Barriers to the Single European Market (SEM)

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Abstract

In 1992 the Single European Market (SEM), based on the Single European Act 1986 (SEA 1986), was due to take effect in the European Union (EU). The SEA 1986 provided four basic freedoms in order to accomplish the SEM without internal frontiers: the freedom of goods, capital, service and the free movement of people. Since then, the SEM has proved a remarkable development prompting some scholars to suggest that the EU is like a country in terms of economy.

A great deal of debate has focused on whether the EU is (or is able to develop into) an economic or political union. If the EU currently falls short of political union, is there any chance to develop into a political union in a near future? In order to answer this question I, in light of neofunctionalism, began to consider whether the SEM was fully established in the EU, because the contents of the four basic freedoms, looked at as a whole, including the freedom of people especially, are not less than a political union. If the answer is positive, I can say that political union is a reality and that the neofunctionalist propositions are correct. If not, the proposition that economic spill-over will produce a political spill-over proves defective in areas.

This thesis therefore consists of four main chapters, each having three subsections: the freedom of goods, freedom of capital, freedom of service and the free movement of people. Chapter 1 deals with the question of whether the freedom of goods is distorted by either tariff or non-tariff barriers. Chapter 2 is devoted to resolving the issue of whether the freedom of capital is fully guaranteed both in domestic and in international level. Chapter 3 discusses whether the Union is entitled to provide a Union level mechanism, to enable the freedom of services to fully take root. Finally, I ask whether people, as social beings rather than just individual members, have full freedom to move within the union without any distortion either by social benefit, ethnicity, or language.
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Introduction

Arising Neofunctionalism

After the Second World War, European countries came to realise that the expansion of nationalism could ultimately lead to the destruction of the international order in two principle ways. Jean Monnet and Robert Schuman, with this in mind, pioneered to restore the European order. They said that "a start would have to be made by doing something both more practical and more ambitious. National sovereignty would have to be tackled more boldly on a narrower front".¹ Inspired by this, Schuman explicitly proposed the first step in the realization of their vision, a vision of a United Europe. This was known officially as the Schuman Plan. In 1951, Italy, Belgium, Luxembourg, the Netherlands, France and Germany signed the Treaty of Paris, establishing the European Coal and Steel Community (ECSC).

The ECSC was ground breaking in two principal ways. First, its policy aims were ambitious, entailing not only the creation of a free trade area, but also the laying of foundations for a common market, especially for coal. This, it was envisaged, would ensure orderly supplies to all member states, and produce a rational expansion and modernisation of production. This idea witnessed success, at least, as far as coal is concerned.

Second, the ECSC was the first European interstate organisation to display significant 'supranational' characteristics. These characteristics were found in the new central institutions established with the power to oversee the abolition and prohibition of national tariff barriers, state subsidies, special charges, and restrictive practices. Four main institutions were created: the High Authority (HA), the Council of Ministers, the Common Assembly and the Court of Justice. These institutions also had the power to fix prices under certain conditions and to harmonise external commercial policy by setting minimum and maximum rates of customs duties on coal in the ECSC.

¹ Martin Holland, European Integration: From Community to Union, Pinter(UK), 1994, p. 23–25.
The ECSC was the first successful supranational institution even it was in relation to one sector, coal. It was supranational in that the decision of the ECSC, especially the High Authority, was binding on all member states. The HA was charged with ensuring the objectives set out in the Treaty. To enable it the HA could issue decisions which were to be binding in all respects. The HA could also issue recommendations which were to be binding in its objectives. In addition, subsidies, aids, action against a restrictive practice, promotion of research, and the control of prices under certain conditions also fell under the HA's jurisdiction. It could even impose fines as penalties on those that disregarded its decisions.

E. Haas, a pioneer of neofunctionalism, observed and researched this stage of integration in Europe in his book *The Uniting of Europe 1950–1957.* His theory argued that: integration in one economic sector, for example coal, has the potential power to spill-over to other coal-related and political sectors by way of the supranational institutions. Scholars named this neofunctionalism. Strictly speaking, the birthplace of neofunctionalism is 1950–57 in Europe.

After the success of the ECSC, the member countries attempted to develop and construct a common market encompassing all economic sectors. A Committee was established under the chairmanship of Belgian Foreign Minister, Paul-Henry Spaak. The report from the Committee was used as a basis for another landmark treaty: the Treaty of European Economic Community (EEC). The Treaty of EEC first aimed to establish a common market for all economic sectors. The EEC also attempted to approximate the economic policies of member states to promote throughout the community a harmonious development of economic activities, a continuous and balanced expansion in Europe.

Another European concern was also prevalent: whether nuclear power was to be developed as an energy or a source of weapon. Europe's response to this was the establishment of a regime to control such energy. The European Atomic Energy Community (Euratom) emerged from this. As with the ECSC, both the EEC and Euratom had four

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principal institutions designed with supranationalism in mind. They were a Commission (counterpart of the HA in ECSC), a Council of Ministers, an Assembly and the Court of Justice.

The institutional arrangements were again 'supranationalistic' in character with some restriction compared to their counterpart in the ECSC. In particular, the Council of Ministers in the EEC was judged to have too much power. Disappointment that most of the key decisions in the Council would have to be made 'unanimously' was also expressed. The Treaty bodies were trapped because of the unanimous voting rule. Leon N. Lindberg noticed and researched these developments, especially in the EEC and Euratom, and proclaimed it neofunctionalism, with a few differences of emphasis in his book The Political Dynamics of European Economic Integration (1963).

A clear message of his book was that first integration in one economic sector could spill-over to other economic sectors. Second, the power of spill-over could go to political sectors in the end, by way of central institution building.

For the purpose of this paper, it will be neither possible nor necessary to give a full account of various views in the neofunctionalist literature. I propose to return to the original formulation of neofunctionalism, mainly E. B. Haas' The Uniting Europe (1958) and Leon N. Lindberg's The Political Dynamics of European Economic Integration (1963). There are some differences of emphasis between the two. While I draw attention to some of these, the main focus will be on where the two writers converge.

First, the main tenet of neofunctionalism which the two writers have in common is 'economic' integration, which would result in a political integration in Europe by way of central institution building process during the 1950s and 1960s. Their domain was regional integration in general and European integration in particular. Haas even asserted the possibility of generalizing the results to other similar settings provided such settings have similarity with the ECSC whereas Lindberg was more cautious.

By integration, Lindberg is somewhat more restrictive than Haas. He

did not commit himself to 'predicting' a particular outcome of the process, on the placing more emphasis on a 'decision making body' and less transferring of loyalties. Thus, Lindberg's neofunctionalism is more 'descriptive' than 'prescriptive', whereas Haas is more accurately 'prescriptive' and 'strategic' to integration. Hence his definition of integration reads:

The process whereby nations forgo the desire and ability to conduct foreign and key domestic politics independently of each other, seeking instead to make 'joint decisions' or to 'delegate' the decision making process to new central organs; and the process whereby political actors in several distinct settings are persuaded to 'shift' their expectations and political activities to a new center.4)

Second, both perceived integration as a 'process' rather than as a 'condition' for a union. They both saw it as involving some degree of 'institution building' in the new center. The institutions are the HA, Council of Ministers, a Common Assembly, the Court of Justice in the ECSC, the Commission, an Assembly, a Council and the Court of Justice in the EEC/Euratom.

According to neofunctionalism, each national elite will undergo a learning process, developing the conception that their interests are best served by seeking supranational over national solutions. Their activities will therefore refocus expressions and perhaps their loyalties to the new center, the Union. This is the basic assumption behind institution building in the idea of united Europe.

Thirdly, another main focus involves the concept of 'spill-over'. This means that integration within one sector will tend to beget its own impetus to other sectors. For instance, if product A, for instance a plug, is guaranteed to move freely within the Common Market, a related product B, for instance a socket, is likely to have the same benefit. Then most electrical appliances will soon have the same freedom of movement in the Common Market. This is the first logic enclosed under the heading of spill-over. This spill-over effect may be explained by two principles: functional and political spill-over.

Functional spill-over is a mechanism arising from the inherent technical characteristics of the functional tasks themselves. The idea is that some sectors within industrial economies are so interdependent that it is impossible to treat them in isolation. Hence, attempts to integrate certain functional tasks will inevitably lead to problems which can only be resolved by integration of other related sectors.

The Union, assuming it has a common market for a bolt, is likely to have a common market in a nut sector because they are so interdependent. Again, if the Union accomplishes a common market for the wheel of a motor vehicle, it is easier to have a common market in tyres. In the end, it is assumed they would have a common market for all products.

The following step, according to neofunctionalists, is that of political spill-over. Neofunctionalism assumes that the Union will draw loyalty to the central institution, the Union, by providing Union citizenship. If a person is allowed to move in the Union without check, the person is likely to consider the Union as 'his/her' home country. If a person is given the right to vote and the right to stand in the election to the European Parliament, the person is also likely to regard the Union as his/her home country. If a person has his/her fundamental rights protected at the Union level, the person is highly likely to accept the Union as his/her first country together with his/her country of origin. These are the basic ideas of the freedom of people in Europe. By this freedom, they assume that the Union will have the loyalty of citizens. This is the idea of political spill-over.

Assertions of intergovernmentalism over neofunctionalism

Alternatively intergovernmentalists claim that neofunctionalists abandoned their theory after 1965. Why, and on what ground did they assert this? Basically, the spill-over effect had not been recognised between 1965 and the early 1980s. During this time, it was difficult to isolate instances of functional, let alone political, spill-over. To some extent, it seemed natural to assume that Haas' neofunctionalism was based solely on observations regarding the the ECSC. So when the
ECSC witnessed success, so too did neofunctional theory and when the ECSC came to an end, so did the theory. The reason why neofunctionalism was abandoned, then, may be explained by looking at the circumstantial changes in Europe since 1965.

In 1965, the European countries agreed to establish a consolidated institution in Europe. They signed the Treaty of European Communities (EC) whereby all the then existing three treaties were merged. This is the so-called the Merger Treaty (EC Treaty). Understandably, the attraction of the Community's larger market was overwhelming. In 1961, the UK together with Denmark, Norway, and Ireland applied for full membership. These applications failed. The main reasons for this were, as Martin Holland has suggested, French nationalism and French commitment to intergovernmentalism under de Gaulle.

De Gaulle's conception of Europe was the antithesis of that envisaged by Monnet: it was to be an "Europe of sovereign states". In a press conference on 15 May 1962, de Gaulle mentioned that "at present there is and can be no Europe other than a Europe of the states". This is an example on which they based their argument.

During his decade as French president, de Gaulle opposed the extension of Community competences and attempted to thwart all efforts to realise this 'federal' fiction. From this point, until his resignation as president in 1969, de Gaulle was responsible for obstructing Community development in three further ways: by opposition to enlargement; via the Luxembourg Compromise; and by refusing to extend the powers of the Community's existing institutions.

With regard to enlargement, the primary motivation behind French veto was due to its rivalry with the United Kingdom. In a press conference, de Gaulle announced Britain's application was unacceptable to France. The reasons had very little to do with the Community per se. More generally, France appeared to have assumed the leadership of the Six. This means that British membership in an enlarged Community would significantly dilute French authority and challenge de Gaulle's idea of the "organisation, role and policies of a Europe". The applications of the UK,

5) Martin Holland, *European Integration: From Community to Union*, Pinter(UK), 1994, p. 34.
together with the other applicant states, were therefore delayed for another 10 years, and was finally resolved by the Treaty of Accession 1972.

French intention was obvious and incompatible with the Community. France vetoed the Council meeting. This issue surfaced under the guise of the voting rule: majority or unanimity. The 'Luxembourg Compromise' solved the immediate problem but inadvertently created the Community's longest-term problem: the continued use of unanimity as the basis for decision making.

The next step towards integration was establishing a common market and institutional authority. In compliance with its Treaty obligation, the Commission in 1965 proposed that the Community should be given its own financial responsibility and resources. Also, the Commission proposed that the EP be given new powers to amend the budget. France again objected to these proposals on the grounds that national governments should decide at the final stage. In general, the effect was to freeze the integration process.

Researching this stage of integration in the EU from 1965 and 1980, Hoffman argues that the approach was intergovernmental rather than supranationalistic in his article "Obstinate or Obsolete: The fate of the Nation State and the case of Western Europe".

At the heart of the intergovernmentalism is the assumption that the nature and peace of European integration are determined primarily by decisions and actions of independent nation states. This proposition can be analysed in three main areas. First, there is an assumption that the nation state is a conscious actor in international relations. Second, intergovernmentalists argue that the actions of states are based on utilizing what are judged to be the most appropriate means of achieving state goals. Third, an intergovernmentalist approach to interstate relations emphasizes the key role of governments in determining the relations between states.6)

As an example, witnessed by the French case, national government is the last threshold for Community matters to be enforceable. This  

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6) "Obstinate or Obsolete: The fate of the nation State and the case of Western Europe". *Daedalus*, Vol. 95.
governmental power (as opposed to a supranational body) may sometimes be expressed under the guise of a supranational body by way of unanimity in the decision making procedure. This means that a supranational institution's power is in the end subject to the interest of national governments.

The SEM: Neofunctionalism vs Intergovernmentalism?

The 1985 White Paper reignited scholastic interest in neofunctionalism. The basic rationale behind the White Paper was that a Single Market could be established in Europe by removing fiscal, technical and physical barriers. This idea was reaffirmed by Member States in the same year and was signed the following year as the Single European Act 1986.

The SEA 1986 provided a plan to create a European Common Market without internal frontiers by 1992. For Europe to have the SEM, the Act considered that the Union needed to have competence over four basic areas: the freedom of goods, persons, services and capital. Simply, if the Act is properly implemented by the Member States, there must be a Common Market in Europe. The focus of this thesis entails a discussion of the SEM and its multiple facets.

The contracting parties of the Single European Act 1986 proclaimed four basic freedoms were established and protected under the Single Market. According to A. Smith, these fundamental freedoms are designed to provide 'more freedom to the Market'. Accordingly, this thesis consists of four main chapters. The four freedoms are therefore the points into which I research. I concentrate especially on barriers to freedoms and the SEM, because it is possible to prescribe problems and strengthen the foundations of the Market by implementing observations.

It must also be mentioned that the theory may be properly explained and evaluated only by an 'overall' coverage of the SEM, instead of studying a particular area. This is because the ultimate goal of the SEM is a single market for all sectors in Europe. This leads to the hypothesis that the theory of integration may be best explained by a 'blanket

approach'. For instance, if one looks at only the issue of 'mobility' per se, one may conclude that the process of the single market is best explained by neofunctionalism. However if one looks at the Single Market as a whole the answer may differ.

According to neofunctional arguments, regarding the freedom of goods, the first question involves identifying whether or not a spill-over effect exists in the four main freedoms. It seems that the drafters of the SEA 1986 had the bolt–nut, wheel–tyre, and socket–plug arguments in mind. They seemed to assume that the integration process can spill-over into an overall economic sector where an integration of all sectors will finally be accomplished. This is functional spill-over. The next step is political spill-over. This means that, in principle, the spill-over effect will eventually abolish border controls and taxation, in order to have common market.

For the SEM to have the freedom of people in name and practice, the functional spill-over must be effective not only in an individual dimension, but also in a social dimension as well because a person is a social being. Therefore I will look at whether the individual freedom spills-over to the social dimension of the freedom of people by way of Social Europe and language. Also, for the freedom of capital to exist, there must be internal freedom within a Member State and international freedom among Member States as well. This issue will be researched by way of state aid and public procurement. This then, according to neofunctionalists, spills-over to the international arena by way of central institutions. This will be looked at by way of Foreign Direct Investment.

To have the freedom of service in name and practice, there must be a common market for one economic sector first. Then there must be spill-over between similar sectors because they are so alike that one cannot be integrated without the other. I will look at this by way of banking and insurance.

The second main question is, according to neofunctionalism, whether central institutions are used as the driving instrument of integration. I will look at how these central institutions act in the integration process first. The Commission and the Council act in the form of Directives and Regulations which have a direct effect on Member State governments. In
principle, there is little difficulty in accomplishing the SEM, provided that the Community has competence in general economic matters, especially with regard to the four basic freedoms. As a result of this, I first examine the Directives and Regulations in each sub-section.

It is important to note that in Europe, Community Directives are superior over national laws. Some Directives have 'direct effect' on national legal systems while others do not. Whether the Directives have direct effect or not, national laws are subject to Community laws. If the two laws, Community law and national laws, are incompatible, Community laws take precedence. These Directives are issued by the Commission. Another form of Community law is issued in the form of a Regulation. This is issued by the Council. This Regulation enjoys the same legal power as the Directives do. I research these Directives/Regulations first in each subsection because they affirm neofunctionalism.

The third question is whether or not spill-over is effective in political sectors. This examines the question of whether the Union is going to be 'automatically' a political Union. According to neofunctionalism, especially that of E. Haas, this must be so. This in turn entails some specific questions. First, given that the Community has competence over a certain type of issue, can the SEM be better explained by the theory of neofunctionalism? Second, to what extent can the SEM be explained by the theory of neofunctionalism? Third, can economic spill-over be identified in the SEM? Fourth, is functional spill-over recognised and developed into political spill-over in the SEM? Fifth, is cultivated spill-over identified in the SEM? Sixth, does every Member States agree that the Community has overall competence in SEM matters? Seventh, if not, where is the dividing line between the two theories?

Eighth, if the issue is whether the Union has competence over a certain area, how does the Union respond to it? This is the subsidiarity principle which I will discuss in due course. That is to say, do national governments act as actors in the integration process in the SEM? Ninth, can intergovernmentalism 'fill' the gap exposed by neofunctionalism if neofunctionalism is not perfect? Again, if neofunctionalism is not perfect, is there any problem in completing the SEM?
Structure of Thesis

The structure of this thesis consists of four chapters. Under Chapter 1, "the freedom of movement of goods", I will look at direct and indirect restrictions on the freedom of movement of goods. A quantitative restriction especially is researched under the title of standard (1.1). If taxation is imposed more than it would have been to the same product within the country, this is regarded as an indirect restriction to the freedom of goods. (1.3) Also, transport and border control is regarded as a physical control of the freedom of goods. (1.2)

This border control is mixed with the freedom of people. There are various restrictions, whether qualitative or physical, to this freedom of people. The law on migrant workers is a good example of restriction (2.2). Social benefit policy is another important aspect when assessing the freedom of people. (2.3) Language is one of the clear qualitative restriction to the people. (2.1)

Language is linked with the freedom of service, especially for lawyers because there is no common court language (3.1). So, the freedom of service is placed in the third Chapter. Under this Chapter, the main issue is the freedom of the establishment of a branch or a subsidiary in a country other than that where the headquarters are located. Insurance (3.2) and banking (3.3) are good examples because they are interconnected with the issue of freedom of people and freedom of capital, respectively.

Freedom of capital is finally analysed in Chapter 4. The feasibility of capital freedom is analysed by way of foreign direct investment (4.2), because investment indicates the movement of capital across frontiers. The topics of state aid (4.3) and public procurement (4.1), are also discussed as they are forms of political control of the freedom of capital in the SEM.

Finally, it warrants mention that empirical analysis is mostly employed. Literature analysis therefore is primarily used in this thesis. I try to obtain, use and interpret primary sources, if possible. For instance, I based the newest version of the Treaty on the European Union and the
Treaty of the European Community. Therefore the number of provision referred in this thesis is based on the Consolidated Version of the Treaty on European Union and the Consolidated Version of the Treaty Establishing the European Community. I have also made an additional effort to identify the 'root' of problems because it is at the root that we can get the 'prescription' for the problems. Most of them have been possible by way of case law study. The law is stated from 1997 and after. I also try to update the relevant data and sources, especially economic side data.
Chapter 1. Freedom of Goods

1.1 Standards of Goods

Under the Single European Act 1992, the basic and fundamental task of the Union is to create a Single, Common Market, without internal frontiers. To achieve a Single Market, the Act considers that four elementary freedoms are required: freedom of goods, freedom of movement for workers, freedom of services and freedom of capital.

The Union considers that the freedom of goods is the base for the remaining three. It is therefore logical to look at the freedom of goods first. Under Article 23 - 24 EC (the Treaty on European Community)\(^8\), 1) it is prohibited to charge a duty having an effect equivalent to that of customs duties; and 2) it is also prohibited to have measures having an effect equivalent to that of quantitative restrictions under Article 28 and 29 EC.\(^9\)

There may be numerous measures, requirements or barriers equivalent to either quantitative restrictions or customs duties. Discriminatory taxation is one clear example. Border control is another instance because the Common Market, in principle, has no internal frontiers. Lastly, even though there are no internal frontiers, all the standards of a product should be compatible for a product to be circulated without restriction in the Union. Under the freedom of goods I examine standards, indirect taxation and border control.

It is well known that there were numerous factors which caused the

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\(^{8}\) Article 23 of the EC Treaty reads "The Community shall be based on a customs union which shall cover all trade in goods and which involve the prohibition between member States of customs duties on imports and exports and of all charges having equivalent effects, and the adoption of a common customs tariff in their relations with third countries."

Article 24 of the EC Treaty reads "Products coming from a third country shall be considered to be in free circulation in a Member State of the import formalities have been complied with ...."

\(^{9}\) Article 28 EC reads that "quantitative restrictions on imports and all measures having equivalent effect shall, without prejudice to the following provisions, be prohibited between Member States."

Article 29 of the EC Treaty reads "quantitative restrictions on exports and all measures having equivalent effect shall, without prejudice to the following provisions, be prohibited between Member States."
Single Market to fragment. For instance, differing product specifications and regulations are among the most significant barriers in the Market. Each is defined by a law or a standards institute. These are referred to as standards. In 1983, according to the Cecchini Report, it was estimated that there were around 100,000 standards within the Market, making it imperative to discuss standards harmonization.

The nature of standards is simple. The more standards the Market has, the slower the transaction time is likely to be. The more heterogenous the standards are, the more they will cost the market. The more standards the Market has, the more the Market is likely to fragment. In simple terms, the Single European Market is more likely to succeed if there are less standards. Standards therefore are clearly of public interest and a vital issue in the Single European Market (SEM). This section will describe how the European Union (EU) has overcome and resolved problems caused by such standards in order to realise one of the core values of the Single European Act 1989: free movement of goods.

In principle, the Single Market means that a consumer in Denmark has a chance to purchase any product produced not only in Denmark, but in any of the 15 Member States without any discrimination. Specifications for similar products therefore need to be exactly the same. An electric plug bought from one manufacturer in the Market should fit into a socket from another. This is the idea of 'plug compatibility', an approach used by the Commission at the earliest stage. However, progress was painfully slow.10)

It was a laborious process to create detailed Community standards in all ranges of products. As a first step the Commission therefore proposed its new approach to technical regulations, whereby the law enacted by the Council would be short and limited to the objects, such as health and safety, that the specifications were intended to attain. The detailed specifications would then be drawn up by an approved standards institute without any political engagement or procedural problems. This method was well expressed in the so called Low Voltage Directive.11)

enactment of regulations was indeed accelerated after the Directive was adopted.

Even though the Directive made some developments in certain areas, the approaches did not work, especially in the area of foodstuffs, as some Member States had tougher rules on foods. The Commission, with the help of case laws through the European Court of Justice (ECJ), bypassed this stumbling block. One clear example is Cassis.

On 14th September 1976, the Rewe-Zentral AG (the Rewe)\(^{12}\) requested authorisation from the Federal Monopoly Administration for Spirits to import from France certain spirits, including the Cassis de Dijon containing 15 to 20 percent by volume of alcohol. The Administration declined permission, as the liquor was not subject to authorisation under the Law on Monopoly of Spirits in Germany. Article 100(3) of the Law provides that only spirits having a wine-spirit content of at least 32 percent may be marketed in the country. The Rewe brought an action against the decision pursuant to Article 177 and 30 of the EC Treaty. The issue of Cassis was whether Article 100(3) of the German provision, was compatible with the spirit of free movement of goods within the Market as provided by Article 177 and 30 of the EC Treaty.

The European Court of Justice (ECJ) was of the opinion that “a considerable number of divergent national technical standards constitute a restriction on the free movement of goods between Member States” (Cassis 661). The ECJ went on to say that it was “a measure having an effect equivalent to a quantitative restriction on imports, contrary to Article 30 of the Treaty on European Economic Community (EEC)”. The Court later found that the German authorities must allow the sale of beer brewed to the specifications of other Member States.\(^{13}\)

The Cassis established the principle of mutual recognition. This means that a product such as Cassis which conforms to the specifications of one Member State must not be excluded from another unless they can be shown to be damaging to health, safety, environment or other aspects of the public interest. Accordingly, no product produced in any Member State can be prohibited or prevented from having free circulation, unless

\(^{12}\) Rewe Zentral AG v Bundesmonopolverwaltung fur Branntwein (Cassis) 1 [1979] European Courts Reports 649

\(^{13}\) Ibid., 649.
it is proven to have a negative influence on health, safety of humans, animals, or the environment. One product lawfully produced in one Member State must be able to be mutually recognised in an other Member State. This is the principle of mutual recognition. Mutual recognition is therefore a powerful factor in economic integration, which respects the principle of subsidiarity. It allows goods and services to move freely within the Common Market, while respecting the diversity of practices, customs and regulations in the various Member States and avoiding extreme harmonisation at the Community level. Simply speaking, free movement of goods is a rule of law in the Market since Cassis.

It is not claimed that the principle of mutual recognition is a panacea for the freedom of goods to be fully established. It does have problems, as the Commission Paper rightly recognises. For instance, particularly where the new technology sector is concerned, the Community cannot stick to this principle only. New information technology, telecom for instance, is normally therefore left under tight state control.

Again, it is important to ask what the phrase "having equivalent effect" means precisely. It is well known that Article 30 EC had quotas in mind. The actual question, then, turns to whether the ECJ has ever provided any conclusive definition of the provision. For instance, if any Member State has domestic legislation prohibiting resale on a certain day, does it constitute discrimination of freedom of goods? This is exactly what happened in Keck. Mentioning the decision first, the ECJ aggravated the situation around the interpretation of the Article 30. The crucial issue was whether a national measure hinders trade between Member States in a manner equally as severe as quotas. The Court held that "however, contrary to what has previously been decided, the application to products from other Member States of national provisions restricting or prohibiting certain selling arrangements is not such as to hinder directly or indirectly, actually or potentially, trade between Member States... provided that those provisions apply to all affected traders operating within the national territory."16)

15) Emphasis added.
16) Sigmar Stadlinmeier, "Contrary to What has previously been decided...": The Search
Meanwhile the SEA simplified the process of development by allowing such harmonization decisions to be based on qualified majority voting (QMV).\(^\text{17}\) The actual task of devising the details of the standards was off-loaded upon European standards bodies, such as the European Committee for Standardisation (CEN) and the European Committee for Electro-technical Standardisation (CENELEC). All Member governments are obliged to presume that if a product is manufactured according to these standards, that it will comply with the fundamental requirements stipulated in the directive and must be granted free access.\(^\text{18}\)

However, the Community only has the power to enforce the harmonisation process over non health-related products. Under Article 36 (exemption provision), which provides an escape clause if a product is concerned with public order, public morality, public safety; the protection of the health and life of humans, animals and plants; and the protection of industrial and commercial properties, quantitative restrictions cannot be justified. In other words, any product which is proven to be harmful to health is not automatically granted free access. For instance, a chocolate made in one Member State must not be subject to control in another Member State just because the importing country has a different view about how a chocolate should be made, how much it is, how it is marketed and how it should be shaped. It however may be subject to control if and only if the chocolate contains any harmful ingredients.

