

## **GUEST EDITORIAL**

### **The European Monetary Institute's Annual Reports: Fact-finding, means of control, incentive**

#### **1. Introduction**

The European Monetary Institute (EMI) assumed its functions on 1 January 1994. Now it has adopted its first Annual Report, covering 1993 and 1994, it may be useful to examine the role of this publication.

The annual reports of the EMI have a threefold legal function ensuing from the purposes and tasks assigned to the Institute in the Treaty on European Union.<sup>1</sup> Each yearly statement has the following aims: first, fact-finding and checking the data collected before supplying it to Community institutions, EC Member States and their central banks.<sup>2</sup> Second, the annual reports should implement international control by assessing relevant conduct of Member States as to its conformity with Community law, notably with the convergence criteria for admission to the third stage of economic and monetary union (EMU). Third, by registering the progress made towards attainment of the goals set forth by the Maastricht Treaty, the EC Treaty and relevant secondary Community law, each Report gives an important incentive to EC Member States and their central banks, as well as to Community institutions.

The Treaty provisions dealing with the EMI and its yearly statements amply bear out this triple quality. So does the first EMI Annual Report,

1. I.e. in the amended EC Treaty, the EMI Statute and such other protocols annexed to the Treaties as are or may become relevant in establishing the reports, notably the Protocol on the Convergence Criteria referred to in Art. 109J EC and the Protocol on the Excessive Deficit Procedure.

2. As required, in particular, by Art. 109F EC in conjunction with Arts. 7 and 11.3 of the EMI Statute.

adopted by its Council in March 1995, and published in April 1995 in the eleven working languages of the Community.<sup>3</sup> As envisaged by the EMI Statute, the EMI addressed the document to the European Parliament, the Council, the Commission and the European Council.

The second stage of EMU, which began on 1 January 1994, is to prepare EC Member States comprehensively for entry into the final stage of the EMU, scheduled for 1999 at the latest, provided the convergence criteria are complied with by then. "The most important institutional innovation ushered in by the second stage was the establishment of the European Monetary Institute . . ."<sup>4</sup> The EMI replaces the Committee of EC Central Bank Governors, which previously acted as the central monetary policy coordinating body, and should help pave the way for transition to the single European currency. Henceforth, its task is to foster monetary policy coordination and prepare the regulatory, organizational and logistic framework needed by the future European System of Central Banks (ESCB) in order to discharge its functions. Its field of responsibilities ranges from developing monetary policy instruments and harmonizing national payment systems to supervising the preliminary work on designing bank notes and coins for the single currency in the making. Yet "[D]urant cette deuxième étape, la responsabilité . . . de la politique monétaire demeure du ressort des autorités nationales"<sup>5</sup> – an indubitable jurisdictional axiom spelled out as such by Article 3.1 of the EMI Statute and unlikely to simplify the operations of the EMI, especially since the central banks as a group have made it known that they will insist on respect for their pre-eminence over monetary policy before the advent of EMU's third stage.

The EMI Statute requires it to complete the technical preliminary work by the end of 1996 so as to meet the earliest possible deadline envisaged by the Maastricht Treaty for launching EMU, namely 1997. Though the majority view all over the EC rates the early starting date as running far ahead of legal contingencies and attainable economic accomplishments, the EMI takes the 1996 date quite seriously, and has

3. According to the EMI's Rules of Procedure, Art. 12.

4. Deutsche Bundesbank, Annual Report 1994, p. 100, English version.

5. Banque de France, Exercice 1994, Rapport, p. 177.

committed itself to producing by the end of that year a blueprint of the prerequisites for the ESCB to perform its tasks.

## 2. Fact-finding

Both the general layout of the EMI report and the details confirm that it aims at being and is an exercise in fact-finding. This term brings to mind the evolution of the law relating to international disputes, where the notion has from the start been synonymous and interchangeable with "inquiry",<sup>6</sup> with an independent body carrying out the fact-finding required for ascertaining (usually) divergent evidence for the purpose of subsequent assessment. The inquiry by the EMI, for its annual report and with a view to other objectives, is distinguished from those precedents by its legal quality as a permanent supervisory mechanism within the framework of an integrated entity, namely the EC. It aims to take stock of all aspects relevant to its tasks.

The report covers monetary and financial conditions in the Community as well as the activities of the EMI. It includes the EMI's accounts and operational tasks, and measures progress towards convergence, preparatory work for the advent of the single European currency and the institutional features of national central banks.

