

# THE EU SINGLE MARKET: FREE MARKETS, PROTECTIONISM AND EXCESSIVE REGULATION



Centrum für  
Europäische  
Politik

by **Frits Bolkestein and Lüder Gerken**

The future viability of the European Single Market is at risk, although politicians on the European level and in the Member States would certainly dispute that and tend to portray the whole set-up in rosy colours.

But it is much too easy to proclaim the successful achievements of the past and ignore the alarming developments that are jeopardizing the sustainable continuation of the Single Market.

Without doubt, the Single Market is the starting point and heart of in-depth European integration. It has brought us the elimination of trade barriers, the dissolution of what were usually state-protected monopolies and last but not least, extensive deregulation. It is thus the central reason for the prosperity which we enjoy today in Europe.

But it is becoming increasingly and urgently clear that this heart is no longer beating properly, so that it is no longer capable of providing the remaining organic aspects of European integration with the necessary strength.

Four findings indicate that Europe's Single Market policy is moving in the wrong direction. In the end, this could result in the failure of the Single Market project – and with it probably also the failure of European integration altogether.

**First finding: the European Union is increasingly losing its ability to protect the Single Market from intensifying protectionism on the part of the Member States.**

It is part of the fundamental intrinsic nature of the European Union to protect barrier-free movement of goods, services, persons and capital from being undermined by protectionist measures of the Member States. However, this is increasingly no longer possible.

The reasons for this can be found on the one hand in the increasingly frequent and blatant attempts by Member States to assert their protectionist interests by explicitly breaching the Single Market rules.

One example of this is Spain's attempts to prevent a German utility company from taking over a Spanish one. The European Commission ascertained in accordance with the rules that there are no objections to this takeover in terms of competition law. But even so, national egoistic considerations led Spain to use a constant flow of new tricks to prevent the takeover, although this violates EU law. Another example is the way Germany fends off foreign competition right across the board under the guise of "services of general interest". On the other hand, the European Commission as guardian of the treaties frequently fails to exert sufficient pressure when asserting the interests of the Single Market. One example for this is its faint-hearted approach to dealing with German state interventionism in saving the Bankgesellschaft Berlin, which had been brought to the brink of bankruptcy by mismanagement and structures so closely intertwined with state policy as to give rise to suspicions of corruption. The EU only approved of a reorganization package funded by the German tax payer on condition that the Bankgesellschaft and its subsidiary the "Berliner Sparkasse" (Berlin savings bank) be sold in a non-discriminating procedure. But such a procedure which discriminates no bidder contradicts paragraph 40 of the German Banking Act. This stipulates in clear terms that apart from the already existing independent "Freie Sparkassen", only public law institutes are allowed to use the name "Sparkasse" (savings bank), so that a private buyer would have to sacrifice the name "Berliner Sparkasse". Instead of relentlessly demanding an amendment to paragraph 40, which is by all means possible under EU law, the Commission opted to settle for the dubious assurance from Germany that in the future this paragraph would be "interpreted" in accordance with EU law. How this can happen in view of the unambiguous wording remains to be seen, and divergences in the interpretation of the German assurance already emerging today show that the necessary acceptance simply does not prevail in Germany.

But the more frequently the Commission fails to fulfil its duty as guardian of the Single

# THE EU SINGLE MARKET: FREE MARKETS, PROTECTIONISM AND EXCESSIVE REGULATION



Centrum für  
Europäische  
Politik

Market, the weaker it will be in future disputes. And the more frequently the Member States successfully undermine the Single Market, the less willing will they be to respect its basic rules. This automatically results in an erosion of the Single Market.

Fundamental significance should therefore be attributed to the latest proposal for a regulation by the Commission which would considerably confine Member State protectionism in the movement of goods. The background: Article 30 of the EC Treaty and prevailing case law by the European Court of Justice permit an import ban only in the exceptional case when a product from another Member State would jeopardize certain national objectives in the import country, particularly regarding health or consumer protection. This exception is subject to massive abuse, for instance by using the pretext of health protection to protect the domestic industry from foreign competition: the affected foreign companies have to produce counter-evidence in expensive procedures usually prescribed by the import country so that their products are no longer competitive in terms of their price, thus fulfilling the protectionist objective.

The Commission estimates that such abuse costs the EU's economy more than €150 billion p.a. The Centre for European Policy estimates that at least 2.5 million new jobs could be created by preventing abuse along these lines. The regulation now proposed by the Commission reverses the burden of proof: a country which wants to issue an import ban has to prove why the goods in question would be harmful for instance to health. This does not place any restrictions on justified health protection or any other kind of justified protection. It merely makes protectionist abuse much harder, if not completely impossible.

The Commission must push through this regulation. It is one of the most crucial projects to preserve the Single Market. Whether this will succeed is dubious: influential circles in the Member States are already making detailed plans behind the scenes to save their protectionist sinecures and overthrow the proposed regulation.

