



**MARTIN F. HELLWIG**

**Discussion Paper**  
**2024/7**

**NATIONAL CENTRAL  
BANKS AND THE  
GOVERNANCE OF THE  
EUROPEAN SYSTEM  
OF CENTRAL BANKS**

# National Central Banks and the Governance of the European System of Central Banks<sup>1</sup>

Martin F. Hellwig

## Abstract

The paper analyses the role of national central banks (NCBs) in the governance of the European System of Central Banks (ESCB). NCBs are the owners of the European Central Bank (ECB), and their governors dominate the ECB's Governing Council, but in monetary policy operations, NCBs are subordinated to the ECB. The dominance of NCB governors has materially affected Governing Council decisions on relations between NCBs and the ECB, allowing the NCBs to maintain some of their erstwhile glory, sometimes in contradiction to the primary law. Examples involve the monetary funding of investments declared as non-monetary, violations of Treaty provisions for the allocation of income from monetary policy operations, and accounting rules that obfuscate the boundary between ECB-subordinate and independent activities of NCBs. The net effect of these developments is to enlarge the domain of NCB activities.

*Key Words:* European Monetary Union, European System of Central Banks, Governance of the Eurosystem, ANFA, ELA, PSPP, Central-Bank Accounting and Balance Sheets

*JEL Classification:* E50, E58, F53.

---

<sup>1</sup> Paper prepared for the Bucerius Law School workshop "The European Union in Global Perspective – A Governance Model on Trial". I thank Christoph Engel, Christian Hellwig, Jörn Axel Kämmerer, and Hans-Bernd Schäfer for helpful advice. The usual disclaimer applies.

# 1. Loyalty Obligations of National Central Banks in the European System of Central Banks?

In the 2010s, Jens Weidmann, President of the Deutsche Bundesbank from 2011 to 2021, engaged in several public campaigns against the policies pursued by the European Central Bank (ECB). Thus, he publicly opposed the ECB's 2012 program for outright monetary transactions (OMT). In opposition to this program, the Bundesbank even submitted a brief to the German Constitutional Court.<sup>2</sup> In 2014 and 2015, he campaigned against the ECB's plans for massive open-market purchases of securities, the so-called Quantitative Easing (QE). He accepted the ECB's Public Sector Purchase Program only when the ECB's Governing Council decreed that each national central bank (NCB) should only buy debt securities of its own government and that there should be no sharing of profits and losses from these securities between the different NCBs. Given this proviso, Weidmann's Bundesbank supported the ECB in the legal proceedings about the PSPP before the German Constitutional Court. Nevertheless, Weidmann continued to campaign against the ECB's policy of keeping nominal interest rates near zero, or even below zero, for a long time. In 2019, an interview he gave to the tabloid *Bild* was published under the title "Deutschlands oberster Banker rechnet mit Graf Draghila ab" (Germany's top banker settles accounts with Count Draghila).<sup>3</sup>

I have long been wondering about these campaigns, their motivation and their legal basis. The campaigns did promote the popularity of the Bundesbank with important parts of the German public but to what purpose? A campaign within Germany was unlikely to affect the Executive Board or the Governing Council of the ECB.

As a National Central Bank, the Bundesbank is a member of the European System of Central Banks. The President of the Bundesbank is a member of the ECB's Governing Council. Membership of an organization usually comes with obligations of loyalty specified in written or unwritten rules. Members of an organization's decision-making bodies usually are free to object to policy proposals before these proposals are decided. Once a decision has been taken, however, it must be respected. One may therefore ask whether President Weidmann's campaigns were compatible with his obligations as a member of the ECB's Governing Council.

For a central bank, public communication is particularly important. For monetary policy to be effective, the central bank must be credible. Credibility may be undermined if central bank decisions appear to be controversial within the institution, and outsiders infer that decisions may be quickly reversed if majorities change.<sup>4</sup>

---

2 Deutsche Bundesbank (2012).

3 *Bild*, May 14, 2019. One may presume that the title was chosen by the newspaper rather than the interviewee. However, *Bild* had used the defamatory "Draghila" label before, and the President of the Deutsche Bundesbank could have conditioned his willingness to give an interview on the avoidance of any defamatory terms in the title.

4 Linta (2023) shows that market reactions to ECB decisions depended on whether the decisions were announced as having been taken unanimously, by consensus, or by a majority. In particular, the effectiveness of forward guidance was significantly lower when decisions were announced as having been taken by a majority.

In this respect, the Bundesbank itself seems to be quite strict. Deviations of board members from the line taken by the institution have almost never been observed in public.<sup>5</sup> In the past, it would have been inconceivable for say the president of the Landeszentralbank (LZB) Bayern (“central bank in the Land of Bavaria”) to campaign in public against the decisions and policies of the President and the Governing Council of the Bundesbank. Readers will object that, surely, the position of the Bundesbank or its president in relation to the ECB is different from the position of the LZB Bayern and its president, or any other board member, in relation to the Bundesbank. As a matter of political perception and self-perception, this is certainly true.<sup>6</sup> However, I am raising the question as a matter of law. In what sense does the law make the relation of the Bundesbank to the ECB different from the relation of the LZB Bayern to the Bundesbank?

This paper studies the relation between the NCBs and the ECB in the governance of the European System of Central Banks (ESCB). According to the primary law of the European Union, the ESCB is in charge of monetary policy. However, the ESCB itself is not an institution of its own, but a “system” that operates through its members, the NCBs and the ECB. Unlike the Landeszentralbanken in Germany, the NCBs are legally independent institutions. However, the primary law of the European Union calls for a subordination of NCBs under the ECB that is similar to the subordination of the Landeszentralbanken under the Bundesbank. The legal norms emphasize the “independence” of NCBs and the ECB but, for NCBs, this independence concerns their relations with institutions outside the ESCB, not their relations to the ECB.

However, the NCBs’ governors or presidents are members of the Governing Council of the ECB. As a group, they dominate this body, at least on matters of common interest. On such matters, therefore, the collective interest of the NCBs dominates political practice, even to the extent of overriding the primary law.

The paper is organized as follows. Section 2 gives brief overview of the primary law on ESCB governance. Section 3 explains the hybrid nature of NCBs as independent institutions under national law and members of the ESCB under European law. Section 4 discusses the implications of the hybrid role of NCB governors, as heads of their institutions as well as members of the ECB’s Governing Council, for the politics of the Governing Council. Section 5 shows how the politics of the ECB’s Governing Council have caused the ESCB to obfuscate the boundary between the monetary activities of NCBs and non-monetary activities that NCBs carry out on their responsibility and their own account. Section 6 considers the accounting rules of ESCB institutions and argues that these rules support the obfuscation of boundaries between monetary and non-monetary activities in ways that would be illegal in the private sector. Section 7 takes another look at President Weidmann’s campaigns.

---

5 An exception occurred in May 2019 when Board Member Joachim Wuermeling accused critics of Target balances of “populism”, saying that some of “their assertions are simply false”. See “Bundesbank wirft Target-Kritikern Populismus vor” (Bundesbank blames critics of Target system for populism), *Frankfurter Allgemeine Zeitung*, May 10, 2019. He did not make the assertion again in public. The official line of the Bundesbank has always been that, yes, the critics were right about Target balances posing a risk, but, no, the risks were not serious unless a member state were to leave the monetary union. I discuss the Target system in Section 6 below.

6 Many Bavarians would disagree.

The overall message will be that the hybrid nature of NCBs creates conflicts of interest that pose risks for the persistence of the monetary union. NCB governors are conflicted between their European and their national responsibilities and interests. Their national allegiances create centrifugal tendencies within the Governing Council, with little respect for the primary law of the European Union.

## **2. National Central Banks and the ECB in the Primary Law of the European Union**

I first review the primary law for the governance of the European System of Central Banks (ESCB) and the ECB. The primary law is contained in the text of the Treaty on the Functioning of the European Union ("Treaty") and in the Statute of the ESCB and the ECB ("Statute"), which is appended to the Treaty as Protocol No. 4 and has the same legal status as the text of the Treaty. Most relevant provisions in the text of the Treaty are reiterated in the Statute. For simplicity, therefore, I only refer to the latter.

In the Statute, the national central banks make five appearances:

- First, the NCBs jointly own the ECB (Art. 28), with shares determined by a specified key (Art. 29).
- Second, together with the members of the Executive Board of the ECB, i.e., the President, the Vice-President and four other members, the governors (presidents) of the NCBs make up the Governing Council of the ECB (Art. 10).
- Third, in all matters of monetary policy, NCBs must follow the guidelines and instructions of the ECB, which are set by the Governing Council and the Executive Board (Arts. 12.1 and 14.3). The Governing Council is empowered to ensure compliance with these guidelines and instructions.
- Fourth, NCBs "may perform functions other than those specified in this Statute unless the Governing Council finds, by a majority of two thirds of the votes cast, that these interfere with the objectives and tasks of the ESCB." In performing such functions, an NCB acts "on its own responsibility and liability" (Art. 14.4).
- Fifth, the aggregate of "monetary incomes" of the NCBs is distributed among the NCBs according to their paid up shares in the capital of the ECB (Art. 32.1). So is the part of the ECB's profit that is not retained in order to augment the ECB's general reserve (Art. 33). "Monetary incomes" are those incomes that accrue to NCBs in the performance of the ESCB's monetary policy function, net of any interest paid on deposits that commercial banks hold with central banks (Arts. 32.2 and 32.4).

Several aspects of these rules are noteworthy. First, although the NCBs are the owners of the ECB's equity, as institutions, they have no explicit role in the ECB's governance. Their governors

are members of the Governing Council but this is a membership *ad personam*, not a membership in representation of an NCB as a shareholder of the ECB. If a governor is unable to attend a meeting and vote in person, he cannot delegate the vote to an alternate who might represent this NCB's interests.<sup>7</sup> Such delegation is only allowed for decisions on matters pertaining to the distribution of shares in the ECB or the allocation of income between the national central banks that make up the Eurosystem.<sup>8 9</sup>

Second, in all matters of monetary policy, the NCBs are subordinated to the ECB – just as, in the old days, the LZB Bayern was subordinated to the Bundesbank. The NCBs play a role in the implementation of monetary policy, but in this role they are bound by the decisions of the the Governing Council and the Executive Board of the ECB. The incomes generated in the implementation of monetary policy are not attributed to the NCBs where they are generated but are shared between all NCBs in proportion to their shares in the ECB's paid-in equity.

Third, each NCB can independently engage in operations unrelated to monetary policy, subject only to a possible veto by a qualified majority of the Governing Council. Nonmonetary operations involve nonmonetary liabilities and/or nonmonetary assets. The classification of liabilities and assets as "monetary" or "nonmonetary" is subject to a decision of the Governing Council. Monetary liabilities include bank notes in circulation and liabilities from deposits of credit institutions. An example of nonmonetary liabilities would be the liabilities of a pension system that an NCB operates for its employees. Assets that are earmarked to these nonmonetary liabilities, such as the assets of the pension system, are also treated as nonmonetary.

