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The ECB, the courts and the issue of democratic legitimacy after *Weiss*

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Abstract

This article analyses the new challenges that the ECB faces in implementing its monetary policy and asks to what extent judicial review can help address these. The ECB mandate provides no clear guidance for many of the ECB's recent challenges, which include a sovereign bond market panic, technical limits to the efficacy of its tools, and questions concerning the environmental impact of its operations. For this reason, the ECB's decisions suffer from democratic authorization gaps; it makes choices with far-reaching consequences for which there is no clear basis in the mandate. In this context, courts can either opt to accept choices made by the ECB, as the ECJ has mostly done, or, as the Bundesverfassungsgericht decided to do, itself weigh in on monetary policy. Neither approach, we argue, can improve the tenuous democratic legitimacy of the ECB in the absence of proper democratic guidance. There are, however, other ways the Member States and the EU's political institutions can provide the ECB with guidance on how to deal with its new choices.

1 Introduction

The *Bundesverfassungsgericht's* highly controversial decision to declare *ultra vires* the European Central Bank's Public Sector Purchase Programme (PSPP) – and the ECJ's judgment upholding it – strikes at the heart of the EU legal order.¹ Karlsruhe and Luxembourg adopt radically divergent approaches to the constitutional position and legitimacy of the ECB's actions. Why did both courts come to such different answers? As we show in the following, the fundamental issue of legitimacy at stake is of a kind that courts by their nature are ill-equipped to address. The ECB's post-crisis operations often lack a clear basis in its mandate, which undermines the role of that mandate in providing the central bank's choices with democratic legitimacy. Courts either do too little, merely accepting choices made by the ECB, or do too much, themselves determining what the ECB should do. Because in a democratic society the final say should remain with citizens and their elected representatives, the ECB's torturous journey through the courts can only end with them.

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¹ 2 BvR 859/15 et. al., *PSPP*, Judgment of 5 May 2020, ECLI:DE:BVerfG:2020:rs20200505.2bvr085915 (hereafter: "*BVerfG PSPP*").

When the drafters of the Maastricht Treaty designed the ECB in the early 1990s, they accorded principal importance to price stability.² High levels of inflation in the 1970s increasingly led policymakers, central bankers and politicians to believe that price stability should be the primary aim of monetary policy. Achieving price stability would require delegating monetary policy to independent central bankers operating at a distance from elected politicians. Within this monetarist paradigm, independence could be reconciled with the requirement of democratic legitimacy, because central banks would operate within a democratically authorised and narrow legal mandate. Central banks could pursue their price stability objective by means of interest-rate setting and would have only limited discretion. The central bank's legal mandate provides it with democratic authorization, since it spells out both the objectives of the central bank, as well as the instruments with which to pursue these. Democratic accountability for monetary policy decisions is limited to explaining how the central bank has used its well-defined instruments to achieve the price stability objective. In this context, judicial review offers a crucial safeguard to ensure that the independent central bank acts within the confines of its democratically authorised mandate.

The drafting of the Maastricht Treaty was imbued by ideas and concerns that were prevalent in Europe at the time. For that reason it is not surprising that the ECB's mandate reflects assumptions that have become highly contentious since then or even turned out to be false. The dramatic events of the 2007-2008 Global Financial Crisis, the 2010-2012 Eurozone Crisis and the Covid-19 Pandemic have confronted the ECB with new challenges, which were not anticipated in the mandate. It is these gaps in the mandate that led to the ECB saga in the courts. An earlier issue that brought about the 2015 *Gauweiler* ruling, after over 35,000 litigants had filed a case before the *BVerfG*, was that several states faced a sovereign debt market panic.³ The ECB had to decide whether, and if so how, it should intervene to stop the panic, which it did by announcing the Outright Monetary Transactions (OMT) programme and citing existing doubts about the continued existence of the Eurozone and their effect on the ECB's monetary policy. The *Weiss* case originates in the challenge of how the ECB should act when its pre-crisis instruments are no longer able to achieve the central bank's self-imposed 2% inflation target.⁴ This confronted the ECB with the choice between allowing a temporary divergence from the inflation target and risking deflation or using unconventional Quantitative Easing (QE) operations. The ECB chose the latter option, but its choices were highly contested even among central bankers.⁵ The two cases, however, do not exhaust the topics on which the ECB is now navigating unexplored waters. Around the world, central bankers are

² For useful overviews of the role of price stability in the EMU architecture, see: Herdegen, "Price Stability and Budgetary Restraints in the Economic and Monetary Union: the Law as Guardian of Economic Wisdom", 35 *Common Market Law Review* (1998), 9.; Borger, "Outright Monetary Transactions and the stability mandate of the ECB: *Gauweiler*", 53 *Common Market Law Review*; *Common Mark.Law Rev.* (2016), 139–196.

³ Case C-62/14, *Gauweiler et al. v. Deutscher Bundestag*, EU:C:2015:400; 2 BvR 2728/13 etc., *OMT reference*, *BVerfGE* 134, 366, Order of 14 Jan. 2014, ECLI:DE:BVerfG:2014:rs20140114.2bvr272813 (hereafter: "*BVerfG OMT reference*"); 2 BvR 2728/13 et al., *OMT II*, *BVerfGE* 142, 123, Judgment of 21 June 2016, ECLI:DE:BVerfG:2016:rs20160621.2bvr272813 (hereafter: "*BVerfG OMT final*"). The number of litigants is based on *Mehreen Khan*, 'Not a good day for democracy' - German critics attack ECB court ruling, *Financial Times*, 21/06/2016.

⁴ Case C-493/17, *Weiss and Others*, EU:C:2018:1000; 2 BvR 859/15 etc., *PSPP*, Order of July 18 2017, ECLI:DE:BVerfG:2017:rs20170718.2bvr085915 (hereafter: "*BVerfG PSPP reference*").

⁵ See e.g.: *Claire Jones and Stefan Wagstyl*, The eurozone: A strained bond, *Financial Times*, 18/01/2015.

increasingly aware that monetary policy impacts new economic policy objectives such as financial stability and environmental sustainability. In achieving its price stability objective, the central bank could now take these objectives into account and weigh them against each other in implementing its monetary policy, or ignore the relevance of these scientific insights. In the existing institutional set-up, in sum, the ECB will continue to face what we term “authorization gaps”: the central bank has to make choices for which its mandate provides almost no guidance, but which have far-reaching consequences.

In this paper we analyze how this new reality of central banking challenges the continued democratic legitimacy of the ECB’s monetary policy operations and ask to what extent judicial review of central bank action can address this problem. As a consequence of the authorization gaps in the ECB mandate, there is currently no clear democratic answer for many choices the ECB faces. This new situation also complicates the role of judicial review. In the monetarist paradigm the courts could supposedly safeguard the ECB’s democratic legitimacy by ensuring it did not overstep the confines of its legal mandate. In the new paradigm, it turns out that the central bank makes momentous choices even when pursuing its legal mandate, but for which the mandate offers little guidance. The ECJ and BVerfG’s judgments on the ECB’s unconventional monetary programmes reflect distinctly divergent approaches to this problem. The Luxembourg Court allows the ECB broad discretion in pursuing its mandate. This, however, moves concerns about the central bank’s democratic legitimacy decidedly to the background. For the BVerfG these democratic legitimacy problems are front and central. The Karlsruhe judges are unwilling to give the ECB the broad leeway that the ECJ allows it. Instead the BVerfG requires judicial review that weighs in on the ECB’s choices. This approach, however, puts the German judges themselves in a position of making decisions with immense consequences. It is as BVerfG judge Gertrude Lübbe-Wolff put it a few years ago in explaining why they should not take up such a role: “an anomaly of questionable democratic character”.⁶ Both the Luxembourg and Karlsruhe judges, like the Frankfurt central bankers, are neither democratically elected nor democratically accountable. If it is democratically illegitimate for the central bankers to make significant policy decisions, the same holds for the courts. Because judicial review cannot provide adequate democratic authorization, however, the solution must come from outside the courts. We, therefore, propose putting the ECB’s democratic legitimacy on a more secure footing and explore different options for doing this. Only by providing it with adequate democratic authorization will the ECB be able to play its part in responding to the economic policy challenges of the 21st century.

The structure of our argument is as follows. In section 2, we outline the monetarist paradigm that informs the creation of the monetary union in the Maastricht Treaty and we discuss in more detail how this paradigm offers a democratic justification for the ECB’s narrow mandate. In section 3, we show how after 2008 the ECB has been confronted with new challenges that its mandate does not address and that force the ECB to make immensely far-reaching and difficult choices. This makes the democratic authorization previously provided to the ECB by its legal mandate inadequate. In section 4, we critically discuss the ECJ and BVerfG’s review of the ECB’s action through a focus on the Weiss-controversy. The ECJ’s permissive review allows the ECB to respond to a new reality, but leaves the situation of insufficient democratic authorization in place. The BVerfG approach highlights this democratic problem, but its hands-on proportionality

⁶ BVerfG OMT reference, dissenting opinion of justice Lübbe-Wolff, par. 28.

assessment requires courts to weigh in on how the ECB should choose between competing alternatives. This, we argue, is not a role courts are well-equipped to play. The proper response to the ECB's new role is to improve the democratic authorization for its operations. For this we explore several options in section 5. We contend that even within the current constitutional architecture there are several possibilities to provide the ECB's monetary policy with enhanced democratic authorization. Section 6 sums up the arguments.

2. Democratic legitimacy and central bank independence before 2008

Historically, central banks have pursued a wide variety of objectives by using a wide variety of tools. In response to high levels of inflation in the late 1970s, policymakers around the world came to endorse the idea that central banks should be made independent from elected governments. These ideas constitute the paradigm of an inflation-targeting independent central bank, which gave the background for the drafting of the Maastricht Treaty and the ECB mandate contained therein.

This section explores how the ECB's immense power to pursue monetary policy in independence was historically justified. We first outline the monetarist paradigm, which provided the intellectual background to the ECB mandate (2.1). On the monetarist conception, the overriding objective of monetary policy is price stability, which central banks pursue as a technical task of setting interest rates. The idea that monetary policy is a technical matter offers a democratic justification for central bank independence, which in turn supplied a basis for the 1993 BVerfG judgment on the Maastricht Treaty (2.2).

2.1 The Monetarist Paradigm

The 1980s saw broad ideational convergence on how to use the state's ability to create money, which provided the intellectual background for the design of the EMU.⁷ We refer to this set of ideas as the monetarist paradigm of central banking.⁸ The first assumption of this paradigm is that price stability should be the overriding objective of monetary policy, because by pursuing price stability the central bank supports economic growth and employment in accordance with the long-term potential of the economy. The second assumption is the idea that public money creation should be used to set interest rates with the aim of steering the economy towards its long-term potential.

Consider first the idea that the economy has a long-term trajectory of potential output that exists largely independent of monetary policy. Popularized by Milton

⁷ McNamara, *The Currency of Ideas: Monetary Politics in the European Union* (Cornell University Press, 1998); Dyson and Featherstone, *The Road to Maastricht: Negotiating Economic and Monetary Union* (Oxford University Press, 1999); James, *Making the European Monetary Union* (Harvard University Press, 2013).

⁸ The term "monetarism" refers to the historical shift in ideas about central banks, which led to monetary policy being perceived as something important, technical, ideally isolated from electoral politics and set in isolation from fiscal policy. Milton Friedman himself favoured direct control of monetary aggregates over interest rate setting, while key ideas are much older: the idea of the long-term neutrality of money was formulated by David Hume, arguments in favour of central bank independence go back at least to Henry Thornton, while the macroeconomic use of policy rates originates in the nineteenth century central bank practice. Friedman, "The Role of Monetary Policy", *58 American Economic Review* (1968), 1–17, at 15; Arnon, *Monetary Theory and Policy from Hume and Smith to Wicksell: Money, Credit, and the Economy* (Cambridge University Press, 2010).

