important roles in the political process were Prime Ministers Dehaene of Belgium, Lubbers of The Netherlands and Gonzalez of Spain, and more recently, President Chirac of France. Tributes should also be paid to the less prominent but quite crucial role of the central bank governors, such as Pohl of the Bundesbank (the German Central Bank), and Duisenberg of the Dutch Central Bank, who, together with their staffs, provided much of the expertise necessary in the drafting of the various treaty provisions.

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II. THE HISTORICAL BACKGROUND

A. The Treaty of Rome: Economic and Monetary Coordination

It may seem a bit surprising, but in fact the initial Treaty Establishing the European Economic Community (EEC Treaty, or Treaty of Rome) did include the topic of economic and monetary coordination, although the idea of a monetary union was not yet advanced. Thus, in the EEC Treaty, Title II on Economic Policy contains several articles relevant to economic and monetary coordination. Article 104 requires each Member State to “pursue the economic policy needed to ensure the equilibrium of its overall balance of payments and to maintain confidence in its currency, while taking care to ensure a high level of employment and a stable level of prices.” Article 105 further requires states to “coordinate their economic policies,” as well as policies “in the monetary field.” Article 106 liberalizes current transborder payments for goods and services, and Articles 108 and 109 permit safeguard measures for states encountering serious balance of payments difficulties.

Article 105(2) of the EEC Treaty created a body whose importance has steadily increased over the years. This is the Monetary Committee, composed of two representatives from each Member State and two persons appointed by the Commission, whose role is to “review the monetary and financial situation of the Member States and the Community,” and to provide opinions and reports to the Commission and Council. Another specialist body, the Committee of Governors of Central Banks, was established in 1964 to facilitate contacts among the banks and to provide advice on monetary affairs.

The EEC monetary structure first assumed importance at the end of the 1960s as the world monetary system established under the Bretton Woods accords started to break down. In the halcyon days of the 1950s and 1960s, states’ currency exchange rates were fixed in relation to one another, and the U.S. dollar, backed by substantial gold reserves, provided international monetary stability. As world trade and investment expanded enormously during that period, states became much more interdependent, both in economic and monetary terms. Then, in the 1960s, as the economies of some states developed far more rapidly than others, and as certain states suffered serious bouts of inflation, balance of payments difficulties became inevitable. France, Italy, the

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9 Articles 103-109 were deleted by the Treaty on European Union. In addition to the source cited in note 1, supra, their text can be conveniently found in Consolidated Treaties Establishing the European Communities (EC Off’1 Pub. Off. 1987); and in the EEC Treaty provisions contained in George A. Bermann, et al., European Community Law: Selected Documents (1998).


United Kingdom and certain other states were compelled to devalue their currencies in successive monetary crises, while Germany, The Netherlands and Switzerland were obliged to revalue them.

The most serious monetary crisis arose when the dollar came under severe pressure in 1971. President Nixon decided to end the gold standard on August 15, 1971, allowing the dollar to float against other currencies. The Smithsonian Accord of December 18, 1971 institutionalized the system of floating exchange rates.\textsuperscript{12} However, because such rates create uncertainty and instability in long-term financial and commercial transactions, ever since 1971 governments have sought to find a way to return to some form of fixed, or at least relatively stable rates.

Making use of Article 105, the Commission and Council began a series of attempts to alleviate monetary crises in particular Member States and to coordinate economic and monetary policy in order to achieve greater stability within the Community. The 1969 Barre Plan, named after Raymond Barre, then president of the central bank of France, is usually considered to have initiated monetary coordination. In a related move, the Committee of Governors of Central Banks agreed on February 9, 1970, to provide lines of credit to support Member States in times of monetary crisis.

A stage-by-stage plan for attaining economic and monetary union was presented to the Council of Ministers in October 1970 in the form of the Werner Report, named after the Prime Minister of Luxembourg, who served as chairman of a committee of experts representing the Commission, the Monetary Committee, and central bank governors.\textsuperscript{13} A Council resolution endorsed the Werner Report in general terms and resolved to develop an economic and monetary union over a ten year period.\textsuperscript{14} Pursuant to this plan, Council Regulation 907/73\textsuperscript{15} established a European Monetary Cooperation Fund to provide short-term monetary support and facilitate concerted monetary action. A later Council Decision 74/120 urged Member States to align their economic policies with guidelines to be issued periodically by the Council, and called on the central banks to coordinate their monetary policies.\textsuperscript{16} Most Member States entered a system to reduce exchange rate fluctuations to a narrow band, popularly called the "snake." (The band was commonly called a "snake," because, when graphically depicted, it resembles an undulating wave as a particular national currency moves above or below the pegged rate.)

\textsuperscript{12} For further discussion of the U.S. withdrawal from the gold standard and the Smithsonian Accord, see Gold, supra note 11, at 94-98.

\textsuperscript{13} Report on the Realization by Stages of Economic and Monetary Union, Bull. EC 11-1970, Supp. The Werner Report proposed a system of irreversible convertibility of national currencies, free from fluctuation, regulated by a Community system of central banks modeled after the Federal Reserve. The Report's proposal that the EEC Treaty be amended in order to achieve monetary union did not, of course, result in any action. For further details on the Werner Report and Community action to implement it, see Smits, supra note 11, at 15-19.

\textsuperscript{14} Bull. EC 4-1971, at 19.

\textsuperscript{15} Council Regulation 907/73, 1973 O.J. (L 89) 2.

\textsuperscript{16} Council Decision 74/120, 1974 O.J. (L 63) 16.
Unfortunately, the energy recession of the mid-1970s and further monetary crises in certain Member States prevented these Community measures from becoming truly effective. Coordination efforts were reduced, rather than enhanced, in the late 1970s. The goal of a union receded farther into the distance.

B. The European Monetary System

In the late 1970s, the leadership of President Giscard d'Estaing of France and Chancellor Schmidt of Germany, both former Finance Ministers, together with Commission President Roy Jenkins, formerly the U.K. Chancellor of the Exchequer, caused new attention to be focussed on monetary coordination and stabilization. The European Council Meeting at Bremen in July 1978 officially endorsed the concept of a European Monetary System (EMS), which came into force in March 1979.

Membership in the EMS is voluntary, and therefore has produced since its inception a sort of "two-tier" Europe. The Benelux States, Denmark, France, Germany and Italy have been members from the start. The United Kingdom initially joined, but withdrew after a two-month run on its currency reserves, and only joined again in October 1990. Portugal and Spain joined the EMS after their accession in 1986, but Greece did not.

In a 1989 brochure, the Commission described the European Monetary System as intended to achieve the following objectives:

To attain a zone of internal and external monetary stability in Europe (involving both low inflation and stable exchange rates); to provide the framework for improved economic policy cooperation between Member States . . . ; to help to alleviate global monetary instability through common policies vis a vis third currencies . . . .

The Commission further described the EMS as "a pragmatic attempt to progress along the road to economic and monetary union." 19

The European Monetary System has three basic components: an artificial currency, the ECU; exchange rates which are permitted to fluctuate only in a narrow band; and a system of credit and loan reserves to stabilize Member State currencies in times of crisis. 20 All three merit brief treatment.

First, the EMS created an artificial European monetary unit, the ECU, which replaced the prior artificial unit known as the European Unit of Account

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19 Id.
20 Besides the description of the European Monetary System in the Commission brochure, see supra note 18, the EMS is more fully discussed in Klaus Gretschmann et al., The European Monetary System, in Economic and Monetary Union: Implications for National Policy Makers 27 (Klaus Gretschmann ed., 1993); Smits, supra note 11, at 20-26; and John A. Usher, The Law of Money and Financial Services in the European Community 137-46 (1994).
The value of the ECU is fixed as a composite of a "basket" of Member State currencies with weighted values one to another. A macroeconomic calculation of the proportionate size of the national economy underlying each Member State's currency is used in allocating weights to the different currencies. The weighted value assigned to each Member State's currency in the basket was fixed at the outset. The weighted value was then revised every five years, most recently on September 21, 1989. To give an idea, in the 1989 revision, the German mark was set at 30.1% of the total basket value, the French franc 19%, the pound sterling 13%, the Italian lira 10.15%, with the other currencies set at lower percentages. In 1994, as planning for Economic and Monetary Union began, the "basket" was frozen at the 1989 levels, pending the final creation of a single currency.

The European Community uses the ECU for its own budget. All revenues and all expenditures are calculated in the form of ECUs. This enables a standard base to be used in the calculation of budget items from year to year. The European Investment Fund and other financial organs of the Community likewise deal in ECUs. These institutions and the Community itself occasionally float loans on international markets denominated in ECUs. For that matter, in the 1980s private financial institutions began to float loans denominated in ECUs. In the late 1980s, ECUs were often considered virtually as stable as Eurodollars for purposes of long term financial transactions. In 1994, the Commission estimated that there were over 200 billion ECU in private loans.

The ECU is quoted on monetary exchanges and floats against the dollar and other currencies—in December 1997, the ECU equaled $1.10. The ECU is, of course, not an actual currency: there are no bills or coins denominated in ECU, nor is the ECU used as legal tender for everyday private commercial transactions.

The second component of the European Monetary System is its system for the stabilization of exchange rates between the currencies of Member States participating in the EMS. This is called the Exchange Rate Mechanism (ERM). The exchange rates were fixed in 1979 at the outset of the EMS and have been changed only at relatively infrequent intervals. A very moderate degree of floating was initially allowed between currencies, within a band range of 2.25% above or below the exchange rate. This band was increased to 6% for certain Member States during periods of monetary stress or weakness—for example, Italy was allowed to use the 6% margin until 1989, and Portugal and Spain entered the ERM with the same 6% margin.

The functional merit of this limited rate of fluctuation around pegged rates set for long periods of time is that it serves as a reasonably close approximation of the fixed rates of the Bretton Woods system. This means that financial institutions, commercial enterprises, and private investors can enter into medium

21 For a detailed discussion of the ECU, see John A. Usher, The Legal Regulation of the European Currency Unit, 37 Int'l & Comp. L.Q. 249 (1988).

and long-term transactions with a reasonable assurance that neither an unexpected large exchange rate gain nor loss will occur at the end of the transaction. Moreover, the requirement that Member States must maintain their currencies within the flotation band means that Member States are encouraged to combat inflation and to avoid deficit spending on the one hand, and to spur investment and combat recession on the other.

The ERM's pegged exchange rate levels proved to be highly satisfactory in practice for over a decade. Realignment of rates occurred at infrequent intervals in the 1980s, and usually involved only two or three currencies. To give an example, the most significant currency realignment occurred in March 1983 when the German mark rose 5.5%, several other currencies rose 1.5% to 3.5%, and three currencies went down 2.5% to 3.5%.

The third component of the European Monetary System is a credit mechanism by which short and medium term support can be given to Member States encountering serious monetary troubles. The usual mode of support foreseen is the Very Short-Term Financing (VSTF) facility, intended to provide support for 30-45 days. A reserve fund was created, composed of the equivalent of 20% of the gold and 20% of the dollars held by each participating Member State's central bank. This fund was initially set at 25 billion ECU. The EMS can also provide medium term support for a maximum period of 5 years, with a loan fund available of up to 6 billion ECUs. A Member State receiving such a loan must reduce any deficit spending and take action to control inflation.

C. Recent Events in the EMS

Confidence in the Exchange Rate Mechanism of the EMS was badly shaken in September 1992. Stimulated by concern that France might not ratify the Maastricht Treaty, substantial speculation developed on the currency markets, directed against the currencies of Member States whose economies were perceived as weak, and in favor of the German mark. Investors perceived the German mark as the safest long-term currency, because the German central bank, the Bundesbank, persisted in keeping interest rates at very high levels in order to prevent inflation from being spurred by large government expenditures to meet the costs of German unification. Major financial interests, such as multinational corporations and pension funds, decided that it was more prudent to shift large volumes of capital from other currencies to the German mark.

Despite massive intervention efforts by central banks to support currencies under attack, the pressure increased. Several Member States nearly exhausted their currency reserves in a fruitless effort to stabilize their currency. Italy and the United Kingdom concluded that they must temporarily withdraw from the ERM and float their currencies, which then dropped sharply in an effective devaluation, and Ireland and Spain instituted emergency exchange controls. Financial observers noted that the volume of currency market activity, especially the use of currency options on a large scale, had increased enormously since the 1970s, which made it very difficult for governments and central banks to cope with speculative attacks on currencies.
Predictably, Prime Minister Major urged that movement toward economic and monetary union be delayed, while Chancellor Kohl contended that the monetary crisis demonstrated the need to move ahead toward an EMU.

The stability which the exchange rate mechanism is supposed to provide within the EMS, already shaken in September 1992, was even more seriously undermined in 1992-1995. The United Kingdom continued to stay outside the ERM, and Italy withdrew until late 1996. Although remaining within the ERM, Spain and Portugal had to devalue their currencies four times against the mark, cumulatively about 25%, and the Irish pound was devalued by 10% in early 1993.

Despite France's relatively healthy economic condition, the French franc became the subject of such a severe speculative attack on "black Friday," July 29, 1993, that even massive intervention by the German and French central banks was not sufficient to support it. The Community finance ministers and central bank governors were compelled to enlarge radically the fluctuation band of the ERM from 2.25% to 15% above or below the central standard rate. Although the exchange markets then quieted without a devaluation of the franc, the ERM has not been able formally to return to a narrower band. Indeed, in March 1995 a new wave of speculation, triggered by the Mexican debt crisis and the renewed weakness of the dollar, pushed the mark substantially higher in comparison to the franc and several other currencies.

Fortunately, since 1995 the currency markets in the Community have calmed down and exchange rate shifts have been minor. Indeed, by the end of 1996, the currencies of all the Member States operating within the Exchange Rate Mechanism were well within the 2.25% fluctuation band that had prevailed in the 1980s. Moreover, Austria, Finland and Sweden all joined the EMS (although Sweden did not join the ERM), and Italy reentered the ERM in late 1996.

Since 1996, the general exchange rate stability has been promoted by the parallel efforts of Member State governments to meet the criteria necessary to join the final stage of Economic and Monetary Union, coupled with the growing belief of financial market operators that a large majority of Member States will in fact participate in that union. However, in mid-1997, the strong economic performance of the U.S., together with a growing view that a single currency would not be as strong as the mark, pushed the dollar about 20% higher vis-à-vis the mark and other continental currencies, while the U.K. pound also rose relative to the mark, due in part to beliefs that the pound will remain a strong independent currency for at least some time after the commencement of the monetary union.

A. *The Internal Market Program*

Although certainly the manifest success of the European Monetary System in the late 1980s made renewed consideration of a monetary union plausible, it was undoubtedly the success of the internal market program that provided the greatest impetus for serious planning for EMU. To place this in its historical perspective, the early 1980s were not a particularly happy or optimistic period in Community history. Frequent strife between the Council and the Parliament over budgetary and institutional issues, bitter conflicts over finances and the agricultural policy at the level of the Council and of the European Council itself, and a sense that national barriers to intra-EC trade were multiplying rather than diminishing, all contributed to what was frequently characterized as "Europessimism" or "Eurostagnation."

The European Council meeting at Dublin in December 1984, concerned by this state of affairs, decided that the Community "should take steps to complete the Internal Market." By a fortunate coincidence in timing, a new Commission took office in 1985, led by the dynamic, far-sighted and politically adroit President Jacques Delors. Working in close collaboration with another politically astute commissioner in charge of internal affairs, Lord Cockfield, and supported by the entire Commission, they produced the famous 1985 White Paper on Completing the Internal Market. The White Paper proved an almost instant success, securing the immediate backing of the Milan European Council in June 1985, which instructed the Council to act upon the Commission White Paper proposals. Thereafter, the White Paper program captured the imagination first of industrial and financial leaders, then the media, and ultimately the public at large.

The White Paper proved to be an extraordinarily precise and persuasive program for legislative action. It contained a list of 279 proposals for legislation, together with a timetable for action. Within less than seven years, by the target date of December 31, 1992 set in the White Paper, over 95% of the complex legislative program to complete the internal market had been adopted by the Community institutions, and the Member States were well along in the process of enacting implementing measures.


24 European Commission, White Paper on Completing the Internal Market, COM (85) 310 final (June 1985) [hereinafter White Paper]. Following the British nomenclature, the Commission refers to documents containing a program for action as "white papers," thus distinguishing them from "green papers," which are issued for study and comment. Compare note 3, supra. The March 1985 Brussels European Council specifically requested the Commission study which became the White Paper. See Bull. EC 3-1985, at 12.


The extraordinary success of the internal market program naturally promoted greater confidence within the Community institutions and within the political leadership of the Member States as proposals for monetary union began to be advanced. Moreover, monetary union could easily be seen, as noted before, as the "essential and logical complement" to the internal market program. The achievement of a truly European marketplace could clearly never be fully realized so long as monetary frontiers and national currencies made national markets less accessible to products and services coming from other Member States. The creation of a monetary union readily became the next challenge after the progress made in developing an internal market. An integrated internal market appeared a truncated success without the cap of a monetary union.

B. The 1989 Delors Report

Already in 1985, there was awareness of the link between the internal market program and a monetary union. The Luxembourg Intergovernmental Conference, held in the fall of 1985, produced an important series of EEC Treaty amendments called the Single European Act (SEA), whose principal purpose was to add Article 8a (renumbered by the TEU as Article 7a), formally enunciating the goal of attaining an internal market by December 31, 1992. Additionally, the SEA significantly modified the legislative procedure used to adopt internal market measures by an amendment, Article 100a, which enables both easier and more democratic legislative action. Although little noted at the time, the SEA also added a new chapter, Cooperation in Economic and Monetary Policy (Economic and Monetary Union), to the EEC Treaty. This

detailed discussion of the White Paper and the internal market program, see the author’s Chapter 12 in Berrmann et al., supra note 6, and the reference books cited in note 8, supra. Lord Cockfield has written a fascinating narrative describing the background of the White Paper in Francis A. Cockfield, The European Union: Creating the Single Market (1994).

27 Green Paper, supra note 3.

28 An Intergovernmental Conference (IGC) is composed of authorized representatives from each Member State, meeting to discuss possible amendments to the European Community Treaty, pursuant to Article 236 (now deleted and replaced by Article O of the Treaty on European Union). An Intergovernmental Conference functions through frequent, sometimes almost daily, meetings of experts who do most of the preparatory work and initial drafting, together with regular (though more occasional) meetings of representatives at the ministerial level who decide the more important issues and agree upon the final text. Article 236 does not specify any voting mechanism in order to call an IGC. Denmark and the United Kingdom opposed the calling of the Luxembourg IGC, but respected the desire of the majority to hold it.

29 See supra note 7.

30 Article 100a enabled most internal market legislation to be adopted by the Council through the use of qualified majority voting rather than by unanimous approval, and it required the use of the parliamentary cooperation procedure, which obliges the Council to weigh very seriously any amendments proposed by Parliament. Among the many useful articles analyzing the background, scope and effect of the Single European Act are: Claus-Dieter Ehlermann, The Internal Market Following the Single European Act, 24 Common Mkt. L. Rev. 361 (1987); and Hans-Joachim Glaesner, The Single European Act: Attempt at an Appraisal, 10 Fordham Int'l L.J. 446 (1987). At the time, Ehlermann was Director-General of the Commission Legal Service and Glaesner was Director-General of the Council Legal Service.
consisted of a new Article 102(a),\textsuperscript{31} which called for further cooperation to meet the objectives of Article 104, and which raised the possibility of further EEC Treaty amendments to make institutional changes. Eventually, as the Community progressed toward achievement of the internal market, proposals for an Economic and Monetary Union moved to center stage.

At its June 1988 Hanover meeting, the European Council, incited particularly by Chancellor Kohl of Germany and President Mitterand of France, referred to Article 102(a) and "confirmed the objective of progressive realization of economic and monetary union."\textsuperscript{32} The European Council created a special committee, chaired by Commission President Jacques Delors (who was formerly French Finance Minister and an acknowledged monetary expert), to study and propose "concrete stages" toward this goal. The committee consisted of all Member State central bank governors and several economic and banking specialists.\textsuperscript{33}

The Delors Committee Report of April 17, 1989 provided a thorough review of the essential character of an Economic and Monetary Union, together with a pragmatic presentation of three proposed stages in its development.\textsuperscript{34} Although the Delors Report was certainly influenced by the Werner Report, economic and monetary conditions had changed radically since 1970, and the Delors Report both reflected an awareness of the current realities and represented a far more detailed and concrete approach to the creation of a monetary union. Due partly to the practical nature of the committee's proposals, and partly to respect for the high qualifications of the committee itself, this report not only formed the basis for all subsequent discussions, but largely shaped the agenda of the 1990 Rome Intergovernmental Conference.