D. Demiray is correct in pointing out that the Community has not developed an over-arching methodology, and instead merely reacts to events.\(^\text{19}\) Neither the case law nor the Treaty has offered a mechanism that adequately balances the two conflicting interests: freedom of goods and environmental consideration or health related issue. This causes a serious problem in relation to the free movement of goods in the SEM. For instance, if Denmark or Germany apply high standards of food regulation on the basis of genuine health and safety issues, the Community has no power to override it. What the Community is

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17) This will be discussed more fully at a later stage.
18) D. Swann, op. cit., 57.
permitted to do is to harmonise differing municipal laws without Community level legislation. This is mainly the result of many national standards, which are devised to protect humans, animals and plants from injury. Therefore a refusal by a Member State to import goods which do not satisfy its standards of protection is entirely legitimate.

It is interesting to note how the Commission has responded to a manufacturer where the product is defective and the producer is liable. Under the Directive of 85/374/EEC, as amended by Directive 99/34/EC, every producer is, in principle, obliged to make good any damage to health, safety and property caused by a defective product. Nevertheless, as proved by the recent food crisis of 'mad cow', there is no such concept of zero risk. The Community therefore must adopt a system which is best suited to developments, with a view to ensuring the best possible compensation of victims suffering damage from defective product. So the actual issue is whether the Union has such a compensation system to guarantee 'relief from defective products'. The answer appears negative. The Green Paper shows that because the compensation scheme cannot cover every product and it cannot make it an obligation for every producer to be insured.\(^{20}\)

The Commission, in principle, has made some developments in the Common Market. Currently, however, the Commission does not have the means to act rapidly against Member States when there are serious unjustified violations of the principle of free movement of goods. The Commission has proposed a Regulation whereby it could decide quickly to request the Member State concerned take the measures necessary to put an end to any serious and clear violation of free movement of goods coming to its attention.\(^{21}\)

In addition, it must be noted that the right to free access is not absolute. The idea of so-called differentiation provides that the Community may take into account different rules for different regions. For example, Article 7 of the Directive 78/611 allowed Ireland to have a

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higher lead content in its gasoline because they did not have the technical ability to change and its environment was relatively unpolluted. The Treaty of the European Union (TEU) again explicitly states that the Community must take into account the diversity of situations in the various regions of the Community.22)

The environment provides the biggest impediment by which the spirit of free access of goods is restricted. With the adoption of the SEA in 1987, the Community not only had the express purpose of pursuing environmental protection, but it made environmental protection regulations a component of the Community's other policies. Simply speaking, environmental protection constitutes one of the few areas where the Treaty mandates a high level of Community action. For instance, unlike harmonisation of other national provisions, Article 100(A) directs that in completing the internal market, harmonising national environmental protection laws must take as a base a high level of protection. Also, Article 130r incorporates the same terms regarding the aim of Community environmental legislation.23)

The Community claims that it has competence over environmental issues, and a priority is given to environmental protection over the free circulation of goods in the Community through ADBHU. ADBHU was a landmark decision because it declared that environmental protection was a fundamental Community goal that could limit the free movement of goods. The ECJ held that the principle of freedom of trade is not to be viewed in absolute terms, but is subject to certain limits justified by the objectives of general interests pursued by the Community, provided that the rights in question are not substantially impaired.24)

This clearly suggests that one of the four basic goals, the freedom of goods, is subject to environmental considerations. The ECJ is of the opinion that green ideas must be given priority over the Community's goal of free access of products. National environmental measures therefore may restrict the free circulation of goods provided. 1) The national measure must actually seek to protect the environment and not

23) Ibid., 76
24) Ibid., 83
pursue other ends in the guise of environmental protection. 2) The national measure discriminates in favour of a national or local product. One must look to the nature of the goods and determine whether any of the environmental principles of the Treaty justify differentiation, otherwise the national measure must affect all products equally with no discrimination either de jure or de facto. 3) Finally, the national measure must be indiscriminatively applicable, the measure must be the least restrictive on the free movement of goods and must be tailored to reach the goal.

The aforementioned principle of proportionality may be used as a shield to the freedom of goods by some Member States. The principle of proportionality means that legal measures must not go further than is genuinely necessary to achieve the desired objective. For instance, if a regulation was necessary to prevent the consumer from being deceptively sold weak liquor, this could be achieved by content-labelling rather than through directives. In simple terms, much of the harmonisation was not really necessary and should have been confined to cases where there was a genuine threat and where no valid alternative existed.

On the other hand, Kramer maintains that the political and legal objective of creating a permanent, functioning Community-wide internal market pursuant to Article 8A would be thwarted in the long run if a Member State had unlimited rights. Nevertheless, all things considered, this controversy indicates that because there is no agreed Community-wide legislation, a Member State may breach any of these provisions under the guise of environmental protection. Over this the Community has no power. For instance, Flynn notes that Denmark declared that it would avail itself of Article 100a(4) and introduce more stringent standards even though a Council Directive was passed by qualified majority voting as to car emission standard. Simply speaking, the idea of free access of goods is subject to the commitment of not only the Community but each Member State.

As a whole, it has been demonstrated that if specifications or standards are uniform at the Community level, it can not only spur the process of economic integration, but also have an effect on the deregulation of non-tariff barriers (NTBs). However, I have identified
some stumbling blocks such as environmental issues and the idea of differentiation. The main stumbling block is the fact that the Union has partial competence on this issue. For instance, telecom as an information related high tech company is under tight control of the Member States. Product liability does not cover all items in the Market. Non-health related products are not under Community competence, either. In some Member States, retail sales are not permitted on certain dates. All these facts lead to the consideration that the freedom of goods is 'limited'.
1.2 Transport and Border Control of Goods

The idea of freedom of goods can not be attained simply by removing measures or schemes that have discriminatory effects in the Union. The freedom of goods may be thwarted by the transportation and checking of a product at the border. This idea leads an examination of the effect of transportation and border control in relation to the freedom of goods. As one example, an hypothetical person AA is carrying an hypothetical product P, from a country to country B, via C. The person AA needs to use his truck (lorry) and train, where appropriate.

The transport sector accounts for 7 percent of the Union's General Domestic Product (GDP) and is expected to increase up to 16.7 percent by the year 2000. This sector covers transport, energy and telecommunications. The Union has a master plan for European development (Urban Networks) and energy transport networks. The Union, with the help of the European Investment Bank (EIB) or European Regional Development Fund (ERDF) or Cohesion Fund (CF), has some projects of common interest. The projects include such things as the trans-European Transport network, which includes trunk roads and motorways; high-speed rail networks and combined transport networks to Eastern Europe; ports, airports; and traffic management systems connected to these infrastructures.

The theory is that a global reduction in transport costs has the same effect as a bilateral tariff reduction in increasing the market area for efficient producers. Transport cost reductions may increase total welfare without necessarily increasing the welfare of all parties concerned. The Commission, being well aware of this, has been making an effort to establish a Common Transport Network under Article 70-80 of the EC Treaty. More

25) Article 70 of the EC Treaty reads "The objectives of this Treaty shall, in matters governed by this Title, be pursued by Member States within the framework of a common transport policy."

Article 72 of the EC Treaty reads "... no Member States may, without the unanimous approval of the Council, make the various provisions governing the subject on 1 January 1958 or, for acceding States, the date of their accession less favourable in their direct or indirect effect on carriers of other Member States as compared with carriers who are nationals of that State."

Article 75(1) of the EC Treaty reads "in the case of transport within the Community, discrimination which takes the form of carriers charging different rates and imposing different conditions for the carriage of the same goods over the same transport links on grounds of the country of origin or of destination of the goods in question shall be abolished." and 75(3) "The
specifically, Article 75 sets out the substance of the policy and Article 80(1) restricts the scope of the title to road, rail and inland waterway transport.\textsuperscript{26}

It is necessary to mention that the European Parliament (EP) has always advocated a global approach to the Common Transport Policy, believing this to be the key to any progress towards greater economic integration. For instance, the EP in 1985 brought an action against the Council claiming that it had failed to adopt the measures implementing the Common Transport Policy as provided in the Treaty.\textsuperscript{27} The two basic objectives of the Common Transport Policy are the completion of the internal market and creating an environment of sustainability. The corollaries of sustainable mobility are the internalization of infrastructure costs, i.e. the elimination of the distortions of competition between modes of transport.

In order to attain these objectives, the Council (sometimes the Commission) has adopted the following directives. With regard to the transport of goods by road, under Council Regulation (EEC) No 3572/90 and Council Directive 74/56/EEC (which was amended several times) there are some conditions regarding road haulage operators such as professional skills and creditworthiness. Under Regulation 88/192, the access to market by road is liberalised, whereby the quantitative restrictions, Community quotas, bilateral quotas between Member States and quotas applicable to transport in transit to or from third countries were all abolished. Under Council Regulation (EEC) No 311/93 amended in 1998, the definitive cabotage arrangement, as far as transport of goods is concerned, was entered into force. Any carrier meeting the necessary conditions and established in a Member State is entitled to operate, on a temporary basis and without quantitative restrictions, national road haulage services in another Member State.


With regard to coach and bus transport, under Council Regulation 684/92, the Union decided and agreed on the progressive liberalization in principle of virtually all passenger transport within the Community. It must however be mentioned that this is related to the border control issue which is mentioned later.

With regard to inland waterway transport, under Directive 91/672/EEC, the principle of mutual recognition of the professional qualifications of carriers is established. However, the issue of harmonisation of conditions for obtaining a national boat–masters certificate is not yet finalised. Also, under Regulation No. 2919/85, some conditions for access to the arrangements for the navigation of the Rhine were agreed to and signed.

With regard to rail transport, Directive 91/440/EEC, amended by 95/18/EC, established the principle that every railway operating licence issued by the state in which the undertaking is established is valid throughout the Union. Also, Directive 95/19/EC establishes the principle that infrastructure capacity should be allocated in accordance with the law on a non-discriminative basis. Fees charged should also be non discriminatory.

With regard to safety rules, under Directive 91/67/EEC the rule that the use of safety belts is compulsorily is adopted. Also, Directive 82/714/EEC laid down the technical requirements for vessels. In addition, with regard to the transport of dangerous goods by road, the Directive 94/551/EC dealt with some approximation of laws of the Member States. This issue, also, cannot be finalised as it is entangled with border control issues.

With regard to the harmonisation of national legislation, under Directive 85/31/EEC the maximum authorised weight of a truck is 3.5 tonnes, allowing for certain national derogations. Also, under 77/143/EEC (amended several times), the approximation of national laws on the roadworthiness test for motor vehicles and their trailers is achieved. Finally, under 91/439/EEC, a driving licence obtained in one Member State is valid by using a credit card format. These directives are illustrated in the Table below.
Table 1.2.1
Directives on Common Transport Policy in the Union

<table>
<thead>
<tr>
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<tbody>
<tr>
<td>transport of goods by road</td>
<td>NO. 3572/90 EEC No. 74/56/EEC No. 311/93 EEC</td>
<td>professional skills and credit-worthiness are conditions cabotage arrangement: without quantitative restrictions</td>
</tr>
<tr>
<td>coach &amp; bus</td>
<td>No. 684/92</td>
<td>approximation of progressive liberalization</td>
</tr>
<tr>
<td>inland waterway</td>
<td>No. 91/672/EEC No. 2919/85</td>
<td>principle of mutual recognition of qualification some conditions for the access to Rhine river set</td>
</tr>
<tr>
<td>rail transport</td>
<td>No. 91/440/EEC</td>
<td>mutual recognition of licence</td>
</tr>
<tr>
<td>safety rules</td>
<td>No. 91/67/EEC No. 94/551/EC</td>
<td>safety belt is compulsory approximation of laws on the transport of dangerous goods</td>
</tr>
<tr>
<td>harmonisation of national legislation</td>
<td>No. 85/31/EEC No. 77/143/EEC No. 91/439/EEC</td>
<td>up to 3.5 tonnes, automatically allowed to move without check approximation of national laws on road-worthiness tests driving licence is valid throughout the Union</td>
</tr>
</tbody>
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However, as Cockfield (then the Vice-president of the Commission) identified, one of the biggest problems in transport emerged in areas such as cabotage and quotas in some Member States, on the grounds of environmental protection. Cabotage refers to the liberalisation of market entry and also the easing of frontier crossings between Member States. The aim is to have total freedom within the Community market. Environmental issues however again cause problems as they potentially conflict with traditional notions regarding the equality of treatment of alternative modes, in that it implies favouring environmentally-friendly transport. Trans-Alpine Transit (TAT), for instance, especially through Austria and Switzerland has been the subject of much conjecture, not just because of European transport policy, but also because of the context of environmental protection.

The Convention on the protection of the Alps (the Alpine Convention) was signed by six contracting-parties in 1991 to protect the natural environment in the Alps. Under article 2(2)(j) of the Convention, it was designed to reduce the volume of inter-Alpine and TAT to a level not harmful to humans, animals, plants and their habitats by switching more
traffic, particularly freight traffic, to the railway. It does this by providing appropriate infrastructure and incentives complying with market principles without discrimination on the grounds of nationality. Unfortunately, the transport issue has not been finalised yet. The issue of transport is conducted by bilateral negotiation only.

The Transit Agreement with Austria as an alternative was completed on 6 December 1991, and was due to apply from October 1, 1994 as Austria joined the EU. Under the Agreement, Austria is still allowed to apply the 'eco-model' to all transit traffic. Since nitrogen oxide plays such an important part in fatal damage to forests and climate, an average emission of 15.8g Nox/Kwh was agreed between Members. No vehicle which emits more than 15.8g/Kwh is allowed transit through Austria. Therefore, the idea of free movement of goods is again subject to environmental consideration. In order to conserve its natural environment Austria is allowed to carry out checks on the eco-points within its own territory, as part of the general traffic checks.

Moreover, Switzerland, still not an EU Member, is applying a different environmental measure: the overflow system. This allows 40-tonne trucks to transit through Switzerland provided certain strict criteria are met. Every truck over 28-tonne is required to obtain a special permit. In fact, only seven permits out of a total of 15,000 allowed each year were issued between 1993 and 1995. The over-flow system still receives some criticism from EU Members because, under Article 36 of the Swiss Federal Constitution, all transit of goods through Switzerland are required to be shifted to railways within a period of ten years, ie by 2004, in order to protect the Alps.

The issue of freedom of goods and people, in terms of transport, is necessarily related to issues of border control. That is to say, a freedom of movement, whether goods or people, includes all the issues of immigration such as refugees, tax-evasion, drug-control at frontiers, intellectual property right protection, right to data protection and some

28) It has been ratified by six contracting parties: Australia, France, Germany, Lichenstein, Slovenia and the European Union.
30) Ibid., 959.
issues of enlargement. Simply speaking, the freedom of goods, in terms of transport, cannot be conclusively answered without reference to the above issues.

It seems appropriate to describe society in the 21st century as a 'global information society'. Especially in Europe, the more the free flow of goods necessarily accompany the free movement of people across frontiers, the more national authorities are called on to collaborate and exchange personal data in order to perform their duties. According to T. Zerdick, more than half of European citizens think that new information-based technologies will endanger their privacy. The corollary of this is that the Union, especially the Council, is keen to protect private information through legislation or by various other means.

First, the Council's Convention for the protection of individuals, with regard to Automatic Processing of Personal Data (Convention 108), is particularly important because it is the first in public international law with legally binding force concerning data protection. The aim of the convention, signed and ratified though Member States' legislation, is to guarantee every individual a right to data protection. But, as appears in the following Table, Italy and Greece are not bound to this Convention. This means that a hypothetical person AA may be able to move freely to any of the Member States if they obtained a permit from any of the Member States because the information kept in the Data base is the same. However AA may have to obtain another permit to go to Italy or Austria because these two countries are not bound to observe the regulations. As a result, the freedom of goods necessarily, accompanied by freedom of people, is subject to the right to data protection.31)

In addition, the Data Protection Directive has attracted the attention of the Union since the Schengen Agreement brought attention to immigration and refugee issues. The freedom of goods is therefore mixed with immigration, an issue discussed later. At this stage however it warrants mention that seven out of fifteen Member States are full members of the Agreement; two (Italy and Austria) are members but not yet implemented; four out of fifteen have interest and one, the UK, is

not a member of the Agreement. This means that if the hypothetical person AA has an unsuccessful record of applying for refugee status or immigration, s/he may have another problem in moving to the non-full member countries. The Table 1.2.2 explains this.

With regard to Regulation 684/92, freedom of border control is one core element of freedom of goods. However, under Article K.1(9) of the TEU, the European Police Office (EUROPOL) and the European Drug Unit (EDU) were set up in areas in which Member States have a common interest. This means that the idea of freedom of goods is clearly subject to border control by way of EUROPOL and EDU.\(^{32}\)

What must also be mentioned is the inconsistency between Act and Directive or between Acts. As mentioned above, the Council Regulation is subject to Article K.1(9) TEU. Regulation 684/92 provides that as far as buses and coaches are concerned, the Union is heading for liberalization of movements. Article K.1(9), however, provides that each Member State, using EUROPOL or EDU, may be able to check the movement of transport, if a private vehicle is used to the transport. This means that if the hypothetical person AA is moving by a bus or coach, s/he is clearly entitled to claim that there is 'a frontier' in the Community.

Finally, trade between countries is clearly affected by the status of intellectual property rights. The differences of protection in intellectual property rights have been described as a non-tariff or unfair trade practice. This leads into a discussion of the issue of intellectual property rights in the Union.\(^{33}\) There is an international regime on Trade-Related Intellectual Property Rights (TRIPs) which has made some developments. One of the major problems, in relation to freedom of goods, is that in some Member States certain types of products are not patentable. The prime examples are pharmaceuticals, foodstuffs, and chemicals in Austria, Finland, Greece and Norway. This means that if the hypothetical person AA was involved in chemicals or foodstuffs patented in another Member State, they may not prefer to trade with Austria or Finland because it is

\(^{32}\) Ibid., 73

\(^{33}\) It is estimated that up to 100,000 job opportunities may have been lost in the Union because of piracy abroad. Specifically, up to 66 percent of all computer software in France may be pirated, while in Spain and the Netherlands, the figure are 88 and 78 percents respectively. (Mathew, 15)
not patentable.\textsuperscript{34)

<table>
<thead>
<tr>
<th>Member States</th>
<th>Council membership</th>
<th>Convention 108 signed</th>
<th>Convention 108 ratified</th>
<th>Schengen Implementing Convention status</th>
<th>National Data protection legislation</th>
</tr>
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<tr>
<td>Austria</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
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<tr>
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<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>full member (observer)</td>
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<tr>
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<td>Yes</td>
<td>full member</td>
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<tr>
<td>France</td>
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<td>Yes</td>
<td>full member</td>
<td>Yes</td>
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<tr>
<td>Germany</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>member but not yet implemented</td>
<td>Yes</td>
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<td>Greece</td>
<td>Yes</td>
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Copyright is one aspect of intellectual property rights. Copyright in the Union is governed under the Berne Convention. The Union has itself been making progress on harmonising copyright protection under Directive 250/91/EEC, whilst the World Intellectual Property Organization (WIPO) is in charge as a whole, including Europe. The real issue is whether the remedy available under the Berne Convention is adequate. M. O'Regan, who specialises in intellectual property law is of the view that the Berne Convention may not provide adequate remedy because the signatories between the two are different.\textsuperscript{35)

\textsuperscript{34} Ibid., 11
\textsuperscript{35} Ibid., 29
As a whole, the idea of a frontier-free Europe has been developed gradually. Some evidence, however, shows that the free movement of goods are again subject to environmental issues. The TAT Convention is a case in point. Again, the environmental issue is connected to the Alpine Convention, which includes the Swiss as a signatory of the Convention. Environmental issues are interwoven with the issue of enlargement of the Union. The basic idea of freedom of goods is necessarily related to the freedom of people, which is necessarily connected to the issue of border control. The freedom of people may be distorted by the Data Protection Directive. The freedom of people is also subject to drug control by EDU or EUROPOL. The differences of protection of intellectual property rights may affect trade. Trade may also be distorted because some items are unpatentable in some Member States. The trade and freedom of goods is also affected by inadequate remedies available under the European Berne Convention, mainly because the Convention has different signatories than the WIPO.
1.3 Indirect Taxation of Goods

Value Added Tax (VAT), excise duty and corporation tax amount to another type of barrier to the freedom of goods in the SEM. Where one Member State imposes a higher tax rate than others, it may be less attractive to import products. Where, on the other hand, one Member State imposes extremely low tax rates, all other Member States are likely to be disadvantaged because the freedom of goods is affected. This is why taxation harmonisation is important to the freedom of goods.

Equally, from a neofunctionalist point of view, the spill-over effect from the economic sector to the political one is automatic by way of central institution building. Taking into account that the freedom of goods consists of mainly two complementary parts, the tariff and non-tariff barrier as well, a driving force in the non-tariff barrier should over-spill the tariff barrier, political factor. This means that the economic spill-over effect, standardisation and transport systems harmonisation for example, will overcome political barriers such as taxation in the development of the SEM. To put it another way, if the SEM has a common market for VAT, excise duty and company tax, the proposition of the neofunctionalism that economic spill-over will over-spill eventually is automatically proven. This is the fundamental hypothesis of this chapter.

Let me begin with the VAT issue first. The VAT currently levied for the benefit of each Member State rather than the Community is by nature incompatible with the idea of the free movement of goods in the SEM. A fundamental question is whether or not the Union is allowed to levy tax. If the answer is positive, the Union has taken over economic sovereignty from the Member States. However, the answer is negative, as all Member States' economic sovereign power is still in motion independently of the economic spill-over effect.

If the Union does not have the power to levy tax, the next
issue involves the country's entitlement to levy tax, for example, whether the Union, a central institution, can share or 'take' the power to make a decision in taxation. The answer is 'partially' positive because the Union is allowed to provide a certain range of tax rates in the SEM where all Member States are bound to levy tax 'within' the ranges of rates given by the central institution. Article 90 - 93 EC\textsuperscript{36} Treaty provides for the Commission to consider the harmonization of turnover taxes, excise duties, and other indirect taxes in the interests of the Common Market. The Article was strengthened by the SEA making such harmonization mandatory, where it was necessary, in order to ensure the establishment and functioning of the Common Market.

It is logical then to look at the directives in order to understand the overall development of harmonization in taxation. In 1967, in the first VAT Directive, the Community paid attention to the implications of VAT. Under the Directive, the Union introduced VAT, replacing each national indirect tax system. This was designed to remedy the problems caused by re-taxing of import goods and de-taxing of export goods under the old system. In 1977, under the sixth Directive, the Union tried to ensure that each Member State had a broadly identical VAT base. In 1985, the Commission published a Single Market White Paper, part III of which covered the removal of fiscal barriers. This relates primarily to the destination principle. The destination

\textsuperscript{36} Article 90 of the EC Treaty reads that "No Member State shall impose, directly or indirectly, on the products of other Member States any internal taxation of any kind in excess of that imposed directly or indirectly on similar domestic products. Furthermore, no Member State shall impose on the products of other Member States any internal taxation of such a nature as to afford indirect protection to other products."

Article 91 of the EC Treaty reads "where products are exported to the territory of any member State, any repayment of internal taxation shall not exceed the internal taxation imposed on them whether directly or indirectly."

Article 92 of the EC Treaty reads "In the case of charges other than turnover taxes, excise duties and other forms of indirect taxation, remissions and repayments in respect of exports to other Member States may not be granted and countervailing charges in respects of imports from member States may not be imposed unless the measures contemplated have been previously approved for a limited period by the Council."

Article 93 of the EC Treaty reads "The Councils, acting unanimously on a proposal from the Commission and after consulting the EP and the Economic and Social Committee, adopt provisions for the harmonisation of legislation concerning turnover taxes, excise duties, and other forms of indirect taxes..."
principle entitles the country of destination, not the exporting
country nor the Union, to levy tax. As goods left one country
they were de-taxed and were then re-taxed by the importing
country. In terms of finance this is advantageous to the country
of destination as opposed to the exporting country. This
introduced much incentive for trade distortion. Physical frontier
controls were therefore the corollary of the destination principle.
As a result, in 1985 the Commission proposed to introduce the
origin principle in order to remedy the problems exposed by
the destination principle. This was planned to take effect in
between 1996–1999. Table 1.3.1 below shows the development of
directives succinctly.

<table>
<thead>
<tr>
<th>Year</th>
<th>Event Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>1967</td>
<td>First Directive: replacing national indirect taxes for VAT to make sure transparency</td>
</tr>
<tr>
<td>1977</td>
<td>Sixth Directive: Community identical VAT rates</td>
</tr>
<tr>
<td>1992</td>
<td>Transitional period to origin principle</td>
</tr>
<tr>
<td>1996–1999</td>
<td>Origin principle is to take effect in due course</td>
</tr>
</tbody>
</table>

* Source: European Parliament Directorate General for Research, Fact Sheets on the
European Union, Luxembourg, 1997, p. 95

The first question involves the real difference between the
destination and the origin principles. The distinction between the
two approaches is important when considering the problem of
free movement of goods. Let me explain the basic nature of the
origin principle. We start by assuming that a product with similar
characteristics is produced in Holland for 100 guilders and in
Spain for 5,500 pesetas, with an exchange rate of 1 to 55.
Ignoring transportation costs, we also assume that production
costs are identical. Under the origin principle, VAT is applied at
the country of origin, which for the stated goods was 17.5
percent in The Netherlands and 16 percent in Spain, as of the
year 2000. The Dutch-produced item requires 17.5 percent of VAT to be added in both the home and overseas markets. It is sold on the Dutch market for 117.5 guilders and on the Spanish market for 6462.5 pesetas. On the other hand, the Spanish-produced item has had 16 percent VAT added and is thus sold for 116 guilders in Holland and 6380 pesetas in Spain. As a result, the origin principle clearly disadvantages the Dutch with their higher tax rate. So there are many incentives to lower the tax rates; this is the underlying intention of the Union.

It is however true that, with the exception of Denmark, every Member State is operating more than one rate of VAT. Therefore the following question should be whether the Union has an identical VAT rate on a certain product in the Common Market. The Union is working towards harmonization within the basic Community guidelines. One example is Directive 92/77/EEC. This Directive provided some basic guidelines such as: 1) a minimum standard rate applicable to the majority of consumer products of 15 percent; 2) subject to review every two years; 3) with each country allowed to apply a reduced rate for selected different basic commodities, i.e. medication or cultural products; 4) with some derogation being allowed for certain Member States to apply a zero (parking) rate if it introduces a definitive VAT system; and 5) finally, under the Directive, the Union introduced a new maximum 25 percent tax rate, instead of the higher tax rate then in existence.\(^{37}\) Table 1.3.2 below shows the VAT rates in the Common Market. One issue arises as to whether, under the 92 Directive, an item in different Member States is applied to the same tax rate, in the Union. This critical question engenders several minor issues.

