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An Assessment of the Judgment of the Federal Constitutional Court of Germany On the Public Sector Asset Purchase Programme of the European Central Bank

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The Federal Constitutional Court (FCC) of Germany has invented a new and impossible test of proportionality to declare as ultra vires the judgment of the Court of Justice of the European Union in Weiss. Instead of understanding proportionality as the least interventionist means of achieving a certain policy objective, it defines it as the balancing between conflicting policy objectives which in this case are monetary and economic policy. This is not the concept used by the Court of Justice. This definition of proportionality is intended as a substitute for the principle of conferral and whether the European Central Bank (ECB) encroached on economic policy. However, if monetary policy is to be effective, it must impact economic policy. Had the ECB attempted to balance monetary and economic policy effects, it would have infringed Article 127(1) TFEU that requires that the support of economic policy by the ECB is without prejudice to price stability which is the objective of monetary policy. The Federal Constitutional Court did not appreciate the significance of the fact that the ECB buys public bonds from private investors and that the interjection of private investors deprives Member States from the ability to sell unlimited amounts of bonds at prices that would enable them to run indefinite budget deficits.

Keywords: Monetary policy, economic policy, proportionality, ECB, public sector asset purchase programme

1 INTRODUCTION

In March 2015, the European Central Bank [ECB] adopted decision 2015/774 which launched the Public Sector Asset Purchase Programme [PSPP]. The objective of the PSPP was to buy public bonds, under certain conditions, on the secondary market [i.e. after the market operators would buy the bonds directly from the issuing public authorities]. Its purpose was to increase money supply, reduce interest rates

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and eventually stimulate economic activity and raise the rate of inflation to the ECB's target of close to but below 2%.

Soon afterwards, a large number of persons lodged a challenge to the PSPP before the German Federal Constitutional Court [FCC]. The FCC stayed its proceedings and made a reference for a preliminary ruling to the Court of Justice of the European Union [CJEU] in case *C-493/17, Heinrich Weiss and others*.¹ In response, the CJEU decided on 11 December 2018 that the PSPP was compatible with the provisions of the Treaty on the Functioning of the European Union [TFEU].

On 5 May 2020, the FCC found the ruling of the CJEU to be 'incomprehensible' and declared it to be '*ultra vires*'.² It also found that the ECB had not demonstrated that the PSPP conformed with the principle of proportionality and requested the ECB to submit evidence, within three months, that the PSPP did satisfy that principle.

More specifically, Heinrich Weiss and the other applicants argued that the PSPP and related programmes violated the prohibition of monetary financing [i.e. Article 123(1) TFEU] and the principle of conferral [i.e. Article 5(1) TEU].³

The FCC judgment also interpreted the 'right to democratic self-determination' in Germany's constitution [Basic Law] and inferred that it 'protects against a manifest and structurally significant exceeding of competences by institutions, bodies, offices and agencies of the European Union'⁴ and that German institutions 'participating in the execution and in the further shaping and development of the integration agenda (*Integrationsprogramm*)' are obliged to 'ensure that its limits are respected'.⁵ The reasoning of the FCC on these issues is developed in paragraphs 98 to 115 of its judgment. Accordingly, the FCC faulted the Federal Government and the Bundestag for violating the constitutional rights of the applicants.

With respect to the specific actions of the ECB and their assessment by the CJEU in *Weiss*, the essence of the FCC's findings is that:

the ECB, in Decision (EU) 2015/774 ... , neither assessed nor substantiated that the measures provided for in these decisions satisfy the principle of proportionality. In light of this, Decision (EU) 2015/774 ... constitute a qualified, i.e. manifest and structurally significant, exceeding of the competences assigned to the ECB in Art. 119, Art. 127 et seq. TFEU and Art. 17 et seq. ESCB Statute. The differing view of the CJEU set out in its Judgment of 11 December 2018 does not merit a different conclusion, given that on this

¹ Case ECLI:EU:C:2018:1000.

² Case ECLI:DE:BVerfG:2020:rs20200505.2bvr085915.

³ Judgment of the FCC in case 2 BvR 859/15, para. 1, as translated into English and made available on the FCC's website, https://www.bundesverfassungsgericht.de/SharedDocs/Entscheidungen/EN/2020/05/rs20200505_2bvr085915en.html (accessed 2 June 2020).

⁴ 2 BvR 859/15, para. 98.

⁵ 2 BvR 859/15, para. 106.

point, the judgment is simply not comprehensible so that, to this extent, the judgment was rendered *ultra vires*.⁶

In particular, the FCC considered that ‘the Judgment of the CJEU of 11 December 2018 manifestly exceeds the mandate conferred upon it in Article 19(1) second sentence TEU’ because it failed to assess properly the principle of proportionality in Article 5(4) TEU.⁷

The CJEU has already made its views known in a statement that was released on 8 May 2020. It ‘recalled that the Court of Justice has consistently held that a judgment in which the Court gives a preliminary ruling is binding on the national court’ and that ‘in order to ensure that EU law is applied uniformly, the Court of Justice alone ... has jurisdiction to rule that an act of an EU institution is contrary to EU law’.⁸ A similar line of reasoning was developed by the AG in paragraphs 59–61 of his opinion in case C-62/14, *Gauweiler* which was the first ever request by the FCC for a preliminary ruling and which concerned another challenge to the ECB’s bond buying programme.⁹ The response of the ECB has been even more taciturn. Its press release merely mentioned that it took notice of the judgment and reiterated its commitment to its mandate, as well as noting that ‘[t]he Court of Justice of the European Union ruled in December 2018 that the ECB is acting within its price stability mandate’.¹⁰

The FCC judgment has sparked a large amount of commentary in the press and on the blogosphere. This commentary has focused on the validity of the FCC invoking principles of the German constitution and case law to interpret EU law, the consequences of the declaration of the CJEU judgment as *ultra vires* on the legal system of the EU, the risk of similar judgments in other Member States,¹¹ the likelihood or wisdom of the European Commission initiating infringement proceedings against Germany, the possible impact on the current ECB Pandemic Emergency Purchase Programme [PEPP] whose eligibility criteria are less strict than those of the PSPP, the faults in the economic reasoning of the judgment and the broader implications for the future of European integration.¹²

⁶ 2 BvR 859/15, para. 116.

