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The double asymmetry of European integration: Or: why the EU cannot be a social market economy

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Fritz W. Scharpf

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Or: Why the EU Cannot Be a Social Market Economy

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for the Study of Societies

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Abstract

Judge-made law has played a crucial role in the process of European integration. In the vertical dimension, it has greatly reduced the range of autonomous policy choices in the member states, and it has helped to expand the reach of European competences. At the same time, however, "Integration through Law" does have a liberalizing and deregulatory impact on the socioeconomic regimes of EU member states. This effect is generally compatible with the status quo in liberal market economies, but it tends to undermine the institutions and policy legacies of Continental and Scandinavian social market economies. Given the high consensus requirements of European legislation, this structural asymmetry cannot be corrected through political action at the European level.

Zusammenfassung

Das Richterrecht hat eine entscheidende Rolle im Prozess der europäischen Integration gespielt. In der vertikalen Dimension hat es den Bereich autonomer Politik der Mitgliedstaaten wesentlich eingeschränkt und zugleich die Reichweite europäischer Kompetenzen ausgedehnt. Die „Integration durch Recht“ hatte aber zugleich auch eine stark liberalisierende und deregulierende Wirkung auf die sozioökonomischen Regelungssysteme der Mitgliedstaaten. Diese Wirkung war vereinbar mit dem Status quo der „liberalen Marktwirtschaften“, aber sie untergräbt die Institutionen und Politiktraditionen der „sozialen Marktwirtschaften“ auf dem europäischen Kontinent und in Skandinavien. Angesichts der hohen Konsenshürden der europäischen Gesetzgebung kann diese Asymmetrie nicht durch politisches Handeln auf der europäischen Ebene überwunden werden.

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The conclusion that, in a federation, certain economic powers, which are now generally wielded by the national state, could be exercised neither by the federation nor by the individual states, implies that there would have to be less government all round if federation is to be practical (Friedrich A. Hayek 1948 [1939]).

Will history repeat itself? The ideological hegemony of orthodox liberalism ended with the Great Depression of the 1930s, and it may well be that the current global crisis will also end the quarter-century of triumphant neoliberalism not only in Obama's America and in the International Monetary Fund, but also in the European Union. And in fact, after decades of cheap talk about the "social dimension" of European integration or the superiority of the European social model over American capitalism, Christian Democrats and Social Democrats have finally managed to write the commitment to create a European social market economy into the hard letter of Art. 3 (3) of the Lisbon Treaty on the European Union. So the *finalité* of the European political economy is going to be redefined by the ideas that have shaped the socially inclusive and institutionally coordinated social market economies (SMEs) on the Continent and in Scandinavia, rather than by the liberal market economies (LMEs) of the Anglo-Saxon countries and some of the new member states. Or so one might think.

F.A. Hayek, however, the doyen of market liberalism, would have disagreed. Writing in 1939, in the heyday of post-Depression (i.e. Keynesian) economics and politics and before the beginning of the war that would leave Europe in shambles, he anticipated postwar European integration. And he was sure that integration would be good for market liberalism – not because of any hopes for its renewed ideological hegemony, but because it would reduce the institutional capacity of the state to govern the capitalist economy and to burden it with a large welfare state. Hayek's insights were never lost on his neoliberal followers who supported European integration not so much on economic than on normative-political grounds (e.g., Mestmäcker 1988; Buchanan 1995/96). But it seems that they were neither understood by the Christian and Socialist "founding fathers" of European integration – the Schumans, DeGasperi, Adenauers and Spaaks – nor by subsequent generations of "good Europeans" in politics, trade unions and academia whose ideological preferences or manifest interests were quite opposed to unfettered market liberalism.

One reason is that the liberalization that Hayek foresaw was slow in coming. He had assumed that political integration would come first, and that a strong federal government would then create a common market and centralize the policies that could interfere with it. At the same time, however, conflicts of interest among member states were supposed to prevent the creation of a strongly redistributive welfare state whose burdens

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would fall unequally on economically strong regions. In Europe, however, the historical sequence occurred in reverse order, with political integration postponed after the European Defense Community failed in 1954. The European Economic Community began as a customs union whose members were committed to creating a successful common market that they hoped would eventually facilitate political integration as well. In the meantime, the EEC attempted to remove barriers to trade through intergovernmental negotiations, while its member states took charge of social regulations, social transfers, public services and public infrastructure functions.

For more than two decades, this *de facto* division of functions between the Community and its member states remained essentially intact. And as long as that was true, there was little reason to worry about the impact of European integration on the interests and values that were served by the existing domestic socioeconomic regimes. Since the early 1980s, however, economic integration has accelerated and intensified and the liberal transformation which Hayek had expected has indeed been taking place in the multi-level European polity. For the Continental and Scandinavian social market economies, this transformation has become increasingly disruptive, and it is important to understand its causes. Was it brought about by the political dominance of certain (neoliberal) ideological preferences, in which case there might still be hopes for a political reversal? Or was it the belated but inexorable consequence of the structural factors associated with the integration of heterogeneous nation states that Hayek postulated?

In the literature, the most influential attempts to explain European liberalization refer to the interests, ideologies and strategies of influential political actors. In Andrew Moravcsik's (1998) account, every step that has deepened economic integration and liberalized regulatory regimes is explained by the (primarily economic) interests and preferences represented by governments of the larger member states. By contrast, Nicolas Jabko (2006) attributes the surge of liberalizing legislation to the Commission's "strategic constructivism," which persuaded a heterogeneous coalition of political actors that "the market idea" was the solution to all that was wrong in Europe. At the time however, unanimity was still the decision rule of the Community. So some of the smaller member states could easily have blocked initiatives serving the interests of the big three, and there surely must also have been veto players who were not lured by the pied pipers of neoliberalism. So why didn't these dogs bark?

The basic difficulty with both of these explanations, interest-based or ideological, is that they focus exclusively on the agency of purposeful actors while ignoring the (institutional) structure within which actors must define their strategic choices (Giddens 1984). They try to explain Treaty revisions and legislative action by reference to the interests, preferences, worldviews and strategies of actors in national governments, the Commission and the European Parliament while ignoring or downplaying the effect of formal and informal decision rules and the impact which judicial decisions have on the available options of political actors. Instead, structure and agency should be considered as complementary rather than mutually exclusive, explanatory approaches (Scharpf

1997). In the highly structured European policy processes, decision rules – and, more generally, institutions – are bound to create strong asymmetries, favoring some actors and some policy goals, and impeding or obstructing others.¹

The present essay will explore the impact of two institutional asymmetries: the first one favoring policy-making by nonpolitical actors and impeding political action at the European level, and the second one favoring negative integration and impeding specific policies of positive integration (Scharpf 1999: ch. 2). These institutional asymmetries, I will then try to show, have the effect of undermining the institutions and policy legacies of “social market economies” at the national level, and they also impede efforts to re-create similar institutions and policies at the European level.

1 Integration through politics and integration through law

The first of these asymmetries concerns the relationship between legislative and judicial powers in the processes of European integration. In the original allocation of functions, European integration was to be achieved either by intergovernmental agreement on amendments to the Treaties or by European legislation initiated by the Commission and adopted by the Council of Ministers. As a consequence, member governments retained control over the extent and the speed of economic unification and liberalization.² After

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- 1 Some readers have suggested that by focusing exclusively on structural conditions, the following text seems to argue not for a balance between structure and agency, but for a structural determinism that leaves no room for the potential of creative agency. The short response is that my purpose here is to make actors more aware of the structural obstacles they would have to overcome if they tried to create a European social market economy. At a more theoretical level, what I will describe here is a pattern of distributed competences but interdependent policy choices. Of course, the Court could have chosen different interpretations of the Treaties, and the Commission, the Council, the Parliament, political parties and organized actors could have responded differently to the evolution of the case law and to opportunities for Treaty revision. If all these choice options could have been combined and employed in a concerted fashion, the overall process of integration could of course have taken a very different direction. But such instances of “positive coordination” are extremely demanding and very rare even in the hierarchical organization of a national government (Mayntz/Scharpf 1975: 145–150; Scharpf 1997: 112–114, 132–135). In the constellations of EU policy making, however, multiple actors with differing worldviews are pursuing different goals. Hence the far more likely outcome is “negative coordination,” where each actor considers only its own, limited competences and tends to treat the positions of others as given when assessing its own strategic options. In other words, the structural constraints are mutually created and reproduced by strategic actors with distributed powers and non-holistic action perspectives.
 - 2 This is not so in the field of competition law, including the control of “public undertakings,” “services of general economic interest” and of “state aids” (Arts. 81–98 ECT), where the Commission may intervene directly against distortions of competition – leaving it to the affected parties to appeal to the Court.

tariff barriers had been removed, further progress on the removal of non-tariff barriers was to be achieved through the legislative harmonization of national rules. Thus governments would decide when trade would be liberalized and for which products; when controls over capital movements would be lifted and to what extent; which conditions would permit workers to seek employment and firms to provide services or establish undertakings in another member state, and so on. Since the Luxembourg Compromise of 1966 had prolonged the practice of unanimous decision-making, all governments could be sure that no legislation could remove existing economic boundaries without their agreement (Palayret et al. 2006). As long as this condition went unchallenged, member states could also control the interaction effects between economic liberalization and the functional requirements of their nationally bounded welfare states, their systems of industrial relations, and their public revenue, public services and public infrastructure functions. In other words, the member states could ensure that even in the EEC, economic integration would not exceed the limits of what John Ruggie (1982) described as the “embedded liberalism” of the postwar world economy – that is, a regime in which markets would be allowed to expand within politically defined limits that would not undermine the preconditions of social cohesion and stability at the national level.