Friedman, long-term neutrality means that the power of policymakers to stimulate the economy is limited.⁹ The economy's potential output is determined by consumer preferences and the productive capacities of the economy. When policymakers use monetary policy to push the economy above its potential output, prices rise. If policymakers do this repeatedly, market actors come to incorporate inflation expectations into their price-setting behaviour, giving rise to ever higher prices. This line of reasoning led Friedman to conclude that "there is always a temporary trade-off between inflation and unemployment; there is no permanent trade-off."¹⁰

This conception of long-term neutrality became widely accepted after the 1970s' experience of high inflation.¹¹ In 1980, the Federal Reserve, led by Chairman Paul Volcker, raised interest rates as high as 20%.¹² This drove the world economy into a deep recession, but effectively ended a period of high inflation. In Europe, the independent Bundesbank and Swiss National Bank were celebrated for their domestic pursuit of price stability. Econometric evidence appeared to suggest that countries with independent central banks did better at fighting inflation. Hence, the interpretation of the 1970s that came to prevail was that elected governments had made a technical error. Their budgetary policies had aimed to push the economy above its long-term potential, while countries with monetary policy geared towards price stability could avoid such errors.¹³

The second assumption of the monetarist paradigm is that the central bank should pursue price stability by steering interest rates. Indeed, from the late 1990s, it could be stated that "all the central banks in industrial countries implement monetary policy through market-oriented instruments geared to influencing closely short-term interest rates as operating objectives".¹⁴ Despite its pervasive impact on the economy, setting rates is understood as a technical task, which involves the use of one instrument to pursue a clearly defined goal. Since there is only one value of the instrument that is compatible with the achieving the long-term potential of the economy, the discretion of the central bank is very limited.

⁹ Friedman, "The Role of Monetary Policy", 58 *American Economic Review* (1968), 1–17; Klooster, van 't, "Central banking in Rawls's Property-Owning Democracy", 47 *Political Theory* (2019), 674–698, at 685–6.

¹⁰ Friedman, "The Role of Monetary Policy", 58 *American Economic Review* (1968), 1–17, at 11.

¹¹ McNamara, *The Currency of Ideas: Monetary Politics in the European Union* (Cornell University Press, 1998); Blyth, *Great Transformations: Economic Ideas and Institutional Change in the Twentieth Century* (Cambridge University Press, 2002); Eich and Tooze, "The Great Inflation" in Manteuffel, oering-, Raphael, and Schlemmer (Eds.), *Vorgeschichte der Gegenwart. Dimensionen des Strukturbruchs nach dem Boom* (Vandenhoeck & Ruprecht, 2016), pp. 173–196.

¹² Greider, *Secrets of the Temple: How the Federal Reserve Runs the Country* (Simon & Schuster, 1989); Krippner, *Capitalizing on Crisis* (Harvard University Press, 2011).

¹³ Emerson *et al.*, *One Market, One Money: An Evaluation of the Potential Benefits and Costs of Forming an Economic and Monetary Union* (Oxford University Press, 1992), chap. 4; Borio, *A hundred ways to skin a cat: comparing monetary policy operating procedures in the United States, Japan and the euro area*, BIS Working Papers, 9 (Bank for International Settlements, 2001); Bernanke *et al.*, *Inflation targeting: lessons from the international experience* (Princeton Univ. Press, 2001).

¹⁴ Borio, *A hundred ways to skin a cat: comparing monetary policy operating procedures in the United States, Japan and the euro area*, BIS Working Papers, 9 (Bank for International Settlements, 2001), at 1; Bindseil, *Monetary policy operations and the financial system* (Oxford University Press, 2014).

2.2 Central bank independence, Democratic Legitimacy and the BVerfG

Maastricht judgment

Monetarist ideas are visibly reflected in the ECB's legal mandate: price stability is its primary objective.¹⁵ The monetarist paradigm also informs the justification of its high level of independence, which is most clearly reflected in Article 130 TFEU. This provision prohibits Member States' governments, Union institutions or any other body from seeking to influence the ECB's decision-making, and prohibits the ECB from seeking instructions from these actors.¹⁶ Such independence may at first sight seem incompatible with the requirement of democratic legitimacy, since it leaves major decisions to unelected officials who do not stand in a hierarchical relationship to democratically accountable politicians. Building on the monetarist paradigm of central banking, however, there was a clear democratic justification of central bank independence. This justification assumes that central bankers take the outcomes of democratic deliberations as the basis of their actions and then choose the most appropriate course of action in light of considerations of efficiency and technical feasibility. That democratic justification in turn informed the BVerfG Maastricht judgment.

Political legitimacy refers to the justification of public authority.¹⁷ There are broadly two types of features that can provide legitimacy to political decisions and decision-making procedures. The first focuses on the outcomes that such decision-making achieves. Approaching legitimacy in this way requires specifying normative criteria for outcomes and using these to assess the substance of decisions. The normative appeal of democracy is strongly connected to a second strategy, which focuses on process or input rather than outcomes. Democracy has this appeal, because it provides a response to the fact that the quality of outcomes is often a matter of pervasive disagreement.¹⁸

Focusing on outcomes, proponents of central bank independence suggest that democratic institutions are myopic and that their direct accountability to citizens precludes effectively implementing a long-term oriented monetary policy.¹⁹ A closely related argument focuses on *credible commitment*. An independent central bank serves to signal a strong and credible commitment to price stability, which is meant to have

¹⁵ Articles 127 (1) and 282 (2) TFEU, as well as Article 2 of the Statute on the ESCB and ECB. On the role of price stability in the Maastricht EMU architecture see: Herdegen, "Price Stability and Budgetary Restraints in the Economic and Monetary Union: the Law as Guardian of Economic Wisdom", 35 *Common Market Law Review* (1998), 9; Borger, "Outright Monetary Transactions and the stability mandate of the ECB: Gauweiler", 53 *Common Market Law Review*; *Common Mark.Law Rev.* (2016), 139–196.

¹⁶ See also Article 282(3) TFEU. For the further organic, functional and financial safeguards for the ECB's independence, see: Lastra, "The Independence of the European System of Central Banks", 33 *The Harvard International Law Journal* (1992), 475–520, at 482 – 496.; as well as René Smits, *The European Central Bank, Institutional Aspects* (Kluwer Law International, 1997), at 155–158.

¹⁷ Scharpf, F., *Governing in Europe: Effective and Democratic?* (Oxford University Press, 1999); Bellamy, "Democracy without democracy? Can the EU's democratic 'outputs' be separated from the democratic 'inputs' provided by competitive parties and majority rule?", 17 *Journal of European Public Policy* (2010), 2–19.

¹⁸ Waldron, *Law and Disagreement* (Oxford University Press, 2001); Bellamy, *Political Constitutionalism: A Republican Defence of the Constitutionality of Democracy* (Cambridge University Press, 2007).

¹⁹ Kydland and Prescott, "Rules Rather than Discretion: The Inconsistency of Optimal Plans", 85 *Journal of Political Economy* (1977), 473–491; Blinder, *Central banking in theory and practice*, The Lionel Robbins lectures (MIT Press, 1999).

beneficial effects on markets. Independent central banks are thought to do better in setting monetary policy in line with the objective of price stability than elected governments.²⁰

However, these outcome-based arguments in favour of central bank independence are deeply contested. Although early studies suggested that central bank independence contributes to lower inflation, the issue remained far from settled.²¹ Another at least equally plausible explanation of the correlation between independence and inflation is that countries that for historical reasons are inflation averse, like Germany and Switzerland, are also more willing to accept an independent central bank. Independence also has downsides: it limits the policy levers available to elected governments, while hindering effective coordination of monetary and fiscal policy.²² More fundamentally, the monetarist idea that price stability should be assigned overriding importance remained deeply disputed throughout the 1980s and 1990s.²³

Given disagreement over the best use of monetary policy, procedural arguments always had a key role in providing central bank independence with legitimacy.²⁴ Indeed, the very fact that these benefits are contested suggests that the decision whether to make a central bank independent should itself be left to democratic decision-making. Democratic procedures provide an answer to the question of what to do in the face of such disagreement, which rests on fair procedures and the adequate representation of competing interests and viewpoints.²⁵ Representative democracies allow citizens to participate in political decision-making in various ways, in particular by giving them the right to vote for representatives and stand for election in regular competitive elections. To the extent that representative institutions are responsive to public opinion, citizens can exert a continuous influence on political decision-making.²⁶ The participatory mechanisms allow citizens to contribute to political will-formation prospectively, while also allowing them to retrospectively hold their representatives to account and vote them

²⁰ Emerson *et al.*, *One Market, One Money: An Evaluation of the Potential Benefits and Costs of Forming an Economic and Monetary Union* (Oxford University Press, 1992); Alesina and Summers, “Central Bank Independence and Macroeconomic Performance: Some Comparative Evidence”, 25 *Journal of Money, Credit and Banking* (1993), 151–62.

²¹ Alesina and Summers, “Central Bank Independence and Macroeconomic Performance: Some Comparative Evidence”, 25 *Journal of Money, Credit and Banking* (1993), 151–62; Posen, A.S., “Declarations Are Not Enough: Financial Sector Sources of Central Bank Independence”, *NBER* (1995), 253–274; Forder, “The case for an independent European central bank: A reassessment of evidence and sources”, 14 *European Journal of Political Economy* (1998), 53–71; McNamara, “Rational Fictions: Central Bank Independence and the Social Logic of Delegation”, 25 *West European Politics* (2002), 47–76.

²² Ryan-Collins and Lerven, van, *Bringing the Helicopter to Ground. A Historical Review of Fiscal-Monetary Coordination to Support Economic Growth in the 20th Century*, 2018; Braun and Downey, *Against Amnesia: Re-Imagining Central Banking*, 2020.

²³ Kaldor, *The Scourge of Monetarism* (Oxford University Press, 1985); Arestis and Sawyer, “Unemployment and the Independent European System of Central Banks”, 56 *American Journal of Economics and Sociology* (1997), 353–367.

²⁴ Elgie, “The politics of the European Central Bank: principal-agent theory and the democratic deficit”, 9 *Journal of European Public Policy* (2002), 186–200; Lastra, *International Financial and Monetary Law*, 2nd ed. (Oxford University Press, 2015); Tucker, *Unelected Power: The Quest for Legitimacy in Central Banking and the Regulatory State* (Harvard University Press, 2018); Klooster, van ’t, “The Ethics of Delegating Monetary Policy”, 82 *Journal of Politics* (2020), 587–599.

²⁵ Waldron, *Law and Disagreement* (Oxford University Press, 2001); Bellamy, *Political Constitutionalism: A Republican Defence of the Constitutionality of Democracy* (Cambridge University Press, 2007).

²⁶ On this interaction and its relation to democratic legitimacy see: Habermas, *Between Facts and Norms* (Polity Press, 1996).

out of office. The first of these aspects we call democratic *authorization*, the second democratic *accountability*.

The monetarist paradigm informs the democratic justification of central bank independence. It helps to explain why such independence is compatible with the requirements of democratic authorization and accountability. The democratic justification starts off from the observation that it is in principle not undemocratic for a government to bind itself. Democratic legitimacy, in this account, depends crucially on a prospective act of *authorization* by means of a legal mandate, which provides the central bank with a well-defined set of powers and conditions for their use. Clear guidance on how to pursue price stability, while often absent from the mandate itself, can be read into it relying on the monetarist conception of monetary policy. The idea of long-term neutrality suggests that central banks face only limited political choices. The central bank cannot push the economy above its long-term potential. Instead, its task is limited to finding the level of interest rates that steers the economy towards that potential. This makes monetary policy a predominantly technical issue. The main political decisions are made in the legal mandate, which is drafted by a legislature that has its own clear sources of democratic legitimacy. It also means that a central bank does not acquire any arbitrary powers, because it has no discretion to do more than pursue the price stability objective assigned to it.