⁷ 2 BvR 859/15, para. 119.

⁸ See Press Release 58/2020 of 8 May 2020, https://curia.europa.eu/jcms/jcms/p1_2999150/en/ (accessed 2 June 2020).

⁹ Case ECLI:EU:C:2015:400. The full text of the opinion of the AG, <http://curia.europa.eu/juris/document/document.jsf?text=&docid=161370&pageIndex=0&doclang=EN&mode=lst&dir=&occ=first&part=1&cid=9594081> (accessed 2 June 2020).

¹⁰ See ECB press release of 5 May 2020, <https://www.ecb.europa.eu/press/pr/date/2020/html/ecb.pr200505~00a09107a9.en.html> (accessed 2 June 2020).

¹¹ Euronews reported on 19 May 2020 that Hungary ‘will not accept a ruling by the European Court of Justice (ECJ) that said keeping migrants and asylum seekers in a transit zone on its border amounts to detention’.

¹² See e.g. D. Kyriazis, *The PSPP judgment of the German Constitutional Court: An Abrupt Pause to an Intricate Judicial Tango*, European Law Blog (6 May 2020), <https://europeanlawblog.eu/2020/05/06/the-pspp-judgment-of-the-german-constitutional-court-an-abrupt-pause-to-an-intricate-judicial-tango/> (accessed 2

In view of what has already been said on the judgment, the purpose of this article is to analyse the part of the FCC judgment concerning the substance of the PSPP. Indeed, with one or two exceptions,¹³ most commentary so far has not asked the rather fundamental question of whether there is any merit in the FCC's assessment of the proportionality of PSPP and its perceived encroachment on economic policy.

Judgments are typically evaluated according to the text of the relevant law or the inferred objectives of that law.¹⁴ But how can the judgment of a judgment be evaluated? After all, it is the first time in the history of the EU that a national court refuses to comply with a ruling of the CJEU and declares it *ultra vires*, although there have been reports that courts of other Member States have not followed strictly the rulings handed to them by the CJEU.¹⁵ In this case, it seems that the most straightforward approach is to juxtapose the two judgments and identify and evaluate the reasons for which the FCC faults the CJEU.

The article argues that the analysis of the FCC on the substance of the case is wrong on three grounds. It invents a new and impossible test of proportionality, it misconstrues the scope of monetary policy and it fails to appreciate the significance of the ECB's purchase of bonds on the secondary market on the ability of a Member State to borrow and run deficits.

To be fair to the FCC, part of the problem stems from the analysis of the CJEU itself in its judgments in *Gauweiler* [C-62/14] and *Weiss* [C-493/17]. The CJEU was not sufficiently clear as to the boundaries of the proportionality test and the weighting of conflicting interests (i.e. what effects need to be taken into account and how). It was not sufficiently bold to state that monetary policy necessarily had to affect economic policy and that the effectiveness of monetary policy could be

June 2020), M. Maduro, *Some Preliminary Remarks on the PSPP Decision of the German Constitutional Court*, *Verfassungsblog* (6 May 2020), <https://verfassungsblog.de/some-preliminary-remarks-on-the-pspp-decision-of-the-german-constitutional-court/> (accessed 2 June 2020) T. Marzal, *Is the BVerfG PSPP Decision 'Simply Not Comprehensible'?*, *Verfassungsblog* (9 May 2020), <https://verfassungsblog.de/is-the-bverfg-pspp-decision-simply-not-comprehensible/> (accessed 2 June 2020) K. Pistor, *Germany's Constitutional Court Goes Rogue*, *Project Syndicate* (8 May 2020), https://www.project-syndicate.org/commentary/german-constitutional-court-ecb-ruling-may-threaten-euro-by-katharina-pistor-2020-05?utm_source=twitter&utm_medium=organic-social&utm_campaign=page-posts-may20&utm_post-type=link&utm_format=16:9&utm_create=quote-card&utm_post-date=2020-05-08 (accessed 2 June 2020); P. Meier-Beck, *Ultra Vires?*, *D-Kart Antitrust Blog* (11 May 2020), <https://www.d-kart.de/en/blog/2020/05/11/ultra-vires/> (accessed 2 June 2020); L. Bini Smaghi, *The Judgment of the German Constitutional Court is Incomprehensible*, *Policy Brief 25/2020*, Luiss University, <https://sep.luiss.it/sites/sep.luiss.it/files/The%20Judgment%20of%20the%20GCC%20is%20incomprehensible.pdf> (accessed 2 June 2020).

¹³ See P. Meier-Beck, *supra* n. 12.

¹⁴ See P. Craig, *Pringle: Legal Reasoning, Text, Purpose and Teleology*, 20(1) *Maastricht J. Eur. & Comp. L.* 3 (2013). See also the critique of Craig's approach by G. Beck, *The legal Reasoning of the Court of Justice and the Euro Crisis*, 20(4) *Maastricht J. Eur. & Comp. L.* 635 (2013) and Craig's response *Pringle and the Nature of Legal Reasoning*, *Maastricht J. Eur. & Comp. L.* 205 (2014).

¹⁵ I am grateful to a referee who pointed this out. M. Benackova, Ajos (Dansk Industri), *A challenge to the primacy of EU law?*, *KSLR EU Law Blog* (4 Sept. 2017), <https://blogs.kcl.ac.uk/kslreuropeanlawblog/?p=1150#.XtYoulVLjX6> (accessed 2 June 2020).

proportional to its impact on economic policy. And it was not sufficiently thorough in its appraisal of the significance of bond purchases on the secondary market. The CJEU tried to be comprehensive referring to many different factors with the result that it made its judgment vulnerable to the charge that it did not consider all the relevant factors. In admittedly grossly oversimplified terms, this was in a nutshell the grievance of the FCC.

The article is structured as follows. Section 2 below, presents the relevant issues of the ruling of the CJEU in *Weiss*. Section 3 reviews and appraises the judgment of the FCC. Section 4 concludes with a summary of the main points.

