

EUROPEAN UNIVERSITY INSTITUTE, FLORENCE

LAW DEPARTMENT

together with

ROBERT SCHUMAN CENTRE FOR ADVANCED STUDIES

EUI Working Paper **LAW** No. 2000/9

Euro Spectator: Implementing the Euro

1999

**National Reports:
Swedish Report/UK Report/Synthesis Report**

A project directed by:
JEAN-VICTOR LOUIS

BADIA FIESOLANA, SAN DOMENICO (FI)

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© 2000 Euro Spectator, EUI
Printed in Italy in September 2000
European University Institute
Badia Fiesolana
I – 50016 San Domenico (FI)
Italy

National Reports

Swedish Report

ERIC CLAPHAM

UK Report

ROBERT KISSACK

Synthesis Report

STEFANIA BARONCELLI

A project directed by:
PROF. JEAN-VICTOR LOUIS

Research assistants:
JULIO BAQUERO CRUZ
STEFANIA BARONCELLI

LIST OF RAPORTEURS

Herta Baumann. *Assistant – Institute of Political Science University of Vienna*

Eric Clapham. *Stockholm School of Economics*

Louis Chauvel. *Maître de conférences des universités à l'Institut d'Etudes Politiques - Chercheur à l'OSC- Paris*

Régis Chemain. *Maître de conférences à l'Université de Paris X Nanterre - Paris*

Diego Devos. *Conseiller au Service Juridique - Banque Nationale de Belgique- Bruxelles*

Nikos Frangakis. *Director of the EKEME - Athens*

Panos Kazakos. *EKEME - Athens*

Robert Kissack. *Federal Trust - London*

Wim Kösters. *University of Bochum*

Helmut Lang. *University of Vienna*

Jacques Le Cacheux. *Professeur à l'Université de Pau et des pays de l'Adour, Directeur du Département des études, OFCE, Paris - Observatoire français des conjonctures économiques (OFCE), PARIS*

Ingo Linsenmann. *Researcher - University of Cologne*

Manuel López Escudero. *Profesor Titular de Derecho Internacional Público de la Universidad de Granada*

Paul Magnette. *Chargé de recherche au FNRS – Maître de conférences à l'ULB - Bruxelles*

Marina Mancini. *Istituto Affari Internazionali (IAI) - Rome.*

Juan Carlos Monedero Fernández-Gala. *Universidad Complutense de Madrid*

Thorsten Müller. *Researcher - University of Cologne*

Peter-Christian Müller-Graff. *Professor at the University of Heidelberg*

Miguel Poiaras Maduro. *IEEI - Lisbon*

Elena Rigacci Hay. *Istituto Affari Internazionali (IAI) - Rome*

Natalino Ronzitti. *LUISS University, special counsellor at the Istituto Affari Internazionali (IAI) - Rome.*

Maria João Seabra. *IEEI - Lisbon*

Ana Isabel Soares Pinto. *IEEI - Lisbon*

Wolfgang Wessels. *Professor at the University of Cologne - Research Institute for Political Science and European Affairs - Jean-Monnet-Chair*

“Euro Spectator: Implementing the Euro”

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SCREENING COMMITTEE

Michael Artis, Ramon Marimon, Yves Meny,
Natalino Ronzitti, Wolfgang Wessels, Jacques Ziller

The working papers *Euro Spectator. Implementing the euro* have been realised thanks also to the contribution of the Banque Nationale de Belgique, the Deutsche Forschungsgemeinschaft and the European Central Bank

SWEDISH REPORT

Eric Clapham*

1. Political Aspects

Sweden joined the EU in 1995 after a referendum in late 1994. At this time, the Maastricht had already been ratified, and therefore EU membership in principle implied EMU membership. This was however not discussed during the campaign preceding the referendum, more than that the question would be settled at a later stage, and probably through a further referendum. As a result, Sweden is at present in the unique position of not having adopted the common currency, in spite of the fact that Sweden has been able to fulfil the convergence criteria and is without a formal exemption.

After the intense campaign in 1994, there was relatively little public debate on EU-related topics during the following year in Sweden. However, the question of Swedish EMU membership has been the subject of increasing public debate during the last few years. This debate has primarily concentrated on the purely economic aspects of adopting the Euro currency, i.e. whether membership would enhance Sweden's economic prospects. On the other hand, serious debate of the institutional set-up of the ECB and the Stability pact has largely been confined to a narrower group of experts.

1.1 Public Opinion

* *Stockholm School of Economics.*

When analysing public opinion about the EMU, it should be remembered that the Swedish population tends to be the most eurosceptic within the EU. Sweden only recently joined the union, and had earlier taken considerable pride in its non-alliance.

This general attitude affects also public opinion regarding Swedish EMU membership. Since 1996, when regular polls began, the fraction of the population that is against membership has been much larger than the fraction in favour. However, a substantial part of the population has not expressed an opinion in polls.

Opinion about EMU membership follows the same kind of socio-economic pattern as about EU membership. This means that urban dwellers, private sector employees and white-collar worker tend to be more favourable to membership than rural dwellers, public sector employees and blue-collar workers.

Swedes do not appear to attach very great sentiments to the domestic currency. Debate has to a greater extent been focused on whether there is need for monetary policy to achieve sufficient macroeconomic flexibility and whether joining the EMU may have effects on other policy areas.

Figure 1: In a referendum on Swedish EMU membership, would you vote yes or no?
 Surveys are based on 1000 interviews. All figures are percentages.

	October 1998	December 1998
Yes	39	39
No	44	44

Do not know	17	17
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January 1999

May 1999

Yes	45	38
No	38	44
Do not know	17	17

June 1999

October 1999

Yes	36	43
No	46	40
Do not know	18	17

December 1999

Yes	44	
No	41	
Do not know	15	

Source: Sifo Research & Consulting 1999

Figure 2: In a referendum on Swedish EMU membership, would you vote yes or no?

The survey is based on 1000 interviews during 29 Nov – 2 Dec 1999. All figures are percentages.

	Women	Men
Yes	32	56
No	49	33
Do not know	20	10
	Private Sector	Public Sector
Yes	48	37
No	40	47
Do not know	13	17
	Blue collar workers	White collar workers
Yes	31	57
No	53	31
Do not know	17	12
	Three largest cities	Rural areas
Yes	57	33
No	29	52
Do not know	14	15

Source: Sifo Research & Consulting 1999

Figure 3: Which aspects of the EMU-question do you feel is the most important to discuss? (More than one answer possible)

Survey is based on 1000 interviews during 29 Nov – 2 Dec 1999. All figures are percentages.

Currency issues, the Euro, monetary policy	14
Business and trade	8
Whether to participate or not	7
National self determination	5
Effects on Sweden	5
Negative to EU/EMU	3
The environment	2
Agriculture, animals	2
Positive to EU/EMU	2
The EU's relationship with other countries	2
Unemployment, employment	2
Taxes, social security	1
Equality, equity	1
Need for more information	1
National defence	1
A matter of principle: Sweden must join	1
Other	6

Do not know

56

Source: Sifo Research & Consulting 1999

After the introduction of the Euro in early 1999, the public opinion became more favourable to Swedish membership (see figure 1). At this time, polls indicated not only that those in favour outnumbered those against, but that this was result was statistically significant as well.

Several factors are likely to have contributed to this swing of opinion during early 1999. Firstly, as time has passed by the notion of adopting a common European currency, though appearing strange to many at first, has gradually become more accepted. Secondly, the introduction itself appeared very successful, and received considerable publicity in major mass media. Thirdly, an increasing number of trade union leaders and politicians expressed support for Swedish membership.

Nevertheless, many have yet to make up its mind, and swings in public opinion therefore easily occur. As media attention around the single currency petered out, and the Euro began to depreciate against major currencies such as the US dollar, support for the EMU dwindled once again. A low point was reached during the summer, but thereafter support again rebounded reaching almost the same level as in early 1999. This process is likely to have been driven primarily through increasing public support for the EMU among leading politicians. During the year 2000, support has again decreased, reflecting that a large group of people have volatile preferences..

The development of EMU support followed roughly the same pattern in Sweden as in other European countries. Support generally increased in early 1999. However, the average Europeans has a much more favourable opinion about the common currency, than the average Swede. While 64% of Europeans approved according to *Eurobarometer 50*, the same figure for Swedes was only 45%. The

figure for Sweden was however in line with the average of 44% for the four EU countries that have not adopted the common currency.

Concerning the Stability Pact it is noteworthy that it has generated very limited public debate in Sweden. When Sweden approaches a decision on adopting the single currency it is likely that it will become a topic of greater importance. Nevertheless, the overall Swedish macroeconomic policy stance has been in line with that professed by the Pact: consolidation of public finances and promotion of price stability. Sweden is one of a limited number of European Union member states with a public sector surplus, though the public budget has previously been very volatile over the business cycle.

1.2 Transparency and independence of the ECB

In Sweden there has been considerable debate on the transparency of EU bureaucracy and its decision making process – or perhaps more accurately the perceived lack of transparency. However, so far this has been used mainly as an argument against membership in the EU or the EMU, rather than as the starting point for a debate on the future of EU institutions.

Regarding central bank independence, Sweden itself has during the late 1990s, implemented considerable reforms. The Swedish central bank, which is the world's oldest, has traditionally been firmly within the control of the political system. Today, its top management is appointed on mainly non-political merits and for multiple year terms. Also, by law the central bank must have only price stability as its goal. This reform package has been firmly supported by most parts of the Swedish establishment and has generally met little resistance. There have been occasional criticisms, arguing that the central bank should show greater interest in the unemployment rate and that it is implementing an unnecessary tight policy. So far, though, this has carried little political weight.

The concept of an independent central bank pursuing the goal of price stability should be acceptable to Swedes, given that Sweden has already had such a

policy in place since the early 1990s. Nevertheless, it is clear that the independence of the ECB is considerably more pronounced than that of Sweden's central bank. It seems though that this has not greatly affected debate.

1.3 Financial Markets

Swedish financial markets generally responded positively towards both the lowering of the ECB interest rate in April and the hike in November. Against the background of lingering effects of the Asia crisis and sluggish European growth, the April adjustment appeared sensible. The November increase was also considered reasonable given indications of a build-up of inflationary pressures, manifested primarily in the faster than expected money growth rate. Villy Bergström, a member of the Governing Board of the central bank, said that the cut was helpful as “some of Europe's growth problem is due to low demand”¹. Liselotte Siewertz, Head of Spintab Markets, a leading housing credit firm, said in early November that the raise was positive and a sign of the determination of the ECB to keep inflation stable.

Leading interest rate analysts in Sweden have, however, been critical about the ECB being unnecessarily vague. The Swedish central bank has during the last few years adopted an explicit inflation target, and also continuously communicates its analysis of the economy to the financial markets. This is not the case with the ECB to quite the same extent, making it more difficult to analyse understand the ECB's view on the European economy, it is often claimed. There has also been some speculation whether the bank is unduly concerned with the euro's rate of exchange towards other major currencies, at the expense of the inflation target.

¹ Svenska Dagbladet, 10/4 1999.

Analysts are more convinced that they understand the US Federal Reserve's behaviour, even though it has adopted an official inflation target. In this case however a wealth of earlier research and experience is available to professional analysts. Obviously this not the case with a newly established central bank such as the ECB.

It thus appears that Swedish financial institutions have largely been happy with the actual policies perused by the ECB, but would welcome a greater transparency. That includes defining the bank's policy goal explicitly in terms of one variable only, i.e. inflation, and more clearly communicate its analysis and the models.

1.4 Institutional Positions

Seven parties are represented in the Swedish parliament. The Social Democrats, the largest party, currently governs with the support of the Left party and the Greens. The opposition is composed of the Conservative, Christian-Democratic, Liberal and Centre Parties.

In 1961 the then Prime Minister Erlander delivered a well-known speech at the annual congress of metal industry workers' union, which for a long time defined Swedish and Social Democratic policy towards the European Community. The speech maintained that membership in the Community was incompatible with Sweden's military non-alignment. The Social Democratic position was overturned in 1990, and Sweden applied for community membership in 1991.

Since the conservative and liberal parties had advocated Swedish community membership for some time, there was now a strong parliamentary majority in favour of membership. Also the major trade unions and the employers' federation were in favour of membership. Among the political parties, the Left

party and the Greens were against membership while the centre party was divided. The Social Democratic party and to a lesser extent the Christian Democratic party had significant minorities against membership. Following an advisory referendum in the late autumn of 1994, with a small but significant majority in favour of membership, Sweden joined what had then become the European Union (EU) in 1995.

The government appointed a commission 19 October 1995 to consider the consequences of Swedish participation in the third stage of EMU. The commission, lead by Professor Lars Calmfors, consisted of seven economists and presented its conclusions in October 1996². The commission considered the impact of the Euro on the overall economy, conditions for stabilisation policy and political consequences. The conclusion reached was that EMU membership would promote economic efficiency and Swedish political influence in Europe, but would worsen the conditions for a successful stabilisation policy. Therefore the Swedish economy should not join the third stage in 1999, but wait until its economy had improved.

At that time Sweden was still recovering from a severe depression in the early 1990s, and it was considered too dangerous to commit to a fixed exchanged rate. Also the labour market was singled out as an especially weak spot: Since the beginning of the mid 70s Sweden had escaped several severe cost crises due to rapidly rising wages, only by devaluating the currency. Before definitely fixing the exchange rate, Sweden therefore needed a more flexible labour market to compensate for the loss of monetary policy.

It should be noted that the major investigation into the single currency was lead by an economist, and analysed primarily from the point of view that Sweden should join if was economically beneficial, and otherwise stay out.

² State public investigations SOU 1996:158.

In a bill³ accepted by parliament 4 December 1997, the government proposed that Sweden should not join the third stage in 1999, but remain prepared to do so at a later date. The main argument for this policy was the lack of public support for the Euro, as documented by public polls and other indicators.

The “wait and see” approach has remained the official government policy to this day. Overall, there has been a shift towards a more positive attitude towards an EMU membership, and increasing number of political leaders have expressed a favourable opinion towards EMU membership.

Several political parties have long since taken a stance on the EMU issue. The two most market oriented parties, the Conservatives and the Liberals, are in favour, while the Left Party and the Greens oppose membership. Christian Democrats are tentatively in favour, while the Centre Party is sceptical. This almost precisely reflects the position taken in the earlier question of EU membership. When evaluating the positions taken by the different parties, it should be remembered that the EU is traditionally thought of as a right-of-centre friendly project. This is obviously different to the situation in the UK, another non-continental European country. The UK has a lower tax rate and a smaller welfare state than the European Union average. Conservatives in that country therefore have come to fear that integration may lead to the adoption of more interventionist policies.

The major question mark in regards of Swedish EMU policy was long the Social Democratic party. As is not uncommon in Swedish politics, the party could find a majority in parliament regardless of what position it takes. However, the party has delayed taking a stance for some time. Partly this reflected the conclusions reached in the Calmfors report mentioned earlier: there were considerable

³ Government Bill 1997/98:25.

concerns that committing to a fixed exchange rate could be dangerous in view of Sweden's history of rapid wage and price increases. An improving economy during the last few years has eased these concerns somewhat.

However, there is also a strong rift within the party, just as it was in the EU question. Although a majority of the party's leadership is in favour of joining the currency union, a more mixed picture emerges at a grass root level. There is a strong minority group within the Social Democratic Party that feels that the EMU will have negative effects on Swedish society. Ms Margareta Winberg, minister of agriculture and gender equality, has for instance publicised a debate article in Sweden's largest daily newspaper "Aftonbladet" (27 Dec 1999) with the title "With EMU back to 1920". The message is that adopting the Euro would undermine the position of women in Swedish society to such an extent that they would be worse off than in 1920, when women had not yet acquired the right to vote. The reason is that integrating with Europe will undermine the Swedish welfare state, which is thought to have benefited especially women, for instance by providing public sector jobs. The Social Democratic Women's organisation also decided that it is against Swedish EMU membership during January 2000.

According to Stefan Hejelid, an associate Professor of Political Science at Växjö University who has studied the Social democratic handling of the EMU issue, Prime Minister Göran Persson is not negative to a common currency as such. He has on the other hand harboured certain fears that it may eventually come to undermine Social Democratic redistributive policies. He has however, come to realise that the political price in terms of reduced influence in Europe is too high to pay. Especially during the upcoming Swedish 2001 EU presidency, the issue cannot be left totally open. Mr Persson therefore began to stress during 1999 that

the choice is only membership now or membership later – Sweden has not negotiated an exception to the Maastricht treaty as Denmark and the UK have.

However, there has been an unwillingness to create the impression that a pro-EMU stance has been forced upon the party members. Also, committing to the single currency may scare away voters to the anti-EU minded Left Party. The party leadership has therefore mainly waited for a shift in public opinion and within the party. Those in favour of the single currency – among them former Social Democratic Minister of Finance, Erik Åsbrink – have criticised this inertia.

Finally, the party's executive board unanimously declared its support for Swedish EMU membership on 14 January 2000, saying that it would "counter market forces". The Party's congress during 10-12 March 2000 proceeded to accept by a two thirds majority a statement in favour of Swedish membership and that the issue should be settled through a public referendum. Party leadership would have preferred not being obliged to hold a referendum, but was forced to accept this by grassroots opinion and EMU sceptics. A date for the referendum, which under the constitution can only be advisory, has yet to be settled. It is unlikely that it will be later than the autumn following the general election in 2002.

2. Legal Framework: A Note

As a part of the second stage of EMU, the independence of the Swedish central bank (*Riksbanken*) was strengthened. The central bank is regulated by Chapter 9 of the constitution and also by a special *Riksbank* law⁴. Changes in the constitution are regulated in Chapter 8 of the Swedish constitution. The basic requirement is that a bill proposing constitutional change must pass twice in parliament by simple majority, with a general election in between (note that the pending constitutional change is not an issue in the election). Since the present constitution came into effect in 1974 it has been amended after every general election.

The bill⁵ proposing change of the constitution was accepted by parliament the first time 4 March 1998 and the second time 25 November 1998, the latter time together with changes in the *Riksbank* law. The changes came into effect 1 January 1999. The opinion of the Swedish government is that it is necessary to adjust Swedish legislation only when it directly contradicts EU legislation, as the latter automatically takes precedent over national legislation. Nevertheless it is considered appropriate that the constitution reflects how the country is in fact governed. Two difficulties remain: Chapter 9 paragraph 12 which gives the Swedish central bank authority over monetary policy and paragraph 13 which gives the central bank the sole authority to issue notes and coins. The government has said this must be changed before joining the third stage of EMU, but that it is sufficient that the constitutional change is pending, i.e. not been accepted by parliament a second time⁶.