Table 1.3.2
VAT Rates in the Common Market, as of 2000

<table>
<thead>
<tr>
<th>Country</th>
<th>Full rate</th>
<th>Special rate</th>
<th>Country</th>
<th>Full rate</th>
<th>Special rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>Austria</td>
<td>20</td>
<td>10</td>
<td>Belgium</td>
<td>21</td>
<td>–</td>
</tr>
<tr>
<td>Denmark</td>
<td>25</td>
<td>–</td>
<td>Finland</td>
<td>22</td>
<td>8</td>
</tr>
<tr>
<td>France</td>
<td>20</td>
<td>6</td>
<td>Germany</td>
<td>15</td>
<td>7</td>
</tr>
<tr>
<td>Greece</td>
<td>18</td>
<td>–</td>
<td>Ireland</td>
<td>21</td>
<td>–</td>
</tr>
<tr>
<td>Italy</td>
<td>19</td>
<td>16/10/4</td>
<td>Luxembourg</td>
<td>15</td>
<td>3</td>
</tr>
<tr>
<td>Netherlands</td>
<td>17.5</td>
<td>6</td>
<td>Portugal</td>
<td>17</td>
<td>0</td>
</tr>
<tr>
<td>Spain</td>
<td>16</td>
<td>7</td>
<td>Sweden</td>
<td>25</td>
<td>0</td>
</tr>
<tr>
<td>UK</td>
<td>17.5</td>
<td>12/6</td>
<td>Iceland</td>
<td>24</td>
<td>5</td>
</tr>
<tr>
<td>Hungary</td>
<td>25</td>
<td>–</td>
<td>Norway</td>
<td>23</td>
<td>–</td>
</tr>
<tr>
<td>Liechtenstein</td>
<td>6.5</td>
<td>–</td>
<td>Switzerland</td>
<td>6.5</td>
<td>3/2</td>
</tr>
</tbody>
</table>

* Standard applicable to the majority of consumer products.
* Each country applies a lower rate for selected different basic commodities, medication and/or cultural products.
* In the UK, children’s clothes, books, newspapers, newly constructed houses and fresh foods are free of VAT.

Firstly, let me propose a hypothetical situation. The person AA is exporting one item from A to C, which is assembled in the country of A but manufactured in C. Is the product foreign or domestic from country C’s point of view? This can cause a trade distortion depending on the definition of the 'home product'. Discrimination against foreign products has also usually been achieved through a narrow definition of product categories, and the imposition of widely different levels imposed on each of them. The essence of this problem lies in the fact that the Union has no practical competence on this point.

Tsoukalis pinpoints the crucial problem: the real issue should be whether the same product produced in another Member State is assigned the same (or similar) rate of VAT in the Common Market. As the Table above shows, the low rate varies from zero on food, fuel and children’s clothes in the UK to 10 percent in Ireland. The high rates vary from 25 percent in Sweden and Denmark, because the Union does not provide a common 'system for classification of a product'. Given this, it is somewhat unrealistic to speak of a Single Market for any given product.38)

38) Loukas Tsoukalis, From Customs Union to the Internal Market, in The New European Economy, OUP, 1992, p. 227
Furthermore, it is also true that some Member States are operating 'repayment' of the VAT levied. The UK is one example. VAT in the UK is levied on the point of sale of, say, children’s clothes, but it is refunded at the point of production. The end result, then, is no VAT on children’s clothes. With regard to repayment of VAT, an issue may arise in relation to border control as the UK clearly gives an incentive to tax. The issue, as a result, is again 'associated' with other problems such as border control.\(^{39}\)

Again, it is necessary to question whether the VAT system is applied to all products. Article 38 of the EC aims to increase agricultural productivity and thus ensure a fair standard of living for persons engaged in agriculture. This is to stabilize markets, assume the availability of supplies and ensure that the supplies reach consumers at reasonable prices. In short, agricultural policy and the agricultural market have gained a special position in the Common Market, a principle which continues unchanged in the TEU. Therefore agriculture is exempted from the normal taxation rule.\(^{40}\)

The idea of a Clearing House was designed to alleviate the tension between the Union and the Member States. The system allowed importers to reclaim the VAT paid to the exporting country, and apply the importing country’s rate of VAT to the total value of the goods. The sale would be taxable in the hands of the vendor, and the VAT incurred by the purchaser would be deductible irrespective of the Member States in which it had been charged. This system however has attracted considerable criticism on two grounds. Firstly, the clearing house system was seen as unnecessarily bureaucratic and costly; as a result it did not match with the idea of 'economic' integration.\(^{41}\) Secondly, no

\(^{39}\) Ibid., p. 227
\(^{40}\) Commission of the European Union, Europe from A to Z: A Guidebook to European Integration, 1996, p.23.

It is a common knowledge that the attempt to ensure a fair standard of living for the agricultural community primarily through support for Community prices, by way of state aid, at above world prices led the Union being accused by the outside world of protectionism.

For more, see 3.3 this thesis.
provision of any Community Act provides that the Union is entitled to levy taxes. So again, there is an ‘association’ of problems between subsidiarity and the presumption of integration.

Finally, some legal persons (i.e. hospital and public authority) are exempted from tax. However, where these legal persons buy goods over a certain threshold from another Member States they are required to pay VAT on them at their domestic rate. This is despite the fact that the deliveries are, in theory, zero-rated. The vendor, not the importer, is accountable for the tax. The real question is whether the Union has a common set of rules to apply uniformly. If not, which country, exporting or importing, is entitled to set the threshold? Each Member State is allowed to set the threshold, again creating a tension between the Community and sovereign national body. For instance, Denmark and Sweden having high standard rates of VAT is against the idea of a higher threshold.42)

Another area of debate revolves around excise duty. The basic theory of excise duty follows. An excise duty is mainly applied to three general categories of goods: tobacco, alcoholic beverages and hydrocarbon oils. But each of these can be subdivided into a large number of excisable products. Excise duty can be broadly divided into two forms: bonded warehouse and the banderoles system. The first method is based on the close monitoring and supervision of production and movement of the dutiable goods up to the point where duty is paid. This is called the bonded warehouse system, and is operated by the UK. A second method is based on physical marking of the goods on which duty has been paid, using tax stamps or ‘banderoles’. With such a system, it is possible to distinguish between goods on which duty has been paid and goods on which it has not.43)

With regard to alcoholic beverages, Directive 92/83/EEC generally applies. It defines the products on which excise duty is to be levied, and the method of fixing the duty. In the case of beer, alcohol contents must be shown on the bottle in order to impose tax correctly. Under Directive 92/84/EEC the rates were set: alcohol (i.e. spirits) being 55 ECU; intermediate products being 45 ECU; beer being 1.87 per degree of alcohol.

With regard to tobacco, the conclusive regulation is in the Com/94/355 whereby the categories of manufactured tobacco, subject to taxation, are defined. Under the Directive, cigarettes are 57 percent of the tax-included price; hand rolled tobacco is 30 percent of the retail price, or ECU 20 per kilo; cigars are 75 percent of retail or ECU 7 per kilo; and pipe tobacco is 20 percent of the retail price.44)

In relation to the banderoles system, one technical problem again arises. If product P is grown in the country of D and manufactured (or assembled) in the country of S, is the product P, D's or S's? It is a matter of interpretation. If country S wishes to favour a domestic product and a domestic firm against foreign product, it easily does so by giving a 'wide' definition of 'home' product and vice versa. For instance, as Tsoukalas notes, a Scotch whisky can be effectively separated from Italian grappa, ending up with a very different tax burden in the final consumer price.45)

Also, with regard to the warehouse system, the critical point involves how to control over each step at the Community level rather than just harmonization at the Union level. It must again be noted that the warehouse system is not applied Community wide. It is only operated in the UK. The problem then is that there is no Union wide excise duty system.

At this stage, one question must be begged. If the hypothetical person, AA, wishes to import materials for tobacco from country A where the banderoles system applies, to the UK where the

45) Loukas Tsoukalas, The New European Economy, OUP, 1992, p. 120.
warehouse system applies, is the person expected to have a border control because the material is not taxed yet? The answer appears to be positive for two reasons. First, because without tax frontiers the single stage nature of excise duties make it possible for traders to benefit by paying excise duties in the lowest tax jurisdiction. Second, the high rate of excise duty induces traders to make a profit by pursuing more preferential exchange rates. Simply speaking, the Community does not play an important role in excise duty taxation because it is the Member States, rather than the Community, setting the duty rates.46)

As a whole, it is reasonable to argue that the issue of fair taxation of excise duty is unlikely to be achieved because the issue of taxation is so complicated.47) First, there is no uniform duty rate and system within the Community. Second, even though the Commission is proposing uniform duty rates, levied at the national currency equivalent of a uniform ecu level, exchange rate fluctuations during the course of a year will introduce divergences between countries. These may then give rise to incentives for traders seeking to pay duty in countries different from the country of eventual retail sale. Third, relating to the second problem, in excise duty timing is of importance because of its nature: single stage taxation with high rates. Taking all three points, excise duties contain many technical and fiscal problems.

Attention should finally be paid to company taxation, because the final tax rate of an item is affected not only by the VAT rate (or excise duty rate) but also the company tax rate, even indirectly. Legislation on the taxation of companies has usually been based on Article 100 of the Rome Treaty. The Commission has made very limited progress in this difficult area of company taxation. Some developments are as follows.


47) Ibid., 140.
intended to eliminate double taxation dividends paid by a subsidiary in one Member State to a parent company in another. Directive 90/436/EEC introduced procedures for disputes concerning the profits of associated companies in different Member States. Also, the Commission proposed a common system of taxation applicable to interest and royalty payments made between parent companies and subsidiaries in another Member State, which was however unsuccessful.\(^48\)

One of the main issues involves the national sovereign power of taxation. As far as company tax is concerned, the question of location is particularly relevant as three different company taxation systems are operating in the Market: classical, split and imputation systems. The location of parent companies and their subsidiaries, where the products are sold and where their shareholders live all affect the amount of total tax paid. There is no obvious solution to the problem of who has jurisdiction or who has a just claim to a particular share of these revenues under the current system.

Let's assume that a multinational German company is considering where to set up its new production plant. The cost of production and the potentional profits for the new products are identical in The Netherlands and Germany. As can be seen in Table 1.3.3, corporation tax is 43.6 percent in Germany and 35 percent in The Netherlands. Also, Germany adopts an imputation/split system whereas the Netherlands adopts a classical system.\(^49\) This means that consumers cannot compare the prices, in terms of tax, between products of different Member States, mainly because the company taxation system is not set by the Union.

\(^49\) A classical system requires that the taxation of corporate and personal income (when the profits are distributed to shareholders) are completely separated. Thus, profits distributed to shareholders will first be taxed as company income and then separately as shareholder's personal income. So, in fact, it is double taxed.

In contrast, in the split system retained profits is taxed at a higher rate than distributed profits to allow for the extra tax paid on them by shareholders. Imputation system allows all or part of the corporation tax paid on distributed profits as a credit against personal income tax liability.
Table 1.3.3
Corporation Tax in the Union as of 1998

<table>
<thead>
<tr>
<th>Country</th>
<th>percent</th>
<th>Type</th>
<th>Imputation rates</th>
</tr>
</thead>
<tbody>
<tr>
<td>Germany</td>
<td>43.6</td>
<td>Imputation/Split</td>
<td>36</td>
</tr>
<tr>
<td>France</td>
<td>41.6</td>
<td>Imputation</td>
<td>33.3</td>
</tr>
<tr>
<td>Italy</td>
<td>41.2</td>
<td>Imputation</td>
<td>36</td>
</tr>
<tr>
<td>Belgium</td>
<td>40.0</td>
<td>Imputation</td>
<td>33.3</td>
</tr>
<tr>
<td>Portugal</td>
<td>37.4</td>
<td>Split</td>
<td></td>
</tr>
<tr>
<td>Luxembourg</td>
<td>37.4</td>
<td>Classical</td>
<td></td>
</tr>
<tr>
<td>Greece</td>
<td>35</td>
<td>Imputation</td>
<td></td>
</tr>
<tr>
<td>Spain</td>
<td>35</td>
<td>Imputation</td>
<td>9.1</td>
</tr>
<tr>
<td>The Netherlands</td>
<td>35</td>
<td>Classical</td>
<td></td>
</tr>
<tr>
<td>Austria</td>
<td>34</td>
<td>-</td>
<td></td>
</tr>
<tr>
<td>Denmark</td>
<td>34</td>
<td>Imputation</td>
<td>20</td>
</tr>
<tr>
<td>Ireland</td>
<td>32</td>
<td>Imputation</td>
<td>5.3</td>
</tr>
<tr>
<td>UK</td>
<td>31</td>
<td>Imputation</td>
<td>25</td>
</tr>
<tr>
<td>Finland</td>
<td>28</td>
<td>-</td>
<td></td>
</tr>
<tr>
<td>Sweden</td>
<td>28</td>
<td>-</td>
<td></td>
</tr>
</tbody>
</table>

* The Commission is recommending a minimum rate of 30 percent.
* In the UK, small company tax rate is separate, 21 percent.

So one of the main problems involves the treatment of the tax credit. Should a Dutch shareholder of a German company residing in the Netherlands be entitled to receive a personal tax credit against The Netherlands income tax when corporation tax has been paid in Germany? A naive compromise involves that all Member States being allowed to charge a standard rate of corporation tax regardless of who owns the company. This means that, if the Dutch shareholder is currently in The Netherlands, s/he has to be taxed twice, once by the company and the other by direct taxation, whereas if s/he is in Germany, s/he is likely to be taxed only once. So it clearly distorts the freedom of goods and capital. This issue is also clearly connected to the 'freedom of people' because the actual amount of money taxed depends on where the shareholder resides!

In addition, it must be mentioned that under Articles 100 and 99, contrary to Article 100a under which most Common Market legislation was adopted, unanimity rule is required. So, voting rules in the Council are another stumbling block. As Tsoukalis argues, regarding the political feasibility of the Commission’s tax
harmonisation efforts, the unanimity requirement in the Council, persisting differences in the national taxation system, the importance of the interests at stake, and international pressures explain the scepticism expressed by some scholars. Simply, national resistance to harmonisation and integration on fiscal matters seems likely to survive longer than in many other areas. Like Smith, Tsoukalis concludes that strict harmonisation may, in fact, not be necessary: what will be needed in many cases is an agreement on minimum rates of taxation, as long as they are not always based on the lowest common denominator.50)

It is therefore fair to say that the term 'tax harmonisation' lacks substance. VAT, excise duty and corporation tax are at the heart of national fiscal interests. These remain under the control of political interests rather than those of economics. The Community has the mere power to set certain ranges of taxation and has limited jurisdiction, if any. There is no Union wide taxation system. The free movements of goods, therefore, remain distorted by the nationally dominated taxation system.

Recapping the very first preposition: from economic spill-over to political spill-over in the freedom of goods. According to neofunctionalists, the economic spill-over effect will over spill into political sector automatically. This means that, tax harmonisation 'should' be achieved by the domino effect of economic spill-over. Putting it another way, the basic preposition that economic drive such as standard and transport harmonisation will beget spill-over effect in the political sector, taxation for example, is not recognised. I therefore am bound to say that political factors are still in play in the SEM. This means that the neofunctionalism is not satisfactory in understanding the development of the SEM.

50) Ibid, 125
Chapter 2. Freedom of People

2.1 Lingual Barriers

The population of Europe, as of 1997, was around 375 million. The Community of fifteen Member States uses eleven working languages: English, German, French, Italian, Dutch, Danish, Greek, Spanish, Portuguese, Finnish and Swedish. Around two-thirds of the Community people, 210 out of 345 million, use main languages: German (91 million); French (64 million); and English (60 million). The complexity of the problem is caused by the fact that some countries in the EU are bi- or multi-lingual. There is no official language, either in name or effect. Nonetheless, many scholars have not recognised language as a problem to the Union. I, however, think language is one clear example of a barrier. I will thus explain why language is a problem.

Article B of the Maastricht Treaty proclaims its economic objectives toward 'acquis communautaire'. As stated by Article B, one of the immediate objectives of the TEU is economic. Article 8A of the Single European Act gives further information of an internal market comprising an area without internal frontiers in which the free movement of goods, persons, services and capital is ensured. To put it simply, the free movement of these four items is the objective of the Union. We must try

51) Screen, Breaking the Language Barrier, Screen Digest, February, pp. 33-37, 1990, p. 33
52) Article B
The Union shall set itself the following objectives:
- to promote economic and social progress which is balanced and sustainable in particular through the creation of an area without internal frontiers, through the strengthening of economic and social cohesion and the establishment of economic and monetary union, ultimately including a single currency in accordance with the provisions of this Treaty;
- to assert its identity on the international scene, in particular through the implementation of a common foreign and security policy including the eventual framing of a defence policy, which might in time lead to a common defence;
- to strengthen the protection of the rights and interests of the nationals of its Member States through the introduction of a citizenship of the Union;
- to develop close co-operation on justice and home affairs;
- to maintain in full the 'acquis communautaire' and build on it with a view to considering through the procedure referred to in Article N92), to what extent the policies and forms of co-operation introduced by this Treaty may need to be revised within the aim of ensuring the effectiveness of the mechanisms and the institutions of the Community.[Emphasis added]
53) Martin Holland, op cit., 68
and understand, then, why language is problematic to the free movement of these items.

The number of languages used in Europe is immense. In addition to the official languages of Member States spoken in the Union, up to 40 million citizens speak minority or regional languages. These minority languages include Catalan, Basque (Spain, France and Italy), Basque (France), Breton (France), Corsican (France), Frisian (Netherlands), Friulan (Ireland), Calician (England), Occitan (France), Ladin (Ireland), Sard (Ireland), Sorbian (Denmark) and Welsh (UK).54

The above is from the Report of the Commission in 1994. The Community unfortunately however provided no extensive policy involving 'language in the political Union'. While there are directives on the freedom of movement for workers, these directives deal with social policy, working conditions, employment incentives, protection for workers, social security, migrant workers and approximation of certain social policies. None of these directives are directly concerned with languages. So, it may be argued that the real problem to further integration is the fact that the Commission has not identified the lack of a common language as a substantial problem on the way to Common Market.

Let me again propose a hypothetical situation. The person AA, using English as his/her native tongue is moving to another Member State, where English is not spoken, with his/her family for work, immigration or some other reason.

Firstly let us suppose the hypothetical person is moving for a job to another country. Every European citizen has, in principle, the right to a job within Europe without discrimination. However this is not true from a practical point of view if the job applicant is not competent in the local language. The question arises as to what extent the right of free movement of labour (or people) is warranted if the person is not competent in the local language. It is a rule of law in Europe that a knowledge of the (or even a) local language is a precondition to the right of free movement. One case in point is Groener v Minister of Education and the City of Dublin Vocational Education Committee.55

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55) M Anderson & Eberhard Bort(ed.), *The Frontiers of Europe*, Pinter(UK), 1998, p.228

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concerns a Dutch citizen applying for full time teaching in Ireland. The appellant was rejected because she failed an Irish language test. The ECJ held that while, in principle, the right of a national of one Member State to seek employment in another Member State is protected, if there is a conflict between the protection of local culture and freedom of movement under the EC Treaty, the protection of local culture will prevail.

Language also has a bearing on the movement of people and goods as well. So, a question arises regarding the extent to which the right of free movement of goods is warranted or hampered if the goods do not bear the local language of the place it is sold. The real question is whether it is illegal to sell a bottled wine in Germany if German law requires that only Franconian wine may be sold in the 'Bocksbeutel' shape of bottle? Again, is it illegal to sell a frozen yoghurt in France with a label of 'Yoghurt' if French law restrict the use of the word 'Yoghurt' to a live product? One case in point is Piageme v Peeters. The ECJ held that Belgium could not require French and German mineral water labelled in those languages to be labelled in Dutch when sold in the Flemish area of Belgium without allowing for the possibility of using another language easily understood by purchasers. The real problem however arises over product liability. Let me propose one example. If one item produced in Germany is scheduled to be marketed in France, but the item does not show its German producer (or supplier) in French, a consumer in France may not have an 'effective' remedy against the defective product if the consumer does not have a knowledge of German. Furthermore, the Product Liability Directives (99/34/EEC or 85/374/EEC) do not cover this point of issue.

Also, as explained in section 3.3, language in association with the freedom of service causes another problem. One clear example is the Office for Harmonisation in the Internal Market (Trade Marks and Designs) established under the EC Regulation on the Community Trade Mark. The main problem here is that the languages of the Office is different from the official working languages, that is to say, all the Languages of the Office may be the working languages, but not vice versa. Therefore, as far as trade marks and design related property law
are concerned, only the Language of the Office is spoken. This means that all the non-Office language speaking countries and professions from these countries are discriminated against. Dutch, Danish, Greek, Portuguese, Finnish and Swedish are excluded in the languages of the Office. Simply speaking, if lawyer A is moving between the countries out of the Office language, the lawyer 'cannot' represent, at least, the interests of trade mark and design.

It is also true that different languages can deliver different meanings even though one is translated into the other. This results in technical barriers. This is demonstrated in Dega\(^56\), where Dega marketed tinned pineapple in Italy. The labels stated only the name and addresses of the producer/packager, a company established outside the Community, while Article 3(1)(6) of the Directive 79/112 required that a label give particulars of "manufacturer or packager, or of a seller established within the Community." Dega appealed after being fined because the Italian version did not include the comma between the words "packager" and "or of a seller established within the Community". Dega argued that the Article 3(1)(6) requires, at least, one of the three traders mentioned. The issue of Dega therefore was whether Article 3(1)(6) applies only to the seller or if, on the contrary, it must be satisfied by at least one of the three traders mentioned. The ECJ ruled that Article 3(1)(6) applies only to the seller, and not to the manufacturer or packager (supplier).

Again the real issue arises in connection with the supplier's liability. If a supplier is not obliged to give its details, how is a consumer protected from a defect in a product? The Product Liability Directives do not require a foreign supplier to be shown in the local language where the product is marketed. This means that there may be a Single Market for a producer but not for a consumer.

It is irrelevant whether or not the Commission possesses the legal capacity to institute such a policy. The real issue is whether, in practice, such a policy could work. Does the Union want an official language? Or does the Union want to make some dominant language govern the economic flow in Europe? I think the answer is likely to be the latter or

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\(^{56}\) Provincia Autonoma di Trento and Ufficio del Medico Provinciale de Trento v Dega di Depretto Gino Snc, 1997 CMLR 352
at least in between the former and the latter. Why? Simply because of the logical national economic interest. As Biltereyst suggests lingual proximity promotes economic trade and prosperity.\(^{57}\) Therefore, the Union is nothing more than a union of some powerful languages in Europe.

Language may be described as a 'home-town' of nationalism. Nationalism starts with language. If a given community has a common language, a common form of written and oral communication, then that community possesses a powerful vehicle for conveying common ideas and issues. The community is likely to have a sense of 'we-ness'. This is the focal point of nationalism in the light of language. We-ness, brought by community wide common language, is one aspect of nationalism.\(^{58}\) Therefore if the Union has a 'Union language', it is more likely to become a political Union.

Another point is that language has the capacity to make a community. A basic function of language is its inclusive power in an area. One area with a single language is likely to be united whereas one area that is communicated by more than one language is likely to be divided along language lines. History shows that the test of whether an imperial power can survive in a colonial territory depends upon whether the imperial power is able to implant its own language in the colony. In simple terms, language can be regarded as magnetic. If two areas with an identical language confront each other, inclusive power arises whereas if two areas that do not use an identical language, exclusive power arise between themselves.\(^{59}\) This means that if, and only if, the Common Market has one language, the Common Market is likely to become a Market of political fact rather than remain purely an economic Common Market. If a community does not have a common language, it is unlikely to be a community, in name and practice.

It seems timely to evaluate whether the EU can accomplish a Single Market without an all-dominant language. The answer depends upon what the SEM really is. If the single market is just an economic Union

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57) B. Anderson, *Imagined Communities*, Verso (the USA), 1991, p. 183
58) Ibid., p. 183
59) Ibid., 183
without internal frontiers, language is not a clear barrier to all four items of free movement. If the target of the Union is political Union, as provided by Article C of the Treaty and issues of IGC in 1991 and 1997, the answer concerning language may be different. So this issue turns to the question: has the Common Market been used as a 'trojan horse' to achieve a political Union.

Article C of the TEU signifies that its purpose is more than just economic Union. The aim of the provision of Article C is very much political in mentioning that the "Union shall be served by a single institutional framework which shall ensure the consistency and continuity of the activities carried out in order to attain its objectives while respecting and building upon the 'acquis communautaire'. It is, therefore natural to take into account the question of whether language is a barrier to political union. The answer to this issue is, as demonstrated earlier, clearly yes. Language therefore is a critical barrier to the Common Market which has been regarded by some people as a trojan horse to political Union.

Nevertheless, one may argue that the idea of digital language can remove the language barrier in Europe. The grounds for this argument are that the telecommunications sector has undergone a technological revolution since the 1970s. New technologies have altered markets by making available a vast array of new services and equipment so that the importance of human language is weakened. Moreover, many people now agree that the world has moved closer to form one electronic information environment.

However, it seems premature to insist that digital language can replace the barriers posed by natural language. Firstly, the trends in Europe have been for more liberalization than in the USA or Japan. This is because telecommunication sector in Europe has been fragmented into

60) Article C

The article shall be served by a single institutional framework which shall ensure the consistency and continuity of the activities carried out in order to attain its objectives while respecting and building upon the 'acquis communautaire'.

The Union shall in particular ensure the consistency of its external activities as a whole in the context of its external relations, security, economic and development policies. The Council and Commission shall be responsible for ensuring such consistency. They shall ensure the implementation of these policies, each in accordance with its respective powers. [Emphasis added]
autonomous national systems. They are technically incompatible, offer distinct services and equipment, and utilize differing tariff principles. Thus, it is not surprising that the regime for coordinating European telecoms has operated on the principle of pure national autonomy.

The second reason why the 'future language' will not quickly replace the barrier is that each nation state has had a monopoly over terminals, network, and standards. Telecommunications have always been regarded as both a natural monopoly and a public utility, justifying the extensive and exclusive powers of the Member State's Posts, Telegraphs, and Telephones (PTT). Table 2.1.1 shows the degree of monopoly by each Member State.

