

Target2 Imbalances and the "Demokratieprinzip": Some Questions

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By [PETER LINDSETH](#)

One main effect of the Eurozone crisis has been a dramatic shrinkage in interbank lending, which is the normal source of bank liquidity for routine business operations. In this context, a technical feature of the EMU — the ECB's so-called Target2 payment system — has taken up the slack, providing a means of moving liquidity to those banks that need it. The result, however, has been major imbalances in the Target2 system, with excess liquidity flowing away from the Eurozone core (Germany, Netherlands, Luxembourg, and Finland) toward the periphery, where it is sorely lacking.

From an official perspective, the resulting Target2 imbalances are [unproblematic](#) in themselves, unless the Eurozone were to break down. Only then would there be any real risk that these imbalances (amounting to a [547 billion euro](#) claim on the Bundesbank balance sheet at the end of February) could convert into an unpaid liability that the Bundestag might eventually have to make good on its own. But as Jens Weidmann, President of the Bundesbank, [declared](#) last month, he is not worried about Target2 imbalances per se “because I believe the idea that monetary union may fall apart is quite absurd”.

Let's assume the risk of EMU collapse is remote, even “absurd”. Ironically, part of the reason for this absurdity flows from the incentive structure of Target2 itself. To avoid converting mere “imbalances” into potentially massive “liabilities”, the Eurozone core has a strong incentive to take whatever steps are needed to shore up the periphery and thus make collapse politically “absurd”. This is precisely as it should be, one might say, given the sort of economic interdependence that the currency union was designed to promote.

But it also suggests that the incentive structure at the heart of Target2 already contains elements approaching that of a political union. This in itself, along with potential problems with the no-bailout clause of Article 125 TFEU, might be enough to raise some interesting issues regarding Target2 for the German Federal Constitutional Court (GFCC). I detailed some of those in [my original post](#) on EUtopialaw.com. But what I'd like to focus on here is the potential conflict between Target2 incentives and the *Demokratieprinzip* that the GFCC has stressed in its two major decisions on the Eurozone crisis.

The most recent, in February, dealt with the scope of Bundestag oversight of Germany's participation in the EFSF. In that case, the court insisted ([para.109](#)) “that the German Bundestag is the place in which, on its own responsibility, decisions are to be made about revenues and expenditures, including with regard to international and European obligations”. And in its decision on the Greek bailout in September ([para.124](#)), the court further concluded that, “if supranational legal obligations were created without a corresponding decision by the free will of the Bundestag, then the parliament would find itself in the roll of a *Nachvollzug* [literally a ‘re-enacting’ — perhaps better translated as a ‘rubber-stamp’?] and could no-longer exercise overall responsibility for spending policy within the framework of its budgetary rights”. Finally, again last September ([para.125](#)), the court ruled that, “in particular [the Bundestag] is not permitted, even by statute, to subject itself [*sich ausliefern*] to any mechanism of financial effect, which — whether on the basis of its overall conception or an overall assessment of its individual measures — could lead to unclear burdens of budgetary significance, be they expenditures or revenue losses, without prior constitutive consent” of the Bundestag.

As an outsider, I obviously defer to the superior knowledge of German constitutional law experts on the meaning and

import of these passages. They could, in the end, amount simply to a sort of *surenchère verbale* from which the court will have to retreat in the face of the *fait accompli* of monetary union as well as the functional demands of the Eurozone crisis. Nevertheless, they do seem to raise several questions: Might the constitutional problem with Target2 be that—“whether on the basis of its overall conception or an overall assessment of its individual measures”—what are initially “imbalances” could be transformed into real “liabilities” without any vote of the Bundestag, by virtue of another member-state’s default or exit from the Eurozone? Could this risk in turn “lead to unclear burdens of budgetary significance ... without prior constitutive consent” of the Bundestag? Does the incentive structure of Target2 run the risk of turning the Bundestag into a “rubber stamp” [*Nachvollzug*] within the meaning of the GFCC’s jurisprudence? Indeed, one might argue that even the *fear* of any future Target2 liabilities could have a major impact on the Bundestag’s budgetary autonomy, by effectively compelling further bailouts to keep the Eurozone intact. This creates a sort of “sword of Damocles” over German politicians and taxpayers, trapping them in a web of unforeseen legal and political obligation to rescue other Eurozone members (remember the no-bailout clause?), lest Germany face potentially massive Target2 liabilities.

Of course, it seems deeply unlikely that the GFCC would ever prevent Germany from meeting its Target2 liabilities, should they arise, particularly when they would ultimately have to be paid to the Bundesbank to shore up its balance sheet. But any substantial loss via Target2 might also make the court much less likely to grant the usual margin of appreciation to policymakers in their efforts to address the Eurozone crisis going forward. We must wait and see.

This is a revised and condensed version of a [post](#) that appeared originally on [EUtopialaw.com](#). Please consult the original for additional background on the Target2 controversy, including extensive links to online materials.

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