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The Asymmetry of European Integration

or why the EU cannot be a “Social Market Economy”

Fritz W. Scharpf

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Freie Universität Berlin
Kolleg-Forscherguppe
„The Transformative Power of Europe:
The European Union and the Diffusion of Ideas“
Innestr. 26
14195 Berlin
Germany
Phone: +49 (0)30- 838 57033
Fax: +49 (0)30- 838 57096
transform-europe@fu-berlin.de
www.transformeurope.eu

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THE ASYMMETRY OF EUROPEAN INTEGRATION

OR WHY THE EU CANNOT BE A “SOCIAL MARKET ECONOMY”

Fritz W. Scharpf

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 socio-economic 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.

The Author



Fritz W. Scharpf is Emeritus Director of the Max Planck Institute for the Studies of Societies in Cologne. He taught Law at the Yale Law School and Political Science at the University of Constance. From January to April 2009, Fritz W. Scharpf was a guest fellow at the *Kolleg-Forscherguppe*. His substantive research has focused on the political role of the judiciary, on normative democratic theory, on the institutions of multilevel government in Germany and the European Union, and on the comparative political economy of modern welfare states.

Contents

1. Introduction	5
2. Integration through Politics and Integration through Law	7
3. Judicial Deregulation and Legislative Liberalization	12
4. The Vertical Impact of “Integration through Law”	17
5. The Horizontal Impact of Integration by Law	19
6. Conclusion	27
Literature	31

1. Introduction¹

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 1939).

Will history repeat itself? The ideological hegemony of orthodox liberalism had ended in the Great Depression of the 1930s, and it may well be that the current global crisis will also end the quarter-century of triumphant neo-liberalism 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 re-defined by the ideas that have shaped the socially inclusive and institutionally coordinated "Social Market Economies" on the Continent and in Scandinavia, rather than by the "Liberal Market Economies" of the Anglo-Saxon countries and some of the new member states. Or so one might think.

Friedrich 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 post-war 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 neo-liberal followers who supported European integration not so much on economic than on normative-political grounds (see e.g. Mestmäcker 1989; 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 academe whose ideological preferences or manifest interests were quite opposed to unfettered market liberalism.

One reason is that the liberalization which Hayek had foreseen 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 would prevent the creation of a strongly redistributive welfare state whose burdens would fall unequally on economically strong and weak regions. In Europe however, the historical sequence occurred in reverse order. After the failure of the European Defense Community in 1954, political integration was postponed. The European Economic Community began as a customs union

¹ Work on this paper has been generously supported by the Kolleg-Forschergruppe "The Transformative Power of Europe" at the Freie Universität Berlin. It has greatly benefited from my participation (as a "senior post-doc fellow") in discussions of the group and, in particular, with Tanja Börzel and Thomas Risse.

whose members were committed to create a common market whose success, so it was hoped, would eventually facilitate political integration as well. For the time being, therefore, the Community would try to remove barriers to trade through intergovernmental negotiations while the member states remained responsible for 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 interests and values served by the existing domestic socio-economic 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 multilevel 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 (“neo-liberal”) 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 had 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) magisterial account, every step that deepened economic integration and liberalized regulatory regimes is explained by reference to the (primarily economic) interests and preferences represented by governments of the larger member states. By contrast, Nicolas Jabko (2006) attributed the surge of liberalizing legislation to the Commission’s “strategic constructivism” which persuaded a heterogeneous coalition of political actors of “the market idea” as 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 neo-liberalism. 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 are defining their strategic choices (Giddens 1984). Moreover, their focus is exclusively on Treaty revisions and legislative action by political actors while ignoring or downplaying the impact of standing decision rules and of the decisions of non-political actors on the available options of these political actors. Instead, structure and agency should be considered as complementary, rather than as mutually exclusive, explanatory options (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.

The present essay will first explore the impact of two institutional asymmetries - one favoring policy-making by non-political actors and impeding political action at the European level, and the other one favoring European policies of “negative integration” and impeding policies of “positive integration” (Scharpf 1999: Chapter 2). In conclusion I will then try to show how these institutional asymmetries have persistently favored market-liberal interests and policy goals, and how they have undermined or destroyed the capacity of member states to pursue market-correcting policy goals at the national level while preventing the effective pursuit of such goals at the European level. In short, I will argue that European integration

has been, and will continue to be, structurally hostile to the interests and values realized in the social market economies of Continental and Scandinavian Europe.

