

Stefan Oeter

**Conflict at the Interface of Economic
Policy and Law**

**Cognitive Dissonance between European Central
bank and German Constitutional Court**

**Paper at the Workshop „Europe´s Crisis: The Conflict-
Theoretic Perspective“, Freiburg, Sept. 25-26, 2014**

1. Starting Point

- The Euro crisis triggered a series of far-reaching fiscal, economic, social and political reforms in a number of EU states – reforms that are highly unpopular in most member states of the EU
- We can observe strong societal resistance against these reforms, supported by parts of the legal academia and courts
- Resistance is not limited to directly affected states, but occurs also in states that seem more or less not affected by the crisis, like Germany

1. Starting Point

- Resulting conflict between EU and the national legal elites, in particular the constitutional courts, is thus not only explainable in terms of political resistance against intrusive reforms drastically changing the internal social and political fabric
- Some of the resistance is also the product of conflicting visions of the fabric of European integration and differing constructions of EU law – here termed as phenomena of cognitive dissonance.

1. Starting Point

- The most striking example for such a line of conflict is the recent conflict between European Central Bank and the German Constitutional Court.
- The court follows a very traditionalist idea of economic sovereignty with national parliaments as the guardians of national sovereignty, perceiving delegated competences as narrowly limited, with the parliaments policing the limits of delegation of competences.
- Does this not entrust a drug-addict with the task of controlling the supply of drugs? Parliaments are addicts to deficit-spending, debt financing with government loans depending on incentives for banks to buy state-bonds

2. OMT Decision of BVerfG

- Point of Reference is the OMT decision of BVerfG of 14 Jan. 2014 initiating the first referral of BVerfG to the ECJ ever
- Concerns decisive questions of the future development of European monetary policy
- In light of the importance of the questions involved one might expect particular diligence in the Court's reconstruction of ECB policies and of the economic background of the case
- This assumption proves false when analyzing in detail the decision – certain carelessness

2. OMT Decision of BVerfG

2.1. Procedural Issues

- Object of constitutional complaint is strange – usually linked to an act of (German) public authority – but here is the omitting of an action (against a measure of EU policy) the object of the complaint
- Real object of the complaint is the decision by the European Central Bank on OMT – not open to judicial control by BVerfG – instead the complaint is formally directed against the inactivity of German constitutional organs in controlling the activities of ECB
- Difficult to imagine what might be the actions of German authorities in limiting the scope of action of ECB, while direct action of national control of ECB would be contrary to independence of ECB

2. OMT Decision of BVerfG

2.1. Procedural Issues

- Duty to have a debate on ECB policies in German parliament?
-
- “I doubt that any of the motions can be interpreted as being directed against the omission of an open-ended governmental or parliamentary debate. In relation to the specified objects of challenge, this is not a *minus* but an *aliud*. Apart from that, where the Federal Constitutional Court finds itself unable to identify specific decisions as mandatory under the Constitution, it is in my view not entitled to order, as an alternative or as a preliminary to further obligations not yet specified, that parliament or other supreme organs conduct a debate.”
 - Dissent Lübbe-Wolff para. 22

2. OMT Decision of BVerfG

2.1. Procedural Issues

- Rules on Standing in constitutional complaint have been inflated – Electoral rights under Art. 38 para.1 BL have degenerated into some kind of a „Popularklage“
- “An even more blatant innovation for which the Court cannot rely on determinative standards from previous case-law lies in the assumption that under specified conditions not only acts of German federal organs which positively transfer or restrict sovereign rights, but also mere inaction in the face of qualified transgressions on the part of the European Union can be challenged on the basis of Art. 38 sec. 1 GG (...). With this assumption, the Senate departs from earlier case-law, just recently corroborated....” – Dissent Lübbe-Wolff para. 17

2. OMT Decision of BVerfG

2.2. Referral to the ECJ

- Referral is the product of a logical trap created by the Constitutional Court - recent jurisprudence of the Court requires a „sufficiently qualified violation of the integration programme“ (Honeywell decision).
-
- “A sufficiently qualified violation of the integration programme requires that the violation is manifest and that the challenged act entails a structurally significant shift in the allocation of powers to the detriment of the Member States (cf. BVerfGE 126, 286 <304 and 305 with further references>). Transgressions of the mandate are structurally significant especially (but not only) if they cover areas that are part of the constitutional identity of the Federal Republic of Germany, which is protected by Art. 79 sec. 3 GG, or if they particularly affect the democratic discourse in the Member States” (para. 37)

2. OMT Decision of BVerfG

2.2. Referral to the ECJ

- Referral is necessary (according to the reasoning in Honeywell) if an ultra vires act is at stake – but the assumption of an *ultra vires act* requires a „manifest“ violation (difficult to argue in the OMT case)
- There is only a „simple“ violation, if at all, in OMT case
- “It would have to be considered a manifest and structurally significant transgression of its mandate if the European Central Bank acted beyond its monetary policy mandate (aa), or if the prohibition of monetary financing of the budget was violated by the OMT programme (bb).” (para. 38)

