

University of Luxembourg
Faculty of Law, Economics
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Elements of EU Central Banking Law

Series of Lectures in Central Banking Law: Lectures 3-5

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F. EMU: the way forward

A. The EMU as an asymmetrical system by design

1. The asymmetry as embedded in the Treaties

Legal basis: **Article 3(4) TEU**

In the ‘trichotomy’ of categories of EU competences (exclusive – shared – supportive, coordinating, supplementing)

- **(Single) monetary policy** for the MS whose currency is the euro: **exclusive competence (TFEU, Articles 3(1), point (c) and 119(2))**
- **Economic policies of MS: close coordination (TFEU, Articles 5(1) and 119(1))**

A. The EMU as an asymmetrical system by design

2. The four pillars of the Economic Union

(1) **Coordination of economic policies** – broad guidelines of economic policies (TFEU, Articles 120-121 and 136(1))

(2) **Fiscal discipline:**

(2.1) **“Prohibitions”**

- Prohibition of monetary financing of national fiscal expenses (**Article 123**)
- Prohibition of financing national fiscal expenses by privileged access to financial institutions (**Article 124**)
- “No bail out” clause (**Article 125**)

A. The EMU as an asymmetrical system by design

2. The four pillars of the Economic Union (*cont'd*)

(2.2) Excessive deficit procedure (Article 126)

Noteworthy Article 126(10): *“The rights to bring actions provided for in Articles 258-259 [i.e., infringement procedure] may not be exercised within the framework of paragraphs 1-9 of this Article”*

(3) **Economic solidarity** (Article 122)

(4) **Sovereign crisis management mechanism** (Article 136(3)): *the only amendment to the TFEU as a response to the current fiscal crisis in the eurozone*

B. Six key elements of the Monetary Union

1. General overview

- (1) **Primacy (but not exclusivity) of ‘monetary stability’** within the ‘**hierarchy**’ of objectives for the Eurosystem (see further below, under 2)
- (2) No ‘**financial stability**’ mandate (argument from phrasing of TFEU, **Article 127(5)-127(6)**)
- (3) The ECB (an EU institution) as the “**hub**” in the Eurosystem – the “spokes” being the NCBs—Members of the Eurosystem: principle of decentralisation

Note: the ECB as a “hub” also in the SSM – the “spokes” being the NCAs of the participating MSs (including, as the case is, NCBs): no application of the principle of decentralisation

B. Six key elements of the Monetary Union

(4) An independent and accountable ECB – with autonomous regulatory powers (TFEU, Article 132)

(5) Powers of NCBs within the Eurosystem: Articles 14.3 and 14.4 ESCB and ECB Statute

(6) Tasks of the ECB:

- **basic, within the Eurosystem (TFEU, Article 127(2))**
- **specific (Article 127(6))**
- **other**

B. Six key elements of the Monetary Union

2. The primary and the secondary objective of the Eurosystem

(1) The “primary” and the “secondary” objectives of the Eurosystem are laid down in **Articles 127(1) and 282(2), second and third sentences TFEU** (repeated *verbatim* in the **ESCB/ECB Statute**):

- The **primary objective** is to maintain price stability. The ECB and the NCBs of the Member States whose currency is the euro are, therefore, competent, within the Eurosystem, for defining and implementing monetary (and exchange-rate) mainly to safeguard price stability.

B. Six key elements of the Monetary Union

2. The primary and the secondary objective of the Eurosystem (*cont'd*)

- The **secondary objective** is without prejudice to the primary one; thereunder, the Eurosystem must:
 - support the general economic policies in the EU to contribute to the achievement of its objectives as laid down in **Article 3 TEU**; and
 - act according to the principle of an open market economy with free competition, favouring an efficient allocation of resources (a “generic” statement on respect for market economics) and in compliance with the principles set out in **Article 119(3) TFEU**

B. Six key elements of the Monetary Union

(2) In this context, the following is further (briefly) noted:

- *First*, the rationale behind this hierarchy of objectives lies within the prevailing view that the Eurosystem can only pursue its secondary objectives if the primary one, i.e., price stability, has been assured. Accordingly, it is expected that its basic tasks are performed with the aim to combat inflation (or disinflation) and, only if this is achieved, to influence growth, employment, environmental and other conditions. *On the other hand*, the Eurosystem does not have a “dual primary objective”. This is the case with some other central banks, such as the US Federal Reserve System (or “Federal Reserve”, “Fed”), i.e., the US central banking system, which has a dual mandate and thus defining and implementing its monetary policy on the dual basis)

B. Six key elements of the Monetary Union

(2) In this context, the following is further (briefly) noted:

- *Second*, the general economic policies in the EU which the Eurosystem must support have recently come to include a high level of protection and improvement of the quality of the environment. In this respect, in accordance with the **2021 “European Climate Law” (Regulation (EU) 2021/1119)**, a binding objective of climate neutrality in the EU by 2050 has been set in pursuit of the long-term temperature goal set out in the 2015 Paris Agreement (approved in the EU by **Council Decision (EU) 2016/1841** of 5 October 2016), which forms part of the general economic policies in the EU

C. The basic tasks assigned to the ECB within the Eurosystem

1. The individual basic tasks

(1) definition and implementation of the EU **monetary policy** (see further below, under 2)

(2) conduct of **foreign-exchange operations** consistent with the provisions of **Article 219 TFEU**

(3) holding and management of Member States' **official foreign reserves**

*(2) + (3) refer to the **foreign-exchange policy in the euro area***

(4) **promotion of the smooth operation of payment systems,**

- wholesale payment systems (**TARGET 2**)
- retail payment systems (**SEPA**)

C. The basic tasks assigned to the ECB within the Eurosystem

2. In particular: definition and implementation of the single monetary policy

2.1 The three periods:

1999-2008: the initial period under (on average) normal conditions

2008-2021: the impact of the three crises:

- the (2007-2009) Global Financial Crisis
- the (2010-2018) Euro area Sovereign (Fiscal Crisis)
- the (2020-) Pandemic Crisis

Since mid-2021: new inflationary pressures (*inter alia*, due to the war in Ukraine, the energy crisis and the supply chain crisis – currently, under relative control)

C. The basic tasks assigned to the ECB within the Eurosystem

2. In particular: definition and implementation of the single monetary policy (*cont'd*)

2.2 Monetary policy instruments

(1) The provisions of the ECB/ESCB Statute:

Article 18.1:

“In order to achieve the objectives of the ESCB and to carry out its tasks, the ECB and the [NCBs] may:

- *operate in the financial markets by buying and selling outright (spot and forward) or under repurchase agreement and by lending or borrowing claims and marketable instruments whether in euro or other currencies, as well as precious metals; [and]*
- *conduct **credit operations** with credit institutions and other market participants, with lending being **based on adequate collateral.**”*

C. The basic tasks assigned to the ECB within the Eurosystem

2. In particular: definition and implementation of the single monetary policy (*cont'd*)

2.2 Monetary policy instruments

(1) The provisions of the ECB/ESCB Statute:

Article 19:

“19.1. Subject to Article 2, the ECB may require credit institutions established in Member States to hold minimum reserve on accounts with the ECB and national central banks in pursuance of monetary policy objectives. (...).

19.2. For the application of this Article, the Council shall (...), define the basis for minimum reserves and the maximum permissible ratios between those reserves and their basis, as well as the appropriate sanctions in cases of non-compliance.”