The Delors Report defined the EMU's aim as the common management of monetary and economic policies to attain common macroeconomic goals. It identified three preconditions for the establishment of an EMU, namely, total and irreversible convertibility of currencies; complete liberalization of capital transactions and integration of the financial sector; and irreversible locking of exchange rates. The report also endorsed the ultimate adoption of a single European currency. The report proposed a treaty amendment to create a major new institution, the European System of Central Banks (ESCB). Initially only an advisory body, the ESCB would evolve through different stages of activities. Its ultimate role would be to formulate and implement monetary policy for the

\textsuperscript{31} Article 102a was deleted by the Treaty on European Union. Its text can be found in the sources cited in note 9, supra.

\textsuperscript{32} Bull. EC 6-1988, at 165.

\textsuperscript{33} The central bank governors served on the committee in their personal capacity, i.e., they did not necessarily represent the views of their national governments. The experts serving on the committee were Commissioner Andriessen, Baron Lamfalussy (General Manager of the Bank for International Settlements in Basel), Miguel Boyer (President of Banco Exterior de Espana), and Niels Thygesen (professor of economics in Copenhagen).

Community, participate in banking supervision on a Community level, and assist Member States to attain price stability and curb budgetary deficits. The ESCB would be composed of all the governors of national central banks, together with a group of central administrators serving for fairly long terms. (The U.S. Federal Reserve System and the German Bundesbank were obviously the models for much of the ESCB structure.)

The Delors Committee Report further laid out three proposed stages toward achieving the EMU. Each stage would require the attainment of certain results, both at the Community and Member State levels. The final stage would give the ESCB responsibility for monetary policy, lock exchange rates, and perhaps lead to the creation of a common Community currency.

The Delors Report initiated a widespread and probing debate on the necessity for, and the goals of an EMU, both at the Community level and in the private sector, and the topic received great attention in the media. It quickly became the most fascinating single idea for the further unification of the European Community since the 1985 Commission White Paper on Completing the Internal Market. Although most commentary on the Delors Report was favorable, John Major, then Tory Chancellor of the Exchequer, issued on November 2, 1989 a policy statement for the United Kingdom advocating national control over monetary policy and criticizing any transfer of power to a centralized bureaucracy, and specifically repudiating the idea of a single European currency. Overcoming the objections of the U.K. government and the reluctance of other Member States to abandon national control over monetary policy and the natural attachment to their own currency clearly represented a difficult task for Community leaders.

C. The Rome Intergovernmental Conference

At this point, the reaction of the European Council to the Delors Report became critical. At its December 1989 meeting in Strasbourg, the European Council approved the main themes of the Delors Report. Moreover, after intensive debate, the European Council voted 11 to 1, over the opposition of the United Kingdom, to call an intergovernmental conference for the purpose of planning an Economic and Monetary Union. The European Council specifically urged the intergovernmental conference to respect the principle of subsidiarity in formulating plans for an EMU, i.e., the Community’s institutions should not be given monetary functions or powers that can be better exercised by the Member States. The European Council finally decided that the first stage set out in the Delors Report should commence as of July 1, 1990, the date of entry into effect of the 1988 directive on freedom of capital movements. A March 1990 Commission study, “EMU: economic rationale and design of the system,” presented by Commissioner Christophersen, then responsible for

37 See infra Part IV for further discussion of this directive.
monetary affairs, recommended that the European System of Central Banks (then popularly known as the Eurofed) should "have a large degree of independence," but that it should nonetheless be "democratically accountable for its actions." The study also emphasized that the ESCB should delegate most policy implementation to the central banks, in accordance with the principle of subsidiarity. The study further endorsed the idea that the ECU should become a single currency for the Community, and not a thirteenth currency in use alongside national currencies. This study served as the basis for a Commission Communication on economic and monetary union, issued on August 21, 1990, which essentially represented the Commission's proposals for the Intergovernmental Conference agenda. Also of influence during this period were the studies and proposals of the Committee of Central Bank Governors, notably its draft statute for the ESCB.

During the year preceding the Rome Intergovernmental Conference, the Conservative government of the United Kingdom continued its strong opposition to key features of the EMU. Prime Minister Thatcher opposed the idea of a European central bank and preferred a weaker body which would only coordinate monetary policy. The U.K. also rejected the concept of Community macroeconomic policy making. Instead of a single European currency, John Major, then Chancellor of the Exchequer, proposed that the ECU represent a thirteenth or alternative currency.

The European Council meeting in Rome in October 1990 effectively set the agenda for the intergovernmental conference. Over the opposition of the U.K., the European Council decided that there should be "a new monetary institution comprising Member States' central banks, and a central organ, exercising full responsibility for monetary policy." The European Council also decided that there should be a single currency, that the new monetary institution should have price stability as its primary objective, that national central banks should be independent of national governments, and that the second stage leading to monetary union should begin on January 1, 1994. Thus, a number of the key features of the later monetary provisions of the TEU were settled in principle at the outset of the intergovernmental negotiations.

The Rome Intergovernmental Conference (IGC) began on December 15, 1990, at the conclusion of a European Council meeting that devoted principal

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40 Submitted on Nov. 27, 1990, the draft statute for the ESCB was published in Europe, Doc. No. 1669/1670 (Dec. 8, 1990).
42 For the nature of an Intergovernmental Conference, see note 28, supra. Although the U.K. opposed the creation of EMU, it participated fully in the IGC negotiations on the topic.
attention to the political issues that would be addressed by the IGC. The IGC worked earnestly for a year, drafting the text of the Treaty on European Union. For greater efficiency, the IGC worked in two distinct groups, one concentrating on the issues surrounding EMU, and the second on the more political issues involving the operations of the Community, the respective powers of the Council and the Parliament, and the elaboration of the Common Foreign and Security Policy and Coordination in Justice and Home Affairs.

To serve as a functional agenda for the discussions of the IGC group dedicated to the issues of EMU, the Commission presented a draft treaty text on December 10, 1990. This can now be assessed as a bold, but successful Commission initiative, showing again the leadership of President Delors and his colleagues. The draft followed closely the Delors Report and the October Rome European Council meeting conclusions, and it greatly influenced the final TEU text that emerged from the IGC.

Following six months of careful review of the Commission draft, the Luxembourg Presidency presented a new text in June 1991, with intensive final debate during the Dutch Presidency in the fall. The Dutch, French, German and U.K. representatives were particularly active in shaping the final text. Most of the articles relating to the Economic and Monetary Union were prepared by technical experts tending to follow the views of Germany and The Netherlands, both states with powerful central banks and a tradition of strict monetary policy and hard currencies. Reaching a consensus proved extremely difficult, due not only to U.K. opposition, but also to hesitations on the part of other Member States. Ultimately, several issues were left to the European Council meeting at Maastricht in December 1991, which, after intensive debate, arrived at essential compromises (notably, the right of Denmark and the United Kingdom to opt out of participation in the final stage of EMU). Thus the TEU provisions on Economic and Monetary Union could finally be completed. Before discussion of these TEU provisions in Part V, however, the important and related topic of free movement of capital should be reviewed.

IV. FREE MOVEMENT OF CAPITAL AS A PRE-CONDITION FOR MONETARY UNION

A. The Treaty of Rome and Early Developments

Free movement of capital is an essential condition for the attainment of an Economic and Monetary Union. Significant restrictions on the movement of capital, or upon payment for sales or services, would frustrate the achievement

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43 The Commission's draft treaty text is described in Italianer, supra note 39, at 66-68.
44 For an extremely detailed review of the drafting of all the key EMU provisions, comparing their status in the various drafts, see Italianer, supra note 39, at 68-111. The text of the Luxembourg Presidency draft (along with texts of other related documents and drafts) is reprinted in Richard Corbett, The Treaty of Maastricht—From Conception to Ratification: A Comprehensive Reference Guide (1993). Since Luxembourg served as President of the Council and of the European Council from January through June of 1990, it likewise acted as President of the IGC.
45 See infra Part V.
of an integrated monetary system and of an integrated market with a single currency. Accordingly, the Delors Report stipulated that free movement of capital was a requirement for the first stage of movement toward EMU.

The Treaty of Rome contained detailed provisions for attaining free movement of capital, one of the “four freedoms” along with free movement of goods, services and persons. The basic provision, Article 67, declared that “Member States shall progressively abolish between themselves all restrictions on the movement of capital.” However, this declaration of principle was modified by the language, “to the extent necessary to ensure the proper functioning of the common market.”

The Court of Justice relied upon this rather ambiguous proviso in concluding that Article 67 did not have direct effect, and therefore required implementing legislation to be adopted by the Council, pursuant to the legislative procedures set out in EC Treaty Article 69. In 1981, in Criminal Proceedings against Casatti, the Court accordingly rejected a challenge to Italian exchange controls brought by a private party defendant based upon the alleged direct effect of Article 67. The Court’s judgment thus left in place national exchange controls long after the end in 1969 of the transition period to achieve the common market. The Court reached this conclusion, despite the fact that it had previously held that Articles 9, 12, 30 and 34, achieving free movement of goods, Article 48 on free movement of workers, Article 52 on the right of establishment, and Article 59 on the free provision of services, all had direct effect after the end of the transition period in 1969. Presumably the Court was motivated in Casatti by a view that the monetary sphere was particularly sensitive and that free movement of capital could only safely be executed through careful review and regulation by the Council.

The Court did, however, advance the cause of free movement of capital significantly in Luisi & Carbone v. Ministero del Tesoro. In that judgment the

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46 Article 67 of the EEC Treaty, together with the related Articles 68-73, were deleted by the Treaty on European Union in 1993. For the original text, see the sources cited in note 9, supra.


48 The doctrine of the direct effect of Treaty articles means that certain articles, whose terms are deemed to be sufficiently precise, absolute and unconditional in conferring rights on individuals, can be invoked by persons and enterprises in national court proceedings in order to set aside contrary national legislation. The doctrine, developed by the Court in 1962, constitutes one of the most powerful means of effectively achieving Community law. See, e.g., Van Gend en Loos v. Nederlandse Administratie der Belastingen, Case 26/62, 1963 E.C.R. 1 (proclaiming the doctrine of direct effect of Treaty articles for the first time, and holding that Article 12 has direct effect); Ianelli & Volpi SpA v. Meroni, Case 74/76, 1977 E.C.R. 557 (Article 30 held to be “mandatory and explicit” and therefore having direct effect); Pigs Marketing Board v. Redmond, Case 83/78, 1978 E.C.R. 2347 (Article 34 has direct effect); Van Duyn v. Home Office, Case 41/74, 1974 E.C.R. 1337 (Article 48 has direct effect); Reyners v. Belgium, Case 2/74, 1974 E.C.R. 631 (Article 52 has direct effect, despite its textual reference to the need to abolish restrictions on the right during the transition period); Van Binsbergen v. Bestuur van de Bedrijfsvereniging, Case 33/74, 1974 E.C.R. 1299 (Article 59 has direct effect).

49 Cases 286/82 & 26/83, 1984 E.C.R. 377. With regard to services, the court concluded that free movement of services applied to give rights of movement to persons who want to go to other States to receive services just as it does to the providers of services who want to carry out trans-border
Court held that Article 106, requiring the liberalization of national rules restricting the trans-border transfer of payments to the extent that free movement of services has been attained, had direct effect inasmuch as Article 59 on the free provision of services also had direct effect. This conclusion caused the removal of Italian and other Member States’ exchange control restrictions on the transborder transfer of funds to pay for services, e.g., in the fields of medical treatment, education and tourism.

Two early measures, the First Capital Directive 921/60 of May 11, 196050 and the Second Capital Directive 63/21 of December 18, 1962,51 did provide for substantial liberalization, freeing most common commercial and private movements of capital from exchange controls or other governmental restrictions.52 For example, the directives ended restrictions on personal capital movements (through gifts, inheritance, or movements resulting from the change of a person’s residence), on the purchase or sale of real estate, on the purchase or sale of securities, on the transfer of insurance premiums and payments, and on short or medium term credit connected with commercial transactions. However, most common banking or finance transactions were not liberalized by the two directives.

This early progress was set back in the 1970s, when several Member States sought to use exchange controls to protect their monetary policies and their currencies during and after the world-wide energy recession. Articles 73, 108 and 109 of the EEC Treaty permitted emergency safeguard measures by the Community, or in emergencies by Member States themselves, with the acquiescence of the Commission. France and Italy made extensive use of such exchange controls. Moreover, when Greece, Portugal and Spain joined the Community in the 1980s, these states had a long tradition of exchange controls, and the Treaties of Accession permitted them to keep such controls for long transition periods.

It is noteworthy that when the Commission issued the famous White Paper on Completing the Internal Market in June 1985, it did not include in its legislative agenda any measure for achieving complete free movement of capital. When, however, the internal market program met with enthusiastic endorsement, the Commission proposed such a measure, and it was adopted with surprising ease and rapidity. Presumably the Member States regarded the proposed directive on free movement of capital as indispensable to an integrated financial market.


52 The directives’ provisions are carefully analyzed by a Commission Legal Services specialist in Peter Oliver, Free Movement of Capital Between Member States: Article 67(1) and Implementing Directives, 9 Eur. L. Rev. 401 (1984). This review was supplemented, with special attention to the Court’s case law, in Peter Oliver & Jean-Pierre Baché, Free Movement of Capital between the Member States: Recent Developments, 26 Common Mkt. L. Rev. 61 (1989).
B. The 1988 Directive and EC Treaty Article 73

Directive 88/361 to implement Article 67\(^53\) mandated the removal of all forms of government restrictions on the movement of capital, and on all payments for goods and services, no later than July 1, 1990 (although Ireland and Spain were allowed to keep certain restrictions until 1992, and Greece and Portugal until 1995). The Directive was rapidly implemented by France and Italy\(^54\)—a rather dramatic development, since their exchange controls dated in some instances to the 1940s. Greece, Ireland, Portugal and Spain also acted to abolish their exchange control structures before the end of their periods of derogation, so that free movement of capital under Directive 88/361 became fully effective in 1994.\(^55\)

Even more important than the Directive was the Maastricht Treaty's insertion of Article 73 into the EC Treaty, totally replacing Article 67 and the related EEC Treaty provisions. The core coverage is now Article 73b:

1. Within the framework of the provisions set out in this Chapter, all restrictions on the movement of capital between Member States and between Member States and third countries shall be prohibited.
2. Within the framework of the provisions set out in this Chapter, all restrictions on payments between Member States and between Member States and third countries shall be prohibited.\(^56\)

The language is absolute and unconditional. It is therefore not surprising that the Court of Justice held that Article 73b has direct effect, enabling private parties to invoke it to strike down incompatible Member State legislation or regulations. This occurred in Criminal Proceedings against Sanz de Lera.\(^57\) In that judgment, the Court also interpreted Article 73d, which permits Member State "measures to prevent infringements of national law and regulations, in particular in the field of taxation and the prudential supervision of financial institutions." The Court concluded that Article 73d permitted Spain to require a prior declaration to its responsible authorities before the export of large sums in banknotes, in order to deter "tax evasion, money laundering, drug trafficking or terrorism," but that Article 73d did not permit any system of prior or subsequent authorizations or licenses for such movements of funds.\(^58\)

Thus, Article 73, as interpreted by the Court in Sanz de Lera, requires the complete free movement of capital since January 1, 1994. Member States may only enforce limited systems of prior declarations for large capital movements, in cash or otherwise, in order to try to prevent illicit activities, or "for purposes

\(^{53}\) 1988 O.J. (L 178) 5.
\(^{54}\) France acted by Decree 89/154 of March 9, 1989, and Italy by a Decree of April 27, 1990.
\(^{55}\) For more detailed and relatively current coverage of free movement of capital, see Usher, supra note 20, at 14-39. See also Weatherill & Beaumont, supra note 8, at 647-52.
\(^{56}\) EC Treaty, art. 73b, as amended by the TEU.
of administrative or statistical information, or [as] justified on grounds of public policy or public security." A vital pre-condition for monetary union was accordingly achieved.

V. THE MAASTRICHT TREATY PROVISIONS ON ECONOMIC AND MONETARY UNION

A. The Three Stages in Achieving Monetary Union

No aspect of the Maastricht Treaty on European Union is of greater practical importance than the provisions on Economic and Monetary Union. Article B of the TEU lists an economic and monetary union and a single currency as among the principal objectives of European Union. A new Article 3a of the EC Treaty declares that the Community should adopt a common economic policy, to be attained "in accordance with the principle of an open market economy with free competition." Article 3a(2) further requires:

the irrevocable fixing of exchange rates leading to the introduction of a single currency, the ECU, and the definition and conduct of a single monetary policy and exchange-rate policy the primary objective of both of which shall be to maintain price stability and, without prejudice to this objective, to support the general economic policies in the Community, in accordance with the principle of an open market economy with free competition.

Thus, the guiding principles of an Economic and Monetary Union are given Treaty (or constitutional) force. Note in particular the emphasis upon "price stability," i.e., the maintenance of a low inflation rate (usually perceived to be 2% or less), as the "primary objective" of the Community's monetary policy. Article 3a(3) notes other guiding principles: "stable prices, sound public finances and monetary conditions and a sustainable balance of payments."

The TEU amendments to the EEC Treaty providing for aspects of the economic and monetary union, together with the Protocols, are extremely complicated. Only an overview is presented here, concentrating on the stages for progressive creation of the EMU, and upon the key features of the proposed institutional structure for the monetary union.

59 EC Treaty, art. 73d.
60 For the text of Article 3a of the European Community Treaty, introduced by the TEU, see sources cited in note 2, supra.
61 EC Treaty, art. 3a(2).
62 Professor Snyder of the European University Institute in Florence has aptly observed that this is "the first time in the industrialized world [that] the objectives of economic policy thus are stated explicitly in a constitution." Francis Snyder, EMU—Metaphor for European Union—Institutions, Rules and Types of Regulation, in Europe after Maastricht: An Ever Closer Union?, at 63, 66 (Renaud Dehousse ed., 1994).
63 Probably the best single reference source for a detailed analysis of the EMU provisions of the TEU is Smits, supra note 11. Smits, General Counsel of The Netherlands Central Bank, was actively involved in the planning of EMU. Also valuable are: Economic and Monetary Union: Implications for National Policy-Makers (Klaus Gretschmann ed., 1993) [hereinafter EMU: Implications]; and European Monetary Integration (P. Welfens ed., 2d ed. 1994). EMU is usually covered rather briefly
Although the EC Treaty goal is one of an Economic and Monetary Union, the substantive EC Treaty provisions differ sharply in their delineation of the economic as opposed to the monetary sphere. Article 3a(2) requires "the definition and conduct of a single monetary policy," and subsequent articles describing the modes of achieving this warrant the conclusion that the EC Treaty intends to shape a true monetary union, a supranational structure.\textsuperscript{64} In contrast, Article 3a(1) only states the goal of a Community "economic policy . . . based on the close coordination of Member States' economic policies." This has much more of an intergovernmental flavor—the Member States devise their own economic policies, and their only Community obligation is one of coordination.\textsuperscript{65}

On the one hand, it is obvious that a monetary union cannot function well without coordination of economic policies, because of the substantial spill-over effect of governmental economic policy decisions upon monetary conditions. On the other hand, centralized Community economic policy-making would require an enormous cession of national sovereignty, because of the close link between economic policy and fiscal policy, tax collection, social security and social welfare systems, and so on. It may be that a successful EMU will lead to greater Community harmonization of Member State tax and social security systems, but for the present the EC Treaty only requires coordination of national economic policies.

In the substantive EC Treaty provisions, a new Article 103 requires Member States to "regard their economic policies as a matter of common concern" and to coordinate them in accordance with guidelines established by the Council, acting by qualified majority. Because this is a highly sensitive area, the Council must first submit its draft guidelines to the European Council for its "conclusion" on them. This is one of the instances in which the TEU recognizes a specific role for the European Council, but still one within the overall Article B mandate that the European Court should give policy guidelines—the Council still takes the final legal act.\textsuperscript{66} The Parliament is to be kept informed, but does

\textsuperscript{64} Snyder, supra note 62, at 66 & 69.

