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**EMU Revisited
Are we Making a Constitution?
What Constitution are we Making?**

FRANCIS SNYDER

BADIA FIESOLANA, SAN DOMENICO (FI)

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European University Institute
Badia Fiesolana
I – 50016 San Domenico (FI)
Italy

EMU REVISITED :
ARE WE MAKING A CONSTITUTION?
WHAT CONSTITUTION ARE WE MAKING?

FRANCIS SNYDER

1. INTRODUCTION

(A) What Is At Stake in EMU

The European Union has an unfinished constitution. Since its inception European integration has been marked by discord about its objectives and, correspondingly, a lack of conceptual clarity in their legal expression. Now, however, it is also characterised by much greater politicisation, a more broadly based scepticism about (if not opposition to) its policies, and an increasing drift towards what is often described as a polycentric polity.

Economic and monetary union (EMU) in such circumstances involves high stakes, both for the European Union (EU) in particular and for European integration in general.¹ From a broad constitutional

¹ For their contributions to this article I wish to thank (in alphabetical order) Michael Artis, Vassil Breskovski, Stephen Clarkson, Emir Lawless, Massimo La Torre, Miguel Poiares Maduro, Raimond Marimon, Michael Morgalla, Candido Garcia Molyneux, Machteld Nijsten, Marcello Oviedo, Martin Schapiro, and Anne-Lise Strahtmann. Early drafts of different parts of the article were presented at the Annual Conference of the Association Internationale des Jeunes Avocats, Florence, Italy, 3 September 1997; the Conference on Compliance and Enforcement of European Community Law, University of Utrecht, Netherlands, 2-3 October, 1997; the Conference on 'European Law: The Basis for the Construction of the European Union', Institute of European Studies of Macau, Macau, 9 May 1998; Fudan University, Shanghai, 11 May 1998; Centre for European Studies, University of Wuhan, 15 May 1998; and Institute of European Studies, Chinese Academy of Social Sciences, Beijing, 19 May 1998. I am especially grateful to my respective hosts, Christopher Vajda Q.C., Professor John Vervaele, Dra. Maria do Ceu Esteves, Professor Dai Bingran, Professor Zeng Linliang, and Professor Qiu Yuanlan and Professor Zhou Rongyao, as to the participants on each occasion for discussion and comments. The article was completed during my stay at the Chinese Academy of Social Sciences (CASS), Beijing, as the first Robert Schuman Professor under the EU-China Higher Education Cooperation Programme. I wish to express my gratitude to the Programme and also to my hosts at the CASS, Professor Qiu Yuanlan (Director, Institute of European Studies), Professor Zhou Rongyao (Director, Centre for European Studies), and Dr Zhou Hong (Deputy Directive, Centre for European Studies). None of these people has read the final version of this article, so more than the usual disclaimer applies.

perspective,² these stakes are essentially three-fold. First, EMU is a test of some of the EU's basic constitutional principles, such as the single institutional framework, the division of powers, subsidiarity, and social cohesion.³ Second, its fate will be decisive with regard to certain constitutionalising processes, which help to determine whether a constitution in merely the material sense (*sens matériel*) can be transformed into a constitution also in the subjective sense; such processes include regional integration, legitimation and the creation of social solidarity. Third, EMU could be crucial in the development of a real EU legal and constitutional culture, one which extends beyond merely administrative, legal and political elites to embrace all EU citizens and even residents.

EMU, as I have argued elsewhere,⁴ is a metaphor for the European Union. It represents the culmination of a process set in train by the founding Treaties, consolidated in the Maastricht Treaty, and left virtually untouched by the Treaty of Amsterdam. The debate about EMU thus is a debate about the future of the EU as a polity, the European social model, and the nature of European identity. EMU was intended from the beginning to be (and may still be) a milestone in the history of European integration, anchoring the internal market, crystallising political integration, and establishing the EU as a major player in international financial markets. It may prove, however, to be a millstone around the neck of a fledgling, causing the young European Union to sink in the turbulent waters of deflation, enlargement, postmodern politics, and globalisation.

(B) Approach of The Article

The present article aims to contribute to this debate. Its approach, following the editors' guidelines, is to analyse EMU in the light of the gradual development of this area of the law over the course of the Community and Union's history. The article considers the relevant

² See F. Snyder, 'General Course on European Community Law: Constitutional Law of the European Union', in *Collected Courses of the Academy of European Law 1995* (Kluwer, 1998), 1-117.

³ Also relevant are the principle of an open market economy, convergence, and maintenance of the *acquis communautaire*: see Ernst-Jachim Mestmaecker, 'De la Communauté économique à l'Union économique et monétaire', (1995) 1 *Revue des Affaires Européennes* 111-121 at pp 111-112.

⁴ F. Snyder, 'EMU - Metaphor for European Union? Institutions, Rules and Types of Regulation', in R. Dehousse (ed.), *Europe after Maastricht: An Ever Closer Union?* (Law Books in Europe, 1994), 63-99.

political, economic and social forces which have shaped the creation and evolution of this body of law, and, where possible, the impact of that law on the EC, the EU and the Member States. Finally, it examines the interaction between the various institutional, doctrinal and other influences in the making, shaping and application of the law.

Such an approach in itself gives the lie to any simple notion of EMU as the result of gradual straightforward changes in legal doctrine or positive law, still less as the product of a legal, institutional and political process which was virtually predestined. Indeed, once we move away from any narrow conception of EMU in terms of so-called 'black letter' law, it becomes difficult to describe EMU in terms of evolution at all. Evolution is an extremely complex and highly controversial concept.⁵ In legal studies, and even in legal anthropology, evolutionary approaches have been few in number and of limited persuasiveness.⁶ Of more utility in respect of EMU might be Marx's genealogical method,⁷ or Vansina's conception of process-models,⁸ but such a deep historical methods, which are usually applied in the study of long-term historical changes, may be inappropriate here.

I wish, however, to retain three points which recourse to the notion of evolution might suggest. First, evolution refers to change over time. Certainly as applied to legal principles, processes and culture, it is inevitably contested and full of conflict. In few areas of EU law is this more true than with EMU. Second, the concept of evolution tends unfortunately to focus our attention on the winners. In studying society,

⁵ As to its complexity, see 'Evolution', *The New Encyclopaedia Britannica, Micropaedia*, Vol. 4, 623, and 'The Theory of Evolution', *The New Encyclopaedia Britannica, Macropaedia*, Vol. 18, 981-1011 (18th edition, 1974, reprinted 1985, Encyclopaedia Britannica, Inc.). As to its controversial character, see e.g. S..J. Gould, 'Darwinian Fundamentalism', (1997) XLIV *The New York Review of Books*(June 12) 34, and related correspondence. See also 'Biology isn't destiny', *The Economist*, February 14 1998, pp 97-99.

⁶ As to examples, see E.A. Hoebel, *The Law of Primitive Man* (Harvard University Press, 1954) and A.S. Diamond, *Primitive Law, Past and Present*(Methuen, 1971). For a useful correction, see S.F. Moore, 'Legal Liability and Evolutionary Interpretation: Some Aspects of Strict Liability, Self-Help and Collective Responsibility', in M. Gluckman (ed), *The Allocation of Responsibility* (Manchester University Press, 1972). For a recent critique, see La Torre, 'Rules, Institutions, Transformations: Considerations on the "Evolution of Law" Paradigm', (1997) 10 *Ratio Juris* 316.

⁷ See K. Marx, *Grundrisse: Introduction to the Critique of Political Economy*(trans. M. Nicolaus, 1973, Penguin Books Ltd.)

⁸ Jan Vansina, 'The Use of Process-Models in African History', in Jan Vansina, Raymond Mauny and L.V. Thomas (eds), *The Historian in Tropical Africa* (Studies presented and discussed at the Fourth International African Seminar at the University of Dakar, Senegal, 1961) (Oxford University Press for the International African Institute, 1964), pp 375-389.

however, including law in society, we must avoid reading history backwards and forgetting the losers. The outcomes of social change are rarely predetermined: EMU, in general or in its present form, was and is not inevitable. Third, evolution often involves path dependence and lock-in, such that the outcomes of past conflicts establishes patterns or sets the agenda for the future.⁹ EMU, despite its short history, is a prime example.

EMU has usually been treated from an economic or economic policy perspective. The former asks whether EMU makes economic-theoretical sense, while the latter focuses on the extent to which it is required for the optimal functioning of the internal market. Here I concentrate instead on the legal aspects of EMU as the complex result of a series of bargains and compromises, driven mainly though not continuously by particular interests, and set within the broader context of systemic changes in Europe and in the international political economy. This approach includes a European perspective, which considers EMU as one more step towards EU political integration. It also takes account of the perspective of national governments, which have often adopted a strategy of seeking to introduce by means of EU institutions, including EMU, economic policies which might be difficult to implement through national political institutions alone.

(C) Argument and Organisation

The main lines of the argument put forward here can be summarised as follows.

First, EMU was created mainly for political rather than economic reasons. In particular it was intended to be an essential, but not the only, part of European political integration.

Second, the overtly political aspects of EMU, designed to be a counterweight to its economic or financial aspects, were negotiated away during the compromise that led to the inclusion of EMU in the Maastricht Treaty. They included an increase in EC budget for redistributive purposes, the deployment of other economic policy instruments, and greater political accountability.

⁹ As to path dependence and lock-in generally, see Brian Arthur, *Increasing Returns and Path Dependence in the Economy* (University of Michigan Press, 1994). As to EC law in particular, see Pierson, 'The Path to European Integration: A Historical Institutional Analysis', (1996) 29 *Comparative Political Studies* 123.

Third, the institutional structure and substantive provisions of EMU, excluding the convergence criteria, which were agreed at the end of the Maastricht Intergovernmental Conference, were mainly the product of a small group of monetary experts. This group was characterised by substantial structural, organisational and even sometimes individual continuity, thus giving great weight to the economic and financial aspects of EMU.

Fourth, monetary institutions and monetary policy, especially before being put into practice,¹⁰ would not usually appear to raise great issues of political controversy and theory. The development of EMU has done so however because it crystallised conflicting views among Member States, organisations and individuals about the nature and purpose of European integration and because it occurred in a historically specific context. See from this perspective, EMU has served both as a stimulant and as a proxy for broader debates about decision-making concerning monetary policy, the future of European integration, and the meaning and effects of globalisation. Even though not always realised consciously or articulated in political terms, the links between globalisation and EMU raised profound questions about personal, national and European identities.

Fifth, these developments and controversies have had very specific implications for the unfinished EU constitution. EMU as a whole exemplifies a trend towards an increasing role of the European Council as a Janus-faced gatekeeper, an *approfondissement* of multi-level governance in the sense of greater interpenetration between EU and national political arenas, and greater institutional and normative heterogeneity in the making and implementation of important EU (and EC) policies.

Sixth, from a broader constitutional standpoint, two main points emerge. On the one hand, EMU has contributed perhaps more than any other policy to the emergence of politics in the EU, which now clearly

¹⁰ It seems clear, however, that public reaction in Europe and elsewhere to monetary policy, even before put into practice, is now influenced by widely known precedents of previous IMF deflationary policies. In the EMU context, this demonstrates once again the extent to which EU policies and political debates are influenced by the broader international context, particularly international institutions and international events, even though individuals might not always consciously or immediately recognise this to be the case. It is also true that EMU was not the only factor to stimulate political debate: see Panos Tsakaloyannis, "'The Acceleration of History" and the Reopening of the Political Debate in the European Community', (1991) 14 *Revue d'Intégration Européenne / Journal of European Integration* 103-102.

has the character of a non-state polity. On the other hand, the substantial growth and popular salience of the European Council can be described as a form of legitimation without democratisation, if by 'democracy' we mean participation in governance either via direct deliberation or by means of directly elected representatives as well as the fragmentation rather than the concentration of power. When viewed in the context of European integration and the development of the European Union, EMU thus is a high-risk political strategy. It is not immutable or irreversible, and if it fails, there is a risk that because EMU and the EU are now so intertwined, they both become unravelled.

The remainder of this article consists of three main parts. Part 2 deals with the construction of the legal framework of EMU. Part 3 discusses the relationship between politics, interests, and policies in this process. Part 4 considers certain controversial issues and legal problems. The conclusion summarises some of the constitutional implications.

2. A CHRONOLOGY OF THE LEGAL FRAMEWORK

The origins of European monetary integration predate the European Economic Community (EEC).¹¹ The European Payments Union came into operation in 1950.¹² An intergovernmental institution, it served as a clearing house, which provided for the multilateral settlement of payments and for short-term credit for balance of payments adjustments among participating states.

The assumption that national governments (now Member States) retained power over economic, cyclical and monetary policies also

¹¹ The following account draws especially on Daniel Gros and Niels Thygesen, *European Monetary Integration* (Longman, 1992); John Driffill and Massimo Beber (eds), *A Currency for Europe: Currency as an Element of Division or Union in Europe* (Lothian Foundation Press, 1991); Klaus Gretschnan, 'EMU: Thoughtful Wish or Wishful Thinking', in Klaus Gretschnan (ed), *Economic and Monetary Union: Implications for National Policy-Makers* (European Institute of Public Administration, 1993), pp 3-23; Peter B. Kenen, *Economic and Monetary Union in Europe: Moving beyond Maastricht* (Cambridge University Press, 1995); Glenda Goldstone Rosenthal, *The Men Behind the Decisions Cases in European Policy-Making* (Lexington Books, 1975) pp 26-30, 101-125; Loukas Tsoukalis, 'Economic and Monetary Union: The Primacy of High Politics', in Helen Wallace and William Wallace (eds), *Policy-Making in the European Union* (Oxford University Press, 3rd edition 1996), pp 279-299; and Horst Ungerer, *A Concise History of European Monetary Integration: From EPU to EMU* (Quorum Books, 1997). See also P. Welfens (ed), *European Monetary Integration* (Springer, 2nd edition 1994).

¹² Accord sur l'establissement d'une Union europeenne de paiements du 19 septembre 1950 (Organisation europeenne de cooperation economique, 1954)

underlay the 1957 Treaty of Rome, but the exercise of these powers was now subject to a new institutional framework and new legal obligations. Within the broad objectives assigned to the EEC by Article 2 EEC,¹³ Article 6(1) provided that 'Member States, acting in close collaboration with the institutions of the Community, shall coordinate their respective economic policies to the extent that it is necessary to attain the objectives of this Treaty ...' For this purpose, Member States were to regard their conjunctural policies and exchange rate policies as matters of common concern.¹⁴ The EEC was granted power to take certain limited action in each area.¹⁵ Each Member State, to quote the heady idealistic language of the Treaty, was '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.'¹⁶ To facilitate achievement of these aims, Member States were required to coordinate their economic policies and for this purpose to provide for cooperation between inter alia their central banks.¹⁷ A Monetary Committee with advisory status was established to promote coordination of monetary policies 'to the full extent needed for the functioning of the common market.'¹⁸

With regard to capital movements, the basic principle was that, during the transitional period and to the extent necessary to ensure the proper functioning of the common market, Member States were progressively to abolish between themselves all restrictions of movements of capital belonging to the persons resident in the Member States and any discrimination based on nationality or in the place of residence of the parties or on the place where the capital is invested.¹⁹ Current payments were to be liberalised by the end of the first stage at

¹³ In the words of Art. 2 EEC, 'It shall be the aim of the Community, by establishing a Common Market and progressively approximating the economic policies of the Member States, to promote throughout the Community a harmonious development of economic activities, a continuous and balanced expansion, an increased stability, an accelerated raising of the standard of living and closer relations between the Member States.'

¹⁴ See Art. 103(1) (conjunctural policies) and Art. 107(1) (exchange rate policies).

¹⁵ See Art. 103(2)-(4) and Art. 107(2).

¹⁶ Art. 104 EEC.

¹⁷ Art. 105(1), first paragraph, EEC. As to economic policy coordination, see Richard N. Cooper, 'Economic Interdependence and Coordination of Economic Policies', in R.W. Jones and P.B. Kenen (eds), *Handbook of International Economics*, vol. II (Elsevier Science Publishers, 1985), pp 1195-1234.

¹⁸ Art. 105(2). EEC.

¹⁹ Art. 67(1) EEC.

the latest.²⁰ These provisions were to be implemented progressively.²¹ As to capital movements involving third countries, Member States were progressively to coordinate their exchange rate policies, within the framework of Council directives, adopted unanimously and endeavouring to attain the highest possible degree of liberalisation.²² A standstill clause applied to new exchange restrictions.²³ Provision was made for safeguard measures in the event that capital movements led to disturbances in the functioning of the capital market in any Member States.²⁴ There was however no reference to any regional currency union, which in any event would have been wholly unrealistic.²⁵

Three further developments occurred soon after the EEC Treaty came into force. The European Investment Bank (EIB) was established in 1958 as an independent credit institution of the EEC with its seat in Luxembourg.²⁶ The following year, the European Monetary Agreement (EMA) replaced the EPU, which had ensured complete currency convertibility between most European states. The EMA provided a fund for coping with temporary balance of payments difficulties, and rules were laid down for the multilateral settlement of payments through the Basle-based Bank of International Settlements (BIS)²⁷ Then, in March 1960 the EEC Council issued a decision to improve coordination of Member States' short-term economic policies.²⁸

The early 1960s, the 'golden age of the Community', saw increased interest in European monetary integration, mainly as a response to international monetary instability and 'the perceived need (especially by

²⁰ Art. 67(2) EEC.

²¹ Art. 69 EEC.

²² Art. 70(1) EEC.

²³ Art. 71, first paragraph, EEC. The second paragraph of this Article provided that Member States declare their readiness to go beyond the degree of liberalisation of capital movements provided for in the preceding articles in so far as their economic situation, in particular the situation of their balance of payments, so permits.

²⁴ Art. 73(1) EEC.

²⁵ See Loukas Tsoukalis, 'Economic and Monetary Union: The Primacy of High Politics', in Helen Wallace and William Wallace (eds), *Policy-Making in the European Union* (Oxford University Press, 3rd edition 1996), pp 279-299 at p 281, who points out that the international monetary system was based on the gold standard, European countries were still concerned about a dollar shortage, and national governments followed firmly Keynesian policies.

²⁶ Treaty establishing the European Community, Protocol (No.A) On the Statute of the European Investment Bank.

²⁷ Accord monetaire europeen du 5 aout 1955 amende par les Protocoles additionales Nos. 2 et 3 et les Decision prises par l'Organisation europeenne de cooperation economique jusque' auler aout 1960 (OECE, 1960).

²⁸ EEC Council Decision of 9 March 1960 on Co-ordination of the Conjunctural Policies of the Member States, OJ 9.5.1960 L31/764.

the French) to insulate Europe from the vagaries of the U.S. dollar'.²⁹ In July 1960 the Council enacted the First Capital Directive, taking a modest step toward implementing Article 67 EC on free movement of capital.³⁰ In October 1962 the EEC Commission issued 'The Action Programme of the Community for the Second Stage', which included a chapter to economic policy and a chapter to monetary policy.³¹ It suggested that from end of the transition period, if not sooner, the Member States should move to a system of fixed exchange rates with a narrow band of variation, and also that by the end of a third stage a full monetary union could be envisaged. The Second Council Directive on the free movement of capital was adopted in December 1962.³²

In June of the following year the Commission recommended strengthening existing monetary cooperation in meetings of ministers of finance, the Monetary Committee and the Short-Term Economic Policy Committee. These recommendations were adopted in a series of decisions and declarations issued by the Council on 8 May 1964.³³ This provided for establishment of a committee of governors of the central banks, which subsequently became a central institution for coordinating monetary policy as well as credit and lending operations in the EEC. It also provided for the creation of a budgetary policy committee, composed of senior officials of the finance ministries of the Member States and of representations from the Commission. The Member States also agreed to consult each other before altering exchange rates in international monetary affairs and to hold discussions in the Monetary Committee before 'taking steps connected with the general working of the international monetary system, having recourse to funds available

²⁹ Loukas Tsoukalis, 'Economic and Monetary Union: The Primacy of High Politics', in Helen Wallace and William Wallace (eds), *Policy-Making in the European Union* (Oxford University Press, 3rd edition 1996), pp 279-299 at p 281.

³⁰ OJ 12.7.60 L921/60. As to amendments, see the Second Capital Directive *infra*. See also Council Directive 85/583, OJ 31.12.85 L372/39, and Council Directive 86/566, OJ 26.11.86 L332/22.

³¹ Memorandum de la Commission sur le programme d'action de la communauté pendant la deuxième étape, COM (62) 300, 24.10.1962, p.107.

³² Council Directive 63/21, OJ 22.1.63 L62/63.

³³ Council Decision of 8 May 1964 on Co-operation between Member States in the Field of International Monetary Relations, OJ 21.5.1964 L77/1207; Council Decision of 8 May 1964 on Co-operation between the Central Banks of the Member States of the EEC, OJ 21.5.1964 L77/1206; Council Decision of 8 May 1964 on Co-operation between the Competent Government Departments of Member States in the Field of Budgetary Policy, OJ 21.5.1964 L77/1205.

under international agreements or participating in large-scale support arrangements on behalf of nonmember countries' .³⁴

In September 1964 the Commission issued a policy statement entitled 'Initiative 1964' in the form of a memorandum to the Council and the Member States. With regard to monetary policy, it stated:

The Commission considers that the aims set out in its Action Programme of October 1962 have become even more pressing and that they should be examined in the light of experience. The interpenetration of markets which has meanwhile come about between the Member States makes progress in the field of monetary policy increasingly urgent.

The aim of the Community is not merely to expand trade between the Member States; it implies merging the six markets in a single internal market and the establishment of an economic union. It therefore appears indispensable to adapt the monetary policy of the Six to the degree of integration already attained in other fields.

The Commission will submit without delay to the Council proposals for the progressive introduction of a monetary union.³⁵

These ambitious schemes were elaborated by the Commission, which linked an increase in its own political fortunes to that of the Community. They remained, however, mainly on paper. The principal practical measures to be adopted were the EEC's first medium-term economic policy programme in 1967³⁶ and a second such programme in 1968.³⁷ Both of these initiatives were powered by the Commission in conjunction with expert committees, without requiring the Council to adopt measures with a higher political profile and more direct political implications.

The late 1960s was a period of political, economic and monetary instability. This put paid to any ambitious proposals for European monetary integration, even if they had been on the political agenda of more Member States at the time. But, even in the aftermath of the Luxembourg Accords, it also facilitated more limited Commission

³⁴ Glenda Goldstone Rosenthal, *The Men behind the Decisions* (Lexington Books, 1975), p 27.

³⁵ European Economic Community, Official Spokesman of the Commission, Information Memo P-59/64 (Brussels, October 1964), pp 4-5

³⁶ JO 25.4.1967 79/1513.

³⁷ JO 30.5.1969 L129/1.

initiatives which were designed to foster greater coordination in economic and monetary matters. Though unsuccessful in the short-term, these initiatives set the agenda for the future: they aired the issues, established the terms of debate, and provided points of orientation for subsequent developments.

On 5 December 1968 the Commission submitted to the Council a memo 'on appropriate policy in the Community on current economic and monetary problems', announcing that before 15 February 1969 it would propose the creation of new means of monetary cooperation. The Council at its meeting of 12 December 1968 reached broad agreement on the need for greater convergence of economic policies and for intensifying monetary cooperation.³⁸ The result was the Commission memorandum known as the 'Barre Plan', named after the then Vice-President of the Commission Raymond Barre.³⁹ It contained three recommendations: closer coordination of short-term economic policies, convergence of national medium-term economic policy orientations, and establishment of Community machinery for monetary cooperation through short-term arrangements for monetary support and possibilities for medium-term financial assistance

The Barre Plan was highly contested, and its principal concrete result was a Council Decision on the coordination of Member States' short-term economic policies.⁴⁰ With an eye on subsequent developments, however, one can say that this debate generated four crucial points of lasting significance.⁴¹

First, this was the first manifestation of the split between 'economists' and 'monetarists'. The former group, in particular Germany, wanted economic union first: in their view, economic convergence was a precondition for monetary integration. The latter, in particular France, wanted monetary union first: they saw the introduction of a common monetary policy as a means of fostering convergence among the Member States' diverse national economies.

³⁸ European Coal and Steel Community, European Economic Community, European Atomic Energy Community, *Second General Report on the Activities of the Community 1968* (Brussels-Luxembourg, February 1969), p 111.

³⁹ ECSC-EEC-EAEC, Secretariat General of the Commission, 'Commission Memorandum to the Council on the Co-ordination of Economic Policies and Monetary Co-operation within the Community' (Supplement to *Bulletin of the European Communities*, No. 3-1969) (Brussels, Publishing Services of the European Communities, 1969).

⁴⁰ JO 25.7.1969 L183/41.

⁴¹ See Glenda Goldstone Rosenthal, *The Men Behind the Decisions: Cases in European Policy-Making* (Lexington Books, 1975), pp 102-105.

Second, the support for and opposition to the Barre Plan reflected national governments' views not only of the priority of economic policy or monetary policy but also of the future shape of an eventual EEC polity. Thus Germany, Italy, and Belgium supported the Barre Plan in part because the coordination of economic policy seemed eventually to presage greater political integration.⁴² France, Luxembourg and the Netherlands opposed it, in part because, in the words of then French Minister of Defence Michel Debré, 'There is no such thing as monetary Europe....Europe is either political and has a currency or it does not exist and has no currency'.⁴³

Third, the Barre Plan debate revealed both the limits of EEC competence and also the fact that the domain of economic and monetary policy was already characterised by a unusual degree of multi-level governance. For example, Coreper lacked the competence to discuss all aspects of the Barre Plan. Some aspects fell within the competence of the Member States, notably within the powers of national central banks or national budgetary authorities. Other aspects were traditionally dealt with by international monetary bodies. The EEC response was to encourage the creation of networks linking specialised committees.