2. OMT Decision of BVerfG

2.3. Interpretation of Art. 119 (3), 127 (1) TFEU

- BVerfG interprets TFEU in a very particular way:

“According to Title VIII of the Treaty on the Functioning of the European Union and notwithstanding the special powers expressly assigned to the Union (e.g. Art. 121, 122, 126 TFEU), the responsibility for economic policy lies clearly with the Member States. In this field of economic policy, the European Union is – apart from individual exceptions that are in particular regulated in Part Three of the Treaty on the Functioning of the European Union – essentially limited to a coordination of Member States’ economic policies (Art. 119 sec. 1 TFEU). The European Central Bank may only support the general economic policies of the Member States (Art. 119 sec. 2, Art. 127 sec. 1 sentence 2 TFEU; Art. 2 sentence 2 ESCB Statute). It is not authorised to pursue its own economic policy. If one assumes – subject to the interpretation by the Court of Justice – that the OMT Decision is to be qualified as an independent act of economic policy, it manifestly violates this distribution of powers.” (para. 38)

2. OMT Decision of BVerfG

2.4. OMT Decision of ECB as General Economic Policy?

- Astonishing reconstruction of the objectives of OMT
- The OMT Decision aims to neutralise spreads on government bonds of selected Member States of the euro currency area which have emerged in the markets and which adversely affect the refinancing of these Member States (thus ECB, Monthly Bulletin September 2012, p. 7; ECB, Monthly Bulletin October 2012, pp. 7 and 8)..” (para. 65)
- Clearly misinterprets the statements of ECB, message not contained in the sources referred to – cited statements only state that there is a disturbance of the transmission mechanism

2. OMT Decision of BVerfG

2.4. OMT Decision of ECB as General Economic Policy?

- “In any case, according to explanations given by the *Bundesbank*, one cannot in practice divide interest rate spreads into a rational and an irrational part.” (para. 71)
- But what is the result of such finding? Interest of EMB in the issue of spreads irrelevant for monetary policy? Any action of ECB that lowers spreads outside its competence?
- “As for the European Central Bank claiming to safeguard the current composition of the euro currency area with the OMT Decision (cf. ECB Press Release of 26 July 2012), this is obviously not a task of monetary policy but one of economic policy, which remains a responsibility of the Member States.” (para. 72)

2. OMT Decision of BVerfG

2.4. OMT Decision of ECB as General Economic Policy?

- Again misinterpretation of the ECB statement – ECB President Draghi only spoke of a duty “to preserve the Euro”
- In the view of the Federal Constitutional Court, the objective mentioned by the European Central Bank invoked to justify the OMT Decision, namely to correct a disruption to the monetary policy transmission mechanism, can neither change the above-mentioned transgression of the European Central Bank’s mandate, nor the violation of the prohibition of monetary financing of the budget.” (para. 95)
- “The fact that the purchase of government bonds can, under certain conditions, help to support the monetary policy objectives of the European System of Central Banks does not turn the OMT Decision itself into an act of monetary policy (...) The (economic) accuracy or plausibility of the reasons for the OMT Decision are irrelevant in this respect.” (para. 96)

2. OMT Decision of BVerfG

2.5. OMT Decision of ECB and Political Conditionality

- Overlap with assistance programs under EFSF and ESM? “By tying the purchase of government bonds of selected Member States to full compliance with the requirements of the assistance programmes of the European Financial Stability Facility and the European Stability Mechanism and thus retaining its own conscientious examination, the European Central Bank makes the purchase of government bonds on the basis of the OMT Decision an instrument of economic policy. This is also confirmed by the fact that it plans to refrain from buying government bonds if the Member State concerned does not meet the economic policy” (para. 77).
- Constructive misunderstanding - tying needed in order not to erode the political conditionality of EFSF and ESM imposed by the community of MSs

2. OMT Decision of BVerfG

2.6. OMT Decision of ECB as Monetary Financing of the Budget?

- “If purchases of government bonds were admissible every time the monetary policy transmission mechanism is disrupted, it would amount to granting the European Central Bank the power to remedy any deterioration of the credit rating of a euro area Member State through the purchase of that state’s government bonds. This would suspend the prohibition of monetary financing of the budget.” (para. 97)
- Assumes a need for a justification for market operations with government bonds. But where does a prohibition of such operations come from?

2. OMT Decision of BVerfG

2.6. OMT Decision of ECB as Monetary Financing of the Budget?

- BVerfG argues with a “Prohibition of monetary financing of the Budget”: “Art. 123 TFEU and Art. 21.1. ESCB Statute forbid the purchase of government bonds “directly” from the emitting Member States, i.e. the purchase on the primary market. This prohibition is, however, not limited to this interdiction, but is an expression of a broader prohibition of monetary financing of the budget (cf. Borger, German Law Journal 2013, p. 113 <119, 134>; de Gregorio Merino, CMLR 2012, p. 1613 <1625, footnote 36, 1627>; Lenaerts/van Nuffel, European Union Law, 3rd ed. 2011, n. 11-037). Union law recognises the legal concept of bypassing as do the national legal systems. It is ultimately based on the principle of effectiveness (“effet utile”) and has repeatedly been alluded to in the Court of Justice’s jurisprudence (cf. most recently ECJ, Judgment of 20 June 2013 Case C-259/12, *Rodopi-M* 91, ECR 2013, p. I-0000, n. 41).” (para. 85).