Initially, moreover, these preconditions were fairly similar in the Original Six, all of which had fairly large Bismarckian-type pension and health care systems that were primarily financed by wage-based contributions. They also had highly regulated labor markets and industrial-relations systems, and all had a large sector of public services and infrastructure functions that were either provided directly by the state or in other ways exempted from market competition. Since France had also succeeded in gaining Treaty protection for its more stringent rules on gender equality in the workplace while agriculture was to be organized in a highly regulated, subsidized and protectionist regime, disagreement on the pace of integration in the competitive sectors of the economy was relatively moderate. All that changed, of course, with the first enlargement, which brought the UK, Denmark and Ireland into the Community – and thus member states with very different types of liberal and social democratic welfare states and labor relations (Esping-Andersen 1990), different agricultural interests and, in the case of Ireland, a very different state of economic development. At the same time, moreover, the world economy was shaken by the first oil-price crisis, and while all national economies were in deep trouble, they diverged widely in their sometimes protectionist responses to the crisis (Scharpf 1991).

As a consequence of the greater diversity of member-state interests and preferences, the harmonization of national rules through European legislation became more difficult. And as European markets continued to be fragmented by incompatible national product standards and trade regulations, it seemed that legislative integration might not progress much beyond the customs union that had been achieved in the first decade. In the face of political stagnation, therefore, hopes turned to the possibility of judicial solutions that might bypass political blockades in the Council. This presupposed that the European Court of Justice (ECJ) would be willing and able to engage in large-scale

judicial legislation. It would have to interpret the unchanged text of the Treaties in ways that would propel European integration beyond the frontier that had been reached under the high consensus requirements of political legislation.

The doctrinal groundwork for this option had already been laid in the early 1960s by two bold decisions of the Court. The first one interpreted the commitments that member states had undertaken in the Treaty of Rome not merely as obligations under international law but as a directly effective legal order from which individuals could derive subjective rights against the states.³ The second one asserted the supremacy of this European legal order over the law of member states.⁴ With these decisions, the Court claimed a status for Community law that differed fundamentally from that of all other international organizations. Why and how they came to be accepted has become a fascinating research question.⁵ The most convincing explanation focuses on the response of national courts to the referral procedure of Art. 234 (ex 177) ECT.⁶ The option of requesting the preliminary opinion of the ECJ on issues requiring the interpretation of European law had the effect of empowering ordinary national courts in the course of ordinary litigation to review the validity of national legislation – which may have been particularly attractive for lower-court judges.⁷ Moreover, as Burley and Mattli (1993: 44) and Maduro (1998: 11, 16–25) have pointed out, acceptance by national courts and academic lawyers was facilitated by the Court's strict adherence to a style of formal reasoning that emphasized logical deduction from legal principles (even if these had originally been self-postulated) rather than the analysis of substantive economic or social problems or policy goals that might justify the particular interpretation.

The strategy of using law “as a mask for politics” (Burley/Mattli 1993: 44) also helped to immunize judicial legislation against political objections. In cases referred to the ECJ, the government whose laws were challenged was not necessarily directly involved as a litigant, and if it was, it was bound to present its objections within the court-defined frame of legal reasoning. Since the Court tended to announce far-reaching doctrinal innovations in cases with low or even trivial substantive importance, it would have been difficult or impossible to mobilize political opposition against the Court's jurisprudence at the national level, let alone the European one. Yet once the “habit of obedience” (Maduro 1998: 11) was established, European law, as interpreted by the ECJ, was woven into the fabric of the law of the land, which ordinary national courts apply in ordinary litigation. To challenge an ECJ ruling, then, governments would have to confront their

3 *Van Gend & Loos*, C-26/62, 5.2.1963.

4 *Costa v. Enel*, C-6/64, 15.7.1964.

5 See for example Burley/Mattli (1993); Garrett (1995); Mattli/Slaughter (1995); Slaughter et al. (1998); Alter (2001); Stone Sweet (2004).

6 Haltern (2007: 187) calls it the “crown jewel among European procedures of legal protection without which a European rule of law would be unimaginable.”

7 Where judicial review exists nationally and is exercised by the highest court or a specialized constitutional court, it may be envied by lower-court judges. It makes sense, therefore, that there are fewer referrals from member states without a tradition of judicial review – and with a strong tradition of majoritarian democracy (Wind et al. 2009).

own judicial system and renounce the respect for the rule of law on which their own legitimacy depends (Halter 2007: 192–194). For all intents and purposes, therefore, ECJ interpretations of European law are now “higher law” in the member states.

The effectiveness of the Court’s judicial legislation is also greatly enhanced by the extreme difficulty of a political reversal. At the national level, courts and constitutional courts are of course also involved in law-making through interpretation. But judicial interpretations of a statute may be corrected by simple majorities in parliament, and even interpretations of constitutional law could usually be revised by qualified parliamentary majorities. By contrast, ECJ decisions based on primary European law could only be reversed by Treaty amendments that need to be ratified in all member states. And decisions interpreting secondary European law cannot be corrected without an initiative of the Commission that needs the support of at least a qualified majority in the Council, and usually an absolute majority in the European Parliament. Given the ever increasing diversity of national interests and preferences, such corrections were and are in theory improbable and in practice nearly impossible. In other words, ECJ interpretations of European law are much more immune to attempts at political correction than is true of judicial legislation at the national level.

By the early 1970s, the basic foundations of judicial power had been built, and the ECJ could begin to expand its domain. In the 1960s, it had only intervened against national violations of unambiguous prohibitions in the Treaty and against protectionist measures that were clearly designed to prevent the market access of foreign suppliers. In 1974, however, a much wider claim was asserted in the *Dassonville* formula which interpreted Art. 28 (ex 30) ECT. This article prohibited “quantitative restrictions on imports and all measures having equivalent effect.” In the Court’s view, this now meant that “all trading rules enacted by member states which are capable of hindering, directly or indirectly, actually or potentially, intra-community trade are to be considered measures having an effect equivalent to quantitative restrictions.”⁸ Under this formula, any national rules and practices affecting trade could now be construed as non-tariff barriers to trade. It was no longer necessary to assert that they served protectionist purposes or discriminated against foreign suppliers, or even that any border-crossing transaction was involved at all. A *potential* impediment would suffice to define a national measure as having an effect “equivalent to quantitative restrictions” on trade.

Given the practically unlimited sweep of the definition, the existence of a “potential impediment” to the exercise of European economic liberties would not, as such, be a disputable issue in future decisions. But the Court also came to realize that the *Dassonville* formula was too wide to be enforced as a strict prohibition in all cases where it might apply. Instead of narrowing the excessive reach of the prohibition, however, the famous *Cassis* decision⁹ introduced a doctrinal solution that allowed much more flexible con-

8 C-8/74, 11.7.1974 at # 5.

9 C-120/79, 20.2.1979.

trols over the content of national policy choices. The textual base was found in Art. 30 (ex 36) ECT, according to which even quantitative restrictions could be applied if they served certain specified public-policy purposes, such as “public morality, public order or public security; the protection of health and life of humans, animals and plants ... etc.,” provided that these would not “constitute a means of arbitrary discrimination or a disguised restriction on trade between the Member States” (Art. 30 [ex 36] ECT).¹⁰

On the face of it, however, Art. 30 ECT did not appear very flexible: its somewhat casuistic list could be interpreted to completely exempt national rules that served one of the specified policy purposes from the reach of Art. 28 ECT. Since the regulation in question – a German law specifying the minimum alcohol content of liqueurs – had been presented as a measure protecting human health, and since it applied to domestic and imported goods without discrimination, that might have been enough to settle the case. In order to avoid this outcome, the Court had to reinterpret the language of Art. 30 ECT.

The first step was to replace the closed list of exemptions specified by the Treaty with its own open-ended formula, according to which “obstacles to movement within the Community ... must be accepted insofar as those provisions may be recognized as being necessary in order to satisfy mandatory requirements relating in particular to the effectiveness of fiscal supervision, the protection of public health, the fairness of commercial transactions, and the defense of the consumer.”¹¹ In this new formula, the specific exemptions granted by the Treaty were reduced to the status of justifications which “may be recognized as being necessary in order to satisfy” one of the Court-defined “mandatory requirements.” And finally, in case the national regulations could not be so justified, the Court announced a new rule of “mutual recognition” stipulating that products “lawfully produced and marketed in one of the member states” must be allowed in the national market.

By adding new justifications (“fiscal supervision,” “defense of the consumer”) that had no basis in the text of Art. 30 (ex 36) ECT and by introducing the new list with “in particular,” the Court had visibly gone beyond the outer limits of text-based Treaty interpretation and asserted its claim to share the Treaty-amending powers of the unanimous member states. But it had done so in a way that was unlikely to provoke political opposition, since it seemed to widen, rather than restrict, the domain of permissible member-state legislation. Moreover, by extending the range of possible exceptions, it introduced a degree of flexibility without having to correct the sweeping *Dassonville* prohibition of all national regulations or practices that might hinder the exercise of Treaty-based liberties.¹² And it did so by establishing a procedural asymmetry between

10 Similar exemptions are specified in Arts. 39, 43, 46, 58 ECT.

11 C-120/78, 20.2.1979 at # 8.

12 A correction, limited to the free movement of goods, was later introduced in *Keck and Mithouard* (C-267/91 and C-268/91, 24.11.1993), where the Court distinguished between rules that might hinder the access of foreign products to the national market and rules “specifying selling arrangements” to which only a discrimination test should be applied.

rule and exception: if an impediment to the exercise of European liberties is alleged, the Court takes judicial notice of its potential effect – which then establishes the rebuttable presumption of a Treaty violation. The presumption may be rebutted, however, if the member state is able to justify the measure in question by reference to one of the “mandatory requirements” accepted by the Court. Yet being treated as exceptions from the general rule of free trade, these requirements are to be narrowly interpreted. And even if that hurdle is overcome, the measure in question must still pass the Court’s “proportionality” test – where the burden of proof is on the member state¹³ to show that its regulation will in fact achieve the alleged purpose, and that the same policy goal could not also be realized by other measures that would restrict trade to a lesser degree.¹⁴

As a consequence, the *Cassis* formula¹⁵ maximizes the Court’s quasi-discretionary control over the substance of member-state policies. Even in policy areas where no powers have been delegated to the European Union, it is for the Court, rather than for national constitutions and national democratic processes to determine the legitimate purposes of national policy. And it is for the Court, rather than for national governments and legislatures to judge the effectiveness and necessity of measures employed in the pursuit of allowable policy purposes (Halter 2007: 741–766).