### 3. The Hybrid Nature of NCBs

The *ad personam* membership of NCB governors in the Governing Council of the ECB can be interpreted as an attempt to have the NCBs participate in ECB decision making without creating a federal structure that gives the NCBs as institutions a say in ECB governance. As members of the Governing Council, NCB governors must not "seek or take instructions from Community institutions or bodies, bodies, from any government of a Member State or from any other body" (Art. 7 of the Statute). This provision of the statute precludes any attempt of any outside institution, even of a decision making body of an NCB, to determine or at least constrain the NCB governor's vote in the Governing Council. The governor's independence is enhanced by the fact that the minutes of the Governing Council do not provide information about individual votes.

---

7 See Art. 10.2 of the Statute. The Statute does permit the appointment of an alternate if a member of the Governing Council "is prevented from voting for a prolonged period".

8 A note on terminology: As defined in the Statute, the ESCB comprises *all* NCBs in the EU and the ECB. Distinctions between NCBs of member states that have and that have not joined the European Monetary Union (EMU) appear in the different articles. Subsequently, as it became clear that some EU members would stay outside EMU for the foreseeable future, the term *Eurosystem* was introduced to designate the set of NCBs in the EMU and the ECB. See the ECB's Annual Report 1998, p. 120.

9 See Art. 10.3 of the Statute. In such decisions, the members of the Executive Board have no votes, and the votes of the governors of national central banks are weighted by the shares of these central banks in the subscribed capital of the ECB.

On a previous occasion when I presented this view,<sup>10</sup> several German authors commented that the ESCB should in fact be interpreted as a federal system in which the NCBs are independent institutions under national law that cooperate with each other and with the ECB in determining and implementing monetary policy for the euro area.<sup>11</sup> However, while it is true that the NCBs are legally independent institutions, they do not participate in ECB decision making as institutions, and they are not entitled to act independently in matters of monetary policy.<sup>12</sup> The Statute of the ESCB and the ECB, i.e. the primary law of the European Union, makes them subservient to the ECB.

The NCBs are in fact hybrids. On the one hand, they are independent institutions under national law. On the other hand, in matters of monetary policy, they “are an integral part of the ESCB” (Art. 14.3 of the Statute), with duties and privileges determined by European law. As a member of the ESCB, the Deutsche Bundesbank is not only a German institution but also a European institution; as a member of the ECB’s Governing Council, its president is not only a German official but also a European official.<sup>13</sup> In the implementation of monetary policy, the Bundesbank is obliged to obey the instructions it receives from the ECB, and its president is responsible for the Bundesbank’s complying with this obligation.<sup>14</sup>

The hybrid nature of NCBs played a key role in two cases before the Court of Justice of the European Union (CJEU), *Rimšēvičs and ECB v Latvia*, C-202/18 and C-238/18, EU:C:2019:139, and *Commission v Republic of Slovenia*, C-316/19, EU:C:2020:1030. In these cases, the Court asserted that “the ESCB represents a novel legal construct in EU law which brings together national institutions, namely the national central banks, and an EU institution, namely the ECB, ... and within which a different structure and a less marked distinction between the EU legal order and national legal orders prevails... . In this highly integrated system intended by the authors of the Treaties for the purposes of the ESCB, the national central banks and their governors have a hybrid status, inasmuch as, although they constitute national authorities, they are authorities acting under the ESCB which ... is constituted by those national central banks and the ECB.”<sup>15</sup>

Given this assessment, the Court ruled that, in their activities as members of the ESCB, the NCBs share the privileges that the Treaty provides to the ECB. Prosecutorial proceedings in

---

10 Hellwig (2018).

11 Homburg (2019), 100; Spahn (2019), 105; Sinn (2019), 174..

12 To appreciate the point, it is instructive to consider the history of the Federal Reserve. From the Federal Reserve’s founding in 1913 until 1935, the regional Federal Reserve Banks enjoyed significant autonomy and engaged in open-market operations on their own initiative. This autonomy was ended by the Banking Act of 1935. See Meltzer (2003), Conti-Brown (2016). The Eurosystem never had anything like the pre-1935 Federal Reserve System.

13 For a legal discussion of this issue, see Siekmann (2006), 29, and Siekmann (2018), Rn. 48.

14 Spahn (2019), 105, and Sinn (2019), 183, try to refute this view by means of examples where NCBs act independently of the ECB. All their examples, however, involve activities that do not pertain to monetary policy, so under Art. 14.4 of the Statute, the NCBs are allowed to engage in these activities “on their own responsibility and liability”.

15 Paragraph 83 of *Commission v Republic of Slovenia*, C-316/19. The first sentence is almost a verbatim quote Paragraph 69 of *Rimšēvičs and ECB v Latvia*, C-202/18 and C-238/18. The second sentence adapts Paragraph 70 of *Rimšēvičs and ECB v Latvia*, C-202/18 and C-238/18. The latter paragraph refers to “the dual professional role of the governor of a national central bank, who is certainly a national authority but who acts within the framework of the ESCB and sits, where he is the governor of a national central bank of a Member State whose currency is the euro, on the main decision-making body of the ECB.”

other matters against an NCB or its governor under national law must therefore involve safeguards against infringements of these privileges.<sup>16</sup> In *Rimšēvičs and ECB v Latvia*, the CJEU even took the unusual step of not merely asserting an infringement of the Treaty but actually voiding the Latvian decision that temporarily prohibited Mr Rimšēvičs from performing his duties as a member of the Governing Council of the ESCB. To justify this deviation from the general principle that national law and institutions and European law and institutions form two separate spheres, the CJEU argued grounds that the Latvian NCB was an institution under European law as well as national law.

#### 4. The Politics of the Governing Council

The *ad personam* membership of NCB governors in the Governing Council does not prevent these governors from seeing themselves as representatives of their institutions and of their countries and from acting accordingly. In their daily work, they rely on people in their institutions and they interact with the political and financial communities of their countries. If they detached themselves from the interests of their institutions and of their countries, their daily work would be fraught with frictions.<sup>17</sup> In fact, the NCB governors are likely to take pride in

---

16 In *Rimšēvičs and ECB v Latvia*, C-202/18 and C-238/18, Mr Rimšēvičs and the ECB contested a decision of the Latvian corruption office that temporarily prohibited Mr Rimšēvičs from performing his duties as Governor of the Central Bank of Latvia because this decision violated the provision of Art. 14.2 of Statute, which requires an involvement of the CJEU in such decisions. In its judgment, the CJEU emphasized that the Latvian decision had not been based on any judgment of the merits of the accusations against the governor and that the material presented in the course of the proceedings was not sufficient for the Court to form its own judgment of the merits as required by Art. 14.2 of the Statute. In *Commission v Republic of Slovenia*, C-316-19, the Court confirmed the Commission's assessment that the Slovenian authorities had violated the Treaty when they conducted a search of the premises of the Central Bank of Slovenia and impounded the governor's computer. According to Protocol No. 7 to the Treaty, which deals with privileges and immunities of EU institutions, the premises and buildings, as well as the archives "of the Union are inviolable"; according to Art. 39 of the Statute, "the ECB" shares in such privileges and immunities laid out in Protocol No. 7 "as are necessary for the performance of its tasks." The Court ruled that "the ECB" in this context comprises the NCBs when acting as members of the ESCB and that "the archives of the ECB" comprises all NCB files that relate to such actions. The Slovenian authorities were concerned with a potential abuse of power in connection with the restructuring of Slovenian banks that had taken place in 2013, at the time a non-ESCB activity, which belonged to the national domain. The Court did not contest their right to carry out this investigation but ruled that they should have coordinated their actions with the ECB so as to safeguard the inviolability of ECB archives.

17 The case *Commission v Republic of Slovenia*, C-316-19, that was mentioned above provides an admittedly extreme example. The disputes about bail-ins of equity and subordinate debt after the 2013/2014 restructuring of Slovenian banks also caused the Slovenian parliament to pass legislation creating a wholesale and unconditional obligation of the central bank to indemnify investors for any damages from bail-ins. In 2022, the Court of Justice of the European Union (CJEU) ruled that this legislation also constitutes a Treaty infringement. The Court argued that, in the absence of unlawful decisions by the central bank, provision for such indemnification was a political act of the authorities, so central bank funding would violate the Treaty's prohibition of monetary financing of the state. The Court also argued that the amounts involved might require the central bank to deplete its reserves and to borrow, which might endanger the central bank's independence (Case C-45/21, <https://curia.europa.eu/juris/document/document.jsf?jsessionid=B315B16F6C8A95FA57B08AB398F3102A?text=&docid=265343&pageIndex=0&doclang=en&mode=lst&dir=&occ=first&part=1&cid=797856>). Given this ruling by the CJEU, the Slovenian Constitutional Court has recently abrogated the law; see Sebastijan Macek, "Slovenian court throws out recourse for bailed-in bank investors", *euractiv*, March 8, 2023 <https://www.euractiv.com/section/politics/news/slovenian-court-throws-out-recourse-for-bailed-in-bank-investors/>. The dispute concerned the central bank's supervisory role, rather than monetary policy, but the contested legislation was an attempt of the political authorities to capture central-bank resources in order to indemnify investors with political influence.

bringing their institutions' interests and views to bear on decision making at the ECB, especially if these institutions have proud traditions to look back on.

By the weight of their number, the NCB governors dominate the Governing Council. Therefore, their attitudes may inject a certain centrifugal tendency into the governance and decision making of the Eurosystem, counteracting the centralization stipulated in the Treaty and the Statute.

In matters of monetary policy, this centrifugal tendency is counteracted by the strong position that the Statute gives to the President and the Executive Board in the Governing Council of the ECB.<sup>18</sup> The President chairs the meetings of the Governing Council, and the Executive Board has responsibility for preparing these meetings (Arts. 12.2 and 12.3). Therefore, they have significant power over the agenda of the Governing Council. They also benefit from a great information advantage in matters concerning the euro area as a whole. Whereas NCB governors may have better information about their own countries, the President and Executive Board are in a better position to assess the overall situation in the euro area. To the extent that attitudes in different countries differ, the President and Executive Board may also be in a position to manage the resulting conflicts between NCB governors.

These advantages of the President and the Executive Board in Governing-Council proceedings, may however not matter much in decisions that concern the status of NCBs relative to the ECB. Such decisions require a different kind of preparation from decisions on monetary policy. Moreover, in such decisions, NCB governors are likely to have similar interests so they can easily use their numerical superiority to make these interests prevail. In particular, one must presume that NCB governors have an interest in maximizing the significance of their own institutions and to reduce the downgrading implied by their being subjected to the guidelines and instructions of the ECB.

Thus, from the very beginning, the ECB has established a principle of decentralization, leaving as much of the implementation of monetary policy as possible to the NCBs.<sup>19</sup> For example, credit institutions have accounts with their NCBs, rather than the ECB. Yet, Art. 17 of the Statute empowers the ECB as well as the NCBs to "open accounts for credit institutions ... and other market participants". The ECB has not made use of this power. Similarly, Art. 19.1 of the Statute empowers the ECB to impose minimum requirements for credit institutions' reserves in accounts with the ECB or the NCBs, but the ECB Regulation on the application of minimum reserves only allows for reserves in accounts with the NCBs.<sup>20</sup>

---

18 The Executive Board consists of the President, the Vice-President, and four other members. According to Art. 11.2 of the Statute, its members are appointed by "common accord of the governments of the Member States at the level of the Heads of State or Government, on a recommendation from the Council after it has consulted the European Parliament and the Governing Council."