⁴ *Regeringsformen* and *Riksbankslagen*, Law 1988:1385.

⁵ Government Bill 1997/98:40.

⁶ Government Bill 1997/98:40, page 86.

Among the four EU countries outside the Euro zone, Sweden is a unique case: It lacks the formal opt-out enjoyed by the UK and Denmark, and unlike Greece managed to fulfil the economic convergence criteria. Ulf Bernitz (Professor of European Integration Law at Stockholm University) pointed out in 1995 that Sweden was formally bound to join the EMU. This appears to be the generally accepted view today in Sweden. Hence Sweden has granted itself an opt-out – arguably a bad example for present applicant countries which have not been given opt-outs. Nevertheless, in the government bill that laid out the policy of not joining the third stage in 1999, an attempt to provide a legal basis for Sweden’s decision is presented⁷. Sweden made a statement when EU membership negotiations opened on February 1, 1993. That statement was: ”A final Swedish position relating to the transition from the second stage to the third stage will be taken in the light of further developments and in accordance with the provisions in the Treaty”. The bill continues: “It was judged to be more appropriate to make a unilateral declaration than to try to get the same formal opt-out that Denmark and the United Kingdom have.”

The government’s position has also been that public opinion is more important than legal formalities. During April 2000 both Romano Prodi and Anna Diamantopoulou have made statements in Swedish media to the effect that regardless of the legal situation, the opinion of the people must be the decisive factor. It is also important that prior to the 1994 EU membership referendum the Government repeatedly stated that EMU participation would be decided at a later stage, after consulting the people. The legalistic argument, although technically probably correct, is therefore politically dead.

⁷ Government Bill 1997/98:25, page 4. Full text available at the following address: <http://finans.regeringen.se/euro/language/engelska/bills/bill.htm>.

The earlier commissioner for EMU and economic policy Yves-Thibault de Silguy did criticise the Swedish failure to adopt the Euro. An indication by the Swedish Prime Minister that EMU was a “shaky” project provoked some anger. De Silguy’s successor, Pedro Solbes, has adopted a softer tone, and has been content to express a wish that Sweden will join soon.

At present the trend appears to be towards accepting a greater degree of divergence in the pace of EU integration among EU member states. This increases the likelihood that continued Swedish unwillingness to commit EMU membership will be tolerated at least for the time being.

Nevertheless, Sweden remaining outside the Euro area does pose certain problems for the EU. In negotiations with prospective future member states in Central and Eastern Europe, the EU standpoint is not to allow exceptions and that agreements must be followed. The fact that Sweden has been able, so to speak, to get away with not strictly following the Maastricht treaty could potentially be viewed as establishing a precedent for other countries.

The EU presently stresses that all future members must strive to reach convergence criteria and join the EMU. There has been an unwillingness to extend the kind of formal exemptions given to UK and Denmark to other countries. If some country were to refuse, once it had entered the union, and refers to Sweden an interesting situation would clearly emerge. It is not immediately obvious what would legitimise Sweden’s non-compliance and the demand for compliance by other countries. Nevertheless this situation will not emerge for some time yet, and it is quite likely that by the time the EU is enlarged the next time, Sweden has already adopted the single currency. It is therefore quite possible that the EU’s current pragmatic attitude towards Sweden will prove the least problematic in the long run.

Finally, what might put Sweden's situation in an entirely new light is if the UK was to join. Whether the UK joins or not is obviously an issue of vastly greater importance to the EU than Sweden's status. With UK in the EMU, the spotlight would be put on Sweden and Denmark, and it is highly likely that both those countries would soon follow suit. However, as things are developing in Sweden at present it is not unlikely that Sweden will join the EMU before the UK.

But before joining some legal alterations are necessary. Sweden at present does not fulfil all its legal obligations regarding the achievement of economic and monetary union, as specified in Article 109(j) of the Treaty and the Statute of the ESCB. This is pointed out, for instance, in the March 1998 convergence report of the Commission.

The most important aspect of this is that the present Swedish constitution specifies that monetary policy and printing of money is the sole responsibility of the national central bank. This must be altered if Sweden is to be eligible to adopt the single currency. In practice, changing this will also imply alterations of several basic laws, though this of secondary importance.

Technically altering the constitution is a minor issue. All it takes to change the relevant paragraphs are two decisions with simple majority in parliament with a general election in between. However, given Sweden's wait and see approach to the single currency, no action has been taken in this regard so far. The next election is in 2002 and the following in 2006. That means that if the changes are to formally come into effect before 2006, the first decision in parliament must be made prior to next upcoming election.

2.1 Euro related legislation

2.1.1 Accounting in Euro

There is nothing that stops a Swedish firm from conducting its business in Euro. However, regarding accounting there is legislation requiring use of Swedish currency. For some time it was discussed whether limited liability companies should be allowed to have its official accounting denominated in Euro. Many major government agencies and business agencies approved this, and it was expected that the government would present a bill to parliament during mid 1999. However, it was delayed, but finally presented in November 1999 and accepted in March 2000. Accounting must in its entirety be in either Euro or Swedish kronor. Taxes are always to be paid in kronor, and for this purpose special conversion tables are to be used. This will mean that the government takes on a currency risk (as long as there is no fixed exchange rate between Swedish currency and the Euro). The government believes that it will not be systematically disadvantaged by such an arrangement, but stands ready to reform the system if that would turn out to be the case.

The decision to switch to accounting in Euro must be made by the shareholders' meeting, and can be valid from 1 January 2001 at the earliest. Taxes will still be paid in Swedish kronor, and be based on the annual average exchange rate between the Swedish currency and the Euro. In the case that Sweden adopts the single currencies this legislation will of course become redundant, and possibly that is why the implementations is delayed.

2.2 Other legislative areas

During 1996 the government initiated the project "Practical Euro preparations", which was to make Sweden prepared to join the Euro zone. One part of this work was a comprehensive listing of needs for legislative change as a result of

the introduction of the Euro. However, this work slowed down after the “wait and see” strategy was formally adopted by parliament in December 1997. Roughly, there is today a good overview of the needs for legislative when result of Sweden adopting the Euro. The bulk of the change necessary will be routine adjustments, such as re-specifying amounts presently expressed in terms of kronor.

Regarding a possible future conversion of government debt into Euro, two methods are allowed in the Maastricht treaty: on the basis of individual holdings or for each outstanding debt instrument. The national debt office has argued that the former alternative is more practical. However this alternative will require special legislation. This is unlikely to cause any difficulties, as it is a standard procedure carried out by all Euro countries.

In the case of delay of Swedish adoption of the single currency, it might be necessary to deal with a situation of the Euro functioning almost as a parallel currency. This could for instance become the case if the major multinationals were to utilise the new legislation allowing them to have their accounting into Euro. It is not impossible that major corporations would then also start billing subcontractors in Euro.

The tax authority especially has expressed concern that it would be difficult to deal with tax payments in two different currencies with a floating exchange rate.

There is also some debate about whether a situation with a parallel Euro currency would create a need for additional legislation. So far, this debate has not produced concrete demands for legislative action. It is likely that the use of the Euro in Sweden will become a practical issue before 2002.

3. Some Trends towards Spill Over

Adopting a new common currency will have effects on numerous policy areas, reaching far beyond monetary policy. One of the most obvious areas is the other major instrument of stabilisation policy, i.e. fiscal policy. According to the well-established Mundell-Fleming model, fiscal policy is ineffective under floating exchange rates, but effective under fixed rates.

To the extent that ECB monetary policy is not well suited to Swedish conditions in the future, for instance due to an asymmetric shock to the Swedish economy, the main macroeconomic stabilisation tool available to policy makers is fiscal policy. It should be noted though that the freedom to use fiscal policy might to some extent be illusory for a small country such as Sweden. Even in a time of recession, it may be difficult to try to stimulate the economy by means of expansionary fiscal policy if major member countries do not do the same. Fear of a build-up of inflationary pressure could scare away investors. Also Sweden has, as a part of a budget reform process, introduced legislated spending caps, which in principle could create difficulties for a government wishing to pursue discretionary fiscal policies.

As many other countries, Sweden has carried out a major program of fiscal consolidation during the 1990s. In Europe this trend towards fiscal prudence has to large extent been driven by the need to fulfil the Maastricht convergence criteria. However, it would no doubt be incorrect to see the EMU as the only driving force, as the pattern has been obvious also in North America. Indeed growing government indebtedness became a pressing issue already after the first oil crises in the early 1970s, and by the 1990s there was finally enough momentum in the political system to tackle the issue even if it entailed painful measures.

In the case of Sweden, it is clear that irrespective of the EMU project there was an urgent need to reduce the massive deficits caused by the severe recession of the early 1990s, which was undermining investor confidence. Nevertheless, the government has frequently referred to the convergence criteria as a reason for implementing the austerity program.

Today, when there may still be sound reasons to continue a policy of fiscal prudence, but no immediate pressure to do so, the convergence criteria may have some role in keeping the government to resist attempts to increase spending. During 1999 and 2000 the Minister of Finance Mr Ringholm has expressed concern over strengthening demands for new expenditure.

The continued integration of the European economies creates a need for harmonisation in many different areas. The effect of adopting the Euro is likely to heighten that need, but without being revolutionary in most cases.

An excellent case of this is tax reform. Sweden finances its extensive welfare state by taxes that are reported to be the world's highest. During the last few years there has been an intensified discussion about whether this state of affairs will prove unworkable in a globalised economy. There is further an ongoing discussion on tax harmonisation within the EU, and for Sweden this is more likely to entail downward rather than upward pressure on tax rates. Nevertheless, adopting the single currency is unlikely to have a dramatic impact on the situation. The Prime Minister has taken the position that the Euro will not have a major impact on these issues.

BRITISH REPORT

Robert Kissack*

1. Introduction – The European Parliament Elections (June 1999)

The British electorate, like those of every other European Union (EU) member, voted in June to elect members to the European Parliament in Strasbourg. Britain is one of the four EU members outside the ECU - the euro-zone under the direction of the newly formed European Central Bank (ECB), and consequently the election campaign was principally fought upon the issue of adopting the euro in the absence of an effective Labour (and Liberal Democrat) campaign. 'Euro-sceptics' argue against future use of the euro and belong to the UK Independence Party and the Conservative ('Tory') Party. Pro-Europeans tend to belong to the Liberal Democrat or Labour Parties, although there is a small but influential minority of Conservative MPs who favour converting to the euro currency. Despite the two distinct opinions within the political arena, little genuine debate between the two sides has taken place. Each side has identified strengths and weaknesses in the arguments that substantiate their position, and stick dogmatically to them. Pro-Europeans say that the euro will improve the efficiency of the single market, and Britain should be participating fully to prevent it being economically disadvantaged by exchange rate fluctuations between the euro and the pound. They suggest that Britain should take the initiative and join soon, rather than stubbornly wait until Britain is economically damaged by non-membership before joining. Their assertions for early entry use the wisdom of hindsight gained from Britain's relationship with the EU predecessors, the European Coal and Steel Community (ECSC) and the European Economic Community (EEC) but in essence believe membership is an

* *Federal Trust - London.*

inevitability forced by economic necessity. Alternatively, Euro-sceptics regard the ‘surrendering’ of the pound and the handing over of control of monetary policy from the Bank of England in London to the ECB in Frankfurt as a mortal blow to British sovereignty. The pound is taken as a symbol of British autonomy against the prevailing political current that flows towards the centralised nightmare of the right, the ‘United States of Europe’. The pro-Europeans have claimed economic reason to further their cause while the euro-sceptics use nationalist rhetoric to stir up sentimental feelings. Consequently, it has become very hard to find a well reasoned and unbiased presentation of the relevant economic and political factors. The lack of clarity was apparent in the election results. The Conservative Party won the largest proportion of the vote, (35.8%), campaigning under the slogan ‘*In Europe, not run by Europe*’. The sceptics would therefore appear to hold the advantage, until one considers the turn out was less than 25%. These two statistics succinctly demonstrate the current climate in British politics. The emotional, nationalist rhetoric used by those who associate defending the pound with standing defiant on the White Cliffs of Dover struck a cord with a small portion of the population, who vigorously campaigned from that perspective. The majority of the electorate remained unconvinced by this argument, but were equally uninspired to vote for the advocates of an unstoppable economic process.

This thumbnail sketch of the political situation highlights two points. The first is that British politicians have suddenly taken notice of the vocal segment of the society who are hostile to Europe. The June election results have signposted the direction the parties shall take over the coming year, galvanised in the last month during the political parties’ conference season. The second point reflects a theme which will be reiterated throughout this report. The debate over the euro and by default, about the EU, is the major fracture both *between* parties and *within* parties. The Liberal Democrats are the most harmonious, the

Conservatives are the most divided and Labour lie somewhere in between. A pro-European group has formed a cross party lines - Britain in Europe (BiE) - that is arguing the case of general EU membership but focusing more heavily on economic concerns. BiE remains locked into the prevailing paradigm where pro-Euro arguments centre upon economics, while critics focus on the political issues of sovereignty and tradition. Both sides are preparing for the referendum scheduled for 2002, and are sticking to their rehearsed arguments rather than engaging in an open discussion. Until an open debate takes place in which *both* sides talk about politics *and* economics, the prevailing paradigm will not be altered and vicious circle shall be perpetuated. This point shall be returned to later, but for the moment let us concentrate on the June election.

1.1 Direction in the Coming Year

As mentioned above, the results of the European Parliament election have defined the political agenda in Britain over the last three months. Early Autumn is traditionally the time in which all the major political organisations (parties and trade unions) hold conferences. The voice of scepticism has been heard and duly recorded, (expressed most forcefully in the UK Independence Party and a little more mildly with the Conservatives), as was evident in the manifestos unveiled at the conferences.

figure 1: European Election Results June 1999 (UK excluding Northern Ireland)

PARTY	PERCENTAGE OF VOTES	SEATS
CONSERVATIVE	35.8	36
LABOUR	28.0	29
LIBERAL DEMOCRAT	12.7	10
UK INDEPENDENCE	7.0	3
GREEN	6.3	2
NATIONAL (SCOT&WALES)	4.5	4
OTHERS	5.7	0

SOURCE: THE ECONOMIST JUNE 19 1999

The election result's strongest influence was felt in Blackpool, where the Conservative Party held its conference. Two years of confusion have reigned since their defeat in May 1997 by Tony Blair's New Labour, and the European elections showed the first signs of a revitalisation in the party's fortunes. It is ironic that the most anti-European mainstream party performed well during the European elections. The leader of the party, William Hague, has progressively strengthened his line against Europe, suggesting that he wanted to re-negotiate the Treaty of Rome to allow all future EU legislation to be adopted by individual member states as they choose rather than uniformly. He sees this approach as being the most suitable method for tackling the issue of enlargement, as 'wider rather than deeper'. The former Prime Minister, Lady Thatcher, remarked that 'In my lifetime all the problems have come from mainland Europe and all the solutions have come from the English-speaking nations across the world.'⁸ However, in a reaction against the party's hardening towards Europe several

⁸ *Financial Times*, London, 6.10.99. page 6.

prominent senior Tories have stepped forward, including Chris Patten (EU Commissioner for Foreign Affairs and former Party Chairman), John Major (former Prime Minister), Michael Heseltine (former Deputy Prime Minister) and Ken Clarke (former Chancellor [Finance Minister]). Their common fear is that the party is making itself un-electable and is driving itself further from its traditional role as the internationalist party in British politics - one should not forget that Winston Churchill was instrumental in founding the Council of Europe and Edward Heath took Britain into the EEC. It has been suggested that one explanation for the Tory slide towards an anti-Europe nationalism is that a party out of power has more freedom in writing a manifesto than a party in power. This is undoubtedly a relevant point, however the majority of observers agree that the party leadership is desperate for unity and is willing to look for it anywhere. The gravity of the situation was highlighted shortly after the conference when pro-Europe Conservative MPs hinted that they might defect *en masse* to the Liberal Democrat Party if the present line on Europe is maintained. The Europe-Question is cutting new divisions in British politics.

The Liberal Democrats lie on the opposite extreme. They campaigned in the June elections for a definite date for a referendum on joining the euro, and have consistently advocated stronger ties with Europe. They polled 12.7% of the vote, much lower than in the last General Election, but celebrated the introduction of Proportional-Representation by winning 10 seats, 8 more than in the previous parliament. The party has criticised the government for not being active enough in promoting a pro-European agenda, allowing the Conservatives to gain the upper hand in their campaign against Europe. This criticism reflects the difference between the Liberals who debate Europe as an economic, political and social issue, and the current government that concentrates only upon the economic aspects. Britain will hold its referendum upon joining the euro when the government decides that the five economic convergence criteria have been

met, a strategy referred to as 'wait and see' (See appendix 2 for the conditions). The Liberal Democrats rightly criticise this approach as being too passive in comparison with the assertive message sent out by the anti-Europe parties.

The Labour Party is regarded to have been the loser in the European election. They received a smaller share of the votes than in the General election mostly because they failed to motivate their supporters to vote. Despite a poor performance in the June elections, the popularity of the party remains high, at around 50%. This suggests that the popularity of the Tony Blair is based on his party's performance in many areas, such as the buoyant economy, the programme of social reform and his leadership in the Kosovo War. However, Blair is a supporter of the euro and is determined to win the next General election to enable him to hold a referendum on the euro soon afterwards. The Labour Party is trying to prevent the euro-question becoming the dominant issue in British politics to do two things. Firstly it must prevent itself becoming unpopular by being 'tarred' with the pro-euro brush, and secondly it must work towards reversing popular distrust of the euro and actively support it. It is therefore little wonder that Blair has chosen to use economic arguments to support Britain in Europe. It emphasises pragmatism over idealism and allows him to distinguish between his political agenda which is clearly popular and an autonomous economic agenda concerned with the euro. Blair has two aids which add to his credibility in taking this option. The first is the macro-economic policy of the Chancellor (Finance Minister) Gordon Brown, that has lead to sustained growth and long-term confidence in British businesses. The second is the reputation of Brown himself, who was recently made chairman of the IMF International Monetary and Finance Committee, a position of prestige in the world of international finance. Blair's approach to the euro-question is to separate it from his domestic political achievements by regarding it as an economic issue alone. It is a logical procedure to follow, but as the Liberal

Democrats have argued, it could eventually prove too rational against the roused emotions of the anti-Europeans.