The *Dassonville* and *Cassis* doctrines were subsequently extended from free trade to free service delivery, free establishment, free capital movement, and the free mobility of workers (Oliver/Roth 2004).¹⁶ In a similar process, moreover, European competi-

13 Dorte Martinsen (2009) has shown that the increasing liberalization of transnational access to national health care has largely been achieved by tightening the evidentiary standards for proving the “proportionality” of restrictive rules.

14 In *Cassis* the Court held that the German regulation was not *effective* in serving its alleged public-health purpose, and that it was not *necessary* for achieving its alleged consumer-protection purpose (which might also have been achieved by less burdensome labeling requirements).

15 The formula found its definitive and more abstract expression in the *Gebhard* case (C-55/94, 30.11.1995), where, with regard to the freedom of establishment, the Court postulated that national regulations that “are liable to hinder or make less attractive the exercise of a fundamental freedom guaranteed by the Treaty” must fulfill four requirements: “they must be applied in a non-discriminatory manner; they must be justified by imperative requirements in the general interest; they must be suitable for securing the attainment of the objective which they pursue; and they must not go beyond what is necessary in order to attain it.”

16 There are, however, interesting differences among these liberties with regard to the type of national regulation that the Court will never allow as a “mandatory requirement.” When the free movement of capital and persons is an issue, the court will generally not accept revenue and budget concerns as an imperative requirement (Schmidt 2007, 2009c). For the trade in goods, regulations of product qualities may be justified, whereas regulations of the conditions of production could never justify a restriction on imports. For services, however, where production and consumption will often occur *uno actu*, regulations of the qualifications of service providers and the process of service provision could massively affect the quality of the service itself. Hence they could not generally be denied the status of a justifiable “mandatory requirement.” This explains why the Bolkestein proposal of a services directive met with massive opposition when it postulated the mutual recognition of regulations adopted and implemented in the country of origin as a general rule.

tion law has been extended to promote the access of private providers to the *service-public* and infrastructure functions that member states had previously excluded from the market or protected against unfettered competition (Smith 2001; Biondi et al. 2004; Grossman 2006; Ross 2007; Damjanovic/de Witte 2008). In principle, therefore, no area of national law, institutions and practices remained immune to the potential reach of European economic liberties and the rules of undistorted market competition.

In other words, by the end of the 1970s, European integration had reached a highly asymmetric institutional configuration: Attempts to remove national barriers to trade through legislative harmonization continued to be severely impeded by the “joint decision trap” (Scharpf 1988, 2006), whereas “Integration through Law”¹⁷ was able to move forward without political interference through the seemingly inexorable evolution of judicial doctrines protecting and extending the Treaty-based rights of private individuals and firms. As I will argue in the next section, however, this asymmetry between judicial and legislative action also had a powerful impact on the capacity for, and the direction of, European political legislation.

2 Judicial deregulation and legislative liberalization

Substantively, the main thrust of judicial action is to extend the reach of “negative integration” (Scharpf 1999). To understand this, one must realize that integration through law could only be achieved because, ever since *Van Gend & Loos* (C-26/62, 5.2.1963), the Court had reinterpreted the commitments of member states to create a common market as subjective rights of individuals and firms against these member states.¹⁸ Without this reinterpretation, the doctrine of “direct effect” could hardly have been invoked by private litigants in national courts, from where they would reach the European Court of Justice through the preliminary reference procedure (Art. 234 ECT). And without these private “enforcers” (Kelemen 2003), European law could never have achieved its present scope and effectiveness. This has a powerful effect on the substantive direction of the ECJ’s case law.

17 This was the title of a large-scale research and multi-volume publication project coordinated at the European University Institute, Florence. See Cappelletti et al. (1985). On the support which this concept had received early on from an enthusiastic Euro-law community, see Vauchez (2008) and Alter (2009: ch. 4).

18 Remarkably, in two early (and very integration-minded) German commentaries on the Treaty of Rome, there is no suggestion of judicially enforceable subjective rights. What is emphasized is the empowerment of the Council to adopt directives that will allow the free movement of goods, persons, services and capital, as well as free establishment (von der Groeben/von Boeckh 1958; Meyer-Marsilius 1960). At the same time, however, relatively small Euro-law associations collaborated with the Court to invent, develop, publicize and propagate the legal concepts that were used in this transformation of Treaty commitments into constitutionally protected basic rights (Vauchez 2008; Alter 2009: ch. 4).

First, the questions the Court will receive and the cases it will see must inevitably constitute an extremely skewed sample of all the interest constellations that are affected by European integration. They will reflect the interest of parties who have a major economic or personal stake in increased factor or personal mobility, and who also have the financial and organizational resources¹⁹ to pursue this interest by seeking judicial redress against national laws and regulations (Conant 2002; Kelemen 2003). What the Court will not see, however, are cases promoting the interests of the less mobile majority of European individuals and firms (Fligstein 2008) and, even more significantly, cases representing the interests that benefit from existing national laws and regulations. Since a favorable decision will encourage other parties to exploit the newly granted liberty from national regulation, and to push for its extension to other areas, the evolution of the case law will not tend to a stable equilibrium in which opposing interests are fairly accommodated (as in the common law of contracts, which can be expected to generate a stable balance between the interests of buyers and sellers). Instead, and independently from any liberal preferences the judges might entertain, its dynamic expansion will be driven by the persistent push of liberalizing interests searching for new obstacles to remove²⁰ (Schmidt 2009b).

It needs to be said, however, that “liberalization” is not necessarily to be understood in a market-liberal or neoliberal sense. Given the dominant focus of the Treaty of Rome on economic integration, it is of course true that most of the Court’s case law responds to the economic interests of business enterprises and capital owners. At the same time, however, the Court has, from early on, protected the social rights of migrant workers against discrimination on grounds of nationality, and it has expanded the guarantee of equal pay for men and women (Art. 141 ECT) into a workplace-oriented regime of gender equality (Cichowski 2004). In highly innovative – or even “artistic” (Hilpold 2008) – decisions, it has also approximated the status of mobile students to that of migrant workers and, in the case enforcing access to *Austrian* universities,²¹ it has even ruled that Austrian taxpayers should pay for the education of German medical students who did not qualify for admission at home. At the same time, the (active and passive) freedom of service provision was used to allow the access of foreign providers to domestic health care systems, and to require that patients seeking ambulatory and stationary health care abroad should be reimbursed by their national systems (Martinsen/Vrangbaek 2008; Martinsen 2009). In the meantime, moreover, the combination of EU citizenship, freedom of movement and nondiscrimination on grounds of nationality is

19 As Lisa Conant (2003) has shown, even consumer interests in liberalized air services could not get a hearing before the Court until major air carriers became interested in opening national markets.

20 Progress may of course come late in some areas, and slow down temporarily in others. But given the constitutional status of Treaty interpretations and the steadying influence of judicial precedents and legal discourse, the overall development is likely to be shaped by the unidirectional effect of a “ratcheting mechanism.”

21 C-147/03, 7.7.2005.

used to minimize national residency requirements that would limit migrants' access to national welfare systems (Wollenschläger 2007; Egger 2008).

Thus it is indeed true that the rights-based case law of the ECJ is expanding into new areas where its evolution is not, or not primarily, driven by the economic interests of big firms and capital owners (Caporaso/Tarrow 2008). In that sense, "liberalization" should now be treated as a generic term describing mobility-enhancing policies that may serve economic as well as noneconomic interests. But that should not be interpreted as progress toward the social embeddedness of the European economy or as the judicial recognition of the values of social solidarity. Instead, effective systems of social solidarity – which presently exist only within member states – may in fact be undermined if the legitimating assumptions of a basic reciprocity of rights and obligations are weakened (Menéndez 2009). Similarly, European citizenship, as defined by the Court, is not about collective self-determination. It is about individual rights of exit from, and entry into, democratically shaped and collectively financed systems of national solidarity (Somek 2008). For the new social liberties as for economic liberties, therefore, integration through law maximizes negative integration at the expense of democratic self-determination in the national polity.

Of even greater importance is a second structural effect. Given its rights-based interpretation of Treaty obligations, the only remedy the Court can offer to the complaints of private litigants is to disallow national regulations that impede factor mobility or personal mobility or that violate standards of nondiscrimination. Hence the immediate effect of such decisions is to deregulate existing national regimes. What the Court cannot do is establish a common European regime that would respond to some of the values and policy purposes which, as a consequence of its decisions, can no longer be realized at the national level.²² If reregulation should be considered desirable, it could only be pursued through political legislation at the European level. And given the high consensus requirements of European legislation and ubiquitous conflicts of interest among extremely heterogeneous member states, one would indeed expect a strong asymmetry between judicially imposed negative integration and legislative positive integration (Scharpf 1999).

However, that is only part of the story. In fact, the *Dassonville-Cassis* line of ECJ decisions has become a most powerful force for the revitalization of European legislation – and it also continues to shape the substantive direction of political action at the European level. To appreciate this effect, however, one must take a closer look at the impact of the ECJ's case law on the policy options of national governments.