Fourth, and also presaging future developments (at least if we read history backwards), it should also be noted that the eventual agreement in July 1968 agreement on the Council decision was subject to numerous hesitations and much reservation. It was considered to be the lesser of two evils, and its adoption was facilitated by the fact that 'none of the proposed mechanisms was to enter into effect without implementing legislation'.⁴⁴ These well-known features of Community decision-making have also characterised recent debates about EMU.⁴⁵

⁴² As to the German ordo-liberal view of the role of EMU in the EEC economic constitution, see Manfred E. Streit and Werner Mussler, 'The Economic Constitution of the European Community: From 'Rome' to 'Maastricht'' (1995) 1 *European Law Journal* 5-30.

⁴³ Commission of the European Communities, *Monthly Bulletin*, 1071, no. 3, p. 97, quoted in Glenda Goldstone Rosenthal, *The Men Behind the Decisions: Cases in European Policy-Making* (Lexington Books, 1975), p. 103, who also remarks various differences of opinion within each of the two groups. It is also striking that to note the expression at European level of national political differences, here between Debré and Barre, as well as the inclusion within the single 'economists' group of both Germany and Italy, nowadays considered to represent extreme differences of opinion with regard to EMU.

⁴⁴ Glenda Goldstone Rosenthal, *The Men Behind the Decisions: Cases in European Policy-Making* (Lexington Books, 1975), p. 106.

⁴⁵ Schneider and Cederman identify the well-known pattern according to which all governments prefer some increase in integration but disagree about the extent of integration: Gerald Schneider and Lars-Erik Cederman, 'The Change of Tide in

In its Final Communiqué of The Hague Summit on 2 December of that year, the Heads of State and Government, then not yet known as the European Council, stated their agreement 'within the Council, on the basis of the memorandum presented by the Commission on 12 February 1969, and in close collaboration with the Commission, a plan in stages should be worked out during 1970 with a view to the creation of an economic and monetary union.' They also stated that the 'development of monetary co-operation should be backed up by the harmonisation of economic policies'.⁴⁶ It was thus in 1969 that the target of a complete EMU was adopted for the first time. This was 'a political decision at the highest level, and it was directly linked to the first enlargement of the Community and the further deepening of integration.'⁴⁷

While agreeing on the principle of monetary unification, the six Member States disagreed however regarding the means. The basic split, already evidenced, was between monetarists and economists. In retrospect it is worth noting that both the economists and many if not most of the monetarists favoured a transfer of fiscal and hence political powers to the centre, though they differed in the strength of their preferences and in their view of the timing.⁴⁸ The basic conflict that emerged thus had two main dimensions: first, whether economic convergence should precede or result from monetary convergence; and, second, whether concomitantly a supranational organ should be created or not. On the whole, the monetarists said no to both questions, while the economists answered both in the affirmative.⁴⁹

Political Cooperation: A Limited Information Model of European Integration', (1994) 48 *International Organization* 633-663.

⁴⁶ European Coal and Steel Community, European Economic Community, European Atomic Energy Community, *Third General Report on the Activities of the Community 1969* (Brussels-Luxembourg, Publishing Services of the European Communities, 1970), p 50.

⁴⁷ Loukas Tsoukalis, 'Economic and Monetary Union: The Primacy of High Politics', in Helen Wallace and William Wallace (eds), *Policy-Making in the European Union* (Oxford University Press, 3rd edition 1996), pp 279-299 at p 281.

⁴⁸ See Charles A.E. Goodhart, 'The Political Economy of Monetary Union', in Peter B. Kenen (Ed),: *Understanding Interdependence: The Macroeconomics of the Open* (Princeton University Press, 1995), pp 448-505 at p 475; who gives as examples of the latter group Daniel Gros and Niels Thygesen, *European Monetary Integration: From the European Monetary System to European Monetary Union* (Longman, 1992); and Lorenzo Bini-Smaghi, Tommaso Padoa-Schioppa, and Francesco Papadia, 'The Policy History of the Maastricht Treaty: The Transition to the Final Stage of EMU', in Guillermo de la Dehesa, Alberto Giovannini, Manuel Guitian and Richard Portes (eds), (Centre for Economic Policy Research, 1993)

⁴⁹ See Francesco Giavazzi and Alberto Giovannini, *Limiting Exchange Rate Flexibility: The European Monetary System* (MIT Press, 1989), p 25; Glenda Goldstone Rosenthal, *The Men Behind the Decisions* (Lexington Books, 1975), pp 102-112. The

Specific normative results followed. In January 1970 the Council passed a resolution in favour of establishing an economic and monetary union in the Community.⁵⁰ The following month, at the quarterly meeting of finance ministers, Germany, Belgium and Luxembourg submitted 'fairly detailed plans' for EMU, though the meeting made clear that 'the major issue was whether to provide monetary support for member states whose currencies experienced difficulties or whether to integrate members' economies so that currency problems would not arise'.⁵¹ At its 6 March 1970 meeting the Council decided to set up a committee under the chairmanship of Pierre Werner, the Prime Minister and Finance Minister of Luxembourg, to draw up a report 'comprising an analysis of the various suggestions and enabling the fundamental choices to be made for a phased establishment of the economic and monetary union of the Community'.⁵²

The Werner Committee consisted of six other members in addition to its chairman: the five chairs of the so-called 'special committees', namely the Committee of Governors of Central Banks, the Monetary Committee, the Budget Policy Committee, the Short-Term Economic Policy Committee, and the Medium-Term Economic Policy Committee, together with a representative of the Commission.⁵³ It submitted an interim report in May 1970 and a final report to the Commission and the Council in October 1970.⁵⁴ It proposed the achievement of a full-fledged EMU by the end of the 1970s. This was to include complete liberalisation of intra-EEC capital movements, irrevocable convertibility of currencies, irrevocably fixed exchange rates, pooling of monetary reserves, and the control of monetary policy by a single European institution. It adopted many of the principles set down in the Commission's March Memorandum. With regard to a European-level fiscal function, it was more ambitious than the subsequent Delors Report.⁵⁵

monetarists included France and Belgium, while among the economists were Germany, the Netherlands and also Italy, at least its then Minister of Finance Emilio Colombo.

⁵⁰ Bull EC, I-1970, pp. 11-16.

⁵¹ Glenda Goldstone Rosenthal, *The Men Behind the Decisions*(Lexington Books, 1975), p 107.

⁵² ECSC-EEC-EAEC, Secretariat General of the Commission, *Bulletin of the European Communities*, No. 5-1970, (Brussels, Publishing Services of the European Communities, 1970), p 50.

⁵³ See *Europe Bulletin*, April 21 1969.

⁵⁴ Rapport au Conseil at à la Commission concernant la réalisation par étapes de l'union économique et monétaire dans la Communauté, JO 11.11.197, C 136/1.

⁵⁵ Compare Council 1970 and Delors Committee 1989. See also Daniel Gros and Niels Thygesen, *European Monetary Integration*(Longman,1992), chapter 1.

These proposals provoked debate and opposition, which was not surprising given the strong differences of views among Member States and the international monetary turbulence at the time. Moreover, this debate took place almost entirely among governments and experts, not as in the case of the Maastricht Treaty among the broader public, which was not really informed and remained virtually unaware of the issues at stake. Among governments, the proposal to create a European stabilisation fund by the end of the first stage of EMU was opposed particularly by Germany, which feared that Bundesbank reserves would be used to support weak currencies, such as (then) the French franc.⁵⁶ In the light of this reaction, the Commission softened the supranational aspects of the proposals and proposed a Council decision on the strengthening of the coordination of Member States' short-term economic policies and a draft Council decision on increased cooperation between the central banks.⁵⁷ Nevertheless, the basic dichotomy between two views of EMU and indeed of European integration itself remained as sharp as before. Indeed, 'government representatives ... stood by their national positions until the very last moment. Only when they were able to work out a formula that left the substantive issues so vague or so flexible as to be almost meaningless were they able to reach agreement.'

⁵⁸

These differences informed the Resolution adopted on 9 February 1971 by the Council and the Representatives of the Member States to the effect that:

'In order to assure satisfactory growth, full employment and internal stability of the Community; in order to remedy structural and regional imbalances in evidence; in order to strengthen the contribution of the Community to international economic and monetary cooperation and thus to arrive at a stable and growing Community, the Council and the representatives of the member states express their political will to establish over the next ten years an economic and monetary union according to a plan by stages, beginning January 1, 1971'.⁵⁹

⁵⁶ Glenda Goldstone Rosenthal, *The Men Behind the Decisions*(Lexington Books, 1975), p 108.

⁵⁷ JO 26.11.1970 C 240/20-26.

⁵⁸ Glenda Goldstone Rosenthal, *The Men Behind the Decisions*(Lexington Books, 1975), p 112.

⁵⁹ OJ 27.3.1971 C28/1; also in *Compendium of Community Monetary Texts*(1989), p. 33.

This Resolution set a series of objectives for the attainment of EMU by stages. They included the complete and irreversible convertibility of currencies, the elimination of fluctuation margins, and the establishment of parity, all seen as prerequisites for a single currency, together with the creation of a Community organisation of central banks. Though linking EMU with the completion of the internal market, the Resolution was without any legal force. This was not however the primary determinant of its short-run inefficacy, which was mainly due instead to disagreements among Member States, domestic policy interests, and the international context.

The summer of 1971 saw the collapse of the fixed exchange rate system. After some months of floating currencies, the Council and the representatives of the Member States in March 1972 adopted a further Resolution,⁶⁰ which, in addition to marking an agreement to create a Regional Development Fund, established the European 'currency snake'. This restricted the fluctuation margins of EEC currencies in respect of each other to 4.5%, with the central banks agreeing to intervene in the money market to ensure this objective. It proved ineffective, however, and the collapse of Bretton Woods led to the collapse of the European fixed exchange rate system.

'Fixed exchange rates, with narrow margins of fluctuation, which had been seen as the most concrete manifestation of the first stage of EMU, proved incompatible with increasingly divergent economic policies and inflation rates. Thus, political commitments, taken at the very top and usually not translated into the appropriate economic policies, finally gave way under market pressure.'⁶¹

But with floating exchange rates after 1973, the 'snake' enforced what was known as 'bloc floating'.⁶² In March 1973 the Council decided not to intervene with regard to the dollar and leave the snake as a joint float.⁶³ In fact, this was a German bloc, in which the Deutschmark served as

⁶⁰ JO 18.4.1972 C38/3; *Compendium of Community Monetary Texts*(1974), p. 30.

⁶¹ Loukas Tsoukalis, 'Economic and Monetary Union: The Primacy of High Politics', in Helen Wallace and William Wallace (eds), *Policy-Making in the European Union* (Oxford University Press, 3rd edition 1996), pp 279-299 at p 282.

⁶² Klaus Gretschnan, 'EMU: Thoughtful Wish or Wishful Thinking', in Klaus Gretschnan (ed), *Economic and Monetary Union: Implications for National Policy-Makers* (European Institute of Public Administration, 1993), pp 3-23 at pp 10-12.

⁶³ Council Statement, 12 March 1973, in *Compendium of Community Monetary Texts* (1974) 63. On the snake, see P. Coffey, *The European Monetary System: Past, Present and Future* (2nd ed. 1987).

anchor for the currencies of smaller EEC countries.⁶⁴ This, as Tsoukalis remarks, 'was the first concrete manifestation of the growing importance of Germany in the Community and Europe more generally.'⁶⁵

From the legal standpoint, two further significant developments occurred prior to the creation of the European Monetary System. The first, a compromise in the continuing debate between economists and monetarists, and foreshadowing more contemporary legal developments, was the enactment in 1974 of the Convergence Decision and the Stability Directive. Both measures expressed conceptions of the prerequisites for further monetary integration, but the former called for a high degree of economic convergence among Member States, while the latter was oriented towards achieving the highest possible degree of stability, full employment and growth. The legal forms in which these differing views were expressed were symbolic. Not only was a smaller margin of manoeuvre recognised as belonging to Member States in respect of economic convergence than in respect of monetary stability and employment policy, in the last of which Member States retained full legal powers. In addition, the very choice of these particular legal acts to encapsulate particular policy *desiderata* reflected the increasing German predominance in matters concerning EMU.⁶⁶

The second development was the creation in 1975 of the European Unit of Account (EUA) and its adoption as the accounting unit, first for European Development Fund and then for the European Investment Bank and the Community budget. Subsequently, in the framework of the EMS it was renamed the European Currency Unit (ECU). The EUA was a basket currency.⁶⁷ Initially it was seen only as a political symbol

⁶⁴ 'The fundamental problem was that there was no independent criterion of value, and by the time the snake was replaced by the European Monetary System it had in effect become a small DM zone': John A. Usher, *The Law of Money and Financial Services in the European Community* (Clarendon Press, 1994), p:138.

⁶⁵ Loukas Tsoukalis, 'Economic and Monetary Union: The Primacy of High Politics', in Helen Wallace and William Wallace (eds), *Policy-Making in the European Union* (Oxford University Press, 3rd edition 1996), pp 279-299 at p 282.

⁶⁶ By 1978 only German, Netherlands, Luxembourg, Belgium and the associated country of Norway remained in the Deutschmark bloc from the original nine members of the 'snake'. The others had dropped out because, 'due to progressive inflation, they were unable to keep their currencies within the snake's margin of fluctuation': (Klaus Gretschman, 'EMU: Thoughtful Wish or Wishful Thinking', in Klaus Gretschmann (ed), *Economic and Monetary Union: Implications for National Policy-Makers* (European Institute of Public Administration, 1993), pp 3-23 at p 11.

⁶⁷ As to which, see below regarding the ECU.

for European integration, but it was to play an important role in bond markets and as a major exchange reserve in the 1980s.⁶⁸

In 1979, the European Monetary System (EMS) was established on the initiative of French President Giscard d'Estaing and German Chancellor Helmut Schmidt. Monetary integration thus was again meant to play a key role in European integration, though the specific implications for national governments and banking institutions differed from country to country and, in the event, the United Kingdom did not join.⁶⁹ The EMS was based on a non-legally-binding instrument, the Resolution of the European Council of 5 December 1978⁷⁰, which lay down the structure of the EMS. Operating procedures were set down in another non-legally-binding instrument, an Agreement between the Central Banks of the Member States of 13 March 1979.⁷¹

In addition to its political rather than legal nature, the Council Resolution on which the EMS was based had another distinctive feature. Instead of creating a comprehensive set of obligations which applied to all Member States, the Resolution left it to each Member State to decide whether or not to join the EMS.⁷² As John Usher has stated, 'in a sense it is an agreement between all the Member States that those who so wish will be bound by the rules and make use of institutions created under Community law'.⁷³ Consequently, it can be seen as a forerunner, if not a precedent, for later forms of differentiation within the Community system, including the Social Protocol under the Maastricht Treaty, the

⁶⁸ For a strong argument about the international reserve role of the ECU, see Ralph J Mehnert, 'The European Currency Unit and Its Use in Developing Countries to Solve Foreign Exchange Related Problems: The Case of the People's Republic of China', (1989) 7 *International Tax and Business Lawyer* 301-352.

⁶⁹ Loukas Tsoukalis, 'Economic and Monetary Union: The Primacy of High Politics', in Helen Wallace and William Wallace (eds), *Policy-Making in the European Union* (Oxford University Press, 3rd edition 1996), pp 279-299 at p 283.

⁷⁰ *EC Bulletin* 1978 No. 12 point 1.1.11. John A. Usher, *The Law of Money and Financial Services in the European Community* (Clarendon Press, 1994), pp 139-142 states that any doubts about the legal basis of the EMS were largely resolved by the insertion of Article 102A EC by means of the Single European Act, the judgement of the European Court of Justice in Opinion 1/91, Opinion delivered pursuant to the Second subparagraph of Article 208(1) of the Treaty. Draft Agreement between the Community on the one hand and the countries of EFTA on the other, relating to the creation of European Economic Area, 1991 ECR I-6079 to the effect that EMU was a Community objective even before the TEU; and also by the express reference to the EMS in Art. 109J EC regarding the convergence criteria.

⁷¹ A revised version may be found in *Compendium of Community Monetary Texts* (1989), at 50.

⁷² See art. 3 of the 1978 Resolution.

⁷³ John A. Usher, *The Law of Money and Financial Services in the European Community* (Clarendon Press, 1994), p 141.

special treatment of the United Kingdom and Denmark in respect of monetary policy, and enhanced cooperation under the Amsterdam Treaty.⁷⁴

The EMS centred on the ECU (the renamed European unit of account). The ECU was a basket currency, consisting of fixed amounts of each EC currency.⁷⁵ Each EC currency had a central rate defined in terms of the ECU. The central rates were used to establish a grid of bilateral exchange rates, with 2.25 per cent margin fluctuations around those bilateral rates, except for the Italian lira and the Irish punt which began with fluctuation margins of 6 per cent and for the pound sterling which initially stayed out of the EMS. Central bank interventions were compulsory and unlimited when currencies reached their permitted margins of fluctuation. Central rates could be changed by common consent. Provision was made for large credit facilities to permit intervention in EC currencies.⁷⁶

The EMS also included a divergence indicator, which was meant to guarantee a certain symmetry in the burden of adjustment between strong and weak currencies. 'In simple words, the introduction of the divergence indicator implied that average behaviour should constitute good behaviour, although this did not square well with another implicit feature of the EMS agreement, namely a more general alignment to German's anti-inflation strategy. The contradiction was soon to become apparent, and the result was that the divergence indicator was never put into effect.'⁷⁷ Nevertheless, a September 1987 agreement provided for the increased use of intramarginal intervention.⁷⁸

With seven realignments between 1979 and spring 1983, the EMS gradually established the practice that realignments were to be common rather than unilateral decisions. The Basle-Nyborg Agreement of

⁷⁴ See Usher, *ibid.*; and Tuytschaever, draft PhD thesis, chapter 2?.

⁷⁵ The first ECU bond was issued in 1981 by the Italian telecommunications company, Stet.

⁷⁶ This summary is based on Loukas Tsoukalis, 'Economic and Monetary Union: The Primacy of High Politics', in Helen Wallace and William Wallace (eds), *Policy-Making in the European Union* (Oxford University Press, 3rd edition 1996), pp 279-299 at p 283.

⁷⁷ Loukas Tsoukalis, 'Economic and Monetary Union: The Primacy of High Politics', in Helen Wallace and William Wallace (eds), *Policy-Making in the European Union* (Oxford University Press, 3rd edition 1996), pp 279-299 at p283.

⁷⁸ See John A. Usher, *The Law of Money and Financial Services in the European Community* (Clarendon Press, 1994), p 144, citing *EC Bulletin* 1987 No. 9 point 1.3.5. As to medium-term financial assistance within the EMS, see Usher, *ibid.*, 1994 at 145-146.

September 1987 consecrated an agreement of the Central Bank Governors, as approved by an informal meeting of Ecofin, regarding movements within the band, management of interest-rate differentials, and intervention as instruments to be used, in that order, to guard against monetary instability. Between 1987 and 1992 there was a strong preference against realignments, as participants sought to maintain their ERM parities against the Deutschmark. To the extent that this restricted the use of interest rates as an instrument of independent monetary policy, the discretion of ERM participants thus was increasing limited.⁷⁹

This discretion was strongly restricted also by the adoption by the Council in mid-1988 of the Third Capital Directive.⁸⁰ It required Member States to abolish restrictions on movement of capital between persons resident in Member States.⁸¹ Where short-term capital movements of exceptional magnitude imposed severe strains on foreign-exchange markets and led to serious disturbances in the conduct of monetary and exchange rate policies, however, the Commission, after consulting the Monetary Committee and the Committee of Governors of the Central Banks, could authorise a Member State to take protective measures in respect of certain listed capital movements.⁸² In cases of urgency, the Member State concerned was entitled to take any necessary protective measures, subject to informing other Member States and the Commission. After consulting the Monetary Committee and the Committee of Governors, the Commission was to decide whether the Member State could continue to apply the measures or should abolish them.⁸³

Taken together, ERM and the Third Capital Directive resulted in a very substantial reduction of national governments' room for manoeuvre in matters of monetary policy. This can be illuminated by referring to

⁷⁹ This paragraph is based primarily on Klaus Gretschman, 'EMU: Thoughtful Wish or Wishful Thinking', in Klaus Gretschmann (ed), *Economic and Monetary Union: Implications for National Policy-Makers* (European Institute of Public Administration, 1993), pp 3-23 at pp 11-12; and Charles A.E. Goodhart, 'The Political Economy of Monetary Union', in Peter B. Kenen (Ed),: *Understanding Interdependence: The Macroeconomics of the Open* (Princeton University Press, 1995), at 458.

⁸⁰ Council Directive 88/361, OJ 8.7.88 L178/5.

⁸¹ *Ibid.*, art. 1(1), which also provided for the classification of capital movements in accordance with the nomenclature in Annex I.

⁸² *Ibid.*, art. 3(1), which also provided that the listed capital movements were those in Annex II.

⁸³ *Ibid.*, art. 3(2).

what economists often call the 'impossibility theorem', the 'impossible trilogy' or the 'unholy trinity'. This holds that

'the following three things are in principle incompatible: fixed exchange rates among a set of national currencies; independent monetary policies in the countries concerned; and full mobility of capital between one and another of the countries. ... Eventually one of the three things will have to give way - the exchange rate, the difference in policy, or the freedom of capital movements.'⁸⁴

By the Third Capital Directive, the EC Member States (with limited exceptions) lost control over capital movements. By tying their interest rates to that of the Bundesbank, the participants in ERM in effect lost control of exchange rate policy. In fact, as Goodhart points out, 'It is arguable that, having accepted ERM membership in this context, governments had already abandoned discretionary monetary policy'.⁸⁵ As will be seen later, EMU will remove national governments' control over exchange rates and further constrict their control over interest rates, though the latter is a process which in practice has already largely occurred.⁸⁶

In January 1988 Edouard Balladur, then French Finance Minister, proposed the creation of a single currency and a European Central Bank to control EC monetary policy. Similar proposals were made in February 1988 by the Italian Treasury Minister, Giuliano Amato,, who gave rather more emphasis to the deflationary bias of the EMS.⁸⁷ These events were informed by the 1985 Commission White Paper

⁸⁴ John Grahl and Paul Teague, *1992 - The Big Market: The Future of the European Community* (Lawrence and Wishart, 1990) ('impossibility theorem'), p 129; see also Paul Riché and Charles Wyplosz, (Editions du Seuil, 1993), p 34 ('impossible trilogy'); Benjamin J. Cohen, 'Phoenix Risen: The Resurrection of Global Finance', (1996) 48 *World Politics* 268-296 at p 280, and Benjamin J. Cohen, 'The Triad the the Unholy Trinity: Lessons for the Pacific Region', in Richard Higgott, Richard Leaver and John Ravenhill (eds), *Pacific Economic Relations in the 1990s: Cooperation or Conflict?* (Lynne Rienner, 1993) ('unholy trinity'). See also the 'inconsistent quartet', including free trade: Tommaso Padoa-Schioppa, 'The European Monetary System: A Long-Term View', in Francesco Giaavaszzi, Stefano Micossi, and Marcus Miller (eds), *The European Monetary System*(Cambridge University Press, 1988).

⁸⁵ Charles A.E. Goodhart, 'The Political Economy of Monetary Union', in Peter B. Kenen (Ed),: *Understanding Interdependence: The Macroeconomics of the Open* (Princeton University Press, 1995), at 458

⁸⁶ 'The Emu core group already has virtually fixed interest rates and virtually identical interest rates. For them, EMU has already started': Wolfgang Munchau, 'Big stride towards EMU', *Financial Times*, Weekend 11-12 October 1997, p 6.

⁸⁷ See Horst Ungerer, *A Concise History of European Monetary Integration: From EPU*

on completing the internal market by 1992, including financial markets.⁸⁸

Such developments also drew legal inspiration from the newly introduced Article 102A EC stemming from the 1986 Single European Act. Article 102a EC was the sole article in a new Treaty Chapter entitled Cooperation in Economic and Monetary Policy (Economic and Monetary Union).⁸⁹ It provided that Member States were to cooperate in order to ensure the convergence of economic and monetary policies necessary for the further development of the Community, taking account of the experience with the EMS and with the ECU.⁹⁰ It also stated that an amendment of the Treaty would be required if further development in the field of economic and monetary policy necessitated institutional changes, in which case the Monetary Committee and the Committee of Governors of the Central Banks should also be consulted as regards monetary policy.⁹¹

In June 1988 the European Council met in Hanover to discuss proposals for establishing monetary union. It agreed to the creation of a committee to study and propose concrete stages leading towards monetary union. Chaired by Jacques Delors, then President of the Commission, the committee consisted also of another member of the Commission (Frans Andriessen), the twelve Governors of the national central banks and three personalities designated by common accord by the Heads of State or Government. This last group included Niels Thygesen, Professor of Economics in Copenhagen; Alexandre Lamfalussy, then General Manager of the Bank for International Settlements in Basle and Professor of Monetary Economics at the Catholic University of Louvain-la-Neuve; and Miguel Boyer, President of

to *EMU* (Quorum Books, Westport and London, 1997), pp 191-192.

⁸⁸ Commission of the European Communities, *Completing the Internal Market: White Paper from the Commission to the European Council* (Office of the Official Publications of the EC, 1985). As to the relationship between monetary integration and the internal market, see Heidemarie Sherman, Richard Brown, Pierre Jacquet, and DeAnne Julius (eds), *Monetary Implications of the 1992 Process* (Pinter Publishers, London, 1990). Already the previous year Belgium had issued the first legal-tender ECU coin, minted to celebrate the Community's 30th anniversary.

⁸⁹ As inserted in Title II of Part Three of the Treaty by Article 20 SEA.

⁹⁰ Art. 102a (1) EC, as inserted by the SEA.