**Second finding: the Single Market is increasingly losing its significant role as pioneer in cutting back excessive regulation; on the contrary, it is increasingly turning into a high-regulation zone itself.**

While it is currently the declared objective – yet again – of the European Commission to reduce bureaucratic burdens, the fact is that all such endeavours in the past have not been particularly successful, and furthermore, this will not have any effect on a far more fundamental problem: for several years now, the Single Market's legislature itself has been undergoing a shift in paradigms.

The original intrinsic nature of the Single Market consisted in the fundamental ability to sell goods made in one Member State in accordance with its national legislation, in other Member States. This is the principle of mutual recognition, or the principle of the country of origin.

However, today this principle is increasingly pushed into the background by the attempt to introduce harmonisation measures which prescribe statutory regulations "on a high level" as uniformly as possible throughout Europe, as regularly formulated in the EU's legal instruments. The result of this policy is not to cut back national over-regulation as a consequence of competition, with over-regulation preventing dynamic economic growth and a corresponding increase in jobs; instead, it merely serves to standardise such over-regulation throughout Europe. In addition, special particularities and traditions of the individual Member States are all lumped together. This is exactly the opposite of what originally characterized the Single Market. Without doubt, this is one of the essential causes behind the increasingly sullen attitude to Europe shown by citizens in general, and entrepreneurs in particular.

One example of this is the services directive. The original version included the mutual recognition of Member State regulations as a means of implementing comprehensive freedom of services – a principle already

# THE EU SINGLE MARKET: FREE MARKETS, PROTECTIONISM AND EXCESSIVE REGULATION



stipulated in the EC Treaty. By contrast, the adopted version creates a uniform framework for national scopes of *restricting* the freedom of services. And as it is already quite clear today that the freedom of services cannot be achieved in this way, in article 16 paragraph 4 the directive opens the doors to extensive harmonisation of Member State regulations, in other words to cementing regulation instead of cutting it back. Here the points have been set in the wrong direction – probably irreversibly.

In this context too, the already mentioned regulation regarding article 30 of the EC Treaty and aiming at preventing protectionist abuse is once again of central significance, because following the services directive, this is the second major attempt by the Commission within a short period of time to assure the application of the principle of mutual recognition.

The success or failure of this project will dictate whether the EU is going to be capable or incapable of making a stand for markets with only the really necessary scope of regulation, in the interests of growth and jobs. If the EU should also fail in this second central project, it will forfeit its corresponding abilities for a long period of time, if not for ever.

This is a very real danger. At the moment, the relevant political groupings are intensively considering the reversal of this directive so that in analogy to the developments with the services directive, an EU-wide uniform health, consumer and other protection is introduced by "harmonisation on a high level".

**Third finding: the Single Market is being increasingly overloaded with social policy issues which are overburdening it.**

Month by month, the Member States can be heard to make the ever louder demand to protect the "European social model" throughout the EU; in doing so, the Member States are supported eagerly by politicians and civil servants in Brussels keen to extend their competences. On the surface, the aim is to make European integration more popular. But in fact, national politics are using this approach

to conceal their failure hitherto to renew their ailing social systems, and get rid of the existing pressure to introduce reforms, at least for the time being.

Quite apart from the fact that such a "European social model" does not even exist, because social policy differs greatly between the various Member States, the attempt to prescribe " a high level of social standards", for example by introducing minimum regulations, for two reasons poses a threat to the Single Market as a whole and must fail.

On the one hand, the harmonisation of social policy in the less advanced national economies which joined the EU in 2004 and 2007 would destroy a cost and thus competition advantage which up to now has at least partly compensated for the far lower labour productivity in these economies. That would really put the brakes on the catching-up process in these countries. (One possible and not quite improbable way out for these countries admittedly consists in assuming a "flexible" approach to applying European regulations, as already practised today in many Member States. After all, there is a certain justification to the saying that EU laws are initiated by the Italians, written by the French and heeded by the Germans and Dutch.)

On the other hand, in some branches the real competitors for Western Europe's highly developed economy are already to be found today, if not at the latest in a few years, in India, China and other up-and-coming non-European countries, and not in Poland or Bulgaria. And these countries would not even dream of adopting the "European social model".

That means that if Europe today prescribes itself high social standards throughout the EU, this will be detrimental not only to the economies in Eastern Europe in the short-term, but also to the economies of Western Europe in the medium term, where politicians can at most gain a period of grace for the necessary social policy reforms. This will make the pressure to adapt in a few years time all the harder. And so the failure of such a social policy throughout the EU is pre-programmed.