<table>
<thead>
<tr>
<th>Countries</th>
<th>Networks</th>
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<th>Terminals</th>
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** O = open; S = semi-open; M = monopoly

It is enough to ask the final question of whether nationalism can be nullified by the idea of 'acquis communautaire'. What is nationalism? I believe as do some scholars an answer to this question comes from where nationalism arises: the nation state. For instance, Kellas argues that nationalism is an ideology which builds on the idea of the nation and makes it the basis for action.61) This definition strongly suggests that the nation state seems to be the harbour for nationalism. Therefore, nationalism built mainly on its local language seems to be incompatible with the EU, because nationalism comes from the nation state, so nation

states, by definition, are incompatible with the Union. This is to say, it is not easy for the Union to nullify the nationalism of Member States.

Others however may argue that nationalism is already being nullified because the EU has 15 Member States, with more waiting. One of the most powerful reasons are the citizenship and supremacy of the Union. That is to say, because the allegiance of the people of the Union has been transferred to the superior Community, citizenship has been conferred.

Let me however ask to whom primary allegiance is owed. By whom is it owed? Article 8.1 of the Maastricht Treaty provides that "every person holding the nationality of a Member State shall be a citizen of the Union." This means that the pre-requisite of the Community citizenship is holding the nationality of each Member State. In simple terms, the Community is an indirect, rather than a direct source of power. The Community therefore does not have the authority that the allegiance of every citizen gives. This encapsulates Weiler's idea of the democratic deficit which indicates that this is associated with the issue of 'citizenship'. I therefore am bound to explore that issue in the following section.

All things taken into account, language is, or functions as, a barrier to the freedom of people. Language may also cause a barrier to the freedom of goods. Moreover, language can cause a problem in relation to services. These are all issues the Commission has yet to address. This is the problem of problems.

Some argue that the importance of language, especially human language, may be discounted because of 'digital' language. That is to say, the Common Market may be accomplished by spurring the freedom of goods through computer transactions. This argument may be right if the TEU focuses only on economic integration and freedom of goods. The TEU however aims for political Union by way of freedom of people and Union citizenship. Therefore the argument is not persuasive because all the standards of networks and terminal are governed by each Member State, rather than by the Union. This means that digital (computer)

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language is based on and cannot avoid 'national' foundations, reflecting nationalism rather than 'acquis Communautaire'.

Also, some argue that nationalism has been, and will be transferred to the Union by way of "union citizenship" under Article 8.1 TEU. However, the Community may not be able to assume the allegiance of people because, as Weiler argues, it is 'indirect', not direct, representation.
2.2 Migrant Workers

Language is not the only barrier to the free movement of workers. For a person (whether a student, a liberal professional, employed or self-employed) to enjoy the freedom of movement some requirements must be met. Not every class of person is eligible for this freedom. I again propose that a hypothetical person AA is moving to another country for the purpose of a job, or study with his/her family. I will focus on freedom of migrant workers, with special emphasis on immigration because immigration is the zenith of the free movement of people.

A survey issued by the Commission showed that no less than 1.6 percent of 375.34 million EC population are working in a Member State that is not the state to which they are nationals. A large majority of these individuals are non-EC nationals and some 5 million nationals work in an EC Member State other than that whose nationality they hold, as of the year 2000. This issue therefore attracts attention.

The legal base for freedom of workers is found in Article 39 - 42 EC Treaty which provides that Union citizens have the right to move and reside freely within the territory of the Member States, subject to the limitations laid down by Community law. Also, as far as immigration and asylum are concerned, Article 61 - 69 applies. This section must be construed in conjunction with Article 39(3)(4) of the Treaty. Under Article 39(3)(4), a Member State may also at its discretion limit their exercise on grounds of public health. Also, these rights do not apply to

64) Article 39 EC reads that "1. Freedom of movement for workers shall be secured within the Community." 2. Such freedom of movement shall entail the abolition of any discrimination based on nationality between workers of the Member States as regards employment, remuneration and other conditions of work and employment."
65) Article 61 EC reads that "In order to establish progressively an area of freedom, security and justice, the Council shall adopt: ..... b) in the field of asylum, immigration and safeguarding the rights of nationals of third countries......

Article 62 of the Treaty reads that ".... shall adopt 1) measures with a view to ensuring the absence of any controls on persons when crossing internal borders....; 2) measures on the crossing of the external borders of the Member States which shall establish a) standards and procedures to be followed in carrying out checks on persons at such borders; b) rules on visas for intended stays of no more than three months.

66) Article 39 EC reads that "3. It shall entail the right, subject to limitations justified on grounds of public policy, public security or public health...." 4. "The provision of the Article shall not apply to employment in the public service."
employment in the public service.

Based on the above provisions, the Commission has issued several Directives and Regulations. Council Directive 68/360 firstly deals with the abolition of restrictions on the free movement of workers and their families within Member States. Directive 77/480/EEC also deals with the education of migrant worker's children. Directive 89/48/EEC harmonises the recognition of their higher education and training for at least three years duration. Finally, Directive 99/42/EEC establishes a mechanism for the recognition of qualifications in respect to professional activities. Several issues arise from an examination of these Directives.

First, who is a 'worker' for the purpose of the Treaty and Directives? The definition of the term 'worker' is not sufficiently clear. On the one hand, there must be a relationship of employment. It matters not whether that employment is full time or part time as long as it is real and effective and not simply marginal or ancillary. S/he is a worker if s/he performs service for and under the direction of another, in return for which s/he received remuneration. This is the rule of law of Levin.\(^67\) On the other hand, as time passes, the ECJ has tried to narrow this definition. The Court, in Birden, held that the worker needs to be duly registered as belonging to the labour force for a Member State. To be "duly registered as belonging to the labour force" a worker is required to have complied with the legislation of the host country to enter its territory and pursue employment. This means that if a person gets a job in a Member State after s/he sneaks into the country, s/he is not a worker for the purpose of the Treaty no matter how long s/he has worked for the company.\(^68\)

The second main issue is which members of a family will be entitled to accompany him/her to his/her place of work. Article 10(1) of the Regulation 1612/68 provides that the following persons are entitled to install themselves with a worker.

a) a spouse and descendants who are under the age of 21 or who are dependants;

b) dependant relatives in the ascending line of the worker and spouse.

\(^{67}\) Levin v Staatsecretaris van Justice, 1982 2 CMLR 454

\(^{68}\) Mehmet Birden v Stadtgemeinde Bremen, 1999 1 CMLR 420
In connection with this second issue, a related question arises as to whether a spouse of a citizen of a Member State is entitled to be granted indefinite leave to remain in the Member State where his/her spouse has citizenship. The answer depends on whether the spouse is a national of a Member State or not. If the spouse is not a national, that is to say, if the spouse is from a non-Member State, the Member State concerned is entitled to decide on the question. Simply speaking, there is no common guideline in the Union as to this point of issue. *Sahota* provides a case in point.

In 1989, A. K. Sahota, a UK national, went to live in Germany, exercising her rights under Article 48 EC. In March 1990, she married S. S. Sahota, a citizen of India at a time when both were lawfully working and residing in Germany. She returned to the UK in 1994, accompanied by her husband, who was given leave to enter as a visitor for six months with a prohibition against taking employment. He then applied for indefinite leave to remain in the UK on the basis that his wife had exercised her EC rights to freedom of movement. The English Court of Appeal held that the applicants were not entitled to remain as a matter of Community law. This case indicates that there should be a clear distinction between EU nationals and non-EU nationals. This is the reason why the Union has been accused of building 'fortress Europe', not 'frontier-free Europa'.

Attention must be given to Commission Recommendation 97/304, which concerns an unemployed person accompanying his/her spouse who is employed in a Member State other than their own. The Union has not succeeded in providing common guidelines on this point because it is a mere 'recommendation' with no legal binding power.69)

In the above paragraph, it is noted that the freedom of movement is subject to 'public security' or 'public health'. Then, in connection with this exemption clause, a third major issue arises as to whether the Union provides uniform guidelines on this point. In theory, it should do because this is a way that the Union could guarantee people are not discriminated against because of their nationality. In practice however, it is the

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Member States, not the Union, that judge and apply 'public policy' exemption provisions. Rogue\textsuperscript{70} is a case in point.

Rogue, a Portuguese national, arrived in Jersey in February 1994 and found employment as a night porter at a hotel. He was dismissed from the hotel for theft and following conviction, was placed on probation for one year. During that time, he again committed theft while employed by a second hotel, for which he served 14 weeks imprisonment and was later served with a deportation order. Rogue's argument relied on Article 4 of the Protocol 3 on the Act of Accession of the UK. He argued that the deportation order was invalid because the Article operated to prevent a national of a Member State being deported from Jersey, since a UK citizen was not capable of being so deported under national law. So the issue was whether Article 4 (equal treatment provision) had been complied with. The ECJ, in preliminary ruling, held that Article 4 of the Protocol did not limit the reasons for deporting a national of a Member State other than the UK to those justified on grounds of public policy.

Another minor issue arises as to the term 'equal treatment between nationalities'. Firstly, it is necessary to ask whether a social benefit or a security scheme is portable when a recipient moves to another Member State. In Snares v Adjudication Officer, the applicant was on a Disability Living Allowances (DLA) in England following a serious accident. When he informed the adjudication officer of his wish to settle in Tenerife where his family lived, the officer decided that his entitlement to DLA ceased on his departure from his UK home. On appeal, the ECJ ruled that the principle of exportability of social security benefits applied so long as derogating provisions had not been adopted by the Community legislature.\textsuperscript{71} The real issue at this stage therefore, regards the benefits of the descendant of the migrant worker.

As I already mentioned, a person who is a descendant and under the age of 21 is entitled to install him/herself as a worker. An issue at this stage is whether a descendant keeps his/her status with regard to a benefit regardless of his/her principal applicant's death. The answer to this question depends on whether the country of origin is a Member

\textsuperscript{70} Rui Alberto Pereira Rogue v Lieutenant Governor of Jersey, 1998 1 CMLR 143
\textsuperscript{71} 1998 1 CMLR 898
State or not at the time of the principal applicant's death. The case is *Romero,*72) Mr. M. Romero was a Spanish national residing in Spain whose father, who had been employed in Germany, died following an accident at work in 1969. From the commencement of his education and vocational training, Mr. M. Romero had received an orphan's benefit from the German government. The payment of the benefit continued until he reached the age of 25 without taking any account of the period of his Spanish military service. Romero requested that the payment should be continued under Article 3(1) Regulation 1408/71. The Article provides that where the legislation of a Member State provided for the extension of the right to a benefit beyond the age of 25 for recipients of benefits whose training had been interpreted by their military service, that state was required to assimilate the military service in another Member State to military service under its own legislation. The ECJ held that a worker must not suffer discrimination on the grounds of nationality under Article 48(2). However it also held that a national of a Member State who died before his country of origin acceded to the Union did not have the status of a worker for the purpose of Article 48(2). This means that there is a an 'unequal treatent' depending on the date of the accession of the country of origin to the Union. Simply speaking, some people in a Member State may qualify for a social benefit while others in the same Member State may not!

A fourth major issue relates to pension schemes. If a hypothetical person is close to the age of pension, it is critical to decide whether to move to another country even though he/she is able to get a work permit in another Member State. This is a corner-stone for 'more' freedom of movement for workers. Under the Council Directive 98/49/EC 73) the Union established the principle of portable pension rights of employed or self-employed persons moving in the Community. The Directive, however, covers the 'supplementary pension' scheme: retirement pensions, survivor's benefits or those provided in respect of some contingencies by statutory social security system under Article 3 of the Directive. This means that if the hypothetical person joins a 'private'

72) *Carlos Mora Romero v Landesversicherungsanstalt Rheinprovinz*, 1997 3 CMLR 1141
pension scheme, the pension is not portable. It must be mentioned that Greece, Italy and Portugal have all introduced legislation to create a framework for private pensions and provide the legal regime for their operation and administration.\(^\text{74)}\) The Union does not provide common guidelines on this point either. The Union instead merely provides a basic guideline, leaving details to Member States. In other words, there are fifteen internal frontiers in the Common Market. This means that the older the hypothetical person is, the harder it is to move to another Member State\(^\text{75)}\).

Another major issue is whether a worker is entitled to remain in the host country permanently when his/her contract expires. In principle, under Regulation 125/70, every worker is entitled to remain permanently in the state where they last worked, provided that s/he has worked and lived there for three years. In fact for a worker to be qualified to live permanently, some additional requirements must be met. The work s/he has done must be in the definition of 'work' laid down by the ECJ. S/he also must be registered in the country in accordance with the domestic law of that Member State. It is the Member State, not the Union, that determines eligibility. This means that each Member State has ample discretionary power to add additional criteria. Gunaydin\(^\text{76)}\) is a case in point.

Mr Gunaydin was permitted to enter Germany in April 1976. Thereafter he followed a number of courses of study during which he was granted a residence permit with restrictions of time and place. In 1982 he married a Turkish national and the couple had two children in November 1986. Mr Gunaydin was taken on by Siemens with a view to following a training course lasting several years, at the end of which he was to be transferred to Turkey. In January 1987, the German authorities granted him a temporary residence permit which was extended several times, with the last occasion on 5 July 1990. On 15 February


\(^{76)}\) Gunaydin and Others v Freistaat Bayern, 1998 1 CMLR 871
1990 he applied (after 24 years in Germany!) for a permanent residence permit, on the grounds that as a result of his career development, Germany had become his home. Despite the support of Siemens, the application for an extension of the residence permit was refused, although the employment authorities agreed to extend his work permit. The reasoning was that his work had been limited to participation in a training programme in a particular undertaking, so he had not been available in the 'general labour market' and had not been duly registered as belonging to the labour force of a Member State. The ECJ did not explain what the 'general labour force' is. If we apply the ratio of Levin, his work is likely to be in the definition of 'work'. The ECJ however, applied a narrow test to him. It may be concluded that the decision of Gunaydin is subject to criticism especially from the point of view of Levin. In simple terms, this means that three years work in-country experience, as a matter of Community law, should be a bridge to a permanent residence permit. In reality, a work permit no matter how long it is, is one thing and a permanent residence permit is quite another.

The other type of legally entitled worker is a refugee or asylum seeker. The number of asylum seekers and refugees has dramatically increased since the collapse of the Eastern Europe. So, the freedom of people cannot be fully understood without paying attention to the asylum policy of the Union.

It is appropriate at this stage to ask what the Community’s approach is to asylum policy: supranational, intergovernmental or both? I call it intergovernmental because each national Member State, rather than the Union, cooperates to attain the degree of integration. Any Member State can veto or even refuse to take part. The Union therefore has no exclusive power to control asylum policy.

Some examples are the Saarbrucken Agreement 1984 (between France and Germany) and the Schengen Agreement 1985 (among France, Germany and three Benelux Countries). Saarbrucken was not successful because the issue itself was thorny and sensitive. Other examples are the Dublin Convention77) on Asylum 1990 and the External Froniers

77) In force 1 September 1997; all 15 Member States are the signatories to this
Convention 1991. The Dublin Convention is designed essentially to prevent multiple or successive applications for asylum in the EU states, laying down as a principle that the decision on asylum should be made by the first country of application and that other signatories to the Convention need not be obliged to reassess identical applications once assessment procedures had been mutually recognised. This approach however did present some problems for Germany. Basic laws of Germany appear to demand that each application for asylum in Germany needs to be assessed in Germany simply because Germany has never agreed for the Union to take over the competence.

The Schengen Implementation Agreement 1990 is another example. Under the Agreement, the Schengen Information System (SIS) was established to cooperate and exchange information among Member States. In 1992, some Member States joined the Agreement: Italy, Spain, Portugal, and Greece. Taking all things together, all the major developments are accomplished by intergovernmental or bilateral approaches rather than supranational means. The Union has little power on this issue.

Finally, in connection with the issue of migrant workers or asylum seekers, the Swiss issue must be looked at. Under Directive 94/103(16), Switzerland agreed on the free movement of seasonal and frontier workers. Also, under 94/103(17), the social security scheme is portable for up to nine months for seasonal workers. It must be mentioned that this Directive does not apply to workers other than those who are seasonal and frontier. Therefore if a hypothetical person AA works anywhere other than the area of the frontier between Switzerland and Liechtenstein, the Directive does not apply. This means that Switzerland provides another stumbling block.

As a whole, I have demonstrated that the Union has again failed to provide a common basis for free movement for workers and asylum seekers. Why? There are two main reasons: sovereignty and strategy.
To grant a refugee status (or residence permit) is at the core of national sovereignty. Some people may argue that allegiance has been transferred to the Union by way of Union citizenship while others argue it has not. Therefore I am bound to look at the following section, on Union citizenship. Also, according to Philip\(^79\), around one quarter of the total number of EU asylum seekers arrive in Germany. So Germany wants to deal with it by bilateral negotiation, mainly by way of the Dublin Convention. This indicates that EU asylum policy is devoid of meaning, a mere slogan as the Union has no real power to control the Member States.

2.3 Social Europe

The Community Charter of Social Rights signed at Turin on 18 October 1961 (the Charter)\(^80\) contains various provisions, including health and safety, living and working conditions, equal treatment for men and women, employment and pay, social protection, persons with a disability, vocational training, labour market, protection of children, elderly people, information/consultation and participation of workers and association of workers.

Moreover, the Union by way ECJ decisions has upheld such fundamental rights as: human dignity (Casagrande, 1962 ECR 773), equal treatment (Klockner-Werke AG, 1962, ECR 655), non-discrimination (Defrenne, 1976 ECR 455), freedom of association, freedom of religion and confession (Prais, 1976 ECR 1589), privacy (National Panasonic, 1980 ECR 2033), medical secrecy (The Commission v Germany, 1992 ECR 2575), freedom of trade, freedom of industry, respect for family life (The Commission v Germany, 1989 ECR 1263), inviolability of residence and entitlement to an effective legal system (Johnston v Chief Constable of the Royal Ulster Constabulary, 1986 ECR 1651).\(^81\)

According to Article 8, every person holding the nationality of a Member State is a citizen of the Union. Nationality is defined according to the national laws of that Member State. Citizenship of the Union is complementary to national citizenship and comprises a number of rights and duties. The rights of the Union

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\(^80\) The Article 136 EC reads that "The Community and the Member States, having in mind fundamental social rights such as those set out in the European Social Charter signed at Turin on 18 October 1961 and in 1989 Community Charter of the Fundamental Social Rights of Workers, shall have as their objectives the promotion of employment, improved living and working conditions, so as to make possible their harmonisation while the improvement is being maintained, proper social protection, dialogue between management and labour, the development of human resources with a view to lasting high employment and the combating of exclusion."

"To this end the Community and the Member States shall implement measures which take account of the diverse forms of national practices, in particular in the field of contractual relations, and the need to maintain the competitiveness of the Community economy."

citizen include the right to move and reside freely; the right to vote and to stand as a candidate in an election to the EP under the Directive 94/80/EC; the right to diplomatic protection in the territory of a third country; and the right to petition, provided the petition is related to a matter which comes within the Union’s field of activity.

All these rights as a matter of principle must fall and be guaranteed in the Community competence rather than that of the Member States’ in order to fully attain the spirit of the Treaty and the SEM. Unfortunately, some of these rights are left to the competence of Member States. None of these rights are absolute and even the determination of who should or should not enjoy the status of Community citizenship is left to a national government which still draws upon its own rules of nationality. For instance, in order to protect their own sovereign interests, each Member State may stipulate that only their nationals are eligible to be elected to offices within the exclusive body of a basic local government unit.82)

Therefore the second major issue regards portable rights and whether they are guaranteed by the Union at the Union level. That is to say, whether the Union has competence in the social security benefit system. One of the key issues in social policy is sexual equality. The legal base for this policy is Article 141 EC 83). Under the legal base, the Commission has issued several Directives. Directive 97/80/EEC, 86/613/EEC and 76/207/EEC are all concerned with equal treatment between men and women as regarding access to employment, vocational training, promotion and working conditions. These Directives especially aim to protect women during pregnancy and motherhood.


82) Ibid., p. 61.
83) The Article 141 EC reads that "1. Each member State shall ensure that the principle of equal pay for male and female workers for equal work of equal value is applied."
86/213/EEC attempted to tackle the problem of women who were sidelined into low-paid occupations. This Directive has led to the abolition of the more obvious forms of sexual discrimination in matters of hiring and firing. For instance, in *Helen Marshall*, which involved an employee of a UK Regional Health Authority, the ECJ put an end to differential retirement ages for men and women.84)

Even though Article 141 is not wide enough to cover all aspects of equality, the ECJ tends to interpret it broadly. In *Defrenne v the Belgium State* a stewardess employed by Sabena challenged the differential pay and pension schemes operated by the airline in respect of its male and female employees. Although the Court ruled that Article 141 did not cover pension schemes, its 1976 judgment said that Article 141 had 'direct effect' in the area of equal pay. This means that so far as payment, not pension, is concerned, a Member State is automatically bound to observe the provision.

The paternity issue was also eventually agreed upon in November 1991. Since 1991, a woman and also a man can have paid leave when the wife falls pregnant. It was the first issue to be agreed under the protocol and as such was adopted automatically by the Commission and Council. The UK also agreed to it, including other Charter conditions in May 1997 when the Labour government took power.

It is important to remember that all these developments are due to the change of voting rules in the Council. Since SEA, the EU extends the use of the 'qualified majority' voting in the Council. Even though the Third Pillar, to which drug and asylum issues belong, in general requires unanimity, some matters of procedure are subject to Qualified Majority Voting (QMV) rule. Under such voting, each Member State has a block of votes depending on the Member State’s relative size and importance. France, Germany, Italy and the UK have ten votes each, Spain has eight, Belgium,

The Netherlands, Greece and Portugal have five each, Austria and Sweden have four each, Denmark Ireland and Finland have three each and Luxembourg has two. It takes fifty four votes out of the possible total of eighty seven for a proposal to be passed. 85) Table 2.3.1 shows this information succinctly.

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It is premature to conclude that there is no discrimination between sexes at all. Springer, in his article *The Social Dimension of 1992: Europe faces a New EC*, is correct in paying attention to the nature of women's jobs. Women in the EU most commonly work in the service sector. Indeed, around 70 percent find their jobs in this sector. Women are also most likely to work in feminised work places. They are bank tellers, nurses, teachers, and cleaners in hotels. They are unlikely to be bank managers, executives in private business, well-paid technicians or hotel managers. Women who work in industry tend to be concentrated in a few sectors which are less well-paid and more labour intensive, such as the clothing and textile industries. Women also fill a disproportionate number of part-time jobs. For instance, they provide 90 percent of the part-time work force in Germany. According to a report, as Table 2.3.2 shows, an average of 11.7 percent of working women are part-time workers. Also, women's pay is around 31 percent less than men's. Additionally, what women want and what society expects for them varies among the Member States. For instance, a French women employed in a bank has a much greater chance of reaching a managerial position than does her British counterpart. 86) Therefore it is fair

85) 1995 32 CML Rev. 898
to say that working women in the EC still have not achieved equality in pay or opportunity, despite laws requiring this. This is especially so because women who hold vulnerable jobs generally lack the skills and mobility for new jobs. They are frequently constrained by tradition and family responsibilities from taking advantage of the opportunities offered in the new market. The unemployment rate of men is 4.3 percent as of the year 2000 whereas that of women is over 10. 5.87)

Table 2.3.2
Share of Employees Working under Temporary Contracts in the Member States, 1988

<table>
<thead>
<tr>
<th>Country</th>
<th>10</th>
<th>20</th>
<th>30 (Percent of Employees)</th>
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In addition, it is necessary to consider the change of circumstances for women and their work in the SEA and TEU. With open borders and increased competition, weak firms will

Greenwood, USA, 1992., p. 66.
87) Female Unemployment rate,
http://www.europa.eu.int/comm/eurosta....roduct=3-t3110pc-en&mode=download
Long-term unemployment,
http://www.europa.eu.int/comm/eurosta....roduct=3-t3080pc-en&mode=download
With open borders and increased competition, weak firms will either go bankrupt or be taken over. All firms will face strong pressure to cut costs. Large firms will restructure. The entire EU economy will become more service and high technology dependent. All these changes will destabilize the labour market, especially for women. Job skills will be outmoded and new ones become required. Such demands for flexibility are serious for working people. At least for the immediate future, this scenario promises insecurity and disruption for some even though a skilled and mobile person will probably find increased opportunities. On the basis of the information above, certain tentative conclusions are possible. Women who work in many of the feminised work places in the EU will face a high probability of unemployment, as Springer argues.

Another issue arises as to regional disparity. It is necessary to ask to what extent the poor southern Member States would follow the guidelines of the EU mainly geared at the rich northern members particularly because this disparity is caused by regional unbalance. The Commission is well aware of this gap. Wise and Gibb argue that the Social Fund (SF) or the European Regional Development Fund (ERDF), together with the European Investment Bank (the EIB), can narrow these gaps.88) The ERDF is designed to promote regional development in less-favoured areas by allowing government intervention to mitigate what are seen as the adverse effects of free market forces. They are underpinned by a belief that it is unacceptable for people in poorer regions to lag too far behind others in terms of social and economic welfare. However it must be mentioned that, as discussed in the state aid section, the equal development between the north and the south is not a simple task, mainly because of the lack of finance. So, freedom of movement of people between the north and the south is hampered by unequal development89)

Another issue is health and safety in the workplace. Article 30 to 39 of the Euratom Treaty made extensive provisions for the protection of health and safety at work. Eventually, Article 100A and 118A of the SEA were passed, guaranteeing workers a high level of protection. In 1976 an agreement on a directive to protect workers exposed to vinyl chloride monomer. In 1979 the ‘Seveso Directive’ was agreed on which aimed to prevent major accidents in the chemical industry and related industries and to limit the effects if they did occur. In 1980, the Harmful Agents Directive was followed by related directives applying to specific harmful agents in the workplace, such as lead, asbestos and noise. Under Directive 89/654/EEC, the Union provided minimum safety and health requirements for the workplace. Directive 90/270/EEC deals with the minimum safety and health requirements for work with display screen equipment. Directive 90/641/EEC is on the operational protection of outside workers exposed to the risks of ionizing radiation during their activities. Directive 90/679/EEC is on the protection of workers from risks related to exposure to biological agents at work. Directive 92/29/EEC is on the minimum safety and health requirements for medical treatment on board vessels. Directive 92/104/EEC is on workers in the mineral extracting industries. Directive 94/33/EEC is on the protection of young people at work. Directive 99/38/EEC and Directive 90/394/EEC are on the protection of workers from the risks related to the exposure to carcinogens at work and extending it to mutagens.

One point attracts special reference. The single most important directive that the EU adopted is the Framework Directive, 80/1107/EEC. The Framework Directive, as it is known, establishes general principles for health and safety which must be incorporated into national law by December 31 1992. All subsequent EU directives for health and safety are based on the principles of the Framework Directive, and a list of topics to be covered by these directives is given in the annex of the directive. The directive applies to almost every type of workplace, public
or private, manufacturing or service.\textsuperscript{90)}

There are however some aspects of the directive still to be improved. One is that the reporting practice is not universally uniform within the Member countries. For instance, France and Germany include accidents occurring on the way to and from work in their total for work-related accidents while others do not. The figures reported to the EU show some differences which cast doubt on their validity. For example, the figures for persons killed in manufacturing indicate that Germany had the worst rate with 1,188 deaths. France was a distant second with only 409.\textsuperscript{91)}

Another minor issue regards wages. Under Directive 91/533/EEC every employer is obliged to inform employees of the conditions applicable to the contract or employment relationship, including working time. Every Member State is required to approximate municipal laws relating to this. At this stage, the critical issue is whether or how the Union determines the similarity of 'work' done by men and that done by women. That is to say, if a bank teller in a Member State is classified as a 'service', it should be the same in all other 14 Member States. However the Union does not or may not be able to do this. This means that the Equal Wage Directive lacks substance.