⁹¹ Art. 102a(2) EC, as inserted by the SEA. As to the subsequent interpretation of this Article, in particular regarding the establishment of a European Reserve Fund, see Committee for the Study of Economic and Monetary Union (The Delors Committee), *Report on Economic and Monetary Union in the Community* (1989), pp32-33 (paragraphs 53-54); see also John A. Usher, *The Law of Money and Financial Services in the European Community* (Clarendon Press, 1994), pp 148-149.

the Banco Exterior de Espana.⁹² Delors chose two rapporteurs: Gunter Baer, a high official in the Bundesbank, and Tommaso Padoa-Schioppa from the Banca d'Italia, and previously rapporteur of the so-called Padoa-Schioppa Report.⁹³

The Delors Committee Report, presented in 1989, was of fundamental importance in determining much but not all of the shape of EMU. It envisaged EMU as a process consisting of three stages, involving closer coordination of economic and monetary policies of EC Member States, the establishment of European Central Bank, and the replacement of national currencies by single European currency.⁹⁴ As its proposals regarding monetary policy are so well-known, and in any event will be dealt with later in so far as they were incorporated into the Maastricht Treaty, the following paragraphs focus on certain aspects of the Delors Report which raise issues that proved subsequently to be extremely controversial.

First, with regard to relations between the EC and the Member States, the Delors Report did not articulate the argument that EMU required or would inevitably entail political union. It did however assert the need for a transfer of decision-making power from the Member States to the Community, primarily in the fields of monetary policy and macroeconomic management. This would entail a single decision-making body in respect of monetary policy and an agreed macroeconomic framework and legally binding procedures and rules in respect of economic policy. Though the two policy areas constituted a single whole, an essential element in defining how they were to be managed was to be the principle of subsidiarity.⁹⁵ Nevertheless, in respect of international monetary cooperation the Delors Report foresaw that 'the Community would assume its full role ..., and a new form of representation in arrangements for international policy coordination and in international monetary negotiations would be adopted'.⁹⁶

⁹² Committee for the Study of Economic and Monetary Union (The Delors Committee), *Report on Economic and Monetary Union in the Community*(1989), Annex I, p 39.

⁹³ Tommaso Padoa-Schioppa (ed), *Efficiency, stability, equity: a strategy for the evolution of the Economic System of the European Communities*(Commission of the European Communities, 1987).

⁹⁴ Among many sources, see Louis, 'A Monetary Union for Tomorrow?', (1989) ... *Common Market Law Review*301; F. Snyder, 'EMU - Metaphor for European Union? Institutions, Rules and Types of Regulation', in R. Dehousse (ed)., *Europe after Maastricht: An Ever Closer Union?*(Law Books in Europe, 1994).

⁹⁵ *Ibid.*, p 14 (paragraph 19).

⁹⁶ *Ibid.*, pp 35-36 (paragraph 59).

Second, with regard to what the Committee regarded as a lesson of 'historical experience', namely that 'in the absence of countervailing policies, the overall impact on peripheral regions could be negative',⁹⁷ the Delors Report emphasised the necessity of macro-economic policy, and in particular of setting an EC-wide fiscal policy. This would be necessary in order to compensate Member States for the loss as a result of EMU of two major monetary policy instruments, namely control of exchange rates and the power to run a budgetary deficit. The Report regarded Community structural and regional policies as necessary to promote balanced development, narrow regional and structural disparities, and avoid serious economic and political risks.⁹⁸ It also considered wage flexibility and labour mobility as necessary elements in eliminating differences in competitiveness between different regions and countries.⁹⁹ In addition, however, it foresaw that

'it might be necessary in certain circumstances to provide financing flows through official channels. Such financial support would be additional to what might come from spontaneous capital flows or official borrowing and should be granted on terms and conditions that would prompt the recipient to intensify its adjustment efforts.'¹⁰⁰

Nevertheless, given the small size of the Community budget, any Community-led fiscal policy would have to be achieved, according to the Committee, by means of the coordination of national budgetary policies.¹⁰¹

Each of these strands in the Delors Report had previously been controversial, was so at the time of the Report, and indeed in the Committee, and has remained so ever since. For example, Winkler cites a Bundesbank board member who called political union 'a *conditio sine qua non*' for a successful single currency and regretted that the original German position 'no monetary union without political union' was dropped at Maastricht.¹⁰² More generally, it has often been argued that

⁹⁷ *Ibid.*, p 18 (paragraph 29).

⁹⁸ *Ibid.*, p 18 (paragraph 29).

⁹⁹ *Ibid.*, p 19 (paragraph 29). The emphasis on countering shocks by adjusting real labour costs and by budgetary policies at national and EC level was subsequently echoed by the Commission in its study 'One market, one money', (1990) 44 *European Economy* 11.

¹⁰⁰ *Ibid.*, p 19 (paragraph 29).

¹⁰¹ *Ibid.*, pp 19-20 (paragraph 30).

¹⁰² B. Winkler, *Towards a Strategic View on EMU: A Critical Survey* (European

the historical experience of currency unions demonstrates that a centralised monetary policy requires strong central political institutions.¹⁰³ Similarly, while the Delors Report echoed the Werner Report in its emphasis on the need for a common fiscal policy,¹⁰⁴ the Bundesbank President Karl-Otto Pohl played, together with Jacques Delors, a central role in the Delors Committee.¹⁰⁵ This ensured not only that the Bundesbank served as the model for the future European Central Bank, but also led to a substantial dilution of Delors' concern for a stronger fiscal policy.¹⁰⁶ This had a precedent: a 1977 Commission report on public finances concluded that 'if only because the Community budget is so relatively very small... in present circumstances monetary union is impracticable.'¹⁰⁷

On the basis of the Delors Report, the European Council meeting in Madrid in June 1989 decided that the first stage of EMU would start on 1 July 1990.¹⁰⁸ A subsequent Council Decision established a system of multilateral surveillance of economic developments and policies.¹⁰⁹ Another Council Decision amended the structure and functions of the Committee of Governors of the Central Banks.¹¹⁰

University Institute, working paper RSC No. 95/18, 1995), p 11, n 24, referring to R. Jochimsen, 'Perspektiven der Europäischen Wirtschafts - und Währungsunion' in *Deutsche Bundesbank: Auszüge aus Presse-Artikeln* No. 26, 3-9.

¹⁰³ See e.g. B. Winkler, *Towards a Strategic View on EMU: A Critical Survey* (European University Institute, working paper RSC No. 95/18, 1995), p 11.

¹⁰⁴ Compare the Delors Report, paragraph 29, with the Werner Report, paragraphs 13 and 14.

¹⁰⁵ On Pohl's influence in the Delors Committee, see Kenneth Dyson, *Elusive Union: The Process of Economic and Monetary Union in Europe* (Longman, 1994), pp 129 *et seq.*; Amy Verdun, *The Role of the Delors Committee in the Creation of the EMU: An Epistemic Community?* (Research Colloquium Series: European Integration and International Relations Robert Schuman Centre, European University Institute, February 12, 1997), p 22.

¹⁰⁶ As to the Delors Committee rejection of a mechanism for fiscal transfers, see Gros and Thygesen (a member of the Delors Committee), *European Monetary Integration: From the European Monetary System to European Monetary Union* (Longman, 1992), p 480.

¹⁰⁷ Commission of the European Communities, *Report on the Role of Public Finance in European Integration* (reference number II/10/77 E) (the MacDougall Report), p 12.

¹⁰⁸ See Council Decision 90/41 on the progressive convergence of economic policies and performance during stage one of economic and monetary union, recital 5, OJ 24.3.1990, 1990 L78/23:

¹⁰⁹ Council Decision 90/41 on the progressive convergence of economic policies and performance during stage one of economic and monetary union, OJ 24.3.1990 L78/23. This replaced Council Decision 74/120 on the attainment of high degree of convergence of the economic policies of the Member States of the EEC, OJ 3.5.1974 L63/16.

¹¹⁰ Council Decision 90/142 OJ 24.3.1990 L78/25.

The recommendations of the Delors Committee formed the basis for the EMU provisions of the Maastricht Treaty on European Union.¹¹¹ In particular, Article 3a(2) EC provided that the activities of the Member States and the Community shall include:

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.¹¹²

These activities were to comply with the principles of stable prices, sound public finances and monetary conditions, and a sustainable balance of payments.¹¹³

The principal exceptions to this generalisation regarding the proximate origins of the EMU provisions of the TEU were two-fold. First, the criteria according to which the convergence of Member States' economies was to be assessed were 'merely hinted at' in the Delors Report,¹¹⁴ negotiated during the pre-Maastricht Intergovernmental Conference, notably in the Monetary Committee, and agreed in the final

¹¹¹ The main provisions are contained in Articles 2, 3a(2), 4a, and a new Title VII Economic and Monetary Policy including Arts. 102a-109m, supplemented by the Protocol on the Statute of the European System of Central Banks and of the European Central Bank, the Protocol on the Statute of the European Monetary Institute, the Protocol on the Excessive Deficit Procedure, the Protocol on the Convergence Criteria referred to in Article 109j EC, the Protocol on the Transition to the Third Stage of Economic and Monetary Union, the Protocol on Certain Provisions relating to the UK, and the Protocol on Certain Provisions relating to Denmark. For surveys of these provisions, see F. Dehousse, 'L'Union économique et monétaire', *Le Traité de Maastricht 1*, C.E.E.I./Centre F. Dehousse, Université de Liège (1992); Goebel, 'European Economic and Monetary Union: Will the EMU Ever Fly?', (1998) 4 *Columbia Journal of European Law* 249; Louis, 'L'Union économique et monétaire', (1992) *Cahiers de Droit Européen* 251 Pipkorn, 'Legal Arrangements in the Treaty of Maastricht for the Effectiveness of the EMU', (1994) 31 *Common Market Law Review* 263-291; Slot, 'The Institutional Provisions of the EMU', in D Curtin and T Henkels (eds), *Institutional Dynamics of European Integration*, vol. II, pp 229-249 (Nijhoff 1994); Snyder, 'EMU - Metaphor for European Union? Institutions, Rules and Types of Regulation', in R. Dehousse (ed), *Europe after Maastricht: An Ever Closer Union?* (Law Books in Europe, 1994), pp 63-99.

¹¹² Art. 3a(2) EC.

¹¹³ Art. 3a(3) EC.

¹¹⁴ Committee for the Study of Economic and Monetary Union, *Report on Economic and Monetary Union in the European Community* (Office for Official Publications of the European Community, 1989), p. 23 (paragraph 30).

hours at Maastricht.¹¹⁵ Second, the ratification of the Maastricht Treaty, notably litigation in Germany and the 1992 referenda in Denmark and France, stimulated a long-overdue widespread political debate about the objectives and means of European integration, which focused in particular on EMU. In addition to clarifying different, competing conceptions of European integration,¹¹⁶ it contributed to the legal framework of EMU the so-called 'Denmark Agreement'. This was a unique instrument in the history of European law, which expressed the position of Denmark in respect of EMU.¹¹⁷

The Maastricht Treaty, which as regards EMU was not modified at all by the Amsterdam Treaty, provides for both economic policy and monetary policy. For these purposes, economic policy comprises price stability, control of excessive budget deficits, and certain common policies. Monetary policy includes a single currency, a central bank, and a single monetary policy body.¹¹⁸ The TEU consecrated the economists' coronation theory of monetary union, according to which economic convergence is a precondition for monetary integration. Nevertheless, the TEU gives monetary policy a much more supranational cast, while the provisions regarding economic policy accord more weight to national governments. However illogical this may appear from the theoretical standpoint, it reflects another political compromise,

¹¹⁵ See Kenneth Dyson, *Elusive Union: The Process of Economic and Monetary Integration in Europe* (Longman, 1994), pp 146-159; Amy Verdun, 'The Role of the Delors Committee in the Creation of the EMU: An Epistemic Community?' (Research Colloquium Series: European Integration and International Relations Robert Schuman Centre, European University Institute, February 12, 1997) p. 24.

¹¹⁶ *Manfred Brunner and Others v The European Union* (Cases 2 BvR 2134/92 & 2158/92 (before the Bundesverfassungsgericht, 2. Senat) (Federal Constitutional Court, 2nd Chamber) [1994] 1 CMLR 57.

¹¹⁷ Denmark and the Treaty of the European Union, Edinburgh European Council, 11 and 12 December 1992, Conclusions of the Presidency, OJ 31.12.1992 C348/1. See also D. Horwath 'The Compromise on Denmark and the Treaty on European Union: A Legal and Political Analysis' (1994) 31 *Common Market Law Review*, pp 765-805. With regard to the position of the UK, Usher has argued that exclusion from Art. 3a(2) EC 'does not necessary mean exclusion from the objective of economic and monetary union': see John A. Usher, *The Law of Money and Financial Services in the European Community* (Clarendon Press, 1994), pp 150-151..

¹¹⁸ As Dunnett points out, not all the criteria set forth by F.A. Mann, *The Legal Aspect of Money*, 5th edition 1992 at 508 for a monetary union are fulfilled, in that 'the central bank will not necessarily be a lender of last resort; national central banks will retain certain reserve assets; external liabilities will not be pooled; and the volume of domestic money may be affected by the exercise of external monetary powers retained by the Council and the Member States': D.R.R. Dunnett 'Legal and Institutional Issues affecting Economic and Monetary Union in David O'Keeffe and Patrick Twomey (eds) *Legal Issues of the Maastricht Treaty* (Chancery Law Publishing, 1994), pp. 138-139

1992 also saw, however, the virtual collapse of the EMS. On the 'Black Monday' of 16 September, market pressures led to the withdrawal of sterling, the suspension of the lira and the devaluation of the peseta. Until then there had been no realignments in the EMS since 1987. Such stability had been based on the convergence of inflation rates by means of monetary policy, with the Bundesbank basically in charge. It relied mainly on close cooperation among central banks within informal networks rather than on EC committees and other institutions. In respect of budgetary policies, however, there was little real convergence, and what existed stemmed from autonomous national decisions rather than EC-level coordination. Overall, EMS remained principally a creature of central bankers: exchange rates were the basic instrument for fighting inflation, and politicians intervened to renegotiate them mainly in times of crisis.¹¹⁹ Yet the ERM crises demonstrated that fixed-but-adjustable exchange rates could be extremely unstable in circumstances of the free movement of capital and the existence of large capital markets, leading economists to conclude that the only alternatives were either floating or fixed exchange rates.¹²⁰

The idea that monetary policy was apolitical thus proved an early victim of the controversial process of ratifying the Maastricht Treaty. The road to monetary union was suddenly filled with debate about the aims of monetary policy, the relation between monetary policy and economic policy, the entitlement of citizens and their elected representatives rather than technical experts to decide, and indeed whether or not EMU really should be a central objective of European integration and if so, on whose terms. This debate contributed perhaps more than any other single factor in the history of European integration to the politicisation of the EU and also of European Union, particularly European Community, law. It has also led to changes, often in appearance and sometimes in reality, in how basic decisions regarding European monetary integration are taken, who participates, and with what ultimate ends in view.

¹¹⁹ See Loukas Tsoukalis, 'Economic and Monetary Union', in H. Wallace and W. Wallace (eds), *Policy-Making in the European Union* (Oxford, 3rd ed. 1996) 279-299, p 284.

¹²⁰ Giorgia Giovannetti and Ramon Marimon, 'A Monetary Union for a Heterogeneous Europe', (European University Institute, Working Paper, RSC No. 95/17, 1995), 9. A short form of this article has been published in Torres (ed), *Monetary Reform in Europe* (Universidade Catolica Editoria, Lisbon, 1996).

2. POLITICAL MONEY

Jacques Rueff was only partly correct when (and if) he stated that 'l'Europe se fera par la monnaie ou elle ne se fera pas'.¹²¹ He neglected to add that money is politics. Had he done so, he might also have observed that 'l'Europe se fera par la politique, ou elle ne se fera pas'. At least with regard to EMU, one thus may assert that the last word about EMU belongs to the political class and those segments of the broader public which in one way or another participate in politics. But not completely

In order to elaborate this point, it is useful to consider briefly certain theoretical explanations of the evolution of the legal framework of EMU. The main points to be made here can be put in form of four statements. First, how one explains the evolution of EMU depends on one's theory of European integration and general theoretical framework. Second, EMU is primarily a political project, despite its fundamental economic importance and its significant legal characteristics. Third, EMU has been characterised, more than any other EU policy to date by the uneven, indeed asymmetric interaction of a technical discourse and a political discourse. Fourth, the evolution of EMU can in my view be explained adequately by combining a theory of two-level games with the notion of an epistemic community.

First, explanations of how EMU evolved are a function of one's theory of European integration and general theoretical assumptions. Two recent syntheses of a growing literature may illustrate the point. Wolf and Zangl distinguish three positions: supranationalism, intergovernmentalism and neoinstitutionalism.¹²² Supranationalists view Maastricht Treaty EMU as the result of a coalition between the Commission and the central banks of MS interested in EMU. Intergovernmentalists emphasise the convergence of interests among Germany, the United Kingdom and France. Neoinstitutionalists stress

¹²¹ The phrase is attributed to him by Daniel Gros and Niels Thygesen, *European Monetary Integration: From the European Monetary System to European Monetary Union* (Longman, 1992); p 3.

¹²² Dieter Wolf and Bernhard Zangl, 'The European Economic and Monetary Union: 'Two-level Games' and the Formation of International Institutions', (1996) 2 *European Journal of International Relations* 355-393 at pp 356-357. As examples of each position, they refer to David R. Cameron, 'Transnational Relations and the Development of European Economic and Monetary Union', in Thomas Risse-Kappen (ed), *Bringing Transnational Relations Back In: Non-State Actors, Domestic Structures and International Institutions* (Cambridge University Press, 1995), Wayne Sandholtz 'Choosing Union: Monetary Politics and Maastricht', (1993) 47 *International Organization* : 1-39 and their own work, respectively.

multi-level games, involving interests on the national, supranational and transnational levels.

Another useful survey of explanations of EMU is presented by Verdun, who gives some of these as well as other examples.¹²³ On one view, EMU was possible in the late 1980s because of a combination of factors, including domestic support for monetary and price stability, the need for a regime of monetary stability, Euro-optimism, the German need to demonstrate its commitment to European integration, the wish of other countries (France, Italy, Benelux) that shadowed German monetary policies to have a greater voice in EC monetary policy, and finally the desire of certain Member States (e.g. Italy) to institutionalise their commitment to low inflation, notably for domestic political reasons. Another view stresses intergovernmental bargaining.¹²⁴ Others emphasise the combination of interstate bargaining, issue linkage, and domestic distributional factors;¹²⁵ the linkage in the IGC between issues such as EMU, the cohesion fund, the social chapter, an extension of the powers of the European Parliament;¹²⁶ international circumstances;¹²⁷ the relationship between domestic politics and EC institutional structure;¹²⁸ the role of ideas;¹²⁹ and the role of experts, in particular central bankers, operating in transnational networks such as committees.¹³⁰ These various explanations of EMU reflect different

¹²³ Amy Verdun, 'The Role of the Delors Committee in the Creation of EMU: An Epistemic Community?', presented at the Research Colloquium Series 'European Integration and International Relations', Robert Schuman Centre, European University Institute, Florence, 12 February 1997, pp 7-14, on which this paragraph is based. I use Verdun's characterisation of different explanations and authors.

¹²⁴ See Moravcsik, 'Preferences and Power in the European Community: A Liberal Intergovernmentalist Approach' (1993) 31 *Journal of Common Market Studies* 473; 1993.

¹²⁵ Barry Eichengreen and John Frieden, *The Political Economy of European Monetary Unification* (Westview Press, 1995).

¹²⁶ Lisa Martin, 'International and Domestic Institutions in the EMU Process', (1993) 5(2) *Economics and Politics*, 125-144.

¹²⁷ Geoffrey Garrett, 'The Politics of Maastricht' (1993) 5(2) *Economics and Politics*, pp 105-123.

¹²⁸ Helen Milner, 'Regional Economic Cooperation, Global Markets and Domestic Politics: A Comparison of NAFTA and the Maastricht Treaty, (1995) 2(3) *Journal of European Public Policy*: 337-360.

¹²⁹ See Kenneth Dyson, *Elusive Union: The Process of Economic and Monetary Union in Europe* (Longman, 1994), p 16, who stresses the 'control over the key ideas and beliefs informing the policy process, in particular the 'capture' of the EMS policy process by economic ideas of 'sound money' and the prevalence of political beliefs about European union'.

¹³⁰ David R. Cameron, 'Transnational Relations and the Development of European Economic and Monetary Union', in Thomas Risse-Kappen (ed), *Bringing Transnational Relations Back In: Non-State Actors, Domestic Structures and International Institutions* (Cambridge University Press, 1995); Amy Verdun, 'The

conceptions of European integration and form part of different theoretical frameworks.

Second, despite its economic, social and legal significance, EMU is primarily a political project. Two highly reputed economists have stated, reflecting a widely held view, that 'neither economic theory nor economic evidence provides a clear case for or against monetary integration....The absence of a clear economic justification for EMU leads us to conclude that events in Europe are being driven mainly by political factors'.¹³¹ Another distinguished economist concludes that "It is probable that those favouring monetary unification within the European Community (EC) are also motivated mainly by political considerations, although the change in the monetary constitution, set out in the Maastricht Treaty, has been discussed largely in economic terms'.¹³² Indeed one of the principal authors of the 1989 Delors Report stated that in the long run EMU was not feasible without political union.¹³³ In 1996 French President Jacques Chirac was reported to have stated that 'behind the single currency was the entire political project that France and Germany have together for Europe and which was at stake'.¹³⁴ Tsoukalis concludes that 'The history of European monetary

Role of the Delors Committee in the Creation of the EMU: An Epistemic Community?' (Research Colloquium Series: European Integration and International Relations Robert Schuman Centre, European University Institute, February 12, 1997). See also Glenda Goldstone Rosenthal, *The Men Behind the Decisions: Cases in European Policy-Making* (Lexington Books, 1975). I wish to emphasise that the work by Dyson is much richer than such a simple characterisation might lead one to believe. Both Kenneth Dyson, *Elusive Union: The Process of Economic and Monetary Union in Europe* (Longman, 1994). In my view Kenneth Dyson, *Elusive Union: The Process of Economic and Monetary Union in Europe* (Longman, 1994) is among the best books written so far about EMU.

¹³¹ Barry Eichengreen and John Frieden, *The Political Economy of European Monetary Unification* (Westview Press, 1995), p 89.

¹³² Charles A.E. Goodhart, 'The Political Economy of Monetary Union', in Peter B. Kenen (Ed),: *Understanding Interdependence: The Macroeconomics of the Open* (Princeton University Press, 1995), at 448. See also Fratianni and Waller, *The Maastricht Way to EMU* (Princeton University, International Finance Section, June 1992, Princeton Essays in International Finance, No. 187), pp 1-2, who state: 'Although there are surely economic benefits to be expected from a monetary union, the main driving force for its (EMU's) resurgence remains the quest for political integration in Europe'.

¹³³ K.O. Pohl 'The Further Development of the European Monetary System (September 1988)' in Committee for the Study of Economic and Monetary Union, *Collection of Papers submitted to the Committee for the Study of Economic and Monetary Union* (Office for Official Publication of the European Community, 1989), p 136. See also Charles A.E. Goodhart, 'The Political Economy of Monetary Union', in Peter B. Kenen (Ed),: *Understanding Interdependence: The Macroeconomics of the Open* (Princeton University Press, 1995), p 455.

¹³⁴ *Agence Europe* No 6801 (n.s.), Saturday 1 September' 1996 p 5 (the verbatim quotation is from *Agence Europe*). The same issue of *Agence Europe* also reported that, on the

integration can be seen ... as a dialectical process between wider political objectives and market realities'.¹³⁵ Put another way, 'politics ... has been the decisive ingredient in the European process from the outset' and that 'there is no such a thing as unpolitical money'.¹³⁶

Clearly the single currency has crucial actual and symbolic implications for national governments and for the building of a potential supranational polity and constitutional culture.¹³⁷ For example, adopting a single currency 'could refocus the attention to gainers and losers on the status of the agent involved, rather than his or her country of residence'.¹³⁸ The single currency may create and emphasise new types of identity, or rather old types within a new political context, namely class and other forms of social and economic differentiation, rather than nationality. It would thus be likely to create and strengthen ties between people in different EC Member States. This in turn could have a decisive impact on the functioning of governance in the context of European integration, including fiscal policy but extending also to constitutional principles, the development of constitutionalising processes and the growth of constitutional culture.

If, borrowing from the late Deng Xiaoping, we can characterise the evolution of EMU as the search for 'capitalism with European

same day, during a ceremony in honour of the 65th birthday of the President of the Bundesbank, German Federal Chancellor Kohl indicated 'that the single currency will have to be introduced, but not on the basis of a weak compromise', while Bundesbank President Tietmeyer indicated that he 'wholeheartedly supported monetary integration but that its foundations should be sound ones'.

¹³⁵ Loukas Tsoukalis, 'Economic and Monetary Union', in H. Wallace and W. Wallace (eds), *Policy-Making in the European Union* (Oxford, 3rd ed. 1996) 279-299, p 280.

¹³⁶ Klaus Gretschmann, Hans-Helmut Kotz and Olaf Sleijpen, 'The European Monetary System: The Geography of Economics versus the Politics of Money?', in K. Gretschmann (ed), *Economic and Monetary Union: Implications for National Policy-Makers* (Dordrecht, Martinus Nijhoff for the European Institute of Public Administration, 1993), pp 27-49 at p 28.