However, this fact-finding is subject to the functional limitation of Article 7 EMI Statute, which means that the substance of the reports must be linked to the EMI's role as precursor of the ESCB, and eventually the European Central Bank (ECB) as specified by the TEU. In short, therefore, whatever information the EMI Annual Report carries, its insertion has to be justified by its relevance to the objectives of the TEU. At the same time, this does not detract from the impartiality and independence of the EMI, so emphatically accorded by Articles 8, 20 and 21 of its Statute.

The EMI's Annual Report 1994 provides a convincing exercise of purposive fact-finding and communication. It also demonstrates the cooperative attitude of the EMI *vis-à-vis* national and Community insti-

6. Cf. 1907 Hague Convention on the Pacific Settlement of International Disputes.

tutions concerned with the transition to a single currency, as it could not have been produced without close cooperation with the central banks of EC members, with the relevant bodies of the European Union and outside entities such as the Bank for International Settlements (BIS).<sup>7</sup>

### **3. Control**

The second legal aspect of the EMI Annual Report relates to monitoring. Supervision of States and their organs in order to ascertain the conformity of their conduct with relevant principles and rules of international law has long been known in intergovernmental practice and public international organizations, and it has always been a salient feature of the European legal system. The EC Treaty requires the States entering EMU to comply with the conditions for the adoption of a single currency. Under the Treaty, the EMI is to exercise an important function in the assessment of convergence and the effort to attain and maintain it. The means of control available to the EMI for that purpose ensue from its assignment to survey, constantly and permanently throughout its life as an independent entity in the framework of the EC, whatever facts and legal developments may be relevant to the achievement of that convergence. In conjunction with this, it has the duty to measure the data collected in order to ascertain their conformity with the criteria set out in the Treaty, notably Article 109J(1) EC. That Article does not reserve this task to the EMI, but calls on both the EC Commission and the EMI to keep the EC Council informed of "the progress made in the fulfilment by the Member States of their obligations regarding the achievement of economic and monetary union".

That the tasks are not assigned exclusively to the EMI reflects the Member States' respect for the Commission's well-established and comprehensive power to ensure the application of the Treaty (Art. 155) and

7. "... a number of recent events have pointed to the need to improve communication between central banks and other supervisory authorities . . . Such cooperation . . . may at times seem slow and laborious but experience has shown that it can succeed and that the benefits warrant the effort invested." (BIS, 65th Annual Report, 12 June 1995, p. 212).

for its prerogative to muster whatever initiative may be required "... to ensure the proper functioning and development of the common market..." (Art. 155 EC). Yet, given the vast range of the Commission's jurisdiction, it stands to reason that the special monetary expertise of the EMI Council and its staff, its reports and other statements regarding EMU carry at least as much weight as those of the Commission: if the high professional quality of the EMI is sustained in the medium and long term, this might even lead to its being accorded preferential acknowledgement in this area.

The beginnings of such an opinion-building process could be seen in the comparison between the "impatient" prose of the EC Commission's "Green Paper on the Practical Arrangements for the Introduction of the Single Currency" of 31 May 1995,<sup>8</sup> with the measured stance of the first EMI Annual Report, by newspapers and certain periodicals.<sup>9</sup>

We are unable here to give a critical appraisal of the standards guiding the reporting and evaluation of data collected by the EMI. Suffice it to say that the major statement on the surveillance and assessment of progress towards convergence, in Chapter I of the first EMI Annual Report, may serve henceforward as a model for rendering accessible and comprehensible the canons international supervision is supposed to ascertain and to implement. The EMI fulfils its role in assessing convergence, and identifies the salient criteria under the four headings of price stability, public finances, exchange rate stability and convergence in long-term interest rates, starting in each case by recalling the terms of

8. For consideration by the European Council at its 26 June 1995 summit meeting in Cannes.

9. The 19 June 1995 memorandum by the EMI Council on the changeover to the single currency, apparently in reply to the EC Commission's 74-page statement, acknowledges that differentiation. "... strict adherence to all the convergence criteria ... is the crucial requirement for ensuring that Monetary Union will be sustainable, that unfavourable market reactions are avoided and that the benefits of the single currency can be reaped in full by all citizens ... the time frame for the changeover should take two main considerations into account. Firstly, a period of around twelve months is deemed to be necessary between the decision by the Heads of State or Government on which countries will participate in the single currency area and the actual starting date of EMU .... Secondly, the introduction of European banknotes and coins should take place within three years after the start of Stage Three ...." (*ibid.*, p. 1, paras. 2 and 3).

the Treaty and the protocol or protocols at issue. This is followed by measurement of recent economic and other factual findings with regard to each Member State. The Report gives an ample identification, description and, if need be, interpretation or even assessment of the standards to be ascertained by EMI surveillance and evaluation. It also deals with the procedure and the means of control employed by the EMI.