2 WHAT THE CJEU SAID IN WEISS

The FCC submitted five questions to the CJEU of which the fifth was found to be inadmissible. The first four questions asked the CJEU to assess the validity of the ECB decision 2015/774 launching the PSPP in the light of Article 119, Article 123 (1), Article 127(1)&(2) and the second paragraph of Article 296 TFEU and of Articles 17–24 of the Protocol on the ESCB and the ECB.

First, the CJEU examined whether the ECB had duly explained its decision. It found, in paragraphs 34–41 of the judgment, that the ECB did explain the reasons of decision 2015/774 because it had published various documents at that time detailing the economic analyses underpinning the decision, the various options it considered and the choices it made.

2.1 SCOPE OF MONETARY POLICY AND IMPACT ON ECONOMIC POLICY

Then, the CJEU turned its attention to Article 119 and Article 127(1) & (2) TFEU.

First, it noted, in paragraphs 50–52 that the FEU Treaty contains no precise definition of monetary policy. It defines only the objectives and instruments of monetary policy, with the primary objective being price stability [i.e. Articles 127 (1) and 282(2) TFEU], while the monetary functions and operations of the European System of Central Banks (ESCB) are laid down in Protocol 4 of the TFEU.

Then, in paragraphs 53–57, the CJEU examined whether decision 2015/774 fell within the scope of monetary policy and concluded that it did because its purpose was to raise the rate of inflation to close but below 2%.

However, the CJEU acknowledged, in paragraph 59, that PSPP could affect economic policy too. Nonetheless, it stressed that '(60) the authors of the Treaties did not intend to make an absolute separation between economic and monetary policies'.

The CJEU went on to underline that '(61) a monetary policy measure cannot be treated as equivalent to an economic policy measure for the sole reason that it may have indirect effects that can also be sought in the context of economic policy' and that '(64) the conduct of monetary policy will always 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'. It concluded that '(66) the ESCB necessarily has to adopt measures that have certain effects on the real economy, which might also be sought – to different ends – in the context of economic policy'.

Indeed, there is but one economy. Economic policy and monetary policy both aim to manage the same economy via different channels and with the use of different instruments. They unavoidably interact. Monetary policy must necessarily influence the behaviour of economic actors in order to keep the rate of inflation below but close to 2%. Both policies can reinforce or constrain each other. This interrelationship was acknowledged soon after the Treaty of Maastricht came into force. Recitals 1 and 8 of Regulation 1466/1997 of the Stability and Growth Pact, which is undoubtedly in the realm of economic policy, state explicitly: 'the Stability and Growth Pact is based on the objective of sound government finances as a means of strengthening the conditions for price stability' and 'the maintenance of sound budgetary positions in these Member States will be necessary to support price stability'. Similarly, price stability facilitates investment and economic growth and therefore supports the typical objectives of economic policy. In this way, it facilitates or strengthens economic policy.

To put it differently, a monetary policy that has no impact on the behaviour of economic operators and, therefore, no indirect impact on economic policy, would be completely ineffective. If the Treaty prohibited monetary policy from having any effect on economic policy it would emasculate it and deprive it of any ability to maintain price stability. Even if one believes that inflation is a purely monetary phenomenon and is determined exclusively by the amount of money in the economy, prices can rise only if demand for goods and services increases. For this to happen, monetary policy must be able to affect the real economy which in turn affects economic policy.

2.2 THE PROPORTIONALITY OF DECISION 2015/774

One of the main arguments of the applicants was that the PSPP infringed the principle of proportionality.

The CJEU acknowledged that '(71) it follows from Article 119(2) TFEU and Article 127(1) TFEU, read in conjunction with Article 5(4) Treaty on the European Union (TEU), that a bond-buying programme forming part of monetary policy may be validly adopted and implemented only in so far as the measures that it entails are proportionate to the objectives of that policy'.

Then it recalled that '(72) according to settled case-law of the Court, the principle of proportionality requires that acts of the EU institutions should be suitable for attaining the legitimate objectives pursued by the legislation at issue and should not go beyond what is necessary to achieve those objectives'.¹⁶

Article 5(4) TEU stipulates that 'under the principle of proportionality, the content and form of Union action shall not exceed what is necessary to achieve the objectives of the Treaties'. Indeed, whether a measure is proportional is assessed in relation to its objectives. In practice, it means that if there is a less interventionist or distortionary means of achieving the same objective, it should be preferred.¹⁷ It does not mean that the effects in one policy area have to be balanced against the effects in other policy areas, unless the Treaties explicitly require so.

For example, according to Article 107(3)(c) TFEU, state aid may be compatible with the internal market when it is necessary for the development of a certain economic activity or economic area, but only 'where such aid does not adversely affect trading conditions to an extent contrary to the common interest'. The same balancing is required by Article 106(2) TFEU which allows measures in favour of providers of services of general economic interest but only on condition that 'the development of trade must not be affected to such an extent as would be contrary to the interests of the Union'.

In fact, nowhere in *Weiss* [or in *Gauweiler* which is the source cited in *Weiss*] did the CJEU refer to balancing between different policies or between the effects of different policies.

It should also be pointed out that the definitions of proportionality in both *Weiss* and *Gauweiler* vary slightly from definitions in other landmark cases. If one follows the trail of case law starting with that which is cited in *Gauweiler* one finally arrives at the following formulation of the principle:

¹⁶ The same wording was used by the CJEU in *Gauweiler*, para. 67, although the word 'appropriate' was replaced in *Weiss* by 'suitable'. EU acts must 'be appropriate for attaining the legitimate objectives pursued by the legislation at issue and must not go beyond what is necessary to achieve them'. The source cited in *Gauweiler* was case C-59/11, *Association Kokopelli*, para. 38.

¹⁷ According to the proportionality test, acts of EU institutions may 'not exceed the limits of what is appropriate and necessary in order to attain the objectives legitimately pursued by the legislation in question; when there is a choice between several appropriate measures recourse must be had to the least onerous, and the disadvantages caused must not be disproportionate to the aims pursued'. [Judgment of the CJEU in case C-343/09, *Afton Chemical*, EU:C:2010:419, para. 45].