¹³⁷ See also Charles A.E. Goodhart, 'The Political Economy of Monetary Union', in Peter B. Kenen (Ed),: *Understanding Interdependence: The Macroeconomics of the Open* (Princeton University Press, 1995), p. 455. See also Stephen Clarkson, 'Perché No? Qualms about Currency Union from over the Sea' (Paper presented at the Workshop The Political and Institutional Deficits of the European Integration Process, European University Institute, 30-31 May 1997), p 18, who asserts that "The elites driving EMU to fruition seem to want a common currency less for economic reasons than to pursue a triple political agenda: neo-liberal restraint of the welfare state, the consolidation of European power in its global context, and the joint agenda of the Franco-German axis.'

¹³⁸ Charles A.E. Goodhart, 'The Political Economy of Monetary Union', in Peter B. Kenen (Ed),: *Understanding Interdependence: The Macroeconomics of the Open* (Princeton University Press, 1995, p 475.

characteristics', one conclusion emerges. This is that we need to evaluate EMU not merely in economic terms but also in political terms. EMU has never been simply a technical economic issue and should not be treated only as such. Consequently, it is essential to be aware of its potential political implications and to address them directly. This includes the likely political consequences of EMU and its costs and benefits, for example with regard to increased political integration, legitimacy and the creation of social solidarity.

Third, EMU, once assumed to be a goal, has thus far involved two major decisions.¹³⁹ The first decision concerns institutional choices, most notably whether to create a unified monetary policy with a single currency and common institutions or whether to rely on the market. The Delors Committee chose the former. This option was endorsed by the June 1989 European Council in Madrid and expressed in the Maastricht Treaty. The second decision relates to the strategy for institutionalisation, in particular whether to use the coronation strategy, on the one hand, or the 'monetarist' or 'locomotive' strategy, on the other hand. These alternatives were discussed at the Intergovernmental Conference in Rome in December 1990, and the December 1991 European Council meeting in Maastricht chose the coronation strategy. Both sets of issues have long been part of the specialist debate regarding European monetary integration. Both have been resolved, for the time being, by high-level political decisions, as expressed in legal form in the Treaty on European Union.

The process of making these decisions has been dominated by two contrasting discourses, which have sometimes intersected but more often run in parallel.¹⁴⁰ The first, a technical discourse, expressed by banking and financial specialists mainly in expert committees and networks, appears to have been continuous throughout the history of debates on European monetary integration. It has been concerned mainly with economic doctrines, theories and hypotheses, such as ideas about inflation, and relations between currency and economic integration or between monetary policy and fiscal policy, and the respective merits of the coronation theory and the monetarist theory. In this realm, legal issues and legal doctrines have been of little

¹³⁹ For a game-theoretical approach to these issues, see Dieter Wolf and Bernhard Zangl, 'The European Economic and Monetary Union: 'Two-level Games' and the Formation of International Institutions', (1996) 2 *European Journal of International Relations*.

¹⁴⁰ I am indebted to Miguel Poiates Maduro for this point.

significance, and politics possibly even less. The banker and the economist have been king.

In contrast, a second, political discourse, articulated by political elites and more recently a broader public, has been discontinuous. Its articulation has varied depending on changes in the pace, nature and economic context of European integration. In practice, political discourse has dominated debates about whether there should be an EMU at all, while technical discourse has dominated debates about the shape of EMU.

When the (discontinuous) political discourse favours the adoption of EMU, it has tended to borrow from or rely upon the (continuous) technical discourse for its ideas regarding strategies of institutionalisation and even, to some extent, regarding institutional choices. In these circumstances, political discourse has fed on and reinforced certain strands of the technical discourse. What is striking, however, is that in the past political discourse has focused almost entirely on whether there should be an EMU. Only recently has political discourse begun to address the issue of how EMU should be brought about. This reorientation has placed our conceptions of EMU in a wholly new perspective. It has opened up a broadly based, highly salutary, and extremely controversial public debate, not simply about the role and governance of monetary policy, but also about the nature and future of European integration.

Fourth, building on these remarks, we can in my view¹⁴¹ explain the evolution of EMU, at least provisionally, by combining two hypotheses to generate a third. The first hypothesis is that changes in the configuration of interests lead to a change in normative and institutional structures. The second hypothesis is that the evolution of EMU has been characterised by the existence of two discourses, a relatively continuous technical discourse and a relatively discontinuous political discourse. By combining these hypotheses, we can generate a third hypothesis. This is that EMU is the result of the coincidence of political and technical interests. Since the 1960s the basic interests expressed in technical discourse have remained remarkably constant, while those expressed in political discourse have varied.¹⁴² EMU is the

¹⁴¹ On the basis of the arguments about legal change, in particular the relations between interests, structures and processes, put forward in Francis Snyder, *New Directions in European Community Law* (Weidenfeld & Nicolson, London, 1990).

¹⁴² For attempts to come to grips with political discourse about EMU, see Glenda Goldstone Rosenthal, *The Men Behind the Decisions* (Lexington Books, 1975), pp 112-

product of their overlap, or, put another way, the basic motor forces of EMU are political.

The continuity of technical interests and technical discourse is captured neatly by the conception of an epistemic community. As defined by Haas, the concept of 'epistemic community' refers to 'a network of professionals from a variety of disciplines and backgrounds... /who/... have (1) a shared set of normative and principled beliefs...; (2) shared causal beliefs...; (3) shared notions of validity...;and (4) a common policy enterprise.¹⁴³ It has been applied, in my view persuasively, to the expert groups which, since the 1960s, have outlined or formulated policies regarding EMU.¹⁴⁴

Verdun, for example, argues that such groups as the Monetary Committee or the Committee of Central Bank Governors have demonstrated a great continuity, often including continuity of individual members.¹⁴⁵ She further argues that they were dominated by central bankers and monetary specialists, including academic economists, who

118; Carsten Hefeker, *Interest Groups and Monetary Integration: The Political Economy of Exchange Regime Choice*(Westview Press, 1997); Amy Verdun, 'An "Asymmetrical" Economic and Monetary Union in the EU: Perceptions of Monetary Authorities and Social Partners', (1996) 20 *Revue d'Intégration Européenne / Journal of European Integration*59.81; Bernard Moss (ed), *The Single Currency in National Perspective: The Limits of European Integration*(in press); B...Connolly, *The Rotten Heart of Europe* (add reference).

¹⁴³ Haas 1992b /cited in Amy Verdun, *The Role of the Delors Committee in the Creation of the EMU: An Epistemic Community?* (Research Colloquim Series: European Integration and International Relations Robert Schuman Centre, European University Institute, February 12, 1997), p 3

¹⁴⁴ In particular, see Kenneth Dyson, *Elusive Union: The Process of Economic and Monetary Union in Europe* (Longman, 1994); Amy Verdun, 'The Role of the Delors Committee in the Creation of the EMU: An Epistemic Community?' (Research Colloquim Series: European Integration and International Relations Robert Schuman Centre, European University Institute, February 12, 1997).

¹⁴⁵ See Amy Verdun, 'The Role of the Delors Committee in the Creation of the EMU: An Epistemic Community?' (Research Colloquim Series: European Integration and International Relations Robert Schuman Centre, European University Institute, February 12, 1997). See also Kenneth Dyson, *Elusive Union: The Process of Economic and Monetary Union in Europe* (Longman, 1994) and, for the earlier period, Glenda Goldstone Rosenthal, *The Men Behind the Decisions: Cases in European Policy-Making* (Lexington Books, 1975). More recently, the Governor of the Central Bank of Ireland has stated that 'As well as inheriting the role of the Committee of Governors, the Council of the EMI is virtually identical in composition to the Committee: Maurice O'Connell, 'The Maastricht Treaty and Aspects of Monetary Union', (1995) 4 *Irish Journal of European Law* 5-17 Writing of the same institutions, John A. Usher, *The Law of Money and Financial Services in the European Community*(Clarendon Press, 1994), p 164, observes that 'in other words the same people carry on, but under a new name and with new powers' .

shared certain views.¹⁴⁶ All members of the Delors Committee, for example,

'believed that further economic and monetary integration was desirable. In addition, they shared four causal beliefs: First, they believed that inflation was detrimental to growth. Second, stable exchange rates were necessary to ensure the proper operation of the Internal Market. Third, the *de facto* dominance of the D-Mark as the anchor currency, and hence the dominance of the Bundesbank in determining European monetary policies was politically unsatisfactory. Fourth,...the Delors Committee wanted national governments to remain fully responsible for national macroeconomic and fiscal policies. Hence, the need for multiple linkages – binding rules would be necessary to contain budget deficits.'¹⁴⁷

The technical and political role of such transnational epistemic communities is well-known in the Community system now,¹⁴⁸ but in the late 1980s it received relatively little attention.¹⁴⁹ With regard to EMU, it derived from 'the structural changes in the nature and structure of capitalism, notably the relationship between EC states and global financial markets and the phenomenon of inflation'.¹⁵⁰ Few groups of experts before or since have had such a profound impact on European integration as the Delors Committee.

The Delors Committee did not, however, act in isolation from the Member States. Indeed, it has been suggested that the Delors Committee was established and given such an important role precisely because many national governments realised their limited room for manoeuvre

¹⁴⁶ Amy Verdun, 'The Role of the Delors Committee in the Creation of the EMU: An Epistemic Community?' (Research Colloquium Series: European Integration and International Relations, Robert Schuman Centre, European University Institute, February 12, 1997).

¹⁴⁷ Amy Verdun, 'The Role of the Delors Committee in the Creation of the EMU: An Epistemic Community?', (Research Colloquium Series: European Integration and International Relations, Robert Schuman Centre, European University Institute, February 12, 1997), p 23.

¹⁴⁸ See the special issue on committees: (1997) 3 *European Law Journal*.

¹⁴⁹ See also David R. Cameron, 'Transnational Relations and the Development of European Economic and Monetary Union', in Thomas Risse-Kappen (ed), *Bringing Transnational Relations Back In: Non-State Actors, Domestic Structures and International Institutions*(Cambridge University Press, 1995), pp 37-78 at pp 73-74.

¹⁵⁰ See Amy Verdun, 'The Role of the Delors Committee in the Creation of the EMU: An Epistemic Community?' (Research Colloquium Series: European Integration and International Relations, Robert Schuman Centre, European University Institute, February 12, 1997).

regarding monetary policy and sought specialist expertise concerning further cooperation.¹⁵¹ We can understand the linkage between national governments and monetary experts by using the theory of two-level games.¹⁵² As Dyson argues, 'the EMS and EMU policy process is best understood as composed of a distinct set of interdependent bargaining relations and rules of the game, embedded in a framework of structures that they have a limited, and fluctuating, capacity to influence'.¹⁵³

Wolf and Zangl apply the theory of two-level games systematically to EMU.¹⁵⁴ They focus on two important issues, institutional choices and strategies of institutionalisation. They distinguish among actors, possible courses of action, and preferences. With regard to actors, they conceptualise the negotiations 'as a connection of two successive games played by the governments of the major member-states - France, Germany, Great Britain - and influenced by the most important domestic actors - the central banks in France, Germany and Great Britain'.¹⁵⁵ Monetary policy lacks the array of organised interest groups which are characteristic of most policy areas.¹⁵⁶ Central banks are the only domestic actors which clearly have special interests in monetary matters; the preferences of other actors are rarely voiced and instead are embedded in market decisions. With regard to possible courses of action, in respect of institutional choices they comprised EMU, a parallel currency concept, the EMS, or floating currencies.¹⁵⁷ Possible courses of action in respect of institutionalisation strategies were the locomotive

¹⁵¹ Amy Verdun, 'The Role of the Delors Committee in the Creation of the EMU: An Epistemic Community?' (Research Colloquium Series: European Integration and International Relations, Robert Schuman Centre, European University Institute, February 12, 1997), p 26.

¹⁵² The seminal article concerning two-level games is Robert Putnam, 'Diplomacy and Domestic Politics: The Logic of Two-Level Games' (1988) 42 *International Organization* 427-469.

¹⁵³ Kenneth Dyson, *Elusive Union: The Process of Economic and Monetary Union in Europe* (Longman, 1994), p. x.

¹⁵⁴ Dieter Wolf and Bernhard Zangl, 'The European Economic and Monetary Union: 'Two-level Games' and the Formation of International Institutions', (1996) 2 *European Journal of International Relations*.

¹⁵⁵ Dieter Wolf and Bernhard Zangl, 'The European Economic and Monetary Union: 'Two-level Games' and the Formation of International Institutions', (1996) 2 *European Journal of International Relations*, p 370.

¹⁵⁶ This relatively narrow view of interests concentrates on subjective interests. For an alternative view, which cannot be developed further here, see Francis Snyder, *New Directions in European Community Law* (Weidenfeld & Nicolson, London, 1990), chapter 2.

¹⁵⁷ See Dieter Wolf and Bernhard Zangl, 'The European Economic and Monetary Union: 'Two-level Games' and the Formation of International Institutions', (1996) 2 *European Journal of International Relations*, pp 371-372.

strategy, favoured by the economists, and the coronation strategy, favoured by the monetarists.¹⁵⁸

After analysing preferences,¹⁵⁹ Wolf and Zangl conclude that the first issue involved (a) a coordination game with distributional conflict at the governmental level and (b) a leader-veto situation at the domestic level (UK leader, German veto). The second issue involved (a) a coordination game with distributional conflict at the governmental level (France, Germany) and (b) a veto-similar position at domestic level (German veto, France similar).¹⁶⁰ The first issue was resolved because 'it was not likely that London and Bonn would block each other with credible threats', and the second because 'only Bonn's threat not to compromise was credible' (because of the Bundesbank's veto position), so the solution corresponded to the German position.¹⁶¹ The second issue was resolved because the Bundesbank held a veto on this issue (as well as on the first). The French accepted the coronation strategy and the convergence criteria, and in exchange obtained the creation of a weak European Monetary Institute. 'Paris acknowledged that otherwise the German government would not have been able to sign the Treaty'.¹⁶²

To conclude this argument, it is useful to recall the position of the Commission. Caught between proponents and opponents of the 'hidden agenda' of federalism,¹⁶³ the Commission embraced the principle of

¹⁵⁸ See Dieter Wolf and Bernhard Zangl, 'The European Economic and Monetary Union: 'Two-level Games' and the Formation of International Institutions', (1996) 2 *European Journal of International Relations*, p 378.

¹⁵⁹ The salient preferences in respect of the first issue were as follows: German government: EMU>PCC>EMS>FLOAT; Bundesbank: EMU>EMU>PCC>FLOAT; UK government: PCC>EMU>EMS>FLOAT; Bank of England: EMU>EM>PCC>FLOAT; note that France partly agreed with the UK government position. The salient preferences in respect of the second issue were as follows: French government: LS>CS>EMS; Banque de France LS>CS>EMS; German government: CS>LS>EMS; Bundesbank: EMS>CS>LS. See Dieter Wolf and Bernhard Zangl, 'The European Economic and Monetary Union: 'Two-level Games' and the Formation of International Institutions', (1996) 2 *European Journal of International Relations*, pp 372-374, 379-381.

¹⁶⁰ Dieter Wolf and Bernhard Zangl, 'The European Economic and Monetary Union: 'Two-level Games' and the Formation of International Institutions', (1996) 2 *European Journal of International Relations*, p 381.

¹⁶¹ Dieter Wolf and Bernhard Zangl, 'The European Economic and Monetary Union: 'Two-level Games' and the Formation of International Institutions', (1996) 2 *European Journal of International Relations*, p 374.

¹⁶² Dieter Wolf and Bernhard Zangl, 'The European Economic and Monetary Union: 'Two-level Games' and the Formation of International Institutions', (1996) 2 *European Journal of International Relations*, p 383.

¹⁶³ The expression is used (also within quotation marks) by Charles A.E. Goodhart, 'The Political Economy of Monetary Union', in Peter B. Kenen (Ed),: *Understanding Interdependence: The Macroeconomics of the Open* (Princeton University Press, 1995, p 477.

subsidiarity.¹⁶⁴ This provided an intellectual balance between the two groups, shifted the terrain of argument from the general to the particular, and provided 'an intellectual smokescreen behind which the ongoing decisionmaking process in the EC can result in a series of pragmatic determinations leading either toward or away from greater federalism'.¹⁶⁵ It also reflected the Commission's assumption, which did not however hold for Germany, that the principal loss of monetary sovereignty occurred during the early ERM, and that the (mainly micro-economic) benefits of monetary integration would take place only at the final stage of EMU.¹⁶⁶

3. SELECTED CONSTITUTIONAL ISSUES

EMU as expressed in the Maastricht Treaty involves a number of controversial matters which, directly or indirectly, in the short-term or the long-term, raise important legal issues. Despite their significance, however, these legal issues are sometimes couched or camouflaged in economic language, which has been predominant in debates about EMU until recently. This section focuses on selected issues which are related directly to the EU constitution.¹⁶⁷ It considers (a) the debate about

¹⁶⁴ See European Commission, *One Market, One Money: An Evaluation of the Potential Benefits and Costs of Forming an Economic and Monetary Union*, European Economy, No. 44 (1990), p 32.

¹⁶⁵ Charles A.E. Goodhart, 'The Political Economy of Monetary Union', in Peter B. Kenen (Ed.): *Understanding Interdependence: The Macroeconomics of the Open* (Princeton University Press, 1995, p 477. Goodhart writes as an economist, not as a lawyer, and most lawyers, including me, would hesitate to accept his characterisation of the EC as a federation.

¹⁶⁶ See Charles A.E. Goodhart, 'The Political Economy of Monetary Union', in Peter B. Kenen (Ed.): *Understanding Interdependence: The Macroeconomics of the Open* (Princeton University Press, 1995, p 482.

¹⁶⁷ For reasons of space, however, it omits the new exchange rate mechanism, the relation of participating Member States to non-participating Member States, and the relation of participating Member States to third countries- As to external relations, see generally European Commission, 'External Aspects of Economic and Monetary Union (Commission Staff Working Document)', *Europe Documents* No 2034, 8 May 1997, pp 1-9. See also 'Europe's Global Currency: Implications for Business Leaders and Economic Policymakers', The Philip Morris Institute for Public Policy Research, Conference Proceedings, Palazzo Lancellotti, Rome, 1-2 July 1996; Jacques Leonard and Philippe Norel, 'Dollar-Euro: Des principes aux enjeux d'un système coopératif', (1997) 405 *Revue du Marché Commun et de l'Union européenne* 92-110; Fabienne Itzkovitz, 'Les perspectives de l'internationalisation de l'euro', (1996) 36 *Revue de l'économie financière* 151-169; Jolin Dixon, 'The Euro and Its International Implications', (1997) 3 *Newsletter of the Instituto de Estudos Europeus de Macau* 11-15; 'France-Afrique: Qui a peur de l'euro?', (1997) 1904 *Jeune Afrique* (2-8 Juillet) pp 70-71. As to relations with the International Monetary Fund, see Rutsel Silvestre J. Martha, 'The Fund Agreement and the Surrender of Monetary Sovereignty to the European Community', (1993) 30 *Common Market Law Review* 749-786. It also omits issues solely of monetary law or private law, such as the introduction of the euro, conversion or

whether the EU is an optimum currency area, (b) the timetable for achieving EMU, (c) the convergence criteria as a legal expression of the coronation strategy, (d) the reallocation of policy instruments among levels of governance, (e) the new legal techniques which are being used to implement EMU, and (f) the legitimacy of EMU.

(A) THE EU AS AN OPTIMUM CURRENCY AREA

In order to gauge the feasibility of EMU, economists have asked whether the EU is an optimum currency area. This question assumes that it is possible to identify a geographical area which presents the ideal economic and political characteristics for the establishment of a single currency.¹⁶⁸ Whatever the merits of this question in general terms, the debate about EMU appears to have stimulated a reassessment of the concept of an optimal currency area, at least as applied to EMU. In this respect, it has been asserted that the concept of an optimal currency area does not lead to any firm conclusions either for or against Maastricht EMU.¹⁶⁹ One distinguished economist has gone so far as to assert that the theory has 'relatively little predictive power', because monetary boundaries and optimum currency areas rarely coincide.¹⁷⁰

rounding, the continuity of contracts, and the legal status of the ECU. For further discussion, see Marianne Lévy-Rosenwald, 'Les problèmes juridiques posés par la monnaie unique', *Revue de l'Economie Financière*, 36, 1996, pp 112-122; D.R.R. Dunnett, 'Some Legal Principles Applicable to the Transition to the Single Currency', (1996) 33 *Common Market Law Review* 1133-1167; Hercules Booyen, 'A Future Currency ECU: The Problem of Succession and the Private Law Implications', *Journal of World Trade*, 28, 6, December 1994, pp 83-98; Ulrich Woelker, 'The Continuity of Contracts in the Transition to the Third Stage of Economic and Monetary Union', (1996) 33 *Common Market Law Review* 1107-1116. See also Council Regulation 1103/97 on certain provisions relating to the introduction of the euro, OJ 19.6.97 L162/1; Graham Bishop, José Pères, and Sammy van Tuyl (eds), *User Guide to the Euro* (Federal Trust and Sweet & Maxwell, 1996); *Le Guide de l'Euro* (Editions Jean-Francois Doumic, 1997); Derek Riley, 'L'Euro: Reflexions autour d'un scénario vraisemblable' (1997) 406 *Revue du Marché commun et de l'Union européenne* 175-191..

¹⁶⁸ For an overview of the literature on optimum currency areas, see G. Tavlas 'The 'New' Theory of Optimum Currency Areas' (1993) 16 *The World Economy*: 663-685 and P. Bofinger, 'Is Europe an Optimum Currency Area?' (Centre of Economic Policy Research 1994). For a critique of this literature as applied to EMU, see B. Winkler, 'Towards a Strategic View on EMU: A Critical Survey', (European University Institute, Working Paper RSC No. 95/18, 1995).

¹⁶⁹ Giorgia Giovannetti and Ramon Marimon, 'A Monetary Union for a Heterogeneous Europe' (European University Institute, RSC No. 95/17, 1995), 7.

¹⁷⁰ Charles A.E. Goodhart, 'The Political Economy of Monetary Union', in Peter B. Kenen (Ed),: *Understanding Interdependence: The Macroeconomics of the Open* (Princeton University Press, 1995: 452. See also B. Winkler, *Towards a Strategic View on EMU: A Critical Survey* (European University Institute, working paper No. 95/18, 1995), p 1, who considers that the oca perspective 'is little more than a special case of the

The relevance of this debate to the EU constitution emerges clearly if one considers the assumptions underlying theories of an optimum currency area, and asks why these theories do not point unambiguously in favour of EMU. Goodhart makes the central point: 'The largest question ... about identifying the EC as an optimum currency area arises from the empirical studies revealing that labor migration in Europe is miniscule in comparison to that in the United States, and that any large increase would cause political problems'.¹⁷¹ The question is important because labour or capital mobility and the exchange rate are alternative ways of dealing with economic shocks. Yet, as Goodhart points out, it is very difficult to evaluate the relative effects of these alternatives.¹⁷² Since labour mobility in the EU is low, however, the main instrument for dealing with economic shocks so far has been the exchange rate.

From the legal standpoint, this apparently technical economic debate raises three important questions. First, to what extent does EU law provide adequate structures of governance for deciding, in a legitimate and democratically accountable manner, which economic policies should be given priority? Second, to what extent should EU (EC) law encourage labour mobility, and to what extent can it do so effectively? Third, if labour mobility within the EU continues to remain low, what other instruments of governance are available to deal with economic shocks after the establishment of a single currency? EMU, as will be seen later, does not provide convincing answers to these questions.

(B) THE TIMETABLE FOR ACHIEVING EMU

According to the Maastricht Treaty, EMU is to be achieved in three stages. This strategy has been criticised from the economic, political and legal standpoints.¹⁷³ From the economic standpoint it is an open question whether EMU should have been achieved in a single overnight leap or whether it should be achieved in stages. The main argument for the former was its necessity to prevent destructive speculation, while the

perennial debate over fixed versus floating exchange rates'.

¹⁷¹ Charles A.E. Goodhart, 'The Political Economy of Monetary Union', in Peter B. Kenen (Ed),: *Understanding Interdependence: The Macroeconomics of the Open* (Princeton University Press, 1995, p 463.

¹⁷² Charles A.E. Goodhart, 'The Political Economy of Monetary Union', in Peter B. Kenen (Ed),: *Understanding Interdependence: The Macroeconomics of the Open* (Princeton University Press, 1995, p 465.

¹⁷³ See e.g. Charles A.E. Goodhart, 'The Political Economy of Monetary Union', in Peter B. Kenen (Ed),: *Understanding Interdependence: The Macroeconomics of the Open* (Princeton University Press, 1995), p 483.

latter was designed to facilitate economic convergence and (perhaps) gather political support. But even though the strategy of stages was chosen, the Member States, in particular Germany, still considered it necessary to adopt subsequently a Stability Pact in order to channel and coerce their partners into line. More specifically, even some time ago, many economists considered that the second stage should have been omitted, because in its early years it simply demonstrated that increasingly fixed exchange rates would not necessarily lead to economic convergence, contrary to the assumptions embodied in the Treaty.

These economic strategies assume the appropriate political conditions. From the political standpoint, however, it may be strongly argued that not only was a strategy of stages indispensable, but also that it should have involved a much more thorough public debate. In this way, the processes of creating institutions, choosing broad policies, and constructing a constitution might conceivably have been based on a more widespread deliberation. Constitutional litigation has served as a surrogate for such deliberation in at least one Member State,¹⁷⁴ but this is not feasible in all. It may also be argued that the strategy of achieving EMU in stages is based on a misguided or unrealistic conception of EU monetary integration, or indeed integration in general. The idea underlying EMU is that of multiple-speed Europe, but a forceful argument can be made that a more appropriate starting point is the notion of variable geometry. Such a conception of European monetary integration demands a more multi-faceted strategy of cooperation than a straightforward series of stages.¹⁷⁵

From a legal perspective, the timetable raises two different issues. First, is the timetable legally binding? The history of the Community is full of examples when time limits have not been respected. In the specific case of EMU, the German Federal Constitutional Court stated in its 'Maastricht judgment' that the time for the beginning of the third stage was a target, not a legally enforceable date.¹⁷⁶ In addition, if the

¹⁷⁴ See the ruling of the German Federal Constitutional Court on the complaint to the effect that EMU should be postponed: *Financial Times* Tuesday 10 March 1998, p 2. See also *Agence Europe*, No. 7136 (n.s.), Monday/Tuesday, 12/13 January 1998, p 9, and No. 7137 (n.s.), Wednesday 14 January 1998, p 14..