2. 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 remained in control over the extent and the speed of economic unification and liberalization². After 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 and for which products trade would be liberalized; to what extent and when controls over capital movements would be lifted; under which conditions workers could seek employment and firms could 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 remained unchallenged, member states were also able to control the interaction effects between the extent of economic liberalization and the functional requisites of their nationally bounded welfare states and industrial-relations, public-revenue, public-service and infrastructure systems. In other words, member states were able to 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 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 protection of women in the work place 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, in 1973, 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).

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.

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, the 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 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 had 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), instead of identifying and analyzing any 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. And 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, let alone the European level. Yet once the "habit of obedience" (Maduro 1998: 11) was established, European

3 Van Gend & Loos, C-26/62, 05.02.1963.

4 Costa v. Enel, C-6/64, 15.07.1964.

5 See e.g. Alter (2001); Burley and Mattli (1993); Garrett (1995); Mattli and Slaughter (1995); Slaughter et al. (1998); 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).

law, as interpreted by the ECJ, was woven into the fabric of the “law of the land” which ordinary national courts are applying in ordinary litigation. Hence to challenge an ECJ ruling, governments would have to confront their own judicial system and to 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.

Moreover, the effectiveness of the Court’s judicial legislation is 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 could 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 could not be corrected without an initiative of the Commission that needs the support of at least a qualified majority in the Council and, usually, also of an absolute majority in the European Parliament. Given the ever increasing diversity of national interests and preferences, such corrections were 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

With this formula, all national rule and practices affecting trade could be defined as a non-tariff barrier 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. It sufficed that a potential impediment could be construed 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

⁸ C-8/74, at # 5.

⁹ C 120/79, 20.02.1979.

controls 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 policy or public security; the protection of health and life of humans, animals or plants [...] etc. ”, provided that these would not “constitute a means of arbitrary discrimination or a disguised restriction on trade between 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 read to exempt national rules serving one of the specified policy purposes altogether 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 re-interpret 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 now 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, if the national regulations could not be so justified, the Court announced a new rule of *“mutual recognition”* according to which products must be allowed in the national market, *“provided that they have been lawfully produced and marketed in one of the member states.”*

By adding new justifications (*“fiscal supervision”*, *“defense of the consumer”*) that had no basis in the text of Article 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

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

¹¹ C-120/78 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, 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.

procedural asymmetry between 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. It may be rebutted, however, if the member state is able to defend the measure in question by reference to a repertoire of possible justifications allowed by the Court. Yet being treated as exceptions, such justifications are to be narrowly interpreted, and where they would apply in principle, the burden of proof is on the member state¹³ to show that the measure in question will be effective in promoting its alleged purpose, and that the same effect could not also have been achieved by other and less burdensome measures.¹⁴

As a consequence, the *Cassis formula*¹⁵ 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 direction and the limits of allowable national policy purposes. 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 (Haltern 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 competition 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.

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 (C55/94, 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 fulfil 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 of persons is in 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 of the process of service provision could massively affect the quality of the service itself. Hence they could not be generally 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.

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 highly asymmetric impact on the substantive directions of European political legislation.

3. Judicial Deregulation and Legislative Liberalization

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-crossing transactions (e.g. Articles 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 neo-liberal or ordo-liberal “economic constitution.” In positive law, however, the ambivalence also seems to have its roots in the wide sweep of the *Dassonville* formula. If European liberties can be violated by national rules having merely *potential* border-crossing effects, 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.¹⁸ Moreover, even where Court-defined liberties and competition rules could and would be 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 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. Instead, the member state had to open its internal market to all products that were lawfully produced and marketed in their country of origin. But the state remained 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

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; Alter 2009: Chapter 4).

18 In the *Volkswagen-Statute* case (C-74/07, 23.10.2007), for instance, the rule establishing a blocking minority of 20 per cent (rather than the more usual 25 per cent) was seen as a potential deterrent to foreign direct investment, and hence to free capital movement. If that 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”.