C. The basic tasks assigned to the ECB within the Eurosystem

2. In particular: definition and implementation of the single monetary policy (*cont'd*)

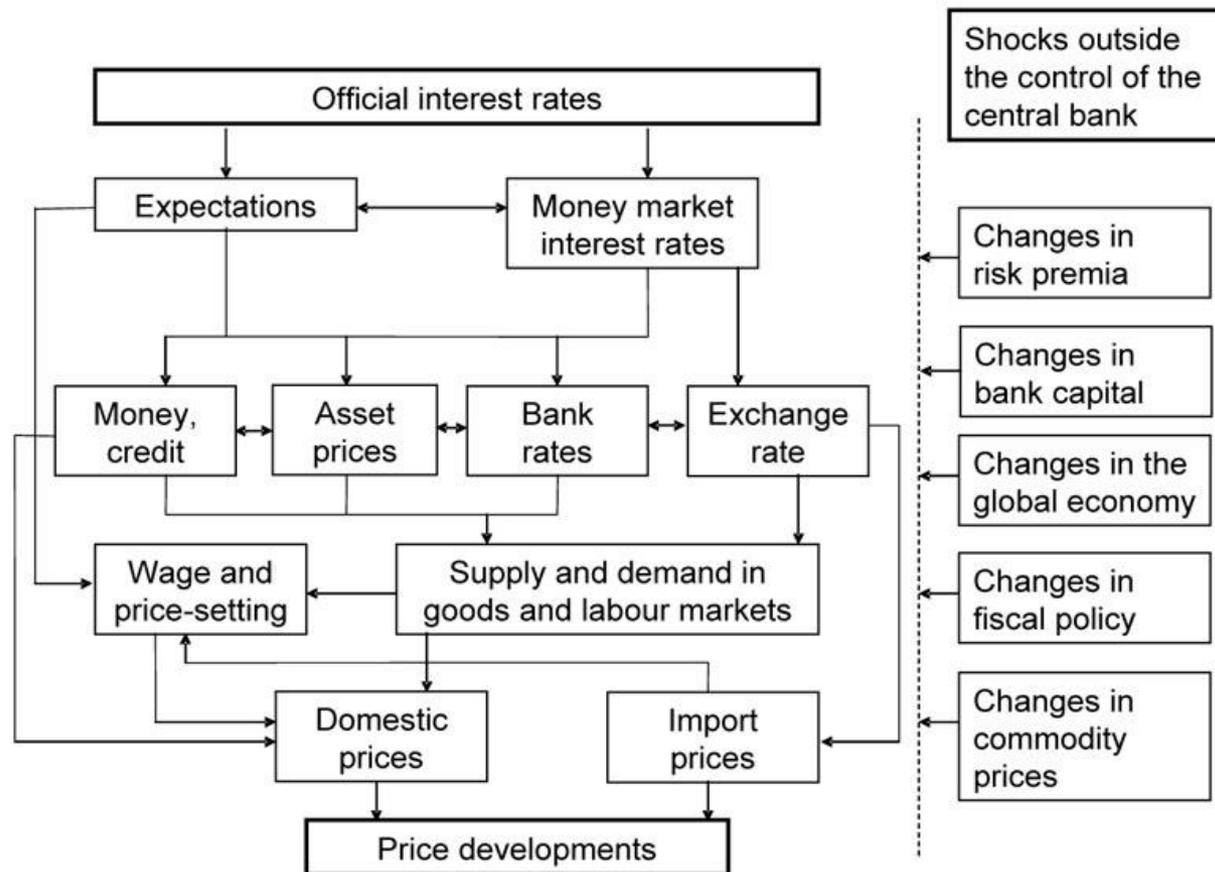
2.2 Monetary policy instruments (*cont'd*)

(2) Under the **general framework** the ECB and the NCBs of the euro area Member States have the following instruments for the implementation of monetary policy:

- conduct of **open market operations**
- offering of **standing facilities (marginal lending facility + deposit facility)** to credit institutions
- imposition on credit institutions (and other categories of financial service providers) to **hold minimum reserves** on accounts with the Eurosystem

C. The basic tasks assigned to the ECB within the Eurosystem

The mechanism for the transmission of monetary policy effects



C. The basic tasks assigned to the ECB within the Eurosystem

TABLE 1:	
A summary of the key ECB legal acts and instruments governing the Eurosystem monetary policy implementation framework	
Legal act/instrument	Aspects addressed
Eurosystem monetary policy operations	
General Documentation Guideline	general aspects of the implementation framework
Valuation Haircut Guideline	valuation haircuts applied to the implementation framework
Guideline (EU) 2019/671	domestic asset and liability management operations by NCBs
Decision (EU) 2019/1743	remuneration of deposits, balances, and holdings of excess reserves
Guideline 2007/830/EC	monetary and financial statistics
Guideline 2008/596/EC	management of the foreign reserve assets of the ECB by NCBs
Minimum reserve system	
Reserve Requirements Regulation	application of minimum reserve requirements