(96) The principle of proportionality, ... , requires that measures adopted by Community institutions do not exceed the limits of what is appropriate and necessary in order to attain the objectives legitimately pursued by the legislation in question; when there is a choice between several appropriate measures recourse must be had to the least onerous, and the disadvantages caused must not be disproportionate to the aims pursued.¹⁸

What is missing from the definition in *Weiss* is the requirement that ‘the disadvantages caused must not be disproportionate to the aims pursued’. Perhaps this requirement was assimilated into the condition that EU acts ‘should not go beyond what is necessary’.

For the purposes of this article, the crucial issue is how the CJEU has dealt with the balancing of the disadvantages caused by monetary policy in *Weiss* and whether its assessment was consonant with previous case law. In reviewing this case law, it is in fact not possible to identify any particular test or method that has been applied by the CJEU in any consistent manner to carry out that balancing. Instead one can identify statements that close the argument. For example, in *Fedesa*, cited above, the Court answered the question whether the disadvantages were disproportional in the following manner: ‘(17) Finally, it must be stated that the importance of the objectives pursued is such as to justify even substantial negative financial consequences for certain traders’. In other cases, the CJEU has found the principle of proportionality to be satisfied because the measures in questions were not manifestly inappropriate.

In *Gauweiler* the CJEU concluded, in a single sentence, that ‘(91) the ESCB weighed up the various interests in play so as to actually prevent disadvantages from arising, when the programme in question is implemented, which are manifestly disproportionate to the programme’s objectives’. Although the CJEU examined the limits and safeguards of the ECB action, it provided no further explanation as to the precise nature of those interests, how they were weighted, and why the disadvantages were not manifestly disproportionate.

My conclusion from the review of the case law on the principle of proportionality is that determining whether a measure is appropriate [or manifestly inappropriate], necessary or proportionate *strictu sensu* is a difficult but not impossible task. By contrast, whether disadvantages are disproportionate, which requires a balancing between the positive and negative effects of a measure, is an exceedingly difficult task that has been settled with a certain degree of inevitable arbitrariness by the CJEU.¹⁹ Perhaps this is indeed the role of the courts; to bring closure to arguments which cannot be resolved with a more scientific or objective method. But the implication of

¹⁸ Case C-180/96, *UK v. European Commission*, EU:C:1998:192. See also cases C-331/88, *Fedesa and Others* [1990] ECR I-4023, para. 13, and Joined Cases C-133/93, C-300/93 and C-362/93, *Crispoltoni* [1994] ECR I-4863, para. 41.

¹⁹ A similar conclusion is reached by Sauter who writes that ‘the occurrence of strict proportionality as detailed balancing between competing rights and norms is rare.’ See W. Sauter, *Proportionality in EU Law: A Balancing Act?*, 15 *Cam. Y. B Eur. Legal Stud.* 439–466 (2013).

this conclusion is that the institution that implements the policy in question must be granted wide decision-making discretion, as the CJEU in fact does.

Given the difficulty of carrying out any true balancing of conflicting effects or interests, it is not surprising that, after considering the information that was taken into account by the ECB, the CJEU concluded, in paragraphs 81–92, that the objective of nudging upwards the rate of inflation could not be achieved with other measures entailing more limited action and that the PSPP did not go beyond what was necessary to achieve that objective.

The applicants also claimed that the PSPP was disproportional because the ECB ran the risk of making a loss and, consequently, it had undesirable side effects. The CJEU's response was that '(93) the ESCB weighed up the various interests involved so as effectively to prevent disadvantages which are manifestly disproportionate to the PSPP's objective from arising on implementation of the programme'. But it did not clarify further how that weighting had been done. Instead it noted that '(94) open market operations authorized by the authors of the Treaties inevitably entail a risk of losses. However, 'the ESCB has adopted various measures designed to circumscribe that risk and to take it into account'.

Open market operations, like any market transaction, involve risk and the possibility of loss. When the ECB buys securities, it necessarily exposes itself to the risk that the price of the securities may decline. The important point here is that if the ECB had to avoid risk it would not engage in open market operations. Of course, the larger the transactions, the greater the exposure of the ECB to risk. But this is a natural consequence of having to resort to unconventional measures to raise the level of inflation.

Moreover, the mission of central banks is not to make profit or avoid risk. It is to achieve their monetary policy objectives assigned to them by law. Therefore, assuming risk or incurring losses is necessary for the achievement of public policy objectives. In case T-79/13, *Accorinti v. ECB*, paragraph 92, the General Court concluded that private investors who bought Greek bonds and the ECB were not in the same situation because the investors sought to make profit while the ECB pursued a public policy objective. The same conclusion was reached by the General Court in case T-749/15, *Nausicaa Anadyomène and Banque d'escompte v. ECB*, paragraph 116.

In conclusion, the CJEU confined itself to examining the negative effects of the PSPP on the ESCB itself rather than on economic policy. We will see later on that the FCC conceived the balancing of the positives and negatives of PSPP in a much wider context.

2.3 PROHIBITION OF MONETIZATION OF PUBLIC DEBT: ARTICLE 123(1) TFEU

Lastly, the CJEU turned its attention to the question whether the PSPP infringed Article 123(1) TFEU.

The CJEU, first, reiterated, in paragraph 103, that Article 123(1) does not prohibit the ECB from buying bonds on the secondary market, i.e. from investors who bought the bonds directly from the issuing Member State or from other investors. However, it went on, in paragraphs 105–106, to recall two conditions that were first defined in its judgment in case C-62/14, *Gauweiler*, paragraphs 97–109, to ensure that there would be no indirect monetary financing. First, the ECB may not buy bonds on the secondary markets if that would have an effect equivalent to direct purchasing of bonds from Member States. Second, the ECB must build sufficient safeguards into its intervention so as to ensure that it does not reduce the impetus to Member States to follow sound budgetary policies.

Then the CJEU went on to examine whether indeed those two conditions had been satisfied.

2.3[a] *Was the PSPP Equivalent to Purchases Directly from the Issuing Authority?*

The crux of the matter here is that if private investors are certain that the bonds they buy from a public authority can subsequently be sold to the ECB on the secondary market then the ECB's purchase is equivalent to buying directly from the issuer. The interjection of the investors has no material effect on the price and quantity of the bonds. This is an important part of the judgments of both the CJEU and the FCC and therefore needs to be analysed in depth.