19 See, for example, the ECB's Annual Reports 1998, 66, and 1999, 48 and 135.

20 See Art. 6 of Regulation (EC) no 2818/98 of the European Central Bank of 1 December 1998 on the application of minimum reserves (ECB/1998/15), *Official Journal of the European Communities* L356/1, 30.12.98. The introductory citations contain the text: "Whereas Article 19.1 of the Statute states that, if the European Central Bank (ECB) decides to require credit institutions established in participating Member States to hold minimum reserves, they are to be held on accounts with the ECB and participating national central banks (participating NCBs); whereas it is considered appropriate that such reserves should be held on accounts with participating NCB." Council Regulation (EC) 2531/98 concerning the application of minimum reserves by the European Central Bank of 23 November 1998, *Official Journal of the European Communities* L318/1,

In a debate about the significance of intra-ESCB claims and liabilities, I once heard a former member of the ECB's Executive Board argue that these positions are large only because the NCBs had early on decided that the ECB would not offer deposit accounts to credit institutions, and the NCBs would be the only ones to offer such accounts. According to this former member of the ECB's Executive Board, this decision was motivated by the desire of NCBs to maintain their position of power over the credit institutions of their countries. Perhaps they also saw the monopoly over relations to their domestic credit institutions as strengthening their own positions relative to the ECB.<sup>21</sup>

In the German debate about the relation between NCBs and the ECB that I mentioned above, some authors have maintained that the NCBs' monopoly over relations with "their" credit institutions supports the view that the ESCB has a federal structure in which the NCBs are autonomous partners. For example, Sinn has claimed that this arrangement reflects a conscious decision of "the Member States and the ECB Governing Council" to prevent the transfer of assets to the ECB.<sup>22</sup> The claim is flawed because the Member States did not take any decision that would have limited the ECB's ability to offer accounts to credit institutions. To be sure, the primary legislation does limit asset transfers from NCBs to the ECB to the NCBs' contributions to the ECB's equity (Art. 28 of the Statute) and (at most) € 50 billion in foreign reserve assets (Art. 30 of the Statute), but this has nothing to do with the right of the ECB to offer accounts to credit institutions. Art. 17 of the Statute explicitly allows the ECB as well as the NCBs to offer accounts to credit institutions. At the level of secondary legislation, the Council Regulation on minimum reserves, which also reflects the wishes of the member states, also presumes that credit institutions may have accounts with the ECB as well as the NCBs. The decision to exclude the ECB from offering deposit accounts to credit institutions was a piece of secondary legislation of the Governing Council. The subordination of secondary law to primary law precludes any interpretation of this decision in terms of principles that would contradict the primary law.

- 
- 27.11.1998, which the ECB Regulation also cites, also refers to reserves in accounts "with the ECB or the national central banks" (Art. 7). The restriction to accounts in NCBs is of the ECB's own making.
- 21 Concerns about power over national credit institutions also played a role in the strict separation of bank supervision from the ESCB that prevailed before the introduction of Banking Union. In a 2014 paper, I explained that power over bank supervision gave member states an opportunity to procrastinate on the recognition and resolution of problems in banks. Such procrastination would maintain weak banks as a basis for obtaining indirect access to the ECB's printing press, as weak banks might use ECB loans, e.g., under the Long Term Refinancing Operation (LTRO) of 2011/12, to invest in their own governments' debts; see ASC (2012), Hellwig (2014b). On the use of LTRO funds by weak credit institutions, see Acharya and Steffen (2015). The 2012 decision of the European Council to create a Banking Union, in particular the Single Supervisory Mechanism (SSM) resulted from a strange deal in which Spain and other countries were given a prospect of ESM financing of bank restructuring in return for agreeing to have supervision moved to the European level. The German participants in this negotiation were keen to impose more discipline on other member states. Subsequently they were surprised by strong negative reactions from some segments of the German banking sector.
- 22 Sinn (2019). Homburg (2019) treats contractual relations between NCBs and credit institutions in the NCBs' countries as evidence of NCB autonomy. He likens the status of NCBs in the ESCB to the status of the German Customs Administrations, which acts under German law even as it implements internationally negotiated tariff agreements. The analogy is inappropriate, however, because, in contrast to Art. 14.3 of the Statute, which obliges NCBs to follow instructions from the ECB, the German Customs Administration is not subject to instructions from the European Commission. A more appropriate analogy would be DB Capital Management Inc. in Wilmington, Delaware, a subsidiary of Deutsche Bank that is legally independent but operates under instructions from Deutsche Bank headquarters.

The interpretation quoted above, that this decision of the Governing Council was mainly a matter of NCB governors protecting their own turf, seems plausible. This interpretation suggests that there is a tension between the two roles of NCB governors, as members of the Governing Council, who should be devoted to the ESCB, and as heads of their own central banks, whose interests may not be aligned with those of the ESCB.

## **5. Nonmonetary Activities of NCBs**

The desire to minimize change relative to the previous regime is also apparent in the handling of “functions other than those specified in this Statute” that NCBs carry out “on their own responsibility and liability” under Art. 14.4 of the Statute. An interesting example is the maintenance of arrangements for the CFA-Franc zone, mainly in Africa. This currency union between France and several of its former colonies was maintained even after the French franc was replaced by the euro. Under the treaties establishing the different parts of the CFA-franc zone, the central banks of that zone are obliged to hold large parts of their foreign-exchange reserves with the French government. Acting as fiscal agent for the French government, the Banque de France offers deposit facilities in which the central banks of the CFA-Franc zone can hold these reserves.<sup>23</sup> These deposits, as well as the assets that are held as counterparts, are treated as nonmonetary activities of the Banque de France.

### **5.1 Financial Assets funded by Monetary Liabilities**

Whereas the activities associated with the reserves of the CFA-Franc zone, or the activities associated with NCB pension funds seem to be self-funding, some of the NCBs’ nonmonetary activities are not. Over the years, many NCBs have held substantial amounts of “financial” assets that were funded by monetary liabilities even they were said to be unrelated to monetary policy. For reasons that will be explained below, the practice has receded, but some NCBs still follow it.

Some of these asset holdings have historical origins. For example, when the ESCB was founded, only a fraction of the NCBs’ reserves of gold and foreign-currency reserves was transferred to the ECB (Art. 30 of the Statute); the remainder, including the NCBs’ shares in the International Monetary Fund, continue to be held by the NCBs.

Further, whereas the ECB decided that the common monetary policy should focus on managing the liquidity available to the banking system, NCBs that had previously relied on open market operations owned large stocks of securities, mainly government debt. To avoid upsetting markets by suddenly liquidating these holdings, these securities were designated as “financial” rather than monetary, and the NCBs in question were allowed to hold on to them even though

---

23 The Banque Centrale des États de l’Afrique de l’Ouest in Dakar, Senegal, is responsible for the CFA-Franc in eight West-African countries, the Banque des États de l’Afrique Centrale in Yaoundé, Cameroon, for the CFA-Franc in six Central-African countries.

they were effectively funded by monetary liabilities. Remarkably, this permission was not rescinded later, when the original holdings matured.

A third category involves emergency liquidity assistance (ELA) to credit institutions whose assets do not meet the Eurosystem's standards for collateral. An NCB is free to provide such assistance, with lower standards for collateral, but it does so under Art. 14.4 of the Statute, "on its own responsibility and liability". Thus, the risk of losses from such lending is borne by the NCB rather than the Eurosystem as a whole.<sup>24</sup>

The treatment of ELA as a function "other than those specified in this Statute" is problematic. Acting as a lender of last resort is a classic task of a central bank, usually justified by concerns for the stability of the payment system, a task of the ESCB that is specified in the Statute (Arts. 3.1 and 22). Moreover, the central bank money that a credit institution obtains through ELA does augment the aggregate amount of central bank money in the system.<sup>25</sup>

The arrangements for ELA go back to decisions taken in the early 2000s just after the monetary union had been founded. At the time, the Economic and Financial Committee of the European Union recommended, and many memoranda of understanding codified, the idea that, in a crisis, member state governments should be in charge of dealing with solvency problems, national central banks in charge of liquidity problems of individual banks, and the ECB in charge of overall market liquidity problems.<sup>26</sup> This division of responsibilities reflected the desire of member state governments and of NCBs to keep control over "their" banks. At the time, I also had the impression that the ECB was wary of moral hazard on the side of member state institutions, in particular with respect to procrastination in the recognition and resolution of problems of weak banks.<sup>27</sup> Subsequently, the financial crisis of 2007-2008 and the euro crisis have confirmed apprehensions that the arrangement was not viable.<sup>28</sup> In 2014, responsibility for bank supervision and bank resolution was shifted from the national to the European level, which much weakened the moral-hazard concerns. Even so, ELA remains an NCB responsibility, despite its significance in the context of tasks that the Statute assigns to the ESCB.<sup>29</sup>

---

24 Fuest and Sinn (2018) assert that the immunization of other NCBs against risks from one NCB's activities under Art. 14.4, such as ELA, is imperfect if such operations result in monetary assets of that NCB falling short of its monetary liabilities, as may happen because the ELA loans are counted as non-monetary assets. In such a constellation, the difference results in a fictitious asset of that NCB, which for purposes of Art. 32 of the Statute is deemed to earn interest at the main refinancing rate. If the amount of this interest fell short of the NCB's share of monetary income under Art. 32 of the Statute, the NCB would have a net liability and there might be a risk of default on this liability. The argument is flawed, however, because it omits the deductions from monetary income that an NCB can take for the interest dues it incurs on monetary liabilities. If the NCB provides ELA to a credit institution, the credit institution uses the funds to satisfy its customers, and the customers transfer the money abroad, the balance sheet counterpart to the fictitious asset replacing the ELA loan will be a Target liability. The interest imputed to this Target liability is the main refinancing rate, exactly equal to the interest imputed to the fictitious asset replacing the ELA loan. Contrary to Fuest and Sinn's claim, the ELA loan does not create any net obligation of an NCB to the Eurosystem.

25 If the credit institution uses this money to pay its customers, the expansion may be unimportant in that the public's holdings of cash and bank deposits do not change. Even so, the expansion hardly falls outside the purview of the ESCB.

26 Economic and Financial Committee (2001).

27 For an evaluation of ELA, see Cadamuro and Papadia (2021), as well as n. 21 above.

28 Even before the financial crisis and the euro crisis, I had warned of this non-viability. See Hellwig (2007).

29 In 2018, ECB President Draghi argued in public that responsibility for ELA should be shifted to the ECB, without success. See: <https://www.ecb.europa.eu/press/pressconf/2018/html/ecb.is180308.en.html>.