The central bank's *accountability*, theorized as independent accountability, is limited to explaining the central bank's actions with reference to its mandate.²⁷ This explanation is procedural in the sense that it focuses on the way that the central bank has sought to use the instruments provided within the mandate to achieve the objectives spelled out in the mandate. The simple and quantitative nature of inflation as a target of monetary policy constitutes a clear standard by which to evaluate whether the central bank has succeeded in achieving the goals assigned to it. Accountability serves to demonstrate that the central bank's actions as a matter of fact realize the central bank's democratic mandate. Given that the central bank's independence limits democratic accountability by excluding any form of political sanctions, a crucial role goes to the courts. It is their role to safeguard that the central bank operates within the confines of its legal mandate and to sanction transgressions.²⁸

²⁷ Lastra, "The Independence of the European System of Central Banks", 33 *The Harvard International Law Journal* (1992), 475–520; Lastra, *International Financial and Monetary Law*, 2nd ed. (Oxford University Press, 2015), chap. 2; Issing, "The Eurosystem: Transparent and Accountable or 'Willem in Euroland'", 37 *JCMS: Journal of Common Market Studies* (1999), 503–519; Magnette, "Towards 'Accountable Independence'? Parliamentary Controls of the European Central Bank and the Rise of a New Democratic Model", 6 *European Law Journal* (2000), 326–340; ECB, "The accountability of the ECB", November *Monthly Bulletin* (2002), 45–57; Fromage *et al.*, "ECB independence and accountability today: Towards a (necessary) redefinition?", 26 *Maastricht Journal of European and Comparative Law* (2019), 3–16. Rene Smits, "Accountability of the European Central Bank", *Ars Aequi* (2019), 27–37. For a critical assessment, see: Deirdre Curtin, "'Accountable Independence' of the European Central Bank: Seeing the Logics of Transparency", 23 *European Law Journal* (2017), 28–44.

²⁸ Lastra, "The Independence of the European System of Central Banks", 33 *The Harvard International Law Journal* (1992), 475–520, at 500; Scheller, *The European Central Bank: History, Role and Functions*, 2nd ed. (European Central Bank, 2006). Amtenbrink, Fabian, "Economic and Monetary Union" in Kuijper, Pieter Jan and et.al. (Eds.), *The Law of the European Union* (Kluwer Law International, 2018), pp. 883–950., at p. 940.

The BVerfG 1993 Maastricht judgment reflects this set of ideas on the democratic justification of central bank independence. One question at stake there was whether the Maastricht Treaty undermined the democratic rights of German citizens by delegating monetary policy to an independent ECB.

In answering that question, the BVerfG interpreted the right to vote of Article 38 of the *Grundgesetz* as giving German citizens not merely a formal right to elect a parliament, but also its “fundamental democratic content”.²⁹ This entails that the constitutional right to vote safeguards that German citizens can actually legitimize the exercise of public authority by electing the *Bundestag*. As the transfer of competences to the EU affects the *Bundestag*’s powers, it affects this democratic substance of German citizens’ right to vote. Secondly, such competence transfers would be incompatible with the *Grundgesetz* were they to hollow out the *Bundestag*’s powers to such a degree that the democratic principle of Articles 20 (1) and (2) protected by Article 79 (3) *Grundgesetz* would be violated.³⁰ Thirdly, the loss of democratic legitimacy could not be fully compensated at the EU level, because the EU was deemed to lack fully developed democratic structures and the German court considered that creating successful democratic structures at the EU level would depend on “certain pre-legal conditions”.³¹ These conditions, such as a common European public sphere, language and shared identity were not fully present at the EU level. On the basis of these reasons the BVerfG concluded “that functions and powers of substantial importance must remain for the German Bundestag.”³² The democratic legitimacy of the Union’s authority meanwhile depends crucially on the *Bundestag*’s assent to the transfer of powers to the EU as contained in the national statute approving the Treaty.³³ This opens the way for *ultra vires* review of EU acts: Union acts no longer covered by the Treaty would lack democratic legitimation from the *Bundestag* and could not be given effect in the German legal order.³⁴

The German judges acknowledged that the Bank’s independence removed an “essential political area” from democratic influence and control.³⁵ However, they held that German participation in the EMU complied with constitutional requirements, because the monetary union was conceived as a “*Stabilitätsgemeinschaft*”, a community devoted to “guarantee price stability as a matter of priority”.³⁶ They upheld the ECB’s independence as “a modification” of the democratic rights of citizens,³⁷ which was justified by reference to

²⁹ 2 BvR 2134, 2 BvR 2159/92, *Maastricht*, BVerfGE 89,155, Judgment of 12 Oct. 1993 (hereafter: “*BVerfG Maastricht*”) (translation in [1994] C.M.L.R. 57), par. 61.

³⁰ *BVerfG Maastricht*, par. 62 and 63.

³¹ *BVerfG Maastricht*, par. 98.

³² *BVerfG Maastricht*, par. 102.

³³ *BVerfG Maastricht*, par. 94 and par. 46-49, 103-106 As a result, the principle of conferral becomes of crucial German constitutional importance. The German court repeats this fundamental idea in its *PSPP*-ruling. See: *PSPP*, par. 158.

³⁴ *BVerfG Maastricht*, par. 106.

³⁵ *BVerfG Maastricht*, par. 153.

³⁶ *BVerfG Maastricht*, par.138 *Maastricht*.

³⁷ The BVerfG construes the ECB’s independence as a modification of the constitutional principle of democracy. This modification is explicitly enshrined in Article 88 of the German Basic Law and compatible with the eternity clause of Article 79 (3) of the Basic Law.

“the special characteristic (tested and proven—in scientific terms as well—in the German legal system) that an independent central bank is a better guarantee of the value of the currency [...] than state bodies, which as regards their opportunities and means for action are essentially dependent on the supply and value of the currency, and rely on the short-term consent of political forces.”³⁸

Just like the Bundestag was allowed to delegate monetary policy to a domestic central bank, it was also allowed to delegate it to an independent EU-institution.

The independence of the ECB was, hence, permitted on the assumption that it would pursue a well-defined task in stabilizing the currency. The flipside of this argument was that if the EMU would depart from its stability conception, Treaty change would be necessary or Germany would have to abandon the currency union altogether.³⁹ Already in the *Maastricht-Urteil*, the Karlsruhe judges therefore opened the possibility that they would police the limits of the ECB mandate.⁴⁰

3. Authorization gaps in the ECB mandate

The monetarist interpretation of the ECB mandate suggests that the ECB has a clear objective and well-defined instruments to pursue it. This interpretation of the mandate provided the ECB’s operations with legitimacy and also implied a straightforward but limited role for judicial review. The actual text of the legal mandate, however, was always much less strict than the monetarist interpretation allowed for. It contains authorization gaps in the sense that the legal text does not prescribe a clear course of action for the significant choices that the ECB faces (3.1). In the past decade, the ECB faced new challenges, which led it to make extensive use of the space available in its mandate to design new operations (3.2).

3.1. The monetarist interpretation of the ECB mandate

In its early years, the ECB came to adopt a very restrictive account of its role in the implementation of monetary policy. This broadly fitted the monetarist vision that had informed the drafting of the Maastricht Treaty and the *BVerfG*’s Maastricht ruling:

Competency for monetary policy is transferred within the limits and the conditions of a mandate which clearly defines the objective of monetary policy and thus limits the amount of legally permitted discretion that the decision-making bodies of the ECB can use in conducting monetary policy.⁴¹

From the beginning, there was considerable distance between the legal text and this monetarist interpretation of the ECB mandate, so that important choices were left to the ECB. First, the goals conferred on the ECB were not codified as such in the Treaty and

³⁸ *BVerfG Maastricht*, par. 154. The *BVerfG* referred in this respect also to the justification for the *Bundesbank*’s independence, see BT Drucksache 2/2781, p. 24-25.

³⁹ *BVerfG Maastricht*, par. 148.

⁴⁰ *BVerfG Maastricht*, par. 106.

⁴¹ Scheller, *The European Central Bank: History, Role and Functions*, 2nd ed. (European Central Bank, 2006), at 127. The preface by former president Jean-Claude Trichet positions the book as explaining the ECB’s aims and activities as a part of its “communication with the world of banking, market participants, academia and the general public” (at 9).

leave considerable discretion to the ECB. Article 127(1) assigns to the ECB an “overriding” objective of price stability, but nowhere do the Treaties define what price stability is. Instead, Article 127 (2) TFEU leaves it to the ECB itself to “define and implement the monetary policy of the Union”⁴². The mandate also permits the ECB to “support the general economic policies in the Union with a view to contributing to the achievement of the objectives of the Union” if this does not prejudice achieving price stability. It is left to the ECB itself to put forward an interpretation of these passages, which the ECB did in 1998 to spell out the 2% target, in 2003 reformulated as close to, but below, 2%, while on both occasions leaving the secondary mandate indeterminate.⁴³

Second, the mandate is very general where it comes to the instruments assigned to the ECB. As the central bankers tasked with drafting the Statute of the ESCB and ECB (hereafter: the ESCB Statute) explained in December 1990, the passages were drafted “with due regard to the evolutionary nature of financial markets” to ensure that the ECB would be able to “respond adequately to changing market conditions”.⁴⁴ Article 18 of the ESCB Statute permits the ECB to trade any “claims and marketable instruments, whether in euro or other currencies”, and also permits lending to counterparties, with the condition that such lending is “based on adequate collateral”. Article 20 licenses the ECB “the use of such other operational methods of monetary control as it sees fit”, conditional on a two-third majority in its governing council. The main substantive constraint on the instrument comes from the monetary financing prohibition in Article 123 TFEU, which prohibits the direct purchase of public debt. It is explicitly drafted, however, to allow for the purchase of government bonds on secondary markets.⁴⁵ This generality stands in striking contrast to the mandate of the Bundesbank, which listed not only permissible assets to trade in, but also specifies in minute detail maturities, required guarantors and other technical risk control measures.⁴⁶

Even if the inflation target and the instruments would have been clearly defined, however, the pursuit of monetary policy would not have been free of far-reaching choices. In its monetarist self-understanding, the discretion accorded to central bankers is mainly of a technical nature and is meant to be exercised solely to find the volume of money creation that steers the economy to its long-term potential. In practice, however, central banks bring down inflation by raising interest rates. This is a blunt tool to bring down inflation, since it achieves its effect by bringing down economic output, raising unemployment and appreciating the currency.⁴⁷ Moreover, there is not one correct way to make the trade-off, since real-time monetary policy making is surrounded by pervasive uncertainty. Central banks, therefore, face a choice in deciding how aggressively to pursue the inflation target, which unavoidably reflects political preferences. In line with the interests of their previous employers, central bankers with a finance background tend to be more inflation averse compared to those with a background in academia or

⁴² See also Article 3.1 ESCB and ECB Statute.

⁴³ ECB, “The outcome of the ECB’s evaluation of its monetary policy strategy”, *Monthly Bulletin* (2003), 79–92.

⁴⁴ CoG, Draft statutes of the European System of Central Banks and the European Central bank with an introductory report and a commentary, 12/1990, 16.

⁴⁵ *Delors Committee*, Report on economic and monetary union in the European Community, 17/04/1989, 22.

⁴⁶ Gesetz über die Deutsche Bundesbank vom 26. Juli 1957 ((BGBl. I S. 745), Arts. 19 to 25.

⁴⁷ Abolafia, “Narrative Construction as Sensemaking: How a Central Bank Thinks”, 31 *Organization Studies* (2010), 349–367; Best, “Rethinking Central Bank Accountability in Uncertain Times”, 30 *Ethics & International Affairs* (2016), 215–232.

government.⁴⁸ In deciding how aggressively to counteract inflation, monetary policy could directly contradict the objectives of governments. In the summer of 1992, the Bundesbank brought down the European Exchange Rate Mechanism (ERM) and sent large parts of the EU economy into a recession by raising interest rates to 9.25% in response to perceived inflation risks resulting from German reunification.⁴⁹ That experience, although it reinforced the view that monetary policy should be left to an EU-level institution, did not lead to a rejection of central bank independence. The economic and social costs of low inflation, it was widely believed, should be accepted in the short run to achieve the long-term objective of price stability. In this sense, monetary policy was meant to be deliberately disproportionate.