Article 123 does not prohibit purchases by the ECB on the secondary market because in the meantime the price of the bond reflects its actual value as assessed by private investors according to the credit worthiness of the issuer. If investors know that the ECB will buy all bonds at the issuing price then they would be willing to pay the issuing price at whatever level is set by the issuer. But if they are uncertain as to whether they can offload the bonds they hold individually, then they would pay in the first place only the price that reflects the true probability of default of the issuer because if the ECB does buy their bonds they need to be able to sell them to other investors. It follows that under these conditions the issuer does not gain anything by the fact that the ECB buys bonds on the secondary market.

In this connection, there is a crucial aspect in all ECB bond buying programmes including the PSPP which is considered at several points in both judgments but whose logical consequence is not sufficiently examined either by the CJEU or the FCC. Both courts have noted that the ECB does not buy all the bonds of each issue. The PSPP, for example, limited such purchases to 25%

of each issue and to 33% of the aggregate bonds per issuer. The limits in the ECB's various bond purchasing programmes mean that investors know with 100% certainty that some of them will not be able to sell to the ECB. The important implication of this is that no investor would want to be left with bonds that are worth less than what they initially cost. Therefore, this simple rule whereby the ECB does not buy the whole issue results in investors not paying for the bond more than its real value, as assessed by the market. This is true regardless of whether the ECB announces beforehand whose bond it will buy, what proportion of the issue it will buy or for how long it will keep the bonds, provided that the ECB buys only a portion of each issue. The interjection of private investors always leads to the formation of a market price when the investors buy the bond from the issuing authority. The degree of certainty of buying by the ECB is not so relevant as the fact that not all investors in the end will be able to sell to the ECB.

Let's see now how the CJEU dealt with the question put to it by the FCC.

The CJEU followed the reasoning it had developed in *Gauweiler* [C-62/14, paragraph 104] and stated that:

(110) the ESCB's intervention would be incompatible with Article 123(1) TFEU if the potential purchasers of government bonds on the primary markets knew for certain that the ESCB was going to purchase those bonds within a certain period and under conditions allowing those market operators to act, de facto, as intermediaries for the ESCB for the direct purchase of those bonds from public authorities and bodies of the Member State concerned.

It then identified 'safeguards' that reduced the certainty for private investors:

– Observance of a blackout period so that bonds issued by a Member State could not be purchased by the ECB immediately after they were issued. [paragraph 114]

– Non-disclosure of the volume of bonds of any given Member State that the ECB intended to buy. [paragraph 118]

– A limit of 25% of any particular issue of bonds and a limit of 33% of the bonds of any Member State that could be bought by the ECB. [paragraph 124]

The CJEU concluded that '(125) when bonds are purchased from a central government of a Member State, a private operator necessarily runs the risk of not being able to resell them to the ESCB on the secondary markets, as a purchase of all the bonds issued is in all cases precluded'. Therefore, private investors are not afforded certainty by the PSPP.

2.3[b] *Reduced Impetus to Conduct a Sound Budgetary Policy?*

The CJEU, first, reiterated, in paragraph 130, that the conduct of monetary policy always entailed an impact on interest rates, which necessarily influenced the financing conditions of the public deficit of the Member States.

While it is true that open market operations and other monetary policy instruments aim to move interest rates and therefore indirectly affect financing conditions of public debt, the question here is not about the existence of such effects but whether the massive purchase of government bonds under the PSPP weakened budgetary discipline.

The answer of the CJEU, in paragraphs 132–141, was that the limits to which the PSPP was subject and the fact that it was temporary did not provide any assurances to Member States that they would be able either to increase their debt indefinitely or not to repay it.

While the temporal and quantitative limits do constrain the ability of Member States to run budget deficits indefinitely, the CJEU could have stressed the importance of the interjection of private investors. Since, as explained earlier, public bonds are acquired by private investors not at face value but at the price that reflects their market value, it is ultimately irrelevant that the ECB buys small or large amounts of those bonds on the secondary market, as long as it does not buy a significant portion of them. Then, the issuing Member State is always subject to the discipline of the market and must maintain a sound budgetary position. If it can sell bonds to the market, then its debt is sustainable.

On the basis of the above analysis, the CJEU concluded that the PSPP did not infringe any primary or secondary law.

Before turning to the judgment of the FCC, it needs to be pointed out that the CJEU did not refer at all to the EU rules that Member States must abide by in the conduct of their fiscal policy. This is strange because monetary policy is not implemented in a vacuum. After all, the referring court was concerned about monetary policy encroaching on economic policy. It is puzzling that in assessing whether the PSPP could attenuate budgetary discipline, the CJEU did not consider the constraints imposed on Member States by Article 126 TFEU, the Stability and Growth Pact and, of course, the Treaty on Stability Coordination and Governance. Even if the ECB would buy all public bonds at face value, Member States would still have to keep their budgets close to balance or in surplus.

3 WHAT THE FCC SAID IN WEISS

As mentioned in the introduction, this article covers only the parts of the FCC judgment that concern the interpretation of EU law rather than German constitutional law.

3.1 THE (NON) PROPORTIONALITY OF THE PSPP

With respect to the question whether the PSPP conformed with the principle of proportionality, given that the CJEU recognized that it affected economic policy, the FCC was of the view, expressed in paragraph 123, that the CJEU disregarded the actual effects of the PSPP and refrained from conducting an overall appraisal. Consequently, the principle of proportionality could not safeguard the competences of Member States. Instead it rendered meaningless the principle of conferral in Article 5(1)&(2) TEU.

In defining the principle of proportionality, the FCC also drew on German law [(125) In applying the principle of proportionality, German law distinguishes between the elements of suitability (*Geeignetheit*), necessity (*Erforderlichkeit*) and appropriateness (*Angemessenheit*) ...] and on similar notions from other legal traditions. This in itself is not unusual. The CJEU also draws inspiration from national legal traditions when it tackles issues for which there is no case law. However, there is rich case law on proportionality that was in fact acknowledged by the FCC which, in paragraph 126, identified its constituent components of suitability, appropriateness and necessity.