\textsuperscript{65} For Professor Snyder, a single monetary policy, "even if subject to checks and balances, demands uniformity," while coordination of economic policies "tolerates diversity." Id. at 66. In contrast, Smits lays stress on Article 3a's goal of "an economic policy" (in the singular) and contends that the coordination of Member State policies should "result in a single economic policy" for the Community. Smits, supra note 11, at 66.

\textsuperscript{66} The background for this approach is discussed in Italianer, supra note 39, at 95-96.
not participate in shaping the guidelines.\textsuperscript{67} I will discuss further the recent execution of this economic coordination in Parts VII and VIII.

The Maastricht Treaty follows the three stage structure proposed in the 1989 Delors Report for the gradual creation of EMU. In accordance with this scheme, on June 1, 1990, the Community began the first stage of progress toward the EMU. The first stage had three components: (1) free movement of capital, already achieved by the 1988 directive described previously in Part IV.B; (2) adherence (at least in principle) of all Member States to the European Monetary System and to its Exchange Rate Mechanism; (3) an increased level of monetary coordination, both by governmental action and through coordination among the central banks.\textsuperscript{68} Somewhat curiously, the TEU never specifically mentions the first stage, but takes it for granted.

The Treaty fixes January 1, 1994 as the date for passage to the second stage (Article 109e). The second stage, from 1994 to the end of 1998, has two essential features: the creation of the European Monetary Institute (EMI), and the commencement of an obligation on the part of Member States to strive to meet certain key economic and monetary conditions for EMU, the so-called convergence criteria.\textsuperscript{69} These conditions which Member States must try to fulfill during the second stage are critical to further progress, but have proved quite difficult to attain for many States.\textsuperscript{70}

The European Monetary Institute (EMI) is described in Article 109e, and the EMI's Statute is laid down in a Protocol.\textsuperscript{71} The EMI is composed of a President, named by common accord of the Member States, together with the governors of the Member State central banks. The EMI's purpose is to coordinate policy and action by the central banks, monitor the European Monetary System, and prepare the instruments and procedures for the single monetary policy of the third stage. The Committee of Governors of Central Banks, created in 1964, has now been replaced by the EMI.\textsuperscript{72} Although it was initially proposed during the Rome IGC that the EMI begin assuming some central bank governance powers, the final TEU text gave the EMI no central bank functions.\textsuperscript{73} The EMI is essentially

\textsuperscript{67} Parliament's minor role is an example of the "democratic deficit," to be discussed further in Part VI.C, infra.

\textsuperscript{68} For a general discussion of the first stage, see Smits, supra note 11, at 41-45. For a description of the operations of the Monetary Committee and the Committee of Governors of Central Banks, which carried out the principal task of monetary coordination during the first stage, see Snyder, supra note 62, at 71-73.

\textsuperscript{69} Smits describes the second stage in detail. Smits, supra note 11, at 45-52.

\textsuperscript{70} For the purpose of a more coherent presentation, the description of the "convergence criteria" and the current state of progress within the Community in the effort to achieve them is provided in Part VII, infra.

\textsuperscript{71} For a more detailed description of the composition, role and function of the EMI, see Pipkorn, supra note 63, at 282-84; Smits, supra note 11, at 49-51; and Snyder, supra note 62, at 74-76.

\textsuperscript{72} EC Treaty, art. 109(1).

\textsuperscript{73} See Italianer, supra note 39, at 93-94. Smits remarks that in this stage, monetary policy remains a Member State central bank's responsibility; until the third stage, there is to be no "monetary policy of the Union." Smits, supra note 11, at 50.
intended to be an intermediary body, paving the way for the European System of Central Banks (ESCB), described below.\(^4\)

Economic and Monetary Union is to be fully achieved in the third and final stage, which consists of: (1) the creation of the European Central Bank and the European System of Central Banks, whose role is to exercise the principal monetary powers of the EMU; (2) a binding system of regulation for the monetary policies of the Member States participating in the final stage of EMU; and (3) the creation of a single currency for the participating Member States, ultimately in the form of banknotes and coins which will serve as the sole legal tender.\(^5\)

A qualified majority decision of the Council will determine which Member States have satisfied the convergence criteria and will participate in the third stage.\(^6\) However, the importance of the decision is such that the Council shall meet in an extraordinary session of the Heads of State or Government, which makes this virtually a European Council decision. The TEU presumably did not formally make this action one to be taken by the European Council, because to date that body has never been given any legislative or legally-binding decision-making function, and because the European Council usually reaches its policy decisions by consensus, while it was desired to use only a qualified majority vote to select those Member States which qualify for entry into the final stage of EMU.\(^7\) Indeed, it was the December 1991 Maastricht European Council itself which dictated the unusual composition of the Council for purposes of Article 109j in order, as Italianer notes, that the decision be taken formally "at the highest political level and within the Community legal framework."\(^8\) The Council will act on the basis of reports produced by the Commission and the EMI, together with specific recommendations from the Commission, and the Parliament must provide an opinion.\(^9\)

Article 109j(3) foresaw that the Council might act to commence the third stage by a decision taken before December 31, 1996 if a majority of Member States met the necessary criteria, but this in fact did not occur.\(^10\) Article 109j(4) prescribed a fall-back position: in all events, the third stage is to begin on January 1, 1999 for those Member States which fulfill the prescribed economic and monetary conditions, even if they do not represent a majority of the

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\(^4\) France, Italy and the Commission urged during the IGC that the European Central Bank be created at the start of stage two, while Germany opposed this suggestion. The idea of an EMI came in a compromise proposed by Belgium. See Pipkom, supra note 63, at 283. Italianer gives further details on the drafting of the EMI provisions. Italianer, supra note 39, at 91.

\(^5\) The second and third aspects of EMU will be further discussed in Parts VIII and IX respectively.

\(^6\) EC Treaty, art. 109j.

\(^7\) Italianer, supra note 39, at 100.

\(^8\) Id. at 100; see also id. at 97-100. For a general review of the Article 109j procedure, see Smits, supra note 11, at 116-20.

\(^9\) EC Treaty, art. 109j(1)-(4).

\(^10\) The December 1996 Dublin European Council formally decided that it was not possible to commence EMU at that time. See infra note 264 and accompanying text.
Community States. In effect, this means that the "two-tier" or "two-speed" Europe approach of the EMS will definitely persist in the EMU—some Member States will participate from the outset, while others will join later (or, conceivably, will never join).

However, the fact that some Member States will not be able to qualify to join the final stage of EMU (or may choose not to do so) will have much more serious implications than the non-participation of certain states in EMS ever did. As Professor Slot has observed, the economies of the non-participating Member States may develop quite differently from those within the monetary discipline of EMU, and the "multi-tier system may also jeopardize the unity and the functioning of the internal market and the homogeneity of Community Law." Fortunately, as we shall see in Part VII, it is currently likely that eleven Member States will be able to qualify for entry into the third stage of EMU, and the others are also expected ultimately to join in that stage.

Due to the implacable opposition of the U.K. government, then led by Prime Minister Major, to any absolute obligation on Member States to join in the final stage of EMU, the European Council meeting at Maastricht in December 1991 agreed upon a special Protocol for the U.K. By its terms, the U.K. has an option to remain outside of the third stage of monetary union even if it meets the economic and monetary conditions set to join it. Denmark then demanded and received a similar Protocol. As a consequence, both Denmark and the U.K. have the right not to participate in the monetary union, i.e., not to be represented in the European System of Central Banks nor to be governed by its rules, and not to replace their currency with the single currency, the euro. These protocols represent perhaps the most important compromise struck by the European Council meeting at Maastricht, certainly crucial in enabling EMU to go forward.

81 Pipkorn observes that the December 1991 Maastricht European Council added Article 109(4) in order to "underline the irreversible character of the move towards EMU." Pipkorn, supra note 63, at 289. However, he contends that Article 109(4) does not have any direct effect, i.e., does not mean that certain qualifying States will automatically enter EMU on January 1, 1999, but rather that the Council must decide whether enough States qualify to make EMU "workable and credible." Id. at 290. Smits calls the transition to the third stage on January 1, 1999 "semi-automatic," but also believes that the Council could postpone that date if not enough States qualified to form "a manageable group." Smits, supra note 11, at 120.

82 Slot, supra note 63, at 244.

83 Id. at 245.

84 The U.K.'s initial position was that no state should enter EMU until after its government should have ratified the decision to enter in accordance with its national constitutional requirements. When this view was rejected by the IGC, the U.K. demanded that it should have the political option whether or not to join the final stage. See Pipkorn, supra note 63, at 287.


86 TEU, Protocol on Certain Provisions Relating to Denmark (also expressly contains a reference to Denmark's power to abrogate any initial decision to opt out of the third stage). For a description, see Smits, supra note 11, at 137-38.

87 The U.K. Protocol is more detailed than that for Denmark, e.g., in ruling out any obligation to avoid excessive government deficits. See Italianer, supra note 39, at 97-98; Smits, supra note 11, at 138-39.
On their side, Denmark and the United Kingdom stipulated in another Protocol\textsuperscript{88} that they would not "prevent the entering into the third stage," an important point because the two states will be represented in the Council meeting held for this purpose under Article 109j(4). At the time of the Edinburgh European Council meeting in December 1992, the other Member States recognized Denmark's exercise of its option not to join in the third stage,\textsuperscript{89} a decision that was apparently quite critical in obtaining the requisite majority in the second Danish referendum that finally ratified the TEU in June 1993. The U.K., initially under the government of Prime Minister Major, and since May 1997 under that of Prime Minister Blair, has carefully kept open its option whether or not to join in the third stage sometime after 1999.

Those Member States which are unable to meet the convergence criteria in 1998 and join EMU in 1999 are not, of course, irrevocably shut out. The Rome IGC decided early on that there should be a periodic reexamination of the qualifications of the non-participating Member States (or "Member States with a derogation," to use the TEU term). The final text of Article 109k stipulates that every two years (hence, initially in the spring of 2000) the Council in its composition of Heads of State or Government will examine the degree to which "States with a derogation" satisfy the convergence criteria. Furthermore, upon demand by any Member State, the Council will examine its qualifications on an ad hoc basis.\textsuperscript{90} Naturally, the governors of the central banks of "States with a derogation" will not be members of the Governing Council of the ECB, nor will those states participate in the election of the Executive Board of the ECB or vote on certain other Council decisions appropriate only for those states participating in the third stage of EMU.\textsuperscript{91}

B. The European Central Bank and the European System of Central Banks

When the third stage begins, the European Central Bank (ECB) and the European System of Central Banks (ESCB), described in Article 106 and a Protocol,\textsuperscript{92} will replace the European Monetary Institute, which will then be liquidated.\textsuperscript{93} The ESCB will be composed of a European Central Bank (ECB) and the national central banks. The ECB in turn will have an Executive Board

\textsuperscript{88} TEU, Protocol on the Transition to the Third Stage of Economic and Monetary Union.


\textsuperscript{90} See Smits, supra note 11, at 136-37.

\textsuperscript{91} EC Treaty, art. 109k(3)-(5).

\textsuperscript{92} The complex TEU provisions on the structure and role of the ECB and the ESCB are ably surveyed in Smits, supra note 11, at 92-115. See also Slot, supra note 63, at 231-36. Italianer informs us that on November 27, 1990, the Committee of Governors of Central Banks presented the Rome IGC with a draft Statute of the ESCB which provided important input. Italianer, supra note 39, at 65. Most of the TEU text on this topic was already settled by the time of the Luxembourg Presidency draft in June 1991. Id. at 79-80.

\textsuperscript{93} The modalities of liquidation of the EMI are set out in TEU, Protocol on the Statute of the EMI, art. 23. "All assets and liabilities of the EMI shall then pass automatically to the ECB," and the President of the EMI "shall relinquish his office." Id.
composed of the President, a Vice-President, and four members, all named for eight-year terms by common accord of the Member States participating in the third stage, without any possibility of reappointment.\textsuperscript{94} Parliament is only consulted in the process of the Executive Board selection.\textsuperscript{95} The ECB's Governing Council, composed of the Executive Board and the Governors of the participating Member State central banks, will be the usual decision-making body, although some issues of lesser importance may be dealt with by the Executive Board alone.\textsuperscript{96} In operational terms, the decisions of the Governing Council will normally be carried out by the national central banks. This structure is accordingly analogous to that of the U.S. Federal Reserve Board and the Bundesbank.\textsuperscript{97}

EC Treaty Article 107 states the important principle that the ECB, the ESCB, and Member State central banks shall have total independence in their decision making.\textsuperscript{98} They are categorically forbidden to take instructions either from Community institutions or from Member States. This provision represents a major policy decision, because most central banks were not independent of their governments,\textsuperscript{99} and because some Member States were reluctant to allow the ECB and ESCB to enjoy total independence from the Council. The principle of

\textsuperscript{94} EC Treaty, art. 109a. EC Treaty, art. 109I(1) specifies that the designation of the initial Executive Board be made by common accord of the participating States only, and that they may decide to limit its initial membership to four or five, rather than six.

\textsuperscript{95} TEU, Protocol on the Statutes of the ESCB and the ECB, art. 50 stipulates this, as well as requiring the consultation of the EMI Council. Smits speculates that Parliament may review the qualifications of proposed Executive Board members in a process analogous to "confirmation hearings" in the U.S. Senate on proposed Federal Reserve Board members. Smits, supra note 11, at 96-97. He also finds it "peculiar that no place was found for the Commission in the nomination process." Id. at 96.

\textsuperscript{96} Professor Slot of Leyden well observes, however, that the "daily business" managed by the Executive Board, is "often of decisive importance in monetary policy." Slot, supra note 63, at 235.

\textsuperscript{97} The Bundesbank was certainly the basic model. Its Central Bank Council (Zentralbankrat) consists of a Directorate (Direktorium) of a President, Vice-President and six other members named by the German Federal Government, serving together with the nine presidents of the State Central Banks (Landeszentralbanken). See Gormley & de Haan, supra note 63, at 99; Smits, supra note 11, at 159. The Bundesbank in turn is substantially modeled on the U.S. Federal Reserve Board. For a description of the structure and role of the Federal Reserve System, see Michael P. Malloy, 1 Banking Law and Regulation § 1.3.2 (1997).

\textsuperscript{98} The important topic of the independence of the ECB and the national central banks is discussed in detail both with regard to the personal independence of their members and the functional independence of the entities in Smits, supra note 11, at 152-68.

\textsuperscript{99} In Europe, the German Bundesbank has traditionally enjoyed the greatest degree of independence, a principle guaranteed by article 12 of its 1957 basic statute: "In exercising the powers conferred on it by this Act, it shall be independent of instructions from the government." Gormley & de Haan, supra note 63, at 97-98. Although The Netherlands Central Bank by custom enjoys substantial independence, there is no statutory basis for this, and the Minister of Finance has the power to issue monetary policy instructions to the Central Bank. Id. at 98. In contrast, in France, the U.K. and the other Member States, the central banks traditionally have been subject to directions of the Minister of Finance. See Slot, supra note 63, at 231. Smits observes that "there is no tradition of central bank independence in the majority of Members States." Smits, supra note 11, at 159. He also notes that France initially wanted the ESCB to take guidelines from the European Council. Id. at 160 n.52; accord, Italianer, supra note 39, at 69.
Independence was strongly advocated by Germany, whose Bundesbank enjoys such independence from its government, as critical in order to ensure that the ECB and ESCB would have the freedom to follow strict, and hence often unpopular, monetary policies.

As noted previously in Part III, the Delors Report and the Commission's Christopherson Report both urged that the ECB (then called the Eurofed) be independent, and the October 1990 Rome European Council meeting included the principle of independence in its agenda for the IGC. The principle was early accepted by the Intergovernmental Conference, figured in the Luxembourg Presidency draft text, and was virtually unchanged in the final TEU.\(^{100}\) Presumably a consensus was quickly reached on the principle of independence for the ECB, as Professor Slot has observed, "mainly because of the superior track-record of the Bundesbank and the Dutch Central Bank in maintaining price stability."\(^{101}\)

Accessory to the principle of independence of the ECB is that of the independence of the national central banks and their members, since, as noted before, the national central banks represent the usual operational arm of the ESCB. Article 109e(5) requires Member States to take action to ensure the independence of their central banks during the second stage. In addition, Article 108 stipulates that Member States must put their national regulations concerning central banks into full compliance with the EC Treaty before the creation of the European Central Bank, which implicitly makes national central bank independence a pre-condition for a state's participation in the third stage of EMU. France and Spain rapidly acted to guarantee the independence of their central banks.\(^{102}\) In a surprise post-election move, the new U.K. Labor government of Prime Minister Blair declared the independence of the Bank of England in May 1997.\(^{103}\) On the other hand, Sweden has refrained from making its central bank independent, a point of importance with regard to its eligibility for the third stage.

The role and powers of the European System of Central Banks are set out in Article 105. Thus, Article 105(1) declares:

The primary objective of the ESCB shall be to maintain price stability. Without prejudice to the objective of price stability, the ESCB shall support the general economic policies in the Community with a view to contributing to the achievement of the objectives of the Community as laid down in Article 2. The ESCB shall act in accordance with the principle of an open market economy with free competition,

\(^{100}\) Italianer, supra note 39, at 80.

\(^{101}\) Slot, supra note 63, at 231. Accord, Gormley & de Haan, supra note 63, at 95; Pipkorn, supra note 63, at 281. I will discuss later, at infra Part VI.B, whether the Treaty's articulation of the principle of independence is so absolute in terms that it might be considered to breach the normally overriding principle of democratic accountability.


favouring an efficient allocation of resources, and in compliance with the principles set out in Article 3a.104

Article 105 gives Treaty (or constitutional) force to the concept that the ESCB’s “primary objective” is “price stability.”105 Article 105(1) thus expressly mandates the ESCB to achieve the TEU goals stated in Article 3a. The language is modeled upon the role assigned to the Bundesbank in its 1957 basic statute.106 The Delors Report enunciated the basic approach of this text, and the October 1990 Rome European Council stipulated that the primary objective of the central monetary institution should be “price stability.”107 The term has never been formally defined, but seems to be universally accepted as an inflation rate ranging from zero up to a maximum of 2%.108 The emphasis on “price stability” testifies to the influence of Germany in the drafting stage, because most other States either had no express principal policy goal for their central banks, or had a more general economic welfare goal (e.g., The Netherlands).109

Note that Article 105(1) stipulates that the ESCB shall support the “general economic policies of the Community,” but “without prejudice” to its primary goal of price stability, and shall also operate in accordance with “the principle of an open market economy with free competition” and the other secondary goals cited in Article 3a. This text is again modeled upon that governing the Bundesbank,110 and will certainly significantly impact the manner in which the ESCB shapes future monetary policy.111

Article 105(2) sets out the “basic tasks” of the ESCB, namely “to define and implement the monetary policy of the Community,” to conduct foreign exchange operations, to hold the Member States’ official foreign reserves (initially to be set at 50 billion ECU), and to promote the smooth operation of the Community payment systems.112 The most important point to note here is that this article effectively transfers most monetary power from the Member States to the ESCB (and not to the other Community institutions). Since, as will be seen in Part

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104 EC Treaty, art. 105(1). Italianer informs us that this text came in late in the Rome IGC, but only made express what had been previously accepted. Italianer, supra note 39, at 78.
105 Snyder correctly observes that this “statement of the aim of price stability as a constitutional principle represents a more unambiguous ranking of the aims of monetary policy than is found even in Germany.” Snyder, supra note 62, at 68. I will discuss this further in Part V, infra.
106 Gormley & de Haan, supra note 63, at 97; Pipkorn, supra note 63, at 281.
108 Italianer cites the Dutch Central Bank President Duisenberg as giving this pragmatic definition in a 1992 speech. Italianer, supra note 39, at 79. The European Monetary Institute also set 2% as the maximum ceiling for inflation that still represented price stability in European Monetary Institute, 1994 Annual Report 50, cited in Smits, supra note 11, at 185 n.158.
109 Gormley and de Haan, both professors at Groningen, translate the statutory objective of The Netherlands Central Bank as: “to regulate the value of the Dutch currency in such a manner as is most useful for the welfare of the country.” Gormley & de Haan, supra note 63, at 97 n.14.
110 Pipkorn quotes Article 12 of the German Bundesbank law to this effect. Pipkorn, supra note 63, at 281.
111 For an analytic discussion of the implications of the text, see Smits, supra note 11, at 187-92.
112 The ESCB’s operational role in regulating monetary policy is of capital importance, but it is too technical to cover here. For a detailed and analytic description, see Smits, supra note 11, at 176-202, 223-306.
VIII, the States participating in the third stage must follow monetary guidelines in their national policies, this represents a genuine and significant transfer of power—and implicitly of sovereignty.