## 5.2 Legal Concerns

The arrangements for monetary financing of financial assets are problematic, on legal grounds and on substantive grounds. The category of “net financial” assets, i.e., non-monetary assets that are funded by monetary liabilities, has no basis in the Treaty or the Statute. Art. 32.2 of the Statute defines “each national central bank’s monetary income” as “its annual income derived from its assets held against notes in circulation and deposit liabilities to credit institutions” and adds: “These assets shall be earmarked by national central banks in accordance with guidelines to be established by the Governing Council.” This rule states clearly that the income on assets funded by monetary liabilities should be shared between the NCBs rather than appropriated by the NCB holding the asset. Such sharing, however, is incompatible with the proviso of Art. 14.4 of the Statute whereby activities that an NCB undertakes “on its own responsibility” are also undertaken “on its own ... liability”.

Instead of concluding that asset holdings under Art. 14.4 of the Statute must not be funded by monetary liabilities, the Governing Council has adopted a rule to the effect that, if the values of monetary assets and monetary liabilities differ, the difference is treated as a fictitious asset or liability that earns or pays interest at the “reference rate” of interest.<sup>30</sup> The reference rate is the rate the Eurosystem charges in its main refinancing operations for banks. If an NCB funds its holdings of financial assets by monetary liabilities, then, in the calculation of the NCB’s monetary income, the actual income on its “net financial assets” is replaced by the putative income on a fictitious asset that earns interest at the main refinancing rate. Any difference between the actual income on net financial assets and the putative income on the fictitious asset accrues to the NCB and is not shared within the Eurosystem.

This rule respects the “on its own ... liability” condition for independent activities of NCBs under Art. 14.4 of the Statute, but it violates the Statute’s definition of “monetary income” under Art. 32.2 of the Statute. To be sure, the Statute leaves the details of the “earmarking” of assets to liabilities to guidelines determined by the Governing Council. However, such guidelines must respect the primary law. It takes a stretch of the imagination to replace the Statute’s reference to actual assets by the fictitious asset in the Governing Council’s approach.<sup>31</sup>

The Statute does allow for the possibility that, initially, “the balance sheet structures of the national central banks do not ... permit the application of Article 32.2”. Art. 32.3 empowers the Governing Council to “decide that, by way of derogation from Article 32.2, monetary income shall be measured according to an alternative method for a period of not more than five years.” This legal norm did justify the initial treatment of certain NCB securities holdings as financial assets funded by monetary liabilities, but it does not justify the continuation of such a treatment beyond the specified transition period of five years.

---

30 See Art. 3(2) of Decision (EU) 2016/2248 of the European Central Bank of 3 November 2016 on the allocation of monetary income of the national central banks of Member States whose currency is the euro (recast) (ECB/2016/36).

31 A prominent legal scholar once told me that only a non-lawyer can take the wording of legal norms as seriously as I do. As a citizen who is neither a lawyer nor an office holder, I would however submit that the freedom that people in power and lawyers take with legal norms is one reason for the rising dissatisfaction of large parts of the population with our democracies.

The ECB argues that the arrangements for financial assets funded by monetary liabilities are needed because, as national institutions, NCBs have obligations under national legislation. Therefore, they hold “financial assets which are related to national tasks of the national central banks. Such financial assets of national central banks include, for example, the counterpart to their capital and accounting reserves or other specific liabilities, their foreign reserves and employee pension funds or assets held for general investment purposes. ... When the monetary union was founded, governments decided to mutualise only those central bank functions and tasks that are necessary to conduct a single monetary policy for the whole euro area. At the same time, they decided to keep national central banks as independent institutions that can continue to perform national tasks provided that these tasks do not interfere with the single monetary policy.”<sup>32</sup>

These arguments only explain why NCBs might hold financial assets at all. They do not explain why NCBs should fund such assets with monetary liabilities. Such funding seems contrary to Art. 32 of the Statute.

For “assets held for general investment purposes”, even the claim that these assets are “related to national tasks of the national banks” is unconvincing. For assets related to specific tasks codified in national legal norms, the imposition of such tasks might even violate the prohibition of monetary financing of the state under Art. 123 TFEU. This issue was raised in a 2022 preliminary ruling of the CJEU following a request from the Slovenian Constitutional Court.<sup>33</sup> The ruling concerned an obligation that the Slovenian parliament had imposed on the Slovenian central bank, which was to compensate bailed-in creditors of credit institutions in bank resolution.<sup>34</sup> The CJEU ruled that the decision to compensate bailed-in creditors belonged to the sphere of the national government and therefore imposing the financial burden of this decision on the central bank would constitute a violation of Art. 123 TFEU.<sup>35</sup> The obligations invoked by the ECB to justify NCB holdings of “financial” assets are different from the obligation at issue in the Slovenian case, but the logic that obligations imposed on NCBs by their governments and parliaments must not violate Art. 123 TFEU would seem to apply to all tasks and obligations that political authorities might impose on NCBs.

The ECB emphasizes that NCB activities under Art. 14.4 of the Statute are for the NCBs to decide. There are two caveats however. First, such activities must concern “functions other than those specified in this Statute”. It is not clear why this condition would hold for NCB open-market purchases and holdings of securities, especially at a time when the ESCB itself is relying on such operations for its monetary policy. Art. 18 of the Statute names purchases and sales of securities in open markets as one of the main instruments of monetary policy.

---

32 See [https://www.ecb.europa.eu/ecb/educational/explainers/tell-me-more/html/anfa\\_qa.en.html](https://www.ecb.europa.eu/ecb/educational/explainers/tell-me-more/html/anfa_qa.en.html) . For a more elaborate explanation, see Deutsche Bundesbank (2016).

33 Case C-45/21-Banka Slovenije, *l.c.* (n.17).

34 The bank failures that motivated this legislation had occurred in late 2013, before the European Bank Recovery and Resolution Directive (BRRD) had come into force.

35 The Court also ruled that the obligation might endanger the central bank’s independence and violate Art. 130 of the Treaty, if the amounts needed were very large so that the central bank would be forced to raise new equity.

Second, such activities must not “interfere with the objectives and tasks of the ESCB”. The ESCB has interpreted this condition in a very narrow sense as a requirement that the liquidity of the banking system that is created by NCB acquisitions of financial assets must not affect the ESCB’s ability to determine the liquidity of the banking system as it wishes for the policy it pursues. This narrow interpretation is problematic.

### 5.3 Agreement on Net Financial Assets (ANFA)

To ensure that NCB acquisitions of financial assets must not affect the ESCB’s ability to determine the liquidity of the banking system as it wishes, in 2003, the members of the Eurosystem concluded an *Agreement on Net Financial Assets* (ANFA), which limits funding of financial assets of NCBs by monetary liabilities.<sup>36</sup> Under this agreement, for each year, there is a limit on the average holdings of net financial assets. The limit is set for the aggregate of the Eurosystem and allocated to NCBs in proportion to their shares in the ECB’s equity.<sup>37</sup> The limit for the aggregate is calibrated to match the minimum level of liquidity that the ESCB might wish to provide to the banking system.<sup>38</sup> The calibration is carried out triennially, but can be performed more often if some party to the agreement asks for this.

This agreement is problematic. Conceptually, calibrating the limit for aggregate net financial assets to the level of liquidity available to the banking system under the ESCB’s chosen policy amounts to a negation of Art. 32 of the Statute, according to which incomes obtained from assets held against notes in circulation and deposit liabilities to credit institutions.

The calibration used to determine the limit also gives the lie to the argument that toleration of NCB securities holdings as independent activities under Art. 14.4 of the Statute was needed to accommodate the large securities holdings of NCBs that had previously used open market operations as the main policy instrument. Even disregarding the fact that the five-year transition period that Art. 32.3 of the Statute provides for such a grandfathering rule is long past, the limit on aggregate net financial assets that the calibration provides is actually growing over time. The agreement actually allows NCBs to *expand* the securities they hold under Art. 14.4 of the Statute, “on their own responsibility and liability”.

The view that compatibility of such holdings with “the objectives and tasks of the ESCB” is only a matter of whether aggregate net financial assets stay below the ESCB’s desired level of liquidity of the banking system is also problematic. Monetary policy involves more than just the liquidity available to the banking system. Securities purchases and holdings of central banks also affect market conditions, particularly interest rates and interest spreads. Even if the Governing Council decides to implement its monetary policy by managing the liquidity available to

---

36 For the most recent version of this agreement, dated 19 December 2022, see <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=IMMC:AGR/2022/12191>

37 If an NCB does not exhaust its limit, the difference is available for use by other NCBs.

38 ELA loans to credit institutions do not count towards the limit. Presumably, ELA lending is interpreted as a measure that neutralizes credit institutions’ losses of banknotes and reserves in a run. For the NCB in question, this interpretation is correct. It is also correct for the Eurosystem as a whole if the run involves cash withdrawals. It is not correct for the Eurosystem as a whole if the run involves transfers to another bank, in the same country or in another country in the euro area, and the transfer raises the liquidity available to the other bank.

banks, securities markets remain relevant for the monetary system and for monetary policy. The ECB itself implicitly acknowledged this fact when it turned to open market operations in a big way in 2015. Even then, however, it maintained the regime described above.

#### 5.4 The Actual Use of ANFA

As of this writing, the matter of financial assets funded by monetary liabilities may seem to be moot. In 2022, net financial asset holdings of the Eurosystem as a whole amounted to *minus* €730 billion on average over the year, i.e., monetary liabilities *exceeded* financial assets by €730 billion.<sup>39</sup> In the past, however, net financial asset holdings were positive and large, and they might become positive and large again if circumstances change. The current numbers probably reflect the fact that the Eurosystem's massive open market purchases since 2015 have reduced the desires of NCBs to hold financial assets.

Initially, in 2002, the Eurosystem's holdings of net financial assets amounted to €267 billion. Subsequently, the holdings increased year after year, reaching €400 billion in 2007 and €600 billion, the maximum until now, in 2011.<sup>40</sup> The faster increase in 2007-2011 can probably be ascribed to the financial turmoil of that period, when several NCBs provided emergency liquidity assistance to banks in difficulties and others, most prominently the Banca d'Italia, supported markets by purchasing significant amounts of securities as financial assets. After 2011, the Eurosystem's holdings of net financial assets first declined a bit, in 2012 and 2013, then rose again, in 2014 and 2015, and since then has declined year after year, becoming negative in 2018.

In the German discussion about the governance and policies of the ESCB, several participants discussed NCB purchases of financial assets as a form of illicit government funding and as an inflationary policy that endangered the ECB's pursuit of price stability.<sup>41</sup> These criticisms are invalid and divert attention away from the real issue. First, the NCBs' purchases of financial assets in secondary markets are subject to control by the ECB, and the ECB enforces the conditions that according to the CJEU ensure that secondary-market purchases do not violate the prohibition of direct funding of governments by central banks.<sup>42</sup> There is no evidence that securities purchases under ANFA have violated these rules.