But the FCC took exception with:

(127) the specific manner in which the CJEU applies the principle of proportionality in the case at hand [because it] renders that principle meaningless for the purposes of distinguishing, in relation to the PSPP, between monetary policy and economic policy, i.e. between the exclusive monetary policy competence conferred upon the EU (Art. 3(1) lit. c TFEU) and the limited conferral upon the EU of the competence to coordinate general economic policies, with the Member States retaining the competence for economic policy at large (Art. 4(1) TEU; Art.5(1) TFEU).

Here the FCC conflated the instruments of the two policies and their effects. Monetary policy belongs exclusively to the EU. The TFEU also defines the instruments of that policy and it is clear that no fiscal competences are conferred to the ECB such as the power of taxation. In this sense there is a separation of instruments. But, nowhere in the TFEU is there a requirement for separation of effects. It would be nonsensical if the TFEU imposed such a separation, as it would deprive monetary policy of its effectiveness.

Nonetheless, the FCC considered that:

‘(133) when applied in this manner, as undertaken by the CJEU, the principle of proportionality enshrined in Art. 5(1) second sentence and Art. 5(4) TEU cannot fulfil its corrective function for the purposes of safeguarding the competences of the Member States. The complete disregard of the PSPP’s economic policy effects means that already the determination of the ESCB’s objectives is not comprehensible from a methodological perspective As a result, the review of proportionality is rendered meaningless, given that suitability and necessity of the PSPP are not balanced against the economic policy effects – other than the risk of losses – arising from the programme to the detriment of Member States’ competences, and that these adverse effects are not weighed against the beneficial effects the programme aims to achieve’. [emphasis added]

It is amply obvious that the main concern of the FCC was the perceived encroachment of ECB on the competences of Member States, for which the appropriate test is the principle of conferral. In this respect the FCC conflated the principles of proportionality and conferral. It used proportionality to rule on conferral and the incursion, in its view, of the ECB in economic policy. Furthermore, the test of proportionality used by the FCC shifted subtly from achieving a policy objective with the least interventionist instrument to balancing the effects of monetary policy against those in economic policy, which is a different policy area.

The FCC criticized, in paragraphs 136–137, the CJEU for accepting the proclaimed objectives of the ECB without detailed scrutiny of the consequences of the PSPP. In its view, the purported monetary policy objective of the PSPP was ‘possibly only invoked to disguise what essentially constituted an economic and fiscal policy agenda’:

‘(138) As the economic policy effects of the PSPP are disregarded completely, the application of the principle of proportionality by the CJEU cannot fulfil its purpose, given that its key element – the balancing of conflicting interests – is missing. As a result, the review of proportionality is rendered meaningless’. [emphasis added]

As seen in the previous section, the CJEU did not disregard the economic policy effects of the PSPP. In fact, it did the opposite. It considered those effects unavoidable for the achievement of monetary policy. The FCC pursued a dogmatic approach that seemed to ignore the necessity of monetary policy to have an economic impact.

The FCC then asserted that:

(139) relying on the principle of proportionality to distinguish between monetary policy and economic policy (Art. 5(1) second sentence and Art. 5(4) TEU) implies that a programme’s effects can render it disproportionate. Thus, assessing the consequences of such a programme is a necessary step in the delimitation of competences.

The FCC went on to identify the various effects of monetary policy on the real economy such as public debt, personal savings, pension and retirement schemes, real

estate prices and the keeping afloat of economically unviable companies and to insist that the ECB should have carried out a ‘weighing these effects against the monetary policy objective’. [emphasis added]

It is undoubtedly true that monetary policy does affect such things as public debt, personal savings, pension and retirement schemes and real estate prices. But proportionality cannot be the correct test for assessing whether the ECB went beyond its competences. This is because monetary policy always seeks to influence the real economy. There is no *a priori* reason that such effects must be in some sense proportional to monetary policy. Moreover, there is no apparent method for weighing them. And, above all, there is no such thing as proportional infringement of the principle of conferral or sufficiently small abuse of competences, as the balancing required by the FCC would imply.

The FCC understood proportionality to mean a balancing of monetary policy and economic policy. This is a new and impossible test that, if it were implemented by the ECB, it would undermine the ECB’s primary task of maintaining price stability.

It is a new test because the notion of proportionality does not require balancing between ‘conflicting’ policy objectives but an assessment as to whether a certain policy objective can be achieved with less interventionist or distortionary means so that EU action ‘shall not exceed what is necessary to achieve’ the particular policy objective. Balancing is carried out only when the treaties require so, as for example, in Article 106(2) TFEU or Article 107(3) TFEU. No such balancing obligation is imposed on the ECB by Article 127 TFEU or Article 282 TFEU. In fact, as argued below, Article 127 TFEU requires the opposite.

The new test is in fact impossible to comply with. The Treaty does not contain any definition of monetary or economic policy. Economic policy can comprise many different actions and instruments. Regardless of how it might have been defined by the ECB, it would have easily been a matter of dispute. More importantly, the ECB would have to identify a common denominator in order to balance the effects of monetary and economic policy. No such denominator exists in the economic literature. But even supposing that such a common measure of economic and monetary policy could have been identified, at which level would it have to be set by the ECB? Either the FCC would have to concede that the ECB enjoyed discretion, otherwise whatever level was determined by the ECB would be declared arbitrary.

In its critique of the CJEU and the ECB, the FCC specified in detail many issues that could have been considered by the ECB, and the CJEU [e.g. savings, pensions, failing firms], but did not articulate what would constitute sufficient assessment of proportionality. It demanded a ‘balancing of conflicting interests’, as the ‘key element’ of proportionality, but did not indicate how that balancing could be established or proven.

But the fundamental problem with the FCC's conception of proportionality is that it contradicts its own view that monetary policy and economic policy must be conducted separately.²⁰ If the ECB had to comply with the proportionality test as formulated by the FCC, it would infringe Article 127(1) TFEU. Article 127(1) stipulates that:

the primary objective of the European System of Central Banks (hereinafter referred to as 'the ESCB') shall be to maintain price stability. Without prejudice to the objective of price stability, the ESCB shall support the general economic policies in the Union with a view to contributing to the achievement of the objectives of the Union as laid down in Article 3 of the Treaty on European Union. [emphasis added].