¹⁷⁵ On monetary union and flexible integration, see e.g. Centre for Economic Policy Research, *Flexible Integration: Towards a More Effective and Democratic Europe* (London, 1995), pp 127-147.

¹⁷⁶ *Manfred Brunner and others v The European Union Treaty* (Cases 2 BvR 2134/92 & 2159/92 before the Bundesverfassungsgericht (2. Senat) (German Federal

'ins' had numbered five instead of the current eleven, it is unlikely that EMU would have proceeded so far as it already has.¹⁷⁷ Second, what are the legal consequences of the timetable? The Treaty provisions regarding the third stage of EMU are concerned either with institutions or with discretionary economic policy-making. Regardless of their effects on national governments, they are unlikely to give rise to enforceable claims on the part of individuals.¹⁷⁸

(C) THE CONVERGENCE CRITERIA

The Maastricht (soon Amsterdam) Treaty requires the Commission and the European Monetary Institute (EMI) to report to the Council on Member States' progress towards EMU.¹⁷⁹ The reports will form the basis for the assessment by the Council of which Member States fulfil the necessary conditions for the adoption of the single currency.¹⁸⁰ Among their key elements is an examination of Member States' economic performance with reference to four different criteria.

These convergence criteria, the legal expression of the coronation theory, are set down in the Treaty.¹⁸¹ Article 109j(1), first paragraph, EC provides - and I emphasise its discretionary elements - as follows (emphasis added):

'The reports shall also examine the achievement of a **high degree** of **sustainable** convergence **by reference to** the fulfilment by each Member State of the following criteria:

- the achievement of a **high degree** of price stability; this will be apparent from a rate of inflation which is closest to that of, at most, the three best performing Member States in terms of price stability;

Constitutional Court, 2nd Chamber) (1994) 1 CMLR 57 at 99 (para. 83). One has only to recall the pleas of various national governments as late as autumn 1997 to the effect that the timetable should be renegotiated.

¹⁷⁷ See also John A. Usher, *The Law of Money and Financial Services in the European Community* (Clarendon Press, 1994), p 154.

¹⁷⁸ John A. Usher, *The Law of Money and Financial Services in the European Community* (Clarendon Press, 1994), pp 154-155. For a discussion as to whether the procedures may be used after the deadlines have expired and the effect of the expiration of the deadlines on the relative competencies of the EC and the Member States, see John A. Usher, *The Law of Money and Financial Services in the European Community* (Clarendon Press, 1994), pp 155-156

¹⁷⁹ Art. 109j(1) EC.

¹⁸⁰ See Art. 109j(4) EC.

¹⁸¹ Art. 109j(1), first paragraph, EC.

- the **sustainability** of the government financial position; this will be apparent from having achieved a government budgetary position without a deficit that is excessive as determined in accordance with Article 104c(6);
- the observance of the **normal** fluctuation margins **provided for** by the Exchange Rate Mechanism of the European Monetary System for at least two years, without devaluing against the currency of any other Member State;
- the **durability** of convergence achieved by the Member State and of the participation in the Exchange Rate Mechanism of the European Monetary System being reflected in the long-term interest rate levels.'

These criteria and the relevant periods for assessing whether they have been met are explicated in a Protocol annexed to the Treaty.¹⁸²

According to this Protocol,¹⁸³ the convergence criteria are as follows (and again I emphasise those parts which would appear, even to a non-economist, to leave room for discretion):

Article 1 The criterion on price stability referred to in the first indent of Article 109j(1) of this Treaty shall mean that a Member State has a price performance that is sustainable and an average rate of inflation, observed **over a period of one year before the examination** , that does not exceed more than 1 _ percentage points that of, at most, the three best performing Member States in terms of price stability. Inflation shall be measured by means of the consumer price index on a comparable basis, taking in account differences in national definitions.

Article 2 The criterion on the government budgetary position referred to in the second indent of Article 109j(1) of this Treaty shall mean that at the time of the examination the Member State is not the subject of a Council decision under Article 104c(6) of this Treaty that an **excessive** deficit exists.

¹⁸² Art. 109j(1), second paragraph, EC, which also provides that the 'reports of the Commission and the EMI shall also take account of the development of the ECU, the results of the integration of markets, the situation and development of the balance of payments on current account and an examination of the development of unit labour costs and other price indices.'

¹⁸³ Protocol on the convergence criteria referred to in Article 109j of the Treaty establishing the European Community, OJ 31.8.92 C224/121 (emphasis added).

Article 3 The criterion on participation in the Exchange Rate Mechanism of the European Monetary System referred to in the third indent of Article 109j(1) of this Treaty shall mean that a Member State has respected 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** . In particular, the Member State shall not have devalued its currency's bilateral central rate against any other Member State's currency on its own initiative for the same period.

Article 4 The criterion on the convergence of interest rates referred to in the fourth indent of Article 109j(1) of this Treaty shall mean that, observed **over a period of one year before the examination** , a Member State has had an average nominal long-term interest rate that does not exceed by more than 2 percentage points that of, at most, the three best performing Member States in terms of price stability. Interest rates shall be measured on the basis of long term government bonds or comparable securities, taking in account differences in national definitions.

Each of these criteria, as my emphasis shows, contains room for interpretation. It is easy to give examples.

First, the exact dates to be used for the purposes of articles 1, 2 and 4 of the Protocol have only recently been decided. However, it is now settled that they will be in early May 1998.

Second, the meaning of 'normal' fluctuation margins was not clear until recently. The original fluctuation margin set in 1979 for most currencies was 4.5%, that is, 2.25% around bilateral rates.¹⁸⁴ A wide band of a 15% fluctuation margin was adopted on a temporary basis on 1-2 August 1993. A year later at least one legal scholar submitted that this wide band should be recognised as the 'normal' margin.¹⁸⁵ The European Council has recently confirmed that the standard fluctuation band will be relatively wide; ¹⁸⁶ its position was expressed in a resolution, which

¹⁸⁴ Except for the Italian lire and the Irish punt which began with a margin of 6% around their respective bilateral rates and the pound sterling which stayed out.

¹⁸⁵ J.A. Usher, *The Law of Money and Financial Services in the European Community* (Clarendon Press, 1994), 141.

¹⁸⁶ European Council, Resolution on the establishment of an exchange-rate mechanism in the third stage of economic and monetary union, paragraph 1.7, Annex II of the

from the formal standpoint is not legally binding.¹⁸⁷ On the basis of precedent and practice, however, it is clear that political commitment, credibility and trust far outweigh a lack of legally binding force.

Third, does Article 2 of the Protocol apply to potential candidates for EMU which are not part of the current European Monetary System (EMS)? The German Finance Minister Theo Waigel reportedly asserted that the UK and Sweden could not participate in the common currency, because they were not part of EMS so could not meet the criteria. To this, the Swedish Finance Minister Erik Asbrink replied that the decisive factor was the stability of the currency, not the length of participation in the EMS. Diplomatically cutting the Gordian knot between the legalistic and substantive positions, Commissioner Guy de Silguy reportedly 'did not take an explicit position on the quarrel, but on the substance of the issue, sided with the Swedish Minister, saying that, in all the Maastricht criteria, what counts is "sustainable stability" of the result obtained'.¹⁸⁸

Fourth, the most controversial legal ambiguity concerns the excessive deficit criterion¹⁸⁹. The Maastricht Treaty requires Member States to avoid excessive government deficits.¹⁹⁰ The Commission is responsible for monitoring Member States' budgetary performance.¹⁹¹ It must in particular examine compliance with budgetary discipline on the basis of the following criteria (once again, the ambiguities are emphasised):¹⁹²

(a) whether the ratio of the planned or actual government deficit to gross domestic product exceeds a reference value, unless

Presidency Conclusions, European Council Amsterdam Summit, 16 June 1997, published in *Europe Documents* No. 2043, Saturday 21 June 1997, pp 5-7 at p 6. It is further expressly stated in paragraph 1.8 that, if closer links are allowed between the euro and other currencies in the exchange-rate mechanism, the existence of such links, particularly if it implied narrow fluctuation bands, would be without prejudice to the interpretation of the exchange-rate criterion in Article 109j EC.

¹⁸⁷ Similarly, the original (and current) EMS was created in 1979 by a European Council resolution: see Resolution of the European Council of 5 December 1978, (1978) 12 *EC Bulletin*, pt. 1.1.11, The operating procedures were laid down by an Agreement between the central banks of the Member States of 13 March 1979, revised version in (1989) *Compendium of Community Monetary Texts* p 50. For further discussion, see J.A. Usher, *The Law of Money and Financial Services in the European Community* (Clarendon Press, 1994), 139-142. EMS 2 has recently been established in the same way; see the preceding footnote.

¹⁸⁸ *Agence Europe* No. 6975 (n.s.), Friday 16 May 1997 p 6 (original emphasis omitted).

¹⁸⁹ Expressed in Article 2 of the Protocol on the convergence criteria.

¹⁹⁰ Art. 104c(1).

¹⁹¹ Art. 104c(2), first paragraph.

¹⁹² Art. 104c(2), first paragraph (emphasis added).

- either the ratio has declined **substantially** and **continuously** and reached a level that comes **close** to the reference value;
 - or, alternatively, the excess over the reference value is only **exceptional** and **temporary** and the ratio remains **close** to the reference value;
- (b) whether the ratio of government debt to gross domestic product exceeds a reference value, unless the ratio is **sufficiently diminishing** and approaching the reference value at a **satisfactory** pace.

The reference values are specified in a Protocol on the excessive deficit procedure.¹⁹³ According to the Protocol, the reference values are 3% for the ratio of the planned or actual government deficit to gross domestic product at market prices; and 60% for the ratio of government debt to gross domestic product at market prices.¹⁹⁴

Despite their appearance, the excessive deficit criteria are not carved in stone. On the contrary, their interpretation has been the subject of almost continuous controversy. The lawyer steeped in legal realism may perhaps take comfort from two points.

The first point stems from the Treaty itself. The Council¹⁹⁵ is to confirm which Member States qualify for EMU. It is to do so according to procedures laid down by the Treaty.¹⁹⁶ So far as the excessive deficit criterion is concerned, the key provision would appear to be Article 104c(6). It provides that (again, emphasising the ambiguity):

The Council shall, acting by a qualified majority on a recommendation from the Commission, and having considered any observations which the Member State concerned may wish to make, decide after **an overall assessment** whether an excessive deficit exists.¹⁹⁷

The scope for discretion, in other words for negotiation and compromise, both significant features of EU legal culture,¹⁹⁸ is obvious.

The second point is more recent in vintage. At the Ecofin Council meeting on 9 June 1997, the German Finance Minister Waigel

¹⁹³ Art. 104c(1), second paragraph.

¹⁹⁴ Article 1, Protocol on the excessive deficit procedure, OJ 31.8.92 L224/120.

¹⁹⁵ Meeting in the composition of Heads of State and Government: Art. 109j(4) EC.

¹⁹⁶ See, in particular, Arts. 109j(4), which refers to Art. 109j(1) and (2), the first of which refers in turn to Art. 104c(6).

¹⁹⁷ Art. 104c(6) EC.

¹⁹⁸ See F. Snyder, 'General Course on European Community Law: Constitutional Law of the European Union', in Academy of European Law (ed), *Collected Courses of the Academy of European Law, Volume VI, Book* (Kluwer, 1998), pp. 41-155.

confirmed that Germany wanted the convergence criteria to be strictly interpreted. To this well-known position, Jean-Claude Juncker, the Prime Minister and Finance Minister of Luxembourg, and the current President of the European Council, gave a reply. As reported in *Agence Europe*, he explained that there would not be "strict interpretation of **criteria** but strict interpretation of **the Treaty**" (emphasis added). He added that, in the Treaty there is "a margin of assessment which should be used to advantage", which does not mean "diluting the criteria"....¹⁹⁹ This would seem to confirm my reinterpretation of Jacques Rueff...

Two other general points need to be made about the convergence criteria. First, do they make sense, and if so, according to what standards? Many economists consider the convergence criteria to be arbitrary numbers, if not undesirable and ineffective.²⁰⁰ This point goes to the question of the specific criteria. With regard to the utility of criteria in general, however, Winkler argues persuasively that the convergence criteria serve several useful purposes. They express valid concerns regarding risks in respect of price stability, economic convergence, and putatively shared values of economic culture, and, I would add, legal culture. They seek to reconcile conflicting interests, in particular by integrating the demands of the Bundesbank and Germany. They serve 'as an entry barrier or a screening device under incomplete information'. They signal preferences or even induce the revelation of preferences. Finally, they indicate the past and present 'stability culture' of different countries.²⁰¹ The last, as already noted, is not simply a matter of political or economic culture but also, within an EU/EC still marked profoundly by its original economic orientation, an extremely

¹⁹⁹ *Agence Europe* No. 6991 (n.s.), Monday/Tuesday, 9/10 June 1997, p 8. For a similar conclusion, see Michael Artis, 'The Maastricht Road to Monetary Union' (1992) 30 *Journal of Common Market Studies*, pp 299-309; Giorgia Giovannetti and Ramon Marimon, *A Monetary Union for a Heterogeneous Europe* (European University Institute, RSC No. 95/17, 1995), p 39; Patrick Artus, 'Les critères de convergence avant l'Union monétaire: Perspectives et problèmes', (1996) 36 *Revue de l'Economie Financière* 57-68 at 67.

²⁰⁰ See for example B. Winkler, 'Towards a Strategic View on EMU: A Critical Survey', (European University Institute, Working Paper RSC No. 95/18, 1995), pp 12, 15; Giorgia Giovannetti and Ramon Marimon, 'A Monetary Union for a Heterogeneous Europe' (European University Institute, Working Paper RSC No. 95/17, 1995), p 50, who point out that the criteria are based on economic conditions in the late 1980s and may not be credible in different circumstances..

²⁰¹ B. Winkler, 'Towards a Strategic View on EMU: A Critical Survey' (European University Institute, Working Paper RSC No. 95/18, 1995), pp 13-15; the quotation is from p 15.

significant element in the emerging EU legal culture which has an impact far beyond the domain of EMU.

A second general point is that, irrespective of their merits as entry barriers to EMU, the convergence criteria are ill-adapted to serve as operating rules for EMU.²⁰² Elaborated so as to reflect economic conditions during a specific period, they may not be appropriate to guide economic policy coordination in different circumstances. This may be especially the case for the 'ins' under conditions of a single currency, or even for the 'outs' confronted with the 'ins' ' single currency. Nevertheless, as shown later, these criteria will continue to guide EMU members even during the third stage of EMU. It should also be noted, however, that the Treaty does not appear to provide any means for Member States to leave EMU, or for them to be ejected from EMU, even though they may be sanctioned by political measures taken by other Member States²⁰³ or by the Court of Justice in an action brought against their central banks by the European Central Bank.²⁰⁴

(D) POLICY INSTRUMENTS AND LEVELS OF GOVERNANCE

The most profound legal issues in respect of EMU, in addition to its legitimacy, concern the relationship between policy instruments and levels of governance. We can understand these issues most easily by first identifying three aspects of public policy, and then factoring them into the ways in which EMU changes distribution of power in the EU system of multilevel governance.

Public policy is usually deemed to encompass three functions: the allocation of resources, stabilisation, and redistribution.²⁰⁵ The meanings of the first and third functions are clear; the second function, stabilisation, the second function, is oriented to such objectives as price

²⁰² See Giorgia Giovannetti and Ramon Marimon , 'A Monetary Union for a Heterogeneous Europe' (European University Institute, Working Paper RSC No. 95/17, 1995), pp 29-30.

²⁰³ As to the Stability Pact and accompanying regulations, see *infra*..

²⁰⁴ See Art. 180(d) EC [Art. 237(d) Amsterdam Treaty].

²⁰⁵ These functions were identified by J.M. Buchanan, *The Demand and Supply of Public Goods* (Rand McNally, Chicago, 1968) and R.A. Musgrave and P. Musgrave, *Public Finance in Theory and Practice* (McGraw-Hill, New York, 1976). Willem Molle adds a fourth, namely external relations: see Willem Molle, *The Economics of European Integration: Theory, Practice, Policy* (Dartmouth, Aldershot, 3rd edition), relevant page in first edition are 27-28. See also Jacques Pelkmans, *European Integration: Methods and Economic Analysis*(Longman, 1997) pp 265-306. Of course, these functions need not be - and typically are not - all performed only by the state: see Robin Murray, 'The Internationalization of Capital and the Nation State', (1971) 67 *New Left Review*84.

stability, economic growth, and employment. In order to achieve its objectives, stabilisation typically involves recourse to fiscal policy (such as taxation and public expenditure) and monetary policy (such as exchange rates, interest rates, and money supply). Redistribution usually entails mainly the use of fiscal policy.

In the EU structure of multilevel governance, these different public policy functions may be assigned to the EC or the Member States (or sometimes other levels of government, which are less directly relevant here). The evolution of the legal framework of EMU since the early 1960s, discussed earlier, has already altered the level of governance at which some of these functions, or aspects of them, are performed. The third stage of EMU will however have further dramatic consequences. The power and responsibility regarding domestic monetary policy and exchange rate policy will be transferred from the national level to the EC level, while the Member States' powers in respect of fiscal policy will be substantially reduced. From the perspective of Member States, the loss of these national policy instruments constitutes macroeconomic losses. Against them in the balance of EMU must be weighed what are essentially microeconomic benefits, such as a reduction in transaction costs and the elimination of exchange rate risks, as well as the possibility of an internationally stronger currency.²⁰⁶ The resulting balance, in the words of one distinguished economist, 'compares largely unquantifiable gains from greater microeconomic efficiency in the functioning of money as a medium of exchange and unit of account with more tangible losses in the authorities' ability to conduct macroeconomic demand management'.²⁰⁷

The extent to which these power shifts matter, and to whom, is highly controversial. It is useful to emphasise two contrasting but interrelated perspectives, first that of political economy, the other that of constitutional law.

²⁰⁶ For a survey, see European Commission, *One Market, One Money: An Evaluation of the Potential Benefits and Costs of Forming an Economic Union* European Economy, No. 44, 1990, pp 63-84. For an evaluation, see Charles A.E. Goodhart, 'The Political Economy of Monetary Union', in Peter B. Kenen (Ed),: *Understanding Interdependence: The Macroeconomics of the Open*(Princeton University Press, 1995, pp 458-460.

²⁰⁷ Charles A.E. Goodhart, 'The Political Economy of Monetary Union', in Peter B. Kenen (Ed),: *Understanding Interdependence: The Macroeconomics of the Open* (Princeton University Press, 1995, p 452, who adds that 'Neither the benefits nor the costs appear to be large'.

From the standpoint of political economy, the effects of the reallocation of power will depend fundamentally on two factors. The first is the incidence and impact of major unanticipated political or economic disturbances, of either internal or external origin or both, notably their severity and whether their impact is symmetrical or asymmetrical, either within a Member State or across the EU as a whole. The second is the efficacy of existing policy instruments to deal with these shocks. Such instruments may be either those at national level which can be used in place of control of the exchange rate or those at EC level.²⁰⁸

Unanticipated shocks are by definition unforeseeable, though the same is not entirely true of the incidence of such shocks as may occur.²⁰⁹ But for the participants in the single currency, their instruments for dealing with shocks will be limited to reliance on the market, interventions in the market, in particular for labour, or fiscal policy. Since the level of government expenditure is narrowly constrained by the convergence criteria, this means that the main burden for adjustment rests with labour market measures or taxation. So far, the unemployment problem in most Member States has proved especially intractable, and the labour market in Europe is far more rigid than in roughly comparable continental systems. Most fiscal functions oriented toward stabilisation or redistribution in the EC are currently taken at national level,²¹⁰ but in the absence of substantial public expenditure tax

²⁰⁸ See, e.g., Charles A.E. Goodhart, 'The Political Economy of Monetary Union', in Peter B. Kenen (Ed),: *Understanding Interdependence: The Macroeconomics of the Open* (Princeton University Press, 1995, pp 460-461; B. Winkler, *Towards a Strategic View on EMU: A Critical Survey* (European University Institute, working paper RSC 95/18, 1995), pp 3-4; Stephen Clarkson, 'Perché No? Qualms about Currency Union from over the Sea' (Paper presented at the Workshop The Political and Institutional Deficits of the European Integration Process, European University Institute, 30-31 May 1997), pp 5-6. Instruments which are alternatives to a floating exchange rate include, for example, types of fiscal policy such as tax, microeconomic tools to the extent not prohibited by the WTO agreements, local-level instruments, or reliance on the market in the form of wage flexibility, labour mobility, or foreign capital: see Stephen Clarkson, 'Perché No? Qualms about Currency Union from over the Sea' (Paper presented at the Workshop The Political and Institutional Deficits of the European Integration Process, European University Institute, 30-31 May 1997 1997, pp 5-8.

²⁰⁹ The impact of shocks depend in part on the degree of openness of the economy concerned, its trade patterns, and the commodity composition of its imports and exports.

²¹⁰ This point is emphasised by Goodhart, Charles A.E. Goodhart, 'The Political Economy of Monetary Union', in Peter B. Kenen (Ed),: *Understanding Interdependence: The Macroeconomics of the Open*(Princeton University Press, 1995), p 466, who also argues that a clear distinction should be drawn between stabilisation and redistribution, with the former to be emphasised in the case of asymmetric shocks and the latter in the case of anticipated regional divergence. The problem remains, however, of asymmetric shocks which have important regional effects. As to national

policy alone may prove insufficient. The danger is that if both labour market and fiscal measures prove ineffective, EMU could result in the divergence, not convergence, of participating states' economies.

Such a scenario raises fundamental issues of EU institutional design and constitutional law. EMU removes from its Member State participants the key instrument of national exchange rate policy and limits their recourse to fiscal policy in the form of public spending. This is the one of the aims of the convergence criteria, the Stability Pact, and the convergence programmes. EMU also prohibits Member States from making use of overdraft facilities with the European Central Bank (ECB) or national central banks or from offering debt instruments for purchase by the ECB or national central banks.²¹¹ It also confers on the ECB the exclusive right to authorise the issue of bank notes within the Community.²¹² It limits the access to capital markets of Member States with an excessive budget deficit.²¹³ At least one author has suggested that technically the European System of Central Banks could come to the rescue of a participating Member State in the event of economic shocks,²¹⁴ but such an interpretation of the Treaty may stretch the bounds of political feasibility.

Given these parameters, there is a real problem that existing political and legal structures may not be adequate or appropriate for performing the necessary economic functions. First, EMU fails to establish the framework for a sufficiently strong fiscal policy at the EU level of governance.²¹⁵ Fiscal policy remains mainly at the national level. Against the background of the weak sanctions provided by Article 103 EC, however, Goodhart suggests that either there will be little effective coordination of national fiscal policies or, if there is, policymaking will

fiscal systems, see European Commission, 'La fiscalité dans l'Union européenne: Rapport sur l'évolution des systèmes fiscaux présenté par la Commission' (COM(96) 546 final, (1992) 2 *Revue du Marché Unique Européen* 181-191; European Commission, Directorate-General for Economic and Financial Affairs, *Towards Greater Fiscal Discipline*, European Economy, Reports and Studies, No. 3, 1994 (Luxembourg, 1995).

²¹¹ Art. 104(1) EC.

²¹² Art. 105a(1) EC.

²¹³ Art. 104c(11), second indent, EC provides a Member State with an excessive deficit may be required to publish additional information, to be specified by the Council before issuing bonds and securities.

²¹⁴ D.R.R. Dunnett 'Legal and Institutional Issues affecting Economic and Monetary Union in David O'Keefe and Patrick Twomey (eds) *Legal Issues of the Maastricht Treaty* (Chancery Law Publishing, 1994), p 146.

²¹⁵ See also D.R.R. Dunnett 'Legal and Institutional Issues affecting Economic and Monetary Union in David O'Keefe and Patrick Twomey (eds) *Legal Issues of the Maastricht Treaty* (Chancery Law Publishing, 1994), p 145.

in fact be transferred to the European level of governance.²¹⁶ It is open to question, however, whether it will be possible to retain fiscal functions at national level in the context of a single currency, when decisions about monetary policy will be taken at European level and decisions about exchange-rate policy will be taken by national governments acting jointly.²¹⁷ In this case the EC/EU institutional architecture for making fiscal policy decisions, in particular the respective roles of the Council and the European Parliament, will be of crucial importance.²¹⁸

This raises a second issue of constitutional significance. In the absence of further political and legal development, there is a serious risk of a major institutional gap at the heart of European integration. The creation of supranational monetary institutions has not been accompanied by the establishment of institutions for making decisions about political priorities and choices among competing social values. This point can be illustrated by referring to the debate about the Stability Pact.

Few aspects of EMU have been more controversial recently than the so-called 'Stability Pact'²¹⁹. From the legal standpoint, we need to refer to the Stability and Growth Pact, the Resolution on Growth and Employment accompanying it, and the legal instruments for putting it into effect. It began when, before the December 1995 Madrid Summit, Germany proposed an agreement intended to maintain fiscal discipline.²²⁰ In legal terms, the agreement would be (and is) designed to

²¹⁶ Charles A.E. Goodhart, 'The Political Economy of Monetary Union', in Peter B. Kenen (Ed.), *Understanding Interdependence: The Macroeconomics of the Open* (Princeton University Press, 1995), p 467.