2007; Nicolaidis 2007; Maduro 2007). In other words, “integration through law” will 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 which member states faced in the processes of European legislation. Whereas in the past national law had remained in force¹⁹ as long as governments did not agree on a harmonization directive, the new default condition would now be “mutual recognition.” This, at any rate, was the interpretation which the Commission began to spread in its early “communications” (Alter/Meunier-Aitsahalia 1994). And instead of waiting for appropriate cases to reach the ECJ through referrals from national courts, the Commission also stepped up its prosecution of Treaty infringements (Alter/Meunier-Aitsahalia 1994: 548; Stone Sweet 2003: 40). The immediate effect of the Court’s decisions, of the Commission’s communications and of 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 in doubt (Schmidt 2008).

The Commission responded to this (largely self-created) uncertainty with reform proposals that would re-empower integration through political legislation. Its White Paper “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.

In the literature, the success of these reform proposals, and the dramatic increase in the volume of liberalizing legislation, is either explained 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 ubiquitous 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.

At the outset it needs to be pointed out that “Integration through Law” could only be achieved because, ever since *Van Gend & Loos* (C-26/62, 05.02.1963), 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.²⁰ Without this re-interpretation, the doctrine of “direct effect” could hardly have been

19 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).

20 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

invoked by private parties in national courts, from where they would reach the European Court of Justice through the preliminary reference procedure (Art. 234 ECT). This basic constellation gives rise to two systematic biases in the ECJ's case law:

First, the questions the Court will receive and the cases it will see will inevitably constitute an extremely skewed sample of total interest constellations. They will reflect the interest of parties who have a major economic or personal stake in increased mobility and deregulation as well as the financial and organizational resources²¹ to pursue this interest through the judicial removal of national laws and regulations (Conant 2002; Kelemen 2003). What the Court will not see, however, are cases brought by the less mobile majority of European individuals and firms 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 the common law of contracts can be expected to generate a fair 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 remove²² (Schmidt 2009b).

It needs to be said, however, that "liberalization" is not necessarily to be understood in a market-liberal or neo-liberal 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 responded 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*,²³ it has even ruled that Austrian taxpayers should pay for the education of German medical students who fail to qualify under *numerus-clausus* requirements 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 the reimbursement of patients seeking ambulatory and stationary health care abroad (Martinsen/Vrangbaek 2008; Martinsen 2009). In the meantime, moreover, the combination of EU citizenship, freedom of movement and non-discrimination on grounds of nationality is used to minimize national residency requirements that would limit the access of migrants to national welfare systems (Wollenschläger 2007; Egger 2008).

Council to adopt the 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: Chapter 4).

- 21 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.
- 22 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".
- 23 C-147/03, 2005.

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 non-economic 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 - which instead are likely to be undermined by weakening the reciprocity of rights and obligations (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 individual mobility and “negative integration” over democratic self-determination in the national polity.

The second bias is even more salient. Given its rights-based interpretation of Treaty obligations, the only remedy which the Court can offer to the complaints of private litigants is to disallow the challenged national regulations. In effect, therefore, its decisions can only have a liberalizing and deregulatory impact on existing national regimes. But the Court is not able to create common European regimes that could substitute for the national regulations that are no longer allowed.²⁴ These would require European legislation which, given that consensus requirements continue to be very high, is still impeded by conflicts of interest or preferences among member states.

Nevertheless, the Single European Act and subsequent Treaty amendments have not only established new legislative competences of the Community, but they have also launched an increasing volume of effective European legislation in areas where national competences have been constrained. 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 quite demanding standards that represent impressive achievements of positive integration. And of course, there are other areas, such as capital taxation or industrial relations, where national action is constrained by the Court’s protection of economic liberties, 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 will be 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

24 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.

25 Gerda Falkner at the Austrian Academy of Sciences is presently directing a conference project which will record and compare the progress of European legislation across a wide variety of policy areas.

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 case law. 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 case law itself could not be reversed, 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 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 Articles 95 or 96 ECT. But under these conditions, the bargaining

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

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

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).

4. The Vertical Impact of “Integration through 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 act as a dynamic stimulus for further legislation ever since. There is no question, therefore, that it 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 which the Treaties had explicitly excluded from the domain of European legislation.

This was possible because by postulating the supremacy doctrine, the Court has assumed the status of a constitutional court in the relationship between the European Union and its member states. But in contrast to the constitutional law 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. In its teleological logic, it should be understood as “partisan law” which - like the “socialist law” of the former German Democratic Republic or the U.S. Supreme Court’s intervention against racial segregation in the 1950s - is employed to promote the purposeful transformation of a pre-existing social and institutional balance.