'Without prejudice to the objective of price stability' means that the ECB must not support economic policies if that would compromise its monetary policy. Balancing of conflicting interests, as the FCC asked the ECB to do, means that the ECB must take into account the impact of monetary policy on economic policy. This unavoidably results in trade-offs and compromises. But the Treaty forbids the ECB to consider any economic effects if that would weaken its ability to maintain price stability. Perhaps the FCC could have said that the ECB should prefer the monetary policy measures that achieve price stability with the smallest impact on economic policy, but it didn't. It complained that the 'suitability and necessity of the PSPP are not balanced against the economic policy effects' and that the 'adverse effects [on economic policy] are not weighed against the beneficial effects the programme aims to achieve' [paragraph 133].

3.2 ENCROACHMENT OF MONETARY POLICY ON ECONOMIC POLICY

The FCC also examined whether the PSPP encroached on economic policy. It stated that:

(163) the interpretation of the ECB's monetary policy mandate, as undertaken by the CJEU, encroaches upon the competences of the Member States for economic and fiscal policy matters. ... [The CJEU] refrains from subjecting the ECB's actions to an effective review as to conformity with the order of competences on the basis of the principle of proportionality, including a balancing of the economic and fiscal policy effects of the PSPP against its monetary policy objective ... The CJEU thus acted *ultra vires*, which is why, in that respect, its Judgment has no binding force in Germany.

²⁰

In this connection, an anonymous referee challenged me to take a position on the 'untenable' division of powers in the Treaty between monetary policy and economic policy. Although this is an important issue, especially because economic theory suggests that a well-functioning monetary union requires centralized fiscal competences that go beyond mere coordination of economic policies, it falls outside the scope of this article.

Then it found, correctly, that:

(170) the PSPP improves the refinancing conditions of the Member States as it allows them to obtain financing on the capital markets at considerably better conditions than would otherwise be the case. ... It is therefore undisputed that the budgetary situations of Member States benefit from the reduction of general interest rates facilitated by the PSPP [...]. This gives rise to the risk – despite the “safeguards” referred to by the CJEU – that necessary consolidation and reform measures will either not be implemented or discontinued [...].

There is no doubt that the ECB’s purchasing of government bonds, by reducing interest rates, makes it easier for Member States to finance their debt. However, it must be stressed that it does not necessarily follow that ‘consolidation and reform measures will either not be implemented or discontinued’. On the contrary, by reducing the costs of servicing the debt of Member States, the ECB intervention may in fact enable Member States to fund compensatory measures to smoothen the negative impact of reform. Moreover, the FCC appeared to ignore the binding effect of Articles 121 and 126 TFEU and of the regulations in the Stability and Growth Pact, even though it mentioned that the PSPP had an ‘impact on fiscal policy terms’. The ECB intervention did not weaken the powers of the Council.

The FCC then returned to the various ways that monetary policy could affect the real economy:

(173) Relevant economic policy effects of the PSPP furthermore include the risk of creating 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 shareholders, tenants, real estate owners, savers or insurance policy holders.

‘(174) As the PSPP lowers general interest rates, it allows economically unviable companies to stay on the market since they gain access to cheap credit’.

(176) In view of the considerable economic policy effects resulting from the PSPP – not all of which are discussed here –, it would have been incumbent upon the ECB to weigh these effects and balance them, based on proportionality considerations, against the expected positive contributions to achieving the monetary policy objective the ECB itself has set.

As discussed earlier, proportionality is not the right test for questions of competence and conferral of powers. The logic of the FCC’s proportionality test is that larger economic effects can only be justified against larger monetary effects. If that balancing could somehow be achieved, it would simply worsen the perceived encroachment on economic policy.

The important point in this respect is that the FCC had a very broad definition in mind of the concept of economic policy. Such a broad definition is not necessarily wrong in itself. It indicates that under the term ‘economic policy’ one can include every conceivable effect on the real economy.

But the breadth of economic policy leads to the conclusion that again the FCC sets up a vague and therefore impossible test for the ECB. The ECB would never be sure whether its analysis would be sufficient.

As with the balancing of conflicting interests, the diversity of effects that fall within the broad scope of economic policy begs the question how they can be summed up in any meaningful manner and whether the ECB would ever be able to conclude credibly that ‘on the whole the economic effects are minimal’. It would have to invent artificial weights for each of the many different effects. The ECB went to great lengths to explain at the time that its actions fell within the scope of monetary policy, that they were necessary given the disruption of the monetary transmission mechanism and that they were not excessive [i.e. they were proportional]. However, the vagueness of the criteria that were used to justify the proportionality of the PSPP rather proves the impossibility of achieving the level of precision demanded by the FCC.²¹

Perhaps more disturbing in this context is the belief of the FCC that because economic policy remains mainly the responsibility of Member States, the ECB must refrain from affecting the real economy. The FCC did not explain how it expected the ECB to implement monetary policy without affecting the real economy and the behaviour of economic operators.

Lastly, monetary policy, like any other public policy, has at all times both positive and negative effects on some economic operators. The fact that the PSPP leads to lower interest rates and may harm savers or enable marginal firms to remain in the market is irrelevant. An increase in interest rates harms borrowers and forces the exit of firms that are viable at lower rates. Regardless of whether interest rates go up or down, someone is harmed. The FCC completely ignored this simple fact. In other words, to criticize monetary policy for having a negative impact on some economic operators is equivalent to criticising monetary policy for having any impact at all.

3.3 SAFEGUARDS AND WEAKENING OF INCENTIVES FOR SOUND BUDGETARY POLICY

In paragraphs 178–195 of its judgment, the FCC carried out a very detailed assessment of the safeguards in Decision 2015/774 such as the various limits on the timing and amounts of bond purchases and found that the CJEU did not review their effects on bond-issuing Member States with sufficient rigour. It underlined, in paragraph 199, that Member States and market operators knew in advance the overall volume of bonds that were to be purchased, the distribution of purchases between the

²¹ See the explanations and press conference of the ECB in Jan. 2015, <https://www.ecb.europa.eu/press/accounts/2015/html/mg150219.en.html> and, <https://www.ecb.europa.eu/press/pressconf/2015/html/is150122.en.html> (accessed 2 June 2020).

national central banks in accordance with their holding of shares in ECB's capital, the eligibility criteria for securities and the initial duration of the PSPP. As will be explained below, this information is not sufficient to eliminate an important element of uncertainty for market operators.