Finally, the representatives of business (the Confederation of British Industry [CBI]) and labour, (Trade Union Congress [TUC]), have recently held conferences. The two have been traditionally antagonistic to one another but in recent years have become more co-operative with each other and shall be participating with the government in another conference dedicated to 'Knowledge Industries' in the near future. The armistice has been brought about by their shared acceptance of the inevitability of Britain joining the euro. It is natural that business, having to plan investment strategies many years in advance have been considering the British position for some time; it is also recognised by the TUC president John Monks that membership of the euro-zone will propel Britain to adopt the industrial-relations practises found elsewhere in Europe, implying a role of the TUC in public policy issues, such as macro-economics and social affairs.⁹ The CBI and TUC represent a pragmatic view on the euro which is shared by the financial sector based in the City of London. All assume that Britain will join the euro at some point in the next 2-3 years - and are the least ruffled by the recent election results because they have made investment plans contingent upon it. In certain respects, one could say that it is now 'up to the politicians' to convince Britain that joining the euro is the right thing to do. But leaving it 'up to the politicians' risks placing too much emphasis on current whims instead of presenting considered opinions to the public. It also risks perpetuating the dominance anti-euro campaigners instead of encouraging government, industry and trade unions to argue their case together.

1.2 Summary of the Present Situation

⁹ John Monks was interviewed by the *Financial Times* on 2.9.99.

The results from the June European elections have galvanised the political debate in Britain around the issue of Britain's role in the EU and the single currency. This is the prism through which British politics must be viewed, both between and within parties. The traditional perspectives of left and right, a socialist programme of nationalisation and the right's nationalist/conservative (i.e. Burkian scepticism towards change) have found a common adversary in the European Union. On the other hand, centre-politics have moved towards embracing the European Union's ideals of increased economic harmonisation coupled with an explicit social programme to promote civil freedoms, liberty and prosperity. The Labour Party has more successfully rid itself of the 'old' left than the Conservatives have of their traditional perspective of economic but not political union.¹⁰ The Conservatives have sought to establish a distinguishable distance between themselves and Labour by moving further to the right, leading them to the inevitable position of advocating an end to European integration. This has led to more moderate Tories joining Labour and Liberal Democrats in a cross-party pro-European campaign organisation Britain in Europe. The political debate over euro-zone membership has been characterised by a series of dichotomies - assertive, patriotic, nationalistic and political in nature from the sceptics, while being passive, complacent and predominantly economic-markets determined by its supporters. The risk of this campaign strategy is that it makes the EU look like nothing more than an economic opportunity Britain is obliged to take, rather than a political community that strives for social goals that Britain should share. By continuing on this tack the sceptics are justified in arguing that European integration represents an infringement on British sovereignty because *both* sides

¹⁰ This point was picked up by Tony Blair in his recent speech at the Labour Party Conference (*The Guardian* 29.9.99) where he criticised "forces of conservatism" on the left and the right as the hindrance towards a better Britain.

consistently fail to attribute a social dimension to the EU. It could be said that the pro-European lobby are at present their own worst enemy by refusing to explain that the EU is about contributing to a vibrant political community - their narrow economic arguments feed the sceptics the diet they depend on. Without embracing a positive view of Europe, sceptics will remain convincing when they claim facelessness characterises Europe to its core.

2. Political Aspects

2.1 Public Opinion

Public opinion in Britain is heavily swayed by the negative press which surrounds the European Union. This can be seen in the monthly opinion polls listed in Appendix 1. Prior to the June elections the euro was enjoying its highest level of support in Britain, peaking at a 35% figure who said they would vote 'yes' for membership in a referendum. This figure declined during the summer, and is only starting to increase again in the last two months. The figure of 28% in November is still less than in March. Reasons for this slide and decline could be the worsening press surrounding the depreciation of the euro during the summer and its revival as BiE begins to campaign. An interesting point to note is that the number of undecided voters, ('Don't Know') has remained constant, which suggests that the decline in popularity of the euro is due to supporters becoming critics, rather than a rise in the number of people expressing an opinion. The dissatisfaction with the euro betrays a more general uneasiness about the EU. Political commentaries are usually neutral or critical and rarely positive towards the successes of the EU. This bias in reporting is reflected in opinion polls, where the majority remain unsure or relatively indifferent to the EU, with minorities for and against on either side. The European election results demonstrate this trend in the high level of apathy

among voters. What are the reasons for this low level of public concern over Europe?

The main reason for the low level of public interest in the EU is that the public judges it through its coverage in the media, which in turn focuses on a few popular issues. Instead of a detailed survey of the performance of the EU in areas such as laws protecting worker's rights (the Social Charter) or the Common Foreign and Security Policy (CFSP), all attention is concentrated upon the euro and corruption. These two issues re-iterate the stereotype that the EU is an inefficient bureaucracy filled with 'grey suits' that want to homogenise all aspects of ordinary life. The public's opinion of the EU is determined by a few high-profile stories.

The euro debate is being held on an uneven playing field. The two sides consistently fail to fully debate all the issues relevant to helping an educated electorate decide for itself. One side talks of losing sovereignty and autonomy in the world, yet is unsure what troubles foreign currency speculation might have for the pound, while the other pays lip-service to notion of 'pooling sovereignty' while concentrating on the number of people employed in Britain in companies that export to the EU. The greatest danger with this approach on the political level, (I shall discuss the economic issues in the following section), is the implication that economic determinism is a stronger force in deciding our future than political will. The purpose of this approach is to neutralise the passionate rhetoric of euro-sceptics with the cold reason of market determination - but it risks performing the opposite - neutralising the politics of the pro-euro camp by making them appear subordinated to economic forces. Until now the euro debate has been dominated by agitated euro-sceptics frantically defending British sovereignty. Until the pro-euro camp confront the claims of their opponents head on, and re-politicise their campaign, they will remain in a

defensive position. Their defensiveness has naturally made them weaker given the highly emotional rhetoric plied by anti-Europeans.

A second issue frequently regarded by the public as a typical characteristic of the EU is cited the level of cronyism in the bureaucracy. Britain (rightly or wrongly) prides itself on a domestic civil service that epitomises honest public service. The resignation of the Santer Commission due to the exposure of nepotism within the European Commission reinforced the public perception of dishonesty in the machinery of the EU. If Britain is to join the single currency, the performance of the new commission under Romano Prodi must be seen by the British public to represent an improvement over its previous ways. The new commission includes the former Labour Party leader Neil Kinnock as vice-president and commissioner in charge of reform. Kinnock's reforms must succeed in two ways. He must bring about change in the commission, and he must present the British public with the evidence for his success. Kinnock's presence in the collective memory of the British electorate remains strong and this should count in his favour in trying to banish for good the impression that 'Brussels' is synonymous with 'inefficient bureaucracy'. At the time of the referendum, the reforms to the EU may be as important as the performance of the euro itself in convincing the electorate to agree to the single currency.

Serious political debate has taken place on the fringes. One of the most interesting contributions made in the last year has been Professor Willem H. Buiter's paper titled *Alice in Euroland*.¹¹ Professor Buiter raises the issue of transparency and democracy in the decision making apparatus of a central bank. He compares the procedure of the Monetary Policy Committee of the Bank of England (of which he is a member) with the Bank of Japan, the U.S. Federal Reserve Board and the ECB. In all cases bar the latter, the minutes and voting

¹¹ *Journal of Common Market Studies* 1999.

records of all meetings are published between two and eight weeks later. Professor Buitter argues that the transparency of this procedure is necessary in an open, democratic society and acts to reassure the citizens that important decisions concerning monetary policy are made with the best intentions. He then goes on to argue that this system is better at coping with the consequences of economic failure, since it leaves open to scrutiny the decisions which with hindsight were proven wrong. From a position reminiscent of Karl Popper's *Open Society*, Buitter argues that the legitimacy of institutions such as central banks in a democracy can only come through transparency and the acknowledgement that if mistakes occur, it is acceptable in a situation that permits scrutiny of the errors made in order to prevent them reoccurring. Professor Buitter asserts that political openness builds stronger political units than secretive, paternalistic systems.

Professor Buitter contrasts this to the current situation at the ECB. The minutes of committee and council meetings are not published for fear that national bank representatives would not be able to take decisions in the interest of the euro-zone when it conflicted with national interests for fear of domestic retribution at the published evidence of their 'disloyalty'. Professor Buitter considers the likely scenario in which the euro-zone begins to perform asymmetrically, when a single exchange rate cannot be simultaneously appropriate for all areas within the zone. During such a period, the political strains in the euro-zone would drastically increase, possibly ending in a crisis of legitimacy. Buitter argues that openness - not secrecy - is the answer because it allows for an enlightened discussion to assist the ECB during the crisis and it allows for the most rapid explanation on why things went wrong so as to prevent them being repeated. The ECB cannot be legitimate in the eyes of the citizens of Europe, accustomed as they are to democratic values, until it follows the example of other central banks.

This article exemplifies the balanced debate over the euro that is woefully absent from British politics at the present time. It is an insightful piece of work that critiques the EMU project with the purpose of improving them. It contributes to our understanding of the ECB and demonstrates the link between democracy, transparency and legitimacy while applying them to the euro-debate. Professor Buiter asks whether it is right to abandon a relatively transparent system in favour of a secretive one and answers by saying it is, providing one attempts to change it.

Public opinion is therefore muted in its indifference and vocal in its frustration with the euro. Around the fringes of public opinion, there is a lively and informed debate taking place, but this does not seem to be transposed into the wider social arena by the media. However, I think it is apparent from the general position made throughout this report that this situation must change if the pro-Europeans in politics wish to convince the public of their beliefs.

2.2 Institutional Opinion

‘Institutional opinion’ shall be taken here to refer to leaders of business, the financial community of the City of London, the civil service and trade unions. They share a tendency to take a pragmatic approach to euro-membership, regarding it as an inevitability which they must prepare for. The Confederation of British Industry and The City of London realise that their long-term competitiveness is dependent upon Britain joining the euro. Many have made contingency plans to make the period between a positive referendum result and membership as short as possible through good preparation and a careful monitoring of the other euro-zone countries. The adoption of the euro would effect all government departments. The Treasury and the Department of Trade

and Industry (DTI) have the most complicated agendas, the former supervising the transition from one currency to the other and the latter preparing all business - from corner-shops to multinationals - for the change-over. Other departments will follow the rest of Britain in re-accounting in euros. The Civil Service therefore must be prepared in the eventuality that a referendum has a positive vote and to facilitate as rapid a transition as possible.

The balanced nature of institutional pragmatism stands in contrast to the public's fanatical political lobbying on a single issue found increasingly within developed states. Britain suffers from the syndrome too, found in the aftermath of a move towards centre politics and the abandonment of the dominant traditional ideologies of left and right. Single issue politics takes over as holistic ideological projects become less popular. Lobby groups thrive by focusing the political energy previously expended over a wide range of issues into one, and by projecting the energy into the political arena. The euro is such an issue in Britain. A mobilised minority is vigorously campaigning for one issue which typifies the disenchantment frequently found on the fringes of centre politics. Political parties are mesmerised by the brightness of the anti-euro campaign in the midst of a dull counter-position. Institutions differ by being more pragmatic and less prone than political parties to being dazzled in this manner.

2.3 Analysis

The public opinion of the euro cannot be separated from their general perception of the EU, implying that public consent to joining the euro will be influenced by the overall performance of the new commission. The debate is being steered at the present moment by the euro-sceptic minority through their single-issue lobbying. Meanwhile, many institutions are steadily preparing to join the euro without entering into a discussion over it. The discussion which is being held -

such as the essay by Professor Buiter - deserves to be heard more widely, across Britain and across Europe. As he says in his paper, the electorate are highly capable of understanding debated issues, and a transparency to the pros and cons of membership will provide more fruitful and inspire a much higher participation than the soundbites that is currently engaged in.

3. Legal Aspects

3.1 Procedure for Britain's entry into the euro

In October 1997 the Chancellor of the Exchequer, Gordon Brown, presented Parliament with his euro-membership criteria. These five points were decided by the Treasury to be the issues by which Britain's case for membership should be considered and are listed in Appendix 2. The EU has a similar set of criteria, numbering four, which it shall consult as Britain (or any other non- euro EU member) presents itself as a candidate for membership. Once Britain decided to join the euro through holding a referendum, the Government would notify the Council of Ministers of its intention. The European Commission and the ECB would begin monitoring the convergence criteria (price stability, sustainable public finances, converging long term interest rates and exchange rate stability). ECOFIN would decide if the criteria had been met, and present a recommendation to the Council of Ministers, who would take the final decision through a qualified majority vote. During the convergence period, the pound would become the effective fiat denomination of the euro, (as the euro-zone is presently doing) until substituting sterling tender for euro notes and coins. The Bank of England, the Treasury, other government departments and private companies are already preparing for the change by drafting change-over plans and carefully monitoring the process elsewhere in the EU. There are two sets of legal issues to consider, at the British level and the European level. I shall briefly describe the European legal processes to which Britain must adhere before looking in detail at how Britain intends to proceed.

3.2. The EU's entry process

If Britain is to adopt the euro it must accept the stated procedure of the 11-euro states. The procedure was laid out in the *Maastricht Treaty and the European Communities (Amendment) Act 1993* under Protocol 11, and is in four stages. The first stage is Britain's *notification* to the EU that it intends to join - the method by which a decision is reached shall be described in section 4.3. This amounts to agreeing to move to stage three of economic and monetary union as laid out in the Maastricht Treaty, which the United Kingdom of Great Britain and Northern Ireland is not obliged or committed to without a separate decision to do so by its government and parliament. The EU Commission and the ECB would then begin an *assessment* process on whether Britain had converged sufficiently with the euro-zone to facilitate entry. Four criteria would be used; price stability, sustainable public finances, convergence of long-term interest rates and exchange-rate stability against the euro.¹² Britain would also have to pass legislation to change the statute of the Bank of England in compliance with the Maastricht Treaty's blueprint for National Central Banks. The reports would be considered by ECOFIN, the committee of European Finance Ministers, who would make a recommendation to the European Council.

Stage three is the *decision* by the Council after consultation with the European Parliament, and assuming that there was a qualified majority in the Council, the proposal would be returned to ECOFIN who would *set an entry rate* for sterling. This rate would become the rate that Britain adopts to convert its national accounts into euros. The figure would require a unanimous agreement by the participating member states of the Council and the UK. These are the legal

¹² These details come from the HM Treasury publication *Outline national changeover plan* p.12.

requirements made of Britain by the EU - let us turn to Britain's current legal situation and what it must do.

3.3 Britain's legislative obligations

The first stages along the road to euro-membership have already been taken. The reforms to make the Bank of England independent described in section 2.2 are necessary to comply with the Maastricht Treaty. Further revisions would have to occur upon entry, such as the removal of the bank's right to set interest rates, (which it would cede to the ECB), while it would retain responsibility for the national debt and monitoring national banks. However, before this could take place, the first stage would be for the government to pass a bill in parliament to hold a referendum. Once this had been passed, the campaigning by both sides would begin. Assuming that there was a positive answer, the government would officially submit notification to the EU. Since Britain must demonstrate stability against the euro for a sustained period of time, it may be advantageous for Britain to join the ERM2, the successor to the Exchange Rate Mechanism, which currently only Denmark and Greece belong to. The government must then move to convert all of its finances, both the current accounts and the bonds it issues, into the euro. It must also change its international treaty obligations and legislate for the use of the euro in the territories and dependencies of Britain.

3.4. Analysis

The short length of this section reflects the fact that Britain has yet to implement many of these acts and they remain dependent upon a positive response in a referendum. Britain is certainly preparing itself discreetly and looking to the euro-11 to learn from their experiences. The Treasury expects it to be possible

to reduce the 80 months scheduled between the 1995 Madrid Summit and the 2002 introduction of notes and coins for the original 11 members to 40 months, from a decision to join to holding a referendum (4 months), to joining (24-30 months), to circulating the currency (6 months) to end.

4. Economic Aspects

4.1 Marking the ballot paper with the Invisible Hand?

The pro-euro campaigners, unified in the *Britain in Europe* campaign, have claimed the high-ground over economic issues. While this undoubtedly counts in their favour, it does not mean that their work is done. They must strive to win the political arguments too, for fear of placing too much emphasis on economic reasoning and too little on emotional sentiments. A brief glance at the *Britain in Europe* press pack distributed during their launch on 14 October 1999 contained the following information:

- More than half of Britain's trade is with the rest of the EU
- 3,500,000 British jobs depend on trade with Europe
- With 370 million people, the EU is the largest consumer market in the world
- Thanks to the EU, British workers enjoy a maximum 48-hour week¹³

The focus is almost exclusively on economic issues and even the last point which deals with EU social policy focuses on the work-place. However, concentrating on economic issues alone does not make the case for Britain's entry to the euro-zone unassailable. The analysis has been broken down into three sections, macro policy, external projection and social policy. Common taxation policies throughout Europe currently only directly effect Britain through the EU Commission's role as trade negotiator, which has been the case

¹³ *Britain in Europe* launch video presentation (14.9.99).

for many years. Direct tax harmonisation policies may follow as and when Britain joins the euro.

4.2 Macro-economic policy

The first criteria for Britain's entry into the euro-zone is convergence between the interest rates in Britain (currently at 5.5%) and the euro-zone, (currently at 3%). The difference between the two rates is caused by Britain being out-of-phase with the economic cycle of the euro-zone economies. Britain went into recession in 1990-1991, with the situation worsening with its ejection from the Exchange Rate Mechanism (ERM) in 1992. As interest rates fell, so to did the value of the pound, falling roughly 30% against the Deutschmark. Low interest rates and a competitive pound resulted in an export-lead recovery which has been sustained over the last 6-7 years through careful fiscal policies, and has been helped further during the last two years by an operationally independent Bank of England setting the interest rate (see section 2.1). By contrast the euro-zone maintained a steady course much longer than Britain, but ran into difficulties during 1995-96¹⁴ as the costs of German reunification financed by government borrowing finally caught up with Germany's economy in the form of high interest rates. The inefficiency of the ex-GDR infrastructure also damaged Germany's economy and as it slowed down, its trading partners were also hurt. Thus Britain and the euro-zone remain in different stages of the economic cycle and until they realign, Britain cannot be incorporated.

¹⁴ A difficulty arising here is that the Euro-zone consists of a variety of differently performing economies, so generalisations tend to be hard. However, Germany, Italy and France make up the largest proportion and at the present time, while France is enjoying prosperity, Germany and Italy lag behind, thus causing the ECB to maintain low interest rates in the interest of these economies.