2. OMT Decision of BVerfG

2.6. OMT Decision of ECB as Monetary Financing of the Budget?

- Art. 123 TFEU probably can be interpreted also to prohibit to circumvent the prohibition of direct financing of state budgets – but difficult to see how this could also comprise market operations with government bonds on secondary markets, if not used exceptionally as a means to finance state budgets
- Argumentation is sloppy: “It can be an (...) indication for a circumvention of the prohibition of monetary financing of the budget if government bonds are purchased on the secondary market to a considerable extent and shortly after their emission by the Eurosystem (market pricing).” (para. 92).
- Boundary line not that easy to draw – margin of appreciation needed for economic actors – otherwise “Anmaßung von Wissen” (Hayek) – Can law determine future monetary policy in its substance?

2. OMT Decision of the BVerfG

2.7. Proposed Restrictive Reading of OMT Decision of the ECB

“The Federal Constitutional Court believes that these concerns regarding the validity of the OMT Decision, based on the interpretation used here, could be met by an interpretation in conformity with Union law. This would require that the content of the OMT Decision, when comprehensively assessed and evaluated, essentially complies with the above-mentioned conditions. In the view of the Federal Constitutional Court, the OMT Decision might not be objectionable if it could, in the light of Art. 119 and Art. 127 et seq. TFEU, and Art. 17 et seq. of the ESCB Statute, be interpreted or limited in its validity in such a way that it would not undermine the conditionality of the assistance programmes of the European Financial Stability Facility and the European Stability Mechanism (...), and would only be of a supportive nature with regard to the economic policies in the Union (...). This requires, in light of Art. 123 TFEU, that the possibility of a debt cut must be excluded (...), that government bonds of selected Member States are not purchased up to unlimited amounts (...), and that interferences with price formation on the market are to be avoided where possible .” (paras. 99-100)

2. OMT Decision of the BVerfG

2.8. Implications of the Path taken by the BVerfG

What results from that?

- ECJ will not follow the line proposed by BVerfG
- If ECJ declares measures of the ECB to be compatible with TFEU, what will be the reaction of BVerfG? – „Dog that barks but never bites“? (Weiler)
- Would BVerfG dare to declare the constitutional complaint to be founded? – Bundestag obliged to hold a debate? – Does that change anything?

3. Cognitive Dissonance as a Driver of Crisis?

- Decision shows a strong cognitive bias that attempts to construe any usual activity of ECB as measures of economic policy outside the mandate of the ECB
- For doing so, the court systematically misinterprets the statements and policies of the ECB (as demonstrated above).
- Probably it is going too far if one assumes a wantonly manipulation of the ECB's position, better to assume a conflicting epistemology





3. Cognitive Dissonance as a Driver of Crisis?

- Epistemic bias – the court is seeing what it wants to see.
- For the long-term sustainability of a sound monetary policy in reaction to the crisis such cognitive dissonance might be fatal.
- It could force a decisive member state like Germany in a futile political conflict over basic issues of monetary policy





3. Cognitive Dissonance as a Driver of Crisis?

- What may be the reasons for such cognitive dissonance?
- Constructivist perspective on institutionalism teaches us that institutions have a strong power of cognitive framing
- BVerfG is epistemically caught in a world of sovereigntism , with an assumption that democratic legitimacy is possible only at national level (and thus the importance of national parliaments must be preserved).
- Construes the integration programme in rather narrow terms that allows national parliaments to „police“ any EU measure against
- *ultra vires acts*.





3. Cognitive Dissonance as a Driver of Crisis?

- Concept of *ultra vires* acts requires a strict limitation of competences transferred to the European level
- Forces the court to impose a very narrow and rigid reading of European treaties, otherwise *ultra vires* control impossible
- Denial of any margin of appreciation
- Such bias might be explained in terms of sociology of knowledge – Epistemic framing of national constitutional court judges relies on cognitive patterns that have been acquired in distinguished national careers – demonstrates a strong distrust against wide powers of European institutions



4. Conclusions

- ❖ The paper tried to demonstrate that not only colliding interests are a strong source of crisis
- ❖ Also phenomena of cognitive dissonance between key institutional actors may create or exacerbate a severe crisis, as a detailed analysis of the OMT decision of the BVerfG has demonstrated
- ❖ Behind such cognitive dissonance is a strongly diverging concept of the rule of law – Law as a detailed work plan for future political action – opposite understanding: law as a loose institutional framework that leaves decisive issues to be decided in the political process – Hayekian question of knowledge: should law determine future action in detail?
- ❖ There is a strong need to overcome such cognitive dissonance and to initiate a process of epistemic convergence, if the EU shall not be weakened in its potential of reacting to severe crisis.