C. The basic tasks assigned to the ECB within the Eurosystem

2. In particular: definition and implementation of the single monetary policy (*cont'd*)

2.3 “Unconventional” monetary policy instruments (after the Global Financial Crisis): temporary” framework (asset purchase programmes)

- Outright Monetary Transactions (‘OMTs’) programme (never activated)
- *third* covered bond purchase programme (‘CBPP3’) (Decision ECB/2014/40)
- asset-backed securities purchase programme (‘ABSPP’) (Decision ECB/2014/45)
- (secondary markets) public sector purchase programme (‘PSPP’) (Decision ECB/2015/10)
- corporate sector purchase programme (‘CSPP’) (Decision ECB/2016/16)
- PEPP (during the pandemic crisis)

C. The basic tasks assigned to the ECB within the Eurosystem

3. In particular: on green central banking within the Eurosystem

(1) As part of the “**Climate Action Plan**” of 8 July 2021 and on the basis of a detailed “**Roadmap of climate change-related actions**” annexed thereto, the Governing Council of the ECB announced on **4 July 2022** its decision to take further steps to include climate change considerations in the monetary policy framework (“**Climate Agenda 2022**”). This relates to the following aspects:

- corporate bond holdings;
- the collateral framework;
- climate-related disclosure requirements for collateral; as well as
- enhanced risk assessment tools and management – including “decarbonisation”

C. The basic tasks assigned to the ECB within the Eurosystem

3. In particular: on green central banking within the Eurosystem (*cont'd*)

(2) On **30 January 2024**, the ECB decided to expand its work on climate change following the stocktake of its climate actions and an adjustment of its work plan in the light of the changing environment and improvements in data availability and methodologies. In this respect, three focus areas were identified to guide its activities in 2024-2025:

- the impact and risks of the transition to a green economy, especially the associated transition costs and investment needs;
- the increasing physical impact of climate change, and how measures to adapt to a hotter world affect the economy; and
- the risks stemming from nature loss and degradation, how they interact with climate-related risks and how they could affect the ECB's work through their impact on the economy and financial system.

C. The basic tasks assigned to the ECB within the Eurosystem

3. In particular: on green central banking within the Eurosystem (*cont'd*)

(3) It is finally worth noting that, taking as a benchmark the initial “dual rate” embedded in the TLTRO programmes, as well as the initiation by the Bank of Japan in December 2021 of a “climate change-related lending program”, proposals have been tabled for the introduction of “**green dual interest rates**”. On the basis of these proposals, lower (even zero) interest rates should be applied to lending for green projects, which would allow more investments in renewable energy projects (including for housing purposes). These include (but are confined to) an “open letter” to the GC of 1 June 2022 by a group of academics and economists, backed (in January 2024) at political level by the French President (Emmanuel Macron).

- The ECB’ stance on this particular aspect is cautious due to the lack of data (yet) to validate green labels.

D. Other tasks and powers conferred on the ECB

1. General Overview

(1) **Specific tasks** in relation to the prudential supervision of (mainly) credit institutions (**Article 127(6) TFEU**):

- in relation to the operation of the **European Systemic Risk Board (ESRB)** within the European System of Financial Supervision (**ESFS**); and
- within the **Single Supervisory Mechanism (SSM)**

(2) Power to **issue euro-denominated banknotes** and exclusive right to authorise the issue of such banknotes by NCBs (**Article 128(1) TFEU**)

D. Other tasks and powers conferred on the ECB

1. General Overview (*cont'd*)

(3) Forthcoming: power to issue the digital euro (under a Regulation to be adopted by virtue of **Article 133 TFEU**)

(4) Power to prohibit the provision of emergency liquidity assistance (ELA) by the NCBs-Members of the Eurosystem in the ELA Mechanism (Article 14.4 of the ESCB/ECB Statute) – see further below, under 2

(5) Determination that a credit institution is “failing or likely to fail” within the Single Resolution Mechanism (SRM)