During the Rome Intergovernmental Conference, there was considerable debate concerning the extent of the role the ESCB might play in prudential supervision of banks and other financial institutions. Although in some Member States the central bank has certain powers of prudential supervision, in most (rather like the American model) prudential supervision is entirely or largely carried out by the Ministry of Finance, aided by other regulatory authorities. Some Member States felt that the Ministry of Finance, or specialized authorities, were better able to carry out prudential supervision of financial institutions and that the ESCB might have a conflict of interest between achieving its goals of price stability and general monetary stability, on the one hand, and properly carrying out such prudential supervision of financial institutions on the other.

A compromise was struck: Article 105(5) calls on the ESCB to "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." This would suggest merely a role of advice, coordination and cooperation for the ESCB.

However, Article 105(6) authorizes the Council to "confer upon the ECB specific tasks" in the prudential supervision of financial institutions (but the text specifically excludes supervision of insurance companies). Such legislation may prove difficult to adopt: the Council must act unanimously, and the Parliament must give its assent. It may be expected that serious proposals for any specific role for the ESCB in the prudential supervision of financial institutions will not be raised until the ESCB has been operational for some time, perhaps years.

The creation and control of the single Community currency, now scheduled to be called the euro (and not the ECU, although that term is used for the single

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113 Smits, supra note 11, at 319-22.
114 Id. at 323-27. Professor Ian Harden contends that prudential supervision of financial institutions is better undertaken by a separate regulatory institution, as is the case in France and Germany, and therefore approves the final TEU approach. Ian Harden, The European Central Bank and the Role of National Central Banks in Economic and Monetary Union, in EMU: Implications, supra note 63, at 149, 159-61.
115 Italianer notes that the Luxembourg Presidency draft text in June 1991 had expressly given the ESCB powers "in the definition, coordination and execution of policies relating to prudential control and stability of the financial system," so that the final TEU text represents a considerable backdown on this subject. Italianer, supra note 39, at 87. Smits observes that two major Member States opposed an ECB role in prudential supervision, and that the compromise final text is "relatively meagre." Smits, supra note 11, at 336.
116 Italianer notes that the text implicitly excludes any role for the ESCB in the regulation of financial markets as opposed to financial institutions. Id.
117 Incidentally, this provision constitutes the sole example of significant legislative power given to the Parliament in connection with EMU.
118 The December 1995 Madrid European Council confirmed the designation of the single currency as the "euro." Bull. EU 12-1995, at 10. See the discussion of the Madrid European Council meeting in Part VII.A, infra.
currency in Articles 3a and 109 of the Maastricht Treaty), is placed in the ECB by Article 105a. Former Bundesbank President Karl Otto Pohl has declared that "every efficient central bank must have . . . the monopoly of money creation," and that the ESCB would be a "tiger without teeth" if it lacked this power.\textsuperscript{119} With regard to the bank notes, which will be the only "legal tender" in the participating third stage Member States, the ECB's power of emission and control is exclusive. Article 105a expressly provides the ECB with the power to determine the denomination and features of banknotes, but, to enable speed in producing the banknotes, the European Monetary Institute has already taken the initial decisions.\textsuperscript{120}

Member States will continue to have the power to issue coins, but the ECB can control the total volume of any issue.\textsuperscript{121} The power to determine the denominations and specifications of coins is given to the Council by Article 105a(2), but the Council must act in accordance with the parliamentary cooperation procedure.\textsuperscript{122}

The European Central Bank has been granted an unusual degree of regulatory power.\textsuperscript{123} Pursuant to Article 108a(1), the ECB may issue regulations to implement its monetary policy for the Community (or, more precisely, for the Member States participating in the third stage of monetary union, until all have joined in this stage), to govern the minimum reserves which it requires banking institutions to keep on deposit with the ECB and national central banks, to regulate bank clearing and payment systems, and to carry out prudential supervision of financial institutions (to the extent authorized by the Council, as noted above). The ECB may also take binding decisions or issue recommendations or opinions. Further, under a rather extraordinary provision,\textsuperscript{124}

\textsuperscript{119} Karl Otto Pohl, Basic Features of a European Monetary Order, \textit{in} European Monetary Integration, supra note 63, at 79, 85. For a more detailed analysis of Article 105a, see Smits, supra note 11, at 203-10.

\textsuperscript{120} These preparations for the single currency will be discussed further in Part IX.A, infra.

\textsuperscript{121} Italianer informs us that the Luxembourg Presidency draft treaty would have given the ESCB the power to regulate the issue of banknotes and coins. Italianer, supra note 39, at 86-87. In contrast, the final TEU text mandates that the ECB alone can authorize banknotes, while the States continue to issue coins, subject however to ECB approval of the total volume of coins issued, since this has an impact on total money supply.

\textsuperscript{122} It is interesting to note that the European Council's mandate that the Turin Intergovernmental Conference should not discuss any change in the Maastricht Treaty's EMU articles resulted in the survival of the parliamentary cooperation procedure in this provision, although the Treaty of Amsterdam will replace elsewhere in the Treaty all references to the cooperation procedure by the co-decision procedure. Pursuant to Article N of the TEU, the Turin Intergovernmental Conference was convened by the Member States in April 1996 to propose amendments to the TEU. This new set of amendments, which received political approval from the June 1997 Amsterdam European Council, was signed at Amsterdam on October 2, 1997 and is called the Treaty of Amsterdam. It is presently in the process of ratification. Its complete text, and the text of the European Community Treaty consolidated with the new amendments, is published in 1997 O.J. (C 340) 1. The cooperation procedure was replaced by the co-decision procedure in Articles 75 (transport), 127 (vocational training), 130c (research and development), 130s (environment), and a number of other provisions.

\textsuperscript{123} Professor Slot observes: "Compared to the situation [of central banks] in Member States, the power to issue regulations is remarkable and once more underscores the independent position of the ECB." Slot, supra note 63, at 235.
Article 108a(3), the ECB may impose sanctions—"fines or periodic penalty payments on undertakings for failure to comply with its regulations or decisions."\(^{124}\)

In view of the scope of the European Central Bank's role and tasks, and the dimension of its regulatory powers, it is important that the EC Treaty clearly delineates the principle of judicial review. Article 173 was amended to grant the Court of Justice jurisdiction over actions brought by Member States, the Council, the Commission or private parties against the ECB to review the legality of its acts, and for actions brought by the ECB against the Community political institutions in order to protect its "prerogatives."\(^{125}\) Similarly, the ECB will have the power to sue the Council, Commission and the Parliament under Article 175 for their failure to fulfill a duty to act in areas "falling within [the ECB's] field of competence," and the ECB can itself be sued for a failure to act to fulfill its duties by those institutions, Member States, or private parties. Article 177 was amended to include the acts of the ECB among those which may be the subject of questions referred to the Court of Justice by national courts. Finally, the Court of Justice was given the power, under Article 180(d), to review the compliance of national central banks with their obligations in the ESCB, and to compel their compliance if necessary.\(^{126}\)

Decision-making in the ESCB and the ECB is governed by a Treaty Protocol on the Statute of the European System of Central Banks and of the European Central Bank.\(^{127}\) For the Governing Council, Article 10 of the Protocol prescribes a quorum of two-thirds, dictates that the Governing Council can usually take binding acts by simple majority, and grants the President a tie-breaking vote.\(^{128}\) Proxies are not permitted, although action by teleconferencing

\(^{124}\) Note that unlike the limits placed by articles 15-17 of Regulation 17/62, O.J. English Spec. Ed. 1959-62, at 87, on the Commission power to impose sanctions on enterprises for their violation of Community competition rules, Article 108a(3) contains no reference to limits on sanctions imposed by the ECB. However, the Court of Justice's power of judicial review of such ECB sanction decisions under Article 173 would enable limits to be set on sanctions. The Court presumably would give considerable deference to ECB decisions, but could reduce or totally eliminate ECB sanctions when it deems them to be excessive, or insufficiently founded on factual findings, as it occasionally has done with Commission fines in competition proceedings. See, e.g., S.A. Musique Diffusion Française v. Commission (Pioneer), Case 100-103/80, 1983 E.C.R. 1825.

\(^{125}\) The ECB's limited standing under Article 173 only to protect its "prerogatives" is parallel to the standing given to the European Parliament under that Article. This limitation is based upon the Court's judgment in Parliament v. Council (Post-Chernobyl), Case C-70/88, 1990 E.C.R. I-2041. For example, the ECB could sue the Council under Article 173 if the Council were to legislate to permit a Member State central bank to issue banknotes as legal tender, because that would violate the ECB's prerogative to issue banknotes. The ECB could not, however, sue the Council because the ECB considers the Council to have made a substantive or procedural error in adopting legislation with implications for monetary policy, e.g., in the prudential supervision of banks, because that would not involve an ECB prerogative. See in this regard the Court's judgment on the merits in Post-Chernobyl, Case C-70/88, 1991 E.C.R. I-4529, 4567.

\(^{126}\) The importance of judicial review with regard to the ECB is discussed further in Part VI.D, infra.

\(^{127}\) The Protocol is attached to the TEU. See also note 95, supra.

\(^{128}\) For more detailed coverage of voting in the Governing Council and the Executive Board, see Smits, supra note 11, at 99-102.
is. A type of qualified majority voting, with the weight of votes set in accord with national central bank shares in subscribed ECB capital, is mandated for important decisions on the ECB's capital structure, control of foreign reserves, and accounts.

Article 11 of the Protocol prescribes that the six Executive Board members must serve full time, be "persons of recognized standing and professional experience in monetary or banking matters," and sets voting rules for the Executive Board parallel to those for the Governing Council. Under Protocol Article 13, the President of the ECB chairs both the Governing Council and the Executive Board, and represents the ECB in external matters. The force of the personality of the initial ECB President, and custom as the institution commences its operations, will partially determine the ultimate power and prestige of the post, but it may safely be predicted that the office of President of the ECB will certainly be as important as that of any Commission member, and may become second in status only to that of the Commission President.

Presumably for purposes of coordination, EC Treaty Article 109b(1) grants the President of the Council and a member of the Commission the right to participate, without vote, in meetings of the Governing Council. The President of the Council may even "submit a motion for deliberation" to the Governing Council. Correlatively, the President of the ECB may participate in Council meetings (on a non-voting basis) when "matters relating to the objectives and tasks of the ESCB" are discussed.

As the prior review suggests, the European Parliament has been given only a modest role in the developmental stages of EMU, and in the institutional structures after it becomes operational. Parliament need only be consulted in the Council's crucial decision on which Member States qualify for entry into the third stage, and in the designation of the members of the ECB's Executive Board. Parliament's most substantial power is negative, its right of assent (or veto) with regard to Council decisions to accord the ESCB prudential supervisory authority over financial institutions, and with regard to Council

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129 The right of the President of the Council and a Commission member to participate in ECB meetings, and of the Council President to submit a motion, is presumably modeled on the status of the Bundesbank, whose basic law permits government ministers to attend Bundesbank meetings. Gormley & de Haan, supra note 63, at 98. Smits contends that the Council President's motion must only be "for deliberation" and hence would not encompass a motion to take a decision or act. Smits, supra note 11, at 170.

130 EC Treaty, art. 109b(2).

131 Whether this approach is justifiable will be discussed in Part VI.C, infra.

132 EC Treaty, art. 109j(4).

133 EC Treaty, art. 109a.

134 Note that in exercising its assent power, the Parliament must either vote to approve or to disapprove, and thus veto the Council's proposed legislation. The Parliament cannot amend the proposal, nor require its reconsideration by the Council. Accordingly, the Parliament's large share in legislative power in the codecision procedure is probably preferable in practice to its power to assent.

135 EC Treaty, art. 105b.
action to amend certain key provisions of the Statute of the ESCB.\textsuperscript{136}

Parliament will exercise a limited power of surveillance or monitoring of the ESCB once the latter commences operations. Article 109b(3) prescribes that the ECB must provide an annual report on the ESCB’s operations and upon its monetary policies to the European Parliament (as well as to the Council, Commission and, somewhat unusually but showing the high profile of the report, to the European Council). The Parliament may hold “a general debate” upon the report.\textsuperscript{137} In addition, relevant competent committees of Parliament may request the President of the ECB and other Executive Board members to come to a hearing (or correlatively, ECB Executive Board members may request to be heard by such committees).

Thus far I have described the role and functions of the ECB and the ESCB with regard to its conduct of monetary policy within the Member States participating in the third stage of the monetary union. What, however, happens with regard to the “States with a derogation” that do not join in the third stage, either because they have opt out rights (Denmark and the United Kingdom), or because they were unable to meet the convergence criteria or other preconditions for participation in the third stage (probably Greece and Sweden, and perhaps other Member States)\textsuperscript{138}\textsuperscript{?} After all, the European Monetary Institute is to be liquidated when the ECB is created.

The TEU does not cover this matter in any detail, but Article 109l(3) cross-references the Protocol on the Statute of the ESCB and the ECB which does so in Articles 43-53.\textsuperscript{139} A General Council is to be constituted, composed of the President and Vice-President of the ECB (but not the other six Executive Board members) together with the governors of the central banks of both the participating States and the “States with a derogation,” not yet (or not ever) participating in the third stage.\textsuperscript{140} The Governing Council takes over the tasks previously performed by the EMI in coordinating the monetary policies of such Member States with a derogation, advising them on how to attain the convergence criteria, monitoring their participation in a new Exchange Rate Mechanism, and so forth. The Governing Council would, of course, disappear when (or if) all Member States qualify to participate, or opt to join in the final stage of monetary union.

Finally, the Maastricht Treaty also deals with international agreements in the monetary sphere in a complicated provision, Article 109, which constitutes a

\textsuperscript{136} EC Treaty, art. 106(5).

\textsuperscript{137} The Parliament’s “general debate” upon the ECB’s annual report may become as important a review of the merits of the Community’s monetary policy as is the Parliament’s debate upon the merits of the Commission’s presentation of its annual agenda.

\textsuperscript{138} See infra Part VII.C.

\textsuperscript{139} The Protocol is attached to the TEU.

\textsuperscript{140} For further discussion of the role and functions of the General Council, see Gormley & de Haan, supra note 63, at 105-06; and Smits, supra note 11, at 97-98.
derogation from the usual Community procedures for entering into international agreements laid down in Article 228.141

The principal role is given to the Council which, acting unanimously, can conclude any formal agreements on exchange rates with third countries, after consulting the Parliament and the ECB (Article 109(1)).142 Such a "formal agreement" on exchange rate systems is presumably intended to cover a Bretton Woods type of arrangement. In the absence of any such "formal agreement" (and such a formal agreement presently does not seem very likely), the Council may, acting by qualified majority, formulate "general orientations" for exchange rate policy which are usually to be binding on the ECB.143

Acting by qualified majority, the Council may also enter into binding agreements with international organizations or third countries on monetary matters.144 This is a power which is certain to be exercised, very likely soon after the commencement of the third stage. The Commission does not have the power to negotiate these arrangements, as it usually does under Article 228. Instead, under Article 109(3), the Council, acting on a Commission recommendation and after consulting the ECB, decides how negotiations shall be conducted, which may well mean that Council representatives will do the negotiating directly. The Commission is only given the comfort that it "shall be fully associated with the negotiations." Manifestly, the Member States want the Council to have the central power position in the sensitive area of international monetary relations and affairs. As a practical matter, however, since so much of international monetary relations consists of informal arrangements and understandings between central banks, the ECB may develop a major role in Community external monetary affairs. As Professor Slot has well observed, "the outside world, i.e., central banks, will see the ECB as the institution to do business with."145

141 Smits provides a detailed, valuable analysis of the Community's external relations in the monetary field under Article 109. Smits, supra note 11, at 365-454. Considerable specific attention is paid to the impact upon the International Monetary Fund in id. at 429-50. Italianer provides a helpful analysis of what the drafters intended to achieve through the quite complicated language of Article 109. Italianer, supra note 39, at 89-90. For an expert appraisal of the possible Community role in the International Monetary Fund, see R. Martha, The Fund Agreement and the Surrender of Monetary Sovereignty to the European Community, 30 Common Mkt. L. Rev. 749 (1993).

142 Either the Commission or the ECB must initially recommend the agreement to the Council. Moreover, the consultation required with the ECB is intended to ensure the reaching of "a consensus consistent with the objective of price stability," which suggests that the ECB has somewhat more than a purely advisory role. Professor Slot describes the ECB's position to be "somewhere between consultation and assent." Slot, supra note 63, at 240.

143 See Italianer, supra note 39, at 241.

144 EC Treaty, art. 109(3).

145 Slot, supra note 63, at 241. An issue that is particularly sensitive and wide-open is how the International Monetary Fund will be restructured in order to adapt to the new Community role in international monetary affairs. See the detailed analysis in Smits, supra note 11, at 434-52.
VI. CONSTITUTIONAL AND LEGAL ISSUES CONCERNING THE EMU STRUCTURE

Not surprisingly, the complex Economic and Monetary Union provisions of the Maastricht Treaty proved to be among the most controversial during the ratification debates in 1992-1993. Many Member State citizens, and a substantial number of political party leaders, felt that the creation of the ESCB would result in centralized and bureaucratic Community regulation, instead of national self-determination, in an area of great political, economic and social importance. This feeling certainly contributed to the adverse June 1992 ratification referendum in Denmark, and the narrow level of support for ratification in the September 1992 French referendum and the July 1993 U.K. Parliament vote. It is noteworthy that the favorable 1993 Danish referendum only occurred after the December 1992 Edinburgh European Council meeting expressly recognized Denmark's exercise of its Treaty Protocol option to remain outside of the third stage of EMU.

Even if one supports the basic concept of monetary union, the Maastricht Treaty provisions on EMU and the institutional structure devised for the monetary union raise interesting and serious constitutional and legal issues. The first issue covered in this Part is whether all of the detailed provisions on EMU are so crucial in nature as to merit their inclusion in the Treaty or annexed Protocols, as opposed to their presentation in secondary legislation. Second, the motive for the Treaty emphasis on the independence of the central bank system is set forth, but not without query as to whether this principle should be enshrined in the Treaty itself. Linked to this is a critical question: should not Parliament have been given a substantial share in the process of creating EMU, or in its subsequent operations, an issue which is an aspect of the famous (or infamous) "democratic deficit" of the Community. Also linked is the importance of judicial review within the monetary structure by the Court of Justice, an aspect of the essential rule of law. Finally, the last section queries the Treaty-based priority given to price stability as the pre-eminent goal of the ECB's monetary policy, and contrasts this with the wider policy perspectives of the U.S. Federal Reserve and The Netherlands Central Bank. Note is taken here of the Treaty of Amsterdam emphasis on attaining high levels of employment, raising the question whether the ECB ought not to give this new Treaty goal a high priority in its monetary policy decisions.

A. The Treaty Force of Detailed Provisions on EMU

The Court of Justice in the famous Les Verts judgment described the Treaty Establishing the European Economic Community and the other constitutive


147 European Council Decision, Problems Raised by Denmark, supra note 89, at 2.
treaties as a "constitutional charter," a characterization repeated with even greater force to justify the Court's reasoning when it struck down aspects of the European Economic Area Agreement in its European Economic Area Opinion. If anything, the Treaty on European Union seems even more aptly to be described as a type of "constitutional charter," because of the TEU's broader articulation of the goals of the Union, its creation of a "citizenship of the Union," and its further transfer of elements of national sovereignty to a supranational institutional structure.

Accordingly, the decision taken by the Rome Intergovernmental Conference, and confirmed by the European Council, to place so many complex and detailed provisions on EMU in the Maastricht Treaty, or in Protocols which have Treaty force, is certainly a debatable one. Many of these provisions would seem to be more suitably embodied in secondary legislation, which could then be adjusted to meet changing needs. As it is, revisions in many provisions of relatively secondary importance can only occur through Treaty or Protocol Amendment. This is not only time-consuming and cumbersome, but carries as a consequence the obligation to resort to popular referenda in some Member States in order to achieve ratification of the amendments. In contrast, the rules governing the structure and operations of the Federal Reserve in the U.S., or national central banks in Europe, are essentially embodied in legislation.