On their face, the Treaty-based liberties are explicitly worded to apply only to national measures affecting trade and free movement between member states or other border-

22 Maduro (1998: 61–78) suggested that the Court, in a spirit of "majoritarian activism," may have achieved a degree of "judicial harmonisation" by upholding national regulations if they agreed with those adopted in most other member states.

crossing transactions (e.g., Arts. 3[1][a], 3[1][c], 56[1] or 81[1] ECT). In the Court's practice, however, this textual constraint is not generally respected (Oliver/Roth 2004: 429–434). This ambivalence may, as Maduro (1998: 158–161) argued, reflect an unresolved normative conflict between an understanding of European economic liberties as safeguards against protectionism or as fundamental principles of a neoliberal or ordoliberal “economic constitution.” In positive law, however, the ambivalence also seems to have its roots in the wide sweep of the *Dassonville* formula. If national rules with merely *potential* border-crossing effects can violate European liberties, these rules may be (and are in fact) challenged in cases which involve no border-crossing transactions at all. Where that is so, the decision must logically apply to domestic transactions as well.²³ And even if Court-defined liberties and competition rules were only applied to border-crossing transactions, the removal of national boundaries through negative integration would still have a major impact on the capacity of member states to shape their internal regimes in accordance with their own political preferences.

The reason is that, in *Cassis*, the Court had also announced the rule of “mutual recognition.” If a national impediment to trade did not fit the Court's list of allowable “mandatory requirements,” or failed to pass its “proportionality” test, it could no longer be applied to exclude imports. Hence, the member state would have to open its internal market to all products that were lawfully produced and marketed in their country of origin, but it was free to maintain the rule for domestic producers. As a consequence, products complying with potentially very different legal requirements would be competing in the same market, and domestic suppliers might suffer from “reverse discrimination” favoring competitors from locations with less burdensome rules. In countries with high standards, one could thus expect administrative difficulties, economic displacement effects and political pressures from disadvantaged national producers (Schmidt 2007; Nicolaïdis 2007; Maduro 2007). In other words, “integration through law” would directly or indirectly undermine the capacity of member states to shape the conditions of production and consumption in their own markets according to national political preferences.

Once this was understood, however, the *Cassis* doctrine also changed the bargaining constellation and incentives that member states faced in the processes of European legislation. While in the past national law had remained in force²⁴ as long as governments did not agree on a harmonization directive, the new default condition would now be

23 In the *Volkswagen* law case (C-74/07, 23.10.2007), for instance, the rule establishing a blocking minority of 20 percent (rather than the more usual 25 percent) was seen as a *potential* deterrent to foreign direct investment, and hence to free capital movement. If this was so, the rule could of course not remain in force for German investors alone. In *Cassis*, by contrast, the minimum alcohol requirement for liqueurs (which was seen as an *actual* constraint to imports) might have been maintained for domestic producers – and then might have been challenged as “reverse discrimination.”

24 This would not be so in areas over which the Community has exclusive competence, so that national solutions are ruled out even if there is no agreement on European legislation (Haltern 2007: 113–118).

“mutual recognition.” This, at any rate, was the interpretation that the Commission began to spread in its early “communications” (Alter/Meunier-Aitsahalia 1994). Rather than waiting for appropriate cases to reach the ECJ through referrals from national courts, the Commission also stepped up its prosecution of Treaty infringements (op. cit.: 548; Stone Sweet 2003: 40). The immediate effect of the Court’s decisions, the Commission’s communications, and the actual or threatened infringement prosecutions was to create an atmosphere of legal uncertainty in which the continued viability of a wide range of national regulations was thrown into doubt (Schmidt 2008).

The Commission responded to this (largely self-created) uncertainty with reform proposals that would reempower integration through political legislation. Its white paper on “Completing the Internal Market” (Commission 1985) specified a strategy for more rapid legislative integration on which a diverse coalition of economic interests and political actors could converge. The campaign culminated in the Single European Act (SEA) of 1986 which, in Art. 95 ECT, reduced the consensus requirements of political action by introducing qualified-majority voting in the Council for measures serving the completion of the Internal Market.

The literature explains the success of these reform proposals and the dramatic increase in the volume of liberalizing legislation either by the liberal preferences of the British, French, and German governments in the mid-1980s (Garrett 1992, 1995; Moravcsik 1998) or by the Commission’s ideological entrepreneurship, which sold the market idea as a general solution to Europe’s problems (Jabko 2006). I see no reason to exclude these factors from an overall explanation. But they pay inadequate attention to the extent to which the *Dassonville-Cassis* line of recent ECJ decisions had undermined the veto positions of member states that had previously opposed European legislation. Faced with the prospect of haphazard judicial interventions against existing national regulations, and with the threat of Treaty-violation prosecutions launched by the Commission, the relaxation of the unanimity rule to facilitate the adoption of common European standards must have appeared as a lesser evil. This is by now well understood (Stone Sweet 2003, 2004; Schmidt 2009a, 2009c; Alter 2009). What is less obvious, however, is the effect of judicial decisions on the substantive direction of subsequent European legislation.

Nevertheless, the Single European Act and subsequent Treaty amendments have not only established new legislative competences of the Community; they have also launched an increasing volume of effective European legislation in areas where national competences have been constrained by the Court. Some of this legislation, it is true, merely systematizes and regularizes the case law and thus contributes to more transparent negative integration. But in quite a few areas, such as work safety, consumer protection and environmental protection, European legislation has adopted rather demanding standards that represent impressive achievements of positive integration. At the same time, there are other areas, such as capital taxation or industrial relations, where the Court’s protection of economic liberties prevents action at the national level, but where neither liberalizing nor regulatory legislation could be adopted at the European level.

The question of how these cross-sectional differences might be explained ought to be high on the research agenda of European legislative studies.²⁵ Since all legislation will at least require qualified majorities in the Council, one should certainly expect that the degree of harmony or conflict among the original interests and preferences of national governments will make a difference. But how these preferences will affect the legislative outcome is greatly influenced by the jurisdiction of the ECJ and, in particular, by differences in the application of the *Cassis* formula.

In policy areas where the general drift of the case law has been hostile to national regulations, the default condition of political negotiations is the rule of “mutual recognition.” This will undermine the bargaining power of opponents to liberalization, and the Commission may then be encouraged to propose a liberalizing directive that consolidates and generalizes the accumulated case law.²⁶ A case in point appears to be the recent proposal of a directive that summarizes ECJ decisions on the rights of patients to be reimbursed for health care obtained abroad.²⁷ But the Commission may also be tempted to exploit its greater bargaining power by proposing a directive that pushes liberalization beyond the front lines that had already been secured by the Court. When that is the case, the affected interests may mobilize political resistance in the Council and in the European Parliament, and the liberalization directive may fail or be reduced to a level significantly below the Commission’s aspirations.

This seems to have happened to the “takeover directive” where the Commission had relied on the early “golden-shares” decisions of the ECJ to propose a radical liberalization of the market for company control, only to see it rejected by the European Parliament in 2001. The directive that was finally adopted in 2004²⁸ was much more limited in its ambitions. But in the meantime, liberalization has gone beyond this directive in the subsequent case law of the ECJ (Roth et al. 2008). The pattern was repeated in the case of the “services directive,” where the version originally proposed by Commissioner Bolkestein was held up in the European Parliament and could only be passed in a version that excluded a range of public and social services and did not install the “country of origin” rule (Schmidt 2009c).²⁹ But the Treaty-based case law itself could not be reversed by legislation, and the Commission relies on it in its new proposal on cross-border health care that tries to recover some of the ground lost by Bolkestein. Similarly, recent ECJ decisions have demonstrated that the “posted workers directive”³⁰ does not prevent the

25 Gerda Falkner at the Austrian Academy of Sciences (www.eif.oeaw.ac.at) is presently directing a project that will record and compare the progress of European legislation across a wide variety of policy areas.

26 As Susanne Schmidt (2000) has shown, such directives may be strongly supported by (former) high-regulation states whose markets the Commission had previously opened through infringement prosecutions.

27 COM (2008) 414 final. See Martinsen/Vrangbaek (2008).

28 Directive 2004/25/EC.

29 Directive 2006/123/EC.

30 Directive 96/71 EC.

Court from invoking the Treaty-based freedom of services provision to strike down wage regulations that had been considered allowable under the directive.³¹ Moreover, in fields like corporate taxation or industrial relations, where it seems obvious that both more liberalization and more harmonization would be politically unfeasible, the Commission may just leave the matter entirely to the continuing progress of the Court's case law (Ganghof/Genschel 2008).

In other words: The liberalizing effect of judicial decisions may be systematized and perhaps radicalized by European legislation. But given the constitutional status of ECJ decisions interpreting Treaty-based liberties, political attempts to use legislation in order to limit the reach of liberalization are easily blocked by the veto of "liberal" governments and, in any case, could not bind the Court and are likely to be frustrated by the subsequent evolution of the case law.

The game is different, however, in areas where the Court has, at least in principle, accepted the legitimacy of national policy purposes, and where some national rules interpreted as impediments to free movement or distortions of competition would also survive its proportionality test – which was most likely for product regulations protecting the health and safety of consumers and workers or the environment. Where that is the case, the Commission could only remove these impediments by proposing directives that would harmonize national rules under Arts. 95 or 96 ECT. But under these conditions, the bargaining constellation is reversed. Now member states with high regulatory standards could defend the status quo by vetoing proposals that do not achieve the same level of protection. Moreover, the Treaty itself instructs the Commission to aim at a "high level of protection" in proposals "concerning health, safety, environmental protection and consumer protection" (Art. 95 [3] ECT) – which may legitimate policy activists among the Commission staff to come up with more ambitious proposals to begin with. At the same time, it seems likely that national actors responsible for environmental protection, health and safety protection or consumer protection would also prefer more effective European rules, provided that the economic pressures of regulatory competition could be neutralized. And these would at least be reduced by having common rules within the EU.³² It is in these areas, therefore, where one could expect, and does indeed find, European legislation establishing quite demanding European standards above the level of the lowest common denominator, and perhaps also above the level achieved in the median member state (Eichener 1997; Pollak 2003; Vogel 2003; Knill 2008).