D. Other tasks and powers conferred on the ECB

Table 2: Allocation of tasks between ECB and NCAs

	Significant supervised entities	Less significant supervised entities
Granting and withdrawal of authorization	ECB	ECB
Assessment of applications for the acquisition and disposal of 'qualifying holdings'	ECB	ECB
Conduct of micro-prudential supervision	ECB	NCA
Conduct of macro-prudential regulation	NCA or NDA	NCA or NDA
Carrying out supervisory tasks in relation to recovery plans and early intervention	ECB	NCA
Conduct of stress-tests	ECB	NCA
Participation in colleges of supervisors	ECB	NCA
Protection of the economic interests of consumers transacting with financial service providers	NCA	NCA
Prevention of the use of the financial system for the purposes of money laundering and terrorist financing	NCA	NCA

D. Other tasks and powers conferred on the ECB

2. In particular: lending of last resort within the euro area

Related to but different from the monetary policy operations is the **provision of emergency liquidity assistance (ELA)**:

- under conditions of **‘constructive ambiguity’**;
- under **adequate collateral** and at a **higher interest rate** than in monetary policy transactions;
- to **‘solvent’ credit institutions exposed to illiquidity**;
- by the **NCBs-Members of the Eurosystem**; and
- under the **“control” of the ECB (Article 14.4 Statute)**

D. Other tasks and powers conferred on the ECB

2. In particular: lending of last resort within the euro area (*cont'd*)

Article 14.4 Statute:

“[NCBs] may perform functions other than those specified in this Statute unless the [GC] finds, by a majority of two thirds of the votes cast, that these interfere with the objectives and tasks of the ESCB. Such functions shall be performed on the responsibility and liability of [NCBs] and shall not be regarded as being part of the functions of the ESCB.”

NB: ELA does not constitute State aid if the conditions set out in para 62 of the Commission’s 2013 Banking Communication are met

D. Other tasks and powers conferred on the ECB

Table 3: The overall tasks conferred upon the ECB

Category of ECB tasks	Legal basis	Implementation in euro area Member States	Implementation in Member States with a derogation
1. <i>Basic</i> tasks (incl. monetary policy (within the Eurosystem))	Article 127(2) TFEU	Yes	No
2. <i>Other</i> tasks and powers (e.g., issuance of banknotes)	Several TFEU articles	Yes	As a rule, no
3. <i>Specific</i> tasks on the macroprudential oversight of the European financial system (within the ESFS)	Council Regulation 1096/2010 (based in Article 127(6) TFEU)	Yes	Yes
4. <i>Specific</i> tasks on the prudential supervision of credit institutions (within the SSM)	Council Regulation 1024/2013 (SSM Regulation, based on Article 127(6) TFEU)	Yes	Under the conditions of the ‘close cooperation procedure’

D. Other tasks and powers conferred on the ECB

Excursus 1: Allocation of tasks and competences between the ECB and the NCBs in the euro area in the context of European central banking law

Task or competence	ECB	NCBs	
		As monetary authorities	As NCAs
Authorisation of banknote issue	✓		
Issue of banknotes	✓	✓	
Definition and implementation of monetary policy	✓		
Oversight of payment systems – operation of the TARGET2 system	✓		
Granting and withdrawal of authorisation to credit institutions	✓		
Acquisition and disposal of qualified holdings in credit institutions	✓		
Micro-prudential supervision in relation to the specific tasks laid down in Article 4 SSMR (including stress tests)	✓ (for significant supervised entities)		✓ (for less significant supervised entities)
Micro-prudential supervision in relation to other aspects (apart from the specific task)			✓

D. Other tasks and powers conferred on the ECB

Excursus 1: Allocation of tasks and competences between the ECB and the NCBs in the euro area in the context of European central banking law (cont'd)

Task or competence	ECB	NCBs	
		As monetary authorities	As NCAs
Use of macro-prudential tools	✓ (exceptionally)		✓ (in principle)
Resolution planning	✓ (for significant credit institutions)		✓ (for less significant credit institutions)
Early intervention	✓ (for significant credit institutions)		✓ (for less significant credit institutions)
Lending of last resort (ELA mechanism)	Powers under Article 14.4 ESCB/ECB Statute	✓	