The motive for the extensive use of Treaty provisions for the structure of EMU, and the description of the stages and conditions for its attainment, presumably was to ensure unanimous backing from the Member States at the outset, and greater certainty in the progressive execution of the successive stages and in the ultimate structure (e.g., with regard to the firm date of January 1, 1999 for the start of the third stage, or with regard to the principle of independence for the ECB and the national central banks).

Although undoubtedly the goals of Economic and Monetary Union, and certain key structural features, merit a place in the Treaty, it may be doubted that a number of details of planning or policy belong there. Already the Treaty reference to ECU as the name for the single currency in Articles 3a and Article 109 is misleading, because the December 1995 Madrid European Council chose the name "euro" instead. Smits contends, and is almost certainly correct, that it is "unquestionable" that the TEU intended the name of the single currency to be "ECU" or "ecu" ("ECU" was used in the English Treaty text, and "ecu" in the French). The single currency's name should properly have been amended.

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150 Professor Louis has well remarked that in no other legal system has the organic law governing a central bank system been raised to constitutional status; it is always, and properly, capable of modification by the legislature. Jean-Victor Louis, The Project of a European Central Bank, in Financial and Monetary Integration in the European Economic Community 13, 17 (Jules Stuyck ed., 1993) [hereinafter Financial and Monetary Integration in the EEC].
151 Smits, supra note 11, at 490. The European Council conclusions referred to "ECU" as a prior "generic term" for European currency unit, but it was never so defined in the Maastricht Treaty. Bull. EU 12-1995, at 10. See text accompanying note 260, infra. Smits rejects the view that the term
in the Treaty of Amsterdam, but no such action was taken. The failure to foresee the need to enable legislation to adopt certain essential rules in advance of the third stage has meant that the important regulation on continuity of contracts, discussed in Part IX, has had to be adopted by the use of Article 235, and the equally important regulation on the introduction of the euro cannot be adopted at all until the number of Member States participating in third stage is set and the ECB is constituted.

Indeed, the fixing of the January 1, 1999 date for the start of the third stage irrevocably in Treaty Article 109j(4) is a very debatable proposition. The efforts to adhere to that timetable have led to severe economic strains in many Member States, and only the application of the convergence criteria in a rather elastic fashion will enable the date to be met. One may wonder whether 2000 or 2001 might not have been more propitious dates, and query whether the TEU needed to fix a terminal date, or might rather have better set parameters for a final date, leaving the final timetable to be set by a European Council closer in time to the event.

B. The Principle of Independence

Not only is the principle of independence for the European Central Bank, and all national central banks participating in the ESCB, given Treaty (or constitutional) status in EC Treaty Article 107 (repeated in Article 7 of the Protocol on the Statute of the ESCB and of the ECB), but it is stated in very strong terms: members of these bodies shall neither "seek or take instructions from Community institutions or bodies, from any government of a Member State, or from any other body." Moreover, the Community institutions and Member State governments pledge to "respect this principle and not to seek to influence" the ECB or the national central banks. The decision to give the Executive Board members a non-renewable, but relatively long eight year term, was linked to the principle of independence—it was felt that any possibility of reappointment might open the way for undue influence on the Executive Board members. Moreover, Executive Board members can only be removed from

"ECU" could be regarded as an acronym for "European currency unit." He further argues that the European Council did not have the power to change the name, which could only be done by Treaty amendment. Smits, supra note 11, at 491-92. He notes that Commission President Jacques Delors took the same position in 1993 in answer to a question from Parliament. See Answer given by Mr. Delors on behalf of the Commission, 1993 O.J. (C 16) 10.

152 See infra Part VII.

153 Pohl, supra note 119, at 84. Smits describes the motive to be "to free the incumbent from political considerations concerning a renewal of his or her term of office." Smits, supra note 11, at 156. However, he queries this, observing that central bank governors whose term of office is renewable often have a "staunchly independent tradition." Id., citing the Federal Reserve Board and The Netherlands Central Bank. An eight year term was presumably chosen because that is the term of office of Bundesbank Directorate members.
office for incapacity or "serious misconduct" by a proceeding before the Court of Justice, ensuring a judicial rather than a political decision.\textsuperscript{154}

Furthermore, this Treaty-enshrined principle of independence applies not only to the Executive Board and the Governing Council of the ECB, but also to all the national central banks participating in the ESCB.\textsuperscript{155} The policy motive for this is obviously to ensure that national central banks can effectively operate as part of the ESCB and that they might have greater leeway in pursuing the goal of price stability and monetary stability on the national level.\textsuperscript{156} As previously observed in Part V, Article 108 of the EC Treaty requires Member States to ensure that the national rules governing their central banks are "compatible with this Treaty" prior to the creation of the ESCB, implicitly meaning that independence of national central banks should be attained during the second stage.\textsuperscript{157}

The motive for this strong declaration of independence for the ECB and national central banks lies in the manifest success of the Bundesbank in achieving a virtually continuous state of stable monetary conditions, low inflation, and a solid currency since the German economic recovery under Chancellor Konrad Adenauer in the 1950's.\textsuperscript{158} Ludwig Erhard, then Finance Minister and Adenauer's successor as Chancellor, advocated a strong, independent central bank. Much of the success enjoyed by the Bundesbank in its regulatory efforts has been attributed both within and outside Germany to the basic legislation governing the Bundesbank, enhanced by custom, according it substantial independence from the political sphere. As former Bundesbank President Pohl has asserted: "Only an independent institution is in a position to resist the ever-recurring wishes of politicians to prescribe monetary policy targets which are often inconsistent with the objective of stability, such as the stabilization of exchange rates or the promotion of growth and employment or the balancing of regional disequilibria."\textsuperscript{159}

Prior to the Maastricht Treaty, most other European central banks were not granted totally independent regulatory powers by legislation. Although custom

\textsuperscript{154} Protocol on the Statute of the ESCB and the ECB, at art. 11.4. Further, only the Governing Council or the Executive Board itself can institute the procedure. For analysis of this topic, see Smits, supra note 11, at 163.

\textsuperscript{155} To safeguard their independence, members of national central banks must have a minimum term of five years and be removed only for incapacity or "serious misconduct" in a proceeding whose decision can be appealed to the Court of Justice. Protocol of the Statute of the ESCB and the ECB, at art. 14.2. See Gormley & de Haan, supra note 63, at 107.

\textsuperscript{156} Harden, supra note 114, at 155.

\textsuperscript{157} See also EC Treaty, art. 109e(5).

\textsuperscript{158} Gormley & de Haan, supra note 63, at 95. Smits cites a number of studies correlating central bank independence in Germany, The Netherlands, and Switzerland with low inflation rates and smaller public deficits. Smits, supra note 11, at 152-54.

\textsuperscript{159} Pohl, supra note 119, at 83. Rosa Lastra, a lawyer with the International Monetary fund, argues that a central bank should be independent in order to check the tendency of political leaders to manipulate "monetary policy for short-term political ends." She further argues that the "skills, expertise and superior economic qualifications of central bankers compared to politicians . . . better guarantee a more objective, more 'neutral' and faster decision-making process." Rosa Lastra, The Independence of the European System of Central Banks, 33 Harv. Int'l L.J. 475, 477 (1992).
usually accorded the central banks wide discretion in decision making, governments did from time to time block central bank decisions or, more rarely, dictate monetary policy to be implemented by the central banks. This was particularly true in France, but also in some measure in Italy, Spain and the United Kingdom.

France, Italy, Spain and the U.K. have now all acted to adopt the principle of independence for their central banks. It remains to be seen whether the principle will be respected in practice, especially in those Member States that have customarily possessed political control over central banks. Efforts by the executive branch, and especially finance ministers, to influence central bank decisions on interest rates or liquidity may well occur. After all, although the Commission is also guaranteed independence by Article 157 of the EC Treaty, it is well known that on occasion Member States have tried to influence commissioners initially nominated by them. In August 1995, press reports indicated that Commission President Santer had formally rebuked the German government for its efforts to incite the two German members of the Commission to oppose the draft consumer warranty directive.160

Independence of the ECB does not mean that it will be free from all commentary or political pressure. The Commission in its initial advocacy of the principle of independence in March 1990 noted that the central monetary institution must be “democratically accountable [as] a necessary complement to its independence in order to make its policies acceptable to the public at large.”161 Smits has well said that “the counterpose to independence is accountability. The central banks . . . have to account for their policies and activities before the political organs . . . [and] come under the scrutiny of the judiciary.”162

As previously noted, EC Treaty Article 109b grants the President of the Council and a member of the Commission the right to “participate” without a vote in Governing Council (but not Executive Board) meetings. The word “participate” implies a right to speak and join in deliberations, not simply a right to attend silently. The Council and Commission representatives may legitimately seek to influence the ECB.163 Indeed, the President of the Council may even “submit a motion for deliberation.”164

Moreover, the Parliament may at least make its views known in the debate following the ECB's annual report to Parliament.165 Perhaps more important, competent Parliament committees may “hear” the President of the ECB and

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161 Supra note 38, at 8.
162 Smits, supra note 11, at 169.
163 As Smits remarks, “to freely opine on the right course of monetary policy.” Id. at 171. Harden describes their role as contributing “to the formulation of monetary policy by discussion.” Harden, supra note 114, at 153.
164 But, arguably, not for decision or action. See Smits, supra note 11, at 171.
165 EC Treaty, art. 109b(3).
other Executive Board members.\textsuperscript{166} Since committees may include members specialized in legal and monetary affairs, and committee meetings can be scheduled at times of major monetary policy decisions, a certain degree of influence can be brought to bear on the ECB.\textsuperscript{167} Furthermore, such ECB contacts with Parliament serve another valuable role, that of informing the public of the ECB's monetary policies and its views on current monetary issues and conditions.\textsuperscript{168}

A final point is that a legitimate question may be raised as to the wisdom of incorporating the principle of independence into the EC Treaty as a constitutional principle. As Professor Snyder has observed, this gives the ECB "formally speaking," greater independence than the U.S. Federal Reserve Board or the Bundesbank.\textsuperscript{169} On a comparative note, the U.S. Federal Reserve Board does not enjoy constitutional status and, although it enjoys great independence by custom, nothing prevents the Congress from adopting legislation mandating certain goals or policies, a power that the Congress has on rare occasion exercised.\textsuperscript{170} Indeed, even the threat of legislation raised by a powerful congressional committee may well have some influence on the Federal Reserve. In the European context, The Netherlands Central Bank enjoys a high reputation for its efficacy in monetary control, even though its independence is largely based on custom and, as noted previously, its status is determined by legislation and it can be subjected to binding instructions from the Ministry of Finance.\textsuperscript{171}

However desirable a very high level of functional independence for the ESCB may be in practice, it remains quite debatable that the principle should be enshrined in the EC Treaty, with constitutional import, rather than in some form of basic secondary legislation. In times of political or economic crises, it may be plausibly contended that the political leadership should have some capacity to overrule central bank decisions.\textsuperscript{172} This observation leads naturally to the next legal and political issue meriting review, the "democratic deficit."

\textsuperscript{166} However, Professor Harden contends that the text does not give Parliament the right to compel ECB members to appear before it, nor the Executive Board a right to appear at will before Parliament. Harden, supra note 114, at 161.

\textsuperscript{167} As Smits observes, the ECB can better "assess the needs and preferences [of the public] expressed through the political process." Smits, supra note 11, at 170.

\textsuperscript{168} Id. at 169.

\textsuperscript{169} Snyder, supra note 62, at 78.

\textsuperscript{170} The best-known example is the Full Employment and Balance Growth Act of 1978 (popularly known as the Humphrey-Hawkins Act), which required the Federal Reserve to consider a variety of factors in setting its objectives, notably "full employment and production." 15 U.S.C.A. § 3101, at § 3101(c).

\textsuperscript{171} Gormley & de Haan, supra note 63, at 98-99.

\textsuperscript{172} It is well known that Chancellor Kohl's government overruled the Bundesbank in setting the monetary terms for German reunification in 1990. See Lastra, supra note 159, at 495. Gormley & de Haan argue that economic theory may also justify a political override of central bank decisions in rare instances of economic shocks. Gormley & de Haan, supra note 63, at 109-12. Smits specifically rejects this view. Smits, supra note 11, at 185 n. 161.
C. The "Democratic Deficit" of the Monetary Union

Over the years, Parliament's endeavors to gain greater powers have been supported by academic and media commentary complaining of the "democratic deficit" of the Community. While the Rome Intergovernmental Conference experts devised the Maastricht Treaty provisions on EMU, Parliament in several resolutions urged that it be given a considerable role in the evolution of monetary union and in its operations once constituted, specifically demanding "democratic supervision" and "public accountability" of the ESCB.173 In large measure, this did not occur, probably because the political leadership of the Member States did not want Parliament to interfere with the decisions taken en route to EMU, and because the drafting experts insisted on the principle of ECB independence in operations after its creation.

The March 1996 Turin European Council decision to the effect that the TEU's monetary provisions should not be placed on the IGC agenda for reexamination by the 1996 Turin Intergovernmental Conference174 had the consequence that Parliament's position could not be improved in the Treaty of Amsterdam. Indeed, as noted earlier,175 the parliamentary cooperation procedure survives in the monetary chapter, although being replaced by the co-decision process everywhere else in the Treaty of Amsterdam.

Perhaps the most important and regrettable illustrations of the "democratic deficit" are Parliament's meager involvement in the political determinations in the shift to the third stage. It may be appropriate that Parliament is only informed in the process of providing economic and monetary guidelines to Member States during the second stage,176 since this is a highly technical process. But the EC Treaty provides that Parliament is only to be consulted in the Council decision identifying the Member States which fulfill the necessary conditions for participation in the third stage,177 and in the subsequent designation of the Executive Board.178

The determination of those Member States that qualify for the third stage is not purely a technical matter. As will be examined in Part VII, this is a highly political decision. The sensitivity and importance of the decision is underlined

173 The October 25, 1989 Resolution on Economic and Monetary Union demanded "procedures for democratic supervision" of the ESCB. 1989 O.J. (C 304) 43, 45. The May 16, 1990 Resolution on Economic and Monetary Union urged "public accountability" of the ESCB as appropriate "in a democratically ordered society." 1990 O.J. (C 149) 66, 68. Later, the October 10, 1990 Resolution on Economic and Monetary Union urged that Parliament be given either the power to assent, or share in a codecision procedure in key decisions for the creation of EMU and the legal status of the ECU, and give its assent to the nomination of the ECB board members. 1990 O.J. (C 284) 62, 63-65.

174 The European Council's agenda for the IGC is contained in Bull. EU 3-1996, at 9-12.

175 See supra, note 122.

176 EC Treaty, arts. 103(2), 103(4) & 104c(10). However, Professor Louis contends that the failure to include Parliament in the process prevents any "effective inter-institutional dialogue for the elaboration of the guidelines." Louis, supra note 150, at 7.

177 EC Treaty, art. 109j(4).

178 EC Treaty, art. 109a(2).
by the unusual requirement that the Council be composed of Heads of State and Government for this purpose—a unique example of providing for a Community legal act at the highest political level.

A decision of parallel significance to determining third stage participants is that on the admission of new Member States into the EU, governed by Article 0 of the TEU. Under this provision, the Council can act only after receiving the assent of the European Parliament, i.e., the Parliament has a veto power. Why should not the Parliament likewise have the right to assent to the determination of the member States comprising the final stage of monetary union? Surely such a decision of capital political importance ought to have the strongest democratic support. The risk that Parliament would block the decision is as minimal as the risk that Parliament would block an accession—although admittedly that risk might enable Parliament to exert some degree of influence on such a vital decision.

One may legitimately wonder also why Parliament should not have a voice in the designation of Executive Board members, as it has requested. After all, in the U.S. the President's nominees for the Federal Reserve Board are subject to confirmation hearings and must be approved by the Senate. (Indeed, in Denmark, some Central Bank members are appointed by the parliament.) Not only is democratic legitimacy better respected by a system of formal hearings and approval by the Parliament, but the process enables a careful and public review of a nominee's credentials and policy views.

Once the monetary union is fully constituted and the ESCB operational, the Parliament's role is also rather modest. It is true that Parliament must give its assent to any Council legislation granting the ECB powers of prudential supervision over credit institutions and other financial institutions, or in any change in significant provisions of the Statute of the ESCB. Otherwise the principle of independence dictated that Parliament be given no role in the ESCB system of monetary policy setting and regulation. As remarked previously, the total insulation of monetary decision making from democratic control is certainly a debatable proposition. Making it hard for Parliament to interfere with the monetary expert bodies is one thing, making it impossible (by the Treaty force of these provisions) is quite another.

Leading commentators have not been slow to raise their concern in this regard. The strongest critique has been offered by Professors Gormley & de Haan in their article, "The Democratic Deficit of the European Central Bank," which concludes that "monetary policy ultimately must be controlled by democratically elected politicians," and urges reexamination of The Netherlands.

179 In its November 12, 1990 Resolution on EMU, supra note 173, Parliament requested the power to assent to the designation of ECB board members.
181 Lastra, supra note 159, at 483.
182 See EC Treaty, arts. 105(5) & 106(5). See also note 134, supra. As observed in the text accompanying note 117, supra, the likelihood that the ECB will receive delegated powers in the prudential supervision of financial institutions in its initial operations is not very great.
and New Zealand models for central bank operations. Professor Snyder worries that the new structure for EMU decision-making "runs the risk of serious problems of popular legitimacy." Professor Louis notes that the TEU provisions on the ESCB have given priority to the structural rules over "ensuring a democratic legitimacy of the new institutions."

In contrast, former Bundesbank President Pohl contends that the ESCB structure "would have an adequately democratic legal base if it came about by an agreement between democratic governments, if the agreement were ratified by democratically elected parliaments and if the system were provided with a clearly defined mandate." In a rather balanced view, Smits concedes that ECB "independence has been written in stone, a feature which may be considered at variance with the imperatives of democracy," but he regards any alternative as "unacceptable politically" because of the overriding concern for price stability and security in managing the new single currency.

Like several other commentators, Smits urges full use of Parliament’s surveillance powers described earlier (the Parliament’s "general debate" upon the ECB’s annual report, together with the possibility of committee hearings) in order to achieve "democratic accountability" of the ECB. He stresses that if the ECB is open to dialogue with Parliament, and if Parliament is sufficiently expert and prudent in its exercise of its limited powers, the dialogue may not only provide valuable monetary and economic information to the general public, but may also enable the popular representatives to exert a genuine influence upon the ECB’s decision making. He urges Parliament to have well-informed MEPs with "eminent economic credentials . . . entering the arena of debate with the ECB President."

In view of the imperative need to ensure that the European Community have an adequate level of democratic legitimacy, one can only hope that Smits will prove an accurate prophet and that the Parliament’s surveillance of the ECB will be far-reaching and effective. Professor Harden contrasts the rather meager TEU provisions in this regard with the more precise reporting obligations placed upon citizens.

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183 Gormley & de Haan, supra note 63, at 112.
184 Snyder, supra note 62, at 77.
185 Louis, supra note 150, at 17. Professor Louis elsewhere complains that "[v]ery severe measures will have to be taken by Member States and sacrifices asked of European citizens without democratic accountability of the institutions concerned." Louis, supra note 150, at 9.
186 Pohl, supra note 119, at 87.
187 Smits, supra note 11, at 176. Lastra agrees, arguing that monetary stability is "a necessary condition for a stable democracy" and the need for central bank independence to achieve monetary stability represents a justification for the exception to democratic control. Lastra, supra note 159, at 479.
188 See supra note 137 and accompanying text.
189 Smits, supra note 11, at 169; see also Pipkorn, supra note 63, at 281. Gormley & de Haan speak of "independence under observation." Gormley & de Haan, supra note 63, at 106. Lastra argues for "accountable independence" as a solution to the "democracy deficit." Lastra, supra note 159, at 481-82.
190 Smits, supra note 11, at 169-76.
191 Id. at 174.
the Federal Reserve, which must provide to Congress twice a year a detailed report on monetary policy and a number of relevant economic conditions, together with its objectives and plans. Furthermore, the Fed is subject to fairly strict oversight by both Senate and House Committees.\textsuperscript{192} Whether Congress is able to exercise any significant degree of influence upon the Federal Reserve’s general conduct of monetary policy is certainly questionable, but at least the reporting system ensures a salutary publicity for national economic and monetary policies and conditions. Perhaps a parallel development may ultimately occur in EMU.