The ECB's legal mandate, in sum, was never as clear as the monetarist interpretation suggested. This complicates the idea that its democratic legitimacy could ever be grounded in a prior act of democratic authorization. If the democratic legitimacy of the independent central bank resides in its pursuance of a narrow legal mandate, it must be possible to establish when the central bank acts in pursuit of that mandate and when it oversteps that mandate. This, however, was never provided for in the ECB mandate as such. It was, instead, the monetarist interpretation itself that assigned clear objectives and instruments to the ECB, while downplaying the significance of its side-effects. Agreement on that interpretation hid the underlying legal indeterminacy from sight.

3.2 New challenges

The drafters of the Maastricht treaty left many issues open; they either decided to not address them or falsely assumed that the ECB would not face them. As a consequence, the ECB's legal mandate provided no clear guidance on how the central bankers had to respond to the challenges posed by the Global Financial Crisis and the Eurozone crisis. Nor does the mandate provide such guidance for the current Covid-19 pandemic. These authorization gaps forced the ECB's Governing Council to agree policies not clearly authorized by its mandate, which in turn opened it up to legal challenge.

| Gaps | ECB decisions | Alternative | ECB Programmes |
|-----------------------------|---|---|----------------|
| Sovereign bond market panic | Buying government bonds to stabilize markets | Disruption of the transmission mechanism and possible end of the Euro | SMP, OMT, PEPP |
| Lower zero bound | Designing new tools that allow the ECB to achieve price stability objective | Lowering the inflation target | APP, PEPP |

⁴⁸ Posen, A.S., "Declarations Are Not Enough: Financial Sector Sources of Central Bank Independence", *NBER* (1995), 253–274; Adolph, *Bankers, Bureaucrats, and Central Bank Politics: The Myth of Neutrality*, Cambridge studies in comparative politics (Cambridge University Press, 2013).

⁴⁹ Bibow, "Germany in crisis: the unification challenge, macroeconomic policy shocks and traditions, and EMU", *19 International Review of Applied Economics* (2005), 29–50; Lastra, *International Financial and Monetary Law*, 2nd ed. (Oxford University Press, 2015), paras 2148–58.

| | | | |
|------------------------------------|---|--|---|
| Environmental impact of operations | Implementing market neutral monetary policy | Incorporating green objectives in the design of monetary policy operations | CSPP, collateral requirements on MROs and LTROs, PEPP |
|------------------------------------|---|--|---|

Table 1. Gaps in the mandate and ECB choices after 2008

The 2015 Gauweiler case revolved around the conditions under which (if any) it would be permitted for the ECB to intervene in bonds markets. Prior to the Eurozone crisis, the few government defaults to occur in the 20th century had predated WWII.⁵⁰ Hence, the ECB was expected to be able to leave prices in government bond markets to decentralized price discovery. Its mandate was, accordingly, drafted assuming that binding rules on government expenditures and the no-bailout clause would prevent a sovereign debt market panic from occurring.⁵¹

The ECB's mandate does not provide any guidance on the extent to which and the means by which it should act in the event that a bond market panic would strike an individual member state. The ECB could therefore make a good case that it should intervene, but it could also justify not doing anything. In May 2010, a year after the spreads between Eurozone member states started to widen, the ECB reluctantly decided to buy sovereign bonds as part of its Security Markets Programme (SMP).⁵² In 2012, the ECB announced its OMT programme to signal its willingness to step in – to buy bonds in unlimited volumes – when member states lose access to markets.⁵³ The ECB's recent Pandemic Emergency Purchase Programme again seeks to influence spreads in bond markets.

Facing legal challenges to its OMT-programme, the ECB justified its decision to intervene pointing to the impact of sovereign debt markets on its ability to achieve its price stability mandate.⁵⁴ The programme, the ECB argued, is part of its mandate because the spreads had consequences for the ECB's ability to implement its monetary policy. The large spreads between the member states undermined its ability to shape financial market conditions across the Euro area. The programme does not conflict with the ECB's monetary financing prohibition because it merely prevents “unjustified interest rate hikes”, due to “unfounded fears of investors”,⁵⁵ while the OMT programme contained various safeguards to ensure markets could determine (justified) spreads in response to economic fundamentals.⁵⁶

⁵⁰ Reinhart and Rogoff, *This Time is Different: Eight Centuries of Financial Folly* (Princeton Univ. Press, 2009); Hébert and Schreger, *The Costs of Sovereign Default* (International Monetary Fund, 2016).

⁵¹ Delors Committee, Report on economic and monetary union in the European Community, 17/04/1989, 20. Touri and Tuori, *The Eurozone Crisis. A Constitutional Analysis* (Cambridge University Press, 2014), p. 48-55.

⁵² ECB, ECB decides on measures to address severe tensions in financial markets, <<https://www.ecb.europa.eu/press/pr/date/2010/html/pr100510.en.html>>, (last visited 2010).

⁵³ ECB, Technical features of Outright Monetary Transactions, (last visited 2020).

⁵⁴ See: *BVerfG OMT reference*, par. 7-12; *ECJ Gauweiler*, par. 46-56.

⁵⁵ *BVerfG OMT reference*, par 7.

⁵⁶ See also: ‘Compliance of outright monetary transactions with the prohibition on monetary financing’ ECB Monthly Bulletin October 2012, p. 7-9; and opinion AG Cruz-Villalón in *Gauweiler*, par. 209-212.

Although the announcement of the OMT-programme in 2012 is widely credited with ending the Eurozone crisis, the ECB could just as well have argued that it should not act. For one thing, it is not clear whether and under what conditions repairing the transmission mechanism falls within the remit of monetary policy. The claim that this should be determined by distinguishing justified and unjustified spreads is developed based on a particular interpretation of the monetary financing prohibition. On the view of Gauweiler and others, for example, the OMT-programme led to a “suspension of the market mechanisms which violates the Treaties”; a view also supported by Bundesbank president Jens Weidmann in his testimony.⁵⁷ The ECB could, therefore, easily have justified not implementing such a programme by formulating a narrow interpretation of its task or a stricter interpretation of the monetary financing prohibition.⁵⁸ Without going into the details of these different legal arguments, we merely want to show here that from the perspective of the mandate, it is genuinely unclear whether, and if so how, the ECB should manage prices in sovereign debt markets. Confronted with an (impending) debt crisis, the mandate does not tell the ECB whether or not to influence market conditions and if so to what extent. It was left to the ECB’s Governing Council to decide what sovereign bond market spreads to accept, and hence whether these could drive individual member states into bankruptcy or not.

The topic of the Weiss-case is a very similar gap in the ECB mandate, namely the issue of what it should do if the tool of setting short-term interest rates is insufficient to achieve the ECB’s inflation target. After 2008, central banks became confronted with what is known as the problem of the so-called zero lower bound. From November 2013 onwards, the ECB’s target rate for short term policies has been below 0.25% (today it is at 0%). This so-called lower zero bound constitutes a technical limit of the interest rate tool, because the interest rate on bank notes is by definition 0%. Moving short term interest rates on central bank deposits much lower would incentivize financial institutions to reallocate their portfolio towards bank notes. This led the ECB to introduce the Asset Purchase Programme (APP).⁵⁹ The public sector purchase programme (PSPP), which is the focus of the Weiss-ruling, is the government bond buying programme that is part of the APP. The ECB also created programmes for the purchase of corporate bonds (CSPP), asset-backed securities (ABSPP) and covered bonds (CBPP1-3). By purchasing bonds, the ECB was able to bring down interest rates in financial markets without needing to lower its deposit rate further.

The problem of the lower-zero bound again confronted the ECB with choices that do not have a clear answer in its mandate. It could either decide to accept inflation below its self-imposed 2% objective or introduce a new set of instruments. The mandate permits both. By purchasing bonds, the ECB chose to continue pursuing its pre-crisis inflation target. However, as we saw, the definition of that target is one proposed by the ECB itself and various members of the ECB’s Governing Council expressed a preference for lower inflation instead. As Jens Weidmann explained in the German *Bild Zeitung*, to the extent that lower prices were a consequence of low oil prices, they should be disregarded by the

⁵⁷ *BVerfG OMT reference*. par. 4-5; 13-15; Weidmann, Eingangserklärung anlässlich der mündlichen Verhandlung im Hauptsacheverfahren ESM/EZB, 11 June 2013, available at <<https://www.bundesbank.de/de/presse/stellungnahmen/eingangserklaerung-anlaesslich-der-muendlichen-verhandlung-im-hauptsacheverfahren-esm-etz-662878>>.

⁵⁸ *BVerfG OMT reference*. par. 5.

⁵⁹ Decision (EU) 2015/774 of the European Central Bank of 4 March 2015 on a secondary markets public sector asset purchase programme (ECB/2015/10)

ECB.⁶⁰ More recently Dutch central bank president Klaas Knot argued that the fact that the “inflation outlook lags behind the ECB’s aim” “is worrying, but it does not imply that restarting a far-reaching measure such as the APP is the appropriate instrument”.⁶¹ On all accounts, the ECB’s asset purchase programmes have had an immense impact on the fiscal space of governments and basically any meaningful macroeconomic variable; according to the ECB’s own account it has created millions of jobs.⁶² Again, it was down to a decision by the ECB’s Governing Council to implement this programme, which it would also have been permitted to abstain from.

Although the two challenges discussed here led to court cases, the ECB has moved beyond tasks clearly defined in its mandate on a much wider range of issues including emergency lending to banks and participation in sovereign debt restructurings.⁶³ The Pandemic Emergency Purchase Programme (PEPP) introduced in March 2020 combines elements of OMT programme and the APP, in ways that are difficult to disentangle; both stabilizing sovereign bond markets as well as pursuing a macroeconomic role in fighting an economic downturn.⁶⁴ The PEPP had an initial envelope of €750 billion, which the ECB’s Governing Council decided to further increase to a total of €1,350 billion in June 2020.⁶⁵ Its design again increases the tension between the narrow role originally envisaged for the ECB by the Maastricht Treaty and its current operations. From a legal perspective, key issues are the programme’s compatibility with the monetary financing prohibition and the ECJ’s proportionality assessment.⁶⁶ The ECJ has held that when the ECB purchases government bonds on secondary markets “sufficient safeguards must be built into its intervention to ensure that [the ECB] does not fall foul of the prohibition of monetary financing”.⁶⁷ In the PEPP-decision, however, the ECB characterises these safeguards as “self-imposed” and indicates that the Governing Council can revise them

⁶⁰ <https://www.bild.de/geld/wirtschaft/anleihe/darum-haben-wir-gegen-das-billionen-paket-der-ezb-gestimmt-39474502.bild.html> “ Sie sind sogar gut, weil sie Verbraucher und Unternehmen um Milliarden Euro entlasten. Das wirkt wie ein Konjunkturprogramm”

⁶¹ DNB, Press release: Klaas Knot comments on ECB policy measures, <<https://www.dnb.nl/en/news/news-and-archive/Persberichten2019/dnb385535.jsp>>, (last visited 13 September 2019).

⁶² Lenza and Slacalek, *How does monetary policy affect income and wealth inequality? Evidence from quantitative easing in the euro area*, ECB Working Paper Series, no. 2190 (European Central Bank, 2018); Hammermann *et al.*, “Taking stock of the Eurosystem’s asset purchase programme after the end of net asset purchases”, 2 *Economic Bulletin* (2019); CGFS, *Unconventional monetary policy tools: a cross-country analysis* (Bank for International Settlements, 2019).

⁶³ Steinbach, “The lender of last resort in the eurozone”, *Common Market Law Review* (2016), 361–383.

⁶⁴ Decision (EU) 2020/440 of the European Central Bank of 24 March 2020 on a temporary pandemic emergency purchase programme (ECB/2020/17).

