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EC: Harmonization by Competition

At their latest meeting in Brussels the Heads of State and Government of the twelve member countries of the European Community again confirmed their intention to achieve a common internal market in the EC according to schedule by 1992. The completion of the European internal market means that every good produced and every service provided in any member country, which can be sold and bought in that country, is also allowed to be bought without any restrictions in any other member state. In addition each person of any profession or occupation has the right to settle down or to seek employment in any of the member states, no matter which of these countries he is a citizen of (implying the same for all sorts of enterprises and companies). Last but not least, all of these individuals or enterprises are permitted to move their financial assets of whichever type freely from any place to any other place within the Community. And all this should be possible without major restrictions on competition.

As fascinating as this idea of Europe as one market for about 320 million people is, it is at the same time a nightmare to think about the question, how these seemingly simple results should be brought about. It was an illusion to believe that most of the work would have been done when the tariff barriers and the quantitative restrictions on imports had been abolished. Indeed, the step-by-step removal of customs duties within the then Community of the six was completed successfully and efficiently within the first decade of the Community's existence.

But the members of the EC were more or less highly developed, industrialized countries with long, very individual traditions as to their organisational, institutional, legal and social framework before they formed or joined the Community. Accordingly, there is a multitude of institutions, laws and regulations with regard to safety, to health and to environmental protection, to protecting the consumer in general, to protecting social achievements and to many other purposes. There are different technical standards, different tax systems and structures, different approaches to macroeconomic policies, which all have some bearing on the flow of goods, services and capital, and on the movement of persons and enterprises across the borders between member states.

The completion of the European internal market will mean a great deal of harmonization with regard to institutions, laws, regulations, technical standards, taxes and policies. How much harmonization and with what result will depend on the way in which it will be reached.

There are in principle two possible ways of getting to the final stage of the European internal market: the one is negotiation, the other is competition.

Choosing negotiations as the principal way of harmonization has many disadvantages. Given the number of issues to be negotiated we might have to wait endlessly before we reach the final stage. Moreover, in order to get results at all the member countries would have to make allowance for each other's peculiarities. In consequence, the results would more often than not be suboptimal with regard to overall economic objectives such as stability, growth and high employment, and the freedom of choice of individuals and companies would probably often be restricted more than necessary by the outcome.

Therefore the way of competition should, as far as possible, be chosen in order to reach the final stage. This presupposes that the member countries mutually consider themselves as being of age, that they are responsible enough, that what is good enough for one country cannot be disastrous for the others and that, therefore, the member countries recognize each

other's laws, regulations, standards and institutional arrangements, at least in the beginning. In many cases superior regulations will then compete away inferior regulations and so on.

This may not always be the best solution. There will be cases for mixed solutions and others for negotiations right from the beginning or after a period of competition. But in many cases mutual recognition would probably do no harm, and then competition can decide whether a superior solution exists to which countries with other solutions have to adjust, or whether some solutions are equivalent and can continue to exist side by side.

With regard to national technical standards, for example, the principle should often be valid that if a product is legally produced and permitted to be sold in one member country it may also be sold in every other member country without any restrictions. Health or security reasons may lead to certain exemptions. In such cases there is a need to harmonize the regulations or to negotiate minimum standards. In other cases it is obvious that for technical reasons there should be some common standards as soon as possible.

The formulated principle should be valid for services, too. Opening the national markets may compete away inefficient national regulations and institutions. Acknowledgement of the different national regulations is not sufficient in the case of state-owned monopolies. The Community has to avoid the exclusion of non-residents from buying from or selling to such monopolies.

A crucial precondition for an efficient functioning of the common market is an effective anti-trust policy. But it is not necessary to totally harmonize company law, for example. The EC should give up all endeavours with regard to industrial targeting, in favour of competitive markets. On the other hand, all or at least most of the targeted subsidies should be abolished.

Another example is regarding taxes. To complete the internal market it is not necessary, in general, to harmonize the tax systems, because taxes are only one factor in determining competitiveness. A need for harmonization probably exists where certain taxes, mainly on consumption, impair trade in goods and services.

Neither would there be a need for an immediate harmonization of the level of the value-added tax rates, if we switch from the country-of-destination to the country-of-origin principle, and if each member country introduced a uniform tax rate for all products. The differences between VAT rates can be taken care of by adjusting the exchange rates accordingly. Should the country-of-destination principle be upheld, a consistent prior-tax deduction procedure would have to be introduced not only at the national but also at the European level. This would have to be combined with a tax clearing system as proposed by the Commission, because every state should receive the taxes on the products consumed within its borders.

With respect to the free flow of capital all kinds of capital controls should be quickly abolished. Every individual and every company should be permitted to deposit money in any member's currency and also to take credit and to conclude contracts denominated in the currency of any member country, notwithstanding that in each country only its own currency is the legal tender.

There are fears that giving up capital controls completely would threaten the existing EMS arrangements unless the coordination of monetary policies were strengthened in advance. But there are contradictory views on what a stricter coordination of monetary policies means. Negotiations prior to giving up capital controls might lead to a system which is ultimately damaging to all member countries' performance. So, even at the risk of having to undertake more frequent and possibly also greater adjustments of exchange rates for a while, the removal of all capital controls will probably give a better lead as to what kinds of additional monetary arrangements have to be decided upon in order to arrive finally at the stage where a genuine European Federal Central Bank System will become possible, preferably with one single currency for all. This will, of course, not occur before all participants are convinced that giving up monetary sovereignty will lead to an improvement rather than to a deterioration of their economic perspectives.

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