This in turn will make citizens even more sceptical about the EU and, quite wrongly,

# THE EU SINGLE MARKET: FREE MARKETS, PROTECTIONISM AND EXCESSIVE REGULATION



Centrum für  
Europäische  
Politik

bring further discredit on the Single Market, although the actual cause is to be found in the inability and unwillingness of the European countries to introduce necessary reforms. National politics will probably react by propagating and implementing even greater *national* protection in the Member States to prevent the alleged negative effects of competition. This in turn would cause the Single Market to undergo further erosion. When will the politicians – both in the Member States and in Brussels – see that cementing today's "high level of social standards" on the EU level will not be able to sustain these standards in the face of world-wide competition without fundamental reforms? Or have they already acknowledged this fact and simply do not have the courage to tell their voters the truth?

## **Fourth finding: the Single Market is increasingly being abused for unrelated political aims.**

One of the key instruments of the EU for protecting the Single Market is anchored in Article 95 of the EC Treaty: the EU is allowed to harmonise national regulations throughout Europe when they hinder the Single Market.

There is real cause for concern about increasingly frequent abuse of this competence in order to create regulations on an EU scale in areas where the EU simply has no competences at all. This is argued with the pretext of helping to secure the Single Market, even though the Single Market is only marginally affected, if at all, while in fact the real crux of the matter is something completely different.

In this way, the Single Market's assignment is perverted by immoderate policy which doesn't care at all about the EU's competence limitations.

A current and quite drastic example is the planned roaming regulation. The Commission severely criticises the undoubtedly high prices for mobile phone calls while being abroad. To become more popular with its citizens, the Commission wants to stipulate upper price limits.

A large section of Germany's political community is eagerly seconding the proposals because they think that making a stand for lower prices will make politicians more popular. But this is not popular, it is populist.

Without a sound analysis of the causes, the sovereign manner of dictating prices makes use of an instrument which would have done credit to a centrally planned economy.

The claimed justification that we are confronted with an abuse of monopolistic market power is not correct. This is confirmed by all investigations hitherto undertaken by the national regulation authorities, which are independent.

In fact, mobile phone users abroad have a choice between various different service providers operating there. These providers engage in intensive competition with each other. The main reason for the high prices which the non-resident users have to pay for phone calls is therefore not to be found in a monopolistic market power on the supply side, but far more in a lack of price awareness by the non-resident users, i.e. on the demand side. They cannot be bothered to undertake the effort of comparing the differences in costs in dialling into the various different foreign networks, so that there is no notable price competition between service providers for non-resident users.

But since when does the fact that consumers or users cannot be bothered to compare prices serve as a justification to implement state manipulation of pricing systems?

This regulation creates precedence: following the example set by the Commission, in future it would become a general task for the state to implement sovereign regulation of prices whenever the state feels that the prices are too high.

The Commission is making use of Article 95 of the EC Treaty in order to assert its factually mistaken objective. The prerequisite here is the existence or threat of differing statutory regulations in the Member States, which would hinder the Single Market. But this prerequisite simply does not apply at all. Not one single Member State of the EU has statutory

# THE EU SINGLE MARKET: FREE MARKETS, PROTECTIONISM AND EXCESSIVE REGULATION

regulations on roaming. Nor is there a threat of any such regulations, because such national regulations would only benefit foreigners, but not the domestic population. The individual Member State can only stipulate upper price limits for the fees charged by its domestic service providers to the foreign customers. This reduces the profits of the domestic service providers. On the other hand, a domestic regulation cannot influence the prices that domestic citizens have to pay abroad. As a result, a national regulation would therefore harm the domestic service providers and not help domestic citizens.

In view of the fact that there is not even a risk of corresponding regulations in any of the Member States, Article 95 certainly cannot be used to justify the regulation. The Commission knows this just as well as its proponents in the Member States. But in spite of knowing better, the project is being forced forward just because there is a general feeling that the European Union must acquire a better image among its citizens.

Other examples of abusing article 95 as a competence standard for EU regulation in areas where the Community has no regulation competence include the ban on tobacco advertising, the consumer credit directive and the regulation pertaining to nutrition and health claims made on foods. So the European Union has already proceeded a long way down this path.

The fact that legal systems are fragile is ignored. Such systems fall apart when deliberately violated by the political community. How can the European Union demand the rule of law from its Member States and its citizens if it doesn't even care about it itself? Here again, this does not bode well for the Single Market.

The four described findings do not draw a rosy future for the Single Market. There is an urgent need to stop and change direction. This call must address all affected entities, both the bodies of the EU itself and the Member States.

The real tragedy rests in the fact that the European political community prescribes itself regulations in economic areas which simply should not be regulated on a European scale, as pure frustration relief, because national egoisms prevent European policy in areas where it would be really necessary, such as for example foreign and security policy, and in the judicial cooperation in criminal matters – and of course in protecting the Single Market in its true sense. As it is, the future viability of the EU is jeopardized on two fronts at the same time.

Frits Bolkestein was a member of the European Commission from 1999 to 2004 with responsibility for the Single Market; he is a member of the Board of Trustees of the Centre for European Policy.

Lüder Gerken is the director of the Centre for European Policy.