31 See C-341/05, 18.12.2007 (*Laval*); C-346/06, 3.4.2008 (*Rueffert*); C-319/06, 19.6.2008 (*Luxembourg*); Joerges/Rödl (2008).

32 In addition, the weakness of cross-sectional coordination in the Council (and probably also within the Commission and among committees in the European Parliament) might leave opposing interests with less veto power than they could have exerted in interministerial bargaining or public debates at the national level. The recent regulation outlawing incandescent household lamps (EC 244/2009) might be a case in point.

3 The vertical and horizontal impact of integration by law

So where does this comparative overview of judicial and political legislation leave us? Integration through law has clearly not replaced integration through political legislation across all policy areas. On the contrary: judicial decisions did provide the crucial impulse for the relaunch of European legislation in the second half of the 1980s, and they have continued to provide a dynamic stimulus for further legislation ever since. There is no question, therefore, that the Court has pushed the domain of European law far beyond the frontiers that would and could have been reached if integration had continued to depend entirely on the processes of intergovernmental negotiations. In the vertical dimension, therefore, ranging from purely national to exclusively European governing competences, the jurisprudence of the Court has acted as a persistent and effective upward-directed force, extending the reach of European law and constraining the autonomy of national institutions and policy choices even in fields that the Treaties had explicitly excluded from the domain of European legislation.

This was possible because by postulating the supremacy doctrine, the Court assumed the status of a constitutional court in the relationship between the European Union and its member states. But in contrast to the constitutional courts of established federal states, the law it has created is not intended to identify and protect a stable balance between the mandates, legitimacy bases and functional requirements of both levels of government. It is an instrument for promoting a dynamic process of ever increasing European integration. And it is fair to say that in this commitment, the Court not only had the full support of the “Euro-law community” (Alter 2009: ch. 4), but that it was also vindicated politically by the 1992 program and subsequent Treaty amendments, from Maastricht through Amsterdam to Lisbon, which progressively widened and deepened the impact of European law.

For pro-European governments, political parties, organized interests and public media, the progressive loss of national autonomy was obviously outweighed by the real and anticipated benefits of Europeanization. But why is it then that the Constitutional Treaty was rejected by referenda in France and the Netherlands, that voter participation in European elections is falling and that the anti-European vote is rising in a growing number of member states? Why is it that the gap between elite and non-elite support for European integration is widening (Hooghe 2003; Fligstein 2008; Haller 2009) and, more specifically, why is it that solidly pro-European labor unions and center-right and center-left political parties are bewildered by a series of recent ECJ decisions which they see as exceeding the powers of the Union and interfering with national norms, institutions and policy choices that have high political salience (see, e.g., Herzog/Gerken 2008; Monks 2008; Liddle 2008; Arbeitskreis Europa 2009)?

The specific decisions, some of which also raised concern in the European Parliament (Committee 2009), had disallowed legislation intended to increase employment oppor-

tunities for the elderly,³³ required Austrian universities to admit German students who failed to qualify for medical education at home,³⁴ and subordinated the right to strike to the freedom of establishment,³⁵ the right to collective bargaining³⁶ and legislative wage determination³⁷ to the freedom of service provision, and the legislative determination of corporate governance³⁸ to the freedom of capital movement. Nevertheless, even left-leaning Euro-Law specialists considered these decisions as judicial business as usual and failed to see what the political noise was all about (see, e.g., Mayer 2009; Reich 2008).

The reason is that European integration has ceased to be an idealistic aspiration. It has become a reality whose hard-law constraints are increasingly felt in the economic, social and personal lives of citizens. And if these citizens are even dimly aware of how European law is produced, they must also realize that the familiar mechanisms that ensure political responsiveness in national politics will not protect their interests in European decision processes. At the same time, however, pro-European legal discourses and political rhetoric are still shaped by the idealistic commitment to promoting European integration against what they consider protectionist impediments and nationalistic opposition. As a consequence, there are no meaningful public exchanges between pro-European elites and national non-elites about the impact of integration on the life-worlds of ordinary citizens (V. A. Schmidt 2006). By the same token, European law has no place for discussions about the relative importance of European and national concerns.

In established federal states, by contrast, the constitutional discourse is necessarily bipolar, concerned with accommodating and balancing the equally legitimate concerns of central and subcentral levels of government. These balances differ in Switzerland, Belgium, Germany and the United States (Obinger et al. 2005), and they may also vary over time – as in America, where the rise of national powers during the New Deal and Great Society periods was followed by a reassertion of states' rights in the New Federalism of the 1980s. In all federations and in all periods, however, constitutional law and constitutional discourses have a bipolar conceptual structure in which legitimate national and subnational concerns have equal normative status.

In European law and pro-European discourses, however, there are no concepts that could identify, define and evaluate legitimate concerns of member states that should be beyond the reach of European law. The principle of “subsidiarity,” which was inserted into the Treaties at the insistence of the German *Länder*, could at best impose limits on European legislation. It was never meant to limit the judicial interpretation of Treaty-based liberties (Davies 2006). But even if this were not so, the principle focuses only on

33 *Mangold*, C-144/04, 22.11.2005.

34 *Republic of Austria*, C-147/03, 7.7.2005.

35 *Viking*, C-438/05, 11.12.2007.

36 *Laval*, C-341/05, 18.12.2007.

37 *Rueffert*, C-346/06, 3.4.2008; *Luxembourg*, C-319/06, 19.6.2008.

38 *Volkswagen*, C-112/05, 23.10.2007.

the technical effectiveness and efficiency of regulations at European and national levels, ignoring the normative and political salience of the concerns at stake. What's more, its prescriptive content becomes indeterminate when differences in the size, wealth and administrative organization of each member state affect the capacity for national solutions. What is subsidiary for Germany need not be so for Cyprus, and the national minimum wage law, which Sweden would have had to adopt in order to comply with the *Laval* decision, would have been acceptable in most member states (Schulten 2009). But it would provoke a major normative difficulty in Sweden, where wages since the 1930s have been determined exclusively by collective agreements between highly organized federated unions and employers' associations (Meidner/Hedborg 1984; Edin/Tobel 1997). In other words, European law has no language to describe and no scales to compare the normative weights of the national and European concerns at stake.

This conclusion is not contradicted by the fact that the Court, in *Cassis* and afterwards, has allowed that certain national impediments to the exercise of Treaty-based liberties might be justified by "mandatory requirements of public interest". For one thing, it is entirely up to the Court to determine which national concerns may qualify as mandatory requirements. For instance, national tax rules that might impede capital mobility can never be justified by an interest in raising revenue, even though this surely must be among the most fundamental and legitimate concerns of any government (Ganghof/Genschel 2008). And national measures serving one of the acceptable policy purposes are then subjected to a proportionality test that is procedurally skewed against national concerns. In other words, the case law does not recognize a sphere of national autonomy in which purposes of public policy and the measures through which these are to be realized should be chosen by democratically legitimated political processes. Whenever it is claimed that such measures might impede the exercise of European liberties, or might violate the prohibitions against discrimination, or might distort market competition, national institutions and policy choices are at the mercy of the ECJ's discretion, which is generally guided by a unipolar logic that maximizes Europeanization at the expense of national autonomy.³⁹ And it is hard to see how that could be different.⁴⁰

39 Generally, that is, but not in every case. In *Preussen-Electra* (C-379/98, 13.3.2001) for instance, a German law requiring networks to purchase electricity from renewable sources at prices above the market level was not seen as a distortion of competition; in the *Brenner Blockade* case (C-112/00, 12.6.2003), Austria's non-interference with a demonstration that had temporarily blocked the Alpine transit from Germany to Italy was not seen as an impediment to the free movement of goods; and in *Doc Morris* (C-171/07, 172/07, 19.5.2009) the German law requiring pharmacies to be individually owned by a certified pharmacist was not seen as a violation of the freedom of establishment. These exceptions appear puzzling to Euro-lawyers who try to identify a general logic in the case law. In my view, they are best understood as manifestations of the Court's discretionary power – which, since it can disallow national policy choices with minimal support in the letter of the law, may also allow them for unexpected reasons. By no means, however, could these exceptional decisions provide the conceptual foundation for a general, and generally fair, balance between crucial European and national concerns.

40 That is, of course, not meant to say that individual decisions could never have gone the other way – especially where they did turn on the Court's interpretation of the proportionality test. As

This relationship, moreover, has been immune to attempts at political correction. Member states had, in Art. 137 (5) ECT, explicitly ruled out EU legislation over pay, collective bargaining, strikes and lockouts, and similar prohibitions were introduced for education (Art. 149 [4] ECT), vocational education (Art. 150 [4] ECT), culture (Art. 151 [5] ECT) and health care (Art. 152 [5] ECT). But these prohibitions did not prevent the Court from disallowing national regulations of the right to strike in Sweden, of pay in Germany and Luxembourg, and of education in Austria. Within the doctrinal framework established by the case law, member states could at best constrain political legislation at the European level, but they could not prevent the Court from extending the reach of Treaty-based liberties into policy areas that the Treaty had explicitly excluded from the domain of delegated powers.⁴¹ As long as these liberties are treated as constitutionally protected fundamental rights,⁴² that conclusion cannot be challenged on technical-legal grounds.