In the GDR, *Parteilichkeit* of the judiciary in matters affecting the class conflict was, of course, required and supported by the legitimacy claims of the socialist state. In constitutional democracies, by contrast, there is a basic tension between the norms of democratic legitimacy and the possibility of judge-made

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 inter-ministerial bargaining at the national level.

law. If its existence is acknowledged at all, however, legal theory insists that judicial neutrality must be the indispensable precondition of its legitimate exercise (Somek 1992). Thus the American Supreme Court's "judicial activism" of the 1950s provoked not only much political opposition but also serious soul searching among its sympathizers in constitutional law and jurisprudence (Bickel 1955, 1962) - and it proved to be unsustainable as a general position. In the specific case, however, the court's partisan intervention against racial segregation found broad public support on the national level, and it came to be politically vindicated in the 1960s by the civil-rights legislation of the Kennedy-Johnson administration. In effect therefore, the Supreme Court had indeed expressed the "sober second thought of the community" (Bickel 1962: 26) - which by the norms of democratic constitutionalism appears as the ultimate justification for the exercise of non-democratic powers of judicial review (Bickel 1962: 26).

A similar argument might indeed be made in support of the partisan activism of the European Court of Justice. Hadn't the European continent been ravished for centuries by the internecine battles among its nations and states? Hadn't nationalism and racism in Germany brought about the moral catastrophe of the Holocaust? And wasn't European integration the one and only hope for peace, democracy, prosperity and the security of human rights on a continent riven by ideological, ethnic and religious conflicts? For the European movement in the years following the Second World War, and for the "founding fathers" of the Community, these were rhetorical questions that established the moral superiority of the integration goal over all countervailing concerns (Haas 1958). But if this historically unprecedented goal was accepted as an overriding commitment, wasn't it also obvious that its realization would be an uphill struggle against the forces of institutional inertia, economic self-interest, political conflicts and popular xenophobia that might inhibit national support at every step on the long road ahead toward "an ever closer union among the peoples of Europe"? If that was so, wouldn't it also follow that the eventual success of the European project must largely depend on the moral commitment, personal dedication, professional competence and strategic skills of pro-European national politicians and of supranational actors in the European Commission, the European Court of Justice and the European Parliament? And wouldn't these actors be justified in employing all instruments provided by the Treaties to overcome political impediments to integration?

The most obvious of these instruments is, of course, the Commission's monopoly of legislative initiatives. But these may be blocked by conflicts among national governments in the Council. Initially less obvious was the strategic usefulness of the Court's monopoly of Treaty interpretation and of the Commission's power to enforce such interpretations through Treaty infringement prosecutions. But it seems that this potential was quickly perceived by Europe-wide groups and networks of "Euro-lawyers" in academe and legal practice. These generated a literature that developed and disseminated the doctrinal foundations of an autonomous European legal system with direct effect and supremacy over the law of member states; they prodded the justices of the European Court to adopt these doctrines; and they collaborated in organizing test cases that would allow the Court to assert them (Alter 2009: Chapter 4). And they also trained cohorts of idealistic young lawyers who wagered their future on the prospect that the domain of European law would be broadened and deepened to provide for fascinating careers promoting the cause of integration in academe, in the legal services of European institutions, in business and in private practice.

Hence the Court had the full support of the Euro-Law community when, in the 1970s, it widened the

definition of “nontariff barriers to trade” and introduced the principle of “mutual recognition” as an alternative to legislative harmonization. Instead of being challenged as an usurpation of the amendment powers of the “Masters of the Treaties” and of the legislative powers of the Council, “Integration through Law” was hailed as a brilliant strategy which, finally, had generated the momentum that was able to overcome political resistance to deeper integration (Cappelletti et al. 1985). Moreover, once the Court had opened a bypass around the political logjam in the Council, the Delors Commission was able to generate political support for the Single European Act and the Internal Market program. Continental governments and political parties with pro-European preferences would back these initiatives on normative and economic grounds while the generally anti-European British Conservatives agreed because they liked the liberalizing effects of the program even more than they disliked the empowerment of European institutions (Moravcsik 1998; Jabko 2006).