It is vitally important that the two rates are as close as possible when Britain enters the euro-zone, so that investment schedules are not disturbed as the ECB rate is adopted. A heavy fall in interest rates at the time of entry would cause the British economy to expand rapidly, as savings decreased and consumption increased. Supply would not increase quickly enough to accommodate the increase in demand for goods and services (given the delay in restructuring production schedules and introducing new investment) thus leading to inflationary pressures. Reduced interest rates could also lead to a property boom fuelled by the availability of low interest mortgages. An increase in the average price of property leads to an increase in the calculated level of equity and can lead to increased investment in stock markets. These examples are just some of the ways inflationary pressures could be triggered, possibly driving up wage demands and leaving British labour too expensive to compete with other euro-zone economies. Furthermore, the removal of the exchange rate as a mechanism for returning the economy to competitiveness through a devaluation would be gone, and possibly result in a long-term decline in employment in Britain. The other extreme - a rapid rise in interest rates at the time of membership - appears a less likely scenario - but would result in a recession due to reduced consumer spending and reduced investment.

A further aspect to consider in the euro debate is the role of the EU as the major trading partner of Britain. As the TUC pointed out in their *Preparing for the euro* brochure, 'in 1996 we (UK) exported more goods to the Netherlands than China, South Korea, Hong Kong, Indonesia and the other 'Asian tigers' put together - and that was before the economic crisis which affected trade with that area'.¹⁵ This picture can be enlarged to account for the whole of the euro-zone, where currently 50% of all UK exports go. To the pro-euro supporters this figure is used to argue the case for euro membership, for it would certainly make

¹⁵ *Preparing for the euro* TUC, January 1999 p.3.

trade easier with the rest of Europe. But for a balanced macro-economic perspective one must consider the effect on the rest of the economy. To do this, one must establish how large this 'other' part is. An informative article by Anatole Kaletsky, an economics commentator in *The Times* (7.9.99/p.31), sought to deconstruct the assumption that because 50% of exports go to the euro-zone, it is logical to join. He begins by quoting the Foreign Secretary, Robin Cook, as stating "We send a great majority of our exports to other members of the European Union". Britain exported 58% of its goods to the EU in 1998. Kaletsky rightly points out that a more important figure is the percentage of *goods and services* exported to the EU - 43% in 1998. He goes on to look at the percentage of goods and services exported to Europe as percentage of the total output of Britain, which was a much lower 19%. This figure denotes how much of the economic activity in Britain is directly influenced by the exchange rate between the pound and euro - in his opinion not much. Kaletsky takes his argument one stage further by distinguishing between the total value of goods and services exported to the euro-zone with the *value added* within Britain. The rationale behind this is that if one half of the components in a production process are bought from European suppliers, a strong pound favours their purchasing, while also hurting their eventual sales. This figure Kaletsky estimates to be about 10% - in his view a small percentage to use as the justification for joining the euro.

This interesting numbers game is useful but ultimately flawed. Just as Kaletsky rightly challenges those who use percentages to advocate euro membership, his numerical presentation must also be challenged and charged with not presenting the full picture. A strong pound that remained over-valued against the euro would damage all sectors of the economy that rely upon exporting to the EU. His assessment that damage to these sectors could be tolerated ignores the spill-overs within an economy and imagines that euro-dependent parts can be

completely isolated from the rest of the economy. If a large section of the economy was to experience a drop in sales due to a long term decline in efficiency - and even the 10% he has reduced the UK economy to is very large indeed considering a recession is defined as two consecutive financial quarters with negative growth (including -0.25%) - Britain would be severely damaged. His stance is also brought into question by economic trade theorists, who since Adam Smith have demonstrated that wealth is created through trade and exploitation of comparative advantage and not measures aiming at autarky. From a macro-economic perspective it remains in Britain's interest to improve as much as possible its chances of trading with other economies.

4.3 External Projection of the euro

Britain is faced with a problem common to all non-euro-zone economies: at what exchange-rate should the pound (or drachma or krona) enter the euro-zone? In this section the focus shall be on the economic external projection of the euro measured by the most watchful observers in Britain, namely British industry. The most pressing issue at the present time is the high value of the pound against the euro. It is in the interests of Britain to set a low level, thus establishing a comparative advantage over the labour costs of other EU members. *The Economist* published a survey by the CBI asking British businesses to state their preferred exchange rate for the pound.¹⁶ The first interesting statistic is that only 26% of the 5000 firms responded. Of those, only 52% agree to British membership, and the agreed value for the pound was 2.60-2.70 DM, or (1.33-1.38 euros). The Economist summarised this as an “unrealistic hope...[t]he pound has not traded anywhere close to this rate, since the launch of the currency at the beginning of the year.” The TUC went further by stating in their *Preparing for the euro brochure* an exchange rate between

¹⁶ The Economist (24.7.99) p.31.

1.25-1.30 euros.¹⁷ While currently unrealistic, it is perhaps not totally out of the question. A crucial factor in making convergence possible is the independence of both central banks and their shared objective of maintaining low inflation, promising an eventual harmonisation. In simple numerical analysis, the euro-zone will begin to grow stronger, and as this happens interest rates will rise to prevent consumer spending increasing and causing inflationary pressure. Meanwhile the British economy is slowing, and to maintain growth at even a reduced rate interest rates will fall, encouraging long-term investment and some consumer spending. As the difference in interest rates decreases, the value of the pound will drop and the euro strengthen as assets are transferred out of pounds and into euros. Therefore it is conceivable that the value of the pound will drop to a more favourable exchange rate as the conditions for membership improve. It is also agreed that a clear political commitment to membership would also steady markets and bring about convergence more rapidly.

Unfortunately this is not quite the rosy picture it appears. It has told the story of the two economies 'passing like ships in the night' - the British economy weakening and the euro-zone strengthening. Under these circumstances there has been no conversion towards the same economic cycle, simply rotation within two separate cycles that are momentarily in-phase. If the momentary in-phase period was mistaken for full convergence, then membership could be awful; just as Britain would need lower interest rates to stimulate the economy, the ECB would be pushing for higher rates to 'cool down' the euro-zone. It would demonstrate the frailty of a political union based on economic interests as described by Professor Buiter. Just as the Governor of the Bank of England, Eddie George, commented that unemployment in the north of England was a price to be paid for the stability of the south, economic deterioration in Britain would be regarded as the legitimate price to pay for prosperity in other EU

¹⁷ *Preparing for the euro* A brochure published by the TUC January 1999 p. 6.

states. With a centralised interest rate across Europe, political ties need to be strong enough to withstand the occasional centrifugal forces which will be exerted on them.

A medium to long term period of economic stability - steady growth and low unemployment throughout all euro-zone economies is necessary to build a political union which will be strong enough to weather the potential difficulties of the future. Hence it is seen as important that Britain joins at a time when its economy is in harmony with the cycles of the other euro economies. The debate over joining the euro does not contest the points raised here. All sides acknowledge that joining the euro-zone at the wrong time could be risky - the contentious issues are how damaging the failure of Britain to join would be and if, at the proposed moment of entry, real convergence had taken place or a mirage of that - the 'ships in the night' scenario.

4.4 Social Policy: labour markets and the promotion of investment through Foreign Direct Investment (FDI)

Labour market regulation is the most important aspect of social policy in the euro-zone. The flow of goods and capital throughout Europe must be matched if the euro is to succeed, since its purpose is to promote stability and growth. These two objectives will be achieved through removing bottlenecks in the euro-zone economy. One model which has attracted much attention is the USA. The US Federal Reserve acts within the American economy as the ECB does in Europe - a single interest rate is set across a diverse and un-uniform economy. The US economy is comprised of states in various stages of growth and decline simultaneously, meaning that the Reserve's interest rate is not always the most appropriate for each state. Europe would probably face greater problems between member states given the fact that the euro-zone comprised of national

economies until very recently. However, the US is vastly better prepared than the EU to deal with the inequalities between regions with two policy tools at its disposal - one micro economic and the other macro economic. Labour mobility is four times higher in the US than in Europe, a reflection on more rigid labour markets and cultural and linguistic barriers to movement. On the macro-economic side the US has an enormous federal budget that is used to redistribute resources to stabilise local economies under pressure from federal policy. If one accepts the similarities between America and the EU, the lower labour mobility of the latter must be regarded as an issue of concern.

British critics of the euro argue the lack of labour market flexibility is a good reason to stay out of the euro-zone. The euro will make demands of the market which the EU's social regulations will prevent from being fulfilled. Against this attitude the TUC has published a document entitled *Jobs in Europe - what the eurosceptics don't tell you* in an attempt to demonstrate the critics wrong.¹⁸ The report sets out independent findings which demonstrate that the 'social partnership economies' of Europe, by which they mean economies that have high union memberships and co-operative (as opposed to confrontational) management - union relations - such as Netherlands, France and Germany - are 'world productivity leaders'. (p.3) The paper contrasts these economies to 'hire and fire' labour markets such as the US and to the UK. It consistently finds that the critics' perceptions of 'social partnership' economies as being inefficient are wrong. Nevertheless, these arguments are by no means conclusive. The data is based on the national economies of euro-zone states prior to the establishment of the euro, and therefore demonstrates that the 'social partnership' model can work on a national level, but it does not address the concerns of those who say that cross-border labour mobility will be the problem the euro-zone must tackle.

¹⁸ *Jobs in Europe - what the eurosceptics don't tell you* TUC, June 1999. Taken from a press briefing given on 2.6.99.

Britain stands between the two extremes of a 'hire and fire' and 'social partnership' labour market. Despite Margaret Thatcher's policies that reduced the power of unions during the 1980's, Britain still values its social security and healthcare systems and is therefore much closer to the European social model than is sometimes admitted. The evolution of the European labour market will be hugely influential on Britain's economic performance as a member of the single market, and even more so when (or if) it joins the euro.

A second aspect of social policy concerns job creation, and in particular attracting foreign investment into Europe. Britain currently receives 40% of all Foreign Direct Investment in the EU, (when 'foreign' means non-EU). Japan is one of Britain's biggest investors (half of all Japanese investment in the EU is in Britain - Toyota, Nissan and Honda have car-plants along with numerous electronics manufacturers) as well as South Korea and other South East Asian countries.¹⁹ The United States also invests heavily in Britain, frequently choosing it as the centre for their European operations given the convenience of the English language. Supporters of the euro claim that the future of this investment would be threatened by Britain's refusal to join the euro-zone. The *Financial Times* (4.10.99) carried the headline 'Japanese urge euro decision' and stated on its front page that Japanese executives were concerned with the high value of the pound against the euro, and by failing to join the euro soon, Britain would jeopardise its chances of receiving further investment. The case for joining the euro is heavily influenced by such statements by multi-national companies.

¹⁹ Most recently, Proton, the Malaysian car manufacturer took control of Lotus Cars of Norfolk.

Dissident voices have been raised against this case.²⁰ It has been pointed out that 60% of all investment in Britain today by Japanese manufacturers is re-investment, replacing or enhancing production facilities currently in existence. This argument aims to persuade sceptics that the threat of an outpouring of investment should Britain stay out of the euro is an exaggeration, since existing infrastructure cannot be abandoned overnight. It has also been said that it is more important to retain access to the single market than join the euro, and only if Britain's membership of the EU was terminated would the case for investing in Britain be seriously damaged. The fact that the Japanese executives in the article cited above pre-supposed a highly valued pound should not be overlooked, since in the event of a weaker pound/stronger euro, the attractiveness of Britain would increase.

While the previous paragraphs have accurately portrayed one of the biggest debates concerning the economics of the euro, they have failed to take into account the real factors determining FDI. The decision to invest abroad depends on much more than exchange rates alone, which by nature are the most unpredictable variable in any equation concerning the long-term viability of FDI. Access to markets, macro-economic stability and local labour market dynamics are equally - if not more important - influencing such decisions. Britain stands half way between the American and euro-zone-norm for labour market regulation and the less strictly regulated labour market in Britain has undoubtedly tempted much of the recent FDI into Britain, and could continue to do so.²¹ The macro-economic stability of the last few years should now become

²⁰ Information comes from 'John Bull stays at home' *The Economist* (9.1.99) pp. 25-26.

²¹ Professor Garel Rhys of Cardiff University regards flexible labour markets and stable macroeconomics policies to have been influential in motor-industry investment in Britain. He clarifies his position by stating that the situation would be 'unsettling' if Britain left the European Union. *The Economist* (9.1.99) p.26.

a long-term reality given the recent independence of the Bank of England and their objective of maintaining low-inflation and steady growth in the economy. A strong currency encourages increased productivity within high-cost factories and places them in a better overall position during periods when the currency is weaker. Taken together, these points are not aimed at refuting the views of those who believe that Britain would be better within the euro-zone, but they do demonstrate that exchange rates are not the sole determinate of FDI, and guaranteeing a flexible labour market may prove equally important in guaranteeing FDI in the future.

4.5 Analysis

Economic arguments have been appropriated by the pro-euro supporters in an attempt to gain legitimacy for their case by appealing to economic logic and the use of reason. Their arguments are not so clean cut as is supposed and obscure a more complex reality where simplistic arguments are found wanting. The economic case for membership remains strong, but the *Britain in Europe* campaign should also work on political and social questions too since it is ultimately a political decision.

Conclusion

An Anglo-Saxon Debate

The recurrent theme throughout this report has been the tendency of the two sides to carve the social world into separate pieces which they can claim for themselves. The pro-Europeans of all political colours have agreed upon an economic agenda, while euro-sceptics retort with a patriotic manifesto for defending British sovereignty. It has been the nature of the British philosophic tradition to divide society into economic and political spheres - the private and the public - since the Scottish Enlightenment figures of Smith and Hume. This continued through Bentham, Ricardo and Mill, and been seen in recent incarnations in the 'Chicago School' of economics under Friedman and Becker. The euro-debate has seen this happen once more, in *Britain in Europe's* campaign to publicly contest the issue on economic grounds. This has a number of flaws. It ignores the real aim of European integration, which is the creation of a peaceful and prosperous region that channels the fruits of its industry back into social improvements. The single market and the euro are means to a higher

social end which is being wrongly interpreted as an end in itself in Britain. Domestically, describing the EU as nothing more than a market opportunity risks portraying politics as an impotent social activity, chastised by the ruthless efficiency of the market. Pro-euro supporters are waiting for Adam Smith's invisible hand to come down and mark the ballot paper in the euro referendum.

A question of identity

The debate in Britain about the euro ignores old ideological lines by defining new boundaries. Pro-Europeans are seen as progressive, while sceptics are conservative traditionalists. But this dichotomy is a mirror that reflects Britain as a whole. Britain is struggling to understand its role in the world at the beginning of the 21st century. The traditionalists mourn the end of British global domination but look to America as its legitimate heir, sharing culture and language. To these people the EU represents the final nail in the coffin of Britain's illustrious history, as the country slowly loses its sovereignty amidst the gradual process of political and economic centralisation in Brussels. To the progressive, Britain, America and the EU have a completely different relationship. The EU represents a new vision of political union that will eventually grow to match the US in influence in the world. Just as America's founding fathers pioneered a new form of political association, the EU has the potential to repeat this visionary exercise in the coming decades. Europe is where Britain belongs, because its culture and history have been shaped over the last 2000 years by it. The list of similarities between Britain and other European states is long: the philosophic heritage from Ancient Greece, the Roman Empire, the Church, monarchies, the industrial revolution, nationalism and global empires. Britain's reluctance to join the euro is partly due to an identity crisis. Until the British realise that their history is as unique as every other European state's, and yet rooted in the same heritage, Britain will only reluctantly

participate in the EU. In deciding whether we want to join the euro, we, the British must decide who we are - whether we shall persist in looking to the past or transform ourselves in the future.

Appendix 1: Opinion Polls

The following opinion poll results are taken from monthly surveys carried out by the ICM Research on behalf of the Guardian Newspaper. The questions asked cover a range of current affairs and have therefore been edited to include only questions directly relating to the euro. The polls can be obtained from the ICM website at <http://www.icmresearch.co.uk/reviews/>

ICM Guardian Poll - November 1999

Q3. If there were to be a referendum, would you vote to join the European Single Currency, or would you vote not to join?

Vote to join	28%
Vote not to join	59%
Don't Know	13%

Q4. Leaving aside how you would vote, in 10 years time, which of the following do you think is most likely?

The Euro will be the currency of most of Europe, Britain included	42%
The Euro will be the currency of most of Europe, but Britain will have retained the pound	23%
The Euro will have failed and each European country will have their own currency	27%
Don't know	8%

ICM Guardian Poll - October 1999

Q1. If there were to be a referendum, would you vote to join the Single European Currency, or would you vote not to join?

Vote to join	27%
Vote not to join	58%
Don't know	14%

ICM Guardian Poll - September 1999

Q4. They [the Liberal Democrats] are also campaigning for Britain to join the Euro and integrate faster into Europe. Does this make you more or less likely to support them, or make no real difference one way or the other?

More likely to support them	16%
Less likely to support them	36%
Makes no real difference	41%
Don't know	6%

Q10. Do you think the party's policies on the new Euro currency is improving, or damaging Labour's chances of winning the next election?

Improving	25%
Damaging	49%
Don't know	26%

Q17. The Conservatives have said that they will rule out membership of the Euro currency likely to vote Conservative at the next election, or make no difference one way or the other?

More likely	23%
Less likely	25%
Make no difference	47%
Don't know	5%

ICM Regular Poll August 1999

Q5. If there were to be a referendum, would you vote to join the Single European Currency or vote not to join?

Vote to join	24%
Vote not to join	60%
Don't know	16%

ICM Guardian Poll July 1999

Q2. Overall would you say the government has done a good job or a bad job on...Relations with the European Union?

Very good job	11%
Fairly good job	46%
Fairly bad job	14%
Very bad job	9%

Q3. If there were to be a referendum, would you vote to join the Single European Currency or would you vote not to join?

Vote to join	25%
Vote not to join	62%

Don't know	13%
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Q4. Leaving aside how you would vote, in ten years time which of the following do you think is most likely?

The Euro will be the currency of most of Europe, Britain included	36%
The Euro will be the currency of most of Europe , excluding Britain	26%
The Euro will have failed, all countries have their own currency	28%
Don't know	10%

ICM Guardian Poll - June 1999

If there were to be a referendum would you vote to join the Single European Currency or vote not to join?

Vote to join	27%
Vote not to join	61%
Don't Know	13%

ICM Guardian Poll - May 1999

Q6. If there to be a referendum would you vote to join the Single European Currency or vote not to join?

Vote to join	35%
Vote not to join	52%
Don't Know	13%

ICM Guardian Poll - April 1999

Q5. If Britain were to join the European Single currency, do you think Britain will loose ability to decide the level of it's own income taxes?

Yes	63%
No	22%
Don't Know	15%

Q6. If there to be a referendum would you vote to join the Single European Currency or vote not to join?