⁶⁵ ECB, “Monetary Policy Decisions”, available at <<https://www.ecb.europa.eu/press/pr/date/2020/html/ecb.mp200604%7Ea307d3429c.en.html>>; Decision (EU) 2020/1143 of the European Central Bank of 28 July 2020 amending Decision (EU) 2020/440 on a temporary pandemic emergency purchase programme (ECB/2020/36).

⁶⁶ For various legal analyses with different perspectives, see: Bobić, Ana; Dawson, Mark: COVID-19 and the European Central Bank: The Legal Foundations of EMU as the Next Victim?, *VerfBlog*, 2020/3/27, <https://verfassungsblog.de/covid-19-and-the-european-central-bank-the-legal-foundations-of-emu-as-the-next-victim/>, DOI: <https://doi.org/10.17176/20200327-122939-0>; René Smits, “The European Central Bank’s pandemic bazooka: mandate fulfilment in extraordinary times”, *EU Law Live*, 23 March 2020; Sebastian Grund, ‘Legal, compliant and suitable: The ECB’s Pandemic Emergency Purchase Programme (PEPP)’, Policy Brief Hertie School, Jacques Delors Centre, <https://www.delorscentre.eu/en/publications/detail/publication/legal-compliant-and-suitable-the-ecbs-pandemic-emergency-purchase-programme-pepp/>.

⁶⁷ *ECJ, Gauweiler*, par. 102; *ECJ, Weiss*, par. 107.

“to the extent necessary to make its action proportionate to the risks faced.”⁶⁸ The central bank also departs from safeguards in earlier programmes. Greek government debt is explicitly included in the programme, which in light of its current credit rating goes against the earlier minimum credit rating requirement on the APP programme. The ECB has also given up on previous issuer limits, allowing it to purchase a much larger volume of debt of specific Member States. Finally, where the availability of OMT emergency lending is subject to an ESM programme, the PEPP is to be used entirely at the discretion of the ECB’s executive board. These features are already leading to further legal challenges. In June 2020, the *Alternative für Deutschland* announced that it would bring a new lawsuit to Karlsruhe against the PEPP, while Mr. Gauweiler has signalled a similar intention.⁶⁹

It is unlikely that litigation over ECB monetary policy will end any time soon, since the authorization gaps in the ECB mandate are likely to become only larger over time. Before 2008, monetary policy could focus on the narrow task of setting one interest rate, because it was assumed that financial markets could be left largely to their own devices. In the past years, central bankers have not only come to question that assumption, but also recognize that their operations shape the long-term trajectory of financial markets. Central bankers now regularly publish on how the design of monetary policy operations affects financial markets and the real economy.⁷⁰ One particularly controversial example of such impact is the ECB’s self-imposed policy of “market neutrality”, which requires it to purchase bonds relative to the volume of Euro-denominated bonds issued.⁷¹ A consequence of this policy is that the ECB’s Corporate Securities Purchase Programme (CSPP) is biased towards debt issued by carbon-intensive firms such as utilities, companies engaged in fossil fuel extraction, and car manufacturers. Because carbon-intensive firms tend to rely more on bond financing than other sectors, the volume of debt of these firms purchased by the ECB is disproportionately large relative to the firms’ size in the EU-economy.⁷² The CSPP thus brings down funding costs for carbon-intensive sectors, thereby encouraging more investment by firms in those sectors. The market neutrality policy, however, has only a shallow basis in the ECB mandate, which merely contains the generic requirement that the ECB should operate “in accordance with the principle of an open market economy”. The ECB’s secondary mandate could also readily justify designing its operations to actively favour low-carbon sectors and bond issuers.⁷³ However, despite the immense significance of the EU’s climate-related and environmental objectives, there is simply no clear legal answer to the

⁶⁸ Decision (EU) 2020/440 of the European Central Bank of 24 March 2020 on a temporary pandemic emergency purchase programme (ECB/2020/17), recital (6).

⁶⁹ <https://www.sueddeutsche.de/politik/gauweiler-etz-anleihen-1.4952757>;

<https://www.omfif.org/2020/06/fresh-german-legal-battle-over-ecb-easing/>

⁷⁰ BIS, Central bank operating frameworks and collateral markets, 31/03/2015; *Corradin, Heider, and Hoerova*, On collateral: implications for financial stability and monetary policy, 2017; *Bolton et al.*, The green swan: Central banking and financial stability in the age of climate change, 2020.

⁷¹ Klooster, van ’t and Fontan, “The Myth of Market Neutrality: A Comparative Study of the European Central Bank’s and the Swiss National Bank’s Corporate Security Purchases”, *New Political Economy* (2019).

⁷² *Matikainen, Campiglio, and Zenghelis*, The climate impact of quantitative easing, 2017.

⁷³ Article 127(1) TFEU; Solana, “The Power of the Eurosystem to Promote Environmental Protection”, 30 *European Business Law Review* (2019), 547–575; Cerrato, Agostini, and Jaberg, Why the PSPP judgment of the German Federal Constitutional Court gives the ECB another incentive to integrate climate change considerations into monetary policy, <<https://europeanlawblog.eu/2020/05/27/why-the-pspp-judgment-of-the-german-federal-constitutional-court-gives-the-ecb-another-incentive-to-integrate-climate-change-considerations-into-monetary-policy/>>, (last visited 27 May 2020).

question how, if at all, the ECB should contribute to them. In June 2020, the BVerfG dismissed a case against the CSPP programme, but signalled that a programme like the CSPP might qualify as economic policy rather than monetary policy if it amounted to state aid or a substantial distortion of competition.⁷⁴ Future ECB environmental and climate-related efforts may again face resistance in the courts.

The ECB, in sum, has since 2008 come to face a range of choices, which are immensely far-reaching and whose resolution stands in need of democratic legitimacy, but which have no clear answer in the ECB mandate. Many policies can be described as pursuing the primary objective of price stability, but they will often have very different consequences for the European economy. Central bankers and outside critics disagree over how to make these choices and can easily cite passages in the ECB mandate to support their preferred interpretation.

4. The limits of judicial review

The new situation complicates the task of judicial review, which brings us to the conflict between the ECJ and the BVerfG over the legality of the PSPP. In the monetarist paradigm, judges could supposedly secure the democratic legitimacy of central bank action by policing the confines of the legal mandate. In the new situation this is no longer the case. The ECB now makes significant choices even where it pursues the objective of price stability. At the same time, these choices lack a clear democratic authorization, because they are not anticipated by the legal mandate, while the ECB's independence means that its *ex post* democratic accountability remains limited.

The ECJ and the BVerfG take very different approaches to this challenge (4.1).⁷⁵ The ECJ adopts a permissive approach that allows the ECB to make these choices as long as it pursues the objective of price stability. This ignores the democratic concern. By contrast, the BVerfG objects to the ECJ's permissive reading on democratic grounds. The German judges want to rein in the powers of the ECB by demanding that the central bank weighs the economic policy effects of its monetary policies and admonish the ECJ for failing to review this (4.2). This presents a welcome acknowledgment that the ECB's pursuit of price stability has significant economic costs.⁷⁶ Yet, it does not and cannot solve the problem. Karlsruhe's approach requires that judges weigh monetary policy objectives against economic effects. As democratically unaccountable judges, they lack both the economic expertise and legitimacy to do so (4.3). Courts can demand better justifications of monetary policies that take economic effects into account, but they cannot ultimately make the decisions and plug the democratic authorization gap for the ECB's post-crisis policies.

⁷⁴ 2 BvR 71/20, 2 BvR 72/20 CSPP, Decision of 15 June 2020, ECLI:DE:BVerfG:2020:rk20200615.2bvr007120.

⁷⁵ See also Mark Dawson and Ana Bobic, "Quantitative Easing at the Court of Justice – Doing whatever it takes to save the euro: Weiss and Others", 56 *Common Market Law Review* (2019), 1005–1040, at 1028–1031; Andrej Lang, "Ultra vires review of the ECB's policy of quantitative easing: An analysis of the German Constitutional Court's preliminary reference order in the PSPP case", 55 *Common Market Law Review* (2018), 923–952, at 937–945.

⁷⁶ Although the BVerfG does not seem to be concerned so much with *costs* but rather with the economic policy *effects*. See further footnote 100

4.1 Permissive versus Restrictive: two readings of the ECB's Mandate

The ECJ's permissive approach is informed by the view that the ECB should be accorded broad discretion in making choices about how it pursues price stability. An argument in favour of this approach, is that the TFEU offers the ECB a wide mandate: it is up to the ECB to define and implement the monetary policy of the euro, while acting independently. EU primary law demarcates only the objectives, tasks and instruments of the ECB. A further reason to grant the ECB this discretion is its specific expertise concerning monetary policy. On this line of reasoning, respecting the ECB's independence entails respecting the ECB's discretion. The ECB's unconventional monetary policies are understood as the ECB's proper use of this discretion, namely to effectively pursue price stability in response to changing circumstances.⁷⁷

The permissive approach underlies the *Weiss* ruling of the ECJ.⁷⁸ The Luxembourg court first delimits monetary policy – the policy assigned to the ESCB – from economic policy by looking at the objectives of the adopted measures and the instruments employed.⁷⁹ This is an interpretative move, because the TFEU does not contain a definition of monetary policy.⁸⁰ A key issue is consequently whether the ECB's policies seek to maintain price stability. Here the ECJ shows considerable deference to how the ECB itself explains the objectives of its policies.⁸¹ In addition, the ECJ checks whether the tools employed by the ECB are those allowed by the ESCB Statute.⁸² Once the measures are found to lie within the sphere of monetary policy, the ECJ conducts a proportionality review of how the ECB has used its powers.⁸³ The Luxembourg Court offers the ECB “broad discretion”, because its decisions involve “choices of a technical nature” and require the making of “complex forecasts and assessments”.⁸⁴ This reflects the ECJ's general approach to EU executive decision-making that involves complex

⁷⁷ For a reading of the ECB's mandate along these lines, see Lang, note 75, p. 937-945.; Vestert Borger, “Central Bank Independence, Discretion, and Judicial Review” in Joana Mendes (Ed.), *EU Executive Discretion and the Limits of Law* (Oxford University Press, 2019), pp. 118–131.; Matthias Goldmann, “Adjudicating Economics? Central Bank Independence and the Appropriate Standard of Judicial Review”, 15 *German Law Journal* (2014), 265–280.; Chiara Zilioli, “Standard of review of central bank decisions: an introduction” in, *ECB Legal Conference 2019* (2019), pp. 23–27, at 25.; Borger, “Outright Monetary Transactions and the stability mandate of the ECB: Gauweiler”, 53 *Common Market Law Review; Common Mark.Law Rev.* (2016), 139–196. Armin Steinbach, “All's well that ends well? Crisis policy after the German constitutional court's ruling in Gauweiler”, 24 *Maastricht Journal of European and Comparative Law* (2017), 140–149, at 145–147.

⁷⁸ See that Court's discussion of the institutional position of the ECB in ECJ, *Weiss*, par. 48-52; See also AG Cruz Vilalon, *Gauweiler*, par. 107-111.

⁷⁹ ECJ, *Gauweiler*, par. 46; ECJ, *Weiss*, par. 53; See similarly Case C-370/12. *Thomas Pringle v. Governmentt of Ireland, Ireland and the Attorney General*, EU:C:2012:756 (hereafter: “*ECJ Pringle*”), par. 53 and 55.

⁸⁰ ECJ, *Pringle*, par. 53; ECJ, *Weiss*, par. 50; ECJ, *Gauweiler*, par. 42.

⁸¹ See in this sense also Lars Bay Larsen, “Legal bridges over troubled waters? Standard of review of European Central Bank decisions by the EU Courts” in ECB (Ed.), *ECB Legal Conference 2019* (2019), at 51.

⁸² See ECJ, *Weiss*, par. 69; ECJ, *Gauweiler*, par. 53-54.