But even if it were technically possible to construct effective hard-law limits of European law, including judge-made European law, it would still be difficult to define the policy areas where national autonomy ought to be protected. The German constitutional court tried to do so in its recent judgment on the Lisbon Treaty, by postulating limits on the potential domain of European powers that are defined by the need to protect the “constitutional identity” of EU member states.⁴³ National autonomy should prevail in areas where policy choices are specifically shaped by preexisting cultural, historical and linguistic understandings (“*Vorverständnisse*”).⁴⁴ Among these, the court included issues of language, religion, education or family law.⁴⁵ These “sociocultural” matters have admittedly not been at the core of pro-integration policies, and even in the Lisbon Treaty they are not included among the exclusive or shared powers of the Union (Arts. 3 and 4 TFEU). But these areas may well become more salient as the EU moves beyond economic integration and seeks to promote sociocultural integration among the “peo-

is true of all courts, the ECJ’s resolution of specific cases is frequently the object of controversial discussions in the legal community. But that should not obscure the structural effectiveness of the path-dependent doctrinal development: Once the supremacy and direct effect of European law had been established, it followed that all Treaty-based subjective rights and liberties would override existing national regulations. And once the requirement of discrimination had been replaced by the prohibition of “potential impediments” in *Dassonville* and by the proportionality test and “mutual recognition” in *Cassis*, the toolset of progressive “negative integration through law” was complete – and with it the ratcheting mechanism that secured the front line established by judicial liberalization against political reversals through European legislation.

41 The Court’s usual response is that, yes, member states retain the right to shape their own industrial relations or social security or health care systems. But in doing so, they must of course respect the Treaty-based rights of individuals and firms. See for example C-158/96, 28.4.1998 at ## 16, 19–20 (*Kohll*).

42 Agustín José Menéndez (2007 at § 31) goes as far as to consider “the effective upholding of the four economic freedoms ... as a *basic precondition* for the effective protection of all *fundamental rights*. This presupposes the claim that in the absence of such a protection, peace and material prosperity is at risk, and with it, political, civic and socioeconomic rights; or in brief, all rights.”

43 BverfG, 2 BvE 2/08, 30.6.2009.

44 Ibid. at § 249.

45 Ibid. at § 252.

ples of Europe.” Even now, it is hard to imagine that national regulations on education or family law could remain unaffected by the Court’s interpretation of European mobility, nondiscrimination and citizenship rights. Even here, therefore, autonomy could not be absolute, and a balancing test would need to be applied. If it were to be attempted, however, it would also become clear that diversity matters, and that the normative salience of particular sociocultural issues varies greatly from one member state to another (Kurzer 2001).⁴⁶

Beyond that, however, the German court also defined “constitutional identity” to require sufficient space for national policy choices shaping the economic and social conditions affecting the lives of citizens – including fiscal and social-policy choices (*ibid.*). This raises still more difficult problems. In contrast to the very limited European competences in sociocultural matters, competences over the economy have been thoroughly Europeanized. And since their exercise would inevitably have an impact on social conditions, some social-policy competences were added in later Treaty revisions as well. In contrast to the sociocultural sphere, therefore, there is no possibility of arguing for a general presumption of national autonomy in the socioeconomic sphere. It is also true, however, that EU member states differ greatly in the institutional structures and normative premises of their existing economic and social systems, and that the specific national configurations have high political salience and may indeed be considered as part of the “constitutional identity” of EU member states.

These differences, which have been all but ignored in legal discourses on European integration, are the object of a growing body of empirical and theoretical research in comparative political economy. In this literature, two distinctions are generally used to describe the basic characteristics of the social and economic structures of advanced capitalist democracies. The first one was introduced by Esping-Andersen (1990) in his account of the “three worlds of welfare capitalism,” labeled “Liberal” (or Anglo-Saxon), “Christian Democratic” (or Continental) and “Social Democratic” (or Scandinavian). His classification focuses on social-policy and industrial-relations regimes and the extent to which they are designed to ensure social equality, social security and the “decommodification” of labor. The second classification, introduced by Hall and Soskice (2001), distinguishes two fundamentally different “varieties of capitalism,” namely “Liberal Market Economies” and “Coordinated Market Economies.” Here the focus is on the relationship between the international competitiveness of national economies and the nation-specific institutional regimes of corporate governance, corporate finance, labor relations, industrial training and industrial R&D.

46 In national federal constitutions, if the sociocultural identity is highly salient in all regional units, the appropriate solution may be a general decentralization of competences, as is true in Switzerland. But if such concerns are much more salient in some units than in the rest of the polity, asymmetric federalism may grant more autonomy to some regional units than to others, as is true in Canada, Spain, or the United Kingdom (Agranoff 1999).

In both classifications, there is a “Liberal” or “Anglo-Saxon” ideal type in which the role of the state is reduced to a minimum. The liberal welfare state provides means-tested social assistance and basic social and health services to the needy, but leaves all others to look out for themselves in the private investment, insurance and service markets. Similarly, in the liberal market economy, the state creates the preconditions of functioning markets by protecting property rights, enforcing private contracts and establishing a regime of undistorted competition. Beyond that, it may intervene in the market to protect public health, work safety, the environment and consumers’ rights. But the liberal state is expected to minimize its involvement in the provision of infrastructure functions and services, and it is definitely not expected to interfere with economic interactions in product markets, labor markets, capital markets, skill markets and technology markets.

By contrast, the state in a coordinated market economy is heavily involved in maximizing the economic benefits of public infrastructure, technology and training policies. Its labor markets are highly regulated and relatively inflexible; industrial relations tend to be shaped by “cooperative” collective bargaining at the level of industries and firms, and interactions between firms and banks and among firms are embedded in relatively stable network relationships. At the same time, the Continental and Scandinavian welfare states provide not just social assistance but social security, by ensuring retirement incomes, health care, and unemployment benefits for all. The Scandinavian welfare state goes even further, providing universal social services for families with children, for the handicapped, and for the elderly. These are financed through steeply progressive taxes which, combined with the “solidaristic” wage policies of powerful and monopolistic unions, ensure a very high degree of social equality (Scharpf/Schmidt 2000a).

Both the Esping-Andersen and Hall and Soskice classifications use ideal types to provide simplified descriptions of highly complex and country-specific configurations. Hence the assignment of a country to a particular type will neither capture all features of the national institutional constellation,⁴⁷ nor is it possible to assign all countries to nonoverlapping clusters (Ahlquist/Breunig 2009). Moreover, these types were derived from configurations that matured in the “golden age” of postwar welfare states and mixed economies, and the distinctions have become more blurred in the meantime as a consequence of national responses to increasing international (global and European) challenges (Scharpf/Schmidt 2000b). Nevertheless, the two methods of classification have generated a rich body of comparative research confirming the systemic importance of the traits used to define the models.

For present purposes, I will simplify even more by collapsing the social and the economic classifications into a single distinction between liberal market economies (LMEs) and social market economies (SMEs). In other words, the ideal-type LME is assumed to have

47 For instance, in countries that are generally identified with the “liberal” model, this is true of the National Health Service in the UK and of Social Security and Medicare in the United States.

a liberal market economy *and* a liberal welfare state; and the ideal SME will combine the characteristics of a coordinated market economy with either a Continental or Scandinavian type of welfare state. This heroic simplification then allows for the construction of a two-dimensional space in which “Europeanization” and “national autonomy” describe the vertical axis of European integration, while the socioeconomic distinction between “social regulation” and “liberalization” defines a horizontal axis that is generally ignored in the Euro-law and Europeanization discourses. The two axes can then be used to construct a two-dimensional diagram for mapping the consequences that the Europeanization of competences and the widening domain of European law will have for member states whose existing institutions differ in the socioeconomic dimension (Figure 1).

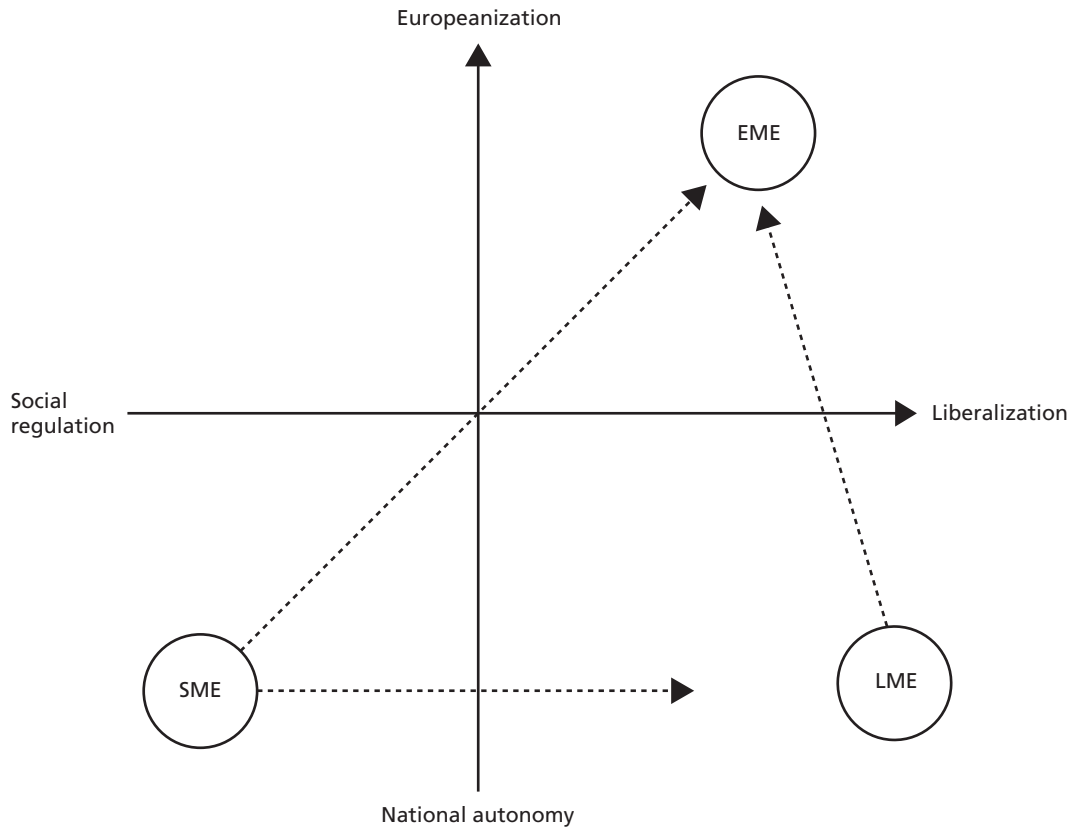
Figure 1 is meant to show that the Court’s enforcement of economic liberties will have the least effect on the institutions and practices of liberal market economies. By the same token, the governments of these member states (which by now include not only the UK, Ireland and – in some policy areas – the Netherlands, but many Central and Eastern European countries as well) have reason to welcome the removal of non-tariff barriers in other member states and the creation of competitive markets in sectors that other countries had reserved for the public sector or otherwise shielded from competition. These more liberal market economies can thus be expected to profit from negative integration and to support whatever additional initiatives for legislative liberalization and deregulation the Commission will propose.