\textit{D. Judicial Review by the Court of Justice}

The Treaty’s provisions on the role of the Court of Justice in the monetary union’s operations have a dual importance: the Court will serve to guarantee the powers and the independence of the ECB, but it will also provide a check on ECB power that is all the more significant in view of the “democratic deficit.” As Professor Slot suggests, the TEU structure “provides greater judicial protection and control than presently exists in several of the Member States. This may counter-balance the lack of Parliamentary control.”\textsuperscript{193} Smits observes that national central banks traditionally have not been “subject to elaborately regulated judicial review,” but that the “extensively regulated legal framework” of the ESCB is natural, since “[t]he Community is based on respect for the rule of law.”\textsuperscript{194}

As previously discussed in Part V, to ensure the rule of law, the Court of Justice has jurisdiction in actions brought by the ECB “to protect its prerogatives” against the other institutions or Member States under EC Treaty Articles 173 and 175, as well as in actions brought by Member States and the other institutions against the ECB. It is quite likely that the Court of Justice may be called upon to decide disputes over the extent of ECB competence or power either in conflicts with the Community institutions, or with national ministries of finance or central banks\textsuperscript{195} (commonly called “turf battles”), for example, in the field of monetary supervision of financial institutions. Also, although the scope of ECB and national central bank independence will probably be more guaranteed by custom, it is not inconceivable that the precise parameters of independence may have to be settled by the Court.

It is unlikely that the ECB will be as eager as the Parliament is to sue the other institutions, but the ECB’s power to do so may still prove a useful safeguard. The Court may also have to decide the force and extent of Treaty obligations and ECB decisions in proceedings against recalcitrant national central

\textsuperscript{192} Harden, supra note 114, at 161-62. The reporting requirements are mandated by statute. See infra notes 209 & 210.

\textsuperscript{193} Slot, supra note 63, at 248.

\textsuperscript{194} Smits, supra note 11, at 106.

\textsuperscript{195} For further analysis of some complicated issues that may arise, see id. at 107-08. See also Slot, supra note 63, at 245-46.
banks or private enterprises under EC Treaty Article 180d and under the Protocol on the Statutes of the ESCB and EC, Article 35.\textsuperscript{196} Moreover, not only Member States and Community political institutions, but individuals may to some extent question ECB regulations and decisions either directly under Article 173 or indirectly in national court proceedings, through the Article 177 reference procedure. Article 190’s requirement that regulations and decisions adopted by the Community political institutions must have a reasoned basis is apt to be applied by analogy to ECB regulations and decisions.\textsuperscript{197} It is likely that recourse to a legal challenge of an ECB decision would rarely occur, and the Court is certain to give a broad field of discretion to the ECB’s monetary measures. Nonetheless, the possibility of review by the Court of Justice should serve as a restraint against arbitrary, poorly reasoned or inadequately justified rules or decisions, in line with well-established Court precedents on the need for a reasoned basis for Council, Commission and Parliamentary acts.\textsuperscript{198}

Another issue that may require Court review is the extent of confidentiality of ECB and ESCB decision-making.\textsuperscript{199} This issue has had to be addressed already with regard to the extent of bank secrecy in application of the First Banking Directive\textsuperscript{200} in a criminal proceeding involving a bank. The Court’s judgement setting limits on the extent of bank secrecy in \textit{Hillegom v. Hillenius}\textsuperscript{201} caused the amendment of the bank confidentiality provision in the First Banking Directive by Article 16 in the Second Banking Directive,\textsuperscript{202} which permits exceptions to bank secrecy obligations in criminal and bankruptcy proceedings. The sensitive nature of ECB or national central bank confidentiality is manifestly more marked than that of commercial banks, but the Court of Justice may nonetheless impose some limits on such confidentiality in order to protect other public interests.

\begin{itemize}
\item \textsuperscript{196} Smits, supra note 11, at 108-09. See also Slot’s discussion of whether the ECB has the power to fine national central banks. Slot, supra note 63, at 246.
\item \textsuperscript{197} Gormley & de Haan, supra note 63, at 104.
\item \textsuperscript{198} For an analysis of when ECB guidelines may be deemed acts subject to judicial review, see Smits, supra note 11, at 109-10. Leading examples of cases in which the Court struck down Commission decisions for failure to provide sufficient reasoning or for failure to permit the private party concerned to state its views in the proceeding are: Germany v. Commission, Case 24/62, 1963 E.C.R. 63; and Transocean Marine Paint Association v. Commission, Case 14/74, 1974 E.C.R. 1063. The Court has also struck down a national central bank interest rate subsidy when it violated applicable Community rules. Commission v. Greece, Case 63/87, 1988 E.C.R. 2875.
\item \textsuperscript{199} Smits finds the Treaty language on the ESCB’s “professional secrecy” obligations unfortunately vague and suspects that the Court of Justice may ultimately have to provide clarification. Smits, supra note 11, at 110-11.
\item \textsuperscript{201} Case 110/84, 1985 E.C.R. 3947.
\item \textsuperscript{202} Second Council Directive 89/646/EEC on credit institutions, 1989 O.J. (L 386) 1.
\end{itemize}
E. The ECB Objective of Price Stability and the Amsterdam Treaty Goal of High Employment

EC Treaty Article 105(1), quoted in Part V above, set "price stability" as the "primary objective" of the ESCB, thus accepting the German argument that the Bundesbank's monetary policy success was due in large measure to its principal emphasis on price stability. Price stability is equated with a low inflation rate for products and services, especially consumer products and services.203 Although the Treaty fixes no specific target, price stability is usually seen as requiring an inflation rate lower than 2%, preferably approaching zero.204 Naturally the ECB will have considerable discretion in fixing a target rate of low inflation, or no inflation, for the Community in view of evolving economic and monetary conditions. It will certainly be subject to criticism and political pressure from Parliament and the other Community institutions if the inflation rate is seen to be at too high a level.

As a secondary duty, the ESCB is required by Article 105 to "support the general economic policies in the Community."205 The ESCB is also to "act in accordance with the principle of an open market economy with free competition," a major innovation in the Maastricht Treaty urged by Germany as a "ground rule" for ESCB action.206 Article 3a(3) lists some other guiding principles which the ESCB should respect: "sound public finances and monetary conditions and a sustainable balance of payments." But although the ESCB will certainly often develop rules and shape decisions to achieve one or another of these secondary objectives, Article 105(1) unequivocally declares these to be "without prejudice to the objective of price stability," which is manifestly given the primary emphasis.207

German fears of inflation are understandable, given the economic disaster of the 1920s, and Germany's enviable post World War II record of low inflation is certainly in large measure due to Bundesbank policies. A low inflation rate encourages long-term investment, confidence in long-term supply contracts, market stability, greater certainty in budgetary planning and tax collection, stable

203 There is no Treaty definition of "price stability," but the universal view is that it is identified with a low level of inflation. Smits describes it as "internal price stability" (the maintenance of domestic market purchasing power for goods and services), rather than "external price stability" (the maintenance of a stable value for a currency in comparison with other currencies). Smits, supra note 11, at 184.

204 See note 108, supra.

205 For an analysis of what might be considered to be Community economic policies, see Smits, supra note 11, at 187-192.

206 Italianer, supra note 39, at 69-70. This principle of an "open market economy with free competition" may prevent the ECB from carrying out rescue operations for weak banks in times of crisis, or from executing subsidy measures. Louis, supra note 150, at 18; Smits, supra note 11, at 190-92.

207 Smits argues that the ECB must always choose a course of action more favorable to stable prices than an alternative which serves other valid goals but is not as favorable to stable prices. Smits, supra note 11, at 187.
securities markets, insurance for long-term savings, social protection for pensioners, and so on.\textsuperscript{208}

But giving primary attention to a low inflation rate may handicap Member State action to combat economic and monetary crises and, in particular, efforts to reduce high unemployment and concomitant social distress. Economists are, not surprisingly, divided on their assessment of the degree of social and economic harm produced by high inflation versus that produced by high unemployment, and upon the precise nature of the link between inflation rates and unemployment rates.

The goal of price stability is often not granted particular priority in guiding the monetary policies of national central banks. Before the Maastricht Treaty, certain Member States, such as The Netherlands, assigned their central bank a broader goal than that of price stability: the goal of promoting general social and economic welfare. Most Member State governments and central banks looked to other goals in the setting of monetary policy. On a comparative note, in the United States the Federal Reserve places a high premium on maintaining price stability, but that is not its only concern. The statutory goal set for the Board of Governors of the Federal Reserve system is to "promote effectively the goals of maximum employment, stable prices, and moderate long-term interest rates."\textsuperscript{209} It is noteworthy that for the Federal Reserve price stability is not given special priority and that "maximum employment" is a specific goal, indeed the first mentioned. The Full Employment and Balanced Growth Act of 1978 added detailed bi-annual reporting requirements for the Federal Reserve, including specifically "past and prospective developments in employment, unemployment, production, investment, real income, productivity, international trade and payments, and prices."\textsuperscript{210}

The Federal Reserve itself has said, in describing its goals, that

\[\text{[m]any analysts believe that the central bank should focus primarily on achieving price stability [but] . . . tension can arise between efforts to reduce inflation and efforts to maximize employment and output . . . [or the need to confront] adverse supply shocks, such as a bad agricultural harvest or a disruption in the price of oil . . . In these circumstances, makers of monetary policy must decide the extent to which they should focus on defusing price pressures or on cushioning the loss of output and employment.}\textsuperscript{211}

For the last two years, some monetary and economic specialists have urged that the Federal Reserve raise interest rates to cut off incipient inflation because unemployment dropped below 6%, and then below 5% (and is currently 4.7%), but Chairman Alan Greenspan and the Federal Reserve Board have declined to

\textsuperscript{208} Even Gormley & de Haan agree on the benefits of price stability. See Gormley & de Haan, supra note 63, at 109-10.


\textsuperscript{210} 15 U.S.C.A. § 3101 et. seq.

do so. The inflation rate has continued to be around 2%. The debate is ongoing in the U.S., but it is clear that the Federal Reserve, faithful to its statutory mandate, is sensitive to concerns for a low unemployment rate as well as for a low inflation rate.

In view of this much more balanced and nuanced presentation of the Federal Reserve's goal in developing monetary policy, one may seriously question the wisdom of entrenching "price stability" as the primary goal of the ESCB and the ECB in the Maastricht Treaty. This is particularly true in view of the current grave problem of high unemployment levels. The 1991-1994 recession in the Community was quite severe and produced historically high unemployment virtually everywhere. Some Member States were especially hard hit—Finland, Portugal and Spain had unemployment at or approaching 20%. Although unemployment declined in many States during the 1994-1996 recovery, it still averages over 10%, and in fact has increased in both France (now at 13%) and Germany (currently over 12%).

Beginning with the December 1993 Brussels European Council, which formally approved the Commission White Paper on Growth, Competitiveness and Employment, the Community has given priority attention to programs to combat unemployment and promote stable, long-term jobs. After several European Councils continued this emphasis, the March 1996 Turin European Council directed the Turin Intergovernmental Council to take up the issue, with the result that the Treaty of Amsterdam contains important provisions concerning employment.

The Treaty of Amsterdam, signed on October 2, 1997 and now in the process of ratification, highlights the importance of Community activity to promote employment by amending TEU Article B to insert "a high level of employment" as a Treaty goal. Similarly, Article 2 of the EC Treaty now includes among the Community's tasks "a high level of employment and social protection" immediately before "sustainable and non-inflationary growth."

The Amsterdam Treaty also inserted into the EC Treaty a new Title VIa on Employment. A central provision is Article 109p(2), which states that "[t]he objective of a high level of employment shall be taken into consideration in the formulation and implementation of Community policies and objectives." The

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215 COM (93) 700 final (December 1993).


217 See supra note 122.
European Council, the Council and the Commission are all expressly mandated to implement this new emphasis on high employment.

Will the new Treaty provisions mandating efforts to attain high employment have potential consequences for the European Central Bank? The text of Article 105(1) was not modified, but obviously a high level of employment is now an integral part of the Community economic policies which the ESCB is required to support. Will this new factor affect to some degree the ECB’s primary emphasis on price stability? Given the political realities—virtually all Member States currently have liberal or social democratic governments—there is certainly the possibility that the ESCB’s policies will be influenced by the Member State governments’ desire to reduce unemployment. In the long run, it may be that the ECB, like the Federal Reserve, may be obliged by pragmatic considerations to give the goal of high employment virtual parity with that of price stability.

VII. THE SECOND STAGE AND THE CONVERGENCE CRITERIA

A. The Second Stage and the European Monetary Institute

When the Maastricht Treaty finally entered into effect on November 1, 1993, its provisions delineating the stages of progress toward an Economic and Monetary Union became operative. Denmark formally exercised its right to opt-out of the third stage at the time of its ratification of the TEU in May 1993, and thus will not (at least initially) participate in the ESCB, nor adopt the single currency. The United Kingdom continues to hold open its option to participate or not, although, as indicated in Part VII.C below, the Labor government of Prime Minister Blair is expected to try to convince the British people to support U.K. participation in the third stage sometime after 1999.

However, in spite of the more skeptical stances of Denmark and the U.K., the other Member States remain committed to the EMU goal. The German Parliament did insist during its ratification process that it provide a specific assent to Germany’s entry into the third stage immediately prior to that stage, and the German Constitutional Court stressed the importance of that final parliamentary assent in the court’s well-known 1993 Maastricht judgment.218 In effect, this means that the German government and its Parliament must review the final decision-making process in spring 1998 that determines which Member States qualify for entry into the third stage in function of their satisfaction of the convergence criteria.219 In the 1993-1994 negotiations with Austria, Finland and

218 The German Constitutional Court’s complex judgment of October 12, 1993 concluded that Germany’s ratification of the Treaty on European Union did not violate its Constitution, as amended by a new Article 23 intended to facilitate the further transfer of sovereign powers envisioned by the TEU. An English translation of the judgment is contained in Brunner v. European Union Treaty, [1994] 1 C.M.L.R. 57. For an excellent analysis, see Matthias Herdegen, Maastricht and the German Constitutional Court, 31 Common Mkt. L. Rev. 235 (1994). The judgment is summarized in Berman et al., 1998 Supplement, supra note 6, at 123-26.

219 See Smits, supra note 11, at 33-34. The Netherlands Parliament also stipulated during its ratification of the TEU that it would scrutinize the process of determining which Member States satisfied the convergence criteria. Smits contends that neither the Dutch nor the German
Sweden, their commitment to join in the proposed monetary union was made a condition for their accession, and the 1995 Treaty of Accession accordingly binds these Member States also to participate in the EMU.

As Article 109e of the EC Treaty provides, on January 1, 1994 the Community entered into the second stage of preparation for EMU. Pursuant to Article 109j(4), this stage is to be followed by the final one no later than January 1, 1999. The European Monetary Institute, composed of the Governors of each Member State central bank and a President named by common accord of the Member States, was created on January 1, 1994. The October 1993 European Council meeting in Brussels established EMI's seat in Frankfurt, in a decision reached with some difficulty because both Amsterdam and London also sought this seat. (Note that the same decision specified that the European Central Bank should also be sited in Frankfurt.) The first President of the EMI was a highly respected banking expert, Alexandre Lamfalussy, formerly head of the Bank of International Settlements in Basel.

Willem Duisenberg, the EMI's second president, who took office on July 1, 1997, and is to serve until the ECB replaces the EMI, is the former president of The Netherlands Central Bank, well-known as an advocate of a strong central bank and strict monetary policy. He is now regarded as the leading candidate to become the first President of the European Central Bank.

In 1994, the EMI commenced operations, first establishing its own procedures, and then starting the task of advising Member States on their monetary policies. Working with a small staff of experts (250 in 1997), the EMI issues an annual report on monetary policy each April, monitors the EMS, and regularly prepares studies and recommendations on aspects of monetary policy, banking and parliamentary review can in any way prevent the respective government from entering the third stage if it qualifies, because this is an absolute Treaty obligation. See id. at 133-34.

220 Participation in the Economic and Monetary Union was included among the key features of the "acquis communautaire," or essential political and economic rules and doctrines of the Community, that had to be accepted by the applicant states before the accession negotiations could take place. See Goebel, supra note 146, at 1155. Somewhat surprisingly, since the opt outs provided by TEU Protocols to Denmark and the U.K. were well known, none of the applicant states sought any similar opt out of EMU. Id. at 1156. For a detailed description of the accession negotiations by two Commission lawyers active in the process, see Dierk Booss & John Forman, Enlargement: Legal and Procedural Aspects, 32 Common Mkt. L. Rev. 95 (1995).

221 The three new Member States acceded to the Treaty on European Union, including its EMU provisions, which had entered into force on November 1, 1993. The Act of Accession, containing adjustments to the TEU necessitated by the addition of the new States is in 1994 O.J. (C 241) 21, as modified by Council Decision of January 1, 1995, 1995 O.J. (L 1) 1 (making the revisions required by Norway's failure to ratify the accession treaty).


225 In view of Dr. Duisenberg's short term as President of the EMI (from July 1, 1997 to May 1998), observers assumed that his choice represented a tacit agreement to name him as the first ECB President. This still seems probable, although the names of other candidates, notably that of the president of the Bank of France, have been advanced.
finance. Article 109f mandates the EMI to prepare the "regulatory, organizational and logistical framework" for the ESCB. Accordingly, together with the Commission, the EMI has been providing the recommendations for legislation and policy in preparing the transition to the third stage of monetary union. In particular, the EMI has been responsible for the technical preparation of the banknotes that will become the single currency. In general, the EMI is performing its role as an "interim institution"—a sort of "John the Baptist" preparing the way of the ECB—in a highly effective manner, although somewhat handicapped by the Rome IGC's decision not to give it operational monetary control powers, which are reserved to the ECB.

Because 1994 marked the start of recovery from the serious 1992-1993 recession that affected the entire Community, the prospects for successful attainment of an EMU then began to improve. As previously noted, the Turin European Council, held in March 1996, did not include any change in the TEU provisions on the EMU on the IGC agenda, with the result that the Amsterdam Treaty makes no change in that regard. Government leaders certainly realize that attaining the requisite convergence criteria demands hard effort and some unpopular measures, but they also appear to recognize the high economic and political costs of failing to create an EMU. Successive European Council meetings in 1995-1997, especially those of Madrid, Dublin and Amsterdam, took several key policy decisions concerning the planning for the third stage, and directed the Commission, the Council and the EMI to make further efforts to achieve the EMU in accordance with the EC Treaty timetable.

Deciding that Member States must meet certain economic and monetary standards in order to join in EMU is one thing; helping them to do so is quite another. Already in the Commission's August 21, 1990 communication on EMU, the Commission laid great stress on the need to develop an effective system of cooperation between the Community as a whole and individual Member States, notably the elaboration of pluriannual economic policy guidelines and multilateral surveillance of budgetary performance. This basic approach was early agreed upon in the Rome IGC and detailed provisions for the execution of cooperative multilateral surveillance were inserted into the EC Treaty itself.

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227 This preparatory process is discussed further in Part IX, infra.

228 See supra notes 71-74 and accompanying text. Smits also notes that the EMI seems to be concerned about making some decisions to plan for features of the third stage, because of the possibility that the ECB, which will represent only the participating states (and not all the Member States represented in the EMI), might take a different view on the issues involved. Smits, supra note 11, at 48.