Vote to join	34%
Vote not to join	53%
Don't Know	13%

ICM Guardian Poll - March 1999

Q5 If Britain were to join the European Single currency, do you think Britain will lose ability to decide the level of its own income taxes?

Yes	63%
No	22%
Don't Know	15%

Q8 If there were to be a referendum, would you vote to join the Single European Currency, or vote not to join?

Vote to join	31%
Vote not to join	53%
Don't Know	16%

Appendix 2: UK Entrance criteria

The five economic criteria set out by the Treasury that determine whether a referendum should be held to decide whether Britain joins the euro are:

- i) Whether the UK economy has achieved sustainable convergence with the economies of the single currency.
- ii) Whether there is sufficient flexibility in the UK economy to adapt to change and other unexpected economic events.
- iii) Whether joining the single currency would create better conditions for businesses to make long-term decisions to invest in the UK.
- iv) The impact membership would have on the UK financial services industry.
- v) Ultimately whether joining the single currency would be good for employment.

Source: HM Treasury: *Outline national changeover plan* (1999) HMSO London. page 3.

SYNTHESIS REPORT

Stefania Baroncelli*

The Third Stage of the European Monetary Union and the Introduction of the Euro

Introduction: the Changeover to the Single Currency

The third stage of the European Monetary Union (EMU) started on the 1st of January 1999 and will be completed on the 31st of December 2001. On the first day of this period a number of occurrences have taken place. The euro was introduced and recognised as the currency of the eleven States belonging to EMU while the conversion rates linking the national currencies of the participant States and the euro to these currencies were irrevocably fixed. Also, the European System of Central Banks (ESCB) and the European Central Bank (ECB), which have been set up immediately after the decision has been taken on which member States adopt the euro, became fully operational with the task of deciding and implementing the monetary and exchange rate policies of the Eurosystem ("Eurosystem" is the term formulated by the ECB to refer to itself and the 11 central banks of the member States which have adopted the euro).²²

The third stage is to be considered as both a transitional and a final phase, designed for the smooth introduction of the euro in cash form. This requires a mechanism of co-ordination for economic policies among the States participating to EMU, whose effects in most cases are not limited to but extend well beyond the third phase. It includes the enforcement of the Stability and

* *European University Institute - University of Florence, School of Law.*

Growth Pact, a progressive fiscal harmonisation, and the co-ordination of macroeconomic and monetary policy (policy mix).

During this period, the States are also called to introduce modifications in their legal order, even though the reform of the national central banks entered into force well before the 1st of January 1999, as they were considered the prerequisites for the States to accede to EMU. The new currency, which from January 1, 1999 has been existing only as scriptural money, will start to circulate as a single unit of account and medium of exchange with its own banknotes and coins from January 1, 2002.²³

The EC Treaty and the attached Statute of the European System of Central Banks enshrine very detailed provisions regarding the powers and the organisation of the ESCB and EMU. On the contrary, these two primary acts contain only few principles on the euro. This latter is the object of secondary legislation, consisting essentially of two Community regulations adopted following the impetus of the various European Councils occurred in the second half of the '90s that have designed the overall changeover scenario for the transition to the third stage. The two regulations have been enacted to give a legal basis to the Presidency Conclusions of the Madrid European Council, of December 1995, on the scenario for the transition to the third stage, which have a mere political value. In fact, the European Council, without being part of the Community institutions listed in Art. 7 (ex Art. 4) of the EC Treaty, has acquired a crucial political power of direction and stimulus within the Community that has been sometimes subject to criticism when this body has

²² On the scenario for the changeover to the single currency, *see* EUROPEAN COMMISSION, DIRECTORATE-GENERAL II - ECONOMIC AND FINANCIAL AFFAIRS, Euro Papers, No. 17, February 1998, p. 11.

²³ To have an idea of the quantity of euro banknotes to be printed for the launch of the new currency, *see* ECB, *Determination of the number of euro banknotes to be printed before the launch date of 1 January 2002*, press conference of 13 July 2000. These estimates can be consulted in the web site of the ECB, at the following address: <http://www.ecb.int/index.html>.

intended to invade the responsibilities of the institutions.²⁴ The EU Council (the Ecofin Council) has an important legal role for the making of EMU and, more particularly, for the introduction of the euro on the basis of Art. 123, par. 4 (ex Art. 109L) of the Treaty, which also attributes to this institution the power to take the other measures necessary for the rapid introduction of the euro as the single currency.

Thus it was in *Dublin*, on 13 and 14 December 1996, that the Council decided that the legal framework for the use of the euro would have been provided by two Council regulations²⁵ and not one as provided in Madrid. For the rest, the Conclusions drawn at the Dublin Summit endorsed those adopted by the *European Council of Madrid*, which was held one year before, in December 1995. In Dublin, the Council decided unanimously, amongst other things, that the third stage of EMU would have only begun on January 1, 1999 due to the lack of a majority of States fulfilling the convergence criteria necessary in order to adopt the common currency before that date.²⁶ The political decision to start with the third stage on January 1999 had already been taken at the European Council in Cannes, in June 1995 and confirmed in Madrid.

The Conclusions of the Madrid Presidency are relevant for the transition to the third stage, because they introduce some legal principles underlying the changeover to the single currency, which have been later on specified in the two Council regulations on the introduction of the euro. Firstly, they make reference

²⁴ For the role of the European Council, the validity of its acts in the making of EMU and some controversial issues, see J.-V. LOUIS, *L'évolution du Conseil européen à la lumière de la réalisation de l'Union économique et monétaire*, in *Studi in Onore di Francesco Capotorti*, Divenire sociale e adeguamento del diritto, Giuffrè editore, 1999, p. 253.

²⁵ EUROPEAN COUNCIL OF DUBLIN, PRESIDENCY CONCLUSIONS, *The legal scenario for the use of the euro*, December 1996, in ABI, *Codice dell'euro. Normativa comunitaria e nazionale e commenti dell'ABI*, Bancaria editrice, 1998, p. 97.

²⁶ EUROPEAN COUNCIL OF MADRID, PRESIDENCY CONCLUSIONS, *The Scenario for the Changeover to the Single Currency*, annex 1, December 1995.

to the concept of *legal tender* when they mention that the transitional period is marked by the coexistence of the euro and the national currencies. These two currencies are linked by a legally enforceable fixed equivalence.²⁷ On the one side, the national banknotes are mere sub-divisions of the euro and “*continue to remain legal tender within the boundaries of the respective national territories until the completion of the changeover to the single currency [...] (and) cease to be legal tender at the latest 6 months after the introduction of euro notes and coins*”. On the other side, circulating euro banknotes and coins “*will have legal status [...] by January 1, 2002*”.²⁸ Unfortunately, this text does not explain the meaning of “legal tender”, and a further inquiry into the two regulations or the EC Treaty (especially Art. 106 (ex Art. 105A)) is fruitless. From a legal point of view, the quality of “legal tender” is recognised by the State to “*coin, money, or circulating medium which the law compels a creditor to accept in payment of his debt, when tendered by the debtor in the right amount*”.²⁹ Clearly, the euro is not legal tender in that sense during the transition period.

Secondly, the Madrid conclusions announce the rule of *no compulsion*, according to which private economic agents are “*free to use the euro; at the same time they should not be obliged to do so. As far as possible, they should be allowed to develop their own mechanisms of adjustment to the changeover*”.³⁰

This perspective concerns private persons, although States have to grant freedom of choice to individuals, subject (as we will see) to certain limitations. The concept of “no compulsion” is not new for the authors of the Maastricht Treaty. But, it had another meaning in the preparatory works of the Treaty. In fact, during the process leading to its adoption some States - namely Great

²⁷ Id. See N. LENIHAN, *The Legal Implications of the European Monetary Union under U.S. and New York Law*, in EUROPEAN COMMISSION, DIRECTORATE-GENERAL FOR ECONOMIC AND FINANCIAL AFFAIRS, Economic Papers, No. 126, January 1998, p. 13.

²⁸ EUROPEAN COUNCIL OF MADRID, *supra* note 26, point 14.

²⁹ BLACK'S LAW DICTIONARY, West Publishing, 1990, term “*Tender*”, p. 1467.

³⁰ EUROPEAN COUNCIL OF MADRID, *supra* note 26, point 9.

Britain and Denmark - upheld a “non-coercive” approach, refusing to enter EMU by way of provisions enshrined in an international treaty.³¹ This position has led these States to sanction their peculiar situation of “States with a special status” into Protocols 11 and 12 of the Maastricht Treaty and is in contrast with that of the other member States, more willing to sanction their obligations in an international treaty.

The *no compulsion* rule in the use of the euro is usually linked to that of *no prohibition*, meaning that people cannot be forbidden to use the euro, if they want to. This parameter is less apparent than that of no compulsion. While the latter is directly explicated in the Conclusions of the Madrid Summit and the euro Council regulations (as we have just seen), the former is implicit in the euro being defined as the currency of the participating member States, with the effect of substituting the national currencies (principle affirmed in the Madrid Presidency Conclusions as well as in Regulation 974/1998, Art. 2 and Art. 3).

The present text aims at offering a final assessment of the results highlighted in the National Reports using mainly a legal-political approach. For this purpose, it will analyse, in the first part (par. 1) the questions arisen in connection with the adoption of the euro in the member States of EMU, including: a brief description of the Community legal sources and their scope of application, an examination on the ambit of discretion and freedom left to the States with a focus on the most controversial legal issues raised by the EC regulations, and, finally, an inquiry on the legal techniques used at national level and the connected problem of redundancy. The second part (par. 2) will be dedicated to the reforms brought about on the national central banks statutes. The analysis will concentrate on the results of the polls presented in the National Reports, which will be confronted

³¹ See J.-V. LOUIS, *Monnaie (Union économique et monétaire)*, in “Répertoire communautaire Dalloz”, février 2000, p. 15.

with the legal traditions and concepts (such as openness, accountability and transparency) of the countries concerned.

1. The Introduction of the Euro

1.1 EC Council Regulations

As already said, the secondary legislation mentioned by the EC Treaty and the Madrid Presidency Conclusions resulted in the enactment of two EU Council Regulations, which enshrine the core principles governing the changeover to the single currency and establish the essential principles of the transition. Although they are legal instruments that *per se* leave a little space to Member States for manoeuvring, there are some spaces left to national intervention.

The first piece of legislation is *Regulation No. 1103 of 1997, "on certain provisions relating to the introduction of the euro"* which entered into force well before the introduction of the euro, on June 20, 1997. This early approval was deemed necessary for reasons of legal certainty and clarity, in order to avoid misunderstandings or bad expectations and to prepare individuals and economic agents for a smooth transition to the European Monetary Union.³² Given the fact that the Regulation entered into force before taking the decision on which States would have participated to the Union, it contains mainly some specific principles applicable to all the States of the Union. It also had the effect of anticipating some legal principles, that entered into force only later on, and of giving a legal form to the general maxims expressed during the summit of Madrid. This is all the more clear if we consider that the recitals in the preamble of the act outnumber the articles, which are only 6 in number.

³² Council Regulation (EC) No. 1103/97 of 17 June 1997, "*on certain provisions relating to the introduction of the euro*", 1997 O.J. L 162/1. The reasons at the basis of the early approval of the Regulation are made clear in recitals (4) and (7). See J.-V. LOUIS, *Euro*, in "Répertoire communautaire Dalloz", octobre 1997, p. 2.

The main principles laid down in this regulation are the correspondence between the euro and the ECU, on the basis of the equivalence 1euro/1 ECU (Art. 2); the important principle of "continuity of contracts (legal instruments)" (Art. 3); and the technical provisions relating to rules of conversion and rounding (Art. 4 and Art. 5).

This act gives important directions in the resolution of some controversial aspects relating to the introduction of the new currency at national level, with reference to the legal relationships linking mostly private economic operators and financial agents. This is all the more so, if we consider that these rules were followed by other non-binding acts of the Community, mostly recommendations, which have as addressees not only the member States but also all the economic agents of the Community. For example, this is the case of the Commission Recommendation on the double pricing and other amounts, which clarifies one of the problematic aspects of the changeover with a view to consumer protection.³³ In particular, this act does not recommend directly double pricing of goods and services, although in the fourth recital double pricing is defined by the Commission as a good way to ensure certainty and clarity for all the interested people. Even if the double indication of price is considered as non-compulsory, however it is recommended that once adopted it has to be used in an unambiguous way, using the conversion and rounding criteria outlined in the Regulation No. 1103.

³³ Commission Recommendation (EC) No. 98/287 of 23 April 1998, "*on double pricing and other amounts*". See especially Art. 5 of the recommendation. Other non-binding pieces of legislation include the Commission Recommendation No. 98/286 concerning "*Bank costs for the conversion into euro*" and the Commission Recommendation No. 98/288 on "*the dialogue, the monitoring and the information to facilitate the transition into the euro*". All these recommendations have been adopted by the Commission on April 23, 1998 and are published in 1998 O.J. L 130/22.

Regulation No. 1103/1997 is complemented by *Regulation No. 974 of 3 May 1998, "on the introduction of the euro"*.³⁴ This piece of legislation, with its schematic and brief style, confirms and specifies the fundamental principles on the introduction of the euro already declared during the Madrid Summit. It establishes, in the first place, the fundamental principle that the euro is the currency of the participating Member States (Part II of the regulation) and refers to the concept of legal tender for the period after 1 January 2002, when both banknotes denominated in euro and in a national currency unit will have such status for a maximum period of six months (Arts. 10, 11 and 15). The difference during this period (which can be shortened by each participant State *via* national law) resides in the national currency units keeping their legal tender status within their territorial boundaries only, and euro banknotes acquiring it in the whole euro-area territory.

1.2 Scope of application of Council Regulations

Regulation No. 1103 of 1997 was enacted on the basis of art. 308 (ex 235) of the EC Treaty, *i.e.* the *ultima ratio* provision entrusting the EU institutions with powers to intervene on certain sectors lacking a more precise legal foundation. The choice of Art. 308 as a legal basis means that all the States of the European Union - their status within EMU being irrelevant - are bound to its provisions. Why has Art. 308 been chosen instead of Art. 123, par. 4? As we have already noted, this latter is the main provision on the matter and provides that it is up to the Council, acting with the unanimity of the Member States without a derogation, to take the other measures necessary for the rapid introduction of the euro as the single currency of those member States. The reason derives from the limited scope of application of Art. 123. As it refers only to the States without a

³⁴ Council Regulation (EC) No. 974/98 of 3 May 1998, "*on the introduction of the euro*", 1998 O.J. L 139/1.

derogation, the enactment of a regulation on its basis would have meant postponing its entry into force until the decision would have been taken on which States participate to EMU. Instead, reasons of legal certainty for citizens and firms in *all the member States* were deemed preponderant so that it was thought necessary to introduce the main principles of the reform well before the entry into the third stage.³⁵ In particular, these provisions were considered as indispensable for dissipating doubts regarding the value of contracts denominated in ecu and national currencies and the way of calculating the conversion rate between the euro and the national currencies.³⁶ The value of "message" purported by the regulation, that we have already emphasised in the previous paragraph, is clearly shown by the existence of some provisions which entered into force only on January 1, 1999, in conjunction with the beginning of the third phase of EMU. This is the case of Art. 2 on the equivalence between ecu and euro.

Regulation No. 974/1998 entered into force on January 1, 1999, and it has instead been adopted on the basis of Art. 123, par. 4. This choice is perfectly in line with the requirements of the EC treaty; however it does not explain if the States non participating to EMU - Denmark, UK, Greece and Sweden - are included in its scope of application. On the one side, it can be argued that the simple reference to the States without derogation made by Art. 123, par. 4, of the EC Treaty justifies a limited scope of application of Regulation 974/1998. This is the thesis upheld mostly by the States with a special status,³⁷ that have

³⁵ Recital 4 of Regulation 1103/1997.

³⁶ These being the main reasons, there were some others favouring this approach, such as the importance for London to have immediate clear provisions on continuity of contracts; the necessity of putting up information programs for conversion; and some doubts as to the possibility for a regulation based on Art. 123 (providing for the adoption of strictly monetary rules) to enshrine more specific legal provisions on continuity of contracts.

³⁷ UK and Denmark are the main promoters of this interpretation. On this point, *see* especially the Greek Report par. 2.1.1 .

also tried to influence the content of the regulation by adding an ambiguous closing formula to Art. 17 of the regulation.³⁸ On the other side, it can be maintained that such regulation, being part of the Community legal order, is applicable to all the States of the Union, notwithstanding their having a special status or a derogation. This interpretation is preferable because it is more consonant to the legal Community principles, as it is standard of primary law that a regulation is entirely applicable in all Member States and binding in its entirety, no matter the content of a contrary clause included in a simple secondary act.

1.3 Scope of discretion left to the States

1.3.1 Internal Legislation Encouraging the Use of the Euro

After distinguishing between the scope of application of the two regulations, it is interesting to examine the scope of discretion accorded to the States by these two pieces of legislation. This is essential in order to acquire a uniform legal framework for the different National Reports.

According to the case-law of the European Court of Justice, regulations are acts incorporated into the legal framework of the member States without the need of internal legislation aimed at implementing or elaborating them. However, as pointed out by the Spanish Report, there are cases when some scope of discretion is recognised to the States (Spanish Report par. 1.3). This is the case, for example, when the regulation itself explicitly enables the member States to explicate its content *via* an internal act.

Regulation No. 1153/1997 does not provide the States with a power of implementation, as its provisions have not only a direct effect but also impose

³⁸ According to Art. 17 of Regulation 974/1998: "*This Regulation shall be binding in its entirety and directly applicable in all Member States, in accordance with the Treaty, subject to Protocols No. 11 and No. 12 [on UK and Denmark] and Article 109K (1) [on States non participating to EMU]*".

on the States clear and complete obligations. These rules, mostly that of continuity of contracts, can be in contrast with recognised principles of civil or commercial law of a member State. However, this clearly implies an obligation of the State (either through legislation or case-law) to apply the provision of the EC regulation which provides for the continuity of contracts, such provision taking precedence over any contrary rule of internal law.

The case of Regulation No. 974/98 is more complex. This act is composed of some articles that do not confer any discretionary power on the States. This is the case of the peculiar Art. 8, par. 3, allowing individuals (with some limitations) to pay debts in euro or in other currencies notwithstanding the will of the creditor.³⁹ The wording of this provision has given rise to various problems of interpretation relating to its extension; such question, however, is

³⁹ Art. 8, par. 3, recognises to individual debtors the power to pay either in euro or in a national currency unit if some conditions are present. First, the debt should consist in an amount denominated either in euro or in a national currency unit of a participating State. Second, the debt should be payable within that member State (thus the currency of this State should correspond to the currency of the denomination of the debit: *i.e.* a debt denominated in French francs payable in France). Third, the debt should be payable by crediting the account of the creditor (*i.e.* no cash payments). If all these conditions are met, then the debtor can discharge himself by paying in the currency of his choice, while the amount paid shall be credited to the creditor in the denomination of his account. This provision implies an obligation of credit institutions to convert the amount paid by the debtor into the currency of the creditor's account at the irrevocably fixed conversion rates.