⁸³ The way in which the Court conducts this proportionality analysis had already been subject to significant criticism. See: Dawson & Bobic, note 75, at 1022-1028; Armin Steinbach, “All's well that ends well? Crisis policy after the German constitutional court's ruling in Gauweiler”, 24 *Maastricht Journal of European and Comparative Law* (2017), 140–149, at 144–145.; Takis Tridimas and Napoleon Xanthoulis, “A legal analysis of the Gauweiler case: Between monetary policy and constitutional conflict”, 23 *Maastricht Journal of European and Comparative Law* (2016), 17–39, at 31–32. Tridimas & Xanthoulis, at 31-32.

⁸⁴ ECJ, *Gauweiler*, par. 68; ECJ, *Weiss*, par. 73.

economic assessments and contested policy choices.⁸⁵ The ECJ reviews the ECB's discretion by checking for manifest errors.⁸⁶ The principle of proportionality, moreover, is applied in a procedural fashion.⁸⁷ This entails that the ECJ does not review so much whether the ECB has made the right decision, but checks rather whether the way in which the ECB arrived at its decision was proper. In this vein, the ECJ examines whether the ECB has "carefully and impartially" examined "all the relevant elements of the situation in question" and whether it has offered an "adequate statement of the reasons for its decisions."⁸⁸ Thus, the ECJ allows the ECB broad discretion to make highly important decisions. This, however, leaves democratic concerns about the ECB's immense discretion within its mandate unaddressed.

Karlsruhe adopts almost the opposite perspective: it takes democratic concerns about the ECB's decisions as its starting point. As a result, the *BVerfG* holds that the ECB's mandate should be construed in a restrictive manner.⁸⁹ More specifically, this is the case for two reasons, both of which have their roots in the *Maastricht-Urteil*. First, an expansion of the ECB's powers would encroach upon Member States' economic policy competences and, consequently, the right of German citizens to democratic self-determination.⁹⁰ Secondly, the independence accorded to the ECB and national central banks makes that these institutions "operate on the basis of a diminished level of democratic legitimation."⁹¹ According to Karlsruhe the combination of both factors requires a narrow reading of the ECB's mandate and full judicial review.⁹² Compared to the ECJ's approach, the *BVerfG*'s assessment has the advantage that it highlights the democratic problem with the ECB's decision-making, albeit based on a distinctly national reading of democracy. Yet, as we explain below, Karlsruhe does not offer a satisfactory response to the ECB's democratic shortcomings. To see why this is the case, however, it is first necessary to explain the key difference between the two courts' approaches.

4.2 Weighing economic policy effects

In our reading, the key point of disagreement concerns how the economic policy effects of monetary policy should be taken into account for assessing the ECB's actions. Karlsruhe submits that these effects should be taken into account in determining whether an ECB measure qualifies as monetary or economic policy. The ECJ, however, is unwilling to classify policies as monetary or economic depending on their effects: it sticks to objectives and instruments. The ECJ acknowledges that monetary policy has economic effects, which could also be pursued through economic policy rather than monetary

⁸⁵ See e.g.: Hanns Peter Nehl, "Judicial Review of Complex Socio-Economic, Technical, and Scientific Assessment in the European Union" in Joana Mendes (Ed.), *EU Executive Discretion and the Limits of Law* (Oxford University Press, 2019), pp. 157–197.

⁸⁶ On such review of discretion in the ECJ case law, see Paul Craig, *EU Administrative Law*, 2nd edition. (Oxford University Press 2012, 2012), at 592–601.

⁸⁷ ECJ, Gauweiler, par. 68. ECJ, Weiss, par. 73. See on this concept Lenaerts, Koen, "The European Court of Justice and Process-Oriented Review", 31 *Yearbook of European Law* (2012), 3–16.

⁸⁸ ECJ, Gauweiler, par. 69; ECJ, Weiss, par. 30.

⁸⁹ *BVerfG PSPP*, see especially par. 136, par. 142 and 143.

⁹⁰ *BVerfG PSPP*, par. 142; par. 158–160; *BVerfG PSPP reference*, par. 65 & par. 102–103; see also *BVerfG OMT reference*, par. 39–40 and 63–68; *BVerfG OMT final* 183–186.

⁹¹ *BVerfG PSPP*, par. 143 and par. 159; see also *BVerfG PSPP reference*, par. 103; *OMT reference*, par. 58–59; *BVerfG OMT final* 187–189.

⁹² The *BVerfG* develops this argument on the narrow reading of the ECB's mandate for the first time in its *OMT preliminary reference*, see par. 58–68. This inference is not made, or at least not explicitly, in the *Maastricht-Urteil*.

policy. Yet, the Luxembourg judges reject a strict separation between the two policy areas.⁹³ This is the case because, among other things, the ECB “necessarily has to adopt measures that have certain effects on the real economy”⁹⁴ when it wants to influence inflation. Moreover, the ECB is legally required to back the economic policies of the Member States and Union if this is compatible with achieving price stability.⁹⁵ The ECJ does not explicitly consider the economic effects of monetary policy in the subsequent proportionality analysis either. It assesses instead whether the PSPP is a suitable means to achieve the inflation target (suitability), whether this target could be achieved by other means (necessity) and how the ECB had addressed the risks of losses (proportionality *stricto sensu*).

Karlsruhe instead holds that it is crucial to consider these economic policy effects for assessing whether the ECB’s measures still qualify as monetary policy. It is not entirely clear whether the *BVerfG* insists on a pristine separation between monetary and economic policy.⁹⁶ What is evident, however, is that the German court maintains that the economic policy effects of the ECB’s measures can be so large that they outweigh the monetary policy objectives. In other words, it could be that an ECB policy has only a limited impact on achieving the inflation target, but enormous economic policy implications. In that case the ECB measure would properly qualify as economic policy instead of monetary policy.⁹⁷ In its final judgment on the PSPP, the *BVerfG* approaches this issue through the lens of proportionality.⁹⁸ The *BVerfG* worries that on the basis of the ECJ’s approach “the ECB is free to choose any means it considers suitable even if the benefits are rather slim – compared to possible alternative means –, while collateral damage is high.”⁹⁹ More specifically with regard to the PSPP, the *BVerfG*’s concern is that its contribution to achieving the inflation target is limited, while the economic repercussions are vast.¹⁰⁰ Thus, to ascertain whether the ECB is still acting within the

⁹³ ECJ, Weiss, par. 60.

⁹⁴ ECJ, Weiss, par. 66.

⁹⁵ ECJ, Weiss, par. 60.

⁹⁶ For example in *BVerfG PSPP reference* the *BVerfG* acknowledges that monetary policy has economic effects: “Of course, the conduct of monetary policy will generally entail an impact on interest rates and bank refinancing conditions, which necessarily has consequences for the financing conditions of the public deficit of the Member States”. (at par. 121) The ECJ’s answer to the German court misinterprets the way in which it put the question. See on this point: Marijn van der Sluis, “Similar, Therefore Different: Judicial Review of Another Unconventional Monetary Policy in Weiss (C-493/17)”, 46 *Legal Issues of Economic Integration*, 263–284., p. 271-273. Nonetheless, in par 142 of *BVerfG PSPP*, the *BVerfG* does seem to insist on a strict separation between economic policy and monetary policy. There it criticizes the ECJ’s holding that “the authors of the Treaties did not intend to make an absolute separation between economic and monetary policies”. The *BVerfG* deems this reasoning “flawed”.

⁹⁷ *BVerfG PSPP reference*, par. 121.

⁹⁸ See especially: *BVerfG PSPP*, par. 139.

⁹⁹ *BVerfG PSPP*, par. 140.

¹⁰⁰ Maduro has criticized the *BVerfG*’s proportionality test only requires the ECB to consider the economic, fiscal and political costs of monetary policy, but not the economic, fiscal and political benefits. Miguel Maduro, Some Preliminary Remarks on the PSPP Decision of the German Constitutional Court, <<https://verfassungsblog.de>>. See also Toni Marzal, Is the *BVerfG* PSPP decision “simply not comprehensible”?, <<https://verfassungsblog.de>>. It is not clear, however, that the *BVerfG* necessarily frames the issue in terms of economic costs and benefits. The concern of the German judges seems mostly stated as one of ‘effects’. This would imply that also the positive economic policy effects could supposedly render monetary policy *ultra vires*. Moreover, the language of costs and benefits raises the further complication that what counts as a benefit and what as a cost may be highly contested.

confines of its mandate, the economic policy effects of that measure should be weighed against its monetary policy objective. The ECJ's failure to have done so renders the ECJ's proportionality analysis "meaningless" for distinguishing between monetary policy and economic policy.¹⁰¹ For that reason the *BVerfG* concludes that the ECJ's *Weiss* judgment is *ultra vires*.¹⁰²

Because it rejects the ECJ's approach, the *BVerfG* conducts its own review of whether the PSPP violates the ECB's monetary policy mandate. Again, the German judges offer the same objection: the ECB Governing Council did not engage in "the required balancing of the monetary policy objective against the economic policy effects resulting from the means used to achieve it".¹⁰³ The German court highlights five economic policy effects of specific concern. The first, is that the PSPP "improves the refinancing conditions of the Member States"¹⁰⁴, which will stop them from implementing "necessary consolidation and reform measures".¹⁰⁵ Secondly, the German judges object to the PSPP's effects on the banking sector, as it "significantly improves the economic situation of the relevant banks and increases their credit rating", while creating an incentive "to increase lending despite the low level of interest rates".¹⁰⁶ Thirdly, the *BVerfG* worries about the risk of real estate and stock market bubbles "as well as the economic and social impact on virtually all citizens, who are at least indirectly affected *inter alia* as share- holders, tenants, real estate owners, savers or insurance policy holders."¹⁰⁷ The constitutional court points in particular to the risk of losses for private savings and the returns generated by pension schemes. Fourthly, the PSPP keeps economically unviable companies afloat by providing access to cheap credit.¹⁰⁸ Fifth, the programme risks endangering the central bank's independence, as the central bank is in danger of becoming dependent on the Member States politics.¹⁰⁹

The economic policy effects of the programme, the *BVerfG* asserts, should have been weighed by the ECB against its monetary policy objective. The *BVerfG* maintains

¹⁰¹ *BVerfG PSPP*, (par. 127, also par. 133 and par 142) The *BVerfG* thus uses the principle of proportionality to delimitate the competences of the EU and the Member States. The ECJ employs the proportionality principle not to delimitate competences, but as a principle that governs the use of the EU's competences. Commentators have criticised the *BVerfG*'s approach as illogical and contradicting Article 5 (1) TFEU. See elaborately on this point: Mattias Wendel, "Paradoxes of Ultra-Vires Review: A Critical Review of the PSPP-Decision and its Initial Reception", *German Law Journal* (forthcoming). One way to understand Karlsruhe's use of proportionality is that it accepts the ECJ's broad reading of the ECB's monetary policy competence under the condition that it is accompanied by a proportionality test in which the economic policy effects are taken into account. In this vein, the *BVerfG* characterizes the ECJ's use of the proportionality principle in par. 128 as "informed by the notion that a generous interpretation of the specific competence conferred may, to a certain extent, be compensated by a sound proportionality assessment." In other words, the ECJ would have been justified to ignore the economic policy effects of the PSPP programme in delimitating the mandate if it had taken these effects into account in its proportionality assessment. What matters for the *BVerfG* is that the economic policy consequences of monetary policy are taken into account at some point. The *BVerfG* stresses that one cannot distinguish monetary policy and economic policy just by looking at the objective pursued and the means used. (par. 135 and par. 137).

¹⁰² *BVerfG PSPP*, par. 163.

¹⁰³ *BVerfG PSPP*, par. 167.

¹⁰⁴ *BVerfG PSPP*, par. 170.

¹⁰⁵ *BVerfG PSPP*, par.

¹⁰⁶ *BVerfG PSPP*, par. 172.

¹⁰⁷ *BVerfG PSPP*, par. 173.

¹⁰⁸ *BVerfG PSPP*, par. 174.