Second, aggregate NCB investments under ANFA were never so large as to impede the ECB's control over the monetary base, the sum of notes in circulation and deposit liabilities to credit institutions. In mid-2002, NCB net financial asset holdings amounted to 60% of the monetary base of €445 billion, in mid-2007 to 49% of the monetary base of €811 billion, in mid-2011 to 56% of the monetary base of €1064 billion.<sup>43</sup> These shares are substantial, but the remaining

---

39 Again see [https://www.ecb.europa.eu/ecb/educational/explainers/tell-me-more/html/anfa\\_qa.en.html](https://www.ecb.europa.eu/ecb/educational/explainers/tell-me-more/html/anfa_qa.en.html)

40 See Deutsche Bundesbank (2016). The numbers comprise all "financial" assets, ELA loans and reserves of gold and foreign exchange, as well as securities.

41 A prominent example is Sinn (2018).

42 Judgment in Case C-62/14-Gauweiler of June 16, 2015.

43 Some contributions to the German discussion give exaggerated numbers for NCB securities holdings under ANFA. These numbers are based on misinterpretations of statistics in Hoffmann (2015). Hoffmann uses the expression „Sonstige Wertpapiere“ sometimes as meaning "other securities", as is appropriate, and

40%, or more, more of monetary liabilities funding monetary assets left the Governing Council and the Eurosystem enough room to manage the monetary base as it wished.

Below, I will argue that the decreases since 2015 were associated with the Eurosystem's massive open market purchases of securities in these years. Therefore, one cannot rule out the possibility that the reversal of monetary policy in 2022 and 2023 may cause a renewed increase in net financial asset holdings. In fact, as of January 1, 2023, these holdings already were €60 billion above the 2022 average of minus €730 billion. It is premature to think of ANFA as moot.

## 5.5 The Economics of Net Financial Asset Purchases

For an NCB, the ability to buy financial assets under Art. 14.4 of the Statute using monetary liabilities for funding has two advantages. First, it can react quickly to adverse developments that lower the market prices and raise the yields of its country's sovereign debt. For example, one may suppose that the €6 billion increase in the Banca d'Italia's net financial asset holdings in 2011 were intended to counteract the effects of northern banks' sales of Italian debt in that year, including a €7 billion sale by Deutsche Bank (announced in late June 2011).

Second, if an asset yields returns at a rate exceeding the Eurosystem's main refinancing rate, it is more profitable for an NCB to buy and hold such an asset under Art. 14.4 of the Statute, "on its own responsibility and liability", than to do so as an operation of monetary policy, subject to the rule of Art. 32 for the sharing of monetary income. If the asset purchase is carried out as an operation of monetary policy, then, according to Art. 32.1 of the Statute, the entire return on the asset must be shared with the other members of the Eurosystem. If instead the NCB buys the asset "on its own responsibility and liability", sharing with other members of the Eurosystem is limited to the part of returns that would be earned if the relevant rate was the main refinancing rate, and the NCB gets to keep the difference. One may assume that this is a major reason why some NCBs have found it attractive to buy certain assets "on their own responsibility and liability".<sup>44</sup>

From this perspective, the approach underlying ANFA amounts to a significant deviation from the principle of income sharing as formulated in Art. 32 of the Statute. According to ANFA, the limit to aggregate net financial assets is calibrated to anticipations of the minimum amount of liquidity provision to euro area credit institutions over the relevant period. Deviations of the actual liquidity provision from this anticipated minimum are only due to imperfect foresight, uncertainty about what liquidity provision to euro area credit institutions will actually be needed. If this need could be perfectly predicted, the anticipated minimum would coincide with

---

sometimes as meaning "other assets", which includes not only securities but also ELA loans and a hodgepodge of other things, including "other financial assets", such as pension fund assets, that are not funded by monetary liabilities. Papadia (2015) explains the issues. See also Hellwig (2018), 369f.

44 Sinn (2018) refers to ANFA (and ELA) as a mechanism for "self-service with the printing press", meaning that ANFA introduces an inflationary factor that is controlled by the NCBs. As explained above, there is no evidence that ANFA has allowed for liquidity creation over and above the objectives of the ECB. Instead, the argument given here suggests that ANFA is a mechanism for self-service in the distribution of monetary incomes.

the actual amount, and ANFA would limit monetary incomes to the amounts generated by applying the main refinancing rate to the NCBs' monetary liabilities. To be sure, the assumption of perfect predictability is wildly unrealistic, but then the conclusion is that any monetary income above the income obtained by applying the main refinancing rate to the monetary liabilities must be due to deviations of actual liquidity provision from anticipated minimum liquidity provision.

One can see why a majority of the Governing Council might like such an approach. However, I wonder by what reasoning the Governing Council considers this approach to be compatible with the primary law under which it is supposed to operate.

## 5.6 Applying the ANFA Approach to Monetary Assets

The Governing Council's disregard of Art. 32 of the Statute has gone even further. When the ECB started the Public Sector Purchase Programme (PSPP) of massive open market purchases, it decided that, for purposes of assessing monetary incomes, assets purchased under this program should be treated like financial assets purchased under Art. 14.4 of the Statute. The monetary incomes attributed to PSPP assets would be assessed with reference to the main refinancing rate. Any difference between actual incomes and assessed incomes would be exempt from income sharing between the members of the Eurosystem.<sup>45</sup> Since the PSPP was part of the monetary policy of the Eurosystem, asset purchases under this program could hardly be considered as activities under Art. 14.4 of the Statute.

According to Art. 32.1 of the Statute, NCB income from these assets should therefore be shared between the NCBs in proportion to their shares in the ECB. The Article refers explicitly to "the income accruing to the national central banks in the performance of the ESCB's monetary policy" without any exception for specific assets or specific operations. There is also no mention that income may be *imputed* to the national central banks on the basis of some reference rate imputed to a fictitious asset.

According to media reports at the time, the decision to treat asset purchases under PSPP as if they were asset purchases on the NCBs' own responsibility was part of a package intended to conciliate Bundesbank President Weidmann, as mentioned in the introduction. The other part of the package was a proviso that each NCB should be in charge of buying securities issued by its own government. Thus, Italian government debt was purchased by the Banca d'Italia, so a default on this debt would hit the Banca d'Italia, rather than the Bundesbank. President Weidmann had previously railed against the planned PSPP on the grounds that German taxpayers would have to bear the default risks, so an arrangement that insulated the Bundesbank from such risks deflected this criticism and enabled him to agree to the program without

---

45 See Art. 3(1)b of Decision (EU) 2016/2248 of the European Central Bank of 3 November 2016 on the allocation of monetary income of the national central banks of Member States whose currency is the euro (ECB/2016/36). In 2020, the wording of this article was amended so that it also applies to securities purchased under the Pandemic Emergency Purchase Programme (PEPP); see Decision (EU) 2020/1735 (ECB/2020/55).

losing face. Hardly anyone was concerned that this package stood at odds with the primary law.

Nor were Germans much concerned with the fact that the Bundesbank President's suggestion cost the Bundesbank a lot of money. Over the years 2016-2019, when PSPP asset purchases were very high, the profits of Banca d'Italia were more than one-and-a-half times the profits of the Bundesbank even though the balance sheet of the Banca d'Italia was much smaller. Banca d'Italia benefited from the fact that it could keep the difference between the interest on Italian government debt and the Eurosystem's main refinancing rate rather than sharing it with the other NCBs. In contrast, the interest on German government debt was close to zero, or even negative, so the Bundesbank did not earn significant profits on its holdings of these securities.<sup>46</sup> Perhaps the Bundesbank accepted the lower profits as an appropriate cost of avoiding the default risks attached to the sovereign debt of other member states. However, the dimension of the tradeoff was never discussed in public.

The application of the approach of Art. 14.4 of the Statute to NCB asset purchases under PSPP and similar programs also contributes to explaining the decline in net financial assets during these years. For the NCB of a country whose sovereign debt paid interest at a relatively high rate, there was no point in buying debt securities as financial assets because purchases of these securities as monetary assets under PSPP were performed under the same rules, namely no sharing of incomes above what was implied by the application of the main refinancing rate.

If ever the Governing Council were to go back to the sharing rule prescribed in the Treaty, one should therefore expect a substantial increase in the net financial assets of some NCBs. To avoid such an increase, the allowed levels of net financial assets would have to be reduced substantially; ANFA would have to be modified dramatically or even rescinded. Given that, except for the Banca d'Italia, net financial holdings at present are negligible or even negative, such a change in ANFA might be politically feasible.<sup>47</sup> However, it is doubtful that the Governing Council would at all be willing to return to the regime for income sharing in Art. 32 of the Statute. The fact that the Statute is the primary law seems irrelevant.

## 6. NCB Accounting and Balance Sheets

The obfuscation of the boundaries between monetary and nonmonetary, subordinated and independent activities of NCBs is reinforced by the NCBs' accounting practices. NCB balance sheets make no clear distinction between positions that arise from subordinated activities and positions that arise from independent activities. If the NCBs were private corporations, their accounting practices would be considered illegal.

---

46 It did however earn significant income from credit institutions holding central bank deposits that bore negative interest. This monetary income had to be shared with the other NCBs.

47 In 2022, the only NCB with significantly positive net financial assets was the Banca d'Italia, whose financial assets exceeded nonmonetary liabilities by ca. € 61 billion. Banque de Belgique had ca. €4 billion of net financial assets, the central banks of Estonia, Latvia and Malta less than €1 billion each.

The problems arise from the hybrid nature of NCBs. As discussed above, NCBs are legally independent institutions that share in the equity of the ECB, but they are also subordinated to the ECB in monetary-policy operations. Some of their monetary-policy transactions involve their relations with the ECB or the other NCBs. These transactions are recorded in a system of internal accounts reflecting intra-Eurosystem relations. These internal accounts have little to do with the assessment of NCB financial health by an outside investor such as a shareholder of the Banque de Belgique. Yet, the Eurosystem's accounting system makes no difference between the different types of accounts.

To see how intra-Eurosystem transactions work, go back to the decision, mentioned above, that only NCBs offer accounts to credit institutions. Suppose that a person in Italy wants to pay €1000 to a recipient in Germany. In addition to the payer's and the payee's banks in Italy and in Germany, the transaction involves the Banca d'Italia, the ECB, and the Deutsche Bundesbank: The Italian bank charges €1000 to its client's account and instructs the Banca d'Italia to perform the transfer. The Banca d'Italia charges €1000 to the Italian bank and asks the ECB to perform the transfer. The ECB charges €1000 to the Banca d'Italia, credits €1000 to the Bundesbank, and asks the Bundesbank to complete the transfer. The Bundesbank credits €1000 to the recipient's bank and asks that bank to credit €1000 to the recipient.