²¹⁷ See Charles A.E. Goodhart, 'The Political Economy of Monetary Union', in Peter B. Kenen (Ed.), *Understanding Interdependence: The Macroeconomics of the Open* (Princeton University Press, 1995) p 465. A former member of the Delors Committee has written that this strategy 'may not be necessarily unworkable or naive, but it is optimistic': Niels Thygesen, 'Why is Economic and Monetary Union an Important Objective for Europe', (1994) 14 *International Review of Law and Economics* 133-145 at p 139.

²¹⁸ Robert P. Inman and Daniel L. Rubinfeld, 'The EMU and Fiscal Policy in the New European Community', (1994) 14 *International Review of Law and Economics* 147-161 conclude that fiscal policies capable of ensuring against asymmetric shocks can be enforced if decision-making is centralised, e.g. within the Council, but that this is much less likely to be the case if decision-making is decentralised, e.g. within the European Parliament..

²¹⁹ See also Pierre Maillet, 'Le Pacte de Stabilité et de Croissance: Portée et limites du Compromis de Dublin', (1997) 404 *Revue du Marché Commun et de l'Union européenne* 5-12; Michael J Artis and Bernhard Winkler, 'The Stability Pact: Safeguarding the Credibility of the European Central Bank', Discussion Paper No. 1688, Centre for Economic Policy Research, August 1997.

²²⁰ See *Agence Europe*, 9 November 1995, No 6601, p 5.

ensure that Member States respected their obligation to avoid an excessive deficit,²²¹ as defined in the Treaty²²² and its accompanying Protocol.²²³

As endorsed by the European Council in Madrid, and reiterated in a Commission report to the June 1996 Florence Summit, the agreement was to be based on the principles that it should

- be achieved in the context of and according to the procedures of the Treaty;
- be agreed at the level of the Union, even though its full application would only concern the Member States participating in the single currency, and
- confirm that the requirements for participation in EMU, either in the first group or at a later date, should in no way be changed.²²⁴

It would include a kind of 'early warning system, based upon the intensification of existing practice with convergence programmes and multilateral surveillance exercise'.²²⁵ Participating Member States would submit 'stability programmes. Secondary legislation based on Article 103(5)²²⁶ would define the basic elements of these programmes and lay down the steps of surveillance by the Union. If a Member State ran an excessive deficit, the excessive deficit procedure would come into play.²²⁷ Secondary legislation based on Article 104c(14)²²⁸ would set out the time limits for the various steps of the procedure, clarify the conditions for imposing sanctions, and define the type, scale and timing of sanctions.

²²¹ The obligation is stated in Art. 104c(1) EC.

²²² Art. 104c(2)(a) EC.

²²³ Protocol on the excessive deficit procedure, Art. 1, first indent, OJ 31.8.92 L224/120.

²²⁴ European Commission, 'Preparation of Economic and Monetary Union: A Review of the Situation (Communication by the Commission to the European Council)', *Europe Documents*, No. 1992, 4 July 1996, at 3.

²²⁵ *Id.*

²²⁶ This Article provides *inter alia* that the Council, acting in accordance with the procedure referred to in Article 189c, may adopt detailed rules for the multilateral surveillance procedure.

²²⁷ This procedure is laid down in Arts. 104c(7)-(14) EC and in the Protocol on the excessive deficit procedure, OJ 31.8.92 L224/120.

²²⁸ This Article provides *inter alia* (in the second paragraph) that the Council shall, acting unanimously and after consulting the European Parliament and the ECB, adopt the appropriate provisions which shall then replace the Protocol on excessive deficit procedure.

As directed by the European Council, and following further work,²²⁹ the Commission submitted a report to the December 1996 European Council in Dublin.²³⁰ At 3 am on Thursday 12 December 1996, after eleven hours of discussion and numerous bilateral meetings, the Ecofin Council reached agreement on a Stability and Growth Pact. It reported to the European Council, having reached a conclusion on all matters except for the precise statistical definition of a serious recession, which would warrant a public deficit greater than the 3% of GDP ceiling. The Dublin European Council on 13-14 December welcomed the agreement. It requested Ecofin to establish a working group to examine two accompanying Commission proposals for regulations, one on the strengthening of the surveillance and coordination of budgetary positions, and the other on speeding up and clarifying the implementation of the excessive deficit procedure.²³¹ It also invited the Ecofin Council to prepare a draft Resolution on the Stability and Growth Pact to be adopted by the European Council in June 1997.²³²

After the Dublin Summit French President Jacques Chirac 'explained that there was no difference of opinion between the Fifteen' on the 'European economic government' that he would like to see in place. 'He said that, in a form still to be determined, the members of the Council and of the European Council whose countries are within the euro will represent an authority to confront the European Central Bank and it is at this level that there will be dialogue':²³³ However, not only were these matters a subject of disagreement between Germany and France: they and EMU in general was extremely controversial in

²²⁹ See *Agence Europe* No. 6805 (n.s.)m Friday, 6 September 1996, p 4.

²³⁰ Commission proposal for a Council Regulation on the strengthening of the surveillance and co-ordination of budgetary positions; proposal for a Council Regulation on speeding up and clarifying the implementation of the excessive deficit procedure, COM(96)496 final, OJ 6.12.1996 C368/9 - 96/0247 (SYN) & 96/0248 (CNS), OJ 6.12.1996 C368/9.

²³¹ For the subsequent version of these proposals, see Commission of the European Communities, Amended proposal for a Council Regulation (EC) on the strengthening of the surveillance and coordination of budgetary policies (presented by the Commission pursuant to Article 189a(21) of the EC-Treaty), COM(97) 116 final - 96/0247 (SYN), Brussels 19.3.97; Commission of the European Communities, Amended proposal for a Council Regulation (EC) on speeding up and clarifying the implementation of the excessive deficit procedure (presented by the Commission pursuant to Article 189a(2) of the EC-Treaty), COM(97) 117 final - 96/0248 (CNS), Brussels 19.3.97.

²³² *Agence Europe* No. 6875 (Special Edition), Sunday 15 December 1996, p 3. For further details, see the Report by the ECOFIN Council to the European Council, 'The Preparations for Stage 3 of EMU', *Europe Documents* No 2015/16, 18 December 1996.

²³³ *Agence Europe* No. 6875 (Special Edition), Sunday 15 December 1996, p 3.

France. Partly as a result, after Chirac called for a spring election, his party suffered severe losses, and he eventually appointed the Socialist Lionel Jospin as Prime Minister. This political 'cohabitation' immediately altered the terms of the debate.

Since its inception as a German proposal, the Stability Pact had changed title, but its contents remained overwhelmingly devoted to stability, not growth. This point was noted by many commentators and participants in the political process.²³⁴ Following the French elections, former Commission President Jacques Delors proposed at the congress of the Party of European Socialists that the Stability Pact should be "complemented" with a protocol setting out the conditions in which MS "will coordinate their economic policies with a view to genuine convergence of their growth and employment policies".²³⁵ A resolution by the European Trade Union Federation (ETUC), addressed to the forthcoming Amsterdam European Council, called for the Treaty to be applied so that transition to the single currency was accompanied by effective coordination of economic policies.²³⁶

Then the new French Minister of Economy and Finance, Dominique Strauss-Kahn, dropped a bombshell. He told the Ecofin that France's new government could not subscribe to the Pact for Stability and Growth: it needed to evaluate and review the Pact in order to achieve a better balance between budgetary discipline and employment policy. He proposed, or at least floated, two potential developments. On the one hand, more emphasis should be given to Articles 102a and 103 EC; these principles on economic coordination should be stated clearly in the Pact. On the other hand, he reiterated the long-standing French concern about the political nature of monetary policy, saying that 'there needs to be a sort of political responsibility, capable of ensuring coordination of economic policies', 'without placing the ECB back into question'.²³⁷

The first proposal received wider support, but the second did not. The Dutch Foreign Minister and Council President, Gerrit Zalm,

²³⁴ For example, MEP Christodoulou (Greek EPP), presenting reports to the European Parliament Plenary Session, Wednesday 28 May 1997, who also remarked on the rigid and mechanical nature of the Pact: *Agence Europe* No. 6983 (n.s.) Thursday 29 May 1997 p 10. In fact, virtually the only direct reference to growth was contained in paragraph 18, which noted that 'Sound government finances ... are an essential condition for sustainable and non-inflationary growth and a high level of employment'.

²³⁵ *Agence Europe* No. 6990 Saturday 7 June 1997 p 3 (original emphasis omitted).

²³⁶ *Agence Europe* No. 6991 (n.s.) Monday/Tuesday, 9/10 June 1997, p 4.

²³⁷ *Agence Europe* No. 6991 (n.s.) Monday/Tuesday, 9/10 June 1997 p 6-7; the direct quotations from Minister Strauss-Kahn are from p 7.

interpreted the reaction to the former as one of 'considerable enthusiasm' for incorporating Articles 102a and 103 into a protocol attached to the Pact. However, the German Permanent Representative, Mr von Kiaw made it clear that while his Government was 'prepared to examine closer coordination of economic policies', it was 'against an economic government that would challenge the independence of the European Central Bank'.²³⁸ Commission President Santer, speaking at the European Parliament, referred to a 'pact for growth, creator of jobs'. Noting that Ecofin had 'recognised the need for EMU to walk on its two feet, monetary and economic', he emphasised that the Union should use the Article 103 procedures to their fullest extent. Later, in a press conference, he noted that the Pact itself started life as a European Council resolution, then was complemented by legally binding regulations. However, he rejected any suggestion that the Union needed 'economic government'. In his view, 'our generation will see neither economic government nor political government' in Europe²³⁹.

Work then started on a draft resolution to be submitted to the Amsterdam European Council. It was to consist of a single text, dealing with both economic coordination and employment. As *Agence Europe* pointed out, 'Subsidiarity will be fully respected. There is no question of Member States giving up their national economic policies, but simply of better coordination at European level....'²⁴⁰ There followed a flurry of meetings, in particular between senior Commission officials and senior French politicians. The Commission then confirmed that the outcome would probably be a European Council Resolution, which would be 'counterpart' of the previously envisaged Resolution on the Stability and Growth Pact.²⁴¹ By this time the fate of these Resolutions was intertwined with that of the 'Maastricht II' Treaty, the Amsterdam Treaty.

The European Summit at Amsterdam reached agreement on both matters. In addition to the new Treaty, to be signed in Amsterdam in October 1997, it adopted a Stability Pact and Growth Pact, a Resolution on Growth and Employment, and various other texts on the third stage of

²³⁸ *Agence Europe* No. 6991 (n.s.), Monday/Tuesday, 9/10 June 1997, p 6; see also *Agence Europe*, No. 6992 (n.s.), Wednesday, 11 June 1997, pp 4-5..

²³⁹ His view was that 'We do not wish to have a Keynesian policy and launch major programmes': see *Agence Europe* No. 6993 (n.s.), Thursday, 12 June 1997, pp 2, 6.

²⁴⁰ *Agence Europe* No. 6993 (n.s.), Thursday, 12 June 1997, pp 6-7.

²⁴¹ *Agence Europe* No. 6994 (n.s.), Friday, 13 June 1997, p 7.

EMU.²⁴² Here I focus on the Stability Pact and the other texts directly related to it.

The Stability and Growth Pact is expressed as a European Council Resolution, together with two Council regulations. The Resolution is not legally binding but provides 'political guidance', both generally and, in particular, regarding the context and the implementation of the two regulations which of course have legal force. The Resolution is stated to be consistent with the Treaty, which however it amplifies and interprets ('gives precision to') on numerous points. To be fully effective, it requires, among other things, the enactment of various Council regulations, as well as the eventual modification of the Financial Regulation before the end of 1998.. The Amsterdam European Council 'invited' the Council to adopt these without delay.²⁴³: an invitation which is difficult to refuse, given the hierarchical relationship between the two Councils and their respective composition

The European Council Resolution on the Stability and Growth Pact provides as follows:²⁴⁴

I. Meeting in Madrid in December 1995, the European Council confirmed the crucial importance of securing budgetary discipline in stage three of Economic and Monetary Union (EMU). In Florence, six months later, the European Council reiterated this view and in Dublin, in December 1996, it reached an agreement on the main elements of the Stability and Growth Pact. In stage three of EMU, Member States shall avoid excessive general government deficits: this is a clear Treaty obligation (fn re non-application to UK under Art 5 of Protocol 11, and re obligation under Art 109e(4) on continued application to UK to endeavour to avoid excessive deficits). The European Council underlies the importance of safeguarding sound government finances as a means to strengthening the conditions for price stability and more sustainable growth conducive to employment creation. It is also necessary to ensure that national budgetary policies support stability oriented monetary policies. Adherence to the objective of sound budgetary positions close to balance or in surplus will allow all Member States to deal with normal

²⁴² *Agence Europe* No. 6998 (n.s.), Thursday 19 June 1997, p 3.

²⁴³ Presidency Conclusions, Amsterdam European Council, 16-17 June 1997, *Europe Documents*, No. 2041/42, Friday 20 June 1997.

²⁴⁴ Resolution of the European Council on the Stability and Growth Pact, Annex I of Presidency Conclusions, Amsterdam European Council, 16-17 June 1997, in *Europe Documents*, No. 2043, Saturday, 21 June 1997, pp 2-3.

cyclical fluctuations while keeping the government deficit within the 3 percent of GDP reference value.

II Meeting in Dublin in December 1996, the European Council requested the preparation of a Stability and Growth pact to be achieved in accordance with the principles and procedures of the Treaty. This Stability and Growth pact in no way changes the requirements for participation in stage three of EMU, either in the first group or at a later date. Member States remain responsible for their national budgetary policies, subject to the provisions of the Treaty; they will take the necessary measures in order to meet their responsibilities in accordance with those provisions.

III. The Stability and Growth pact, which provides both for prevention and deterrence, consists of this Resolution and two Council Regulations, one on the strengthening of the surveillance of budgetary positions and the surveillance and coordination of economic policies and another on speeding up and clarifying the implementation of the excessive deficit procedure.

IV. The European Council solemnly invites all parties, namely the Member States, the Council and the Commission, to implement the Treaty and the Stability and Growth pact in a strict and timely manner. This resolution provides firm political guidance to the parties who will implement the Stability and Growth pact. To this end, the European Council has agreed upon the following guidelines

The Member States

1. commit themselves to respect the medium-term budgetary objective of close to balance or in surplus set out in their stability or convergence programmes and to take the corrective budgetary action they deem necessary to meet the objectives of their stability or convergence programmes, whenever they have information indicating actual or expected significant divergence from those objectives;
2. are invited to make public, on their own initiative, the Council recommendations made to them in accordance with Article 103(4);
3. commit themselves to take the corrective budgetary action they deem necessary to meet the objectives of their stability or convergence programmes once they receive an early warning in the form of a Council recommendation issued under Article 103(4);
4. will launch the corrective budgetary adjustments they deem necessary without delay on receiving information indicating the risk on an excessive deficit;

5. will correct excessive deficits as quickly as possible after their emergence; this correction should be completed no later than the year following the identification of the excessive deficit, unless there are special circumstances;

6. are invited to make public, on their own initiative, recommendations made in accordance with Article 104c(7); (2/3)

7. commit themselves not to invoke the benefit of Article 2 paragraph 3 of the Council Regulation on speeding up and clarifying the excessive deficit procedure unless they are in severe recession; in evaluating whether the economic downturn is severe, the Member States will, as a rule, take as a reference point an annual fall in real GDP of at least 0,75%.

The Commission

1. will exercise its right of initiative under the Treaty in a manner that facilitates the strict, timely and effective functioning of the Stability and Growth Pact;

2. will present, without delay, the necessary reports, opinions and recommendations to enable the adoption of Council decisions under Article 103 and Article 104c; this will facilitate the effective functioning of the early warning system and the rapid launch and strict application of the excessive deficit procedure;

3. commits itself to prepare a report under Article 104c(3) whenever there is the risk of an excessive deficit or whenever the planned or actual government deficit exceeds the 3 per cent of GDP reference value, thereby triggering the procedure under Article 104c(3);

4. commits itself, in the event that the Commission considers that a deficit exceeding 3% of GDP is not excessive and this opinion differs from that of the Economic and Financial Committee, to present in writing to the Council the reasons for its position;

5. commits itself, following a request from the Council under Article 109d, to make, as a rule, a recommendation for a Council decision on whether an excessive deficit exists under Article 104c(6).

The Council

1. is committed to a rigorous and timely implementation of all the elements of the stability and growth pact in its competence; it will take the necessary decisions under Article 103 and Article 104c as quickly as is practicable;

2. is urged to regard the deadlines for the application of the excessive deficit procedure as upper limits; in particular, the Council, acting

under Article 104c(7), shall recommend that excessive deficits will be corrected as quickly as possible after their emergence, no later than the year following their identification, unless there are special circumstances;

3. is invited always to impose sanctions if a participating Member State fails to take the necessary steps to bring the excessive deficit situation to an end as recommended by the Council:

4. is urged always to require a non-interest bearing deposit, whenever the Council decides to impose sanctions on a participating Member State in accordance with Article 104c(11);

5. is urged always to convert a deposit into a fine after two years of the decision to impose sanctions in accordance with Article 104c(11), unless the excessive deficit has in the view of the Council been corrected;

6. is invited to always state in writing the reasons which justify a decision not to act, if at any stage of the excessive deficit or surveillance of budgetary positions procedures the Council did not act on a Commission recommendation, and, in such a case, to make public the votes cast by each Member State.

The detailed implementing provisions for the Pact are contained in two Council regulations.

The first implementing regulation, based on Article 103(5) EC, concerns multilateral surveillance.²⁴⁵ It sets out the rules covering the submission, examination and monitoring of stability programmes and convergence programmes.²⁴⁶ The second implementing regulation, based on Article 104c(14), second subparagraph, EC, concerns speeding up and clarifying the implementation of the excessive deficit procedure.²⁴⁷ Together with Protocol No 5 on the excessive deficit procedure, attached to the Treaty, it constitutes a new set of integrated rules for the application of Article 104c EC, which sets out the excessive deficit procedure.²⁴⁸

²⁴⁵ Council Regulation (EC) 1466/97 of 7 July 1997 on the strengthening of the surveillance of budgetary positions and the surveillance and coordination of economic policies, OJ 2.8.97 L209/1.

²⁴⁶ *Ibid.*, art. 1. These programmes fulfil the function of the presentation of information for purposes of multilateral surveillance, in the terms of Art. 103(3), second paragraph, EC: see Preamble, seventh recital, and arts. 3(1) and 4(1)..

²⁴⁷ Council Regulation (EC) 1467/97 of 7 July 1997 on speeding up and clarifying the excessive deficit procedure, OJ 2.8.97 L209/6.

²⁴⁸ *Ibid.*, Preamble, first recital.

Accompanying the Stability Pact was a European Council Resolution on Growth and Employment. Both the Council Resolution at the origin of the Stability Pact and the Council Resolution on Growth and Employment were political instruments which, taken alone, have no legally binding force. Unlike the Stability Pact, however, the Employment Resolution did not immediately involve any legally binding secondary legislation. It was accompanied by the amendment of the Maastricht Treaty so as to include, in the Amsterdam Treaty, a new Title on employment, with the aim of implementing a coordinated employment strategy by means of the coordination of national employment policies, the use of incentive measures, and the establishment of a committee on employment.²⁴⁹ But it is open to question whether EMU and the Amsterdam Treaty together provide a sufficient legal framework for a strong, coherent EU employment policy. On the one hand, there is substantial doubt about the likelihood of a European-level programme of social protection for workers.²⁵⁰ On the other hand, the reform of the welfare states in Europe has so far, with occasional exceptions, been mainly a concern of national governments.²⁵¹ This points once again to the current political vacuum at the heart of the European Union.

Institutional changes to remedy these deficiencies are likely to be politically unacceptable to many Member States. This applies to the creation of a real fiscal federalism, the development of a stronger EU employment policy, the creation of other EU policies for economic stabilisation,²⁵² or a more active policy of economic redistribution. As the

²⁴⁹ See new Title VI, including Arts. 109n-109r EC. [Arts. 125-129 EC per Amsterdam Treaty]. See also the amendments to Art. B TEU [Art. 2 TEU per Amsterdam Treaty] and Art. 2 EC.

²⁵⁰ See Streeck, Trubek, Bercusson et al, Sciarra on globalisation, M. Rhodes., *A New Social Contract? Globalisation and West European Welfare States* (European University Institute working paper, RSC No. 96/43, 1996); M. Rhodes, 'Globalisation. Labour Markets and Welfare States: A Future of 'Competitive Corporatism'' (European University Institute working paper, RSC No. 97/36, 1997). See also Pierre Guibentif and Denis Bouget, *Minimal Income Policies in the European Union* (Uniao das Mutualidades Portuguesas, 1997).

²⁵¹ See also David Mayes, 'European Economic Cooperation, Economic and Monetary Union, and the Need for a European Social Policy', in P. Kosonen and Pk:k Madsen (eds), *Convergence or Divergence? Welfare States Facing European Integration* (Publications Office of the European Communities, 1995), pp 59-76; Giorgia Giovannetti and Ramon Marimon, 'A Monetary Union for a Heterogeneous Europe' (European University Institute, Working Paper RSC No. 95/17, 1995), pp 8-9

²⁵² 'Virtually no stabilization is achieved through the current federal budget': see: Charles A.E. Goodhart, 'The Political Economy of Monetary Union', in Peter B. Kenen (Ed),: *Understanding Interdependence: The Macroeconomics of the Open* (Princeton University Press, 1995), p 469 ;

Franco-German debate about the Stability Pact shows, there is currently no political agreement in support of such changes to the EU constitution.²⁵³ This is reflected in legal principles, such as the principle of subsidiarity or the legal requirement in Article 199 EC that the EC run a balanced budget. It was encapsulated neatly in a warning given by the Swedish Prime Minister in December 1996 against the possibility that, by leading to fiscal federalism, EMU would transform the EU into a federation, and thus into 'something completely different than the EU the Swedish people, after some agony and a long and trying debate, approved' at the 1994 referendum.²⁵⁴

(E) CONVERGENCE PROGRAMMES

The origins of EMU as an unusual graft combining high politics with 'comitology'²⁵⁵ are mirrored in the novel legal techniques that have been used thus far in its practical governance. We have already seen that the Stability Pact combines a non-legally-binding instrument, a European Council Resolution, in other words 'soft law' at the highest level, with two Council Regulations, both products of Ecofin, that is, highly technical economic regulations rivalled in the Community system only by agricultural measures. Here I focus on another legal instrument, namely convergence programmes. Convergence programmes are the legal and policy instruments for achieving economic convergence, which in theory is a precondition for entry into EMU. But what are

²⁵³ Within the EC... there is not now, or in sight, an agreement that all area inhabitants should have broadly the same menu of benefits and taxes. Indeed there is scarcely accord on minimum standards for the provision of public goods. Insofar as redistribution takes place at all, it occurs through the more covert mechanism of structural, or cohesion, funds, which are themselves subject to a variety of operational problems': Charles A.E. Goodhart, 'The Political Economy of Monetary Union', in Peter B. Kenen (Ed.): *Understanding Interdependence: The Macroeconomics of the Open* (Princeton University Press, 1995), p 468.

²⁵⁴ Swedish Prime Minister Goran Persson, in an editorial published in *Svenska Dagbladet*, quoted in *Agence Europe* No 6883 (n.s.); Monday/Tuesday 30/31 December 1996, p 3. To put it another way, 'Centralising policy ... entails welfare losses to the extent that preferences are heterogeneous': B. Winkler, *Towards a Strategic View on EMU: A Critical Survey* (European University Institute, working paper RSC 95/18, 1995), p 5.

²⁵⁵ That is, 'comitology' in the broad sense of recourse to specialist committees, not in the narrow sense of committees governed by Council Decision 87/373, OJ 13.7.87 L197/33, on the exercise by the Commission of powers delegated to it by the Council. D.R.R. Dunnitt 'Legal and Institutional Issues affecting Economic and Monetary Union in David O'Keeffe and Patrick Twomey (eds) *Legal Issues of the Maastricht Treaty* (Chancery Law Publishing, 1994), p 144 n73 quotes Smit & Herzog, (1982-1992), 3-630.17 to the effect that 'Article 109c of the Treaty bears embarrassing witness to the successful effort of unelected and yet not independent officials to constitutionalise their position of power'.

convergence programmes, what is their legal basis, are they legally binding, and what if anything ensures that they will be put into practice?

The expression 'convergence programmes' refers to reports prepared by the Member States regarding their macro-economic situation, in particular (but not only) inflation rate and public spending. Such programmes predate the Treaty on European Union.²⁵⁶ The first phase of EMU began on 1 July 1990. In preparation, Council Directive 90/141 of 12 March 1990²⁵⁷ enabled the Council to undertake twice-yearly multilateral surveillance of all aspects of Member States' short-term and medium-term economic policy. A political agreement at an informal Ecofin Council meeting on 10-11 May 1991, anticipating the Maastricht Treaty,²⁵⁸ called for the more systematic presentation of reports prepared for this purpose by the Member States. This agreement was consecrated by the 26-27 June 1991 Luxembourg Summit, which also noted the intention of various governments to present a report. On 11 November 1991 the first report was presented to the Ecofin Council by Italy. It was followed by reports from Ireland, Germany, Portugal, Spain, the Netherlands, Belgium, Greece and the United Kingdom.