229 These decisions are described further in Part VIII.A, infra.

230 Commission, Communication on EMU, supra note 39, at 23-25.

231 Italianer, supra note 39, at 71 & 76-77. For a detailed analysis of the Treaty procedures, see Smits, supra note 11, at 72-74.
In application of Articles 103 and 104c, the Community has energetically undertaken the serious coordination of economic and monetary policy, in particular to give guidance to Member States in the elimination of excessive deficits and accumulated debt. The Council adopted a series of technical regulations and decisions in late 1993 in order to make more precise the standards for avoiding excessive government debt and for the calculation of financial resources, as well as to oblige Member States to consult the EMI on any monetary proposals. The ban under Article 104 on the direct financing of government deficits by central banks (popularly referred to as "no more bailouts") came into effect on January 1, 1994.233

The Commission reviewed the excessive deficit levels that were considered to prevail in all Member States except Ireland and Luxembourg, and on November 7, 1994 the Council for the first time issued guidelines for corrective action.234 This process of review and guidance continued in 1995-1997, with the Council issuing further guidelines for Member States whose monetary conditions had deteriorated (e.g., France and Germany), while removing others (Denmark, Finland and The Netherlands) from the list of those having an excessive deficit.235 The remarkable level of progress that several Member States, notably in the Mediterranean tier, have made toward qualifying for the third stage during the 1995-1997 period is due in no small measure to the efficacy of this surveillance and planning procedure, which sets targets in a more objective fashion. Political leaders may then point to these targets as a means of justifying unpopular budget saving measures to the general public.

The economic condition of all Member States improved radically in 1995, and moderately since then. Due in part to this relative economic health, but perhaps even more to unusually strong political will, most Member States have made great, and in some instances surprisingly rapid, progress toward attaining the TEU's mandatory convergence criteria, which now shall be explained in more detail.

B. The Convergence Criteria

Article 109e(2) prescribes that Member States shall, during the second stage, adopt "multiannual programmes intended to ensure the lasting convergence necessary for the achievement of economic and monetary union, in particular with regard to price stability and sound public finances," and 109e(4) adds that the Member States "shall endeavor to avoid excessive government deficits." Articles 104c(2) and 109j(1), supplemented by the Treaty Protocols on the Excessive Deficit Procedure and on the Convergence Criteria, set in more

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233 Smits discusses the vital nature of this rule in Smits, supra note 11, at 74-77.
specific terms the economic and monetary conditions Member States must meet for eligibility to participate in the third stage of monetary union.

Three of these conditions, set fairly early in the Rome Intergovernmental Conference, have proved surprisingly attainable. The first is "a high degree of price stability," measured by the attainment of an inflation rate close to that of the three best performing Member States in terms of price stability. The text is somewhat ambiguous: it is not clear whether the point of reference should be the average inflation level of the three best performing states, or the inflation rate of the poorest among the three best performing states. However, the use of the word "close" to that level permits a degree of flexibility in application in any event. Article 1 of the Protocol on Convergence Criteria specifies that "close" shall mean that the target inflation rate should be one not in excess of 1.5% above the inflation rate of the three best performing States, using the "consumer price index on a comparable basis" to gauge the inflation rate.

In the period 1994-1997, the Member States made highly satisfactory progress in lowering their inflation rates, in some cases to one half or one third of their prior level. By the end of 1996, the Commission estimated the average inflation rate of all Member States at slightly above 2.6%, and the Commission expects that figure to drop to around 2.1% in 1997. The average inflation rate for the three best performing Member States was around 1.5%, and should stay around that level in 1997. By the end of 1996, the Commission concluded that ten states were within the required inflation rate range, and by the end of 1997 only Greece is certain to have an excessive inflation rate (and even Greece has made significant progress in this regard).

Closely connected to the inflation rate criterion is the second one, requiring Member States' long term interest rates to attain a level not exceeding by more than 2% the level of the three best performing states. Long term interest rates tend to move in tandem with inflation rates (although not invariably), and these rates fell throughout the Community in 1994-1997. The Commission viewed eleven Member States as satisfying this criterion in 1996. By the end of 1997,

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236 Italianer informs us that the precise text, with the percentage figures, was worked out in October 1991. Italianer, supra note 39, at 99.

237 Smits argues for the use of the average inflation rate. Smits, supra note 11, at 124. This seems the most likely to be adopted.

238 Protocol on the Convergence Criteria Referred to in Article 109j of the Treaty Establishing the European Community, annexed to the TEU.


242 Greece's inflation rate is expected to drop from 8.5% in 1996 to 3.5% in 1999. Commission Press Release, supra note 240, at 3.

243 Protocol on the Convergence Criteria, Article 5.

only Greece is fairly certain to have long term interest rates exceeding by 2% the average level (slightly above 6%) of the three best performing states.245

The third criterion is that a Member State's currency must remain within "the normal fluctuation margins provided for by the exchange rate mechanism of the European Monetary System without severe tensions for at least the last two years before the examination".246 Neither the EC Treaty nor the Protocol specifically require that Member States formally adhere to the Exchange Rate Mechanism247—an important point, since Finland joined and Italy rejoined the ERM in October and November 1996 respectively,248 and Greece, Sweden and the U.K. continue to remain outside the ERM. As was noted in Part II above, the exchange markets have been quite stable since mid-1995.249 Satisfaction of this criterion is expected for all Member States, with the possible exception of Greece.

The fourth and by far the most difficult criterion is that Member States must not have an excessive deficit. Under Article 104c and Article 1 of the Protocol on the Excessive Deficit Procedure,250 this criterion has two aspects: (1) the current annual government deficit should not exceed 3% of the national gross domestic product (GDP) at market prices; and (2) the accumulated total government debt should not exceed 60% of GDP. Article 2 of the Protocol specifies that key terms are defined in accordance with the usage of the European System of Integrated Economic Accounts and that, in particular, the term "government" includes "central government, regional or local government and social security funds, to the exclusion of commercial operations." This definition is especially important for the calculation of total government debt of federal states, since their component states or regions often have substantial debt.

The idea that Member States must not have an excessive deficit in order to qualify for the third stage was accepted early on,251 but the setting of a yardstick to measure such deficits proved to be a difficult task. The exact terms were still not set in the June 1991 Luxembourg Presidency draft and were only agreed upon in October on the basis of a Monetary Committee study.252 In view of the traditional use of deficit financing by many Member States to meet current

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245 These figures are not yet available for 1997. The text estimate is based on a report, Convergence Situation of Potential EMU Members, produced monthly by Deutsche Morgan Grenfell.
246 EC Treaty, art. 109j(1) and Protocol on the Convergence Criteria, Article 3.
247 Smits holds the contrary view that formal participation of Member States in the ERM "seems to follow" from the text. Smits, supra note 11, at 126. With all due deference to his expert opinion, it would seem implausible, and politically impossible, for the other Member States to exclude Finland or Italy from participation in the third stage in the Article 109j decision that will occur in May 1998 only because they did not join the ERM until October or November 1996.
249 Id. at point 77.
250 Protocol on the Excessive Deficit Procedure, annexed to the TEU.
251 The Commission's August 21, 1990 Communication on EMU urged that this principle, with a "yardstick" to measure it, should be set in the Treaty. Commission, Communication on EMU, supra note 39, at 25.
252 Italianer, supra note 39, at 82.
social and economic needs, and the enormous accumulated government debt loads of several states, the excessive deficit criterion was always recognized as the “make or break” factor in qualification for the final stage.

Although almost all Member States made remarkable progress in 1995-1997 toward reducing their annual deficit and lowering their accumulated total debt, nonetheless, many would be unable to meet the Protocol criteria if these were to be applied strictly. This is especially true for the total debt aspect, because several Member States have attained extremely high levels in the past. Thus, at the end of 1996, Belgium, Greece and Italy had total debt levels well in excess of 100% of GDP, and Austria, Ireland, The Netherlands and Sweden all had debt levels in excess of 70% of GDP.253

Fortunately, the drafters of the relevant TEU Treaty provisions foresaw the need for a certain degree of flexibility. Article 109j(1) stipulates that Member States must not have an excessive deficit, but that provision cross-references to Article 104c(6), which gives the Council the responsibility for deciding “after an overall assessment whether an excessive deficit exists.” The Council in turn works on the basis of a Commission report which need only find, according to Article 104c(2), that the current annual deficit “has declined substantially and continuously” and is “close to the reference level,” and that the total accumulated government debt “is sufficiently diminishing and approaching the reference value at a satisfactory pace.”

Accordingly, both the Commission in its report and the Council in its final decision may conclude that a Member State’s sustained progress toward meeting the Protocol levels is sufficient, even though the state has not yet attained the required levels.254 It is noteworthy that the Council decided in 1997 that Denmark, Ireland and The Netherlands do not have an excessive deficit,255 even though all three states still have accumulated government debts in excess of 60% of GDP, because all three have continuously and significantly reduced the total government debt.

C. Current Prospects

The relative flexibility in applying the Protocol standards is extremely important because in early 1997 the severe unemployment rates in several Member States (which continue to exceed 10% throughout the Community, and currently exceed 13% in France and Spain), together with other economic problems (notably the continued cost to Germany of its financial aid to former East Germany), have compelled several Member States to incur budget costs that make it rather doubtful that they will precisely hit the Protocol targets by the

253 Estimates vary—the text figures are based on Deutsche Morgan Grenfell reports on the Convergence Situation of Prospective EMU Members.
254 Smits declares that both the Commission and the Council may go beyond the quantitative reference criteria and make a qualitative judgment on the degree of compliance of a State with the criteria. Smits, supra note 11, at 79.
255 Bull. EU 5-1997, at 16. The Council decision specifically added Finland and The Netherlands to the list of States without an excessive deficit, joining Denmark, Ireland and Luxembourg.
end of 1997. Indeed, when the new French Socialist government of Prime Minister Jospin won its surprising victory in June 1997, it announced its intention to giving the battle against high unemployment a higher priority than meeting the deficit criterion, although it subsequently reaffirmed its intention to meet the Maastricht Treaty convergence criteria.

Despite the manifest unhappiness of Germany's Bundesbank with the prospect, it appears likely that the Community leaders will be relatively lenient in 1998 when they assess how closely Member States must come to the deficit and debt target figures. Several Member States may barely meet or marginally exceed the 3% annual deficit criterion, in some instances (as in France and Italy) by the use of extraordinary sales of state assets or unusual taxes. Article 109j(4) stipulates that in early 1998, the Council acting in the composition of Heads of State or Government, based on Commission and EMI reports, must decide whether Member States meet the convergence criteria, and accordingly move to the third stage of the monetary union. France attempted to have the June 1997 Amsterdam European Council delay this date, but without success.²⁵⁶ Most observers, including financial market experts, currently expect that the Council will consider that almost all Community States will be deemed to meet the convergence criteria, with the exception of Greece.

At the time of the Danish referendum in May 1993, Denmark exercised its opt-out right stipulated in a TEU Protocol, but the current Danish government is believed likely to move for reconsideration of the issue in a referendum at some auspicious point after the third stage begins. Similarly, the labor government of Prime Minister Blair in the U.K. announced in late 1997 its intention to exercise the U.K. opt-out granted by its Protocol, but to try to secure popular support for U.K.'s entry into the third stage of EMU no later than the date of the next U.K. election (hence, no later than May 2002).²⁵⁷

The Swedish government presently does not desire to join the third stage. Although Sweden is quite likely to satisfy the convergence criteria, Sweden has not made its central bank independent and accordingly technically does not satisfy a Treaty-based criterion for joining. At present it appears that the other Member States will acquiesce in Sweden's failure to take the necessary measure to join the third stage. This is rather surprising, considering the insistence that Sweden and the other applicant states must consider the joining of EMU as a non-negotiable condition for their accession in 1995, but presumably it is now politically unpalatable to pressure Sweden into joining, or for that matter to take any legal action against Sweden.²⁵⁸


²⁵⁸ Permitting Sweden to opt out without any Treaty Protocol to this effect represents an unfortunate acceptance of the "Europe à la carte" mentality. Presumably, if the Commission or
Accordingly, the current prospect is that a large majority of Member States, probably eleven (excluding Denmark, Greece, Sweden and the U.K.), will begin the third stage of monetary union on January 1, 1999, the date set by Article 109j(4). This has a number of important consequences. Politically, this is quite desirable, because it will reduce the tensions inevitably produced by a "two-tier" Europe, tensions that would be particularly severe if all the Mediterranean states failed to join. With regard to the Member States that don't join in 1999, there is a good prospect that all will join by or around 2002 (even Greece has pledged to meet the criteria by that date). Given the enormous economic, monetary and even political ramifications of participation in the final stage of monetary union, it is of capital importance that ultimately all Member States join in the venture. Moreover, most of the Eastern European states that are scheduled to begin negotiations in 1998 to join the Union are also reasonably likely to be capable of joining the monetary union as well by the date of their accession (which in any event is unlikely to be earlier than 2002).

From a monetary point of view, the addition of a number of Member States that traditionally have not had strong economies, or that have often been willing to incur substantial government deficits, may well mean that the monetary union will not be as fully committed to strict monetary policies as Germany and The Netherlands have been. Consequently, the new single currency may well fail to match the traditional strength of the German mark or the Dutch guilder. That is certainly the forecast of most financial market experts presently. (In Part II above, it was noted that both the dollar and the U.K. pound have markedly appreciated against all the continental Community states' currency in 1997, in part because of concern about the future strength of those apt to be replaced by the euro.) This possible adverse result, however, should be more than balanced by the fact that an EMU composed of all, or virtually all, the Member States will maximize the market benefits of greater cost and price transparency and more efficient competition, already mentioned in Part I above. Moreover, if the entire Community is within the EMU, more economic and monetary resources will be available to the ECB and the Community political institutions to confront the problems posed by temporary recession or high unemployment in some Member States. Although economists are divided in their assessment of the level of risk that some states are more prone to asymmetric economic shocks than others, the risk of such shocks is certainly genuine. If all the Member States, including those with relatively sound economies, such as Denmark, Sweden and the U.K., are part of EMU, central planning to confront crises may well be easier to execute and to carry out.
VIII. POLICY DECISIONS AND MEASURES TO PREPARE FOR EMU

A. European Council Policy Decisions

During 1995-1997, the Commission and the European Monetary Institute worked intensively to prepare reports, studies and draft proposals for the policy decisions and regulatory measures necessary to successfully prepare in time for the shift to the third stage of EMU in 1999. The Council, working usually in its composition of finance ministers (the “Ecofin Council”), generally approved the proposed initiatives, although often with significant modifications. The most serious issues were transmitted to the European Council for determination, sometimes by compromises, at its regular meetings.

The first series of major policy decisions were taken by the Madrid European Council in December 1995. This meeting endorsed the “scenario for the changeover to the single currency,” largely as proposed by the Commission and the EMI.259 Since press reports suggested that Italy and Spain were inclined to prefer a delay in the inauguration of the final stage of EMU, the European Council’s determination to accept the proposed scenario, strongly advocated by Germany, represented a significant policy decision. The European Council also adopted the name, “euro,” for the banknotes and largest denomination coins for the new single currency, considering the name to be “simple” and to “symbolize Europe” while being easy to use in all languages. (The name “ECU” was rejected because of fears that investors who had lost money through their purchase of ECU-denominated securities, in comparison to the stronger dollar or mark-denominated securities, would not have total confidence in a currency using the ECU name.260)

The scenario, or timetable, called for the preparation of all essential draft texts by the end of 1996, and for their revision and approval in 1997-1998. As soon as possible after the determination of the Member States qualifying for entry into the third stage in early 1998, those states should select the Executive Board and the central bank governors constituting the Governing Council of the ECB. The ESCB and the ECB should then begin preliminary operations. In 1998, the Council and the ESCB should complete the adoption of secondary legislation and start the production of euro banknotes and coins.

On January 1, 1999, the formal date of commencement of the third stage, the critical legislation should enter into force, notably that irrevocably fixing the rates for conversion from national currencies into the euro, and that on continuity of contracts. During 1999-2001, the euro would be used for Community and participating Member State accounts, loans and inter-state financial transactions. A Council regulation should provide a “legal framework”


260 Smits, supra note 11, at 491 n.19. Smits not only considers the change to be improper, because taken by the European Council instead of through a Treaty amendment, but also unfortunate since “the name ‘ecu’ had historical roots and sounded much better than the horrid and unimaginative name ‘euro.’ ” Id. at 492. The latter comment is certainly widely shared.
for the use of the euro beginning in 1999. Private parties might use the euro in their transactions starting in 1999, but would not be required to do so (the principle commonly known as "no prohibition, no compulsion."\textsuperscript{261}) The euro banknotes and coins should be introduced and become legal tender on January 1, 2002, and national currency should cease to be legal tender no later than June 30, 2002.

The December 1995 Madrid European Council scenario was of capital importance in the evolution toward EMU. It marked the end of any hesitation produced by the prior recession and turmoil in the currency exchange markets during 1991-1994. The approach adopted in the scenario was pragmatic, clear-cut and established a definite agenda for specific actions.\textsuperscript{262} It also represented a decisive commitment to move ahead toward EMU without any fundamental change, so that the subsequent March 1996 Turin European Council saw no reason to place issues concerning EMU on the Turin IGC agenda.\textsuperscript{263}

The next major policy decisions came at the Dublin European Council in December 1996.\textsuperscript{264} The meeting officially confirmed that the third stage of EMU could not begin early, but would definitely start on January 1, 1999. This insistence on adherence to the EC Treaty timetable marked the political determination of Chancellor Kohl of Germany and President Chirac of France in particular, as several other Member States were inclined to postpone that date.

A major debate in 1996 concerned the Commission's proposed "stability and growth pact," intended to ensure that Member States would continue to maintain budget discipline and comply with the deficit criteria after joining the monetary union. Germany fought vigorously for strict standards,\textsuperscript{265} while most other Member States wanted more lenient ones, applied through a political decision, rather than applied by the Central Bank on purely monetary grounds. The December 1996 Dublin European Council set a compromise. Its conclusions directed that a structure be created for systematic, ongoing surveillance of Member States' budgetary and economic conditions with the goal of anticipating serious problems and avoiding any need for sanctions. States that nonetheless do not continue to meet the annual standards are to be sanctioned by being obliged to pay over a large non-interest bearing deposit equivalent to a sum representing from 0.2% to 0.5% of their GDP to the European Central Bank, to be kept until the deficit is reduced, with the risk that the deposit would be forfeited if the deficit status is not corrected within two years. However, the Council should

\textsuperscript{261} Id. at 132.

\textsuperscript{262} Smits describes the Madrid scenario as "relatively simple and user-friendly, [ensuring] an efficient change-over without competitive distortions." Id.

\textsuperscript{263} See supra note 174 and accompanying text.


\textsuperscript{265} The initial idea came in a German Ministry of Finance proposal in late 1995, which was taken up but modified by the Commission in view of the position taken in preliminary discussions in the Monetary Committee and the Ecofin Council. See Smits, supra note 11, at 84-85.
have the power to waive this sanction for Member States suffering a severe recession or other economic crisis.\textsuperscript{266}

The Dublin European Council also endorsed the proposal from the Econfin Council and the EMI for a new Exchange Rate Mechanism, ERM II, to govern relations between the Member States joined in EMU's third stage and those remaining outside. This was obviously a topic of considerable sensitivity. The proposal does not require any Member State to join in ERM II. Those that do join will only be obliged to keep their currencies within a relatively wide band, presumably the present ±15\% range.

At the June 1997 Amsterdam European Council meeting, an effort by the newly-elected French Socialist government of Prime Minister Jospin to retard the 1999 target for the third stage was firmly rejected by the other Member States. The meeting reaffirmed the need to act early in 1998 to set the number of participating Member States and to create the ESCB. The meeting also endorsed the text of the key pieces of secondary legislation, the formal structure of ERM II, and the technical decisions on the design of the euro coins.\textsuperscript{267}

The December 1997 Luxembourg European Council meeting endorsed the further progress on the legislative front, and urged that more rapid action be taken in 1998. Thus, it requested Member States to present their final 1997 statistics in February 1998, that the Commission and the EMI issue their reports on the Member States' convergence levels in March, and stipulated that the final decision on the identity of the participating Member States should be taken in May 1998.\textsuperscript{268} The European Council likewise reaffirmed the importance of ongoing coordination of national economic policies in the final stage.

Thus the stage is now set for the critical final series of policy and structural decisions to be taken in 1998 to launch the third stage of EMU. As previously indicated, although the statistics are apt to show that several Member States (notably France, Germany and Italy) are very close to the wire in meeting the convergence criteria, it is expected that the Commission and EMI reports will be somewhat liberal in applying the Treaty and Protocol standards. At the Council meeting scheduled for May 1-3, 1998, the Council in its extraordinary composition of Heads of State and Government will decide which Member States qualify for entry into the third stage. All Member States will vote on this issue. Naturally, only the states qualifying for the third stage will participate in the designation of the Executive Board members and the national central bank governors, who together will comprise the ECB, whose creation should take place shortly thereafter.

