The ECB's Mandate: Does It Need to Be Modified to Be Fit for the Future?

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My talk will not paint the big picture of the present and future role of monetary policy but rather concentrate on the ways and means of a modification and its (legal) limits. The big picture should be left to the economists who can much better integrate all aspects in a beautiful model and are free to develop new ideas without the nasty little restrictions of the various legal systems.

Before deliberating a modification of the ECB's mandate it is essential to clarify the starting point, the present-day understanding of the ECB's mandate. In view of the far reaching discord on the legality of the asset purchase programmes of the last years, it has basically to be an abstract of the legal limits of the Eurosystem's (Article 282(1) TFEU) tasks, objectives and competences (I). In the second section a short look will be taken on the highly controversial question of how much leeway should and may be given to the Eurosystem in defining its competences and objectives (II). This statement will be followed by some thoughts on the yardstick to be applied for giving an answer to the topical question (III). The concluding remarks will be devoted to the increasingly advocated "average inflation targeting" and the proposals for a monetary financing of sovereign deficits (IV).

I. The ESCB's competences

The so-called mandate of the ECB, or rather more precisely: of the ESCB, has been an object of fierce legal dispute, mainly triggered by the asset purchase programmes of the Eurosystem. Although a fundamental discord could be recognized among economists and a few other academics the focus of the controversies was eventually on legal questions. The different opinions on the concrete substance of the tasks, objectives and competences of the ESCB finally lead to several diverging judgments

of the German Federal Constitutional Court and the Court of Justice of the EU. The apex was allegedly reached with the outright refusal of the German Court to follow the directions of the (preliminary) ruling of the Court of Justice on the Public Sector Purchase Programme (PSPP) in May of this year.

A transgression of competences by the Eurosystems's outright purchases of public sector debt evolved as the most controversial issue. In the course of the debate, volume and timing of the purchases gained an increasing role in judging it as either monetary policy, an exclusive competence of the EU, Article 3(I) lit c TFEU, or economic policy, left to the Member States, Articles 119, 127 TFEU. Nevertheless, the CJEU dismissed without reservation all concerns of the German Federal Constitutional Court in its referral decisions as unfounded. It did not see a transgression of competences nor a – prohibited – monetary financing of government deficit and judged both the OMT and the PSPP as in conformity with EU law. In its ensuing final judgment on the PSPP, handed down on 5 May 2020, the German Court stated in addition to its prior legal concerns on the actions of the Eurosystem a clear transgression of tasks and competences of another organ of the EU; this time of the Court of Justice. In its opinion, the Court of the EU bluntly failed to properly review the legality of the purchases and to question sufficiently the facts presented by the ECB.

According to its *ultra vires* judicature, these twofold violations opened the door to its own review of acts of the institutions and organs of the EU normally reserved to the European Court. In the course of its own review of European Union law, the Court saw a violation of the fundamental principles of conferral and proportionality, Articles 4(1) and 5(1) TEU.

The recourse to the principle of proportionality, however, is highly questionable in the context competences but allowed a flexible answer to the opinion of the European Court.

II. The softening of the rules distributing the competences between the EU and its Member States

Almost relentlessly, the representatives of the ESCB like to reiterate that they are acting “within their mandate”. This is nice to hear but of little significance since the term “mandate” is a “weasel word”. It is not part of the language of the primary law which is considerably more precise and differentiated. By employing it, the delineation of tasks and competences is already blurred and the question *quis judicabit* gains additional weight. The CJEU has further diluted the legal rules on the distribution of competences by conceding a wide margin of discretion to the ESCB in deciding on the limits of its competences. Thus the institution affected, decides almost autonomously on the scope of its competences. The strict rules of the primary law turn into non-binding guidelines lacking widely judicial control.

Such an interpretation is hardly compatible with the intention of the framers of the Treaties to install a clear cut distribution of competences between the EU and the Member States. In addition, the requirements of the democratic principle and the principle of (limited) conferral, which are all fundamental to the primary law of the EU are jeopardized. Moreover, the crucial stability of the institutional order of a multi-level organization like the EU is severely endangered.

The principal objective of the ESCB is to maintain price stability. Its exclusive competence is confined to monetary policy. Without prejudice to this goal, it may or – perhaps - should support the economic policy of the competent authorities. From this follows, that it is not allowed to pursue its own economic policy including fiscal policy.

The rationality of this delineation has been frequently attacked from various sides but it is the law of the EU and has to be obeyed no matter how dysfunctional it might be judged by economists.