Convergence programmes thus were already in use before the Maastricht Treaty. Though mandated by Council Decision 90/141, convergence programmes were initially not Community legal instruments, nor were they legally binding. Instead they relied for their efficacy and implementation on administrative and political relations between national governments and Community (and Union) institutions, in particular the Commission and Ecofin. However, they soon became an indispensable element in the multilateral surveillance of Member States' economic policies in the light of the convergence criteria and the Council's broad economic guidelines.²⁵⁹

²⁵⁶ According to Art. 102a(1), which was added to the EEC Treaty by the Single European Act, the Member States were required to cooperate 'In order to ensure the convergence of economic and monetary policies which is necessary for the further development of the Community'. However, it was not until the early 1990s that specific instruments were adopted for this purpose. The remainder of this paragraph is based on J. Closs, G. Reinesch, D. Vignes and J. Weyland, *Le Traité de Maastricht: Genèse, Analyse, Commentaires* (Bruylant, 1993), pp 177-180. They remark that these programmes were initially known as 'crash programmes' (p 179, n 34)..

²⁵⁷ Council Decision 90/141/EEC of 12 March 1990 on the attainment of progressive convergence of economic policies and performance during stage one of economic and monetary union, OJ 24.3..90 L78/23.

²⁵⁸ Namely Art. 109e(2)(a), second indent, as to which see below.

²⁵⁹ As to the broad economic guidelines, see Art. 103(2), (3), (4). See also Commission's recommendation for the Broad Guidelines of the Economic Policies of the Member States and the Community, COM(96) 211 final; Council Recommendation (EC) 96/431

The Maastricht Treaty enlarged and consolidated the range of Community instruments concerned with monetary integration. In respect of convergence programmes, the Treaty required Member States, prior to the beginning of the second stage of EMU on 1 January 1994,²⁶⁰ to adopt, if necessary, with a view to permitting the assessment provided for in subparagraph (b), 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.²⁶¹

The Maastricht Treaty also reinforced the multilateral surveillance procedure, designed as a means of coordinating Member States' economic policies.²⁶² It also created the excessive deficit procedure, intended to ensure fiscal discipline.²⁶³ Though formally distinct, the three procedures all concern budgetary discipline and in practice have tended to be linked.²⁶⁴

Revised convergence programmes have recently been presented by France 1997-2001),²⁶⁵ Germany (1997-2000),²⁶⁶ Ireland²⁶⁷ and Italy (1998-2000).²⁶⁸ We can take the Italian programme as an example. Worked out by the Italian authorities, in conjunction with the Commission services, it provided for structural reforms in four areas: pensions, social

on the broad guidelines of the economic policies of the Member States and of the Community, OJ 18.7.96 L179/46.; Commission's Recommendations for the Broad Guidelines of the Economic Policies of the Member States and the Community, COM(97)168 final:

Commission, Progress report on the implementation of the 1996 Broad Economic Policy Guidelines, COM(97)169 final; Council Recommendation 97/479 on the broad economic guidelines of the economic policies of the Member States and of the Community, OJ 2.8.97 L209/12.

²⁶⁰ As provided by Art. 109e(1) EC.

²⁶¹ Art. 109e(2)(a), second indent, EC.

²⁶² See Arts. 102a and 103 EC. Multilateral surveillance formally began in 1990 and was subsequently governed by Council Decision 90/141/EEC of 12 March 1990 on the attainment of progressive convergence of economic policies and performance during stage one of economic and monetary union, 24.3.1990 L78/3.

²⁶³ Art. 104c EC and the Protocol on the Excessive Deficit Procedure. As to the excessive deficit procedure, see *supra*. Council Decision 90/141, 24.3.1990 L78/23

²⁶⁴ For a more detailed comparison, see Robert Brookes, 'Parliamentary Scrutiny of UK Convergence Programmes: the One that Got Away', (1996) 2 *European Public Law* 437-451 at pp 445-447, 449-450.

²⁶⁵ See *Agence Europe* No. 6936 (n.s.), Monday/Tuesday, 17/18 March 1997, pp 8-9.

²⁶⁶ See *Agence Europe* No. 6936 (n.s.), Monday/Tuesday, 17/18 March 1997, pp 8-9.

²⁶⁷ See *Agence Europe* No. 6991 (n.s.), Monday/Tuesday, 9/10 June 1997, p 8.

²⁶⁸ See *Agence Europe* No. 7002 (n.s.), Wednesday 25 June 1997, p 7; No. 7010 (n.s.), Saturday, 5 July 1997, p 6; No. 7012 (n.s.), Wednesday 9 July 1997, p 8.

security, the civil service, and taxation. Its goals by the year 2000 were a decrease in the budget deficit to 1.8%, a decrease in global public debt to 116.3%, a drop in inflation to 1.5%, a fall in unemployment to 10.4%, and an increase in employment by 0.9%. This was expected to lead to a fall in interest rates, hence a reduction in the debt service burden from 10.8% as of 1997 to 7.28% of GDP and a reduction in the overall fiscal charge to 47.8% of GDP. The flexibility of the labour market and the privatisation of state-owned companies was to continue. The programme in draft form was welcomed by the Commission as 'encouraging'.²⁶⁹

The Ecofin Council²⁷⁰ discussed the Italian programme at its 7 July 1997 meeting. It 'acknowledged with satisfaction the remarkable progress in convergence achieved by Italy, particularly as regards inflation, interest rates and currency stability'. It emphasised the crucial importance of the political commitment behind the programme's budgetary objectives. However, it invited the Italian authorities to consider the budgetary objectives as 'ceilings'. It also pointed out that, while the assumptions on growth and interest rates were reasonable, the evolution of interest rates would depend on low inflation and monetary stability and on successful budgetary structural adjustment. Reform measures should aim in particular at the reduction of the national deficit. Structural reforms were 'most welcome'. Most important were 'the reform of the welfare state,' notably pensions, and of the tax system, especially avoiding revenue shortfalls. On the basis of its discussion, the Council invited the Commission and the Monetary Committee to monitor the implementation of the programme and to report to the Council once concrete budgetary measures were defined in the 1998 Budget Law.²⁷¹

Recently the Commission, at Ecofin's request, assessed the possibility of reinforcing these procedures. It considered that convergence programmes 'have proven effective, and should remain the

²⁶⁹ *Agence Europe* No. 7002 (n.s.), Wednesday 25 June 1997, p 7. The assessment by *Agence Europe* was rather less enthusiastic. While generally positive, it stated that 'The Council should nevertheless stress the absolute need, for the Italian authorities, to stay on this track and respect the objectives they have set themselves paying special attention to reducing social expenditure': *Agence Europe* No. 7010 (n.s), Saturday 5 July 1997, p 6..

²⁷⁰ The Ecofin Council consists of the ministers of economy and finance of the Member States. They constitute the Council for the purposes of EMU matters: see Declaration No. 3 relative to the Third Part, Titles III and IV, of the Treaty establishing the European Community, OJ 29.7.92 C191/98.

²⁷¹ These and other conclusions by the Council are reported in *Agence Europe* No. 7012 (n.s.), Wednesday 9 July 1997, p 8.

pivot of the convergence process'.²⁷² At the same time, however, it underlined the importance of obtaining greater political commitment from the Member States. To this end, it proposed to modify the format of convergence programmes to include:

- a statement of key objectives and time horizon for their achievement;
- assumptions about the macroeconomic environment;
- policy measures to be taken;
- contingency measures in the event of slippage; and
- regular updating and, if necessary, a specific date for submitting a new programme.

The proposal rested on a triangular political and institutional bargain. If a Member State made increased efforts, and if the Commission gave it a positive recommendation, the Ecofin Council would politically endorse the programme. In the institutional jockeying for power which is characteristic of the Community system, this might appear to redound mainly to the benefit of the Commission. Less clear in its implications was the Commission's proposal that Council endorsement would require more effective monitoring, mainly by means of secondary legislation. Monitoring and Ecofin recommendations for corrective action where appropriate were to be the main elements of Community surveillance.

The Commission also proposed that the targets and the recommendations in the broad economic policy guidelines²⁷³ be made more country-specific. Such a procedure would tend to merge more closely the broad economic policy guidelines and the convergence programmes. This could have the effect of narrowing the distinction between economic policy and monetary policy within EMU so far as the locus of decision-making is concerned.²⁷⁴ Thus it might increase the weight of the European Council, Ecofin and the Commission in national economic policy-making. It may also strengthen the partnership

²⁷² Commission Report to the Florence Summit, 'Preparation of Economic and Monetary Union: A Review of the Situation (Communication by the Commission to the European Council), in *Europe Documents* No. 1992, 4 July 1997, p 4.

²⁷³ Formulated by the Council *ex* Article 103(2), first paragraph, and then, on the basis of the Council's report, discussed to a conclusion by the European Council *ex* Article 103(2), second paragraph.

²⁷⁴ For example, see Snyder, 'EMU - Metaphor for European Union? Institutions, Rules and Types of Regulation', in R. Dehousse (ed), *Europe after Maastricht: An Ever Closer Union?* (Law Books in Europe, 1994), 63-99.

between the Commission and national governments, implicating governments in further two-level games and thus raising the stakes in domestic politics, for example in Italy. Furthermore, it may also alter the delicate balance between Germany and France as to the relationship between economic policy and monetary policy.

The convergence programmes thus have proved a powerful instrument of policy coordination. They have increasingly played a role in the guidance, not to say negotiated direction, of national economic policies by Community and Union institutions. In embryonic form, they represent the potential development of a Union-wide economic policy-making system, in particular by means of the coordination of national fiscal and budgetary policies. Going further towards the centralisation of economic policy within the European Union, several Member States have reportedly asked the Commission to 'study the feasibility of linking certain payments from the Community budget to developments in real exchange rates and of introducing macroeconomic conditionality with respect to Structural Fund payments.'²⁷⁵

Convergence programmes were designed originally to achieve the general aims of EMU, in particular in so far as economic convergence, according to the coronation theory, was merely a precondition to monetary integration. At least this is what seems to emerge from the EC Treaty. Furthermore, if one takes the Treaty literally, there would not appear to be any necessary link between convergence programmes with regard to monetary policy and multilateral surveillance with regard to economic policy.²⁷⁶ It is true that economic convergence is a common theme, albeit expressed as a means in relation to (the more supranational) monetary policy and as an end in itself in relation to (the more intergovernmental) economic policy.²⁷⁷ However, the policy instruments in each case were distinct:²⁷⁸ information forwarded by the

²⁷⁵ Commission Report to the Florence Summit, 'Preparation of Economic and Monetary Union: A Review of the Situation (Communication by the Commission to the European Council), in *Europe Documents* No. 1992, 4 July 1997, p 4. As to the follow-up of these proposals, see Commission Communication to the Council on reinforced convergence procedures and a new exchange rate mechanism in stage three of EMU, COM(96) 498 final; ESC Opinion on the impact of Economic and Monetary Union: economic and social aspects of convergence and measures to increase awareness of the single currency, CES 1089/96.

²⁷⁶ As to multilateral surveillance, see Art. 103(2)-(5), which is found in Title VI Economic and Monetary Policy, Chapter 1 Economic Policy.

²⁷⁷ See also European Community, 1996 Annual Economic Report, COM(96) 86 final; European Commission, Report on convergence in the European Union in 1996, COM(96) 560 final.

²⁷⁸ At least if one does not discount for sloppy drafting of the Treaty, and consider that

Member States and reports by the Commission in the field of economic policy,²⁷⁹ and convergence programmes in the field of monetary policy.²⁸⁰ Nevertheless, in this instance at least, the legal texts have not stifled the Community's institutional dynamics and reined in its policy instruments. Convergence programmes have jumped the fence. As the preceding discussion indicates, today they tend to serve the aims of both monetary policy and economic policy. The institutional consequences of the extension of the field of this policy instrument remain to be seen. So too do their consequences for relations between the Member States and for different conceptions of the European Union.

Nevertheless, convergence programmes have an ambiguous, if not anomalous, legal status. Though endorsed by Ecofin, they are not published documents and are not the subject of any formal Community decision. They remain national documents, not Community measures, and in principle they are drafted by national authorities alone. Even though they now play an important role in national and EU decision-making, they are subject to few legal safeguards at Community or national level. Convergence programmes thus raise potentially serious problems of transparency, accountability, and democratic participation.²⁸¹

In view of the third stage of EMU, convergence programmes have now been formally incorporated into the armoury of Community instruments but in a confusing manner. The first implementing regulation in respect of the Stability Pact concerns multilateral surveillance.²⁸² It sets out the rules covering the submission, examination and monitoring of stability programmes and convergence programmes.²⁸³ Both types of programmes are stated to provide an essential basis for price stability and for strong sustainable growth conducive to employment creation.²⁸⁴ Roughly analogous rules apply to

convergence programmes *ex* Art. 109e(2)(a), second indent, and information forwarded by Member States *ex* Art. 103(3), second paragraph, are equivalent.

²⁷⁹ See Art. 103(3), first and second paragraphs, EC, respectively.

²⁸⁰ Art. 109e(2)(a), second indent, EC.

²⁸¹ For example, in the United Kingdom convergence programmes have not been subject to Parliamentary scrutiny: see Robert Brookes, 'Parliamentary Scrutiny of UK Convergence Programmes: the One that Got Away', (1996) 2 *Public Law* 437-451.

²⁸² Council Regulation (EC) 1466/97 of 7 July 1997 on the strengthening of the surveillance of budgetary positions and the surveillance and coordination of economic policies, OJ 2.8.97 L209/1.

²⁸³ *Ibid.*, art. 1. These programmes fulfil the function of the presentation of information for purposes of multilateral surveillance, in the terms of Art. 103(3), second paragraph, EC: see Preamble, seventh recital, and arts. 3(1) and 4(1)..

²⁸⁴ *Ibid.*, arts. 3(1), 7(1).

both types of programmes. However, the requirements for stability programmes and for convergence programmes apply to different groups of Member States. Stability programmes are to be submitted by Member States which are participating in the single currency.²⁸⁵ It is assumed that, in accordance with Article 109j EC, they will have already achieved a high degree of economic convergence and a sustainable government financial position.²⁸⁶ In contrast, convergence programmes are to be submitted by the Member States not adopting the single currency.²⁸⁷ It is assumed that these Member States 'will need to pursue policies aimed at a high degree of sustainable convergence',²⁸⁸ if only because all Member States are committed to budgetary positions or close to balance or in surplus.²⁸⁹

Stability programmes must be submitted before 1 March 1999²⁹⁰ and convergence programmes before 1 May 1999.²⁹¹ The programme must contain specified, detailed information on the Member State's budgetary position and price stability in the case of a stability programme²⁹² or on variables related to convergence in the case of a convergence programme.²⁹³ It must be updated annually and made public.²⁹⁴

Within two months of the submission of the programme, and on the basis of assessments by the Commission and the Monetary Committee,²⁹⁵ the Council must examine the programme within the framework of multilateral surveillance under Article 103 EC.²⁹⁶ It must examine

²⁸⁵ *Ibid.*, art. 3(1).

²⁸⁶ See *ibid.*, Preamble, eighth recital.

²⁸⁷ *Ibid.*, art. 7(1).

²⁸⁸ *Ibid.*, Preamble, ninth recital.

²⁸⁹ *Ibid.*, Preamble, second recital.

²⁹⁰ *Ibid.*, art. 4(1).

²⁹¹ *Ibid.*, art. 8(1).

²⁹² As to this information, see *ibid.*, art. 3(2), (3). In addition to assumptions and policy measures, it includes the medium-term objective for the budgetary position of close to balance or in surplus, the adjustment path towards this objective for the general government surplus/deficit, and the expected path of the general government debt ratio: see *ibid.*, art. 3(2)(a).

²⁹³ As to this information, see *ibid.*, art. 7(2), (3). In addition to assumptions and policy measures, it includes the medium-term objective for the budgetary position of close to balance or in surplus, the adjustment path towards this objective for the general government surplus/deficit, the expected path for the general government debt ratio, the medium-term monetary policy objectives, and the relationship of those objectives to price and exchange rate stability: see *ibid.*, art. 7(2)(a).

²⁹⁴ *Ibid.*, arts. 4 (stability programmes), 8 (convergence programmes).

²⁹⁵ The Committee is set up by Art. 109c(1) EC.

²⁹⁶ Council Regulation 1466/97, art. 5(1), first paragraph (stability programmes), art. 9(1) (convergence programmes), OJ 2.8.97 L209/1..

- whether the Member State's medium-term budget objective provides for a safety margin to ensure avoidance of an excessive deficit,
- whether the economic assumptions underlying the programme are realistic, and
- whether the measures being taken and/or proposed are sufficient to achieve the targeted adjustment path.²⁹⁷

It must also examine

- whether the contents of the programme facilitate closer coordination of economic policies, and
- whether the Member State's economic policy is consistent with the broad economic policy guidelines.²⁹⁸

The Council is required to monitor the implementation of the programmes.²⁹⁹ In addition, in the case of convergence programmes, the Council must monitor the economic policies of non-participating Member States in the light of the convergence programme objectives with a view to ensuring that their policies are geared to stability, and thus to avoid real exchange rate misalignments and excessive nominal exchange rate fluctuations.³⁰⁰ In the event of a significant divergence between the budgetary position and the medium-term objective or adjustment path, it must give early warning in the form of a recommendation based on Article 103(4) EC.³⁰¹ If the problem persists, the Council must make a recommendation to the Member State to take prompt correction measures and may make the recommendation public.³⁰² In accordance with Article 103(4) EC, the President of the

²⁹⁷ *Ibid.*, art. 5(1), first paragraph (stability programmes), art. 9(1), first paragraph (convergence programmes)..

²⁹⁸ *Ibid.*, art. 5(1), second paragraph (stability programmes), art. 9(1), second paragraph (convergence programmes). As to the broad economic guidelines, adopted on the basis of Art. 103(2) EC, see Council Recommendation of 7 July 1997 on the broad economic guidelines of the economic policies of the Member States and of the Community, OJ 2.8.97 L209/12.

²⁹⁹ *Ibid.*, art. 6(1) (stability programmes), art. 10(1), first paragraph (convergence programmes).

³⁰⁰ *Ibid.*, art. 10(1), second paragraph.

³⁰¹ *Ibid.*, art. 6(2) (stability programmes), art. 10(2) (convergence programmes).

³⁰² *Ibid.*, art. 6(3) (stability programmes) art. 10(3) (convergence programmes). Note that while Art. 103(4) provides that the Council 'may' make a recommendation, Council Regulation 1466/97 states that the Council 'shall' make such a

Council and the Commission must include the results of their multilateral surveillance in their report to the European Parliament.³⁰³

(F) THE LEGITIMACY OF EMU

The legitimacy of EMU is closely bound up with the nature and function of its institutions, the European Central Bank (ECB) and the European System of Central Banks (ESCB).³⁰⁴ In order to untangle a complex debate, it is useful to distinguish between credibility, legitimacy and accountability. Credibility refers to the belief that an institution will carry out properly the functions entrusted to it, while legitimacy refers to the belief that a specific institution is widely recognised or at least accepted as being the appropriate institution to exercise specific powers. Accountability refers to the fact that the institution is, or is deemed widely to be, more or less responsive, directly or indirectly, to the people who are affected by its decisions. In the case of the ECB, the three concepts are empirically interrelated but analytically distinct. With them in mind, the following paragraphs consider (a) the credibility of the ECB, (b) the potential impact of a uniform monetary policy in a highly diverse set of economies, (c) the potential political implications of the Bundesbank model, and (d) the accountability of the ECB.

Credibility is widely recognised as a crucial determinant in the eventual success or failure of the ECB.³⁰⁵ The term 'credibility' refers essentially to whether or not the addressees of the ECB trust the ECB and believe that it is capable of carrying out its legal mandate, in particular achieving its primary objective of maintaining price stability.³⁰⁶ The addressees of the ECB include not merely the banking public, but also

recommendation. Both provide that the Council 'may' make the recommendation public.

³⁰³ *Ibid.*, art. 12.

³⁰⁴ See in particular R. Schmit, *The European Central Bank: Institutional Aspects* (Kluwer, 1997). See also Hugo J. Hahn, 'The European Central Bank: Key to European Monetary Union or Target', (1991) 28 *Common Market Law Review* 783-820. As to the background, see *Vers un système européen de banques centrales: Projet de dispositions organiques* (Rapport du groupe présidé par Jean-Victor Louis) (1990).

³⁰⁵ As to the literature on credibility, see Persson and Tabellini, *Macroeconomic Policy, Credibility and Politics* (Harwood Academic Publishers, 1990); A. Cukierman, *Central Bank Strategy, Credibility, and Independence: Theory and Evidence* (MIT Press, 1992); Giavazzi and Pagano 'The Advantage of Tying One's Hands. EMS Discipline and Central Bank Credibility' (1988) 32 *European Economic Review*. Note however that Winkler concludes that 'Unfortunately, the credibility literature has nothing substantial to say about the ultimate sources of credibility': see B. Winkler, *Towards a Strategic View on EMU: A Critical Survey* (European University Institute, working paper RSC No. 95/18, 1995), p 7.

³⁰⁶ See Art. 3a(2) EC.

and in particular national central bankers, financial institutions, and economic policy-makers. The Maastricht Treaty sought to assure the credibility of the ECB by providing for ECB independence, in the sense of independence from control of monetary decision-making by political authorities.³⁰⁷ Artis and Winkler argue that the Stability Pact had a similar purpose.³⁰⁸ Such a strategy appears to be consistent with the evidence based on economic research.³⁰⁹ But it neglects other aspects of credibility, such as historical experience, participation in the same political culture, an economic culture of price stability and low inflation, and embeddedness in a trusted political system. Its main aim was to reach a compromise between the credibility of the ECB and what is often called the 'symmetry' of the system, namely the distribution of power between monetary and political authorities.³¹⁰ Whether this compromise will prove sufficient to meet the competing demands which will be placed on it remains to be seen.

There is thus a tension between credibility and legitimacy. This is exemplified first in the fact that each addresses a different audience, as seen in the Maastricht compromise between credibility and symmetry. Another example of the same tension is manifested in the potential contradiction between uniformity and diversity. Regardless of the existence of similar 'house cultures' of the various national central banks and the long-standing cooperation between them in specialist committees and networks, the various national banks operate in

³⁰⁷ This was consistent with the Commission's view that the credibility of the ECB would not be problematic because of the ECB's pivotal role in a system of central banks which had already demonstrated their commitment to price stability and its statutory independence and legally prescribed priorities. See European Commission, *External Effects of Economic and Monetary Union* (Commission Staff Working Document), Europe Documents No 2034, 8 May 1997).

³⁰⁸ Michael J Artis and Bernhard Winkler, 'The Stability Pact: Safeguarding the Credibility of the European Central Bank', Discussion Paper No. 1688, Centre for Economic Policy Research, August 1997.

³⁰⁹ 'Empirical evidence from 17 developed countries during the period 1973-86 by Alesina (1989) appears to support the contention that the more independence a central bank has, the more likely it is to be successful in combating inflation at a lower cost in unemployment....In such a complex matter as inflation it may be dangerous to make such a simple connection between inflation and central bank independence. The central bank may be operating discretionary policy but the more independent of government influence a central bank is the more its inflationary stance is likely to be believed'. A. Alesina, 'Politics and Business Cycles in Industrial Democracies', *Economic Policy*, no. 8, April 1989.

³¹⁰ See B. Winkler, *Towards a Strategic View on EMU: A Critical Survey* (European University Institute, working paper RSC No 95/18, 1995) p 8-10, who argues that the 'independence' solution to the credibility problem is insufficient and will require the development of stronger European political institutions.

different national political systems and political cultures, leaving aside the recent emergence due partly to EMU of a shared economic culture of low inflation and stable prices. Yet the polity, political culture and legal culture of the EU are for the moment in their infancy or at least differ substantially from those of the Member States.

In this context, an important concern regarding legitimacy stems from the view that EMU and the constitutionally mandated policies of the ECB may have very different effects in different Member States. The legal and institutional framework of EMU may be too rigid to cope with national diversity. It is open to serious doubt whether the same interest rate is really suitable for all participants in the single currency, given existing differences among national economic growth rates, banking and industrial structures, and degree of openness to foreign trade.³¹¹ Such rigidity may be especially nefarious in the case of unforeseen economic shocks. These shocks may magnify existing forms of differentiation or create new differences as a result of the inability of the individual Member States to have recourse to their traditional monetary policy instruments. In addition, arrangements in addition to the new convergence programme requirements to cope with relations between the 'ins' and the 'outs'.³¹² A further element is that of enlargement, which considering that EMU is part of the *acquis communautaire* will require careful management if it is not to place EMU at risk.³¹³

A third preoccupation with regard to the legitimacy of EMU concerns the Bundesbank model. While the independence of the ECB and the lack of a real 'economic government' at EU level have been

³¹¹ See 'Can one size fit all?', *The Economist*, March 28 1998, p 82, reviewing Ramana Ramaswamy and Torsten Sloek. 'The Real Effects of Monetary Policy in the European Union: What are the Differences?', IMF Working Paper No. 160, December 1997, and Rudiger Dornbusch, Carlo Favero, and Francesco Giavazzi, 'A Red Letter Day?', CEPR Discussion Paper No. 1804, February 1998. See also D.R.R. Dunnett 'Legal and Institutional Issues affecting Economic and Monetary Union in David O'Keefe and Patrick Twomey (eds) *Legal Issues of the Maastricht Treaty* (Chancery Law Publishing, 1994), p 143; B. Winkler, *Towards a Strategic View on EMU: A Critical Survey* (European University Institute, working paper RSC No.95/18, 1995), pp 4-5.

³¹² For reasons of space it is not possible to deal with this important topic here. See however John A.A. Arrowsmith, 'La non-participation à la phase 3: La vie à l'étage inférieur de l'UEM', (1996) 36 *Revue de l'Economie financière* 185-202; Filip Tuytschaever, 'The Changing Conception of Differentiation in EU Law, draft PhD Thesis, European University Institute, Florence.