The EMI sees itself as a permanent supervisory mechanism with aims, tasks and functional targets geared to the attainment of the ultimate aim sanctioned by the Maastricht Treaty. As for the methods available for securing compliance with the substance of its mission, the Report presents the scope of its activities as a network comprising the observance and measurement of whatever economic or other factual development and legal evaluation may be of relevance to the advent of the EMU. From an organizational point of view, the EMI seems to be able to assume the procedural width and depth required for the accomplishment of its considerable task. The list of committees, subcommittees and working groups ensuing from cooperation with and between central banks endorses the impression that the well-tested procedures under the aegis of the Committee of Governors of the EC Central Banks up to the end of 1993, will also support the new institute.

The means of control available to the EMI include comparison of the figures and percentages set out in the EC and Maastricht Treaties with numerical results of acknowledged national economic indicators. They do not comprise corrective action, as there is no mandate to take sanctions. The EMI has, however, the faculty to exercise influence by its expertise, the publication of its findings, notably on national economic indicators, and to assess these in terms of the criteria of convergence. Its first Annual Report provides testimony of this.

The perspicacious use of that method is particularly characteristic of the concluding Chapter III, on institutional features of national central banks. There is an initial exposition of the normative scope of the relevant provisions,<sup>10</sup> and a note on the role of the EMI in monitoring central banks' fulfilment of them. Compliance with the prohibition on the

10. Arts. 104, 104A and 108 EC.

availability of central bank credit to the public sector under Article 104 EC is documented by a table showing central banks' claims against the relevant institutions; apparently the authors of the report were so convinced that the obligations at issue would be progressively implemented, that they felt justified in limiting their text to statements of fact and of law evidencing the critical elements of the respective briefs. Equally, the obligation of EC Member States to secure the independence of their central banks and the latter's primary objective to promote price stability, is dealt with by an unemotional line-up, setting forth the present features of national central banks in the European Union and noting prospective initiatives by member governments tending to change existing legislation and identifying relevant amendments, where required. The measured recital of that entry remains as impressive as the wealth of its contents. Altogether, the passages reveal an impressive reservoir of mutual trust between the institution of control and the entities subject to surveillance. If that sentiment means that supervision by the EMI over Member States and their central banks will be implemented with efficiency, this conclusion may encourage both the EMI and the persons and entities under its inspection. Still, it is worth recalling that the satisfactory quality of control by the EMI ensues from an express legal commitment to begin with.

#### **4. Incentives**

The third legal aspect of the annual reports, arises from the duty to provide incentives for getting or staying in line with the requirements of the Maastricht Treaty envisaging access to the EMU only by those States that satisfy the criteria of convergence at the relevant time.<sup>11</sup> The identification of the legal advantages resulting from full participation in the EMU right from its start is certainly a task of the EMI. The first EMI Annual Report provides a clear and comprehensive enumeration of the

11. Incontestably part of the duty to prepare the third stage of the EMU assigned to the EMI in the broadest terms by Art. 109F EC and the agency's Statute (Arts. 2-4, 6-8).

legal, economic and political benefits accruing to EU members that enter the third stage without any qualification. But it stands to reason that the EMI has an equal obligation to sort out and explain the disadvantages for the EU States which are barred from access to the third phase of EMU. One wonders whether the scarcity of remarks on the inconvenience likely to arise for the "outsiders" will remain a feature of the following annual reports by the EMI. The line-up of relevant disadvantages might indeed comprise a sketch of the legal shortcomings resulting from the maintenance of the national currency while the derogation in favour of the member concerned remains in force. True, the monetary, economic and political drawbacks incidental to that state of affairs would have to have pride of place. Yet, the amplification of the EMI reports by such a feature would amount less to an element of pressure on the "outsiders" than a compensation for the lack of such an effort by the negotiators and signatories of the Maastricht texts.

In fact, the latter countries are as entitled to advice, legal and otherwise, as are the States that can expect to qualify for entry into EMU right from the beginning of the third stage, if only on the ground that equal justice under law requires respect for the benefit of all members of an intergovernmental entity, be it international or supranational in nature. If the EMI, quite appropriately, provides incentives to the more fortunate States that will manage to satisfy the requirements of Article 109J straight away by explaining to them the legal, economic and political advantages accruing to them under that heading, it places itself under the obligation to make the others aware of the drawbacks they will face and to inform them as thoroughly and perspicaciously as the former group about the legal, economic and political inconvenience ensuing from temporary exclusion.