1. The Pringle case (27 November 2012)

(a) Interpretation of:

- provisions relating to the Union's exclusive competence (Articles 3(1), point (c), 3(2) and 127 TFEU)
- various provisions of the ESM Treaty relating to economic policy (Articles 2(3), 119-121, 122, 123, 125 and 126 TFEU)
- Article 4(3) TEU
- Article 13 TEU (role allocated to Commission, ECB and Court)
- the general principle of effective judicial protection

1. The Pringle case (*cont'd*)

(b) Rulings

(1) The above TEU and TFEU Articles and the general principle of effective judicial protection do not preclude the conclusion between the Member States whose currency is the euro of an agreement such as the Treaty establishing the ESM or the ratification of that Treaty by those Member States

(2) The right of a Member State to conclude and ratify the ESM Treaty is not subject to the entry into force of **Decision 2011/199 of the European Council**

Important: Article 136(3) TFEU was not even necessary, since MS were entitled to conclude the ESM Treaty as an international treaty outside EU law

1. The Pringle case (*cont'd*)

(b) Rulings

(3) The *Pringle* ruling was the first seminal judgment in which the use of novel and flexible measures to guarantee financial assistance between Member States was assessed and deemed to be lawful under EU law.

(4) The Court also observed that the TFEU does not contain a definition of the Eurosystem's monetary policy. Thus, on the basis of a functional approach, the TFEU provisions related to this policy refer to its objectives (pursuant to Articles 127(1) and 282(2), namely, to maintain price stability) rather than its instruments.

2. The Gauweiler case (16 June 2015)

(a) Interpretation of:

- **Articles 119, 123(1) and 127(1)-(2) TFEU**
- **Articles 17-24 of the ESCB and ECB Statute**

(b) Ruling

The above TFEU – ESCB/ECB Statute Articles must be interpreted as permitting the ESCB to adopt a programme for the purchase of government bonds on secondary markets, such as the OMT programme – under conditions though

3. The United Kingdom vs. ECB case (4 March 2015)

Annulment of the ECB’s “**Eurosystem Oversight Policy Framework**” obliging central counterparty clearing systems to be located within a Eurosystem MS – **Point (101)**:

*“(…) In the absence of an explicit reference to the clearing of securities in **Article 22 of the Statute**, it must be concluded that the choice of the term ‘clearing and payment system’ is intended to make it clear that the ECB has competence to adopt regulations to ensure efficiency and safety of payment systems, including those with a clearing stage, rather than granting it an autonomous regulatory competence in respect of all clearing systems.”*

1. The case for completing the EMU

- Tackling persisting economic and social divergences
- Tackling remaining sources of financial vulnerability
- Tackling high debt and increasing collective stabilisation abilities
- Increasing the efficiency and transparency of the EMU governance

Establishment of (1) a “Financial Union”, (2) an “Economic and Fiscal Union” and (3) a “Political Union”

2. Main pillars

(a) Strengthening the EMU architecture and anchoring democratic accountability:

1. primary and secondary objectives of the Eurosystem: the case for promoting sustainability
2. institutions and rules for a fully-fledged EMU

(b) Re-convergence in a more integrated **“Economic and Fiscal Union”**

(c) A genuine **“Financial Union”**: beyond the Banking Union and the Capital Markets Union (currently, the **“Savings and Investment Union”** project)

TABLE 4: A simplified central bank balance sheet

Assets	Liabilities
1. Gold and reserves	1. Banknotes in circulation & CBDCs
2. Claims on banks related to monetary policy operations (“open market operations” & “marginal lending facility”)	2. Liabilities to banks related to monetary policy operations (“reserve accounts” and “deposit facility”)
3. Other claims on banks	3. Liabilities to other parties (in domestic or foreign currencies)
4. Securities issued by Governments – firms – financial firms	4. Other liabilities
5. Other claims (in domestic or foreign currencies)	5. Revaluation reserves
6. Other assets	6. Capital and reserves