³¹³ See Philippe Vigneron and Philippe Steinfeld, 'The Enlargement of the EU and EMU: Some Legal Considerations', (1998) 13 *Butterworths Journal of International Banking and Financial Law* 18-21. See also Fritz Breuss, 'The Impact of EMU on External Trade Relations with CEECs', presented at the Third ECSA-World Conference, 'The European Union in a Changing World', Brussels, 19-20 September 1996.

identified as important concerns, these two points are often simply a shorthand for reluctance or indeed opposition regarding the adoption of the German Bundesbank model as the institutional model for the ECB. Leaving aside the fact that this model is criticised most frequently by people from Member States other than Germany, there is a real question as to whether it is the most appropriate in the very different legal, institutional and political arrangement of the European Union. Put simply, the Bundesbank in Germany operates within a specific historical, political and legal context,³¹⁴ but the salient features of this specific context do not have any obvious counterpart in the EU taken as a whole. In the early 1990s the Bundesbank's official pronouncements stated that 'In the final analysis, a Monetary Union is an irrevocable joint and several community which, in the light of past experience, requires a more far-reaching association, in the form of a comprehensive political union, if it is to be durable'.³¹⁵ We can read this pronouncement as an attempt to recreate at least some of the features of the specific German context within the EU as a whole. Individuals and organisations from other Member States, as already seen, have different visions of the desirable EU polity.

A fourth aspect of the debate regarding the legitimacy of EMU concerns the relationship between legitimacy, democracy and accountability. The German Federal Constitutional Court in its 'Maastricht judgment' treated the autonomy of the ECB as 'a modification of the democratic principle for the purpose of protecting the confidence in the redemption value of a currency'.³¹⁶ To what extent is this justified, or, in other words, what does the democratic principle mean in the context of monetary policy?

Two different views are presented by Gormley and de Haan, on the one hand, and Verdun, on the other hand. The former argue that the

³¹⁴ See David Marsh, *The Bundesbank: The Bank that Rules Europe* (Heinemann, 1992); Ellen Kennedy, *The Bundesbank: German's Central Bank in the International Monetary System* (Pinter, 1991).

³¹⁵ 'Statement by the Deutsche Bundesbank on the establishment of an Economic and Monetary Union in Europe', *Monthly Report of the Deutsche Bundesbank* vol. 42, 10 October 1990, p 40, quoted in Daniel Wincott, 'The European Central Bank: Constitutional Dimensions and Political Limits', (1992) 11 *International Relations* 111-126 at p 123.

³¹⁶ *Manfred Brunner and Others v The European Union Treaty* (Cases 2 BvR 2134/R/92 & 2159/92 before the Bundesverfassungsgericht (2. Senat) (German Federal Constitutional Court, 2nd Chamber) (1994) 1 CMLR 57 at 104 (para. 96). See also Matthias Herdegen, 'Maastricht and the German Constitutional Court: Constitutional Restraints for an "Ever Closer Union"', (1994) 31 *Common Market Law Review* 235-249 at p 247.

objectives of monetary policy should be decided according to normal democratic procedures and then monetary policy should be delegated to the ECB. Based on this view, they conclude that ECB falls short of democratic accountability. They propose that the ECB should be more accountable to the European Parliament, which should also be involved by means of the co-decision procedure in elaborating the ECB legislative framework.³¹⁷ Verdun argues that the democratic deficit of EMU stems from three factors: lack of parliamentary accountability, lack of transparency, and the asymmetrical development of monetary policy, on the one hand, and political, budgetary or fiscal integration, on the other hand. In evaluating this state of affairs, she emphasises the importance of considering the alternatives, namely the status quo or 'non-EMU', in which most Member States have only limited influence over monetary policy. Nevertheless, the legitimacy of EMU could become problematic if more people oppose ECB policies, because the Treaty is relatively rigid and the EU has few redistributive mechanisms. Consequently she argues in favour of a broader transformation of the EU polity in the long run.³¹⁸

It may be suggested that these changes have already begun. On the one hand, the European Parliament has asked for greater power with regard to the ECB, first for regular testimony by the ECB President, and ultimately for a formal veto power over the members of the ECB executive board.³¹⁹ This presages a struggle for power among the EU/EC institutions. On the other hand, the European Council has played an extremely significant role in the run-up to the third stage of EMU. In my

³¹⁷ Laurence Gormley and Jakob de Haan, 'The Democratic Deficit of the European Central Bank', (1996) 21 *European Law Review* 95-112. See also Peter Kenen, *Economic and Monetary Union in Europe: Moving beyond Maastricht* (Cambridge University Press, 1995), p 42, and Christopher Taylor, 'The Role and Status of the European Central Bank: Some Proposals for Accountability and Cooperation', presented in the Workshop on 'The Political and Institutional Deficits of the European Integration Process, European Forum, European University Institute, Florence, 30-31 May 1997.

³¹⁸ Amy Verdun, 'The Democratic Deficit of EMU', paper presented in the European Forum, European University Institute, Florence, 31 January 1997. See also Guido Montani, 'Moneta europea, riforma dello Stato del benessere e democrazia economica', (1990) 32 *Il Federalista* 199-239; Rolf Knieper, 'The Sovereignty of Money: Legal Problems of European Monetary Integration', (1991) 19 *International Journal of the Sociology of Law* 121-148. In addition, as Harden points out, Ecofin has no democratic legitimacy of its own, and the ECB does not have the powers or the appropriate form of accountability to serve as the 'economic government' of the Community: see Ian Harden, 'The European Central Bank and the Role of National Central Banks in Economic and Monetary Union', in Karl Gretschnann (ed), *Economic and Monetary Union: Implications for National Policy-Makers* (European Institute of Public Administration, 1993), pp 149-163 at p 163.

³¹⁹ 'EU Notebook', *The Wall Street Journal Europe* Thursday, April 2, 1998, p 1.

view, this signals a more general transformation in the distribution of power in the EU system of multilevel governance, and in particular a closer engagement and greater interpenetration of the national and EU political arenas. It is an example of increased legitimation without increased democratisation. EMU thus can be seen as process of institutional choice³²⁰ or institutional learning, but sometimes with unintended consequences.

In considering the legitimacy of EMU in social terms rather than merely in procedural terms, one needs to distinguish between three different senses of legitimacy: legitimacy within certain technical task-specific limits; conditional legitimacy, for example legitimacy which is conditional on future developments such as the emergence of more overtly political institutions of governance; and legitimacy *tout court*. The first position is closest to that of the German Federal Constitutional Court, both as regards EMU and as regards the EU in general, or more recently the views of Majone regarding powers delegated to executive agencies.³²¹ The second position is reminiscent of the views of Gormley and de Haan, on the one hand, and Verdun, on the other hand.

The third position is strengthened by three current factors regarding EMU. One is the emergence of an emphasis on low inflation and price stability as an increasingly important shared feature of EU economic/political/legal culture. The other is the importance of the European Council as the primary motor and steering mechanism of the EU policy. The last is the increasing voice being given to the idea that EMU in general, and the convergence criteria in particular, should include an express reference to the objective of increasing employment.³²² Taken together, these three elements may presage broader constitutional changes in the EU as a result of EMU, unless uncontrollable economic shocks result in increased economic

³²⁰ In the sense used by Neil K. Komesar, *Imperfect Alternatives: Choosing Institutions in Law, Economics, and Public Policy* (University of Chicago Press, 1994).

³²¹ See for example Giandomenico Majone, 'From the Positive to the Regulatory State: Changes and Consequences of Changes in the Mode of Governance', (1997) 127 *Journal of Public Policy* 139-167, and his forthcoming article in (1998) 4 *European Law Journal*, in press..

³²² See e.g. Brian Bercusson *et al*, *A Manifesto for Social Europe* (European Trade Union Institute, 1996); Roger Blanpain *et al*, *Fundamental Social Rights: Proposals for the European Union* (Peeters, 1996); Vincenzo Guizzi, 'Il Ruolo del Parlamento Europeo in materia di integrazione economica e monetaria', (1996) 1 *Rivista di Diritto Europeo* 3-11 at p 10.

differentiation, a loss of ECB credibility, and widespread political opposition to EMU, including its legal framework.³²³

4. CONCLUSION

A Dutch journalist has written a surprising whodunnit about European economic and monetary union (EMU).³²⁴ I hope we non-Dutch speakers can all soon enjoy a translation. In the meantime, I have tried in this article to excavate some of the principal legal issues raised by the saga of EMU. My purpose has been neither to treat EMU from the standpoint that '... the introduction of the euro will be the crowning of economic integration and the rocket launcher of political union,'³²⁵ nor to reflect the more critical assessment that it creates unconstitutional 'forms of factual compulsion, which in practical terms will make the journey towards European union irreversible'.³²⁶ Instead I have focused on the legal evolution of EMU, how to explain it theoretically, and some of its main characteristics from a broader constitutional perspective.

The legal aspects of EMU are sometimes extremely controversial, either in public or behind the closed doors of diplomatic and monetary negotiations. Legal and other technical debates often as a kind of shorthand for political disagreement. Competing economic theories frequently play the same role.³²⁷ This was the case long before EMU was set as a priority European Union objective.³²⁸ This does not mean, of

³²³ In other words, *pace* Charles A.E. Goodhart, 'The Political Economy of Monetary Union', in Peter B. Kenen (Ed),: *Understanding Interdependence: The Macroeconomics of the Open* (Princeton University Press, 1995), p. 478, the political concerns in respect of EMU are not at all trivial, and the importance of EMU cannot be reduced simply to the interconnection with monetary policy and other policies such as the single market or trade policy..

³²⁴ Roel Janssen, *De Struisvogel Code (The Ostrich Code)* (Balans, 1996), reviewed by James Morgan, 'Death and the Emu', *Financial Times*, Weekend June 28/29 1997 p VI Weekend FT.

³²⁵ Jacques Delors, in *Nouvel Observateur*; No 1699, 1997, quoted in *Agence Europe* No. 6990 (n.s.), Saturday 7 June 1997 p 2.

³²⁶ Argument of the complainants, in *Manfred Brunner and Others v The European Union Treaty* (Cases 2 BfR 2134/92 & 2159/92) before the Bundesverfassungsgericht (2. Senat) (German Federal Constitutional Court, 2nd Chamber) (1994) 1 CMLR 57 at 73, 75. See also B. Moss (ed), *The Single European Currency in National Perspective: A Community in Crisis?* (in press).

³²⁷ See Kenneth Dyson, *Elusive Union: The Process of Economic and Monetary Union in Europe* (Longman, 1994).

³²⁸ To the effect that EMU was formally a Community objective before the Maastricht Treaty, see Opinion 1/91 Opinion delivered pursuant to the Second subparagraph of Article 208(1) of the Treaty. Draft Agreement between the Community on the one hand and the countries of EFTA on the other, relating to the creation of European Economic Area, 1991 ECR I-6079. As to the Maastricht Treaty, see Treaty on European Union, Preamble 6th recital, Art. B 2nd indent TEU, Art. 2 EC. See generally Snyder, 'EMU -

course, that all legal aspects of EMU have been or are politically controversial. But, in the future also, political conflicts about EMU are likely often to appear in legal camouflage. This dialectical relationship between politics and law, political discourse and monetary discourse, and political discourse and legal discourse should not be surprising. The driving force in EMU, including its main legal aspects, has always been politics.³²⁹

The intimate connection between law and politics in EMU is likely to remain even after 1 January 1999. This is the date currently envisaged for the start of the third stage of EMU. It is the decisive step towards a single currency, when nominal exchange rates will be irrevocably fixed³³⁰ between the currencies of the participating EU Member States. The Maastricht Treaty provided for the possibility of an earlier date.³³¹ However, in December 1996 the Council of the European Union decided that a majority of Member States did not fulfil the necessary conditions for the adoption of the single currency.³³² Consequently, the default position laid down in the Treaty for the start of the third stage applies.³³³

Metaphor for European Union? Institutions, Rules and Types of Regulation', in R. Dehousse (ed), *Europe after Maastricht: An Ever Closer Union?*(Law Books in Europe, 1994), 63-99.

³²⁹ For example, see Gretschnann, Kotz and Sleijpen, 'The European Monetary System: The Geography of Economics versus the Politics of Money?', in K. Gretschnann (ed), *Economic and Monetary Union: Implications for National Policy-Makers* (Nifhoff for the European Institute of Public Administration, 1993), 27-49 at 28; Loukas Tsoukalis, 'Economic and Monetary Union', in H. Wallace and W. Wallace (eds), *Policy-Making in the European Union* (Oxford, 3rd ed. 1996) 279-299 at 280; Barry Eichengreen and John Frieden, *The Political Economy of European Monetary Unification* (Westview Press, 1995), at 89; Charles A.E. Goodhart, 'The Political Economy of Monetary Union', in Peter B. Kenen (Ed),: *Understanding Interdependence: The Macroeconomics of the Open*(Princeton University Press, 1995), at 448; Fratianni and Waller, *The Maastricht Way to EMU*(Princeton University, International Finance Section, June 1992, Princeton Essays in International Finance, No. 187), 1-2; Bernard Connally (former head of unit of DGII/D/3 EMS, National and Community Monetary Policies in the European Commission), *The Rotten Heart of Europe*(1995); Paolo Guerrieri and Pier Carlo Padoan, *L'Economia Politica dell'Integrazione Europea* (Il Mulino, 1988); Bernard Moss (ed), *The Single European Currency in National Perspective: A Community in Crisis?*(forthcoming)..

³³⁰ Article 109l(4) EC.

³³¹ Article 109j(3) EC.

³³² Council Decision (EC) 96/736 in accordance with Article 109j(3) of the EC Treaty on entry into the third stage of EMU, OJ 24.12.96 L335/48. The Decision was taken by the Council meeting in the composition of the Heads of State and Government. It was based on an assessment by the Ecofin Council under Article 109j(3) EC, following a recommendation by the Commission. As to this assessment, see the Report by the Ecofin Council to the European Council, 'The Preparations for Stage 3 of EMU', Annex 1, *Europe Documents* No 2015/16, 18 December 1996, p 7). According to Article 109j(3) the Council was also required to take due account also of the opinion of the European Parliament.

³³³ That is, 1 January 1999: see Article 109j(4) EC.

Recently (as of the date of writing), the list of Member States that are initially to participate in the single currency has been determined.³³⁴

We can understand the evolution of EMU as a combination of two-level games involving an epistemic community. What remains to be explained, however, is why EMU provoked such intense reactions, thus contributing so much to the politicisation of EU law and thus to the development of the EU as a polity and as a constitutional system.

In my view, the scale and depth of the response to EMU stemmed from four main conjunctural, and partly overlapping, reasons, which evoked widespread reactions at the individual, organisation and societal levels. (a) EMU coincided with the spread of deflationary economic policies, widely described, perhaps prematurely, as 'the end of inflation'.³³⁵ (b) It also coincided with the Maastricht debate on the future of European integration, raising issues of legitimacy, democracy, and the fashioning of political institutions suitable for an increasingly complex system of multi-level governance. (c) It coincided with the uneven effects of globalisation within (and on) the EU Member States, thus stimulating a debate on European values, the welfare state, and the European model of society. (d) In the face of these challenges, EMU seemed to leave the emperor naked. Despite initial attempts to establish an EU fiscal policy alongside EMU, or even to situate EMU within a strong EU polity, EMU as eventually agreed was a 'victim of narrow conceptualisation of money as essentially an economic and technical phenomenon'.³³⁶ By focusing solely on monetary policy, it removed from Member States certain basic policy instruments for dealing with economic shocks, without creating sufficient new equilibrating instruments at European level. In doing so, however, it neglected popular political culture and eschewed wide political debate.

³³⁴ As to the Commission report, see European Commission, 'Euro 1999: Report on progress towards convergence and the recommendation with a view to the transition to the third stage of economic and monetary union, Part 1: Recommendation (25 March 1999) (Luxembourg, Office for Official Publications of the European Communities, 1998). The European Council finalised the list of participating Member States at the end of March or early April 1998: see *Agence Europe* No. 7213 (n.s.), Special Edition, Sunday, 3 May 1998.

³³⁵ As to these policies, see the best-selling book by R. Bootle, *The Death of Inflation: Surviving and Thriving in the Zero Era* (1996, paperback edition 1997, Nicholas Brealey Publishing). For a more cautious assessment, see David Hackett Fischer, *The Great Wave: Price Revolutions and the Rhythm of History* (Oxford University Press, 1996), pp 233-234.

³³⁶ Kenneth Dyson, *Elusive Union: The Process of Economic and Monetary Union in Europe* (Longman, 1994), p xi.

Set in its broader context, therefore, EMU has served both as a stimulant and as a proxy for broader debates about monetary policy decision-making, the future of European integration, and the meaning and effects of globalisation. It is instructive to recall the extent to which the search for 'capitalism with European characteristics' was in fact fuelled by the proposals and preparation for EMU. They made clear not only the inconsistency between the governance of monetary policy at EU level and that of fiscal policy at national level. They also revealed, more clearly and indeed more frighteningly than ever before, the fact that the EU does not really have any strong stabilisation or redistributive function, in other words, any strong 'social' function. Whether true or not, it is widely believed that globalisation has led to the end of inflation. In the EU and abroad, the German Bundesbank is generally seen as the champion of deflationary monetary policy. The spectre of a Buba-dominated EMU thus generated strong political reactions. Globalisation, deflationary monetary policy and EMU are often considered to be inextricably intertwined. For ordinary people, they seem to have (and in fact may have) similar implications, notably with regard to changes in the nature of work, job insecurity, and potential or actual unemployment. Seen from this perspective, EMU can be viewed as a threat to personal identity.

In addition, it has become increasingly obvious that the EU's economic strength and political weakness are both due mainly, though not only, to national governments. As a consequence, the policies of Member States towards the EU become increasingly controversial among national electorates, and EU policies and EMU in particular have become highly politicised. This has involved a fierce debate about whether the Member States are giving up their economic policy instruments without anything to replace them at the EU level of governance. For once, the debate has not been limited to experts. As a result, it has raised issues about democracy, legitimacy and accountability of EMU decisions without a representative political master. A lay person may be shocked to be reminded that the debate among experts began as early as the late 1960s. The two schools of thought about monetary policy, monetarists and economists, then diverged not only about the technical aspects of the governance of the economy but also about the extent of the aims, architecture and identity of an integrated Europe. Now, however, this debate is part of mass politics, and it is not limited to European economic integration. It also

concerns European political integration, the nature and survival of the social welfare state, and the identity of the EU in a global context.

By stimulating the politicisation of EU policies and law, EMU has contributed directly to the development of the EU as a polity and a constitutional system. This contribution can be summarised in nine points.

(1) The Stability Pact, and indeed EMU as a whole, exemplifies significant recent trends in the development of the EU constitution. The EU is in the midst of changes toward increased multi-level governance and greater institutional heterogeneity. This is especially the case regarding political sensitive issues, such as EMU. In this case the *approfondissement* of multi-level governance means specifically the greater interpenetration of the EU and national political systems. The gradual emergence of a new configuration of EU politics thus is closely intertwined with developments in and across national political systems. In the past, this relationship between two levels of governance might have been seen as antagonistic. Now, however, it has become dialectical.

(2) This dialectical interaction between different levels of governance involves a two-fold dilemma that in the EC has been well-known for years. This concerns the choice of level of governance, on the one hand, and the type of economy, on the other hand.³³⁷ The former involves the question as to whether the EC or the Member States should take action, while the latter concerns the extent of governmental action, that is, the relationship between state and market.

As I have tried to suggest in this article, however, EMU reconfigures and reconstitutes this dilemma in a strikingly new form. The first leg of the dilemma, which concerns levels of governance, no longer poses - if it ever did - such a clear choice between two sharp alternatives. Reality can no longer be captured by a simple reference to the end points on a spectrum. The evolution of EMU demonstrates that practice, usually if not always, involves a complex combination of elements of both and indeed more than two levels; in fact, one can go further to add that EMU shows the metaphor of levels should be replaced by the notion of polycentricity. Now a serious intellectual effort needs to be made to come to grips with this polycentricity, including EMU, in constitutional terms.

³³⁷ See also my article on 'Monetary Union: A Metaphor for European Union? Institutions, Rules and Types of Regulation', in R. Dehousse (ed), *Europe after Maastricht: An Ever Closer Union?*(1994), pp 63-99 at 83.

The second leg of the dilemma has been altered even more profoundly. It no longer refers to the form of economy, that is, concerned with the extent of state intervention in the market seen as a technocratic issue. Instead, even if we choose to retain this old language, we must see this leg of the dilemma as quintessentially political. Not only does it inevitably involve some combination of state and market. More fundamentally, it concerns what are essentially political questions, concerning the use of power, the choice of values, and the determination of the basic features of polity, society and identity.

(3) These changes have fostered the increasing politicisation of the EU itself. This has led less, however, to the increasing democratisation of the EC and the institutions within the EC framework than to the strengthening of the EU institutions, and particularly the European Council. The European Council has increasingly assumed the roles of both gatekeeper and channel. In contrast to the Commission, the Council, the European courts, or the even the European Parliament, it can draw on the resources of both the EU and the national political arenas. These arenas are increasingly overlapping and interconnected, but so far at least the European Council has a unique and in both arenas an overtly political role. To some extent, it thus can foster or retard the processes which might tend to merge these arenas, in other words European political integration. The European Council by no means has a monopoly of EU politics. As events regarding EMU in France, Germany and Italy among other Member States have shown, it is still possible to *scendere in piazza*.

(4) The role of the European Council fosters greater interpenetration between the EU and national political systems. It has in my view also strengthened the EU, as distinct from the EC, as the legal framework which is of constitutional salience, though not necessarily legal relevance, to citizens (and others). But the development of EMU has not necessarily improved the democratic character of the four main European Community institutions. Instead, we can see the European Council as representing a conjunction of (various national) democratic systems and acting, according to the principle of single institutional framework, as a real institution of the European Community. At least in the case of EMU, the increased role of the European Council thus is a sign of the emergence of EU politics. But the strengthening of the European Council also serves as a surrogate for political changes in EC

institutions. It represents a form of increased legitimation without increased democratisation.

(5) EMU may potentially result in a qualitative transformation of the EU constitution. This effect can be seen as the political and legal side of the coin of which the other side is the lowering of microeconomic transaction costs. It involves the development of certain constitutionalising processes, notably the creation of forms of social solidarity which have long existed within national boundaries but which, up to now, are relatively little developed on an EU scale. I refer, in particular but not only, to the identities of class and other forms of social and economic differentiation. Seen in the light of EMU, these are types of identity and potentially forms of political loyalty which are non-national in character and cut across national boundaries. Doubtless there are other forms of social solidarity and other types of identity which share these characteristics.

(6) EMU has already stimulated or reinforced the development of certain aspects of an EU legal or constitutional culture. Of special importance are the value placed on low inflation and price stability; the placing of employment and thus the welfare state model at the centre of public attention; and the strengthening of the European Council as a central institution in European integration. The latter reinforces the idea that Member States are Masters of the Treaty, but it does so in an unusual way, namely by emphasising that the Masters of the Treaty are the Member States not individually but acting together. This is a crucial point in the development of a new EU constitutional culture.

(7) The example of the Stability Pact illustrates closer forms of cooperation between the European institutions and the Member States. European Council guidelines aim to, and in effect do, bind the Council, the Commission and the Member States. Under the aegis of the European Council, the Ecofin has enacted regulations which provide for relations and procedures involving the Council, the Commission and the Monetary Committee in very precise detail. National administrations are increasingly channelled and constrained, for example, in respect of the EMU convergence criteria. Nor are these solely administrative issues. The cooperation between EU and national institutions is highly political, for example within the European Council and Ecofin. Similarly, the enforcement of EC law regarding EMU has a very direct and dramatic impact, often a restructuring impact, on national political institutions and processes.

(8) The processes, tools and techniques involved so far in ensuring the effectiveness of EMU are quite heterogeneous. Three points in particular deserve to be emphasised. One is the use of European Council conclusions as strong political guidelines, even though in theory they have no legal force. Here their force derives partly from the position of the European Council in the hierarchy of EU institutions. It also derives however from its direct links with national political systems in the Member States.

In addition, a frequently used legal technique involves what we can call 'nested norms'. This is a kind of Russian doll of rules, with European Council political guidelines on the outside, and a series of increasingly detailed legally binding rules on the inside. Only the latter have legal force, but they take their political and social meaning, hence their effectiveness in practice, from the former. In other words, the effectiveness of EU/EC measures depends on the existence of a common political framework at EU level, on the one hand, and on the fact that this political framework is deeply rooted in and ultimately derives its legitimacy from the individual national political systems of the Member States, on the other hand.

Furthermore, EMU also exemplifies the use of much more detailed rules and tighter deadlines. The adoption and subsequent effectiveness of these measures is facilitated by the emergence of stronger EU political institutions, notably the European Council. Seen from the standpoint of compliance with law, this can be viewed as an example of harmonisation, not only of legal rules and administrative practice but also of national economic systems, economic ideologies and political cultures. Their contribution to the development of an EU constitutional culture remains to be analysed.

(9) EMU is a high-risk political strategy. It is so intertwined with the future of the EU that, if it fails, European integration as we know it may be in danger. The evolution of EMU thus illustrates the extremely complex, often contradictory nature of the real constitutionalisation of European integration.³³⁸ This involves not just the elaboration and application of legal principles, but also the development of numerous constitutionalising processes and the gradual emergence of an EU constitutional culture. If our question is 'are we making a constitution?',

³³⁸ The progress of EMU from the EU standpoint can be followed on the following websites: (1) <http://www.europa.eu.int/pol/emu/en/emu.htm>; (2) <http://www.euro-emu.co.uk>

the study of the evolution of EMU leads us to answer 'yes'. If, however, our question is 'what constitution are we making?', this article has suggested that, within certain limits, only politics will tell.