The situation is very different for countries located near the other end of the socioeconomic spectrum. In the article cited at the beginning, F.A. Hayek (1948 [1939]) had expected that in a European federation the competition among national economies would bring about a conversion to the liberal model. In the meantime, however, Hall and Soskice and their collaborators (2001) have shown that the international competitiveness of “coordinated market economies” benefited from comparative advantages created by domestic institutions and practices that both complemented and displaced the mechanism of pure market interactions. Given their different production profiles, and their orientation to different markets, coordinated economies could be as efficient as the liberal ones – in fact, looking at the balance of current accounts, they are generally more successful in economic terms. At the same time, however, they are extremely vulnerable to the deregulation that comes with the legal constraints of negative integration and liberalization.

Thus, the Court’s recent decisions are not only disabling crucial features of national labor law, industrial relations law and wage setting practices. Its interpretation of the freedom of establishment clause also allows firms to evade national rules of corporate governance by incorporating in a different jurisdiction.⁴⁸ Since we already know from the *Volkswagen* case that the Court saw the freedom of capital movement as potential-

48 C-212/97, 9.3.1999 (*Centros*); Roth (2008).

Figure 1 The effect of Europeanization on Social Market Economies (SME), Liberal Market Economies (LME) and the emerging European Market Economy (EME)



ly impeded by a statute defining the blocking minority in the shareholder assembly,⁴⁹ there is every reason to expect the same verdict should the ECJ have to review a statute requiring the participation of workers on the supervisory board of large companies. In short, the Court's decisions are undermining the institutional foundations on which the comparative advantages of coordinated market economies have depended. The liberal transformation, which Hayek had wrongly expected to result from the pressures of market competition, is finally occurring under the legal compulsion of ECJ jurisprudence (Höpner/Schäfer 2007).⁵⁰

49 C-112/05, 23.10.2007.

50 It is frequently remarked that much of this transformation has been brought about by national legislation. That is both true and unsurprising. First, many instances may be explained by Carl Friedrich's (1937) "law of anticipated reactions": Realizing the vulnerability of their existing regulations under ECJ case law, national governments may prefer orderly adjustment to haphazard judicial interventions. What is often even more important is the fact that the politics of social market economies will usually include a sizable segment of actors in political parties, interest groups, the media and academe who are committed to market-liberal reforms. For these actors, ECJ decisions may open a political window of opportunity in which previously effective veto positions are disabled.

The situation is similar when it comes to the characteristic features of different types of welfare states (Falkner 2009). Once again, the Court's interventions to ensure free mobility, undistorted competition and nondiscrimination have no effect on the privately provided social services, pensions, and health care that are characteristic of liberal welfare states. Social market economies, by contrast, use a much wider variety of institutional arrangements, including basic pensions financed through tax revenues, compulsory pension insurance, or subsidized private pension funds. Similarly, they tend to rely on publicly provided social services, on social services provided by subsidized nonprofit or private organizations, or on health care provided by public, nonprofit or private organizations and private practices – which may be financed by general taxation, compulsory insurance or by publicly subsidized private insurance, etc. These arrangements are of course affected by the impact of European law on tax revenues from mobile capital. And since more generous welfare states must necessarily regulate benefits, beneficiaries and conditions of reimbursement, they are also vulnerable to legal challenges based on European mobility, competition and nondiscrimination rules.

At the same time, the institutional variety of these solutions increases their vulnerability to economic liberties. Whenever social services and transfers are not exclusively provided by the public sector and financed by general taxation or compulsory insurance, they may be challenged under European rules on the freedom of service provision, the freedom of establishment, state aids, public procurement and competition law. Admittedly, not all these challenges have been launched yet, and not all will succeed. But ECJ and Commission decisions⁵¹ have already put enough pressure on publicly subsidized charities in Germany to require a market-oriented reorganization of the traditional system of social services they provide. The Commission also plans to create competition regimes for social services that would emulate the market-maximizing models established for the telecommunications, transport and energy markets (Ross 2007).⁵² It remains to be seen whether the Commission's plans and the Court's jurisdiction will be modified by Art. 14 of the Lisbon Treaty and Art. 2 of its "Protocol on Services of General Interest," which stipulates that "the provisions of the Treaties do not affect in any way the competence of Member States to provide, commission and organise non-economic services of general interest" (Damjanovic/De Witte 2008).

At the same time, the Court has extended the rights of beneficiaries of publicly or collectively financed health care to avail themselves of more attractive or more timely services offered abroad, at the expense of domestic taxpayers or insurance funds (Martinsen/Vrangbaek 2008), and the Commission has proposed a "directive on the application of patients' rights in cross-border health care"⁵³ that would systematize and generalize

51 Commission (2005), for example.

52 See White Paper on Services of General Interest, COM (2004) 374; Implementing the Community Lisbon Programme: Social Services of General Interest in the European Union, COM (2006), 177 final.

53 COM (2008) 414 final.

the case law. Beyond that, the Court's extension of the rights of personal mobility, non-discrimination and EU citizenship has reduced or eliminated member states' control over EU migrants' access to nationally provided public and social services and transfers (Hatzopoulos/Do 2006; Wollenschläger 2007).

From the perspective of mobile individuals, these developments must seem attractive. But since EU member states differ widely in their normative commitment to solidarity and equality, and hence in the level of social services and social transfers they provide for their citizens, the Court's generosity ignores the foundations of the social and political construction of solidarity, and it also violates the norms of reciprocity. A British citizen moving to Denmark or a German medical student moving to Austria is allowed to claim benefits that a Dane or Austrian moving in the opposite direction could not obtain. In the name of transnational solidarity, the Court has weakened or eliminated the nation-state's control over the balance of contributions and benefits and the boundaries of state generosity. This does indeed create incentives for transnational mobility, and it may contribute to the interweaving of European societies. At the same time, however, the extension of personal mobility rights for individuals creates special burdens for national welfare states with high levels of collectively financed services and transfers, and thus also creates incentives favoring convergence toward the liberal minimum of social protection (Menéndez 2009).

In short, Court-imposed negative integration and deregulation will have no great effect on the institutions and policies of LMEs with relatively low levels of social regulation and minimal welfare states. What's more, competitive opportunities for LMEs will increase as negative integration opens up and deregulates formerly protected markets in other member states. Existing economic institutions in SMEs, by contrast, will be systematically weakened by the deregulatory effect of negative integration and the competitive pressures resulting from mutual recognition, while their welfare-state institutions will be challenged by European competition law, mobility rights and nondiscrimination law. In Figure 1, therefore, the existing socioeconomic regimes of SMEs will be pushed to the right toward a more "liberal" configuration.

If this comes to pass, and much of it already has, member states with SME institutions and political preferences will have to turn to European legislation in order to realize the 1980s promise of a "social dimension" or the 1990s vision of a "European social model" or the current postulate of a "highly competitive social market economy" (enshrined in Art. 3, III of the Lisbon EU Treaty). If they do so, however, they will confront a second structural asymmetry: high consensus requirements still hamper European legislation, even after Lisbon, and generally favor status-quo positions. But this status quo has been redefined by negative integration in favor of LME member states. Since the LMEs in Europe do not depend on European legislation to maintain their own socioeconomic regimes, they are free to veto any European initiatives that would impose more demanding regulations on their liberal economies, or that would require more generous social benefits. As a consequence, the "European Market Economy" that could at best be

brought about through positive integration would resemble the socioeconomic regimes of LMEs, rather than recreate a social market economy at the European level. The structural constraints of European integration have cut off access to the top-left quadrant of Figure 1, exactly the location toward which the pro-European Christian Democrats and Social Democrats would like to move.

4 Conclusion

The evolution of European integration has confirmed Friedrich Hayek's prediction, published in 1939, that the integration of previously sovereign nation-states in Europe would reduce the capacity of states to regulate the capitalist economy and to burden it with the costs of an expensive welfare state. It took a bit longer than expected, however, because member governments initially retained control over economic integration. This meant that they were also able to preserve the conditions of "embedded liberalism" and thus protect the integrity and diversity of national institutions and policy legacies against the pressures of economic competition. Indeed, European social market economies reached the peak of their development and institutional diversity during the first two decades of the Community's existence. Integration through law changed all that, and as a consequence European law, judicial and legislative, is now cutting deeply into the substance of the socioeconomic regimes of social market economies.