In any case, however, “Integration through Law” - like the US Supreme Court’s anti-segregation law ³³ has been 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 outweighed by the real and anticipated benefits of Europeanization. In Germany, for instance, the constitutional court has repeatedly found it necessary - most dramatically in its decision upholding the Lisbon Treaty - to reprimand parliamentary majorities for neglecting their constitutional obligation to scrutinize European legislation and Treaty revisions that reduce the domain of democratic self-determination at the national level.³³ If that call to duty were heard, the unquestioned support for integration may be contested even in the profoundly pro-European German politics.

5. The Horizontal Impact of Integration by Law

But these are debates among political elites that do not explain why voter participation in European elections is falling and why 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; 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 opportunities of the elderly;³⁴ they had required Austrian universities to admit German students who failed to qualify for medical education at home;³⁵ they had subordinated the right to strike to the freedom of establishment,³⁶ the right to

33 BVerfG, 2BvE 2/08, 30.06.2009.

34 Mangold, C 144/04, 22.11.2005

35 Republic of Austria, C 147/03, 07.07.2005

36 Viking, C 438/05, 11.12.2007

collective bargaining³⁷ and legislative wage determination³⁸ to the freedom of service provision, and the legislative determination of corporate governance³⁹ 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. Reich 2008; Mayer 2009).

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 ensuring 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 (Schmidt 2006). And 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 bi-polar, concerned with the accommodation and balancing of the equally legitimate concerns of central and sub-central levels of government. These balances differ between Switzerland, Belgium, Germany or 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 re-assertion 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 sub-national 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 the technocratic effectiveness and efficiency of regulations at European and national levels, but ignores the normative and political salience of the concerns at stake. Moreover, its prescriptive content becomes indeterminate when the capacity for national solutions is affected by differences in size, wealth and administrative organization. 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. But it provokes a major normative difficulty in Sweden, where ever since the 1930s wages have been determined exclusively by collective agreements among highly organized and encompassing unions and employers' associations (Meidner/Hedborg 1984; Edin/Topel 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.

37 *Laval*, C 341/05, 18.12.2007

38 *Rueffert*, C 346/06, 03.04.2008; *Luxembourg*, C 319/06, 19.06.2008

39 *Volkswagen*, C-112/05, 23.10.2007

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*”. First of all, it is entirely up to the Court to determine which national concerns will at least be considered 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 concern 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.⁴⁰

The question is if this could be different. At the level of black-letter law, 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 none of these prohibitions would or could prevent the Court from extending the reach of Treaty-based liberties into the policy areas which the Treaty had tried to reserve to its member states.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 a core of national autonomy needs to be protected. The German constitutional court tried to do so in its recent judgment on the Lisbon Treaty by postulating limits to European powers in areas where political decisions are

40 Generally, that is, but not in every case. In *Preussen-Electra* (C 379/98, 13.03.2001) 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, 12.06.2003), Austria’s non-interference with a demonstration that had temporarily blocked the Alpine transit from Germany to Italy was not seen as an impediment of the free movement of goods; and in *Doc Morris* (C 171/07, 172/07, 19.05.2009) 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.

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. See e.g. C 158/96, 28.04.1998 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.”

specifically shaped by pre-existent cultural, historical and linguistic understandings (“*Vorverständnisse*”).⁴³ Among these, the court included regulations of language, religion, education or family law. It is indeed true that these “socio-cultural” matters have not been at the core of pro-integration policies, and even in the Lisbon Treaty they will not be 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 socio-cultural integration among the “peoples of Europe”. And even now, it is hard to imagine that national regulations of education or family law could remain unaffected by the Court’s interpretation of European mobility, non-discrimination and citizenship rights. In other words, autonomy could not be absolute, and a balancing test would need to be applied. But if that were attempted, it would also become clear that diversity matters, and that the normative salience of particular socio-cultural issues varies greatly from one member state to another (Kurzer 2001).⁴⁴

However, the German court also postulated a need to protect member state autonomy in policy areas shaping the economic and social conditions of national societies - which raises still more difficult problems. On the one hand, existing economic and social diversity among member states is not of the pre-political or even primordial nature of socio-cultural differences - which generally ought to be respected and protected, rather than shaped, by public policy. It is to a much greater extent itself the product of purposeful policy interventions. And on the other hand, competences over the economy have *ab initio* been the centerpiece of European powers. And since their exercise would inevitably have an impact on social conditions, social-policy competences have been added in later Treaty revisions. In contrast to the socio-cultural sphere, therefore, there is no possibility of arguing for a general presumption of national autonomy in the socio-economic 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. These differences, which are all but ignored in legal discourses on European integration, have become 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) account of “the three worlds of welfare capitalism”, labeled “liberal” (or Anglo Saxon), “christian-democratic” (or Continental) and “social democratic” (or Scandinavian). This 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 one, introduced by Hall and Soskice (2001) identifies 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.