The attempts to widen the domain of monetary policy at the detriment of economic policy, not least in view of future needs, are legally questionable. Even more questionable is an oscillating interpretation of the term monetary policy corresponding to the respective political goals pursued. Such a situation-oriented understanding almost at will can, however, be noticed in the judicature of the CJEU with a narrow delineation in *Pringle* and a wide interpretation in *Gauweiler* (OMT) and *Weiss* (PSPP).

The same holds for the understanding of the term “price stability”. If it is extended to cover almost any inflation rate, the financial stability, the stability of institutions including the banking systems, and the prevention of recessions, the ESCB could pursue almost as wide an objective as the Federal Reserve System. This is, however, based on a distinctively different legal setup with different statutory goals.

III. The applicable yardstick

The necessity of a modification of the ECB’s “mandate” hinges in principle on three variables: (i) The present delineation of the “mandate”, basically a legal assessment, (ii) a normative economic evaluation of central bank tasks, and (iii) a forecast of future needs. An abstract appraisal of what central banks can and should achieve is not part of my talk. The same holds for the forecast which is by its nature rather unreliable. If the economic analysis, however, leads to the advisability of a modification of the present “mandate”, the legal assessment depends to a large extent on the understanding of the objectives, tasks, and competences of the Eurosystem as laid down in the primary law of the Union.

On the basis of the wide understanding as described above, leaving the result in principle to the discretion of the ECB, a modification of the legal framework would hardly be necessary to be fit for any future requirements. On the basis of a stricter understanding of the distribution of competences and its effective control by the judiciary, an amendment of the Treaties would appear to be indispensable. It seems to be safe to forecast strong objections of the German Federal Constitutional Court if it follows its present line of judicature.

IV. New interpretation of price stability and prohibition of monetary financing

(1) In specific, a restatement of the term “price stability” as an average over a specific period of time defined autonomously by the central bank would be questionable from the legal point of view. As regards the democratic principle, it is already hard to accept that a numerical limit for an aspired inflation rate with its ramifications for almost everyone is set autonomously by an executive body, like the ECB or the

ESCB. In some countries, this decision was even regarded as so crucial that it had to be set by the representatives of the people. In conformity with this view, the primary law of the EU does not acknowledge the setting of an inflation target, not least by an executive body. The term “inflation” is totally foreign to the relevant clauses of the primary law. The ESCB is strictly bound to the maintenance of price stability and not to pursue an inflation target, no matter what numerical value is attributed to it.

Following this line of legal arguing, not only inflation targeting of any kind but using an average inflation rate as a yardstick even more fails to comply with wording and rationale of the primary law. In the German legal literature at the time of framing the law, price stability meant 0% inflation as a target but usually accepting a fairly wide band of numbers as an outcome but not as a goal. It would have to be doubted that the GFCC would accept a switch to such a different regime of measuring consumer price inflation in employing monetary policy or an outright “average inflation targeting” without a treaty change.

(2) Monetary financing of sovereign debt appears to be a viable, almost costless solution of budgetary problems, specifically in time of need. In effect, already the present asset purchase programmes without a defined exit come close to a monetary financing. From an economic point of view they could be consolidated with the sovereign debt of the Member States whose currency is the euro. If this strategy is advisable plays a major role in the economic debate. Even in an environment of real and nominal negative interest rates, it is not sure that the benefits outweigh the costs. Four concerns have to be considered: (i) The central bank policy might be dominated by fiscal policy and thus loses its independence. (ii) The role model of the Bank of Japan casts doubts whether such a policy is suitable to attain the aspired goals. (iii) The monetary financing might in the end turn out not to be costless imposing high social and economic costs in a medium range. (iv) The distributional aspects are often not regarded sufficiently.

From the legal point of view, it is still the common understanding of Article 123(1) TFEU that it prohibits monetary financing of government deficits. However, Article 127(5) TFEU might serve as a backdoor to the legality of monetary financing in the

present situation. The clause allows a contribution of the ESCB to the policies pursued by the competent authorities. The clause restricts the ESCB to an ancillary role, a mere support of the implementation of decisions elsewhere taken, and prohibits an autonomous policy of the ESCB outside monetary policy.

A very wide interpretation of these prerequisites might open the door to some extent. But in substance the allowed contribution is confined to supervisory policies and the stability of the financial system. This obstacle can hardly be overcome to allow general monetary financing even in the time of crisis. Since the clause is *lex specialis,* and hence the only way for a (limited) transgression of monetary policy, all other sideways or backdoors are closed by it.