Indeed, a few paragraphs later on, the FCC appeared to concede that sufficient uncertainty for market operators remained in the system:

(202) It was established in the oral hearing that the purchase limit of 33% still allows for a sufficient "safety margin" ensuring that there is no actual certainty regarding purchases of bonds by the Eurosystem; it was also established that only on this condition can it be assumed that the market is not dominated by the Eurosystem, which is imperative for preventing Member States and market operators from being largely certain that newly issued government bonds will be purchased by the ESCB.

Nevertheless, the FCC went on to criticize the CJEU on the grounds that:

(214) given that the CJEU refrained from conducting a more thorough review, some of these "safeguards" cannot be comprehensibly assessed as to whether they even constitute suitable means for ensuring the necessary level of uncertainty on the part of Member States and market operators in relation to the bond purchases.

The FCC was correct that the CJEU did not examine explicitly the suitability of those safeguards or their impact on the level of uncertainty and only once did it refer to their contribution to the effectiveness of the PSPP [at paragraph 111] without, however, elaborating how they achieved that. But, the FCC also failed to carry out an 'overall assessment and appraisal of the relevant circumstances' which is necessarily a subjective exercise. The conduct of monetary policy is always prospective. It aims to affect the expected future behaviour of economic operators. It is based on modelling of past behaviour to predict future behaviour and therefore has an unavoidable element of experimentation. Experts can and do disagree. Therefore, when the FCC stated that the ECB and, by implication the CJEU, had to demonstrate that the safeguards constituted 'suitable means for ensuring the necessary level of uncertainty' and the extent to which 'the failure to use certain options reinforces market expectations that might actually lead to certainty' it in fact raised the standard of proof very high and lowered the degree of discretion of the ECB very low.

At the same time, the FCC committed the same omission as the CJEU by neglecting to consider the decisive nature of the interjection of private operators between the sale of public bonds on the primary market and the purchase by the ECB on the secondary market. Just like the CJEU, it also ignored whether Member States could escape from complying with Article 126 TFEU, even if the ECB would pursue an accommodating monetary policy.

As already explained in the previous section, the CJEU referred to 'sound budgetary policy' first in *Gauweiler* and then *Weiss*, and considered that that would

be the case if monetary policy would not 'lead to excessively high levels of debt or excessive Member State deficit'. Therefore, could the PSPP lead Member States to pursue unsound budgetary policy by enabling them to keep selling bonds for as long as the ECB was willing to buy them?

As argued in the previous section, the answer to this question is that once a market price is formed as a result of the interjection of market investors, a Member State can sell bonds in the first place only on terms and in amounts that the market is willing to buy. By definition, any country can run a budget deficit only as long as the market is willing to finance that deficit. If, therefore, sound budgetary policy means remaining subject to the discipline of the market, which necessarily entails the ability to repay the debt owed to the market, the purchase of public bonds by the ECB does not attenuate the discipline of the market as long as private investors are willing to buy those bonds first.

4 CONCLUSIONS

The ECB implements monetary policy on the basis of complex models of the Eurozone economy. The ECB has a pretty good idea of how the economy is affected when it tweaks this or that instrument. Since any movement in interest rates is likely to generate gains for some and cause losses for others, it is perfectly reasonable to expect the ECB to use its monetary instruments judiciously and not to go beyond what is necessary to nudge the rate of inflation to close but below 2%. But to expect it that somehow it can weigh the increase of inflation to the desirable rate against the impact on this or that economic sector is setting for it an impossible standard of performance. Even if one believes that the ECB has strayed beyond its mandate, balancing of conflicting interests is neither the right test for infringement of the principle of conferral, nor for the proper conduct of monetary policy.

The judgment of the CJEU in *Weiss* may not be a paragon of comprehensive and meticulous assessment of the ECB's PSPP. Some of the criticisms of the FCC are well founded. However, the judgment of the FCC itself is defective in at least eight respects.

First, it invents a new and impossible test of proportionality. Instead of understanding proportionality as the least interventionist means of achieving a certain policy objective, it defines it as the balancing between conflicting policy objectives which in this case are monetary and economic policy.

Second, it holds that the ECB must not encroach on economic policy and rejects the view of the CJEU that monetary policy has an inevitable and, in fact, welcome impact on economic policy. A monetary policy that does not affect the real economy would be an ineffective policy.

Third, economic policy is a vague term that covers many different aspects of the real economy. By demanding that the ECB accounts for all possible effects on economic policy, the FCC sets an unattainable target for the ECB and exposes it to unending criticism of not having considered sufficiently this or that effect or of not having defined the right weight for the different effects.

Fourth, monetary policy, like any other public policy, always has positive or negative effects on some economic operators, regardless of whether interest rates increase or decrease. The ECB cannot avoid negative effects, even if it does nothing. However, legitimate public policy concerns may in fact require the ECB to impose costs on certain economic operators, as for example, when it tries to deflate an asset bubble.

Fifth, for none of the above tests of proportionality, in general, or of minimising encroachment on economic policy and negative effects on economic operators, in particular, has the FCC defined what would be a justifiable or acceptable balance. The ECB is destined to fail without knowing the standard of proof it must achieve.

Sixth, had the ECB attempted to balance monetary and economic policy effects, it would have infringed Article 127(1) TFEU which requires that the support of economic policy by the ECB must be without prejudice to price stability.

Seventh, the FCC appeared to be using its own test of proportionality in order to prevent the ECB from straying into economic policy and infringing the principle of conferral. This is an inappropriate test for dealing with questions of competence. The balancing of conflicting effects may in fact worsen the perceived infringement, if the effectiveness of monetary policy is directly related to the size or extent of its impact on economic policy.

Eighth, the FCC did not appreciate the importance of the fact that the ECB buys public bonds from private investors and that the interjection of private investors deprives Member States from the ability to sell unlimited amounts of bonds at prices that would enable them to run indefinite budget deficits. The FCC, like the CJEU, did not take sufficient account of the constraining effect of Article 126 TFEU and the Stability and Growth Pact.