The third major point is the development of industrial democracy and better employment. The philosophical roots of industrial democracy can be found in nineteenth-century Europe, based on a general reaction against problems arising from the industrial revolution and excessive individualism. Certain social thinkers believed that a society should be bound together by mutual responsibility and obligation, and rejected the idea that wages form the only tie between owner and worker.

Most Member States therefore changed their primary target to greater employment because unemployment increased in the

period from the mid 1970s to early 1980s. The Social Action programme in 1974, set by the Paris Summit, is the response to this problem. The basic goal of the programme is better employment in the Community. Moreover, the European Social Fund provides the means to achieve the objectives of the European Employment Strategy: protecting and promoting employment and combating unemployment, discrimination and social exclusion. The European Employment Services (EURES) is another institute that promotes employment. The EURES is a European labour market network aimed at facilitating the mobility of workers in the European Economic Area. The European Works Council was established under Directive 94/45/EC to inform and consult employees. Some political interests groups underpinned these developments. Union of Industries of the EC (UNICE) and European Trade Union Confederation (ETUC) are those most prominent.

However, as Wise argues, the idea of industrial democracy and employment protection depends upon the actual power of labour unions in each Member State. The European Union does not provide any common guidelines. This means that, according to Gibb and Wise, if a labour union in Germany is more active than one in Spain, the employees in Germany are better protected than those of Spain. Therefore the critical issue at this stage is whether the labour union is guaranteed the same power by the Union. The answer is clearly 'no' because the labour union is under the control of each Member State.

Also, another difficulty arises due to the threshold of applying the Fifth Directive on Company Law (the Fifth Directive). The draft Fifth Directive was originally presented to the Council. It proposed that all companies with over 500 workers be required to establish two-tier boards, one supervisory, the other for day-to-day management of the enterprise which would involve representatives of the workers. In the face of stiff opposition

92) https://europa.eu.int/comm/dg05/empl&esf/index_en.htm
from the European Employers' Organization, UNICE, and from some Member States, the Commission took the proposal back and raised the threshold number of employees to 1,000. Nevertheless, these proposals remain unaccepted.94)

To summarise, there is no uniform law that guarantees the idea of employment protection and industrial democracy. Gibb and Wise pinpoint that all these developments are 'ad hoc' rather than institutional in nature. This is because, unlike theory, the percentage of incorporation of the directives into local law varies between the Member States. It is correct to say that there are a number of problems stemming from national governments' failure either to implement existing Community law or to enforce it properly. These result in barriers to trade. There is a strong belief that this is the most pressing problem. It is not surprising to conclude that there is no Common Market, in terms of industrial democracy and employment protection.

Finally the protection of workers is another key problem of the Common Market. Under Directive 77/187/EEC, a transfer or merger of business (or part of business) is not grounds for dismissal of workers. The transferee is obliged to observe the terms made between transferer and employee. Also, under Directive 98/59/EC each Member State is obliged to observe collective judicial and administrative rules on collective redundancies. However, it must be mentioned that the right of the employee is so vulnerable that the transferee may dismiss a worker on the ground of economic, technical or organizational reasons under Article 4(1) of the Directive.

The minimum wage is another aspect of Social Europe. The EC policy on this topic is rather limited. The primary objective has always been to remove the legal barriers of Member States which still impede the free movement of labour. The EU continues quite successfully to refine its measures to end legal barriers, but it hesitates to tackle more controversial problems such as the

difficulties arising from different social security systems or minimum wages. These difficult problems have been discussed, but remain too controversial to become the subject of a formal proposal. The EU will probably undertake more controversial measures to harmonise the differences between Member States.  

From these above discussions, I draw a number of conclusions. The Union is built on a two (some people argue, multi) - tier Europe. The rich northern Members are more ready to implement certain measures, whereas the poor southern Members are not. The Union therefore cannot enforce all measures because each Member has different views on the notion of the principle of subsidiarity. Different Member States have different interpretations of this principle. There is only a limited enforceability. The engine for integration of the Union, the SEM, is regarded as a trojan horse to a political Union but no one Member State wants to surrender its sovereign power. Each Member State may think that it would be better to be 'in' than 'out', in economic contexts. All these discussions can be resolved by a single stroke if the ECB is guaranteed an independent role, free from political intervention. However, there is a strong belief that the ECB is likely to be swayed by compromise of the national political interests of the big two. As a result, the idea of a 'Human Europe' has been painted only by politicians rather than economic power, the engine of integration in the Union.

As a whole, let me evaluate this chapter from a neofunctional point of view. The freedom of people in the individual dimension is to be escalated to the social dimension due to a spill-over effect. That is to say, the freedom of individual migrant workers is to be escalated to the freedom of movement of people in social dimensions, the idea of a social Europe. From the start, the freedom of people faced numerous barriers, so the spill-over effect is hardly recognised in this topic. If there were a common market in terms of the freedom of people, then neofunctionalism could see its success. However, the freedom of people is limited

95) Ibid., 114.
for various reasons.

It is important to consider this point: if a migrant worker, a lawyer in one Member country, is granted the move to another country, s/he clearly wants to have the freedom of movements of his/her profession as a lawyer. Therefore I am bound to look at the freedom of service in the following chapter.
Chapter 3. Freedom of Services

3.1 Freedom of (Legal) Service

The freedom of service includes two basic principles. On the one hand, a person or a firm should be guaranteed the right without discrimination to set up a branch. On the other, a person or a firm should be guaranteed the right without discrimination to offer their services across frontiers in other Member States while remaining in their country of origin. So, people in especially liberal professions, such as lawyers, bankers, or insurance companies are generally affected by the freedom of services. I therefore focus on banking, insurance and legal professions respectively.

European integration leads to the increasing mobility of lawyers, and even more frequently their clientelle. Clients coming from a foreign country are no longer exceptional cases. Many legal relationships are covered by more than one legal system because the legal profession crosses borders in the same way many other professions do. This growing internationalization of legal contacts stimulates the urge for a uniform legal language. This is not to say that EU citizens will all have to speak French, English, or German, but the legal notions they use should have the same content regardless of the legal systems they have. This clearly is the direction EU law needs to work on. In addition, the amount of EU legislation has increased enormously during the last decades. About 100 years ago it may have been possible for a lawyer to know all existing legislation, but these days there is no lawyer who knows the details of all statutes. This clearly indicates that harmonisation of the structure of all legislation and a good understanding of this structure by all lawyers will be of great importance for the SEM to build a single market in name and practice. I use the term 'legal service' not just for a service
provided by a lawyer, but also if the service is based on the Community-wide legislation.

Based on these understandings, I will focus on the fact that legal services with a lingual barrier cause a serious problem because many issues are interwoven. This section explores problems caused by the differences in legal systems, the differences of training/admission to a bar, and the combination of lingual/legal issues. I will then explain a problem caused by the lack of Community-wide legislation, especially in contract law. The absence of EU-wide common contract law provokes many hindrances in the SEM. The real question, however, is not whether the EU can legislate a common contract law, but why the EU can not do so. In order to answer these questions, I again begin by proposing that person AA who is a law graduate in country E goes to another country B to practice.

It would be logical to find out the Treaty base first. The right of establishment and the freedom to provide services is given by the Rome Treaty. S57(1) of the Treaty of Rome provides that "in order to make it easier for a person to take up and pursue activities as self-employed persons", the Council shall, "on a proposal from the Commission and in cooperation with the European Parliament, acting unanimously during the first stage and by a qualified majority thereafter, issue directives for the mutual recognition of diplomas, certificates and other evidence of formal qualifications." Again, s57(2) provides that "for the same purpose, the Council shall, before the end of the transitional period, acting on a proposal from the Commission and after consulting with the European Parliament, issue directives for the consideration of the provisions laid down by law, regulation or administrative action in the Member States concerning the taking up and pursuit of activities as a self-employed person".96)

Under these provisions, on 21 December 1988, the Council finally adopted Directive No.89/48/EEC on a general system for

the recognition of higher-education diplomas awarded on completion of professional education and training of at least 3 years duration. This is known as the ‘General System Directive’.

The first problem is caused by the fact that there is more than one legal system in the Union. There are two broad legal systems: the Common law system and the civil law system. The civil law system comprises the Roman law family and the German law family. There are therefore three major legal families in the EU: the Romanistic; the Germanic; and the Common law legal families.\(^\text{97}\) England and Ireland only belong to the Common law group whereas Belgium, Luxembourg and the Netherlands belong to the Romanistic group. Germany has the civil law system. The court structure of Scotland and Wales are different, but similar to that of England. Therefore, if person A is moving from a Common law country to a Roman law group or a Germanic group, S/he will find the differences enormous.

One of the biggest differences involves the training and admission of a lawyer to the bar. In Common law countries, the traditional barrister/solicitor distinction is present. In general, a barrister can plead before the most senior courts whereas only a solicitor can meet with clients and provide direct legal advice. Thus, in Common law countries, when a law graduate finishes his/her training course, s/he is required to choose one of them, while the other system does not require this.\(^\text{98}\) In Germany, however, there is no solicitor/barrister distinction. Legally speaking, all lawyers are entitled to plead before all the courts in Germany. The problem is therefore that if person A is admitted as a solicitor sole in country E, it is not confirmed yet whether A is entitled to practice in another Member State, and vice versa.

One might argue that, under the principle of mutual recognition of s57(2)(3) of the EEC, person A must be able to practice in

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\(^{98}\) The system in Scotland and Northern Ireland is different from that of England and Wales. For more information, see United Kingdom Legal System, [https://www.wwlia.org/uk-brief.htm](https://www.wwlia.org/uk-brief.htm)
another country B. Under the Directive,99) The EU does not provide for recognition of national 'diplomas' but each Member State shall recognise a 'career' for the purpose of pursuing activities as lawyers by way of provision of services, saying that any person holding the professional title has a certain amount of years of career. In so doing, where in a Member State the pursuit of the activities in question is subject to the possession of general, commercial knowledge and ability, that Member State must accept as sufficient evidence of such knowledge and ability that the activity in question has been previously carried on in another Member State. The period required is either two or three years, depending on whether it was completed in an employed or self-employed capacity and whether or not the relevant experience was preceded by a course of training.100) These questions are all difficult because the legal systems, training period, education period and even ethical standard are different between Member States. So, it would be fair to argue that in principle, the person, AA is entitled to provide service if A has met all the requirements stipulated by a host Member State in the EU.

Another question arises. If person AA has a degree/diploma in law but is not admitted to the bar in the home country, can A be admitted to the bar in another country where applicants are required to sit a special examination? Technically the answer is yes, but an applicant must obtain all requirements required by the host country. One clear example is Thieffry v Counsel de l'Ordre des Avocats a la cour de Paris.101) The plaintiff, a Belgian national, held a Belgian diploma in law which had been recognised by the University of Paris as equivalent to the French law degree. He had also gained the qualifying certificate for the profession of advocate, but on admission to the Paris Bar, was rejected because he did not hold the French diploma. The ECJ

101) 1977 ECR 776
held that, if a national of one Member State had had his/her qualification recognised as equivalent in the host Member State and had sat and passed the special qualifying examination of the profession in question, the act of demanding the national diploma prescribed by the host country’s legislation constituted a restriction incompatible with the freedom of establishment guaranteed by Article 52 of the EEC Treaty. Nevertheless it must be mentioned that it would be better to have a Union wide common guideline to the Common service Market.

However, one further point arises: whether a distinction should be made between academic equivalence, granted with a view to permitting further studies, and mutual recognition having 'civil effect', granted for the purpose of practising a profession. The ECJ did note that the distinction fell within the scope of the national laws of the different Member States. Thus it is for the competent authorities, taking account of the requirements of Community law, to judge whether a recognition granted by a university authority can also constitute valid evidence of a professional qualification conferring the right to practice. This means that there are no Community wide guidelines. Each Member State can effectively reject recognition by distinguishing Thieffry.\textsuperscript{102} There are then many potential technical barriers.

Nevertheless the General System Directive is well aware of the above points, attempting to cover loopholes where there are major differences in education and training, or in the structure of a profession. Article 4 of the Directive provides for a compensation mechanism: evidence of professional experience, an adaptation period or an aptitude test.\textsuperscript{103}

All of the above problems worsen when legal and lingual problems are added. As J A Usher notes, law and the problems of language seem to be synonymous, especially in the context of the European Union. The Union, as explained in 2.1, uses eleven working languages.\textsuperscript{104} The first question is whether those

\textsuperscript{102} Laslett, op. cit., 201
\textsuperscript{103} Laslett, op. cit., 32.
working languages are the court languages in the EU. The answer is yes. The ECJ and the European Court of First Instance (ECFI) allow all working languages to be used as languages of procedure. However, all judgments are automatically published in all languages. Even now there are entities created under EU law which do not allow all the languages mentioned above to be used for all purposes.

One clear example is the Office for Harmonisation in the Internal Market (Trade Marks and Designs), established under the EC Regulation on the Community Trade Mark. While an application for a Union trade mark may be filed in any of the eleven languages, if the applicant is using a non-office language, the applicant is required to indicate a second language which is an Office Language. The 'languages of the Office' are defined as English, French, German, Italian, and Spanish. Dutch, Danish, Greek, Portuguese, Finnish and Swedish are excluded from the languages of the Office. If the application is in another language, the Office may then write to the applicant in one of those second languages, and the applicant is required to accept it in opposition, revocation or invalidity proceeding. Simply speaking, if lawyer A is moving between the countries out of the Office language, the lawyer cannot represent clients, at least in the interests of trade mark and design.

This was challenged by a Dutch lawyer before the ECFI and on appeal to the ECJ, but the ECFI’s action was held inadmissible, and the appeal held unfounded. The substantive issue therefore is yet to be determined by the EU.

Sometimes a problem arises from translation mistakes. An example is provided in Unkel v Hauptzollant Hamburg Jonas. In Unkel, a question was asked by a German court, among other things, about the provision of a regulation governing export refund. (Commission Regulation 1041/67/EEC; OJ 1967 314/9) The English text provides that "the limit for claiming payment of

104) For more information, see 4.1 of this article or J A Usher 222.
the refund shall be six months". The German counterpart and other language versions however said that "the documents in support of the claim must be presented within six months". So the question revolved around what these documents were, a question nobody would have considered on the basis of the English text. The translator of the English version eventually inserted an embarrassing note to the effect that the English text of the regulation made no reference to the documents!106)

It does not matter whether a lawyer has a habitual residence in the country s/he is practising. This idea, of the freedom of legal service, was confirmed by Van Binsbergen v Bestuur Van De Bedrijfsvereniging voor de Metaalnijverheid. Van Binsbergen concerned a lawyer who provided legal service for Mr. Van Binsbergen on 30 November 1973. The lawyer, Mr. Kortman, was informed that he was no longer entitled to act as Mr. Van Binsbergen’s representative because, during the course of the proceeding, Mr. Kortman had transferred his habitual residence from Zeist, in Holland, to Neerloeteren, in Belgium. The lawyer brought an action against the decision. The ECJ held that the first paragraph of Article 59 and the third paragraph of Article 60 of the EEC must be interpreted as meaning that the national law of a Member State cannot, by imposing a requirement as to habitual residence within the Member State, deny service to a person established in another Member State. There is a right to provide services, where the provision of services is not subject to any special condition under the applicable national law. These two case laws therefore suggest that the insurance company X is entitled to provide services in country B, even without habitual residence.

I do not claim that an institution (as opposed to a person) does not have to have an establishment. For an institution to be able to provide a service, the institution should have an establishment in the host country with a licence granted by a home country.

The home country rule was established by two major case

106) Ibid., 223.
laws: Reyners and Van Binsbegen. Reyners v The Belgium State concerned a person born in Brussels of Dutch parents. The plaintiff, Reyners, had retained his Dutch nationality, although he had resided in Belgium, where he had been educated and made *docteur en droit belge* according to a diploma issued by the central selection committee on 23 July 1957 and confirmed on 13 September 1957. The issues of Reyners are 1) whether Articles 55 and 57 EEC, providing the freedom of establishment by foreign nationals excludes such professions as doctors; and 2) whether Article 52 of the Treaty of Rome, since the end of the transitional period, is directly applicable.

The ECJ held that the exception to the freedom of establishment provided for by the first paragraph of Article 55 must be restricted to those activities referred to in the Article 52. It is however not possible to give a description in the context of a profession such as that of avocat of activities such as consultation and legal assistance. Also, Article 52 of the Treaty is a directly applicable provision in a particular sphere of the directives prescribed by Article 57 of the Treaty. As a result, this indicates that a person A with A’s nationality (for instance Dutch citizenship) is entitled to market in another Member State B, for instance Belgium, because the idea of freedom of movement applies not only to people but also to a firm or company under Article 58(1)(2) EEC.

As a whole however, it matters whether A has a diploma issued by the country where s/he wants to practise; whether the host country has the same legal system/training course and admission procedure even though the General System Directive tries to cover some discrepancies (?). It may be an insurmountable barrier even if A’s mother tongue is the same as the language of the host country. (Dutch Lawyer’s case)

Let me consider the following that a lawyer is advising a person who is negotiating a contract between parties in different countries. Problems arise because there is no Union wide uniform law in private aspects. An important aspect of this is that of
private law because the legal service has limitations. This is due to the fact that there is no Union wide legislation. I do not claim that legislation needs to cover every aspect because of the proportionality principle. What I claim is that if there is a significant difference between Member States, the Union is required to enact uniform legislation to cover all Member States. A clear example is the law of contract.

According to J Basedow and Dunnet, private law, especially the law of contract, is an essential and constitutive element of the SEM. There are four main reasons why the EU is in need of a Union wide contract law. First, the economy is so developed and traditional contract law is not wide enough to cover all types of transaction in the EU. Second, the traditional definition of offer and acceptance becomes vague partly because a computer is involved in the commercial transaction and partly because the Member States' understanding on matters of law are different. 107) Third, some scholars find that contract law plays an important role in the underpinning of long-term, cooperative relationships between the Member States. 108) Finally, as of 1 January 1999, the EU went to its third stage of monetary Union; the ECU became a formal single currency governed by a common set of interest rates set by the European Central Bank.

The Commission, aware of this situation, proposed the 'Principles of European Contract Law" through the "Commission on European Contract Law" in 1995. 109) The Commission tries to cover differences as a matter of law with regard to offer, acceptance, performance and remedies in the contract, especially in cross-border transaction. I will show a couple of examples of differences between the Member States. One difference is over very basic terminology of offer and acceptance in contract law in the EU. In all legal systems, codified or not, the rules on the

formation of contracts stem from offer and acceptance. However, there is nothing at all covering this in the French Civil Code. A more recent code merely gives the impression that offer and acceptance is the only way a contract can come about.\textsuperscript{110}

In addition, the Member States have not agreed on the term 'offer', especially as to when the offer is made. For instance, Courts in France hold that where someone has advertised goods for sale in a newspaper with a price, a contract is formed with the first person to fulfill the conditions of offer unless s/he lacks a particular capacity. Normally however, this is treated as an 'invitation to treat'. If it is treated on the one hand as an invitation to treat, the contract is not complete when someone expresses his/her intention to buy at the marked price, but in France the shopkeeper is bound to sell the item when someone expresses his/her intention to buy the item at the marked price, because the moment someone expresses his/her intention, it is to be treated as an acceptance. Again in France, it is treated as illegitimate to revoke an offer whereas it is not in other countries. Moreover, as the economy and computer skills develop, agency becomes indispensable in contract law. However, Roman law has no general concept of agency or representation, which involves one person acting for another, while other law families do.\textsuperscript{111}

It would then be logical to ask whether the Council or European Parliament has adopted the proposal proposed by the Commission in 1995. If not, why? Even though there are many calls for EU wide contract law from various scholars, the Union has not adopted such yet. There are two main reasons for this.

First, there is an 'assurance' argument. The Community wide common contract law has not been adopted mainly because all of the entangled issues surrounding single European currency are not resolved yet. In fact, there are provisions under national laws


\textsuperscript{111} Ibid., 218.
of obligations which allow, under certain circumstances, one party to demand either not to be bound any more, or to have certain terms of the contracts modified. These provisions are a response to the introduction of the single currency in 1999. Responding to these concerns, the Commission's Green Paper, and the Presidency Conclusions of the Madrid European Council of 15 and 16 December, clearly confirmed that "the substitution of the euro for national currencies should not of itself alter the continuity of contracts" and "... in the case of fixed interest rate securities and loans, this substitution will not of itself alter the nominal interest rate payable by the debtor, unless otherwise provided in the contract." However it has to be recognised that markets seem to look for further explicit reassurances.

Another reason involves the principle of subsidiarity under Article 3b TEU. As I repeatedly mention, since the adoption of the Maastricht Treaty in 1992, Community action must follow the principle of subsidiarity. The first question raised in this context is whether the harmonisation of contract law as a measure proposed for the establishment of the internal market would fall within the exclusive competence of the Community. Even though some scholars argue that the Community has an exclusive competence for all actions which purport to establish the internal market, others, including Basedow, note that "it is indeed difficult to understand why the Community should have an exclusive competence for the harmonisation of contract law."

A second point regards the tests of comparative efficiency. It does not relate to certain areas of the law, such as the law of contract, but to the 'objective of the proposed action'. In other words, it would be up to the legislators to check whether the objective could be better achieved by the Member States or the Community. There is no fixed answer. On the one hand it is clear that a single Member State cannot bring about European uniformity by its own laws, but on the other, the traditional way

113) Basedow, op. cit., 1130.
of making uniform law, i.e. the adoption of international
convention, does not seem to be a suitable alternative because it
is a highly unreliable instrument for bringing about uniformity
within a reasonable timespan.\textsuperscript{114}

As a whole, I have identified that the idea of freedom of legal
service is limited for four main reasons. First, the legal systems
are different. Lawyers' training and admission is not uniform.
Second, language again poses an insurmountable barrier to legal
services (the message of the Dutch lawyer's case). Third, the
fact that there is no EU wide contract law causes another
difficulty in the area of legal services. Finally, all these issues
are interwoven with each other. They interact to cause more
difficulties. The freedom of services therefore has a long way to
go. Moreover, it is clear with regards to that a Common Market
does not exist in the Union, the freedom of service and freedom
of establishment context.

\textsuperscript{114} Ibid., 1127.
3.2 Insurance Services

Under Article 49 - of the EEC Treaty, the right to provide services is guaranteed. A cross-border insurance market has been a reality since 1993. In principle, then an insurance company approved in one Member State may market its policies in all other Member States. The problem is that one Member State, as far as some supervisory regime is concerned, may have different regulation from others. For instance, Germany has stricter regulations and policies than the UK. Thus, the actual questions governing this section are 1) whether there is an EU-wide rule with regard to authorisation, supervision and solvency; and 2) whether the Community has the power to harmonise different national regulations.

For the sake of convenience, I again propose that person AA, who insures himself, his car, and camera with an insurance company X in his/her country of origin (O), is moving to another Member State, host country (B). While moving, if the person A has a car accident in country B, a problem arises as to whether he is able to claim his insurance policy in the host country or in the country of origin. For him/her to claim in the host country, the real issue is that the insurance company X should have freedom to move to another member states across the border. To determine this, it is necessary to distinguish between life and non-life insurance.

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115) Article 49 reads that "within the framework of the provisions set out below, restrictions on freedom to provide services within the Community shall be prohibited in respect of nationals of Member States who are established in a State of the Community other than that of the person for whom the services are intended."

"The Council may, acting by a qualified majority voting on proposal from the Commission, extend the provisions of the Chapter to nationals of a third country who provide services and who are established within the Community."

Article 50 reads that "services shall in particular include:

a) activities of an industrial character;
b) activities of a commercial character;
c) activities of a craftsman;
d) and activities of the professions.

Article 54 reads that "As long as restrictions on freedom to provide services have not been abolished, each Member State shall apply such restrictions without distinction on grounds of nationality or residence to all persons providing services."

For more information, see Consolidated Version of the Treaty Establishing the European Community (EC Treaty).
It is logical to look at the development of the insurance sector by way of the Directives first. With regard to non-life insurance, in 1964 under Directive 64/225/EEC\(^{116}\) the Council tried to abolish restrictions on freedom of establishment and freedom to provide services in reinsurance and retrocession. In 1973, the Directive 73/239/EEC (the First Non-life Directive)\(^{117}\) established 'home country rule'. This means that the home country rather than the host country is in charge of the insurance company, in respect to taking up and the pursuit of business in this sector.\(^{118}\)

The Second Non-life Directive, 88/357/EEC,\(^{119}\) made further development and set provisions to facilitate the effective exercise of freedom to provide services. Especially where motor vehicles are concerned, it is in 1990 Directive (90/232/EEC)\(^{120}\), that avail itself the coverage, including civil liabilities resulting from car accidents. Finally in the third Non-life Directive 92/49/EEC\(^{121}\), home rule in principle was extended to the withdrawal of licences. Therefore, home country rule is, in principle, the rule of law in the Common Market.

Alternatively, with regard to life-insurance, it was in 1979 with the First Life-insurance Directive 79/267/EEC\(^{122}\) that home country rule, in principle, was established with some derogations. In 1992, the Third-life Insurance Directive 92/96/EEC\(^{123}\) made further developments on the home country rule. So, in principle, taking up life insurance and cancellation, in principle, of a business is a domain of the home country. Home country rule


provides that, in connection with my hypothetical situation, the country of origin AA is in charge of granting, supervising and canceling the licence of an insurance company, X. Some issues arise from an examination of the Treaty provisions and Directives.