\textsuperscript{266} For a more detailed summary, see id. at 86-90. In Smits' appraisal, although he considers the structure politically necessary, he deprecates this "further intrusion of the European Council in an area reserved for the Community institutions." Id. at 90.


B. Essential Measures for EMU

Turning to the regulatory measures adopted to facilitate the progress toward EMU, a matter of great concern since the Delors Report has been the degree of differences between Member States in their computation of key statistics. In 1991, a committee on monetary, financial and balance of payment statistics was created to try to improve the consistency and reliability of statistics in that field, and in 1992 the Commission adopted a priority program for action to achieve reliable and comparable statistics for the period 1993-1997.269 Undoubtedly the most important single measure adopted in this field is Council Regulation EC 2494/95 on harmonized indices of consumer prices.270 This regulation set up a system to improve the comparability of consumer prices in Member State statistics, imposed an obligation to provide "honest and complete information,"271 required monthly production of source data, and created a structure for the compilation of a European Index of Consumer Prices by the Commission. Obviously, the need to ensure accurate national consumer price statistics is critical for the ultimate assessment of the number of Member States that meet the price stability criterion for entry into the third stage.

The Dublin European Council’s policy decision on the nature of the “stability and growth pact” has been carried out by the adoption of two regulations, both on July 7, 1997. The first, Council Regulation EC 1466/97 on the surveillance of budgetary positions and economic policies,272 is intended, as its name suggests, to improve the flow of economic information from Member States to the Commission and Council, and thereby to improve the surveillance of the states’ economic and monetary positions. Each state participating in the final stage of EMU must adopt annually a Stability Program, consisting of medium-term budgetary objectives which show the state’s budget to be in surplus or at least close to balance, and which provide relevant data and assumptions on economic developments.273 These State Stability Programs are to be assessed by the Commission and the Council.274 The Council may, if it has concerns, provide recommendations intended to serve as an “early warning” to the Member State to make adjustments.275 The Council has the discretion to decide whether to make its recommendations public (a step that might well create greater pressure upon the Member State in question). A similar approach is to be followed for non-participating Member States to monitor their progress toward satisfying the convergence criteria.276 The Regulation is to enter into effect on July 1, 1998,

271 1995 O.J. (L 257) 1, at art. 7.
272 1997 O.J. (L 209) 1.
273 See Council Regulation EC 1466/97, art. 7.
274 See id. at art. 5.
275 See id. at art. 6.
276 See id. at arts. 7-10.
essentially coinciding with the creation of the ESCB and the final preparations for the third stage.

The second measure, Council Regulation EC 1467/97 on the implementation of the excessive deficit procedure, provides the legal force and the details for execution of the Dublin European Council policy decision. This regulation, citing EC Treaty Article 104c, notes the obligation upon Member States participating in the final stage of EMU to continue to avoid excessive deficits. If the Council decides that a participating Member State has an excessive deficit, the Council shall promptly recommend corrective measures. If the state fails to take effective action expeditiously, the Council may impose a sanction in the form of a non-interest bearing deposit equivalent to at least 0.2% of the state’s GDP, with possible higher levels of sanction as a function of the size of the state’s deficit. This deposit shall “as a rule” be converted into a non-recoverable fine if within two years, in the opinion of the Council, the excessive deficit status is not corrected. The Council may excuse the excessive deficit if the Member State has experienced “an annual fall of real GDP of at least 2%,” or if the state can demonstrate that its annual GDP reduction of less than 2% is nonetheless sufficiently exceptional in character. The system set up for penalties is obviously intended to constitute a deterrent that would motivate any Member State to avoid an excessive deficit, or to correct one quite expeditiously.

IX. PREPARATION FOR THE SINGLE CURRENCY, THE EURO

A. Studies and Planning for the Euro

The dimensions of the technical difficulties involved in creating a single currency were outlined in a 1994 Commission Communication, “Practical problems involved in introducing the ecu as the European Union’s single currency.” The Commission provided a longer study in its 1995 Green Paper on the Introduction of the Single Currency. Both rejected a “big bang” rapid introduction in favor of a carefully regulated preparation over three years, followed by a several month transition period for the actual introduction of the single currency.

The studies note that the banking industry and the financial sector will require massive revision of denominations of loans, deposits, security instruments and operating procedures, and that automatic teller machines must be modified, computer software programs revised, and so on. Public administrators, especially the tax, social security and budgetary authorities, will likewise have serious problems in restructuring, while in the private sector the retail industry will need

278 Council Regulation EC 1467/97, art. 3.
279 See id. at art. 12.
280 See id. at art. 13.
281 See id. at art. 2.
to revise operations substantially. Since 1995, the Commission, together with the European Monetary Institute, has encouraged studies and conferences to involve as many interested parties as possible in the process of planning and concrete preparation. Thus, a roundtable conference organized by the Commission in January 1996 was attended by 500 representatives of all the sectors concerned and resulted in guidelines for private sector action. The most recent major Commission study is its October 1, 1997 Communication on Practical Aspects of the Introduction of the Euro, advising both public authorities and the private sector on the manifold measures necessary in 1999-2002 to ensure a smooth transition to the euro.

In accordance with the timetable approved by the December 1995 Madrid European Council, on January 1, 1999 the Member States participating in the final stage of monetary union will permanently freeze their national currencies into the until then merely nominal single currency, the euro. In fact, to provide greater stability to the financial markets, the December 1997 Luxembourg European Council instructed the Council to decide on the precise conversion rate for each participating national currency in early May 1998.

As noted previously, in the three-year period from 1999 to 2001, the participating Member States will use the euro for all national budgetary and accounting purposes, will float their debt only in euros, and will use euros for their inter-state monetary movements. In effect, the national currencies of these states will exist only as expressions, or sub-units, of the euro as the official currency. As the Green Paper states, the euro "becomes a currency in its own right, for which the national currencies are perfect substitutes, i.e., different denominations of the single currency."

Financial institutions must operate in euros in their dealings with central banks and on an inter-bank basis. Commercial enterprises will be encouraged to use the euro as much as possible in their internal accounts and external transactions, but will not be required to do so—the principle is one of "no prohibition, no compulsion." Many large multi-national groups, especially in Germany and The Netherlands (e.g., Daimler-Benz, Phillips and Siemens), have already announced their intention to do so. Thus, they will set up their internal accounts on a dual basis, keeping them both in euros and in their national currency, will float their debt predominantly in euros, and will invoice and accept payment in euros as well as in national currency. Many banks are likewise expected to handle client deposit and loan accounts on a dual euro/national-currency basis, which should help in the process of familiarizing the general public with the new currency. London and other financial centers are expected immediately to trade securities denominated in euros.

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286 See also supra note 268 and accompanying text.
287 Green Paper, supra note 3, at 18.
To advance planning in the capital markets, the Commission issued in July 1997 the Giovannini Report, proposed by financial sector experts. Note that all enterprises organized in corporate form must redenominate their capital, securities and debt in euros no later than June 30, 2002. Many are engaged in advance planning. Commission studies have suggested that all Member States create the legal possibility of no-par shares to facilitate this changeover. The process may produce tax consequences in some states, which will probably necessitate specific legislative treatment.

Because it will take several years to print and safely store the enormous number of new euro banknotes to issue as legal tender on January 1, 2002, the EMI has moved rapidly to fulfill its role, foreseen in EC Treaty Article 109f(3), of setting the technical specifications for the banknotes. An April 1995 EMI report set the denominations at 5, 10, 20, 50 and 100. After detailed studies and a competition in mid-1996 to select the design for each face of the banknotes, the EMI decided to use non-existent monuments and bridges with a European cultural flair on the banknote faces, together with the European flag. Each denomination will have a different size, a different color and will have tactile qualities to help the visually impaired to differentiate them.

Article 105a of the EC Treaty gives the Council the power to determine the nature of euro coins. The process of setting their denominations and features is now well advanced. The Commission proposed a draft Council regulation on the denominations and technical specifications of euro coins, which, incidentally, must be reviewed by the Parliament under the cooperation procedure. This text proposes one and two euro coins, and 1, 2, 5, 10, 20 and 50 cent coins. The draft sets their shape, size, color and edges, and notes that the vending machine association representatives and the European Blind Union were duly consulted to ensure that the coins would be as suitable as possible for convenient and safe use. Since the June 1997 Amsterdam European Council has given its endorsement to the Commission draft, the Council should adopt the final regulation soon.

B. Essential Measures for the Creation of the Euro

The most important measure necessary to launch the single currency is still in draft form, a proposed regulation on the introduction of the euro. This must remain a draft, because it is to be adopted using EC Treaty Article 109 I (4) as its legal basis, which means that action must be taken by the Council in a special body representing the participating Member States after they are

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291 1997 O.J. (C 208) 5.
293 1997 O.J. (C 236) 8. The text was substantially modified and made more detailed in its review by the Council and the Parliament. For the Commission's initial proposal, see 1996 O.J. (C 369) 10.
designated, presumably in May 1998, and after the ECB is constituted and can
give its opinion on the text. However, in view of the critically important nature
of the draft, and to promote legal certainty, the European Council meeting at
Amsterdam in June 1997 took the unusual step of adopting a specific resolution
endorsing the draft text.294

The draft regulation on the introduction of the euro essentially would give
legal force to the policy decisions reached by the Madrid European Council in
December 1995. Article 2 adopts the name, euro, for the single currency, and
divides one euro into one hundred cents. Article 3 prescribes that the euro is to
be substituted for national currency units at the irrevocable fixed rates to be set
by the Council pursuant to Article 109 1 (4). (As noted above, this is now
scheduled to occur in May 1998.) The euro is then to be the unit of account for
the ECB and all participating national central banks.

Articles 10-11 of the draft regulation mandate the ECB to put euro banknotes
into circulation on Jan. 1, 2002 at the latest, and the Member States to issue
euro and cent coins at the same date, both assuming the status of legal tender.
Under Article 15, national currency banknotes and coins may remain legal
tender for no longer than six months thereafter. Article 12 requires participating
states to “ensure adequate sanctions against counterfeiting” of euros.

The transition period, 1999-2001, is covered in Articles 6-9 of the draft
regulation, which provide essentially that all legal instruments (laws, regulatory
or administrative acts, judicial decisions, contracts, instruments of payment, etc.)
may be set either in euros or in a national currency. Acts to be performed under
the instrument (e.g., payment under a sales contract) are then to be carried out in
the currency specified—but subject to anything the parties involved may agree
(thus adopting the principle of private party autonomy). However, a debtor
always has the option to pay a creditor either in euros or the national currency.
Member States may redenominate their prior outstanding debt into euros, but
they are not obligated to do so. They may also permit organized markets (e.g.,
stock or commodities exchanges) to change their units of account from the prior
national currency to euros.

Of equal importance, and finally adopted, is Council Regulation EC 1103/97
on certain provisions relating to the introduction of the euro.295 This is
commonly known as the Article 235 Regulation, because it was adopted by use
of Article 235 of the EC Treaty, since the monetary provisions of the TEU set
no legal basis for it. It is also known as the “continuity of contracts regulation,”
because that is its principal subject. Although a Recital to the Regulation notes
that “it is a generally accepted principle of law that the continuity of contracts
and other legal instruments is not affected by the introduction of a new

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294 1997 O.J. (C 236) 7.
295 1997 O.J. (L 162) 1. The initial Commission draft is in 1996 O.J. (C 369) 8. For a thorough
discussion (but prior to the final Regulation text) of the continuity of contract and other issues
involved in the creation of the euro, see D. Dunnet, Some Legal Principles Applicable to the
Transition to the Single Currency, 33 Common Mkt. L. Rev. 1133 (1996) and V. Wolker, The
Continuity of Contracts in the Transition to the Third Stage of Economic and Monetary Union, 33
currency," nonetheless "in order to reinforce legal certainty and clarity," the Regulation was adopted. Another Recital expresses the hope that third country jurisdictions will accept and apply the principles set in the Regulation, because its terms represent the monetary rules of the jurisdiction issuing the currency.

The key provision is Article 3, which states:

The introduction of the euro shall not have the effect of altering any term of a legal instrument or of discharging or excusing performance under any legal instrument, nor give a party the right unilaterally to alter or terminate such an instrument. This provision is subject to anything which parties may have agreed.\(^{296}\)

This expressly binding rule of continuity of contracts is meant to bar completely any claim for rescission, cancellation or non-performance under national law based on statutory or case law rules on frustration, impossibility, material alteration of terms, inequity, and so forth. Note however that the principle of party autonomy is respected: the parties may agree to the contrary. While it is probably true that the rule of continuity of contracts would have been applied in national courts in any event, the Regulation will certainly provide clear guidance to business operators and avoid unnecessary litigation.

Article 2 of the Regulation further specifies that any reference in a legal instrument to an ECU should be replaced by one to a euro, on a one ECU to one euro basis. Finally, Article 4 stipulates that conversions from national currencies into euros shall be made by a calculation with six significant figures, without any rounding off. This sets a standard with considerable precision.

The Regulation's expressed hope that third countries will respect the principle of continuity of contracts elaborated in its text has already found a definite resonance in New York. On July 29, 1997 the New York legislature adopted a statute on Continuity of Contract which specifically provides that in all contracts subject to New York law which refer to a European national currency, or to the ECU, as a subject or medium of payment, the reference should be replaced by a reference to the euro, if the Member State of the currency is replacing its currency with the euro.\(^{297}\) Similar legislation is pending in California and Illinois, and may be adopted not only in other U.S. states, but also in foreign jurisdictions. The value of such legislation lies in the legal certainty thus provided to the principle of continuity of contracts in the jurisdiction adopting it; but there is a potential adverse effect if courts in other jurisdictions without such legislation are led to doubt the principle of continuity of contracts in the absence of a specific statute.\(^{298}\)

Thus, although not all issues have been completely resolved, the basic structural devices for the introduction of the euro as the new single currency for all participating Member States have been set as of the end of 1997. Once the ECB has taken office, the draft regulation on the introduction of the euro can be

\(^{296}\) Council Regulation EC 1103/97, art. 3.


\(^{298}\) For a careful analytic appraisal, see Michael Gruson, The Introduction of the Euro and Its Implications for Obligations Denominated in Currencies Replaced by the Euro, 21 Fordham Int'l L.J. 65 (1997).
adopted and, during the course of 1998, further accessory legislation and regulations can be put in place. On January 1, 1999, the euro can then become a reality.

CONCLUSION

We return to the question posed at the outset of the article: will EMU fly, or, more realistically, will EMU function well in operation, performing satisfactorily, although perhaps not at the high level of success some had aspired for it? At the present time, the end of 1997, the prognosis is favorable.

In order to provide perspective, this Article has traced the genesis and historical progression in the development of Economic and Monetary Union. Beginning with the somewhat prophetical Werner Report of 1970 and the pragmatic achievements of the present European Monetary System, in place since 1979, the Article has described the aspiration for monetary union, noting that the latest impetus has come naturally from the success of the internal market program, launched by the Commission White Paper in 1985.

Appropriate space has been devoted in Part IV to the attainment of free movement of capital in 1991, a long-sought goal, whose achievement is an essential pre-condition for monetary union. The unconditional nature of free movement of capital as set forth in the post-Maastricht EC Treaty Article 73, authoritatively interpreted in 1995 by the Court of Justice, provides assurance that this foundation stone for monetary union will not be undermined.

Due tribute has been paid to the seminal 1989 Delors Report, which set out both the essential features of economic and monetary union and the pragmatic three stage program for its attainment. This Article has naturally devoted in Part V considerable detail to the description of the Maastricht Treaty provisions on the progressive evolution of EMU through the three stages, and upon the structure, role and powers of the European System of Central Banks and the European Central Bank. Modeled directly upon the German Bundesbank, and indirectly upon the Federal Reserve system, the ECB is bound to become a powerful body within the Community structure, independent in its functioning, limited only by its obligation to provide reports and accounts of its actions and by a fairly elaborate system of judicial review.

The article's most important purpose is to provide in Part VI a critical review of certain constitutional and legal features of monetary union. Placing so many secondary features of the proposed EMU into the EC Treaty itself, with constitutional force and the inevitable difficulty in amendment, is quite questionable. Why the Treaty drafters believed that independence of the ECB and the national central banks is so critical has been reviewed, but not without query as to the merit of the total independence prescribed by the Treaty. Linked to this topic is the issue of democratic legitimacy. The Article presents the concern, shared with other commentators, that Parliament's proper role as the voice of the people has been neglected, and points particularly to the unfortunate omission of Parliamentary assent to the decision on which Member States qualify for EMU, and upon the designation of ECB executive board members. It
can only be hoped that Parliament will energetically and effectively undertake its role in surveillance of the ECB, and that the ECB will prove willing to cooperate loyally in this process.

In a Community under the rule of law, the importance of judicial review is capital. The Article discusses the diverse procedures by which the ECB may solicit the aid of the Court of Justice in protecting its prerogatives, and by which, conversely, the ECB can be called to account before the Court by Member States, Community institutions and private parties. "Turf battles" can be effectively resolved in this manner, and the Court may have to fix the parameters of ECB or national central bank independence, as well as those for the obligation of professional secrecy.

Finally, on a highly topical note, this Article discusses the motive for the Treaty's designation of price stability as the priority goal for the ECB. Despite the surface plausibility of giving price stability such priority, the Article queries whether it would not have been more advisable to set out several economic imperative interests as the ECB goal, on the Federal Reserve model, or to state a general economic welfare goal, as was done in The Netherlands. In view of the Amsterdam Treaty's new emphasis on high employment as a Treaty objective, the Article queries whether the ECB might not be able to make high employment a preeminent secondary consideration in setting its policies.

The process of qualification for entry into the third stage merited considerable attention in Part VII, which attempted to describe the complex convergence criteria set for the Member States, and the nuanced manner in which they might be ultimately assessed. The Article joins with current sentiment in estimating that eleven Member States will join the final stage in May 1998, all but Denmark, Greece, Sweden and the U.K. The opt out provisions for Denmark and the U.K. are indicated, along with the status of the Member States "with a derogation" that will (temporarily, we hope) not participate in the third stage. Finally, the article contends that there is great political value in having as many Member States as possible in EMU, and that the economic advantages in the more transparent and economically efficient market place achieved thereby will outweigh any possible disadvantages in lessened concern for price stability.

In the final two Parts, the article more summarily describes the progress made by the institutions with the aid of the EMI, and under the policy guidance of the European Council, since 1995. The specific timetable for further action is in place, since the December 1995 Madrid European Council. Key regulations have either been adopted or await adoption in 1998 to ensure a legal framework for the new single currency, the euro. Although the transition period from 1999 to 2002 will be difficult and very costly, the goal of a single currency is in sight.

This returns us to the first Part, and the anticipated benefits of EMU. No one can be sure whether the pot of gold at the end of the rainbow will be as large as initially hoped, but many economic benefits are certain. Member States have made astonishing progress in taming inflation and budget deficits and are unlikely to change course radically now. Economic growth is apt to be steadier and more certain. Central monetary guidance from the powerful ECB can only be an element of stability and assurance. The internal market's cap in the form
of transparent trans-border costs and prices and increased European-wide competition is certain to be attained. The euro may well become a serious competitor for the dollar on the international monetary stage.

In conclusion, and not least, EMU's political and psychological benefits will be enormous. Its success will mark a major step toward political unity. The popular recognition of a European identity will be radically augmented by the adoption of a common currency.

Of course, many questions remain open and many issues remain to be resolved before EMU will be complete and judged as a success. Will in fact, the "outs," the Member States not participating in the final stage of EMU in May 1998, be able to, or be willing to join relatively soon, or will the "two-tier" Europe persist, with pernicious political and economic effects? Will all the applicant states from central Europe be able to meet the economic standards required to join EMU, or will this prove to be a serious impediment for some of them? Will the system of economic surveillance and cooperation after EMU begins work smoothly, or will there prove to be an occasion for the operation of the dread sanction system? Will a successful EMU provide impetus for movement toward new Community endeavors, such as tax harmonization and agricultural policy reforms? Finally, will it advance significantly the political agenda in other aspects of the Union?

Only the passage of time can provide the answers, but it is certain that the Economic and Monetary Union will reshape the future of the European Union.