¹⁰⁹ *BVerfG PSPP*, par. 175.

that it cannot ascertain that such a balancing exercise has taken place at any stage of the PSPP's duration.¹¹⁰ For that reason, the proportionality of the programme cannot be established.¹¹¹ The programme violates Article 5 (1) and 5 (4) TEU and as a result exceeds the ECB's monetary policy mandate making the PSPP *ultra vires*.¹¹²

In principle, the consequence of this is that the PSPP cannot be applied in Germany, because it has no binding effect in the German legal order. German constitutional bodies¹¹³, administrative authorities and courts are not allowed to participate in it, a consequence that is particularly relevant for the *Bundesbank*.¹¹⁴ However, the *BVerfG* left a way out. The *Bundesbank* could continue to participate in the PSPP during a three-month transitional period. After that it would have to stop its participation, unless the ECB Governing Council takes a new decision "that demonstrates in a comprehensible and substantiated manner that the monetary policy objectives pursued by the ECB are not disproportionate to the economic and fiscal policy effects resulting from the programme."¹¹⁵ Only in light of a new proportionality assessment it is possible "to reach a conclusive decision as to whether the PSPP in its specific form is compatible with Art. 127 (1) TFEU."¹¹⁶ The German government and *Bundestag* were thus legally required to take steps that the ECB's Governing Council produces a proportionality assessment.¹¹⁷

¹¹⁰ The German court in fact makes a very strong claim, namely that "It is not ascertainable that any such balancing was conducted, neither when the programme was first launched nor at any point during its implementation; [...] Neither the ECB's press releases nor other public statements by ECB officials hint at any such balancing having taken place." (at par. 176). ECB Council members have rightly pointed out that the ECB has in fact discussed and published on the economic side-effects for years, see e.g.: *Martin Sandbu*, German court has set a bomb under the EU legal order, *Financial Times*, 05/05/2020. *Martin Arnold*, Christine Lagarde says ECB is 'undeterred' by German court challenge, *Financial Times*, 07/05/2020. One example is a speech by ECB Executive Board Member Isabel Schnabel of 11 February 2020 at the *Juristische Studiengesellschaft* in Karlsruhe (!). The speech addresses the economic side effects of the ECB's unconventional monetary policy, stressing that "Germany consists not only of savers, but also of borrowers, taxpayers, property owners and, of course, workers." Isabel Schnabel, Narratives about the ECB's monetary policy – reality or fiction? - Speech by Isabel Schnabel, Member of the Executive Board of the ECB, at the *Juristische Studiengesellschaft*, <https://www.ecb.europa.eu/press/key/date/2020/html/ecb.sp200211_1~b439a2f4a0.en.html>.

¹¹¹ *BVerfG PSPP*, par. 176.

¹¹² *BVerfG PSPP*, par. 177-178.

¹¹³ These are the *Bundestag*, *Bundesrat*, *Bundespräsident*, *Bundesregierung* and the *Bundesverfassungsgericht* itself.

¹¹⁴ *BVerfG PSPP*, par. 234-235.

¹¹⁵ *BVerfG PSPP*, par. 235. A new ECB decision is not forthcoming.

¹¹⁶ *BVerfG PSPP*, (par. 179).

¹¹⁷ The German judges struggle to identify clearly what the Government and *Bundestag* should do to stop the *ultra vires* actions of the ECB. The most concrete the German court gets is where it requires that "[t]he Federal Government and the *Bundestag* must clearly communicate their legal view to the ECB or take steps to ensure that conformity with the Treaties is restored." (par. 232) On this point, see: *Mattias Wendel*, "Paradoxes of Ultra-Vires Review: A Critical Review of the PSPP-Decision and its Initial Reception", *German Law Journal* (forthcoming). The same problem was the source of considerable criticism on the *BVerfG*'s OMT-reference and forcefully put by dissenting justice *Lübbecke*, par. 19 - 26. See also: *Mattias Wendel*, "Exceeding Judicial Competence in the Name of Democracy: The German Federal Constitutional Court's OMT Reference", 10 *European Constitutional Law Review* (2014), 263–307, at 280–282; *Mayer*, "Rebel Without a Cause? A Critical Analysis of the German Constitutional Court's OMT Reference", 15 *German Law Journal* (2014), 111, at 124–127.

4.3 Democratic legitimacy and judicial review of the ECB's actions

So did Karlsruhe's more restrictive approach fix the ECB's democratic shortcomings? The BVerfG does provide a limited improvement that results from three factors. First, the German court acknowledges the weak democratic authorization for the ECB's unconventional operations, which is a consideration wholly absent from the ECJ's approach. Second, the German judges are justified in stressing the significant potential implications of the ECB's unconventional monetary policies. The test employed by the BVerfG marks a departure from the monetarist paradigm of central banking. In that paradigm, a restrictive interpretation of the central bank mandate entailed that central banks should largely ignore the economic effects of their monetary policy and not compromise on achieving price stability.¹¹⁸ This is the opposite of what the BVerfG now demands and reflects a newfound awareness of the societal impact of using monetary policy to achieve price stability. Thirdly, the new test can enhance the ECB's accountability when understood as independent accountability. The BVerfG's review requires the ECB to explain how it has taken into account the potential negative effects of its monetary policies and to justify its choices in light of these effects. A criticism of the ECB's current accountability practices is that they take an overly legalistic form. The ECB focuses on explaining how its operations contribute to the price stability objective, which moves the substantive reasons for choosing one course of action over others to the background.¹¹⁹ As was stressed in section 3, some of the most important issues today, however, concern the broader economic impact of the ECB's operations; their consequences for government financing, employment, environmental sustainability, financial stability and the like. The BVerfG's review can help bring these reasons and their contested nature into the foreground, raising broader awareness of the political choices that monetary policy now involves. The unofficial response to the BVerfG judgment contained in the account of the ECB's monetary policy meeting of 3-4 June 2020 reflects this potential, as it includes an explicit discussion of the asset purchase programme's proportionality.¹²⁰

Nonetheless, requiring that the ECB better explains and justifies its decisions does not make those decisions democratic. In the end, the independent central bankers still make the choices.

The alternative that judicial review can offer is that the judges weigh in on how the decisions should be made. This is part of what Karlsruhe requires, as it demands that

¹¹⁸ On precisely this ground, some have criticised the BVerfG's new test, see: Phedon Nicolaidis, The Judgment of the Federal Constitutional Court of Germany on the Public Sector Asset Purchase Programme of the European Central Bank: Setting an Impossible and Contradictory Test of Proportionality, <<https://eulawlive.com>>, (last visited 15 May 2020).

¹¹⁹ *Braun and Hoffmann-Axtheim*, Two Sides of the Same Coin? Independence and Accountability of the European Central Bank, 2017; Dawson, Maricut-Akbik, and Bobić, "Reconciling Independence and accountability at the European Central Bank: The false promise of Proceduralism", 25 *European Law Journal* (2019), 75–93, at 77–80.

¹²⁰ The ECB's Governing Council reasoned that the benefits of the PSPP outweighed its negative effects, in essence because "the euro area economy would have fared much worse without the policy stimulus asset purchases." (p. 11) The document notes "broad agreement" among members of the Governing Council about this assessment. (p. 12) Yet, the Governing Council acknowledges that deciding these issues is not a technical matter, as "different weights might be attached to the benefits and side effects of asset purchases" (p. 12). See: ECB, "Account of the monetary policy meeting of the Governing Council of the European Central Bank held in Frankfurt am Main on Wednesday and Thursday, 3-4 June 2020" <<https://www.ecb.europa.eu>>, last accessed 21 July 2020.

the ECB's assessment is subject to judicial review. Such review entails that the ECJ - or ultimately the *BVerfG* - must also assess whether the monetary policy objective of an ECB measure has been adequately balanced against its economic policy effects.

The inherent limitations of what courts can do in this respect are illustrated by the *BVerfG Weiss* ruling itself.¹²¹ Firstly, it is not clear that courts currently possess the required expertise to engage in the review that Karlsruhe requires.¹²² The comparative expertise of judges is the correct interpretation of the law, which is of little value where the ECB mandate provides no clear answers. Evaluating the economic consequences of monetary policies, meanwhile, is a complex task with which the German judges clearly struggle. The *BVerfG* does not acknowledge that the causal link between the PSPP and the economic policy effects is contested and subject to pervasive uncertainty.¹²³ The Karlsruhe judges also identify side-effects selectively and fail to acknowledge non-price stability related beneficial effects of low interest rates.

Secondly, and most fundamentally, judicial review does not by itself provide the ECB's operations with democratic legitimacy.¹²⁴ Strict review supplants the discretionary choices of one democratically unaccountable body – the ECB – with that of another – in this case the ECJ or *BVerfG*.¹²⁵ It makes judges the arbiters of how the economic effects of monetary policy should be weighed against its contribution to the monetary policy objective. Not just the ECB operates on a diminished level of democratic legitimation.

¹²¹ See similarly for the last two objections: Andrej Lang, “Ultra vires review of the ECB’s policy of quantitative easing: An analysis of the German Constitutional Court’s preliminary reference order in the PSPP case”, 55 *Common Market Law Review* (2018), 923–952, at 943–945.

¹²² Goodhart and Lastra, “Populism and Central Bank Independence”, 29 *Open Economies Review* (2018), 49–68. Tooze, Adam, *The Death of the Central Bank Myth*, Foreign Policy, 13/05/2020. On these limitations, see also Bateman, *Public Finance and Parliamentary Constitutionalism* (Cambridge University Press, 2020), chap. 8. In the OMT-reference the *BVerfG* famously dismissed the ECB’s expertise in favour of “the convincing expertise of the *Bundesbank*”. *BVerfG OMT reference*, par. 71.

¹²³ This is also reflected in the assessment of the ECB itself in response to German court’s judgment in ECB, “Account of the monetary policy meeting of the Governing Council of the European Central Bank held in Frankfurt am Main on Wednesday and Thursday, 3-4 June 2020” <<https://www.ecb.europa.eu>> , last accessed 21 July 2020. See also Lorenzo Bini Smaghi, *The Judgment of the German Constitutional Court is incomprehensible*, 15/05/2020.

¹²⁴ This problem reflects long-standing questions about the limited democratic qualities of courts. See e.g.: Bickel, *The Least Dangerous Branch: The Supreme Court at the Bar of Politics*, 2nd ed. (Bobbs-Merrill, 1986); Waldron, “The Core of the Case Against Judicial Review”, 115 *The Yale Law Journal* (2006), 1346; Bellamy, “The Democratic Qualities of Courts: A Critical Analysis of Three Arguments”, 49 (2013), 333.

¹²⁵ In this respect, one can also criticise the *BVerfG*’s test as being far too vague, because it is not clear at all when the economic policy effects of monetary policy become so large that they outweigh its monetary objective. One could even question whether the German court applies its own test coherently. A key concern of the *BVerfG* is that the PSPP improves the refinancing conditions of the Member States, which benefits “the budgetary situations of Member States”. (*BVerfG PSPP*, par. 170.) It is not obvious that this constitutes a threat to the economic policy competences of the Member States. On the contrary, one could easily argue that it supports the Member States to conduct autonomous economic and fiscal policies by lowering their debt burden. That the *BVerfG* favors instead that the Member States are subject to financial market discipline and adopt “necessary consolidation and reform measures” (*BVerfG PSPP*, par. 170) sounds more like a desire on the German judges’ side to curtail the Member States economic policy competences. At the same time, this reasoning evinces a deep distrust towards the functioning of the Member States’ democracies. Part of the problem is that Karlsruhe approaches legitimate questions about how to weigh the economic costs and benefits of monetary policy through the lens of the division of competences. This lens does not adequately capture the problem.

Both the Luxembourg as well as the Karlsruhe judges are in a structurally similar position: they are independent judges who are not democratically accountable to citizens. The BVerfG has a further democratic deficit, because in an EU context, it is especially problematic that a German court rules on these topics while the ECB's monetary policy affects all citizens of the Eurozone Member States.