The main issue is the extent to which home rule is applied. As far as non-life insurance is concerned, the rule includes such points as grant (Article 6 Non-Life Directive), financial supervision (Article 9 Third Non-Life Insurance Directive), and technical reserves requirements\(^{124}\) (Article 13 Third Non-life Directive) of the license. Cancellation of the licence is, in principle, up to the home country under Article 14 of the Third Non-life Directive, but in fact the host country may exercise the power of control under Article 6(3) Third Non-life Insurance.\(^ {125}\)

On the other hand, as far as life-insurance is concerned, home rule extends to establishment (Article 7 of the Third Life Directive), financial supervision (Article 9 of the Third Life Directive) and technical reserves required under the licence (Article 18 Third Life Directive). As in non-life insurance, cancellation is technically excluded under Article 6(3) Third Non-Life Directive.\(^ {126}\) Also, the host country may require information written in its own language under Article 38 Third-Life Directive. The host country, in addition, can exercise control by way of an 'on the spot' verification system under Article 8 of the Third Life Directive.\(^ {127}\)

Another question is, from the Union's point of view, whether some Member States apply stricter rules or conditions to the

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124) A host country may require an insurance undertaking to cover their technical provisions required under Article 21 of the Third Non-life Directive.
126) Article 14 (Third non-life Directive) provides that authorization granted to an insurance undertaking by the competent authority of its home member states ..... On the other hand, Article 6(3) (Third non-life Directive) reads that "nothing in this section shall prevent Member States from maintaining in force or introducing laws, regulations or administrative provisions ... for the normal exercise of supervision. These two provisions seem to be inconsistent. Therefore it may be argued that home rule, in terms of cancellation of a licence, is subject to host country rule, and vice versa.
company X. As a matter of fact, the 15 Member States do not apply the same conditions even though the Union provides the basic guideline of home rule. One example is *Germany v the Commission*. In 1986, the Commission took a test case against Germany to the Court of Justice. The key issue was the extent to which a country was permitted to impose authorisation and other regulatory requirements on insurance companies based in another Member State and wishing to offer cross-border services. The ECJ found that insurance was a particularly sensitive area from the point of view of the protection of the consumer, so in the field of insurance, there existed compelling reasons relating to the public interest that might justify restrictions on the freedom to provide services.\(^{128}\)

Another question is whether a host country is entitled to "require for the insurance company X to have establishment in the host country". As far as non-life insurance is concerned, under Article 32 of the Third Non-life Directive, a host country may require an establishment of a branch to have a licence granted by a country of origin in a host country. Also, in regard to life insurance, a host country may require an establishment of a branch under Article 32 of the Life Directive, even though the host country may not require a prior approval under Article 29 of the Third Life Directive.\(^{129}\) This means that all fifteen Member States may provide different establishment requirements which would not have been the case if the Union had competence.

Let us revisit the travelling person AA who lost his camera and had a car accident. The camera is easily covered under insurance. There is no issue in relation to the camera, meaning that the freedom to provide service in contents insurance is available with no substantial barrier in the Common Market. A major emphasis is focused on the car and whether the car is covered when the person has an accident in a foreign country. This turns to the issue of whether the insurance company has

\(^{128}\) *The Commission of the EC v Federal Republic of Germany*, ECR 1986, 3755

Similar cases were taken against Denmark, France, and Ireland.

\(^{129}\) op. cit., Article 29.
the freedom to establish and provide a service in all Member States. Since 1990, car insurance has been available in foreign countries. A motor vehicle used to be excluded from non-life insurance. It was in the Motor Vehicle Directive 90/232/EEC\(^{130}\) that the Union harmonised laws of the Member States relating to insurance against civil liability in respect to the use of motor vehicle. However, it must be mentioned that the Directive contains one problem: disputes settlement. Under Article 4 of the Directive, a host country may decide which insurer must compensate the victim if disputes arise. The essence of this problem is that the Union has no dispute resolution mechanism available to all Member States. This means that the end result of a car accident may be different, depending upon which jurisdiction the person belongs.

It is understandable, if a legal dispute arises for the injured party to want the damages and legal action fee covered under their insurance policy. So the insurance issue is clearly associated with freedom of legal service. The real issue at this stage is therefore whether legal expense accompanies the insurance policy. The Directive 87/344/EEC (the legal expense Directive)\(^{131}\) provides that costs in relation to the payment of the premium bear the cost of legal proceedings and to provide other services directly linked to insurance are covered. However, this Directive has an important loophole. If a legal defence is carried out in a Member State other than the one in which the insured person normally 'resides', this Directive is not applied under Article 2 of the Directive. That is to say, if the hypothetical person, from Germany for instance, has a car accident while travelling in France, the person is likely to bring an action in the French court, and is highly likely to employ a French-speaking lawyer. If this is the case, the person may not be covered because the lawyer is not from the country of his 'normal residence'.

\(^{130}\) EUR-LEX, Directory of Community Legislation in Force: Dir. 90/232/EEC  

\(^{131}\) EUR-LEX, Directory of Community Legislation in Force: Dir. 87/344/EEC  
clearly indicates that the issue of legal expense insurance is again associated with language and freedom of people. The Union is therefore in urgent need of a common guideline in this sector.

Arguably one of the most important issues is whether the hypothetical person is covered under any Directive when s/he has an accident. This may be answered mainly by reference to Articles 2 to 4 of the First Life Directive. These Articles provide exceptions to life insurance portability. The conclusive answer depends upon what sort of policy the person has. As an example, if the hypothetical person is injured with a policy covering only in case of death, he may not be covered under Article 3(1) of the First Life Directive. Also, some activities may not be covered under Article 4 of the First Life Directive because the Article expressly allows some derogations under national law. This is critical because it is somewhat unreasonable to argue that there exists a Common Market with such a limited freedom of services.

In relation to the life directives, if the person AA has a genetic problem the question is whether an insurance company is entitled to ask about this. Does this conflict with the right of privacy? Is the Community entitled to enforce the insurance company not to have the person A tested for a genetic predisposition? The argument surrounding this issue is open. On the one hand, there is an argument for the respect of privacy, while on the other, there is an argument for insurers. The real issue is not whether the insurance company is entitled to force the person A to be tested but whether existing information is to be disclosed or not. Sandberg proposes the Dutch solution as the most attractive. The Dutch Committee for Insurance made an ethical proposal that insurance companies be prohibited from demanding unlimited disclosure.132) This argument indicates that the Union has not decided between Union Directives and the Treaty provisions.

Some fundamental questions, however, still arise. One of the main disputes between Member States is on accounting of

insurers' investment. The crux of the problem is that there are no EU-wide guidelines or principles. Under the 4th Company Law Directive, companies incorporated in the Community can account for their assets on a historical basis or on the basis of market valuation. The Commission, with the backing of the UK, Ireland and The Netherlands, argue that insurance, including that of banks, should be required to account for investment on the basis of a market valuation, because this would give the public a truer picture of the financial health of the company concerned. Germany, however, counter-argues that it would lead to discrimination if the insurance industry is the only sector faced with this accounting requirement.133) So the accounting system is again fragmented in the Common Market.

Moreover, the problem worsens when the internal insurance market is confronted with taxation. Basically, two rules exist with regard to taxation on insurance. On the one hand, every non-life insurance contract is subject exclusively to the tax system of the Member States in which the risk is situated. On the other hand, every life insurance contract is subject to the country of origin, which may be different from the country where the risk is situated. This means that life insurance, compared to non-life insurance, has less mobility because the person A may be covered when, and only when, s/he resides in his/her habitual residential country. Overall, as Ottow and Swann argue, the completion of the internal insurance market is not yet in sight.134)

The subsequent question should be whether the home country rule is absolute. Unfortunately home country rule is subject to host country's technical control. As I mentioned earlier, the granting of a licence and technical reserves are under the home country's control whereas cancellation is not. As an example, Article 6(3) of the Third Non-life Directive provides, "nothing shall prevent Member States from maintaining in force, or introducing laws, regulations or administrative provisions

requiring the approval of the memorandum and articles of association and the communication of any other documents necessary for the normal exercise of supervision." This means that every host country has some leeway to exercise the power of control. Therefore the real problem is that all 15 Member States, in principle, are entitled to licence to provide services but, at the same time, all fifteen Member States are allowed to take measures to control the freedom of services.

I therefore ask whether the Union provides any common rules applicable to all fifteen Member States. The answer is negative. The Union has only made a compromise of all fifteen national interests. The end result of an accident may be different depending upon the country in which the hypothetical person has a normal residence. A clear indicator of this is that the Commission is of the opinion that it is "necessary to grant derogations in the UK (1996 to 1998) and Greece (1996 to 1998) concerning insurance services" under the Commission Regulation No 1226/1999.135)

Alternatively, the Commission may want to control nationalistic insurance markets by applying competition rules under Article 84–94 EEC. This, however, has proven an unusable card until the year 2003. In 1993 the Commission adopted a 'block exemption' expiring in 2003. The focus of block exemption is that the Commission excludes the insurance sector from competition rule. At this stage therefore the real question is whether the Commission is entitled to extend the block exemption and whether the Member States are agreeable to it. This issue is left to the interpretation of the subsidiarity principle, which itself is subject to interpretation, as I explained in 3.1. This argument is truly open. This means that the Commission is not fully guaranteed to extend over the year 2003.136)

Finally, the Switzerland issue causes concerns in the insurance

market in the Union. Again, let me propose a hypothetical situation. If a person has a car accident, causing the person serious injury and a camera to be stolen, are the car and the person covered? Simply speaking, both of them are not necessarily, while the camera is. This means that the Motor Vehicle Directive cannot be enforced in Switzerland. The two parties (Switzerland and the Union) have not agreed on life insurance policy under the agreement on Direct Insurance, other than Life Insurance. According to Article 1(A), a motor vehicle is excluded from the insurance policy "unless the vehicle is registered in Switzerland under the law of Switzerland." Life insurance is also basically excluded. This means that the European insurance market is fragmented. There is no common rule applicable to all Member States.

As a whole, I have identified that the European insurance market is divided into fifteen pieces. The Common Market has compromised all the nationalistic interests under the guise of 'home rule', which is devoid of meaning because home rule is not a common European rule. The Commission may be able to argue that it has the jurisdiction to give more incentive for the Common Market to be fully established after year 2003. However this option is subject to the rule of subsidiarity, which is fluid and vague. I am therefore bound to conclude that the common non-life insurance market is far from our vision of a common market, let alone the life-insurance market.

3.3 Banking Services

The term 'bank' includes such institutions as banks, enterprises engaging in financial brokerage and securities, and institutions that publicly take deposits. According to the Cecchini Report, financial services (mostly bank and insurance company related) account for 7 percent of Union GDP. More importantly though the financial sector can produce up to half of the overall benefits to be derived from the completion of the Common Market. Therefore it appears important to look at this sector in depth.

As far as banking is concerned, Articles 49-55\textsuperscript{138}) of the EC Treaty are the prime provisions. This sector has traditionally been subject to strong governmental supervision, resulting in extremely stringent regulation of access to the banking profession and its exercise, and rules that vary from one Member State to another. Hence major efforts have been made to bring these divergent rules into line and secure their mutual recognition so as to enable the freedom of capital and services to be fully exercised.

The Commission has issued several directives in order to accomplish the freedom of services in the banking industry. The initial effort was made through the Directive 77/780 EEC. The Directive established the principle that a credit institution may be established or obtain authorisation provided that certain conditions are met. The following Directive 89/646 established the principle of single Community authorisation. This means that if one credit institution is granted authorisation by a Member State, the institution is allowed to pursue all basic banking business throughout the Community, either by setting up a subsidiary or by providing its services directly from the country in which it was established. Under Directive 89/299 EEC, as amended by Directive 91/633 EEC, the Union laid down common basic rules for all credit institutions authorised in the Community. In

\textsuperscript{138}) For more information, see 3.2 Insurance Service in this thesis.
addition, Council Directive 89/647 EEC, 91/15 EEC, 94/7 EEC and 95/15 EEC harmonised and tightened up solvency standards to protect depositors and investors. In 1994, the EP and the Council created Directive 94/19 EEC with the aim of providing Community-wide protection for depositors in credit institutions, this was aided particularly by making guarantee schemes set up in one Member State applicable to depositors in subsidiaries set up in another. Finally, the Council Directive 91/308 EEC requires Member States to prohibit money laundering and introduce appropriate penalties for such offences.

For the sake of conveniency, let me again suppose that one hypothetical institution AA in country A is considering setting up a branch or subsidiary in another Member State, B. The first issue asks whose jurisdiction is applied, A's or B's, when services are sold across the frontier. That is to say, is it the home country or host country that is to be in charge of the establishment of a bank? Does the Community have a common rule applicable to all credit institutions with respect to this issue?

It is the home country that is, in principle, in charge of banking in general in the EU. The host country has been required to apply the 'home' rule since the ruling of Cassis. Home rule is applied to such matters as authorisation, financial supervision, reorganisation and the winding up of a company. The Commission has held the position that it should be possible to facilitate the exchange of such financial products at a Community level, using a minimal coordination of rules as the basis for mutual recognition by Member States.

Home country rule was established in the First Banking Directive 77/780 (First Directive) in 1977[139]. This Directive warrants analysis in depth. It concerns mainly the establishment of branches within the EU, and setting up licence requirements for credit institutions to operate in a Member State. Under the First Directive, once a credit institution is licensed in one

Member State, the credit institution, in theory, is allowed to set up another branch in another Member State. However, it is not automatically entitled to do this. A branch in a foreign country may be required to have the initial capital in order to obtain a licence. In this way, the First Directive paved the way for freedom of establishment, but it cannot be argued that the Directive removed all obstacles.

The Second Banking Directive 89/646/EEC\(^{140}\) (the Second Directive) complements the First Directive, and does not substitute for home country rule. However, the Second Directive is a landmark directive because it established some fundamental principles. Under the Second Directive, the EU Member States had to bring their national laws into conformity with the provisions of the Second Directive by 1 January 1993. In particular, the Second Directive aims to 1) remove the barriers to establishment and the right to provide service, 2) harmonise license and supervision requirements through mutual recognition and 3) increase cooperation between bank supervision authorities of the Member States. In regards to these developments, a credit institution in one Member State is entitled to set up a branch in any of the other Member States in the EU.

However, as Davidson rightly points out, there are some exceptions to the freedom of services on various grounds. He, in general terms, argues that because of the political sensitivity involved in capital movements, it may be justifiable for a Member State to take protective measures to prevent disturbances in authorisation. Member States also retain some powers for the sake of the national economy, such as regulation of the short-term economic cycle (Article 103), protection of the balance of payments (Article 104, 108 and 109), the exchange rate (Article 107) and public health and public safety (Article 55 EEC).\(^{141}\) I will explain why home rule is not fully established.

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\(^{141}\) S. Davidson, in J. Lodge, op. cit., p. 125
The principle of home country regulation, which is the basis of the Second Directive, is not absolute in one aspect. The home country rule co-exists with the host country rule. Let's assume that a competent authority of the host Member State ascertains that an institution having a branch or providing services in its territory is not complying with the legal provisions in force, say consumer protection for instance, in the Member State. It is the host country, rather than home country, that shall request that the institution concerned put an end to the irregular situation under Article 19(3) EEC. The ultimate sanction for failure to comply is the suspension of all activities. There is leeway for a host country to have a problem, concerning the interpretation of the provision. Consequently, home country rules have to coexist with host country rules on the grounds of consumer protection, as there are no Community guidelines.142)

Let me go on to ask about external relations with regard to banking. The Common Market is clearly known to have the goal of a frontier-free market. However, this may be possible only between the Member States. The Common Market is, in fact, seen as a fortress market by non-EU Members. The SEM is not henceforce an open market but a blockade in relation to countries outside Europe. Therefore this sometimes functions as a barrier to enlarging the Common Market. It is true that the Union's basic and fundamental principle, in relation to non-EU Members, is the reciprocity rule. Given that the reciprocity rule is one of the basic principles, the problem is that there is no universal definition of the principle widely accepted in domestic or international agreements.143) As a result, and as the Commission recognises, the EU has been repeatedly accused of protectionist policies by non-EU Members.

This protectionist policy also invites protectionism from non-EU countries. Switzerland is a clear example. The Swiss Banking Act is considered to conform with the uniform licensing

142) D. Llewellyn, op. cit., p. 130
143) Dakolias, op. cit., p. 76
principle of the Second Banking Directive. However, a foreign bank in Switzerland is not allowed to use a name which indicates the Swiss character of the institution. It must use a commercial name that does not indicate a Swiss character and must supply a declaration to the Swiss National Bank to the effect that the applicant has committed itself the Swiss National Bank to comply with its directives in respect to the protection of Swiss credit and monetary policy. Also, there is a minimal capital for a bank, SFrs. 2,000,000. In simple terms, the Common Market is trapped between the frontier-free market of service and enlargement.

Switzerland may again be a source of concern in relation to data flows between branches in other Member States. Let me suppose that there is a multinational bank operating in three different countries, including Switzerland. The question then arises over whether the multinational bank is allowed to transmit data on its customers between its branches in another country. Legally speaking, it is permitted under the Data Protection Directive, for one branch to transmit its data to another branch in another Member State. However if the data transmission is between branches, with Switzerland on one side, the bank must have unambiguous consent from its customers because the Common Market can not force Switzerland to comply with the Directive. Therefore it is fair to conclude that there is not one Common Market in the Community, given that Switzerland is ‘in’ the Common Market in geographical terms.

In addition, it is necessary to consider whether the Union has the power to regulate the deposit rate of a bank. That is to say, which authority, Member State or the Community, is authorised to regulate the deposit rate. The argument is open. On the one hand, Chiappori argues that economic and financial movements

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144) Michel Haymann, op. cit., p. 86
cannot be politically regulated. Each Member State retains the power to regulate the economic aspects. On the other hand, McKenzie and Khalidi argue that the financial markets are now global and no longer have a significant geographical element. The optimal supervisory body should be international in order to minimise the possibility of competitive distortions arising from different national interpretations. In the end, this problem turns to the issue of subsidiarity under Article 3b.

The subsidiarity rule has been a fundamental principle in the process of forming the Community. The legal bases of this principle are Article A1 TEU and 3b Maastricht Treaty. There has been much discussion on the different interpretations of this principle. One way of understanding the root of the differences is to look at the ideological and historical aspects of the principle. It is commonly accepted that the British Conservative Party, concerned about national sovereignty, has affected the interpretation of the principle. For instance, a Jean Monnet Paper argues that the British view is reflected in the wording of Article 3b because the Article refers only to "the exercise of power on the part of the Community institutions or the Member States" rather than on the part of the citizen. Another version of this principle appears to reflect Christian Democratic philosophy, judging from the wording "as closely as possible to the citizen". Therefore it can be argued that there is a consensus that the concept is "highly fluid and vague". To make things more complex, it must be mentioned that the ECJ did not have interpretative power over this issue until the Community passed the Treaty of Amsterdam.

The argument as to whether the Union is authorised to regulate interest rates is open-ended. On the one hand, the Union may argue that it has the power to set, under the general guidance of

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147) The Jean Monnet Chair, Reapprasing Subsidiarity's Significance after Amsterdam, Harvard Law School Jean Monnet Chair: http://www.law.harvard.edu/programs/jeanmonnet/papers/99/990702.html, p. 4
148) Ibid., p. 2.
149) Ibid., p. 4.
the ECB, the interest rates because it is the body that can better protect the interest of the citizen. Alternatively though, it may be argued that "people are less mobile than money, goods, or ideas in a sense that they remain 'nationalised' dependent upon border control" and that EU Member States remain the crucial focus of economic accountability for their citizens, even though a number of relatively successful sectoral transnational networks have been established.

All we can conclude is that there is much uncertainty and that some directives were and may be challenged on the ground of the subsidiarity rule. An example of this type of association of problems is Austria's problem with the Council Directive of 10 June 1991 on the Prevention of the Use of the Financial System for the Purpose of Money Laundering and Austrian Constitutional Law. The 1991 Directive requires Member States to ensure that banks check the identification of their customers by means of supporting evidence. In Austria, however, the anonymity of the bank account is guaranteed by Constitutional law. Thus the Union has no grounds to punish Austria because Austria relies on a 'voluntary' commitment of the banks. As a result, it may be concluded that Community competence is not respected on the grounds of the inappropriateness of the level of decision making.

A final point of contention arises from concerns expressed by many regarding the security of their accounts in foreign banks. Therefore, with regard to Directive 94/19, a point regarding the deposit guarantee scheme warrants mention. Under the Directive, depositors are guaranteed a minimum level of protection against undesirable outcomes of asset allocation decisions taken by bank managers who, by virtue of their monopoly of information concerning the bank's portfolio, have greater power than the depositor. Unfortunately the Directive contains loopholes. First,

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150) Ibid., p. 4.
151) Ibid., p. 10.

For examples of such challenges to the Community competence, see Germany v Commission 1987 ECR 3203, and Germany v Parliament and Council (challenges to the tobacco advertising Directive), and Una Film v Parliament and Council.
the Directive does not require compulsory membership, mainly a result of the subsidiarity principle. Germany, Italy and Portugal remain voluntary members. Second, some countries do not provide a protection scheme against deposits made in foreign branches of domestic banks. France, Luxembourg, the Netherlands, Portugal and Spain are such countries. Third, some countries do not provide protection against deposits made in foreign currencies. Belgium, France and the UK are included in this category. Finally, a great disparity exists between Member States in terms of the amount of the compensation, varying from Finland, being unlimited to Denmark being DKR (local currency) 250,000 (about 32,155 ECU). This means that not all account holders in Denmark will be compensated if banks go bankrupt. So, it may be argued that the insurance scheme is devoid of meaning. Many people are not fully relieved from security concerns of their foreign account. Table 3.3.1 demonstrates this.

<table>
<thead>
<tr>
<th>Country</th>
<th>Maximum compensation limit</th>
<th>Deposits in foreign currency</th>
<th>Deposits in foreign branch of foreign banks</th>
<th>Deposits in foreign branch of domestic banks</th>
<th>Public or Private scheme</th>
<th>Member compulsory or voluntary</th>
</tr>
</thead>
<tbody>
<tr>
<td>Belgium</td>
<td>BF 500,000</td>
<td>No</td>
<td>Yes</td>
<td>Yes</td>
<td>Private</td>
<td>Compulsory</td>
</tr>
<tr>
<td>Denmark</td>
<td>DKK 250,000</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Public</td>
<td>Compulsory</td>
</tr>
<tr>
<td>France</td>
<td>FF 400,000</td>
<td>No</td>
<td>Yes</td>
<td>No</td>
<td>Private</td>
<td>Compulsory</td>
</tr>
<tr>
<td>Germany</td>
<td>30% of bank’s own funds</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Private</td>
<td>Voluntary</td>
</tr>
<tr>
<td>Ireland</td>
<td>&lt; £5,000 - 80%</td>
<td>No</td>
<td>Yes</td>
<td>No</td>
<td>Public</td>
<td>Compulsory</td>
</tr>
<tr>
<td></td>
<td>5,000 to 10,000 70%</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>10,000 to 15,000 50%</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>maximum 10,000</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Italy</td>
<td>&lt; 200M: 100%</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Private</td>
<td>Voluntary</td>
</tr>
<tr>
<td></td>
<td>200M to 1B: 75%</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>maximum 800M Lira</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Luxembourg</td>
<td>LF 500,000</td>
<td>Yes</td>
<td>Yes</td>
<td>No</td>
<td>Private</td>
<td>Compulsory</td>
</tr>
<tr>
<td>Netherlands</td>
<td>HFL 40,000</td>
<td>Yes</td>
<td>Yes</td>
<td>No</td>
<td>Public</td>
<td>Compulsory</td>
</tr>
<tr>
<td>Portugal</td>
<td>&lt;HFL 1.5M: 80%</td>
<td>Yes</td>
<td>Yes</td>
<td>No</td>
<td>Public</td>
<td>Compulsory</td>
</tr>
<tr>
<td></td>
<td>1.5 to 3 M: 60%</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>maximum 2.1 M HFL</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Spain</td>
<td>PTA 1.5M</td>
<td>Yes</td>
<td>Yes</td>
<td>No</td>
<td>Public</td>
<td>Voluntary</td>
</tr>
<tr>
<td>UK</td>
<td>£20,000: 75%</td>
<td>No</td>
<td>Yes</td>
<td>No</td>
<td>Public</td>
<td>Compulsory</td>
</tr>
<tr>
<td></td>
<td>maximum £15,000</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Austria</td>
<td>OS 200,000</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Public</td>
<td>Compulsory</td>
</tr>
<tr>
<td>Finland</td>
<td>Unlimited</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Public</td>
<td>Compulsory</td>
</tr>
</tbody>
</table>

The Common Market fails to provide one uniform rule, whether it be in the home or host country rule. This has resulted in a compromise of incompatible economic interests. Each nation retains the power to control economic and financial policy under the guise of consumer protection. So, the level of protection between domestic and foreign accounts differs. Many remain concerned for their security and compensation if their bank goes bankrupt. In these situations, the Union's effort has not permeated to the Member States' level. For instance, some Directives are challenged or not enforced on the ground of consumer protection. Finally, the fact that Member States do not have a common opinion on the subsidiarity rule causes additional problems.

One hypothesis in regards to this chapter is whether the spill-over from domestic freedom of services to international freedom of services is recognised. If so, according to neofunctionalism, we can successfully argue that there is a common market for service, which is obtained through neofunctional spill-over. However, I have demonstrated that the freedom of service in domestic markets do not spill-over to the Union level. The Union has not achieved a common market mainly because of national fiscal and lingual barriers. That is to say, lingual and fiscal factors are independent variables in the process of integration.

It is also relevant to note the distinction between the freedom of establishment of a bank branch and the freedom of capital between banks or branches. I deal with it in the following Chapter 4.
Chapter 4. Freedom of Capital

4.1 Public Procurement

Establishing the freedom of capital is another aim of the EU. The main issues falling under this include Foreign Direct Investment (FDI), procurement, and state aid. A discussion of these categories by no means constitutes a thorough analysis of the freedom of capital. For instance, financial policies and the domestic interest rates of Member States may in some respects be directly relevant to the freedom of capital.

A working definition of the freedom of capital is necessary for analysis of this chapter. In principle, the freedom of capital means that capital from any Member States in the EU is entitled to make a free movement without political, financial, legal, strategic or technical restrictions. However, this freedom is unlikely to be attained because controlling the circulation of capital is an essential component of national sovereignty. Therefore every Member State is confined to control the flow of capital within the law set by the EU in order to establish a Single Market. The freedom of capital in this paper therefore means that there are no technical, procedural and systemic barriers in circulation of capital between Member States. Political, financial, and strategic barriers may be present provided they are within the limit set by the EU. Again, I refer to the term 'capital' in its plain and literal meaning. That is to say, it does not include skills, labour power, technology and (intellectual) property even though these may be understood as a type of capital in the wider sense of the concept. I begin with procurement for the sake of logical continuity with the preceding chapter.

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152) Therefore special attention is required in reading the book written by D. Myers and P. Hart because they use the term 'capital' as a wider sense.
Governments act consciously in any modern economy. Government purchases of goods and services typically account for some 15 percent of the Union GDP (as of 1997, which was worth ECU 1,000 billion). A recent survey shows that import penetration rates were 22 percent for the economies combined while those of the public sector amounted to 2 percent. It follows that, in their decision between purchasing from overseas or domestic suppliers, governments can have a marked impact on international trade patterns. In fact, the significance of government procurement policies as non-tariff barriers to trade is a worldwide phenomenon. Governments use them because they can return tax money to domestic residents, create more jobs at home, and reduce imports. These side effects are seen as a truth among both scholars and economists.

Under the Treaty of the EC, Member States began to commit themselves to non-discrimination and the freedom of their capital. Under Article 56 - 60 EC all public works and contracts are bound to comply with the principles set by the Union. To effect these laws, the Commission has proclaimed several directives, such as the Works Directive in 1971, the Supplies Directive in 1977, 1981 and 1989, the Works Directive in 1990, the Utilities Directive in 1993, the Public Services Directive in 1993 and the Utilities Directive in 1994.