This chain of transactions presumes that the NCBs have accounts with the ECB that can be charged or credited when they enable cross-border payments within the euro area. These are the so-called *Target* accounts, where "Target" is an acronym for the electronic system for processing payments inside the Eurosystem.<sup>48</sup> The NCBs' balance sheets contain the positions in these accounts as assets and liabilities along with their assets and liabilities from other activities, as if these positions had comparable legal and economic status.<sup>49</sup> This accounting practice has induced many observers to interpret the balances in Target accounts as genuine claims on or obligations to the ECB.<sup>50</sup>

In fact, under the prevailing primary and secondary law, positive Target balances do not confer any claims and negative Target balances do not impose any obligations. An NCB with a positive Target balance cannot ask the ECB to "reimburse" it, whatever that may mean, nor can the

---

48 The full name is *Trans-European Automated Real-Time Gross Settlement Express Transfer System*.

49 There are also some other accounts for intra-Eurosystem claims and liabilities. An important example concerns claims and liabilities in the context of swap agreements with central banks issuing other currencies, most importantly the Federal Reserve. In the fall of 2008, as well as later crises, such accounts played a role in providing support to European credit institutions without US subsidiaries that had borrowed dollars and could not roll over these borrowings when money markets froze. The Federal Reserve lent dollars to the ECB under a swap agreement, the ECB passed these dollars on to the NCBs, and the NCBs passed them on to the banks. For details, see Hellwig (2018), 363f. and Adam Tooze (2018).

50 For an early example, see Peter Gauweiler, *Anstieg der Forderungen der Deutschen Bundesbank gegenüber der EZB und nationalen Notenbanken innerhalb des Eurosystems seit 2006 sowie Rechtsgrundlage, demokratische Legitimation und Absicherung dieses Verleihs deutscher Staatsgelder* (Increase of Bundesbank Claims on the ECB and the NCBs in the Eurosystem since 2006: Legal basis, democratic legitimacy and collateralization of such lending of German funds), Fragen Nr. 15-18 in: Deutscher Bundestag, *Schriftliche Fragen mit den in der Woche vom 28. März 2011 eingegangenen Antworten der Bundesregierung* (Written Questions to the Federal Government and Answers Received in the Week of March 28, 2011), Drucksache 17/5322, 8-10. The Federal Government's response to Gauweiler's questions states very clearly that Target balances do not reflect lending relations or subsidies between different countries but are merely parts of the internal accounting system of the ESCB.

ECB ask an NCB with a negative Target balance to repay its “debt”.<sup>51</sup> Under the rules of the Governing Council, Target balances are treated as monetary assets and liabilities, with interest attributed according to the “reference rate”, i.e. the interest rate for the Eurosystem’s main refinancing operations.<sup>52</sup> However, these attributions of interest income to Target balances do not translate into interest incomes or interest costs of the NCBs. The interest attributed to and NCB’s Target claims or liabilities is part of the NCBs’ monetary income and thus subject to income sharing between the different NCBs. In the aggregation of monetary incomes across NCBs, the Target claims and liabilities cancel out, and so do the attributions of positive and negative interest to these claims and liabilities. The amount that any NCB receives as its share of monetary income of the Eurosystem is completely independent of the NCB’s Target balance.<sup>53</sup>

---

51 The prevailing law does not allow for the possibility of exit from monetary union, except in connection with an exit from the EU as a whole. If a member state proposes to leave the EU altogether, the status of intra-Eurosystem claims and liabilities of that country is up in the air and must be determined in the exit negotiations under Art. 50 of the Treaty on European Union. A letter of January 18, 2017, from ECB President Draghi to two Italian members of the European Parliament, makes the same claim. However, a leaving country whose NCB has significant Target liabilities would likely claim that Target accounts are merely internal accounts of the Eurosystem and have no legal significance. As we have seen with the exit of the United Kingdom, the outcomes of such negotiations have more to do with the objectives and the bargaining powers of the different parties than with their presumed legal titles. In Hellwig (2018), Section 5, I have argued that a country that wants to leave has factual power over the assets owned by its central bank and there is nothing to prevent the country from taking these assets away from the Eurosystem. At the same time, the country’s NCB would lose its claims to a share of monetary incomes of the NCBs and of the ECB’s profits. Interestingly, the rule for the allocation of asset purchases and incomes that has been adopted for the PSPP has the property that the PSPP leaves the difference between the value of assets owned by an NCB and the value of the NCB’s share in Eurosystem income and ECB profits unchanged.

52 See Annexes I and II of Decision (EU) 2016/2248 of the European Central Bank of 3 November 2016 on the allocation of monetary income of the national central banks of Member States whose currency is the euro (ECB/2016/36).

53 For details, see Hellwig (2018), 360 ff. The claim of Sinn (2014), that interest on Target balances is added to the Target balances on a yearly basis is thus invalid. Sinn (2019), 195-198, does not refute this assessment but suggests that we should interpret the excess of, say, the Bundesbank’s share in monetary income over the monetary income generated by assets funded from the Bundesbank’s own money creation as remuneration for the Bundesbank’s Target claims. This interpretation has no basis in the law. On the economic issues involved, see note 55 below.

Sinn (2019), 199-201, also claims that there is a compound-interest effect because the Bundesbank’s share in the Eurosystem’s monetary income is “paid” through an increase in the Bundesbank’s Target claims, which increases the interest the Bundesbank will receive in the subsequent year. This claim is also invalid. Sinn fails to take account of the fact that the counterpart in the balance sheet of the increase in the Bundesbank’s Target balance that comes with the “payment” of the Bundesbank’s share in monetary income is an increase in the Bundesbank’s undistributed profits, which is a nonmonetary balance sheet position. This position might be added to the Bundesbank’s reserves, or it might be “paid” to the government, which would increase the government’s deposits with the Bundesbank. In either case, the increase involves a nonmonetary liability of the balance sheet. If the Bundesbank’s monetary assets, which include its Target claims, exceed its monetary liabilities, the income “payment” to the Bundesbank increases not only the Bundesbank’s Target claims but also the excess of the Bundesbank’s monetary assets over its monetary liabilities. As discussed above, this excess is treated as a fictitious liability that bears interest at the reference rate. The increase in assessed interest on the Bundesbank’s monetary assets is exactly matched by the increase in assessed interest on this fictitious liability, so the “payment” of income has no effect on the subsequent period’s monetary income of the Bundesbank. If the Bundesbank’s monetary assets fall short of its monetary liabilities, the argument is even simpler. In this case, the Bundesbank’s monetary liabilities are unchanged. The increase in Target claims that results from the “payment” of income to the Bundesbank reduces the difference between the Bundesbank’s monetary liabilities and its monetary assets. This reduction also reduces the level of the fictitious asset that stands in for the excess of monetary liabilities over the actual monetary assets of the Bundesbank. Since this fictitious asset is deemed to pay interest at the reference rate, just like the Target claims, there is again no effect of “payment” of income on the subsequent period’s monetary income.

The appearance of Target balances in NCB balance sheets violates the principle of fair-value accounting. According to this principle, balance sheet entries for assets and liabilities should fairly reflect the economic benefits or the economic burdens associated with these assets and liabilities. Since Target balances have no effects on future payment streams, their fair value is zero. To be sure, the NCBs do receive income from their (and the other central banks') monetary policy activities, and fair-value accounting requires the prospects of such incomes to make an appearance in their balance sheets.<sup>54</sup> However, the Target balances do not serve this purpose.<sup>55</sup>

If the NCBs and the ECB were private corporations under corporate law, monetary policy would be considered a joint operation of these institutions. For such a joint operation, International Financial Reporting Standards (IFRS) prescribe the method of *quota consolidation* of assets and liabilities.<sup>56</sup> Under this method, each institution would have a separate set of accounts for assets and liabilities involved in the joint operation. For the institutions' own financial reporting, these separate joint-operation accounts would be consolidated over the different participants, and each participant would report its share of the consolidated assets and liabilities in its own balance sheet. Intra-system claims and liabilities would disappear in the consolidation, and there would be no room for misunderstanding the claims and liabilities as legal titles.

Because the members of the Eurosystem are acting under public law rather than corporate law, they may disregard the International Financial Reporting Standards. Their independence from outside influence gives the Governing Council full sovereignty over accounting practices. However, for someone like the private shareholders of the Banque de Belgique, an accounting system based on quota consolidation would provide greater clarity about the true financial health of the institution. Use of such an accounting system would also have avoided some of the acerbity of intra-euro-area discussions of the past decade.

From the perspective of the NCBs, however, the commingling of monetary and nonmonetary activities in a single set of accounts had several advantages. Most importantly, it allowed them to hide the fact that, in their monetary-policy activities, they are not independent, but must

---

54 Homburg (2019) suggests that the inclusion of Target balances in national accounts should be taken as evidence of their economic significance. This suggests overlooks the fact that national accounts rely on the numbers that the NCBs report to them, so they do not provide independent evidence that these number mean what he takes them to mean.

55 The view of Sinn (2019), 195-198, that the excess of the Bundesbank's share in monetary income over the monetary income generated by assets funded from the Bundesbank's own money creation can be interpreted as a remuneration for the Bundesbank's Target claims is problematic. The excess of the Bundesbank's share in monetary income over the monetary income generated by assets funded from the Bundesbank's own money creation contains the realizations of income streams from loans and securities held by other central banks. These income streams depend on many variables other than target balances. Interpreting them as "interest" on Target claims blurs the boundary between non-contingent interest claims on specified legal titles and outcome-dependent claims on other assets.

56 See International Accounting Standards Board, *International Financial Reporting Standard (IFRS) 11*. German commercial law, also stipulates quota consolidation (§ 310 HGB) unless the joint arrangement takes the form of a joint venture over which the reporting institution has substantial influence (§§311, 312 HGB), in which case the law also allows the *equity method*. Under this method, the institution reports only a number for value of its participation in the joint venture. For joint ventures, since 2014, IFRS has prescribed the equity method. Since none of the participating institutions of the Eurosystem can be said to have *substantial* influence on its own, the comparison to a joint operation seems to be more appropriate than a comparison to a joint venture. Note, however, that, under the equity method, accounts that reflect intra-operation relations also do not appear in the reporting institution's balance sheet.

follow instructions from the ECB. Their accounts reflect all their transactions, as if they were sovereign in all of them.<sup>57</sup>

The commingling of monetary and nonmonetary activities also facilitates the funding of non-monetary activities by money creation and thereby the diversion of income out of the sharing mechanism provided by the Statute. If there was a separate set of accounts for monetary and nonmonetary activities, NCBs that want to buy and hold financial, nonmonetary assets would have to bother about funding these assets. Such funding might come from the Eurosystem, even the monetary policy part of the NCB itself, but then the Eurosystem would have to address the monetary-policy implications of the operation. Leaving such transactions to the full discretion of NCBs, subject only to the quantitative limit provided by ANFA, would not be so easy.

In summary, the Eurosystem's accounting practices also support the assessment that the dominance of NCB governors makes the Governing Council an instrument of the NCBs' common interest in minimizing the effects of European Monetary Union on their own status and the public appearance of their own status.