## **5. Exchange rate fluctuation bands**

There is one other monetary and legal issue discussed in the first EMI Annual Report which merits specific comment. It arises from the conjunction of Article 109J(1), third indent, EC and Article 3 of the Pro-



tol on the Convergence Criteria<sup>12</sup> on the one hand, and the decision by EU Ministers of Finance and the Committee of Governors of EU central banks of 2 August 1993, to widen the fluctuation margins of the Exchange Rate Mechanism (ERM) for compulsory intervention in the European Monetary System (EMS) to 15% in either direction, while leaving central parities unchanged.

It is a matter for consideration whether the assessment of the condition for entry into the third stage of EMU according to the Protocol should measure the conduct of Member States on the basis of the narrow fluctuation margin of 2.25% around the ECU-related central rate as determined by the Resolution of the European Council of 5 December 1978, on the Establishment of the European Monetary System and the Related Matters, or the more generous margin of 15% applied since 2 August 1993. The EU Council acknowledges both the continuing validity of the wider ERM fluctuation band for compulsory intervention, with a margin of 15%, and on the other hand the maintenance of the original and narrow margin of 2.25% around the ECU-related central rate. The view of the EMI Council on the situation that "in the light of this experience and in the current circumstances, the EMI Council considers it advisable to maintain the present arrangement" thus coincides with that of the Council.<sup>13</sup> Altogether, this does not simplify the situation.

Apart from the bilateral understanding between the Dutch and the German Central Banks continuing to apply the limit of 2.25% between their currencies, it appears indubitable that at least at the time of writing that narrow margin has been exceeded by the bilateral exchange rates of other EU States' monies, in some instances considerably and for considerable time. The widening of the fluctuation bands also had the legal and monetary purpose of avoiding any re-alignment, i.e. any changes

12. "The criterion on participation in the Exchange Rate Mechanism of the European Monetary System referred to in the third indent of Art. 109j(1) of this Treaty shall mean that a Member State has respected the normal fluctuation margins provided for by the Exchange Rate Mechanism of the European Monetary System without severe tensions for at least the last two years before the examination. In particular, the Member State shall not have devalued its currency's bilateral central rate against any other Member State's currency on its own initiative for the same period."

13. 7 Oct. 1994, EMI Annual Report 1994, p. 56.

of the ECU-related central rates, as long as the 15% limit remained honoured.

Relevant texts and developments suggest that the narrow margin of 2.25% commands in each case the criterion of adhering to "normal fluctuation margins" in Article 3 of the Protocol on the Convergence Criteria. Admittedly, the start of the assessment of suitable candidates for entry into the third stage of EMU is still several years away. But the question merits consideration much earlier, as a response different from the one assumed here would reveal an inclination to soften up at least one convergence criterion. If the advocates of a 15% fluctuation margin prevail, that would run counter not only to the meaning of this and the other convergence criteria as communicated by all signatory governments to their parliaments and other public institutions when introducing the Maastricht Treaty for approval and ratification by their Heads of State. It would also be contrary to the conclusions drawn by these institutions when assessing the relevant provisions. That misgivings should arise from the advocacy of applying the wider margin, seems fairly certain. It is also likely that the ensuing public debate could become incisive, since the supporters of the Maastricht Treaty considered the covenant as an acknowledgment that EMU would amount to a union involving monetary stability, in particular as regards the exchange rates of those monies that would disappear with the advent of the third stage.<sup>14</sup>

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14. The consequences in Germany of such a situation might be especially grave, following the judgment by the German Federal Constitutional Court of 12 Oct. 1993, but also as a result of the procedural and substantive condition placed by the German Parliament on access by the Federal Republic to EMU, namely that such access would be contingent on a new resolution by the *Bundestag* rigidly assessing compliance with the criteria of convergence on the part of the EU members chosen to enter monetary union at the outset of the third phase. A passage from the Court's opinion sums up the thought common to them: "This conception of the currency union as a stability-oriented community is the basis and substance of the German Law on Accession. Should the monetary union not be able, ... to develop continuous stability, ... it would be departing from the concept of the Treaty." (English translation of the judgment in Winkelmann (Ed.), *Das Maastricht-Urteil des Bundesverfassungsgerichts vom 12. Oktober 1993* (1994), at p. 793).

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