It is logical to note the history of the development of public procurement. The threshold was diminished from 1 million to 400,000 Euro depending on the item. It is illegal to split tenders into small contracts to avoid the threshold under the Directives.

155) A. Breton and P. Salmon mention that domestic preference in public procurement is a 'fact' in their article. See Albert Breton and Pierre Salmon, Are Discriminatory Procurement Policies Motivated by Protectionism?, KYKLOS, vol.49, 1996, p. 47.
156) The Article 56(1) EC reads that "within the framework of the provisions set out in this Chapter, all restrictions on the movement of capital between Member State and between Member States and third countries shall be prohibited."
The Article 59 EC reads that "where, in exceptional circumstances, movements of capital to or from third countries cause, or threaten to cause, serious difficulties for the operation of economic and monetary union, the Council, acting by a qualified majority voting, may take safeguard measures with regard to third countries for a period not exceeding six months..."
A successful bidder must be advertised in the Supplement to the Official Journal of the European Communities (OJEC) to guarantee transparency and openness to foreign bidders. In principle, each potential bidder, whether domestic or foreign, is entitled to participate in a tendering in the Union under these provisions and directives. Table 4.1.1 shows in detail the development of the directives.

Let me propose that a would-be contractor AA from country A is seeking to bid in a public procurement in another country B. Again, let me propose that A speaks Dutch. A is running a small to medium size firm.

The first issue is whether the hypothetical person AA is entitled to every public contract in the Union. It is firstly important to mention that not all contracts are open to foreign bidders. Some major areas affecting national security as the Table 4.1.1 above shows have been excluded. Defence (not for civil use), telecommunications, transport, postal, energy and water...
are included in this category. It is not easy to gauge the impact of these industries on the national economy as a whole but it is safe to say that they form the basic infrastructure of the national economy. So, basic industries which are likely to affect seriously the national economy are excluded from those directives.

In addition, Hartley argues that the threshold is still too high to interest to SMEs. He argues that as of 1992 more than 70 percent of contracts were awarded to large firms rather than SMEs. The underlying reasons behind this is that the cost to firms in preparing bids, estimated at 10 percent of the final contract cost, might have dissuaded SMEs from bidding for contracts tendered under the Directive.157)

Also, under these directives, all procurement contracts that come within the scope of the legislation are to be advertised in the OJEC. The first question is therefore whether all public contracts over the amount set by the Union are advertised in the Journal. It is said that not all public contracts are advertised under the pretense of ignorance of the directive and for other reasons.158)

The OJEC is issued five times weekly. Some 300–500 copies are published on each of these days. It is also available on the internet under Tenders Electronic Daily (TED). This indicates that public works are well advertised without prejudice. The real issue is whether or not there is a common set of rules regulating the whole contract procedure at the Community level and whether or not each Member State adheres to these rules. The transparency and fairness of the whole procedure of public contract depends on the compliance of Member States the Union law. Lodge argues that Member States are only likely to comply with Union laws when a high level of political attention is cast on a certain issue, as is the case with the Single Market. The

more concern that is cast on a certain issue, will generally result in a higher level of compliance. As an example, by December 1992, 81 percent of the directives that were essential to realising the SEM programme had been implemented but by January 1993 this had fallen to 69 percent. The compliance of each Member State varies along the implementation ratio, and depends upon also the item exchanged. Due to its delay, the Public procurement sector provides a clear example. It is therefore hazardous to generalize on the implementation ratio without regard to the nature of the item and its implication to each Member State.

<table>
<thead>
<tr>
<th>Country</th>
<th>%</th>
<th>Country</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Denmark</td>
<td>92</td>
<td>France</td>
<td>79</td>
</tr>
<tr>
<td>Italy</td>
<td>87</td>
<td>Spain</td>
<td>77</td>
</tr>
<tr>
<td>UK</td>
<td>86</td>
<td>Portugal</td>
<td>76</td>
</tr>
<tr>
<td>Belgium</td>
<td>85.5</td>
<td>Luxembourg</td>
<td>75</td>
</tr>
<tr>
<td>Netherlands</td>
<td>82</td>
<td>Ireland</td>
<td>74</td>
</tr>
<tr>
<td>Germany</td>
<td>79</td>
<td>Greece</td>
<td>72</td>
</tr>
</tbody>
</table>

EU: 80.4%
The EU average is calculated by the writer.

It is important to understand the actual procedure of a contract. A central issue is whether all eleven working languages are formally allowed to be used in the tendering procedure, and the amounts of days allowed to a potential tender in preparing a contract. If all the working languages are permitted, 36 days for the preparation of a contract does not seem to cause any serious prejudice against foreign bidders. But if this is not the case, it can cause problems for the hypothetical person AA. It must first be noted that the hypothetical person AA is not allowed to use his/her mother tongue in the tendering procedure. The person AA should use the language of the awarding authority rather than his/her mother tongue, for example Greek. This shows that language remains a substantial barrier to full union. Therefore, the question is not a matter of fairness or transparency but again of the lingual barrier, even though the OJEC now advertises the
contract 52 days before.\textsuperscript{159)} As already mentioned, the problem is worsened by the fact that some issues in public procurement are interwoven with those of European standards. A clear example is each Member State having ample room to avoid opening the public procurement market because there are no common community standards. This means that any Member State may not open its market under the pretense of different standards, especially in health, life-related and environmental areas.\textsuperscript{160)}

At an early stage of a public contract procedure, every potential bidder, including the hypothetical person AA, is entitled to access the information released. The notice should contain such information as the person authorised, date and time and place of opening. The notice should not however mention the name of a specific company. In the case of the \textit{EC Commission v The Netherlands}, a Dutch contracting authority published a notice which contained no reference to those persons authorised to be present at the opening of the tenders, or the date, time and place of the opening and indicated the name of a specific software system being required without adding it the words "or equivalent". The Commission considered that such a procedure breached point 7(a) and (b) of Annex III as well as Articles 9(5) and 7(6) of the Public Procurement Directive and, as a result, brought an action for a declaration against the Dutch government. The ECJ held that the Dutch had breached the conditions and were therefore liable to pay the costs.\textsuperscript{161)}

The next question, then, is whether or not price should always be the sole criteria in deciding who is awarded the tender. The answer contains two parts. If the \textit{OJEC} advertised a special criterion when it publishes a notice, then the advertised criterion is applied. Otherwise price criteria are applied. So the real

\textsuperscript{159)} E-mail correspondence, December 13 Monday 1999, eurobal@opoce.cec.eu.int.
\textsuperscript{160)} I mentioned that in \textit{ADBHU}, the ECJ held that the idea of freedom of goods is subject to environmental protection.
\textsuperscript{161)} \textit{EC Commission v The Netherlands (Re Meteorological Station Operation System), 1996 1 CMLR 477}
question is whether the awarding authority is open to apply special criterion when special conditions were not advertised. It seems that the answer is no.

In the case of Portsmouth City Council, the applicant intended to let a 'Maintenance contract' and an 'Improvement contract'. Each contract had a value exceeding the threshold of the application for the Public Works Directive, and the UK Regulations that implemented it. The applicant had despatched to the OJEC a notice in respect of the contract, stating that tenders would be accepted on the basis of "best value for money". The awarding authority made a contract with a company named PCS, taking into account not only the prices, but also the cost to PCS Portsmouth of redundancies if PCS were not to be granted the contract. However, Peter Coles submitting the lowest prices, was initially awarded the contract. The other party sought a judicial review, as a result of which the decision was reversed, based upon the Regulation 20(3) of the Public Procurement Directive.

Regulation 20(3) requires that when an authority is making an award on the basis of the most economically advantageous terms, it is required to state in the contract notice or tender documents the precise criteria which it applies in making the award. The English Court of Appeal, because of this, held that the awarding authority was in breach of the Regulations.

The question then is whether the awarding authority is obliged to announce 'all' criteria 'in the order of priority'. For instance, if OJEC announces that service, bidding price, and the variety of items procured are the points to be marked, but does not announce this to foreign tenders it is evident that domestic tenders have a strong advantage through the 'technical control' of necessary information. Obviously, if person A is not informed about the priority of importance, A is likely to lose the tendering.

There are a number of ways to tender for public contract and public procurement included in these are: open procedure, restricted and negotiated procedures. It is basically left to the awarding authority to decide whether it will employ open
procedures or one of the other. Under open procedure, in principle, every potential bidder is allowed to tender. An invitation may involve a restricted procedure where only a pre-selected group of companies is allowed to tender. Under a negotiated procedure, the awarding authority negotiates with several companies on the tender. A typical reason for an authority choosing the later method is that a previous open invitation may have resulted in no acceptable offer. As a matter of practice, person AA may be interested in the proportion of tender invitations with a corresponding award notice for each EU Member State. As a basic guideline, about 42 percent of all tender invitations have a corresponding contract award notice. More importantly, there is considerable variation between Member States, ranging from 4 percent up to 93 percent. Recent additions to the EU – Greece, Portugal, and Spain – provide very few award notices and have varied greatly through the years. This has not been a major problem at this stage because the implementation of directives, as to public procurement, in these countries was delayed until 1998 at the latest, for domestic economic reasons. This indicates that the opening up of public procurement is not appealing for every Member State!

However, if this arises in any one of the existing Member States, it will create problems. For instance, in 1993 the proportion of Danish tender invitations with corresponding contract award notice increased dramatically (by over 30 percent), only to decline to its previous figure in the following year. Again, Luxembourg provides an example of the questionability of report. The figures demonstrates that there were almost 50 percent more contract awards than tender invitations in 1992, 1994 and 1995. Table 4.1.3 shows these succinctly.


163) S. Martin, Keith and Andrew unfortunately do no give a definitional clue in their article: what is domestic and what is foreign firm and whether multinational corporation is in the definition of domestic firm, etc.
Another issue revolves around the percentage of foreign bidders awarded in the tender, the percentage of domestic bidders awarded in a tender, and the percentage of non-EU bidders awarded in a local authority tender. According to S. Martin and K. Hartley, about 96 percent of domestic bidders are awarded tender, while fewer than 0.35 percent are awarded to firms in non-EU countries, and 0.3 percent to other EU Member States. The import penetration ratio in public procurement was about 2 percent at the Community level as of 1993, which was lower than the average import ratio of 22 percent in the economic sector as a whole. Table 4.1.4 shows the percentage by countries.

Finally let me explain the final stage of a contract. Contract award notices published in the OJEC should include the name and address of the successful bidder. This is designed to enhance the transparency of the contract procedure. The issue is whether the name of the successful bidder and his/her address is sufficient for an unsuccessful bidder to assess the fairness and transparency of the contract. It does not seem to be fair and transparent unless the 'marking criteria' are released along with the successful bidder and his/her address.

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164) A data on central authority is not available. So, only local authority is focused on.
Table 4.1.4:
Number of local authority contracts awards by nationality of purchaser and nationality of vendor for EU, 1993

<table>
<thead>
<tr>
<th>Member State</th>
<th>Domestic</th>
<th>EU</th>
<th>Non-EU</th>
<th>Various</th>
<th>None reported</th>
<th>Total</th>
<th>Import penetration ratio, 1993 (all goods)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Belgium</td>
<td>32</td>
<td>1</td>
<td>1</td>
<td>0</td>
<td>0</td>
<td>34</td>
<td>0.524</td>
</tr>
<tr>
<td>Denmark</td>
<td>341</td>
<td>3</td>
<td>2</td>
<td>4</td>
<td>8</td>
<td>358</td>
<td>0.231</td>
</tr>
<tr>
<td>France</td>
<td>1,688</td>
<td>3</td>
<td>5</td>
<td>2</td>
<td>23</td>
<td>1,721</td>
<td>0.162</td>
</tr>
<tr>
<td>Germany</td>
<td>2,731</td>
<td>14</td>
<td>6</td>
<td>5</td>
<td>84</td>
<td>2,840</td>
<td>0.182</td>
</tr>
<tr>
<td>Greece</td>
<td>7</td>
<td>0</td>
<td>0</td>
<td>1</td>
<td>0</td>
<td>7</td>
<td>0.220</td>
</tr>
<tr>
<td>Ireland</td>
<td>35</td>
<td>1</td>
<td>1</td>
<td>0</td>
<td>0</td>
<td>38</td>
<td>0.541</td>
</tr>
<tr>
<td>Italy</td>
<td>999</td>
<td>1</td>
<td>2</td>
<td>0</td>
<td>39</td>
<td>1,041</td>
<td>0.159</td>
</tr>
<tr>
<td>Luxembourg</td>
<td>10</td>
<td>0</td>
<td>1</td>
<td>1</td>
<td>0</td>
<td>12</td>
<td>0.242</td>
</tr>
<tr>
<td>Netherlands</td>
<td>57</td>
<td>1</td>
<td>0</td>
<td>3</td>
<td>0</td>
<td>61</td>
<td>0.421</td>
</tr>
<tr>
<td>Portugal</td>
<td>21</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>21</td>
<td>0.314</td>
</tr>
<tr>
<td>Spain</td>
<td>13</td>
<td>0</td>
<td>0</td>
<td>1</td>
<td>0</td>
<td>14</td>
<td>0.161</td>
</tr>
<tr>
<td>UK</td>
<td>1,685</td>
<td>0</td>
<td>9</td>
<td>25</td>
<td>25</td>
<td>1,734</td>
<td>0.216</td>
</tr>
<tr>
<td>EU12</td>
<td>7,599(96.4%)</td>
<td>24(0.3%)</td>
<td>27(0.3%)</td>
<td>40(0.5%)</td>
<td>191(2.4%)</td>
<td>7,881(100%)</td>
<td>0.255</td>
</tr>
</tbody>
</table>

Notes: The imports penetration ratio is calculated as imports/total domestic demand.

Then, if a person is prejudiced against in the contract, the next question involves deciding whether a working remedy is available. In principle, the Commission may take the case to the ECJ through CFI. Damages are available if caused directly by the awarding authority. In the case of *Embassy Limousines and Services* the applicant submitted a tender to the European Parliament to provide taxi services and was told that it had been successful. It then entered into contracts for cars and mobile phones, and recruited drivers informing Parliament of this. However, the signing of the contract was delayed, initially pending an investigation of the applicant and the quality of its services. The investigation concluded that the allegations regarding quality of service were unfounded. Parliament then annulled the original invitation to tender and awarded the contract to another company pending the re-opening of the tendering procedure. The applicant sought compensation from Parliament under Art. 215 EC for the damages. The CFI, following *Team*, held that the applicant's investment in cars,
mobile phones and personnel had been made as a result of the confirmation that the applicant would be awarded the contract, and had been made before the applicant could have been aware that it might not be given the contract.

However, granted that the country concerned has a complaints system, the main problem involves costs in both time and money. For an aggrieved bidder the costs of complaining, appealing or reviewing the decision might be greater than costs of being discriminated against.\(^{166}\) So it cannot be said to be an effective remedy in guaranteeing free movement of capital.

Public procurement is essentially a public contract. Any specific behaviour of an awarding authority may affect the result of the tender, in terms of transparency and fairness. This means that the EU urgently needs European common contract law which covers all contracts in Europe. Nevertheless, one may argue that some barriers, lingual for instance, may be overcome by setting up a subsidiary company or by direct investment in another country. I therefore look at the issue of Foreign Direct Investment (FDI) in the following section, 4.2.

4.2 Foreign Direct Investment

It is logical to give an operational definition of foreign direct investment (FDI). FDI in this section refers to an investment that is made to add to, to deduct from, or to acquire a lasting interest in an enterprise other than that of the investor, the investor's purpose being to have an effective voice in the management of the enterprise in the host country. Other investments in which the investor does not have an effective voice in the management of the enterprise are mainly portfolio investments.\(^{167}\)

Articles 56 to 60 of the E.C.\(^{168}\) provide the basis of freedom of capital. These Articles aim to remove all restrictions on capital movements between Member States and third countries.\(^{169}\) It is critical to realize that there have been two streams of developments in the FDI. One is Bilateral Investment Treaties (BITs) and the other is the Community Directive.

The Union has issued some Directives in order to accomplish the freedom of capital. The first Community measure to implement the idea is the 1960 Directive, amended in 1962 by which the Community unconditionally liberalised FDI, whether short or medium term lending. It was not until the Single Market was launched that the progress begun in 1960–62 was resumed. Two Directives, in 1985 and 1986, extended unconditional liberalization to long term lending for commercial transactions.

The 1988 Directive (88/361/EC) however does include a safeguard clause enabling Member States to take protective measures for countries such as Spain, Ireland, Portugal and Greece under ss47 and 209, under the so-called transitional period provision.

On the other hand, some Member States decided not to wait for Community decisions and abolished virtually all restrictions on

\(^{168}\) For more information, see Public Procurement section.
capital movement. This process is known as BITs. The Federal Republic of Germany did so in 1961, the UK in 1979 and the Benelux Countries in 1980.

Let me first look at the overall pattern of FDI in Europe. A broad pattern of FDI in Europe, inbound and outbound, has sharply increased since the middle of 1980s, especially in the aftermath of the common deregulation of capital and product markets. The aggregate stock of FDI is estimated around 14.8 to 17.4 percent of the Union GDP. Inward FDI in Europe is around 14.8 percent of the Union GDP, outward FDI is around 17.4 percent as of 1995. Table 4.2.1 below shows it succinctly. Therefore it can be said that the FDI is an essential part in understanding the freedom of capital\(^{170}\) in Europe. The term 'freedom of capital' does not include the physical export of means of payment, such as coins, bank notes or bearer cheques. Article 73 EC specifically states that these are prohibited. In *Sanz De Lera and Others*, the defendants were each prosecuted for attempting to export Spanish currency to a non-Member state in the form of banknotes without obtaining the necessary export authorisation or making a prior declaration as required by Spanish law. The Spanish national court referred it to the ECJ. The ECJ held that in this situation, Article 73 is inapplicable to national law, so the national law should be observed.

| Table 4.2.1: European Union 15 Foreign Direct Investment stocks |
|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|
| Outward FDI     | Inward FDI      |
| $ billion       | 213.2 | 286.5 | 777.2 | 1208.8 | 185.0 | 226.5 | 712.2 | 1028.1 |
| % of GDP        | 7.4   | 7.1   | 13.8  | 17.4  | 6.4   | 5.6   | 12.7  | 14.8  |
| % of total      | 41.5  | 41.8  | 46.1  | 44.3  | 38.4  | 30.8  | 41.5  | 38.7  |


It is important to be aware that FDI acts as a channel through which new ideas, technologies and working practices can be established in host countries.\(^{171}\) According to Barrel and Pain

\(^{170}\) *Spain v E.U. Council (Re Medicinal Product Certificate)*, 1996 1 C.M.L.R. 415

\(^{171}\) Ray Barrel and Nigel Pain, The Growth of Foreign Direct Investment in Europe,
UK, France and Germany are the main destinations for inward investment and major investors in the EU. As Table 4.2.2 below shows, the three major Member States account for around 40% of outflows investment and 34% of inflows of G-10. This leads me to the question: what factor(s) determines foreign investment in Europe?

Simply speaking, it is the business environment. What then is this business environment? The traditional wisdom was that FDI was determined, as Ray points out, by the size of the market and labour productivity. Therefore the labour-intensity and size of a calculated product were the main considerations. This has changed since the early 1990s. A desire for better management with high-technology leads over competitors, patent protection and intellectual property rights for instance are now the prime considerations.

<table>
<thead>
<tr>
<th>Table 4.2.2. FDI outflows and inflows ($: billion, annual average)</th>
</tr>
</thead>
<tbody>
<tr>
<td>---------------------------</td>
</tr>
<tr>
<td><strong>UK outflows</strong></td>
</tr>
<tr>
<td><strong>UK inflows</strong></td>
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<tr>
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It is necessary to mention that in the EU, there is a European
Company law under Article 54(3)(g) EC. The objective of the Company law is to require all companies in the EU subject to the jurisdiction of the Member States to observe a minimum of common objectives to further the establishment of an undistorted system of competition. It must be mentioned that this law aims to remove legal barriers rather than economic-financial obstacles manipulated by each Member State.

Then the real question is whether or not intellectual property laws, or other laws regulating intellectual rights, such as patents are protected when a company invests in a foreign country. Unfortunately, the answer is negative. In *Merck*, P claimed that D had infringed on the patents which P held in the UK for certain pharmaceutical products by importing the products from Spain and Portugal and selling them in the UK. At the relevant time, Spain and Portugal had joined the Community, but had not made patent protection available for the products in question.

This case requires a detailed account to avoid confusion. The actual issue concerns the interpretation of ss47 and 209. As neither country allowed the effective patenting of the product, the Act of Accession required both of the Member States to make such products patentable at a future date. So the first real issue was in regard to the transitional period: whether the three year period ran from the exact day on which the product became patentable or whether the period began at the end of the calendar year. The court held that the period began on the exact day from which the patent became available because of the idea of freedom of movement. The second issue which is relevant to this chapter was whether the applicant could rely on the patent granted by the UK to get benefit from Spanish products. The ECJ held that "where the holder of a patent for a pharmaceutical product sold the product in one Member State where patent protection existed, and then marketed the product himself in another Member State where there was no patent protection, he could not rely on his patent rights in the first Member State in order to prevent others from importing the product from the second Member State and
marketing it in the first Member State."\textsuperscript{172) This clearly means that there was no common Community legislative protection for intellectual property rights. However the court however did mention that "ratification of European Patent law was under process in each Member States." \textsuperscript{173) So, by now, it appears that this will not cause any serious problem amongst at least the 15 existing Member States because freedom of goods is a norm. Nonetheless, it may cause a problem if any country makes a new entry to the Union. For instance, if person AA, a Turkish, begins marketing in one Member State by importing an unprotected item from Turkey, the patentee is not protected under the patent because Turkey is not a full Member of the Union yet. It is just a waiting Member country. It may be therefore concluded that the ratio of \textit{Cassis} is subject to \textit{Merck}. This means that there is less incentive for a patent holder to invest in a foreign country until there is a common Community level intellectual property law.

What does the term common Community level intellectual property law mean? In Europe, it is a norm that if person AA is granted a right in one area, the person is automatically granted the patent right in the 15 Member States as a whole. This means that, in principle, intellectual property law is unlikely to cause any serious problems in Europe.

The real question is however whether common Community intellectual property law is well administered in the Union without distortion. The European Patent Office (EPO) is in charge of patents in the EU. The office is a transnational body and is designed to guarantee transparency and fairness in patent applications throughout the EU. The EPO, simply speaking, is an administrative body in the Union. So the actual question turns to whether and how the Union holds the EPO to account for transparency. W. Cook is of the view that EPO does not make a full guarantee. In \textit{Lenzing}, the applicant, the Austrian company

\textsuperscript{172) Merck \& Co. Inc and Others v Prime Crown Ltd and Others, 1997 1 C.M.L.R. 83. \textsuperscript{173) Ibid., 83
Lenzing AG, was the proprietor of a European patent right in the field of cellulosic solution production, granted by the EPO in December 1992. Oppositions were filed against the patent by both a German and an English company. In May 1994 the Opposition Division upheld the patent, and the opponents appealed to the EPO Technical Board of Appeal. After a hearing, the Board revoked the patent without giving any option of judicial review. Judicial review is one of the basic rights for Community citizens. So the FDI in Europe is staggering because transparency in the administration of the legislation is not fully guaranteed by the authoritative body concerned.¹⁷⁴)

As I mentioned at the outset, the second basic feature in FDI in general is Bilateral Investment Treaties (BITs). Taking into account the fact that most FDI is governed by bilateral investment treaties, it is more important to ask whether BITs affect or distort the ideas of freedom of capital. Table 4.2.3 below, to begin with, shows BITs in the EU.

BITs generally, though not always, include provisions on admission, treatment, transfer of capital and compensation. There are two main questions here. First, whether the idea of the common FDI market is fully established, and second whether the BITs are consistent with the Community’s policy in pursuing common market. So, the first question should focus on the admission of foreign investment. Generally speaking, a foreign investment cannot, in the nature of things, be admitted in the territory of a host state in conformity and consistently with its domestic law. According to M. I. Khalil, the drafters of the majority of BITs have deemed it appropriate to set out an express provision to that effect. For instance, after analysing 335 (including 260 EU) BITs he concluded that in 59 BITs, of which 42 are UK, 7 Dutch and three Belgian, the obligation to admit a foreign investment is expressed to be subject to the contracting parties’ right to exercise powers conferred on them by their own

Table 4.2.3: BIT List

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<td>EU 11 Total:</td>
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<td>260 BITs</td>
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Note. Some Member States information is not available.


Another point of interest is treatment by a host country. The obligation to admit foreign investments, to facilitate the transfer of their proceeds and to agree to a reasonable mode of settlement of disputes arising out of them are all aspects of treatment. A basic starting point is the duty to accord the foreign investment ‘fair and equitable treatment.’ It however must be mentioned that not all the treaties contain this ‘fair and equitable treatment’ provision.\(^{176}\) This means that there is no Union wide FDI market.

As foreign investment would seriously be discouraged without the prospect of the ability to transfer the proceeds, it is not surprising that all treaties provide, according to M.I. Khalil, that such proceeds shall be transferred 'without delay'. Nevertheless, more than one sixth of the treaties recognise that the balance of payment may make it difficult for them to allow immediate transfers of large sums of money. 177) Again, the Union failed to provide a common set of rules applicable to the FDI in Europe.

The Council of Europe Convention 1950 provides that no one shall be deprived of his possessions except in the public interest and subject to conditions provided by law and by the general principle of international law. The Convention also expressly provides that expropriation is subject to the general principle of international law. As a general rule, a foreign possession must be expressed either expressly or implicitly in the host country legislation. The expropriation may be done only if public interest requires it. If a foreign possession is expropriated, an adequate compensation is the norm. Therefore the actual issue at this stage is whether or not the compensation provision is real and absolute. According to Khalil, the Council of Europe Convention provides that there is "no absolute right to compensation; only if principle of proportionality so demands, then it may be compensated." 178) Simply speaking, the European market is fragmented into BITs and there is no guarantee of a common set of rules at the Community level.

The last question is whether the principle of direct effect of Community law is fully established in FDI. That is to say, are Community legislations override any BITs that are inconsistent with the Community legislation? The basic answer is yes, however it is not so simple because so many technical problems are combined in FDI. The investors are not fully satisfied with the protection of their FDIs mainly because of the complexities of technical and administrative procedures.

As a whole, it is fair to conclude that the idea of freedom of capital, in terms of FDI, is established at a reasonable level. Nevertheless, there are some remaining problems caused by the fact that most problems are interwoven. The starting point is that there are two streams of development: one by the Union and the other by BITs. Neither of them provide a Union level common set of rules. Therefore I am bound to conclude that there are as many FDI markets as the number of BITs in Europe. A Single Market is far away!