Academic literature on the subject is extensive. *See*, for example, N. LENIHAN, *supra* note 27, p. 18; J.-V. LOUIS, *El nuevo Derecho monetario de la Unión Europea*, in “Noticias de la Unión Europea”, Agosto/Septiembre 1999, 175/176, p. 10; H. BRONKHORST, *General Introduction to the Provisions of the EC-Treaty and of Secondary Legislation Concerning the EMU and the Euro*, in J.-V. LOUIS - H. BRONKHORST, *The euro and european integration*, P.I.E., Peter Lang, Brussels, 1999, p. 104.

not considered here, since the aim of this article is not to provide guidelines to individuals and firms on how to follow up their business transactions in euro.⁴⁰

But regulation No. 974/98 embodies other provisions, which empower the States to exercise some discretion. It is the case, in the first place, of the fourth paragraph of Article 8, which allows the States to redenominate the public and private debt in euro and enables markets and systems of payments to use the euro in their operating procedures for the exchange, clearing and settlement in the field of securities and commodities. Apart from this, the general principle remains that other provisions can be adopted by the participating States only within the "*timeframe laid down by Community legislation*".⁴¹

This means that each participating State can redenominate its outstanding debt into euro during the transitional period. The majority of the participating States have decided to do so. For example, this is the case of Austria, Belgium, France, Germany, Italy (only for government securities denominated in LIT negotiable on regulated markets)⁴² and Spain.⁴³ (Austrian Report par. 2.3, Belgian Report par. 2.1.2 b), French Report par. 2 II B) 2), Italian Report par. 2.1.4, Spanish Report par. 1.3.2).

It is interesting enough to note that the notion of "redenomination" has been used in a particularly narrow meaning: as explained in Art. 1 of Regulation 974/1998 "redenominate" means changing the unit of the amount of outstanding debt from a national currency unit to the euro unit without altering any other

⁴⁰ See J.-V. LOUIS, *supra* note 39, pp. 12-13, according to whom the language used in Art. 8, par. 3, "*no es ciertamente de las más felices*" and gives rise to questions concerning its extension. For example, there are contrasts as to the inclusion of payments by checks in the provision.

⁴¹ Art. 8, par. 5, of Regulation 974/98.

⁴² Art. 5, par. 1, of Legislative Decree No. 213.

⁴³ For data not included in the National Reports, see MONETARY COMMITTEE, *Debt redenomination and market convention in stage III of EMU*, in EUROPEAN COMMISSION, Euro Papers, No. 28, July 1998, p. 10, especially Table 1.

term of the debt, "*this being a matter subject to relevant national law*". Thus redenomination simply implies the mechanical operation of converting an amount from one currency into another, in accordance with the rounding rules established in Regulation 1153/1997, but it does not have the effect of modifying any other terms of the debt, such as its nominal value. The nominalistic principle has been recognised explicitly by Recital 14 of Regulation 1998, allowing the national law to alter the nominal amount of outstanding debt. This means that a modification of the nominal amount of bonds will be only possible if the law of the State governing the issue recognises this possibility.⁴⁴ The redenomination of outstanding national debt has also a "waterfall" effect. In fact it also allows other issuers of debt (such as bonds, securities negotiable in the capital market and money market instruments) to do the same as long as they are denominated in the currency of the State which has taken this initiative. The only way to limit such right of the issuer is the agreement of both parties to exclude it from the contract. Thus issuers of debt instruments denominated in Belgian and French francs, Italian liras and Spanish pesetas, are allowed to redenominate them in euro, subject to certain limitations.⁴⁵

A supplementary scope of discretion is accorded to the participant States by Art. 15 of Regulation 974/98, according to which they are free to shorten the period of double legal tender. The possibility of shortening has been favoured by the Commission, which in May 1998 considered that a "*period of 6 months for dual circulation, the maximum foreseen [...] is too long. There is a need for the period of dual circulation to be as short as possible*".⁴⁶ Recently such question

⁴⁴ See N. LENIHAN, *supra* note 27, p. 18.

⁴⁵ Belgium: *see* Law 30 October 1998, especially Arts. 15, 19, 20 and 21; France: *see* section III of Law 2 July 1998; Italy: *see* Legislative Decree No. 213 of 24 June 1998, especially Art. 11; Spain: *see* Law No. 46 of 1998, especially Arts. 16-22.

⁴⁶ See EUROPEAN COMMISSION, DIRECTORATE GENERAL II - ECONOMIC AND FINANCIAL AFFAIRS, *From Round Table to Recommendations on practical aspects of the introduction of the euro*, Euro Papers, No. 23, May 1998, p. 34.

has gained a new impetus with the publication in July 1999 of a report where the Commission proposed to the Member States to set a deadline of only a few weeks. Such proposal was accepted by the participating member States at the Ecofin Council of 8 November 1999. The States adopted a common declaration and announced that they would take all the necessary measures to enable the execution in euro of the bulk of cash transactions “*by the end of a fortnight from 1 January 2002*”.⁴⁷ In the same occasion the States decided that the national currencies would cease to be legal tender shortly after the end of the transitional phase, within a period of four weeks and two months from 1 January 2002.

Germany has already declared that it will shorten the length of the period of dual circulation. This country envisaged the possibility to reduce this time to zero, so that the euro would have been the only legal means of payment from 1st January 2002 (“legal Big Bang”). However, after a discussion on the compatibility of such decision with the word “shortening” used in Art. 15 of the regulation, the deadline was partially modified. The transitional period of parallel circulation (of DM and euro) was extended until 28 February 2002 for commerce, banks and vending machines. The former deadline of January 1st was instead kept for bank transfers, invoices and so on (“modified Big Bang”). As a consequence, during this period of time vending machines, banks and shops will be allowed to accept DM notes and coins. On the other hand, they will not be allowed to keep these notes and coins but will have to cash them at the *Landeszentralbanken* (the central banks of the German States) or any bank, if they are retailers. The only exception are the vending machines, that will be still allowed to give change in DM. This decision was adopted only after a ‘joint declaration’ of the associations concerned, such as the vending machine industry and the retail and

⁴⁷ See EUROPEAN COMMISSION, *Euro coins, From Design to Circulation*, Euro Papers, No. 37, May 2000, p. 24.

credit sector, dated 22 October 1998,⁴⁸ and after the agreement on the modified big-bang regulation (“modified deadline”).

1.3.2 Consequences of the Introduction of EC Euro Regulations on the Domestic Legal Order: Some Controversial Aspects

As already said, the Member States can also elaborate internal rules to complement the EC regulations, whenever needed implicitly, in order to guarantee the efficacy and “*effet utile*” of the regulation. The approach chosen in Madrid as confirmed by the euro Council regulations is minimalist; as already seen Community provisions regarding the legal changeover to the common currency have dictated only few essential principles leaving up to the States the task of enacting more detailed legislation so as to solve problems likely to show up during the introduction of the new currency.⁴⁹ For example, the EC legislation does not give any indication either on the techniques to be used whenever States decide to redenominate the public and private debt, or on the parameters for monetary revaluation of legal instruments.⁵⁰ Furthermore, the EC legislation explicitly requires supplementary measures to “*ensure a balanced changeover, in particular for consumers*”: even though such provision was intended to refer to Community measures, it also has an indirect impact on national legislation as such measures should be introduced by the States in the internal order.⁵¹

The National Reports show that all the States have been aware of the important role they had been called to play in this respect. Most of them have put up special task forces willing to individuate the major fields of intervention and to filter and “clean” the entire legal system so that provisions in contrast with the

⁴⁸ Federal Ministry for Finance, press release of 23.10.98 and 07.07.99.

⁴⁹ R. PANIZZA, *Euro 2000*, Selcom Editoria, Torino, 1998, p. 74.

⁵⁰ G.L. TOSATO, *L'unione economica e monetaria e l'euro*, Giappichelli, Torino, 1999, p. 104.

⁵¹ Recital 1 of Regulation 974/1998.

EC legislation can be eliminated. This is the approach followed mainly by *Austria*. This country considered the necessity of adopting the regulations on euro as the occasion to reform other fields of legislation, for reasons of clarity and legal certainty. A working group called "Legistik", charged with listing all the legal provisions to be adjusted to the new phase, was established dealing with the legal framework of the changeover. According to this approach, every provision has to be changed individually and not through a general amendment (Austrian Report par. 2.1). A wide range reform of private law, centred on company law and continuity of contracts, was carried out accordingly.

Provisions on continuity of contracts enshrined in Regulation No. 1153/1997 have been the source of vivid internal debates concentrating on the validity of legal instruments under the new scenario. As a matter of fact, all the National Reports agree that in 1999 no proceedings or case-law on issues concerning the euro have been initiated or handed down due to the early stage. However some of them stress that in the future the majority of cases will be originated by the provisions on continuity of contracts, for their conflict with some general principles of law, such as the monetary equivalence rule (Greek Report par. 2.1.2) or some contractual clauses such as force majeure and supervening excessive hardship (Italian Report par. 2.2.1). Also, for some part of the doctrine, there may be cases when a continuation of the contract would be in violation of the necessity of it having a cause.⁵² It is the case of currency swaps, *i.e.* those agreements consisting in the exchange of one security for another and used by corporations and financial institutions to hedge against changes in interest and foreign exchange rates, even though it is true that other authors have rejected such objection⁵³ (Italian Report par. 2.2.1). Finally, it should not be

⁵² R. RONFINI, *Gli effetti giuridici dell'euro*, Cedam, 1998, p. 89.

⁵³ The compatibility of swaps with the principle of continuity of contracts is supported for example by the Commission. According to this view, a cross currency interest rate swap, concerning two currencies of member States participating to EMU is not invalid but it is simply transformed into an obligation of one party to make a series of net payments to its

forgotten that the principle of continuity of contracts is granted subject to anything which parties may have agreed.

This kind of problem appears more acute in Mediterranean countries, such as *Greece, Italy and Spain*, maybe due to the lack of a certain body of precedents, as appears in the Greek Report (Greek Report par. 2.1.2). In these countries the fear has been expressed that an alteration of the balance between creditor and debtor in favour of the latter could occur, mostly in fixed interest rates contracts. This problem has been solved in *Belgium* for consumer protection purposes with a legislation forbidding the seller to alter or terminate unilaterally the contract because of the introduction of the euro (Belgian Report par. 2.1.2 b)).⁵⁴ Similarly and on a more general level, the *Spanish legislation* has abolished the possibility to have recourse to court on the ground of the substitution of pesetas into euro (Spanish Report par. 1.3.1).⁵⁵ In Spain such provision has been the source of some criticism; not only for the prolixity of the text chosen that specifies every single possibility of alteration of the contract, but also for the existence of Art. 24 of the Constitution granting an effective judicial protection to individuals. According to the Spanish rapporteur, private persons and entities

counterparty. As for contracts where the only purpose is to cover an exchange rate risk (which has become non-existent because the currencies in the swap have become permanently fixed), the introduction of the euro does not make them invalid, if we take the view that such fixed parity was one of the risks that the parties had taken by drafting such a contract. Another justification is that such permanent fixed parity was well foreseeable in most contracts. See EUROPEAN COMMISSION, DIRECTORATE GENERAL II - ECONOMIC AND FINANCIAL AFFAIRS, *The legal framework for the use of the euro. Questions and answers on the euro regulations*, Euro Papers, No. 10, December 1997, p. 11.

⁵⁴ Art. 54 of the "Euro Law" of 30.10.1998.

⁵⁵ Art. 10 of Law No. 46/1998. According to this Article "*la sustitución de la peseta por el euro no constituye un hecho jurídico con efectos modificativos, extintivos, revocatorios, rescisorios o resolutorios en el cumplimiento de las obligaciones y que dicha sustitución no exime ni excusa del cumplimiento de las obligaciones vigentes ni autoriza la alteración unilateral de su contenido, salvo pacto expreso en contrario de las partes*".

would have been better protected if the legislator had copied the text of Art. 3 of Regulation No. 1103/1997 and not specified the various cases of application.

On the contrary, problems seem to be minimal in countries that have more tradition of case-law on currency reforms. In *Austria*, for instance, several currency reforms (dealing also with the phenomenon of hyperinflation) have taken place and a consistent case-law acknowledges that the burden of risk should be borne by creditor. If this is true for currency reforms, it is all the more true in the present case, which is a mere currency conversion (*i.e.* only a change in the denomination). According to the Austrian Report, the system of private law, which has been restated for reasons of clarity, was already in line with the EC principles (Austrian Report par. 2.3).

1.3.3 Spaces Left to the Intervention of the States: Tendencies in National Law

States are left free to regulate the changeover in the way they deem appropriate in the areas left aside by the two EC regulations. In this respect the States have been recognised a freedom of action with the only non-binding limitations deriving from the several acts adopted by the European Communities. This is the case of the already mentioned recommendations adopted by the Commission in 1998 and other acts enacted by different Directorates General of the same institution, concerning accountancy rules and rounding.⁵⁶

States can therefore approve rules on corporations, such as accountancy and redenomination of capital rules; on public administration, such as income declarations; and on protection of creditors and consumers, such as publication of prices in euro as well as in the national currency.

⁵⁶ EUROPEAN COMMISSION, DG XV, *Accountancy rules on the introduction of the euro*, visible at the following address: <http://europa.eu.int/en/comm/dg15/dg15home.html>; EUROPEAN COMMISSION, DGII, *Introduction of the euro and rounding of monetary amounts*, in ABI, *Codice dell'euro. Normativa comunitaria e nazionale e commenti dell'ABI*, Bancaria editrice, 1998, p. 131.

The approach chosen by the States conforms with the "no prohibition, no compulsion" approach. Thus, balance-sheets of enterprises can be usually be published either in euro or in a national currency and the same applies to the conversion of the capital of enterprises (Austrian Report par. 2.3, Belgian Report par. 2.1.2 b), French Report par. II A), German Report par. 2.1, Italian Report par. 2.1.4); sometimes income and VAT declarations can also be established in euro (Belgian Report par. 2.1.2 a)⁵⁷, Italian Report par. 2.1.4⁵⁸) while in some cases income declarations in euro are not permitted (French Report par. 2 II D)⁵⁹, German Report par. 3.2⁶⁰). In Spain, the legislator has explicitly stated that conversion payments should be made for free (Spanish Report par. 1.3.2)⁶¹.

What is more interesting is that in some cases also non-participating countries are using the euro as a parallel currency. This is the case of Sweden, where the balance sheet of enterprises can be drawn either in euro or in Swedish kronor. As for accounting, a new law, passed in March 2000, recognised that it must be entirely either in euro or in kronor, although taxes are always to be paid in kronor, according to special conversion tables (Swedish Report par. 2.1.1). This odd situation can give rise to some fiscal problems mostly if multinationals decide to draft their accounts in euro so that tax authorities should be forced to deal with payments in two different currencies linked by a floating exchange

⁵⁷ See Royal Decree of 15 December 1998.

⁵⁸ In Italy amounts of income declarations can be shown in euro from 1 January 1999 and creditors may request payments from government in euro if a payment by cash is not involved. This principle, however explicitly stated, is a consequence of Regulation No. 974/1998.

⁵⁹ In France income declarations in euro are forbidden; it is possible however to pay taxes in euro. See Titre III of Law No. 98-546 of 2 July 1998.

⁶⁰ In Germany income declarations are drawn in DM, while amounts in euro are given for information.

⁶¹ Art 15 of Law 12/1998 of 28 April 1998, entered into force on 1 January 1999.

rate. This is the reason why it is predictable that in Sweden the question of the use of the euro will rise to public debate before 2002.

1.4 Redundancies in Legislation

Some States have raised the question of what method should be used in drafting the legislative reform both of the national central banks and on the introduction of the euro (for a summary of the main legislative acts adopted on the introduction of the euro and their legal form, *see* Table 1). On the one hand, there are modifications required by the parameters of legal convergence on the independence of the national central banks and their integration into the ESCB imposed to the Member States by Art. 109 (ex Art. 108) of the Treaty. On the other hand, reforms have been clearly promoted by the two Council Regulations on the introduction of the euro.

It should be clear from the beginning that a standard method of adaptation does not exist, as neither the Treaty nor the statute require a harmonisation of national legislation.⁶² National legislators are simply bound to the principle of direct applicability and supremacy of Community law in adopting domestic provisions on the introduction of the euro and the institutional modifications required to enter the third phase of EMU. This is all the more clear if we consider the report published by the “forefather” of the ECB, the European Monetary Institute (EMI) in October 1997, where it appreciates the status of the domestic legislation of the Member States and evaluates its compatibility with the dictates of the Treaty without, however, imposing a single solution for realising such adaptation. The EMI limits itself to highlight the points of the internal legal

⁶² On the lack of harmonisation of national legislation for the adaptation to the Treaty, *see* J.-V. LOUIS, *Monnaie (Union économique et monétaire)*, in “Répertoire communautaire Dalloz”, février 2000, p. 10.

framework that are judged in contrast with the requirements of Stage three of EMU, but it does not suggest a one-way solution.

These observations promote further considerations, based on the different kind of legal sources which are at the basis of the reform of the currency and of the national central banks (the content of such reform will be examined *infra*, par. 2). The incorrect drafting of an internal act aimed at introducing the euro in the domestic legal order, consisting for example in the manipulation of the EC regulations, can give rise to relevant problems for its contrast with the EC monetary regulations, given their direct applicability in the Member States. These obstacles on the contrary do not exist for the reform of central bank statutes, which does not require the harmonisation of national laws.

The question of the technical adaptations that are legally necessary for entering stage three of EMU has been discussed mainly in Belgium, Austria, Spain and Greece. In *France* as well some debates have taken place, the outcome of which is the inclusion of provisions on the introduction of the new currency in one single piece of legislation.

A specific approach has been followed in *Belgium*. In this country the Council of State has criticised the legislative draft on the reform of the statute of the National Bank of Belgium prepared by the Belgian Government for having reproduced directly applicable provisions of the Treaty and the Statute, and has judged it redundant; according to the Council it would have been sufficient to introduce some general provisions making reference directly to EC law. For example, in the Council's words, it was enough to state that "*the National Bank of Belgium shall form an integral part of the European System of Central Banks and it shall be governed by... the Statute of the European System of Central Banks*". As a consequence the Belgian Government decided to change the wording of the draft, incorporating the provisions of the Statute of the ESCB on

the tasks, objectives and features.⁶³ This is also the method followed, for example, by the *Italian legislator*, which makes reference to the relevant provisions of the EC Treaty and EC regulations without restating their content (Italian Report par. 2.2.2).