Given this state of affairs, governments, political parties, unions, publicists and academics who are at the same time committed to European integration and to the ideals of a social market economy have basically two strategic options, one proactive and one defensive. The first one would emphasize political mobilization, persuasion, campaigning and lobbying strategies to overcome the obstacles to creating equivalents to national social-market regimes at the European level. From what I have said before, it should be clear that I consider this as an extremely difficult and, at best, long-term option which will bring little relief to the present problems of social market economies. Above all, its protagonists need to realize that, given the consensus requirements of European legislation, it will not suffice to mobilize political support in Continental and Scandinavian member states. The most likely effect would be counterproductive confrontations with veto players defending the comparative advantages of liberal market economies. What would be needed are initiatives that are attractive from the perspective of both types of national regimes. How hard this is likely to be is presently shown by the difficulties of reaching agreement on the substance and severity of common European capital-market and banking regulations, even though common interests should be at a maximum as the worldwide crisis of unregulated financial markets has hurt the liberal economies of the UK, Ireland or the Baltic states even more than it damaged the social market economies.

In any case, I will not pursue this option further, but focus my conclusions on the need to defend and protect the national regimes of social market economies against the legal compulsions of negative integration. Given the Court's interpretation of primary European law, combined with the diversity of socioeconomic regimes at the national level and with the high consensus requirements of political action at the European level, it is easy to see that this development could not have been prevented and cannot be corrected by European legislation. What is perhaps less clear is that the asymmetry could hardly have been avoided and probably cannot be corrected by the European Court of Justice itself.⁵⁴ The most basic reason is that the legitimacy of judicial lawmaking, by common-law courts, civil-law courts or by constitutional courts, depends on the observance of a generalizing logic (Holmes 1881; Esser 1964). The decision must focus on the specific facts of a particular case, but it cannot be *ad hoc*. Even where preexisting rules are not available or do not fit, the judge-made rule must satisfy the Kantian categorical imperative: it must be possible to defend it as a general rule for all cases of this nature.

Hence even if the Court had tried to develop criteria for a fair constitutional balance between European competences and national autonomy, it would have had to define these in general terms, which in principle could be applied to the relationship between the Union and all its member states. Yet any general criterion defined in the vertical dimension is likely to have different and highly asymmetric impacts on member states located at different positions in the horizontal dimension. Even the "sociocultural" concerns discussed by the German constitutional court vary in their normative and political salience from one country to another, and the socioeconomic differences between social market economies and liberal market economies are at the very root of the normative tension and political dissatisfaction generated by the recent progress of legal integration. But they are also at the root of the Court's problem.

A *general* rule that would respect politically salient concerns in the most highly regulated member state (say, Swedish rules on the sale of alcoholic beverages) would obviously define European economic competences far too narrowly, but an equally general rule that would merely protect the practices of the most liberal member state might massively interfere with the political identity and legitimacy of SME member states. And if the rule were to aim at a compromise between these extremes, it would merely create both problems at the same time. To put it another way: in the face of normatively salient diversity across national institutions or policy legacies, no general rule could establish a fair vertical balance. It is thus entirely understandable that the Court never tried to

54 See note 40 above. One could of course ask whether the doctrinal development that established the dynamic effectiveness of negative integration could have been avoided. But one should not forget that the crucial decisions of the 1970s were widely welcomed by pro-European public opinion and political actors. And even if *Dassonville* had not added the prohibition of "potential impediments" to the rule against discrimination on grounds of nationality, that would not have been enough. There would still be legitimate national concerns that can only be protected by resort to discriminatory measures – or how else should Austria have protected its medical education against the mass inflow of students from Germany.

define general criteria for a European–national balance. Instead, the *Dassonville-Cassis* formula allowed it to assert the general supremacy of all European concerns, but to combine this with the possibility of exceptions that the Court would grant at basically its own discretion.

But even if these exceptions were guided by principles, it should be clear that the *Cassis* formula cannot accommodate the diversity of normative and politically salient national concerns. The “mandatory requirements of public interest” that might be invoked to justify national impediments are, of course, defined by the Court in general terms. How could, what is not mandatory for the UK be mandatory for Sweden? And to the extent that applications of the “proportionality test” are guided by criteria, these are of a purely technical, and hence universal, character, referring to the effectiveness and necessity of European versus national measures, rather than to their normative significance and political salience. In fact, the Court has no criteria for dealing with and assessing the “legitimate diversity” (Scharpf 2003) of the socioeconomic institutions and policy legacies that are affected by its decisions.

In each country, such institutions and legacies have often been shaped by intense political conflicts and historical compromises – which is why they differ so much from one another. Individuals have come to take them for granted and to base their life plans on them. That does not mean that they should, or could, be protected against change. In fact, the socioeconomic regimes of SMEs are under immense pressures to adjust to dramatic changes in their internal and external policy environments. At the same time, however, such changes are highly controversial in national politics and they need to be defended in public debates by governments facing the sanctions of political accountability. Instead, the supremacy of European law allows for judicial interventions that may short-circuit these political processes. If these are to be accepted as legitimate, they need to be justified by arguments that invoke clearly important European concerns and that are highly sensitive to the specific sociocultural and politico-economic concerns that are at stake in the particular member state. This the ECJ has never attempted, and it is indeed hard to see how it could gain the necessary familiarity and empathy with the institutional traditions and the political cultures of the EU’s twenty-seven member states.

But what could be a more acceptable alternative?

In its decision on the Lisbon Treaty, the German constitutional court saw itself in a better position to define limits for the exercise of European powers. Emboldened perhaps by its own record of maintaining (or upsetting) the federal balance in Germany, it not only urged both houses of parliament to ensure that European legislation would not exceed the powers conferred to the Union, but also reasserted its own readiness to exercise these *ultra-vires* controls and to defend the core elements of the German “constitutional identity.” And, what is more interesting in the present context, it left no doubt that this

would also apply to the interpretation of Treaty by agents at the European level.⁵⁵ In other words, the supremacy of European law and the ECJ's monopoly of interpretation are seen to be constrained not only by the "principle of conferral" (Art. 5 ECT; Art. 5 TEU Lisbon), but also by criteria derived from the national constitution and defined by the national constitutional court's monopoly of its interpretation.

Being embedded in the German political and normative culture, the *Bundesverfassungsgericht* has of course no difficulty identifying a hard core of institutions and policy areas where democratic self-determination at the national level ought to prevail over European interventions. More over, the court also emphasizes the "integration openness" and the "Europe-friendliness" of the German constitution, and it asserts its full support for this constitutional commitment to European integration. In other words, the decision avers the court's willingness to strike a fair balance between European and national concerns in its future decisions. On the basis of its past record, there is surely no reason to doubt these commitments.

Nevertheless, the decision appears fundamentally flawed because the court has failed to consider its generalized implications in the light of the Kantian categorical imperative. The authority claimed by the German court could of course not be denied to the courts in all member states. And while these would surely be equally sensitive to the specific and diverse concerns of national autonomy and identity, there is no reason to expect that their understandings of the "Europe-friendliness" of their national constitutions would converge, or that they would all assign the same relative weights to the European concerns at stake. The overall result might be a chaotic form of differentiated integration through an accumulation and perhaps escalation of unilateral national opt-outs.

I have tried to show that the ECJ's *Kompetenz-Kompetenz* is not only distorting the vertical balance between the powers of the Union and the requirements of democratic self-determination in its member states, but that it also has an asymmetric impact on the horizontal balance between social market economies and liberal market economies. This double asymmetry is presently undermining political support for European integration and weakening democratic legitimacy at the national level. It needs to be challenged and corrected in order to reestablish a workable balance between the equally salient values of European "community" and national "autonomy." But a normatively and pragmatically acceptable balance cannot be achieved by asserting the power of national high courts to declare unilateral opt-outs from European law in procedures in which the interests of other EU member states and the concerns of the Union have no voice at all. The Lisbon decision may not provoke escalating conflicts culminating in secession and civil war – as the assertion of John C. Calhoun's nullification doctrine had done in the decades preceding the American civil war (Bancroft 2008; Ellis 1989). But it may still have severely disruptive effects in the European Union as well.

55 BVerfG, 2 BvE 2/08 at §§ 238–241.

What we need instead are procedures that facilitate the mutual accommodation of European and national concerns. Here it does indeed make sense to leave the definition of fundamental national concerns to national governments or national courts, rather than to the uncertain empathy of the ECJ. But there must be a possibility of review in the light of similarly or more salient European concerns. One possible solution has recently been proposed by a former chief justice of the German constitutional court (Herzog/Gerken 2008). It would allow ECJ judgments to be appealed to a European Constitutional Court composed of the chief justices of all EU member states. For reasons explained elsewhere, I would prefer a political, rather than a purely judicial solution – which would again have to define *general* criteria that could not accommodate the diversity of legitimate national concerns. Instead, the political solution I proposed would allow member governments to appeal to the judgment of their peers in the European Council in cases where European law is felt to impose unacceptably tight constraints on politically highly salient national concerns (Scharpf 2009).

There may well be other and better solutions, but none of them will come about unless the “good Europeans” in Continental and Scandinavian social market economies realize that integration through law is a mode of policy-making that is structurally biased against their interests and normative preferences. It systematically weakens their established socioeconomic regimes at the national level and it also generates a liberalizing bias in European legislation. Furthermore, they should understand that the socioeconomic asymmetry of European law is caused by structural conditions whose effect does not depend on the ideological orientations of members of the Court or the Commission. For this same reason, it can hardly be corrected through changes in the party-political composition of the Council or through elections to the European Parliament.

In short, good Europeans need to draw a distinction between their continuing support for political and social integration in Europe on the one hand, and their unquestioning acceptance of policy choices dictated by a nonaccountable judicial authority on the other hand. A European social market economy cannot come about, and social market economies at the national level will be destroyed, unless the politically uncontrolled dynamics of (negative) “Integration through Law” can be contained.

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