It is important to consider that if the investment is made by a Member State, it is regarded as state aid, whereas if it is made by the non-public sector, it is regarded FDI in Europe. Therefore I am bound to look at state aid in the following section, 4.3.
4.3 State Aid

In the preceeding section, I argued that the Common Market, in terms of FDI, is fragmented into bits of BITs which provide many technical barriers. I have therefore concluded that the idea of the freedom of capital is not fully established. This section develops a slightly different focus from the preceeding sections. This section involves an internal capital flows, rather than external flows between states. I will therefore look at state aid in order to find out whether the idea of freedom of capital is fully established.

To constitute a state aid, under Article 87 - 89 of the EC Treaty, four criteria must be satisfied: 1) it must provide a firm with an advantage; 2) it must be granted by the state or state resources; 3) it must have particular characteristics, i.e. it must favour only certain undertakings or the production of certain goods; 4) it must affect trade between Member States. If any of the above are not satisfied, Article 87 EC is not applicable.180 Also, all aid of less than ECU 100,000 per firm, over a period of three years, with the exception of export aid, is not subject to Community control and the Commission need not be notified.181 This is the Commission's interpretation of state aid. From a practical point of view, let me propose a hypothetical situation: A company is intending to invest 120,000 ecu over four years, of which more than two thirds comes from state funds. We need to understand whether this constitutes a state aid. The answer is unclear because on the one hand, in terms of the amount of capital, it falls under the definition of a state aid, however on the

179) The Article 87(1) EC reads that "save as otherwise provided in this Treaty, any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, in so far as it affects trade between Member States, be compatible with the common market."

The Article 89 EC reads that "The Council, acting by a qualified majority, may make any appropriate regulations for the application of Articles 87 and 88 and may in particular determine the conditions in which Article 88(3) shall apply and the categories of aid exempted from this procedure."


181) Ibid., 59
other hand, in terms of the duration, it does not.

Also, the court applies a slightly different criteria. The CFI had the chance to develop a more concrete definition of state aid in *Breda Fucine Meridionali SPA*. The court held that in order to determine whether investment by a public authority in the capital of an undertaking constituted state aid within the meaning of Article 92(1), it is necessary to consider whether in similar circumstances a private investor might have provided injections of capital\(^{182}\) of such an amount. Although the comparison need not be with an ordinary investor, laying out capital with a view to realising a profit in a relatively short time, it must at least be the conduct of a private company or private group of undertakings pursuing a structural policy and guided by prospects of profitability in the longer term. Where injections of capital by a public investor disregard any prospect of profitability, even in the longer term, such provision of capital must be regarded as aid within the meaning of Article 92 E.C.\(^{183}\)

However this definition remains unclear. One holds that it is state aid if it is ”done by state or state resource” while the other maintains that it is a state aid if it is ”done by a state or state resources in the view of a private investor.” Also, how many years constitute ’long term’? Further, how many years constitute ’short term’? The basic problem with state aid is the problem of definition. It is helpful to look at the provisions of the Treaties of the Union. Article 3(g) and 92 to 94 of the EC, and Article 4 and 67 of the ECSC Treaty govern state aid.

Article 92 provides for a general prohibition of state aid if the aid is preferential to a domestic company. The first problem is that there is more than one way of giving state aid in Europe. The Article covers not only aid granted directly by the Member States, but also aid that uses state resources. This includes any agencies that might distribute aid on the basis of government funding such as local authorities, public establishments, and

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\(^{182}\) Emphasis added.

various authoritory organisations. This also includes any form of resources, including non-payable subsidies and loans on favourable terms with low interests rates, and tax exemptions which may distort or merely threaten to distort competition.\textsuperscript{184)\ }

The Commission is responsible for three administrative and procedural frameworks under Article 93 of the EC Treaty. The basic function of administrative and jurisdictional procedure is to ensure that no aid is granted without the Commission's agreement. First, the Commission, under Article 93(1), carries out a review of the aid already granted by the Member State concerned. Second, the Commission then may require the Member State concerned to inform it of plans to grant or alter aid under Article 93(3). Third, under Article 93(2), if any Member State is deemed to be in breach of the law, the Commission begins infringement proceedings by formally serving a notice to the Member State and charging it with the requirement to comment within a given period of time, i.e one month.

So the real question at this stage, in relation to the various forms of state aid, is how the Commission determines whether a Member State is in breach of the provision. It is logical to begin with the objectives of state aid. State aid policy has two main objectives: either competition or competitiveness and cohesion. These correspond with the objectives of equity between EU Member States, EU economic strength relative to the extra-EU international economy, and the spreading of the benefits of integration across Member States. Sustaining competition in the Common Market requires that the Commission minimise the distorting impact of state interventions within the EU. Cohesion demands that state aid policy be applied consistently across Member States, with the needs of poorer regions figuring significantly in the Commission's calculations of compatibility of state intervention with the Common Market.\textsuperscript{185)\ }


Regional aid is one tool for providing equity between Member States. This is based on the idea of "Europe with a human face" or a "Social Europe". This type of aid aims for equal development and benefit, rather than any incentive of competition in the EU. This includes aids such as Research and Development Aid, Environmental Aid, Rescue and Restructuring Aid, State Aid for Small and Medium-sized Enterprises (SMEs), Employment aid, Training Aid and Aid for Deprived Urban Areas. Also, aid to make good the damages caused by exceptional events, such as natural disasters or aid for certain areas of the Federal Republic of Germany affected by the previous division of Germany, are considered to be included. This aid is automatically exempted and entitled to be declared compatible to the Common Market under Article 92(2). The Commission has finished the Regional State Aid Map for this purpose.\(^\text{186}\)

Additionally, there are some other possible areas of exemption, although they are not automatic. These include aid to under-developed areas, aid to promote the completion of major projects of European interest and aid to promote culture and heritage conservation. These may be considered to be exempted under Article 92(3).\(^\text{187}\) They are designed to promote equal development in order for an \textit{aquis communautaire}. The actual problem, it seems, is the Union's failure to provide a consistent set of rules for the provision of aid.

The second major objective of state aid involves improving competitiveness in the global trading arena. The rationale behind this is that the EU consists of independent Member States with their own sovereign concerns, a concept opposing the spirit of the Common Market. A state aid is therefore a major tool in the expression of its sovereignty. Simply, state aid is a symbol of nationalism rather than super-nationalism. This applies in the aid given to particular industries, such as the motor vehicle industry, shipbuilding, steel, coal transport, agriculture, and fisheries.\(^\text{188}\)

\(^{186}\) For more information, see http://europa.eu.int/comm/dg04/regaid/1999/en/html.
This is called sectoral aid. Some reference to these sectors is required.

As regards to shipbuilding, the Seventh Directive on Aid to Shipbuilding is an attempt to guarantee transparency. The Commission has kept the common production aid ceiling at 9 per cent for large vessels and 4.5 per cent for vessels costing less than ECU 10 million as well as for conversions.\textsuperscript{189} The Fifth Steel Aid Code was applied to the steel industry until 1996. In December 1996 the Commission adopted a new Steel Aid Code to cover the period until the ECSC Treaty expires in July 2002. Decision No 3632/93/ECSC of 28 December 1993 establishes Community rules on state aid to the coal industry from 1994 to 2002. In the air transport sector, the Commission has maintained strict control of state aid. Most of the national airlines were recapitalised and subjected to restructuring plans. The Commission therefore gives priority to controlling the implementation of these plans and verifying that all of the conditions laid down in the decisions authorizing aid for the restructuring of the airlines are complied with. Previous experience in the agricultural sector has shown that assurances given by Member States are insufficient in guaranteeing compliance with mandatory Community rules. The Commission now asks Member States to submit samples of logos, trade marks and slogans. These are used to verify compliance with policy on publicity aid in agriculture. Nevertheless, it must be acknowledged that the Directive does not sufficiently cover this. For instance, each Member State has enough room to avoid the scrutiny of the Union as it provides a threshold, in terms of finance, regardless of the size of a company. The Union does not provide a threshold of finance in proportion to the size of a company.

The motor vehicle sector provides an opportunity for in-depth

\textsuperscript{188} These are not exhaustive. For more information, see http://europa.eu.int/commm/dg04/lawaid/aid3.htm or European Commission, 26th Report on Competition Policy: published in Conjunction with the General Report on the Activities of the EU – 1996, 1996, pp. 58–66

\textsuperscript{189} Ibid., 59
examination. Between 1990 and 1994, the ECJ, including the CFI, ruled on 39 decisions negatively. Six out of 39 were motor vehicle related cases.\(^\text{190}\) They were as follows: \textit{Volkswagen}, \textit{Toyota Motor Corporation}, \textit{Rover Group}, and the \textit{Renault Group}. The motor vehicle sector includes the manufacture of engines but excludes all parts and accessories for motor vehicles and engines. State aid granted to a company producing only a part of a motor vehicle is exempted. State aid to this sector is granted mainly by way of regional, rescue and restructuring aid. Therefore state aid granted to the motor vehicle industry is examined solely in the light of normal criteria for regional aid. The \textit{Suzuki Manzanares} is a case in point.

\textit{Suzuki Manzanares} produces parts of motor vehicle engines. The issue of this case involved whether the aid granted to Suzuki Manzanares constituted regional aid, not whether it constituted aid under Article 92. According to the decision, based on the small part manufactured by Suzuki Manzanares in the total net cost of the engines and the fact that no sub-assembly takes place on site, the Commission regarded the plant as a component factory which was thus not covered by the framework of state aid to the motor vehicle industry.\(^\text{191}\) This clearly illustrates the issue of certainty of precedent in the EU, because the reason Suzuki does not fall under the definition of the provision is not sound.

Another, more substantial, issue is that state aid is not self-contained. State aid, as I mentioned earlier in this chapter, is designed to improve competitiveness in and out of the Common Market. However, it may constitute over-competition, which is prohibited under Article 85 and 86 EC. The actual question therefore involves the blurred line between over-competition and competition. The actual amount granted, no matter how much, does not seem to be the decisive criteria in State Aid. It is therefore quite fair to conclude that the Commission agrees that

\(^{190}\) http://europa.eu.int/comm/dg04/aid/ineg1990.htm  
\(^{191}\) 26th Report, op. cit., p. 61
it is "quite difficult to draw any conclusions as to the general trend"\textsuperscript{192}) and criteria for it.

The uncertainty, in terms of definition and interpretation, becomes apparent when we understand the basic nature of the two objectives of State aid: cohesion and competition. One is designed to spur supernationalism in the EU whereas the other provides for national interest. In simple terms, the Commission seems to be trying to harmonise two incompatible goals.

Moreover, even the court cannot resolve the uncertainty caused by the Commission. \textit{Ryanair} is one clear example. In August 1993, the Irish government notified the Commission, in accordance with Article 93(3) EC, of its intention to make a capital injection of IR £175 million into the Aer Lingus group as part of a restructuring plan. Following a procedure initiated pursuant to Article 93(2) of the Treaty, the Commission adopted Decision 94/118 in which it held that the restructuring aid to be granted to Aer Lingus was compatible with the Common Market, provided that certain conditions were met. Aer Lingus failed to meet the conditions.\textsuperscript{193}) Following this, Ryanair Ltd applied for the annulment of the contested decision. The ECJ held that "it was not normally possible for the Commission to depart from the scope of its initial decision without reopening the procedure and it could only adopt a decision derogating from an unfulfilled condition in the case of relatively minor deviations." However, as opposed to the ratio of \textit{Suzuki}, "in respect of aid already approved in principle but which was to be paid in successive tranches over a relatively long period in association with a restructuring plan, the Commission must enjoy a power to


\textsuperscript{193}) The conditions included a commitment by the Irish government not to proceed with the second and third tranches of the aid if Aer Lingus failed to achieve an IR £50 million annual reduction in costs, to provide the Commission with a report on the progress of the restructuring programme, and not to expand the operating fleet over the period of the restructuring plan other than for transatlantic operations. On 21 December 1994, the Commission however adopted a decision authorising the Irish government to pay the second tranche of the aid to Aer Lingus on the basis that the progress of the restructuring plan and the results achieved were satisfactory even though Aer Lingus had not achieved the IR £50 million reduction in costs required by Article 1(a) of the contested decision.
manage and monitor the implementation of such aid."\textsuperscript{194)

If state aid is found to breach Article 93(2), the court has the discretion to allow a policy requiring the repayment of aid or to annul the Commission's decision.\textsuperscript{195) Rover and Renault provide specific instances of this in the motor vehicle industry. BP Chemicals Ltd is another clear case in the chemical sector. In 1992 and 1993, Enichem SPA (Enichem) received two capital injections of 1,000 billion and 794 billion lire, from ENI SPA (ENA), a holding company which had been created on the dissolution of the public entity, Ente Nazionale Idrocarburi. Until 1995 the Italian State Treasury was ENI's sole shareholder and EniChem was close to a 100 per cent subsidiary, producing and marketing a wide range of chemical products. In the course of proceedings under Article 93(2) EC, set up to investigate the capital injections, of which no prior notification had been given under Article 93(3) EC, the Commission was presented with a restructuring plan for EniChem, which contained a proposal for ENI to invest a further 3,000 billion lire into the company. In July 1994, the Commission announced its decision to close the proceedings in respect to the first two capital injections, thereby approving the aid already granted to Enichem which it held to be compatible with the Common Market. It also decided that since the third capital injection would have been made by a private investor operating in a market economy, it did not constitute state aid. Both findings were challenged by BP Chemicals Ltd (BP), who applied to the court to annul the contested decision. The CFI upholding BP found that the Commission should have had doubts on the question of whether the third injection was so sufficiently distinct from the first two that it could be analysed in isolation from them, and that it was not in a position to assess whether the decision to make the third injection of capital would have been taken by a private investor operating in a market economy.\textsuperscript{196)}

\textsuperscript{194) Ryanair Ltd v E.C. Commission, 1998 3 C.M.L.R., p. 1023
\textsuperscript{195) The Commission normally maintains that the grant already paid should be repaid whereas the court seems to be reluctant to order repayment of the equity installed.

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As a whole, uncertainty in terms of interpretation and application to the Articles of state aid is the first and most important problem. There is no authority able to give an objective and impartial interpretation because the Commission and the court can give inconsistent results, judging by the cases of Ryanair and Suzuki. The state aid provisions are designed to harmonise two goals which, by their nature cannot be harmonised. Who can be persuaded that there is a Common Market, in terms of state aid, in Europe?

I have demonstrated that no Single Market exists for state aid. According to the logic of neofunctionalism, internal freedom of capital, public procurement for instance, is to spill-over into inter-national level, state aid meaning that once the internal freedom of capital is fully established, this is to spill-over into the freedom of capital in inter-national level. However, the spill-over effect has not been recognised between inter-national levels, let alone at the internal level. Simply, the idea of freedom of capital is far from the reality in the SEM, mainly due to national sovereignty in economic and financial sectors. Thus, I conclude that the hypothesis of neofunctionalism is unsatisfactory.

196) BP Chemicals Ltd v E.C. Commission, 1998 3 C.M.L.R. 693
Conclusion

This thesis contains three propositions. First, there is economic spill-over within an economic sector. This spill-over effect in turn spills to a next, closely related economic sector. Second, this economic spill-over effect then spills to the political sector whereby the Union takes over the decision making power from Member States. Third, these two spill-over effects can be encouraged by the process of central institution building. To put it another way, in theory, economic spill-over in one sector will cause economic integration in that sector and eventually the integration of all economic sectors. An advanced form of economic integration, according to neofunctionalism, is the SEM. The SEM is therefore deemed to produce a political union: the European Union without internal frontiers. Simply speaking, neofunctionalism (especially with regard to the SEM) appears the best approach in explaining the integration process.

As noted above in the third proposition, neofunctionalism rightly argues that the SEM is best explained by way of its central institution building process. Central institution building itself is a process of integration of the Member States, because institutions of the Union take over the decision making power of each Member State. A fundamental principle of law in the EU is that Union law enjoys superior status over each Member State and has direct effect in all Member States. Community law is made mainly by the central institutions such as the Commission, the Council of Ministers, the EP and the ECJ. The ECJ is charged to ensure that each economic step of the integration process complies with the superiority principle of Union law and that the Community law is honoured by its Member States. The EP makes every effort to ensure the Community interest is best protected through the Community legislation process. A guiding principle of the EP is to instill loyalty from European citizens by giving them a right to vote in
Community level elections and a right to petition by way of an ombudsmen.

However, every economic sector is also fragmented into parts along the frontiers of the Member States. A true SEM is not a reality. This means that the spill-over effect, which is the fundamental proposition in this thesis, has not fully taken effect even within the economic sector, let alone in the political sector. Therefore, neofunctionalism appears defective in this point.

Another major problem of neofunctionalism is that the central institutions, the agents for neofunctionalism, is not given 'full competence'. Neo-functionalism argues that the central institutions can facilitate the process of integration "provided the institutions have sufficient competence on all matters".\textsuperscript{197} Neo-functionalism appears to assume that the process of taking competence is 'automatic'. In reality, however, the process of taking competence by those central institutions is checked and hindered by national governments' conscious choice and attempt to preserve national sovereignty.

As explained in 1.3 (indirect taxation) the Union has competence to approximate the rate of taxation. The Union, however, does not have the power to levy Union tax over a transaction of goods in the SEM. All Member States clearly retain the power to levy tax. This is a key argument. The freedom of goods is hindered by political factors and national governments.

In addition, the fact that Member States are allowed so many exceptions in effect prevents the SEM from forming a true common market. The Union and the central institutions therefore cannot complete the integration process consistent with the logic of neofunctionalism. Let me explain the freedom of goods argument first. The freedom of goods has not fully taken root in all the Member States for specific reasons. These reasons include public health, environmental considerations,

\textsuperscript{197} See the introduction of this paper for more information.
national security, and telecom related infra-structures. The basic rationale of neofunctionalism; the economic spill-over effect, is not yet found in these sectors because they are influenced by political and strategic considerations rather than pure economic factors. Thus, with regard to the freedom of goods, neofunctionalism does not explain all aspects satisfactorily.

Again, with regard to the freedom of people, the Union has competence over, for example, a common visa format, but the Union does not provide a common set of visa requirements. The Union also has the power to grant the portability of pensions in the public sector, but not in the private sector. Moreover, while the Union purports to protect basic human rights in such a way that nationality related discrimination is not allowed, there are so many criteria it can not be argued that there is a common market for people. In addition, social benefits for workers are a Community competence, but those for a worker's family may not be, because Member States have different rules for granting social benefits. As a whole, it seems impossible to argue that the freedom of people is fully established. This means that intergovernmentalism in conjunction with neofunctionalism remains alive in many areas.

Next, with regard to the freedom of service, it is important to be aware that most Directives are based on the home country principle, called simply the 'home rule'. What is the home rule? Each home Member State is legally allowed to control and cancel the licence of establishment or a branch set up to provide a service in the host country. This means that the number of rules are equal the number of Member States in the Union. The Union, in other words, does not have any supranational common rules at all, as evidenced by the examples of banking and insurance.

Also, with regard to the freedom of capital, Member States are not allowed to give preferential aid in principle. In fact, each government offers preferential treatment to its domestic firms. Why is this? Because the Union does not have clear set of rules on this point of issue, as
illustrated by the examples of aid to the motor vehicle industry. This means that the neo-functional approach is not fully effective in the freedom of capital in nature because there are a multiplicity of independent political factors in force in the SEM.

Subsidiarity is another major area that neofunctionalism fails to explain in the SEM. This rule may be interpreted in two ways. First, whether the Union has competence on a certain issue and second, if so, to what extent does the Union have the power to make a decision. Let me deal with the second question first. The focus of this rule is whether and what extent the Union is allowed to make a decision on a Community matter. The rule provides that "the lowest possible body is entitled to make a decision on a given point of issue". This means that if there is a dispute between the Union and Member States as to competence, there is a presumption that the Member State, not the Union, has the power to make the decision. There is no presumption that the Union is entitled to make a decision if any issue is contentious. This shows that the subsidiarity rule itself is a 'reflection' of the struggle between central institutions and national governments as well as between neofunctionalism and intergovernmentalism. Let me give a couple of examples. The Union has the power to set rules regulating common visa formats in the Union. Similarly, the Union also has the power to introduce a law regulating freedom of establishment. It is however arguable whether the Union has the power to provide common criteria or requirements for resident visas in the Member countries. Equally, it is arguable whether the Union has the power to secure 'identical' interest rates in all banks across frontiers. Neofunctionalists are unable to argue that the Union has such a power because it lies with each national government. Simply, this type of integration is better explained by intergovernmentalism. The existence of the subsidiarity rule in the SEM indicates that neofunctionalism is neither satisfactory nor fully effective.

Also, even if a competence is given by Community law, if it is not satisfactorily clear for some reasons, as I argued in various sections, the subsidiarity issue also arises. Neo-functionalism seems to fail in
predicting this type of problem, instead it assumes that the central institution has 'automatic' competence by way of spill-over to a central political body. For instance, if the Union tries to carry out a new policy it may be challenged by a Member State on the ground of subsidiarity.

The third major problem is caused by the difference in the nature of the ECSC, EEC and the SEM. The ECSC may be described as a 'one-dimensional' market because it provided only a common market for coal. However, the SEM may be described as a 'three-dimensional' because it tries to accomplish the integration of all economic sectors along with basic political integration. Haas' theory thus can be described as based on the single market for one sector, one dimensional integration. He therefore was able to argue that the integration of the coal market would spill-over into another sector, and eventually to the political sector by way of the central institution building process. However, the conditions of the SEM are different. The SEM seeks a common market for 'all' rather than just 'one economic factor'. It is natural then that an unexpected problem arises due to the multitudinousness of the SEM, the problem of association.

Not many problems in the SEM are self-contained. The problems are interwoven, often with two or three issues mixed together. For instance, border control combines with the issue of transport. The transport issue is mixed with immigration or asylum issues. The free movement of people can not be separated from taxation and lingual issues. Lingual problems are mixed with legal problems. Every problem invites another, interweaving all problems.

The problem of association is again aggravated by more reasons. Firstly, it is aggravated because of inconsistency between Union laws. The inconsistency for instance between Directive 684/92 and Article K.1(9) demonstrates this. Sometimes the Union law is incomplete, making the situation worse. The Product Liability Directive is of little use unless either, it provides a practical remedy, or makes sufficient coverage of a product by forcing the producer to join into the scheme. Therefore some
may argue that there can be a common market for producers, but not consumers in the SEM. Dega is a good example for the 'freedom of goods for the producer, not the consumer'.

The SEM is again criticised because there are huge gaps between the four basic freedoms. For instance, it is of little use for a person to have a freedom of movement unless the attached social benefits, pension for instance, are portable. The freedom of goods may not be of much use if it is not underpinned by the free movement of people. Also, the freedom of service is not effective if it is unsupported by the freedom of people and capital. Simply, one freedom fetters another, and vice versa. These gaps between the four freedoms are another dimension of the real reality of the SEM.

These aggravated problems may result partially from the unsettled principle of subsidiarity, which is a fundamental rule of Community law. Scholars cannot agree on the interpretation of this principle. For example, no one can give a conclusive answer to the question: can the Union set a deposit rate at the Union level? The Community may have competence to set 'a range of deposit rates' but not a set rate. What is then 'a range of rates'? No Member State would fully agree on the interpretation of the term, 'a range of rates' because some prefer high rates whereas others do not. This problem stems from the fact that each Member State retains sovereign control. That is to say, functional spill-over is blocked by the function of governmental power. Consequently, neofunctionalism is again found unsatisfactory on this point.

Enlargement poses another stumbling block for the Union. This is the fourth major criticism of neofunctionalism. In terms of geography, Switzerland is 'in' the Union but as a matter of Community law she is 'out'. The four main freedoms therefore are unable to be automatically transferred to Switzerland. To make matters worse, the Union has no way of resolving this issue, other than waiting for Switzerland to join. The expected economic spill-over is in suspense and political factors are
only a vision. Therefore it may be argued that neofunctionalism has failed again because there has been to date no spill-over effect between the EU and Switzerland.

It is important to ask what integration is? Is the political integration process a dependent or independent variable to economic spill-over? According to neofunctionalism, political union is an 'automatic' result, so a dependent variable of the economic spill-over by way of institution building. This means that integration in one sector will develop into the integration of another, and then eventually to political union. However, I find no spill-over effects between sectors in the SEM. For instance, the spill-over effect in goods has yet to flow into taxation which is essential to the completion of the freedom of goods as a whole. Again, the freedom of establishment in banking is only protected internally, not throughout the Union. The spill-over effect does not appear in the insurance sector either, even though bank and insurance are similar in nature. Therefore neofunctionalism again appears wanting on this point.

Another subsequent issue is whether the idea of 'acquis communautaire' can nullify nationalism within Member States. Language may not be surmountable because the issue is associated with all four fundamental freedoms in the market. Language is connected to the freedom of people, as illustrated in Groener. It is also mixed with the freedom of goods, as shown in Piageme. This again has a bearing on the freedom of service as observed in the case of Office for the Trade Mark and Patents. This suggests that the language issue is unlikely to be resolved unless all surrounding issues are resolved around the same time, which seems unlikely.

It is also important to consider 'cultural and social' identities in the SEM context. Neo-functionalism hardly considers this point considering that all factors other than economic ones are dependent variables. It focuses only on economic union and argues that political union will provide the loyalty of citizens, once Union citizenship is created automatically. However, culture is not just a dependent variable of the
integration process. It may act as an independent variable in some circumstances. As illustrated in the linguistics section; language has inclusive power. It has a tendency to develop into a, so-called, ideology and nationalism. Nationalism acts through national governments. The French case of the 1960s is an example. Again neofunctionalism fails to account for the relationships between economic, political, ideological and cultural integration.

Neo-functionalism regards central institutions, as 'bridge-heads' to political integration. This 'bridgehead argument' is suggested in the following statement: "the SEM is a trojan horse to a political Union". Behind this statement is the idea that if the central institution assumes full decision making power, it can quickly advance political integration. That is to say, where the Council acts by way of either majority or QMV, not unanimity, in all sectors, political integration is more likely. However, the real fact is that the Council does not have the full power to develop political integration because it does not apply QMV in the fiscal sector where unanimity applies. Each government clearly retains its fiscal power. Therefore the 'trojan horse' argument which provides the basis for economic bridge-head is defective.

It can be concluded that neofunctionalism remains a useful theory in the process of integration in Europe. However, the theory provides only a 'basic' guideline to the integration of all sectors. Intergovernmentalism is necessarily complementary especially where political and cultural integration is involved. It was therefore reasonable for the drafters of the SEM to have neofunctionalism in mind. However, neofunctionalism remains inapplicable in some aspects. The spill-over effect between the economic and political systems are not recognised automatically. Many political factors are in motion independently. Cultural and ideological factors are not the only dependent variables. This suggests that political Union is unlikely, at least in the near future.
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http://www.europa.eu.int/comm/eurosta....roduct=3-t3110pc-en&mode=download
Asylum applications,

http://www.europa.eu.int/comm/eurosta....roduct=3-t3010toa-en&mode=down

Long-term unemployment,

http://www.europa.eu.int/comm/eurosta....roduct=3-t3080pc-en&mode=down
F. Others

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