In contrast to democratically accountable bodies, court proceedings often limit the perspective taken into account to those involved in the case, the representatives of their interests and occasionally relevant experts. Thus, a judicial procedure is likely to offer only a skewed sample of the views and affected interests on a given issue.¹²⁶ This problem is particularly visible in the *Weiss*-proceedings before the BVerfG. The core group of applicants share a conservative political outlook and regard the ECB's post-crisis policies as a dangerous departure from the stability-oriented architecture conceived at Maastricht.¹²⁷ Key plaintiffs include the original leaders of the right-wing *Alternative für Deutschland*, Joachim Starbatty and Bernd Lucke, the CSU-politician Peter Gauweiler, the former president of the Federation of German Industries (BDI) Heinrich Weiss, as well as conservative legal scholars such as Karl Albrecht Schachtschneider and Markus Kerber. Some plaintiffs claim that their real aim is to end the euro.¹²⁸ The Karlsruhe proceedings offer an amplified audience for their contested views. In addition, the expert testimony selected by the BVerfG consisted mainly of German economists with conservative affiliations and representatives of the German financial sector, such as the German Insurance Association and the Association of German Banks.¹²⁹ As Adam Tooze put it powerfully in a comment: "It was as though the court had summoned oil companies, and oil companies only, to give evidence on the question of carbon taxes."¹³⁰ These procedural flaws in the proceedings are also reflected in the BVerfG's judgment: the German court highlights only a specific set of affected interests, which happen to be those of German savers and pensioners.

In sum, courts can demand better justifications of monetary policies that take economic effects into account, but they cannot ultimately make the decisions and plug the democratic authorization gap for the ECB's post-crisis policies. The BVerfG itself seems to recognize the limits of its approach: it demands of the ECB to weigh the different public interests involved and explain how it has done so, but it does not want to rule on the proportionality of the PSPP itself. Ultimately, we believe, the only way to solve the

¹²⁶ Scharpf, F.W., "The asymmetry of European integration, or why the EU cannot be a 'social market economy'", 8 *Socio-Economic Review* (2010), 211–250; Waldron, "The Core of the Case Against Judicial Review", 115 *The Yale Law Journal* (2006), 1346; Bellamy, "The Democratic Qualities of Courts: A Critical Analysis of Three Arguments", 49 (2013), 333.

¹²⁷ See *De Cabanes Antoine and Fontan, Clément*, Why Germany's Far Right Wants Judges to Rule Europe's Monetary Policy, *Jacobin*, 24/05/2020; Fontan, Clément and De Cabanes Antoine, "La Cour de Justice face à Gauweiler. La mise en récit de l'indépendance de la BCE" in, *In: Antoine Bailleux, Elsa Bernard, Sophie Jacquot, Les récits judiciaires de l'Europe: concepts et typologie* (Bruylant, 2019), pp. 170–191. On this context more broadly see *Nik de Boer*, Judging European Democracy, PhD dissertation University of Amsterdam 2018 esp. chapter 4.

¹²⁸ *Markus C Kerber*, Letter: Those challenging the ECB's rescue measures are not mad, *Financial Times*, 27/04/2020. He identifies the people he represents as a "a group of moderate, pro-European sceptics including many renowned academics and entrepreneurs" that believes "the euro experiment should be brought to a smooth end, instead of waiting for a collapse that would bring far-reaching collateral damage for European integration."

¹²⁹ See BVerfG PSPP, par. 82.

¹³⁰ *Tooze, Adam*, The Death of the Central Bank Myth, *Foreign Policy*, 13/05/2020.

ECB's current democratic deficit is that democratic institutions provide the ECB with guidance on how to use its monetary powers.

5. Democratizing the ECB

The task of setting out the objectives and instruments was always meant to go to elected politicians, but they have neglected that task during the past decade in leaving it to the ECB to make its own choices – and defending them in the courts. This makes the position of the ECB fragile, since it cannot point to an unambiguous democratic authorization for its post-crisis choices. Going forward, it is unlikely that the ECB will be able to incorporate the EU's climate-related and environmental objectives into its operations without more formal backing, setting it up for new legal challenges. By not providing the ECB with adequate democratic guidance, the EU's political institutions weaken it as an institution. There are, however, many ways in which the member states and the political institutions of the EU can provide the ECB with targeted democratic guidance.

For one thing, of course, the member states can revise the legal provisions in the EU treaties that govern the ECB's mandate.¹³¹ New legal provisions can serve to clarify how the ECB should deal with the economic impact of its policies, as well as their consequences for government budgets, environmental sustainability, financial stability and comparable issues. However, the EU's economic and social priorities will continue to change and it is unlikely that any legal mandate will be up-to-date for long. One way to address this is to let political institutions define monetary policy targets on a recurring basis. Such a procedure exists in the United Kingdom where Article 12 of the Bank of England Act 1998 requires that the Treasury spells out the price stability objective and the government's economic policy at least once per year.¹³² In the EU context a similar procedure could be devised where the Council and European Parliament specify the monetary policy target on a regular basis and provide direction on how the ECB should interpret its secondary mandate. Such democratic guidance would also create a more fine-grained basis for the ECB's *ex-post* accountability.

However, even within the current Treaty framework, there remains significant and often unacknowledged scope for providing the ECB with adequate democratic authorization. First, to answer how the ECB should deal with sovereign bond markets, Article 125(2) TFEU permits the Council to specify the definition of the ECB's monetary financing prohibition.¹³³ Using this procedure, the Council could specify the type of asset purchases and conditions it regards as still compatible with Article 123 TFEU. Second, to provide the ECB's choice of instruments with democratic authorization, Article 129

¹³¹ For an elaborate treatment of various proposals, see Fabian Amtenbrink, *The Democratic Accountability of Central Banks* (Hart Publishing, 1999). In our view, the simplified revision procedure of Article 48 (6) TEU could be used for this purpose, because this procedure applies to Part III of the TFEU, of which the provisions on the ECB are part. Treaty amendments on the basis of the simplified revision provision procedure are subject to the condition that they do not increase the competences of the Union. No such increase in the competences of the EU would take place, as monetary policy is already an exclusive competence of the Union and the ECB already as a secondary mandate to support the general economic policies in the Union. The changes we propose do not entail an expansion of the Union's competences, but would involve a specification of what the current mandate of the ECB requires. In particular, they would provide a greater role for the Council and EP in clarifying what the ECB's mandate entails.

¹³² Bank of England Act 1998 section 12.

¹³³ It currently does so in Council Regulation 3603/93 of 13 Dec. 1993 specifying definitions for the application of the prohibitions referred to in Articles 104 and 104b(1) of the Treaty, O.J. 1993, L 332/1.

(3) TFEU allows the Council and European Parliament to amend Article 18 of the ESCB Statute, which specifies the instruments of monetary policy. Amendments to this Article could clarify the permissibility of asset purchase programmes and the conditions under which they can be activated. Third, to address how the ECB should deal with the economic policy effects of its operations, the Council can set out broad economic policy guidelines in accordance with the procedure of Article 121 (2) TFEU and articulate how it sees the role of the ECB in realizing its secondary mandate. Fourthly and in conjunction with the previous three proposals, the ECB itself could draw more proactively on relevant politically sanctioned legal instruments. An example of where the ECB has already done so is its OMT programme, as its activation is dependent on “strict and effective conditionality attached to an appropriate European Financial Stability Facility/European Stability Mechanism (EFSF/ESM) programme.”¹³⁴ This coupling presented a marked improvement on the prior SMP-programme, where the ECB bought government bonds on a discretionary basis and appears to have used its leverage to formulate its own informal conditionality.¹³⁵ In the OMT programme, such conditionality became subject to the approval of the Euro area’s Finance Ministers, who are accountable to their national parliaments.¹³⁶ The same could be done with the recently adopted Regulation 2020/852, containing the so-called EU Green Taxonomy and which clarifies in detail which economic activities are compatible with the EU’s environmental objectives.¹³⁷ This framework and similar legislative tools should be a starting point for the ECB to develop its future operations.

Will democratization of the ECB along these lines allow short-term electoral incentives to dominate the long-term orientation of monetary policy? The ECB’s independence serves to prevent political interference in the day-to-day operational choices of the central bank. In this regard, what is often described as a democratic deficit of the EU is also a strength. Electoral cycles are not synchronized across the EU and its democratic procedures involve numerous veto players. More importantly, arguments in favour of independence, as we showed in Section 2, were never supposed to mean that central bankers should set their own objectives and decide on the most adequate tools to pursue them. These topics go far beyond the mere technical question of how to maintain growth at its long-term potential. They are also by their nature less vulnerable to myopia, rather constituting quintessentially political questions concerning the long-term trajectory of the economy that would normally be left to the democratic process.

Governments have shown little interest so far in using the means within the Treaties to strengthen the ECB’s democratic legitimacy. Should their silence or even informal support be interpreted as a form of democratic consent?¹³⁸ From a democratic

¹³⁴ ECB, Technical features of Outright Monetary Transactions, https://www.ecb.europa.eu/press/pr/date/2012/html/pr120906_1.en.html.

¹³⁵ In 2011 ECB President Trichet and Italian Central Bank Governor Draghi infamously sent a letter to the Italian Government in which they provided detailed requirements on how Italy should carry out structural economic reforms. On this letter, see Beukers, “The New ECB and its Relationship with the Eurozone Member States: Between Central Bank Independence and Central Bank Intervention”, 50 *Common Market Law Review* (2013), 1579, at 1598-1601.

¹³⁶ See Article 13 of the ESM Treaty.

¹³⁷ REGULATION (EU) 2020/852 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 18 June 2020 on the establishment of a framework to facilitate sustainable investment, and amending Regulation (EU) 2019/2088, OJ L 198/13, 220620.

¹³⁸ See for example regarding Merkel’s support for OMT Macron’s on the PEPP respectively: Claire Jones, The ECB after Draghi: ‘You need an actor who can act fast’, *Financial Times*, 13/03/2019; *Martin*

perspective mere informal consent provides unclear and ambiguous authorization at best. The political position is not explicit, nor was it preceded by open debate that allows for weighing competing interests and putting forward alternative viewpoints. Neither does such informal consent amount to a clear decision for which elected politicians can be held to account.

6. Conclusion

Karlsruhe's decision to declare the PSPP *ultra vires* reflects a justified concern about the democratic legitimacy of the ECB's unconventional monetary policies. Yet, as we have argued judicial review by either the ECJ or the BVerfG cannot solve the ECB's democratic authorization gaps. In the end, only renewed democratic authorization is able to provide an adequate answer. Within the monetarist paradigm discussed in Section 2, this democratic problem was not meant to exist. Since 2008, as Section 3 showed, the ECB has been confronted with new choices, which have no clear answer in either the monetarist paradigm or the ECB mandate. These choices, however, often have far-reaching consequences and their resolution stands in need of democratic legitimacy. Section 4 analysed how the Luxembourg and Karlsruhe courts struggle with the ECB's new role. On the one hand, the ECJ broadly accepts the status quo in leaving it to the ECB to use its expertise in deciding what to do. The alternative strategy adopted by the BVerfG lands it in an uncomfortable position: it lacks both the required expertise and legitimacy to evaluate the ECB's choices. In Section 5, we showed that there are ample means available within the existing Treaties to enhance the democratic legitimacy of the ECB. In leaving it to the ECB to set out its own course, the member states and the political institutions of the EU are failing to play their part as elected representatives and are thereby weakening the ECB's ability to address the major economic challenges of the 21st century.

Arnold, ECB to launch €750bn bond-buying programme, Financial Times, 19/03/2020. Dissenting judge Gerhardt had argued in the OMT-reference case that the *Bundestag*'s lack of action should have been read as "an expression of its majority decision for a certain policy when handling the sovereign debt crisis in the euro currency area." (Gerhardt, dissenting opinion OMT, par. 23) The German Government had approved the OMT programme, which the *Bundestag* had accepted "with open eyes" after hearing the President of the ECB and assessing the ECB's policy. In addition, the *Bundestag* had not criticised the OMT programme by "political means" or brought annulment proceedings before the ECJ.