A different approach has been followed by the *Austrian* decision-making bodies: the working group "Legistik", established for the changeover, has been working on the assumption that a general amendment to internal legislation is not enough and that, as a consequence, every single provision in contrast with EC legislation on EMU should be modified individually. As a result, the text of many of the new provisions is similar to those of the Treaty, even word by word (Austrian Report par. 2.2).

An effort of systematisation on the subject has also been made in *Spain*, where EC euro legislation has been implemented *via* a general legal act enshrining general principles: the Law No. 46/1998 ("*ley paraguas*") complemented by national regulations and acts adopted by some of the *Comunidades Autonomas* within their jurisdiction aimed at explaining the use of the euro in their administrative and financial affairs. The techniques adopted by the Spanish legislator in drafting the legislation have been criticised for some modifications introduced in the text of the EC Treaty and the Statute of the ESCB. Such application of EC law in the national order is contrary to the case-law of the Court of Justice, because it contradicts the dictates of EC legislation to which the States are obliged to conform. A better way of proceeding would have been to follow the example of Belgium and to include a reference to Community law in the national legislation. Or, instead, to reproduce literally the provisions of the Treaty, in the Austrian way, provided that the origin of the texts is made very clear, even though such type of proceedings can be justified only for the

⁶³ See EUROPEAN MONETARY INSTITUTE, *Legal Convergence in the Member States of the European Union* (as at August 1997), October 1997, p. 10. See also PARLIAMENTARY PAPERS, HOUSE OF REPRESENTATIVES, No. 1061/1, 96/97, 4 June 1997.

legislative reforms on the national central banks and not for the euro legislation that has legal consequences directly on citizens.

Some other problems derive from the unclear division between the powers that the Bank of Spain has on its own, and the functions it exercises as a member of the System of Central Banks. Given the different limitations to which the two types of functions are subjects, in accordance with Art. 14 of the Statute, this unclear division can be the source of a questionable interpretation of the Statute of the Bank of Spain. In fact, the national central banks, as members of the ESCB, are mere "operating arms" of the ECB; on the contrary they are completely free in their action if they exercise different functions, with the limit of not interfering with the objectives and tasks of the ESCB (Art. 14 of the ESCB Statute; Spanish Report par. 1.2.1).

Finally, also *Greece* has taken a stance that is similar to the Austrian. The Greek legislator has not only considered the adoption of EC legislation on EMU as an occasion for a wider review of relevant legislation, but it has also rejected an approach based on a general piece of legislation abolishing incompatible provisions if not followed by a contemporary identification of such invalid acts. This thoughtful attitude taken by Greek political powers *vis-à-vis* the institutional arrangements of EMU and its adaptation within the national order shows their interest to join the union as soon as possible. As a matter of fact, the exclusion of Greece from the first wave of countries members of EMU was dictated only by economic factors and not by a lack of adaptation to the Community legislation (clearly this appreciation refers only to the reform of the Bank of Greece and not to the euro legislation, which is not a parameter of legal convergence).⁶⁴

⁶⁴ These impediments were recognised by the Council in the decision 98/317 of 3 May 1998 "in conformity with Art. 109J, paragraph 4, of the Treaty" on the member States adopting the euro, 1998 O.J. L 139, p. 30.

Table 1 - Main National Legal Provisions on EMU and Procedures of Adaptation

STATES	MAIN NATIONAL LEGAL PROVISIONS ON EMU	PROCEDURES OF ADAPTATION
AUSTRIA	<i>Central Bank Statute</i> Nationalbankgesetz [Central Bank Act], BGBl I No. 60/1998	<ul style="list-style-type: none"> • The text of the new provisions is very similar to that of the EC Treaty and ESCB Statute, even literally
	<i>Introduction of the euro</i> Private Law Amendments	<ul style="list-style-type: none"> • Refusal of a general amendment: every provision in violation with EC legislation ARE modified individually • Many legislative changes do not relate directly to euro but to other fields, for reasons of legal certainty • Each federal Minister is responsible for the process of adaptation within its sphere of jurisdiction
BELGIUM	<i>Central Bank Statute</i> Law of 22 February 1998 (The New Organic Law of the National Bank of Belgium)	<ul style="list-style-type: none"> • Legislative power exercised by Government • A first draft of the law had been criticised by the Belgian <i>Conseil d'Etat</i> for reproducing provisions of both the EC Treaty and the ESCB Statute. Such opinion led the Belgian Government to delete those provisions that were a mere reproduction of Community law. As a result, the new law states the objectives, tasks, and other characters of the National Bank of Belgium through direct reference to the articles of the EC Treaty and the ESCB Statute

	<p><i>Introduction of the euro</i> Law of 30 October 1998 (Law on the introduction of the euro)</p>	<ul style="list-style-type: none"> Legislative changes in various fields deriving from the introduction of the euro have been concentrated in one single act
FRANCE	<p><i>Central Bank Statute</i> Law 93-980 of 4 August 1993 (Statute of Bank of France) Law 98-357 of 12 May 1998 (Insertion of the Bank of France into the ESCB)</p>	<ul style="list-style-type: none"> Law 93-980 grants the Bank of France a degree of independence and defines the stability of prices as its main objective Law 98-357 transfers monetary policy to the ESCB; change policy to the Council of the EU; modifies the role of the Bank of France for the payments system
	<p><i>Introduction of the euro</i> Law No. 546 of 2 July 1998 (introduction of the euro)</p>	<ul style="list-style-type: none"> This is a general piece of legislation “<i>portant diverses dispositions d’ordre économique et financier</i>”. Only Chapter II of this act enshrines the adaptations to the new currency. Such chapter establishes the various legislative modifications necessary for the changeover (capital and debt instruments redenomination, continuity of contracts, etc.)
GERMANY	<p><i>Central Bank Statute</i> Reform of the Statute of the Bundesbank Act (<i>Sechstes Gesetz zur Änderung des Gesetzes über die Deutsche Bundesbank</i>, in: <i>Bundesgesetzblatt 1997</i>, part I, No. 88, 30 December 1997, p. 3274-3275) of 22 December 1997</p>	<ul style="list-style-type: none"> Only specific amendments

	<p><i>Introduction of the euro</i></p> <p>Law of 9 June 1998 (accounting law, debt enforcement proceedings)</p> <p>Law of 24 March 1999 (social security and administration): in force retrospectively from 1 January 1999</p> <p>Law of 16 December 1998 (notes and coins, definite introduction of the euro cash)</p>	<ul style="list-style-type: none"> • The Legislation on the introduction of the euro is quite detailed. The intent of the national legislator has been to bring any national provisions in conflict with the EC euro regulations into line, to guarantee complete clarity • Relevant problems linked to the federal structure of Germany
GREECE	<p><i>Central Bank Statute</i></p> <p>Law No. 2609 of 1998 (independence of the Bank of Greece)</p>	<ul style="list-style-type: none"> • Fulfilment of legal convergence criteria notwithstanding the status of State with a derogation • General legal act abolishing incompatible provisions complemented by an identification of such invalid acts
ITALY	<p><i>Central Bank Statute</i></p> <p>Legislative Decree No. 385 of 1993</p> <p>Law No. 483 of 26 November 1993</p> <p>Law No. 433 of 17 December 1997 (delegation to Government):</p> <p>Legislative Decree No. 43 of 10 October 1998</p>	<ul style="list-style-type: none"> • Law 483 of 1993 forbids the Bank of Italy to grant any advance to the Ministry of the Treasury and gives it all the decision power for the compulsory reserve • Leg.ve decree 43 of 1998 states that the Bank of Italy is an integral part of the ESCB and acts in conformity with the instructions of the ECB
	<p><i>Introduction of the euro</i></p> <p>Law No. 433 of 17 December 1997 (delegation to Government):</p> <p>Legislative Decree No. 213 of 24 June 1998</p> <p>Legislative Decree No. 206 of 15 June 1999</p>	<ul style="list-style-type: none"> • Law of delegation 433 of 1997 establishes the following general principles that have to be followed by Government: continuity of legal instruments and legal relations, neutrality of the transition to the single currency, full information on transition rules, gradual transition to the single currency

<p>PORTUGAL</p>	<p><i>Central Bank Statute</i> Decree-Law 235/1995 Law No. 3 of 5 February 1996 Law No. 5 of 31 January 1998</p>	<ul style="list-style-type: none"> • See Table 1 of Portuguese Report
	<p><i>Introduction of the euro</i> Decree-Law 138/1998 Decree-Law 343/1998</p>	<ul style="list-style-type: none"> • See Table 1 of Portuguese Report
<p>SPAIN</p>	<p><i>Central Bank Statute</i> Law No. 13 of 1 June 1994 (independence of the Bank of Spain from government) Law No. 12 of 28 April 1998 (integration of the Bank of Spain into the ESCB)</p>	<ul style="list-style-type: none"> • Law 13 of 1994 transfers monetary policy to the Bank of Spain and guarantees its independence • Law 12 of 1998 integrates the Bank of Spain into the ESCB
	<p><i>Introduction of the euro</i> Law No. 46 of 1998 ("Ley paraguas") Various regulations Legislation of <i>Comunidades Autonomas</i></p>	<ul style="list-style-type: none"> • Adaptation via a general act with legal principles complemented by regulations and acts of the <i>Comunidades Autonomas</i> • Criticism for the drafting of Law 46 of 1998 for the reproduction of EC legislation with some modifications: problems of redundancy
<p>SWEDEN</p>	<p><i>Central Bank Statute</i> Law No. 1385 of 1988 (Riksbank Law)</p>	<ul style="list-style-type: none"> • The procedure has not been completed yet

2. The Statutes of the National Central Banks

The National Reports agree that the major legislative adaptations required by the EC Treaty and the Statute of the ESCB have consisted in the modification of the State's central bank statutes. These parameters of legal convergence have been dictated directly by primary law, and have been considered as the necessary preconditions for Member States to accede to the third stage of EMU.⁶⁵ This is especially true for those States lacking a tradition of independent central banks, such as France and Italy, Belgium, Spain and Portugal (although their degree of independence varies), but it is also true for those which historically have enjoyed a higher grade of independence from the political powers, legally or *de facto*, such as Germany and The Netherlands.⁶⁶

⁶⁵ On the legal preconditions for acceding to stage three of EMU, *see*, for example, F. CONLLEDO LANTERO, *Las reformas legislativas que la Unión Económica y Monetaria exige para nuestro sistema financiero*, in "Noticias de la Unión Europea", Agosto/Septiembre 1999, 175/176, p. 36.

⁶⁶ For a measurement of the central bank independence from a legal and economic point of view before the central banks statutes were adapted to the requirements of the ESCB Statute, *See* BRIAULT - HALDANE - KING, *Central Bank independence and accountability: theory and evidence*, in "Bank of England Quarterly Bulletin", February 1996, p. 63. According to these authors, the central banks of Italy, Sweden and France enjoyed a low level of independence while the central banks of Belgium and Spain were in a middle position. The highest degree of independence was traditionally acknowledged to the central banks of Germany and Switzerland. In the middle position was also the Bank of The Netherlands and the Federal Reserve System, although enjoying a greater degree of independence than those of Belgium and Spain. The Bank of England, finally, was lying at the lowest spectrum of the graphic. The requirements of legal convergence established by Art. 14 of the ESCB Statute and Art. 109 (ex Art. 108A) of the EC Treaty, requiring that each State is responsible for the compatibility of domestic legislation with the obligations of legal independence, has of course changed this state of affairs. A new updated indicator for central bank independence has been drawn up taking into account such reforms. According to this the central bank with the greater degree of independence, in addition to the ECB, remains the Bundesbank (5 scores)

2.1 Problems of Constitutional Legitimacy

One of the conditions for member States to be accepted as members of EMU was the obedience to the parameters of legal convergence fleshed out in the ESCB Statute.

At first sight, a modification of the Statute of the *Bundesbank* may seem superfluous: according to the common view, the Bundesbank Act has served as the blueprint for the ECB! However, as pointed out in the German Report, the factors of independence required by the ESCB Statute for the national central banks are even stricter than those of the Bundesbank. It is sufficient here to remind that, before the 1997 reform, the Bundesbank Act acknowledged to the members of the Federal Government the power to defer the decisions of the Central Bank Council for up to two weeks (German Report par. 2).

Probably the most difficult process of adaptation has taken place in France and Portugal, where the approval of the reforms on central bank independence has given rise to problems of constitutional legitimacy. Before the introduction of the reform by Law 93-980 of 4 August 1993 the *Bank of France* was a political body lacking personal and functional independence. The first indication of a change was the modification of the provision of the Statute that granted the Government the power to remove the Governor and the two vice-Governors from their position without the formulation of an explicit reason; the new formula allows a removal only for "*faute grave*" and "*incapacité d'exercice des fonctions*".⁶⁷ The second radical transformation is linked to functional independence. Before the reform, according to Art. 4 of Law No. 73-7 of 3

followed by the central banks of The Netherlands, Denmark and France (4 scores), Belgium, Spain, UK and US (3 scores), Sweden and Italy (2 scores). This table is reported in DE HAAN - AMTENBRINK - EIJJFINGER, *Accountability of central banks: aspects and quantification*, in "Banca Nazionale del Lavoro, Quarterly Review", June 1999, p. 189.

⁶⁷ Art. 10 of Law 4 August 1993.

January 1973 the Bank of France had the clear political task of "*préparer et participer à la mise en oeuvre de la politique monétaire arrêtée par le gouvernement*". We do not need a lot of rhetoric to emphasise the modifications already introduced by Art. 1 of Law No. 93-980, according to which the Bank was charged with "*définir et mettre en oeuvre la politique monétaire dans le but d'assurer la stabilité des prix*".

The question of constitutional legitimacy was originated by the difficult insertion into the French legal system of a provision, such as the one that we have just mentioned, which is in contrast with the main principles of a semi-presidential system. From a Constitutional point of view, France is a country where all the political power is concentrated on the hands of the Government.⁶⁸ The power of the two chambers of Parliament is reduced to some sectors established by the Constitution while Government exercises all the (extensive) residual power *via* regulations. It is the Executive that - in consultation with the President of the Republic that should be compulsorily consulted by the Prime Minister in the exercise of his functions - decides and executes the major political decisions of the nation and is responsible for the whole administration. Such government-centred system could not be farther from the principles of "horizontal" and "non-hierarchical" administration required by an independent central bank. This is the reason why the *Conseil Constitutionnel*, in its decision of August 1993 on the constitutional validity of the law that laid down the new statute of the Bank of France, ruled such reform unconstitutional as it could not be enacted before the entry into force of the Maastricht Treaty. The provisions of the Constitution at the origin of the contrast were Articles 20 and 21, *i.e.* those indicating the core principles of a semi-presidential system, according to which it is up to the Government to decide and carry out the politics of the

⁶⁸ For a comparative analysis of the French Constitutional system, See G. DE VERGOTTINI, *Diritto costituzionale comparato*, Cedam, 1993, p. 574; S. MERLINI, *Appunti*

Nation and it is to the Prime Minister to direct it. As the French *Conseil Constitutionnel* exercises, if requested, a control *a priori* on the text of legal acts before they enter into force, it decided that such a transfer of monetary power from the Government to the central bank could not be justified on the solely basis of Art. 88, par. 2, of the Constitution: this article acknowledges the transfer of power from the State to the European Union on the basis of the Treaty of Maastricht, but it was not in force at that time. It would have been necessary to wait until this article was in force to justify the reform.⁶⁹ The provision has been modified in 1998.

Also the *Bank of Portugal* underwent a major process of change; as explicated by the Portuguese Report, "*initially a public owned company, the Portuguese Central Bank is now a special legal entity governed by public law and enjoying administrative and financial autonomy*" (Portuguese Report par. 2.1). But it is the requirements on the functional independence that were the source of major criticism and the reason of a Constitutional amendment concerning the Bank of Portugal functions. Since 1997 Art. 102 of the Portuguese Constitution has been changed into a more flexible text in order to put the central bank functions in line with the dictates of the Maastricht Treaty. From that year on the new text of the Constitution reads as follows: "*the Bank of Portugal, in its capacity as a central bank, shall carry out its functions in accordance with the law and with the international rules to which the Portuguese State is bound*".

An interesting evolution is taking place also in *Sweden*, a country where the statute of the central bank is regulated directly by the Constitution. Although formally out from EMU, this country is not only adopting the euro as a parallel currency but it has also passed a piece of legislation aimed at strengthening the independence of the Swedish central bank. As a consequence, a constitutional

sulle forme di governo, Giappichelli, 1999, p. 89; C. MORTATI, *Le forme di governo*, Cedam, 1973, p. 249.

⁶⁹ See Decision No. 93-324 of 3 August 1993, in JORF 5/6/1993, p. 11014.

reform has taken place in order to harmonise the Constitution with the rules of the ESCB Statute. Although this Constitutional reform has already entered into force on January 1, 1999, it is not sufficiently large to put in line the Swedish central bank with the requirements of independence required by the Maastricht Treaty. That is why a new Constitutional reform, eliminating the monopolistic power of the central bank in the fields of monetary policy and the issue of notes and coins, is deemed necessary before Sweden decides to join the third stage of EMU.⁷⁰

Lastly, it is interesting to remember that also *Austria* passed a Constitutional reform related to EMU; however, it was not connected to the statute of the central bank but to the Stability Pact.⁷¹ This relevant decision, which deals with problems of co-ordination among the various levels of governance inside the State, has already been discussed by Prof. J.-V. Louis in the introduction and does not need further investigations. Also, it should not be forgotten the judgement of the German Constitutional Court on the more general problem of adherence to Germany to the European Union. Although it makes reference also to the provisions on EMU, the German High Court has upheld its constitutional validity.

2.2 Accountability of the Central Banks: a Tradition of the Northern Countries?

One of the most debated questions on the status of central banks is that of *accountability*. The reason for such discussion is clear: more independence on

⁷⁰ Chapter 9 of the Swedish Constitution deals with the status of the central bank. The exclusive power of the central bank to enact monetary policy and issue banknotes and coins is recognised by chapter 9, par. 12 and par. 13.