## 7. Back to President Weidmann's Campaigns

In the introduction, I had raised the question whom Bundesbank President Weidmann was addressing and what purpose he was trying to achieve with his campaigns against the ECB. A major topic of these campaigns concerned fiscal risks. For example, in an interview in December 2014, he warned that, if the members of the Eurosystem bought massive amounts of the debt of member states and a member state defaulted on its debt, the Eurosystem would suffer

---

57 Interestingly, the Bundesbank's position on the status of Target claims is less clear than that of the German government mentioned above. Beginning with its Annual Report 2011, 48-50, and its 2012 Statement to the Federal Constitutional Court, 23-25, the Bundesbank has referred to target balances as if they were legal titles, rather than reflections of transactions in the internal accounts of the Eurosystem. The Bundesbank regularly emphasizes that increases in Target claims as such only create risks in the event of some country's exit and that otherwise risks to the Eurosystem arise from liquidity creation, rather than transfers of liquidity within the system. For a more recent and detailed statement, see Deutsche Bundesbank, Stellungnahme anlässlich der öffentlichen Anhörung des Finanzausschusses des Deutschen Bundestags am 5. Juni 2019 zu dem Antrag der Fraktion der FDP „Kapitalmarktunion vertiefen, Staatsschulden entprivilegieren, TARGET2-Salden verringern“ (BT-Drucksache 19/6416) sowie zu dem Antrag der Fraktion der AfD „Target-Forderungen unabhängig vom Fortbestand des Euros besichern“ (BT-Drucksache 19/9232) (Statement on the occasion of the Bundestag's Finance Committee's public hearing on the submission „Deepen capital markets union, eliminate privileges of sovereign debt, reduce Target balances“ of the Free Democratic Party (FDP) and the submission „Make Target claims safe even if the euro does not persist“ of the Alternative for Germany (AfD) (<https://www.bundesbank.de/de/presse/stellungnahmen/stellungnahme-der-deutschen-bundesbank-anlaesslich-der-oeffentlichen-anhoerung-des-finanzausschusses-des-deutschen-bundestags-am-5-juni-2019-798206>). On its website (<https://www.google.com/search?client=firefox-b-d&q=bundesbank+zinsen+auf+target+salden>), the Bundesbank asserts that participating NCBs “pay interest” on Target liabilities and receive interest on Target claims. This assertion echoes Sinn (2019), 195-198. As explained above, in the text and n. 53, the assertion misinterprets the role of interest on Target balances under Decision ECB/2016/36. The Bundesbank fails to make clear that interest on target balances concerns a set of transient accounting positions that disappear in the aggregation of monetary incomes in the Eurosystem and are irrelevant for the shares of monetary incomes that NCBs receive.

a loss. This loss would be shared among the different central banks and ultimately would have to be borne by taxpayers.<sup>58</sup>

At the time, I criticized this emphasis on the fiscal repercussions of the proposed policies, rather than their suitability for monetary policy.<sup>59</sup> In opposition to ECB President Draghi's plans for massive asset purchases, particularly the Public Sector Purchase Programme (PSPP), President Weidmann might have contested the ECB's assessment that there was a danger of deflation and that the ECB had to fight this danger. He might also have argued that the scale of the planned program exceeded what was needed to fight deflation and therefore implied a risk of inflation. Instead of referring to price stability, however, he focused on business risks to the NCBs and their implications for taxpayers. He seemed more concerned about central banks' business risks than about price stability.

Business risks are an inevitable feature of central bank operations, not only for open-market operations, but also for lending to banks.<sup>60</sup> Open-market operations are a standard instrument of monetary policy. Art. 18 of the Statute empowers the ECB and the NCBs to engage in open-market operations without raising any concerns about the implied business risks. Wholesale warnings about central banks' business risks from open-market operations suggest that the warner may be prioritizing business risks concerns over price stability.<sup>61</sup> Such a prioritization has no basis in the Treaty and the Statute, which give the highest priority to price stability.<sup>62</sup>

The Bundesbank had previously used the same warning in the brief it submitted to the German Federal Constitutional Court (GFCC) in the OMT case.<sup>63</sup> In that case, some of the plaintiffs who contested the legality of the ECB's OMT program had argued that open-market purchases of government debt securities would violate core conditions of the German Basic Law that are essential to the German constitutional identity. Such purchases would involve risks of losses, so that there might be negative effects on the Federal budget. ECB decisions that caused such

---

58 Jens Weidmann, Für die Verluste haften die Steuerzahler (Losses will hit taxpayers), *Frankfurter Allgemeine Sonntagszeitung*, December 28, 2014.

59 See Martin Hellwig, Jens Weidmanns gefährliche Argumente (Jens Weidmann's dangerous arguments), *Frankfurter Allgemeine Sonntagszeitung*, January 5, 2015, and Martin Hellwig, Richtige und falsche Ängste vor einer expansiven Geldpolitik (Appropriate and inappropriate fears for an expansionary monetary policy), *Frankfurter Allgemeine Sonntagszeitung*, March 9, 2015.

60 See Hellwig (2014a, 2015).

61 Quite likely, the warner is also disregarding the fact that business risks are exaggerated if one fails to take account of the profits from the creation of new central bank money. Any counterfeiter knows that using forged money to buy stocks is profitable and if the stocks lose in value, the profits decrease but do not become negative. The same logic applies to a central bank, except that it does not have to fear the police and in its balance sheet, it treats its note issue as debt. In a fiat money regime, however, banknotes do not oblige the central bank to anything and deposits of credit institutions only oblige the central bank to deliver banknotes. Treating the note issue as debt may be useful for deflecting political pressures to "produce" lots of notes and immediately pay out the profits to the government. See Hellwig (2014a, 2015).

62 When formulated in more general and more abstract terms, such a prioritization might also justify using the printing press to fund the public budget.

63 Deutsche Bundesbank (2012), 25-29. In the 1970s, the Bundesbank itself had used open-market operations for monetary policy. Subsequently, however, it abandoned this practice and relied only on managing the liquidity available to the banking system. This Bundesbank tradition provided the background to the Eurosystem's choice of monetary strategy in the 2000s. The ECB's turn to open-market operations, first on a small scale with the Securities Markets Programme in 2010, then on a massive scale with the announcement of the – potentially unlimited – OMT Programme in 2012, was strongly resisted by the Bundesbank, whose representatives saw open-market purchases of sovereign debt securities as a first step in a transition to fiscal dominance in violation of the Treaty's prohibition of funding member state governments.

loss would be in conflict with the fundamental constitutional norm that the Bundestag must be fully in charge of decisions concerning the Federal budget. The Bundesbank's statement to the Federal Constitutional Court confirmed the plaintiffs' arguments about the risk of losses and the potential impact of losses on the Federal budget. The Federal Constitutional Court itself alluded to the issue in its request for a preliminary ruling from the CJEU, but reserved judgement on it. Implicitly, however, it was warning the CJEU that it might take recourse to the issue of parliamentary sovereignty in budget matters and the German constitutional identity.

The cited interview from December 2014 must perhaps be seen in this context. At the time, the OMT case was still up in the air. The final recommendation of the Advocate General and the judgment of the CJEU were expected for 2015. There was a prospect that the CJEU would deny the plaintiffs' and the GFCC's claims that OMT transgressed the limits sets to the ECB by the Treaty. The Federal Constitutional Court would in principle be bound by the CJEU's judgment, but the opponents of OMT, some of them opponents of monetary union altogether, hoped that the GFCC might still reject the OMT Programme on the grounds that it violated the German parliament's sovereignty in budget matters and the German constitutional identity. President Weidmann's renewed focus on the risk of losses from open-market purchases and the implications of such losses for the Federal budget reminded the German public of this issue and put pressure on the GFCC.

The interview followed the Bundesbank's tradition of public protest against developments it disliked. The argument that open-market purchases of other member states' government bonds might saddle taxpayers with risks of default on those bonds must be seen in the context of the German debate about the ECB, with its strong elements of nationalism.<sup>64</sup> It appealed to nationalist disdain of other countries' unsound policies and to fears that others were taking advantage of Germany. Such mobilization of public support might not sway the ECB, but it would strengthen the Bundesbank's position in the German polity and perhaps sway the GFCC.

While saying hardly anything about the issue of German constitutional identity, the CJEU's OMT ruling commented on the issue of risks to taxpayers with a few remarks to the effect that risks, including risks of losses, are unavoidable in monetary policy operations, including open-market operations, so given the empowerment of the ESCB to engage in such operations that is contained in Art. 18 of the Statute, the fact that such purchases under the OMT program

---

64 Public support of the Bundesbank in Germany has long involved an element of nationalism. For many people, the repeated revaluations of the Deutschmark in the 1980s and 1990s were occasions for national pride, combined with disdain for countries whose currencies were devalued. The Bundesbank used to play on this sentiment – never mind the repercussions in other countries. When in an interview in September 1992, Bundesbank President Helmut Schlesinger asserted that the preceding weekend's exchange rate adjustment in the European Exchange Rate Mechanism (ERM) was insufficient and that additional adjustments were needed, he triggered the run on the English pound that caused the United Kingdom to leave the ERM. It also caused some very bad feelings on the other side of the English Channel. Exchange rate policy at that time did not belong to the domain of the Bundesbank but to the domain of the government. With similar disregard for the potential foreign policy repercussions of the Bundesbank's transgressing the boundaries of its domain of competence, more recently, a high official of the Bundesbank called for Italy to impose a levy on private wealth in order to reduce its public debt. See Karsten Wendorff, „Rom sollte Italiener zur Solidarität verpflichten“ (Rome should impose solidarity on Italians), *Frankfurter Allgemeine Zeitung*, 27. Oktober 2018. The article appeared under the author's name but he presented his proposal in his role as head of the Bundesbank's public finance department.

would involve such risks could not be regarded as an additional source of concern.<sup>65</sup> The subsequent judgement of the Federal Constitutional Court put the issue aside with the argument that the quantitative limits on OMT securities purchases mandated by the CJEU provided a sufficient bound for the risks in question, as if the constitutional argument was tied to the size of the positions involved.<sup>66</sup>

If the Federal Constitutional Court had taken on the issue of risks of Bundesbank losses, as President Weidmann may have thought appropriate, the implications might have been drastic, including possibly a call for a German exit from the European Monetary Union, on the grounds that the budgetary implications of monetary union were incompatible with the German constitutional identity. The Court might have limited itself to calling for a German non-participation in OMT, but then the question would have been why risks from OMT were any worse than risks from other open-market operations and indeed risks from providing refinancing loans to credit operations. The subject would have come up again with every new ECB program because every program of a central involves fiscal risks. Complaints about risks from the ECB to German taxpayers would be unstoppable, except by exit. President Weidmann may not have had this objective in mind, but then he did not make clear where he thought his arguments would be leading.<sup>67</sup>

The spring 2015 decision of the Governing Council, discussed in Section 5.6 above, to treat assets purchased under the PSPP as if they were financial assets purchased by NCBs under Art. 14.4 of the Statute, “on their own responsibility and liability”, seems to have defused the issue of potential NCB losses from these purchases and made it possible for the Bundesbank to support the legality of program in subsequent GFCC proceedings without losing face.<sup>68</sup> This decision insulated the Bundesbank from the effects of a potential sovereign default by another member state, but as discussed above, it also violated the income sharing requirement of Art. 32.1 of the Statute.<sup>69</sup>

---

65 See the Court’s judgment in the case *Gauweiler and Others*, C-62/14 of 16 June 2015, 123-126.

66 See GFCC judgment of June 21, 2016 – 2BvR 2728/13, 218f. In its PSPP judgment in 2020, the GFCC also put the issue of budgetary risks aside, this time because it was much more interested in its own conflict with the CJEU than in the Bundesbank’s conflict with the ECB.