⁷¹ The Stability Pact of 1997 imposes tight fiscal common obligations on the member countries. For an explanation of the consequences of the Stability Pact on the countries of the Union, see C. D'ADDA, *The EU and the euro: an example to imitate?* in "Banca Nazionale del lavoro, Quarterly Review", 1999, p. 388.

legal terms can be justified only in an open and transparent context where the decisions taken by the central banks are subject to discussion and open criticism from the democratically-elected institutions. The expressions “independence” and “accountability” are usually considered as opposite concepts in the description of the relationship between the central bank and the elected institutions. However in legal terms this is not so, on the condition of considering the word "accountability" as a synonym of the terms "responsibility" and "liability": *i.e.* "the condition of being actually or potentially subject to an obligation", or the "condition which creates a duty to perform an act immediately or in the future", or, finally, "the state of one who is bound in law and justice to do something which may be enforced by action".⁷² If such concept were only based on the existence of a legal basis whose infringement brings about judicial control, the fact of the ECB being subject to the jurisdiction of the European Court of Justice would be already sufficient to justify its independence.

However, such vague definitions take into account only some partial and civil aspects of the concept of institutional accountability, while legal theory makes reference to other concepts such as those of "democratic responsibility" and "democratically elected institutions", that explicit the connection between one institution and the electorate (or its representatives). This being so, the accountability of a central bank is determined, in the first place, by its enabling act, which is usually an act of delegation from the Parliament. But this act - that for the ECB consists in a Treaty- does not replace the need for an institutional check, mostly from the legislative and executive branches. Powerful parliaments, such as that of the United States, can investigate an independent central bank either through its own hearing and subpoena power or through its auditing and investigative arm, while the executive power can exert his control

⁷² BLACK'S LAW DICTIONARY, West Publishing, 1990, term "*Liability*", p. 914.

through various instruments, such as the appointment and termination of agency officials and the supervision of its rule-making authority.⁷³

In addition, this arrangement should be coupled with means capable of assuring an effective *transparency* so that external controllers can have a full and comprehensible picture of the reasons at the basis of the central bank decisions. This is why this kind of accountability is usually coupled with effective channels of communicating the main political decisions to external audiences; useful instruments in this respect are the publication of the minutes of the meetings and decisions taken, as well as of the reports on different economic indicators, such as the inflation target.

All the National Reports deal with the question of accountability, though to a different extent. EC provisions do not impose strict obligations in this respect so that internal legislation is still very different from a State to another. As a matter of fact, the Statute of the ESCB requires only that the mandate of the Governor of the national central bank cannot be inferior to five years and that he can be removed only for serious misconduct or for not fulfilling anymore the conditions required for the performance of his duties.⁷⁴ Other requirements imposing reporting duties concern exclusively the ECB and not national central banks.

The most interesting National Reports in this respect are perhaps those concentrating on two countries which, not surprisingly, have decided to stay out from EMU: Sweden and UK. At the other side of the accountability spectrum lies Austria, which, according to the National Reports, has no reporting requirements to Parliament.

In *Sweden* the Governor is not only obliged to appear before the Parliament (*Riksdag*) three or four times a year but it should also present the profit & loss accounts and balance-sheet. The Parliament is responsible for its approval at the

⁷³ W. F. FOX, *Understanding Administrative Law*, 3rd edition, Matthew Bender, New York, 1997, pp. 31 and 67.

⁷⁴ Art. 14.2 and Art. 14.3.

end of the financial year. But the most powerful tool in the hands of the *Riksdag* is the power of discharging the Governing Board of the central bank for cause. Finally, the central bank submits the Annual Report to the *Riksdag* and to parliamentary auditors. The authority of the Swedish Parliament is strong indeed, notwithstanding the amendments that have been introduced in the late '90s granting more independence to the central bank. The Swedish system has also other interesting features related to its tradition of "openness": the central bank has in the last few years adopted an explicit inflation target and has also communicated its analysis of the economy to the financial markets (Swedish Report par. 1.2).

Given all that, it is not surprising that in Sweden the major point under discussion in financial circles and public opinion is the lack of transparency of the EU bureaucracy and of the ECB altogether. They criticise the ECB because they judge its behaviour and its vision of the European economy as difficult to understand, and because they cannot have recourse to historic records, as they do for the Federal Reserve, given that a reasoned evaluation cannot be based on less than two-year old data.

Also the *UK Report* has at its core the question of accountability. The Bank of England is considered in economic circles as the most accountable central bank of Europe.⁷⁵ This is explained by the high number of reports delivered by the Bank: a first report to Parliament with its accounts for the previous year, a second report also to Parliament describing its behaviour in banking supervision, a quarterly inflation report on the results obtained in reaching the inflation rate established by the government and its previsions in reaching the inflation target for the future.⁷⁶ These reports, mostly the third on inflation target, are heavy burden for the Bank, and have a great impact on elected bodies. These obligations of the Bank should be added to the frequent appearance of the

⁷⁵ See DE HAAN - AMTENBRINK - EIJJFINGER, *supra* note 66, p. 183.

⁷⁶ See EUROPEAN MONETARY INSTITUTE, *supra* note 63, p. 10.

Governor in front of the Parliamentary committees, although its impact is diminished by the observation that the Bank does not stand alone in front of the Parliament, but through the intermediary of the Chancellor of the Exchequer or another Treasury Minister. The Bank of England has also reached a good record of transparency, mostly due to the announcement of the quantitative Government inflation target and the publication of the minutes of the meetings between the Chancellor and the Governor where the policy on interest rate is decided. Another important tool to ensure a good degree of transparency is the publication of the minutes of the Monetary Policy Committee, which are released on the Wednesday of the second week after the meeting takes place. The Bank of England Act of 1998 has entrusted the Monetary Policy Committee with the responsibility of setting interest rates on the basis of the Government's inflation target.⁷⁷

It is noteworthy that transparency and legitimacy are the issues that have inspired most of the criticism on the acceptance of the euro in the English public opinion and informed commentators. A secretive and only partially accountable system such as that of the ECB is hardly acceptable - argues for example Prof. Buiter, expressing the view of most of the English academic world - because it will hardly survive the unavoidable failures of the system.⁷⁸ Such framework,

⁷⁷ Id. The minutes of the meetings of the Monetary Policy Committee are visible also in the web-site of the Bank of England, at the following address: <http://www.bankofengland.co.uk/>.

⁷⁸ See W. H. BUTER, *Alice in Euroland*, in "Journal of Common Market Studies", 1999. The European Parliament shares the same views. In 1999, for example, the Committee on Economic and Monetary Affairs of the European Parliament "calls again for decisions taken at meetings of the ESCB Governing Council to be published, stating explicitly the arguments for and against the decision taken, as well as the reasoning used in reaching these decisions" and "considers it necessary, in the interests of transparency and credibility, that the ESCB should make it clear how monetary policy is intended, over and above the objective of price stability". See EUROPEAN PARLIAMENT, COMMITTEE ON ECONOMIC AND MONETARY AFFAIRS AND INDUSTRIAL POLICY, *Resolution on the annual report for 1998 of the European*

characterised by an excessive degree of rigidity and lack of openness, will not be able to evolve in a true political unit and will be subject to crisis of legitimacy should an economic crisis, such an asymmetric shock, intervene. This interpretation, based on economic reasoning, highlights the difficulty of justifying the decision of the ECB not to publish the minutes of the committees and the Council for fear that the members coming from the national central banks would not be free to support the interests of the euro-zone as a whole should they be in conflict with the national interest (UK Report par. 3.2).

One important institutional dialogue with both the Parliament and the Government exist in *Spain*, where the Bank of Spain has the obligation to report on the objectives and the implementation of monetary policy and to publish every year the objectives of monetary policy for the year with the implementation methods. Also the budget should be submitted to Parliament for approval (although the parliamentary consent is not binding). In addition to that, the Governor may be required to attend the meetings of the Fiscal and Finance Policy Council, a co-ordinating body gathering the representatives of central and regional governments (Spanish Report par. 1.2).

Also in *Greece*, a country where the question of the independence and accountability of the central bank has been highly debated in the political arena under the aegis of "*Can we have a democracy without a demos?*" there is a dialogue with the Parliament: one parliamentary committee is competent for

Central Bank, 4 May 1999. On the 5th of July 2000 the ECB has presented its 1999 Annual Report to the European Parliament. The latter has adopted a resolution on this report: the European Parliament, on the one hand, congratulates the ECB for its capacity of assuring a low rate of inflation and interest rates in the Euro zone countries but, on the other hand, urges the ECB to enhance its level of transparency requiring, for example, the publication of the minutes after each meeting with the explanation of the choices of monetary policy. It is interesting to note that such request does not include the votes cast by the members of the Council. This Report is visible in the web site of the European Parliament, at the following address: <<http://wwwwdb.europarl.eu.int/oeil/oeil.Res112>>.

expressing his opinion regarding the suitability of the candidates for the appointment as governors and the central bank is obliged to publish its annual report and the financial statements (Greek Report par. 1.3.3).⁷⁹

We can thus conclude on the question of accountability of central banks recognising that all the States under observation have modified the statute of their central banks, enhancing their independence *vis-à-vis* the political powers and eliminating external influences, but keeping at the same time their reporting commitments and sometimes even reinforcing them, as in the case of the Bank of England.

In some cases, these powers of control by political institutions have merely been transferred from euro-related areas to *non euro-related areas* within the same central bank. We can take the example of the French "*Conseil de la politique monétaire*", entrusted with the task of explaining to the nation the monetary policy carried out by the ESCB, which has been kept only for functions unrelated to the ESCB. The maintenance of this council has been justified by the French reporter on the ground that the Senate acknowledged the importance of this body for the democratic legitimacy of the Bank of France (French Report par. I.A)). More generally, it cannot be denied that it is sometimes difficult to eliminate bodies that have played an important role in the past, but which have now lost some of their justification. We can also take the example of *Belgium*, where Law of 22 March 1993 had already restricted the large power of the Minister for Finance to resist the execution of the measures adopted by the Bank that were thought contrary to the law, statutes or interests of the State, as well as the right of the Government Commissioner to suspend the decisions of the

⁷⁹ The phrase reported was pronounced by Tsoukalis, professor at the Athens University and former counsellor of prime minister Papandreou, as specified in the Greek Report par. 1.3.3.

On the reporting requirements of the Bank of Greece, *see also* EUROPEAN MONETARY INSTITUTE, *supra* note 63, p. 17.

National Bank if contrary to the same parameters. Such power, whose exercise had been limited to the existence of legal grounds by the reform of 1993, has now been restricted exclusively to non-ESCB related tasks of the Bank (Belgian Report par. 2.1.3). Finally, we can make reference to the case of *Spain*, where the above-mentioned Fiscal and Financial Policy Council, entrusted with the task of taking rules on financial discipline for regional governments, has been set up with a jurisdiction centred on non monetary policy issues.

3. Public Opinion and Institutional Features

The National Reports explain the different attitudes towards the euro using a dynamic and country-oriented approach. In some States, for example, the level of acceptance of the euro can be found in the low degree of confidence in national governments, such as in Belgium, Greece and Italy, where the euro tend to be considered as a remedy to internal evils (Belgian Report par. 1.2.1); in some other States it can be identified in the pride put on the national currency, as in Germany (German Report - introduction); in others it may reside in the enthusiastic support towards the European integration process, such as in Italy and Spain (Italian Report par. 1.1; Spanish Report par. 2.1). These results largely coincide with those suggested by other studies, based on different types of approaches. This is for example the case of the Müller-Peters-Papermans-Kiell Report, which builds up a map of pro/against euro countries based on psychological factors.⁸⁰

⁸⁰ MÜLLER-PETERS-PAPERMAN-KIELL, *The psychology of the EMU. A cross-national study of the attitudes towards the euro*, IAREP, International Association for Research in Economic Psychology, Journal of Economic Psychology. This paper can be consulted at the following web address: <http://www.wiso.uni-koeln.de/wisopsy/forschung/euro/>. This report puts forward other factors that can have an influence on the public opinion on the euro, such as the high level of national patriotism (in Finland, Sweden, Denmark, Germany, Austria and Greece), and the pride states put on cultural and historical symbols (mostly Italy).

They also coincide by far and large with the data of the Eurobarometer research. This paragraph will accordingly refer to them (even though they are limited to a short period of time, *i.e.* autumn 1999) as they describe the state of the opinion at an aggregate level in all the member States, making it possible a cross-country comparison.⁸¹ According to the Eurobarometer data, traditionally *euro-sceptic countries* are UK, Denmark and Sweden (correspondingly, only 25%, 42% and 43% of the public opinion in favour of the euro) whilst *euro-enthusiastic countries* are Italy (85% of public opinion in favour of the euro), Luxembourg (79%), Ireland (78%) and Belgium (77 %). Countries with a positive attitude towards the euro coincide usually with those favouring the European Union as a whole, even though there are some exceptions, as shown by Belgium where the public opinion has welcomed well the introduction of the euro notwithstanding a medium degree of acceptance of European integration (Belgian Report par. 1.2.1).

It could be interesting from a political/legal point of view to see if the degree of acceptance of the ECB model (and its degree of accountability) has been influenced by the legal traditions and the model of central bank of the country under study.

According to the Eurobarometer results, in 1999 the *countries which were more favourable to the introduction of the ECB* were The Netherlands (85% of favour) and Ireland (77%). On the other side, UK (44%), Spain (62%), Greece and Denmark (64%) expressed their disagreement. The preference expressed by *The Netherlands* is to be considered as normal, given that the Dutch central bank is traditionally highly independent, at least *de facto*. It is true that Art. 28 of the Dutch central bank established a mechanism of instructions from the government to the central bank, but this provision has never been used. Its

⁸¹ The results of the Eurobarometer can be seen at the following address: http://europa.eu.int/comm/dg10/epo/eb/eb52/eb52_ann.pdf. These percentages are presented

existence (and the theoretical possibility of its use) has instead been the source of a dialogue between the bank and the political institutions. Another crucial factor for the success of the ECB in this country is Mr. Duisenberg, the current President of the ECB, being the former President of the Dutch central bank.

Similarly comprehensible, although for opposite reasons, is the behaviour of *UK, Greece, Spain, Austria* and *Portugal*, that before the reforms were used to central banks subservient to the political powers. Less direct is the link between the high support of the ECB and the legal traditions in central banking of *Belgium* and *Italy* (both 74% in favour); this appreciation can perhaps be justified on the basis of the widespread acceptance shown by these two States towards the euro. The favourable position of *Sweden* towards the ECB can also give rise to some perplexities. Sweden is not only one of the more convinced anti-euro countries of Europe, but the *Riksbank*, the oldest central bank in the world, has also traditionally been under the control of Parliament.

The Eurobarometer data on the *accountability of the ECB to the European Parliament* can perhaps shed light on some controversial points. Following the Eurobarometer report, the States are more likely to trust an accountable ECB if their correspondent model of central bank provides mechanisms of accountability through political oversight. This is the case of Finland, Sweden and Denmark. The example of *Sweden* is especially relevant, as its support for the ECB can be justified only if this latter is accountable to the European Parliament (the support of the Swedish public opinion for this kind of accountability being significantly high). *France* shows the highest support for an accountable central bank; this enthusiasm can perhaps be interpreted more as a will to contrast a German-like independent institution than as a real trust in parliamentary controls, given the secondary role exercised traditionally by Parliament *vis-à-vis* the Bank of France if compared to the Government. At the

in the Annex of Eurobarometer 52 / Eurobaromètre 52. It takes into accounts data for the period October-November 1999 and has been released in April 2000.

opposite level (low degree of acceptance) we can find *UK* (only 59% of public opinion in favour of an accountable ECB) followed at a distance by *Portugal* (69%), *Germany* and *Spain* (73%). The distrust (or, maybe, lack of interest) in an accountable central bank conforms with the Portuguese and German traditions of central banking, as their central institutions have been exempted from significant forms of accountability; more peculiar is the case of Spain as the Bank of Spain, as already seen, is subject to relevant controls *vis-à-vis* Parliament and Government. This situation can maybe be explained with reference to a possible separation between the political will and the opinion of the public at large.

It is now time to draw some conclusions on the relationship between, on one side, the legal status of the national central banks as described in the National Reports and, on the other side, the national preferences on the euro and the ECB (and its character of accountability) expressed by the public opinion and summarised so far.

Firstly, the data described above can be interpreted as a sign of the *uniqueness of the situation of UK*; as a matter of fact the opinion expressed by the public and its distrust for the euro, EMU and all its accessories has no relation with the current status of the Bank of England and the English legal traditions. The majority of the English opinion is simply opposed to the European integration process as a whole.

Secondly, the *public opinion on the ECB* registered in others countries is largely a reflection of the country-specific legal and economic central banking traditions. At least this is clearly the case for Spain, Greece, Austria and Portugal. More surprising is the support in favour of the ECB registered in Italy, Belgium and France: in these countries the public opinion shows a great interest in this kind of institution notwithstanding its unfamiliar features. The position of Sweden is also not well-defined, as the Swedish public opinion is of the view

that the euro is not to be trusted (only 43% of support) but at the same time indicates its preference for the ECB at the condition (however) that it should be accountable.

Finally, the percentages on the *accountability of the ECB* described above seem to confirm the direct relationship between the preferences of the national public opinion and the legal/economic traditions of central banking of the country. The only controversial case remains that of France, as it highly supports a parliamentary accountable ECB despite the model of responsibility proposed does not fully conform to it.

Conclusions

The third stage of the European Monetary Union is to be considered as a transitional and final phase, designed for the smooth introduction of the euro and intended to enable the States to prepare their economic and legal framework. The new currency, which, from January 1, 1999 has been existing only as scriptural money, will start to circulate in cash form from January 1, 2002.

During this period, the States are called to introduce modifications in their legal order. It is true that the legal reforms related to the status of the national central banks entered into force well before the 1st of January 1999, as they were considered the prerequisites for the States to accede to EMU. However, such reforms neither followed the same patterns nor reached a complete homogeneity: harmonisation is not necessary in this field. This is probably also the reason why the discussion on the euro and EMU has been livelier in the outer countries than in the participating ones.

Different solutions have however been adopted by the States member of EMU for the introduction of the euro into the internal order whenever the EC legislation, based mainly on Regulations No. 1103/1997 and No. 974/1998, either granted them some scope of discretion, or did not regulate the matter, or regulated it through soft law, for example with recommendations.

The States in such process of adaptation have used different legal approaches. Some States have considered the introduction of the euro as a reason for changing all the internal provisions in contradiction with the EC principles on the euro, some others have drafted internal acts reproducing literally the words of the EC regulations on the euro (including or not some modifications), and others have simply make reference to the EC acts without restating them.

Finally, the States still have different preferences toward the concepts of independence and accountability of the central bank according (partially) to their legal traditions on central banking, even though the major divergence consist in the acceptance/refusal of the euro *per se*, and not on the configuration of the ECB.