67 However, if the GFCC had actually gone all the way to declaring European Monetary Union to be incompatible with parliamentary sovereignty over the federal budget and calling for a German exit, the Bundesbank would have found that the arguments given in proceedings against the ECB could also be applied to the Bundesbank, not only in the matter of needing parliamentary approval for incurring risks, but also in the matter of subjecting substantive consideration about monetary policy to judicial review as the Bundesbank did in its 2012 Statement to the Federal Constitutional Court in the matter of OMT. At the time of the GFCC’s hearings on OMT, I therefore called the Bundesbank’s statement an “own goal”; see Martin Hellwig, *Eigentor der Bundesbank (Own Goal of the Bundesbank)*, *Handelsblatt*, June 11, 2013.

68 As explained above, this decision has reduced the Bundesbank’s profits and the Bundesbank’s payouts to the German government since 2015 quite substantially.

69 Whether this decision really insulated the Bundesbank from haircuts on other member states’ debts, is actually unclear. Art. 32.4 of the Statute empowers the Governing Council to “decide that national central banks shall be indemnified... in exceptional circumstances for specific losses arising from monetary policy operations undertaken for the ESCB”. This formulation suggests that, in contrast to standard accounting practices, such losses are not integrated into monetary income. It also shows that, if push came to shove, the Governing Council could decide to indemnify an NCB affected by losses from a haircut on its own government’s debt, despite the decision discussed in the text.

## 8. Concluding Remarks

The analysis of this paper suggests that, as far as European law is concerned, the question I posed in the introduction is moot. Whatever loyalty obligations may come with membership of an NCB in the ESCB and with membership of an NCB governor in the Governing Council of the ECB are irrelevant if the Governing Council fails to enforce them. Moreover, because the NCB governors form a large majority of the Governing Council, such enforcement is unlikely. Any action of the Governing Council that would restrain the outside politicking of an NCB governor would create a precedent that might be turned against any other NCB governor at a later time. Such action is therefore unlikely.

The dual role of NCB governors, as members of the Governing Council of the ECB and as heads of their own institutions gives rise to a conflict of interest whenever NCB relations with the ECB are at stake. This conflict of interest may not be so much of a problem in monetary policy decisions as such, where the centrifugal tendencies from NCB special interests are probably counteracted by the strong position of the ECB President and Board. But even then, public expressions of opposition to ECB policies by NCB governors may undermine and credibility and thereby the effectiveness of monetary policy.<sup>70</sup>

In other matters however, the NCBs' interests clearly dominate. The treatment of financial assets under ANFA and the treatment of open-market operations since 2015 show that the dominance of NCB interests may prevail even against the primary law. One might consider this to be irrelevant because, after all, it does not seem to have affected the functioning of monetary policy. One might argue that, if Governing Council decisions go counter to the income sharing provisions of the Statute, then so be it, since the NCBs themselves are most directly affected. However, the lack of respect for the primary law that is shown by responsible officials contributes to popular disaffection and undermines our democracies.

The NCB governors' conflicts of interest are particularly problematic when NCB subordination to the ECB and even NCB membership in the Eurosystem are at stake. In the OMT and PSPP cases, the line of argument pursued by the Bundesbank could easily have led to the German Federal Constitutional Court's asserting the need for democratic, i.e., parliamentary control of ECB decisions that implied risks for the public budget. Since all monetary policy decisions involve some risks to public budget, that might have been the end of the ESCB, perhaps even the end of central bank independence as we know it.

Is there be any alternative setup that would avoid the conflicts of interest? In considering this question, one must keep in mind that the continued existence of NCBs and the presence of NCB governors in the Governing Council of the ECB reflects not only the Treaty makers' desire to accommodate existing central banks within the new system but also, more fundamentally, the view that it is useful to bring decentralized information and interests to bear on monetary policy.

---

70 See Linta (2023).

Concerns for decentralized information and decentralized interests also played a role in the creation of the Federal Reserve System in the United States. In that system, however, the regional Federal reserve Banks are not tied to any political units and any jurisdictions. There are only twelve regional Federal Reserve Banks, versus fifty states, and some boundary lines of Federal reserve districts pass through state territories. The presidents of the regional Feds have interactions with and loyalties to their regional constituencies, but they do are not specifically associated with particular polities where they are prominent in public discourse. The regional Feds themselves have no glorious histories to which they might want to return. They exist only because Federal law has created them.

A dissociation of the domains of decentralized central banking institutions from individual polities might also reduce conflicts of interest in the European Union. Any such attempt however would meet with strong resistance. Legally, such a dissociation could be based on the fact that, under the Treaty, monetary policy is in the domain of the European Union, rather than the member states. However, as in other areas of European integration, such a move would cause resentment among all who take pride in the own central banks' past achievements.

For the time being, therefore, it seems that we must continue to live with the frictions and the risks that stem from the NCB governors' hybrid role. One can only hope that the ambitions of these governors, and their home constitutencies, will not at some point lead to a rejection of NCB subordination to the ECB and an attempt at dissociation from the ECB. Dissolution of a common currency is likely to be a very messy affair.

## 9. References

Acharya, Viral V., and Sascha Steffen (2015), The Greatest Carry Trade ever? Understanding Eurozone Bank Risks, *Journal of Financial Economics* 115 (2), pp. 215-236.

ASC (2012), Forbearance, resolution, and deposit insurance, Report 2012/01 of the Advisory Scientific Committee, European Systemic Risk Board, Frankfurt.

Cadamuro, Leonardo, and Francesco Papadia (2021), Emergency Liquidity Assistance: A New Lease on Life or Kiss of Death?, Blog, Bruegel, Brussels, 28 May 2021, <https://www.bruegel.org/blog-post/emergency-liquidity-assistance-new-lease-life-or-kiss-death>.

Conti-Brown, Peter (2016), *The Power and Independence of the Federal Reserve*, Princeton University Press, Princeton, N.J.

Deutsche Bundesbank (2012), Statement to the Federal Constitutional Court, with a particular focus on the OMT programme and the matter of TARGET2 balances, December 21, 2012, <https://www.bundesbank.de/resource/blob/799688/a6e46b9d71e86f076c2aa07e1cd24b7a/mL/2012-12-21-omt-data.pdf>.

- Deutsche Bundesbank (2016). The Role and Effects of the Agreement on Net Financial Assets (ANFA) in the context of implementing monetary policy, *Monthly Report* March 2016, 83–93.
- Economic and Financial Committee (2001), Report on financial crisis management, European Commission, Economic Paper 156, [https://ec.europa.eu/economy\\_finance/publications/pages/publication908\\_en.pdf](https://ec.europa.eu/economy_finance/publications/pages/publication908_en.pdf) .
- Fuest, Clemens, and Hans-Werner Sinn, Target-Risiken ohne Euro-Austritte (Target Risks without euro exits), *ifo-Schnelldienst* 71, 2018.
- Hellwig, Martin (2007), Switzerland and Euroland: European Monetary Union, monetary stability and financial stability, in: Swiss National Bank (ed.), *The Swiss National Bank 1907-2007*, Neue Zürcher Zeitung Publishing, Zürich 2007, 741-780.
- Hellwig, Martin (2014a), Financial Stability, Monetary Policy, Banking Supervision, and Central Banking, in: European Central Bank (ed.), *Monetary Policy in a Changing Financial Landscape*, Conference Proceedings of the ECB Forum on Central Banking, Sintra 2014, 21-54; also: Discussion Paper 09/2014, Max Planck Institute for Research on Collective Goods, Bonn.
- Hellwig, Martin (2014b), Yes Virginia, There is a European Banking Union! But It May Not Make Your Wishes Come True, in: Austrian National Bank (ed.), *Proceedings of the 42<sup>nd</sup> Economics Conference*, Vienna 2014, pp. 157-181; also: Discussion Paper 2014/12, Max Planck Institute for Research on Collective Goods, Bonn.
- Hellwig, Martin (2015), Financial Stability and Monetary Policy, Paper prepared for the Federal Reserve Bank of Atlanta Conference on Central Banking in the Shadows: Monetary Policy and Financial Stability Postcrisis, Discussion Paper 10/2015, Max Planck Institute for Research on Collective Goods, Bonn.
- Hellwig, Martin (2018), Target-Falle oder Empörungsfalle? Zur deutschen Diskussion über die europäische Währungsunion (Target trap or outrage trap? The German discussion on European Monetary Union), *Perspektiven der Wirtschaftspolitik* 19 (2018), 345-382.
- Hoffmann, Daniel (2015), *Die EZB in der Krise: Eine Analyse der wesentlichen Sondermaßnahmen von 2007 bis 2012* (The ECB in the crisis: An analysis of the most important special measures 2007-2012), Schriftenreihe zur Erforschung des Geldwesens 1, Pro BUSINESS GmbH, Berlin.
- Homburg, Stefan (2019), Targetsalden sind nicht empörend, sondern gefährlich (Target Balances are not outrageous but dangerous), *Perspektiven der Wirtschaftspolitik* 20, 98-102.
- Lintä, Tanja (2023), Forward Guidance and Credibility, mimeo, Toulouse School of Economics.

- Meltzer, Alan (2003), *A History of the Federal Reserve, Volume 1: 1913-1951*, University of Chicago Press, Chicago.
- Papadia, Francesco (2015), ANFA or a perfect storm in a cup of tea, *Money Matters – Perspectives on Monetary Policy*, 17 December 2015.
- Siekmann, Helmut (2006), Die Unabhängigkeit von EZB und Bundesbank nach geltendem Recht und dem Vertrag über eine Verfassung für Europa, Institute for Monetary and Financial Stability, Working Paper No. 2, Frankfurt.
- Siekmann, Helmut (2018), Kommentar zu Art. 88 GG, in: Michael Sachs (ed.), *Grundgesetz: Kommentar*, 8<sup>th</sup> edition, C.H. Beck, Munich.
- Sinn, Hans-Werner (2014), *The Euro Trap. On Bursting Bubbles, Budgets, and Beliefs*, Oxford University Press, Oxford 2014.
- Sinn, Hans-Werner (2018), Fast tausend Milliarden Euro Target-Forderungen der Bundesbank: Was steckt dahinter? (Almost one thousand billion Target claims of the Bundesbank: What are the reasons?) *Ifo-Schnelldienst* 71(14), ifo-Institut, Munich 2018.
- Sinn, Hans-Werner (2019), Der Streit um die Targetsalden. Kommentar zu Martin Hellwigs Artikel „Target-Falle oder Empörungsfalle?“ (The dispute about Target balances: Comment on Martin Hellwig’s “Target trap or outrage trap?”), *Perspektiven der Wirtschaftspolitik* 20, 170-217.
- Spahn, Peter (2019), Targetsalden und die Vollendung der Währungsunion (Target balances and the completion of monetary union), *Perspektiven der Wirtschaftspolitik* 20, 103-106.
- Tooze, Adam (2018), *Crashed: How a Decade of Financial Crises Changed the World*, Viking, New York.