In both classifications, there is a “liberal” or “Anglo-Saxon” ideal type in which the role of the state is

43 BVerfG, 2 BvE 2/08, 30.06.2009, at § 249.

44 In national federal constitutions, if the socio-cultural 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).

reduced to a minimum. The “liberal welfare state” provides mean-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 consumer 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 “coordinated market economies” 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 go beyond social assistance to social security by ensuring retirement incomes, health care and unemployment benefits for all, and the Scandinavian welfare state goes even further by 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 policy of powerful and monopolistic unions, ensure a very high degree of social equality (Scharpf/Schmidt 2000).

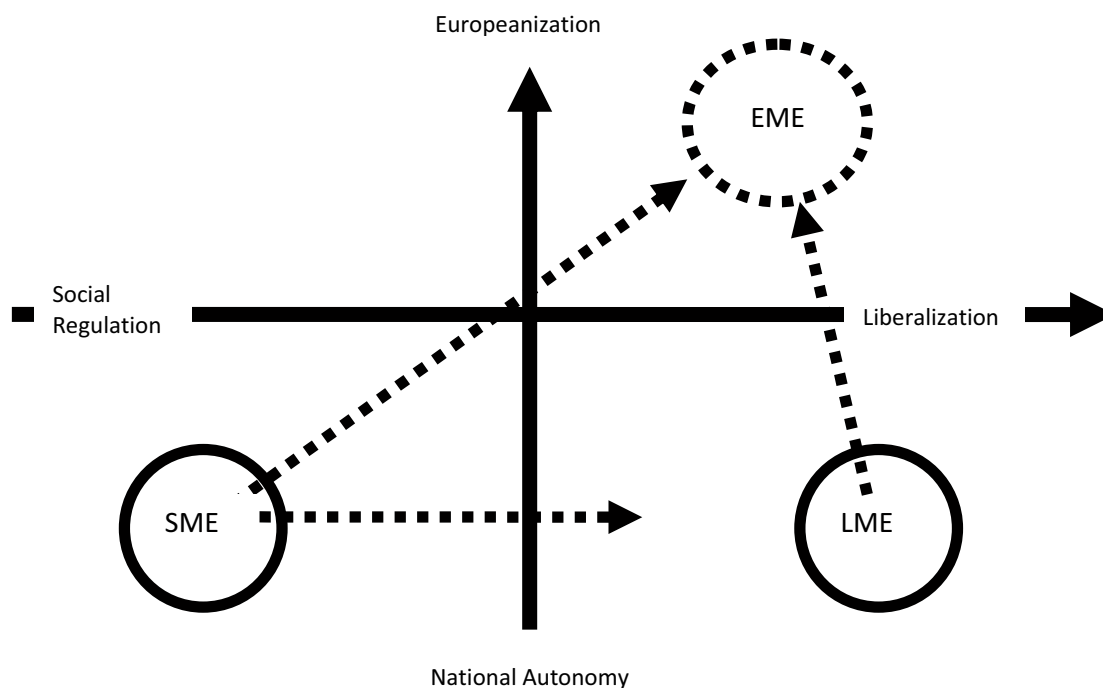
Both of these classifications are of course using “ideal types” that provide simplified descriptions of highly complex and country-specific configurations. Hence the assignment of a country to a particular type will not capture all features of the national institutional constellation,⁴⁵ nor is it possible to assign all countries to non-overlapping clusters (Ahlquist/Breunig 2009). And of course these types are derived from configurations that have matured in the “golden age” of post-war welfare states and mixed economies. Hence the distinctions have become more blurred through national responses to global and European challenges (Scharpf/Schmidt 2000a). Nevertheless, they have generated a rich body of comparative research that generally confirms the systemic importance of the traits that are 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, I suggest that the liberal market economies of the comparative capitalism literature will also be liberal welfare states, and that the coordinated market economies will have either Continental or Scandinavian types of welfare states. This heroic simplification then allows the construction of a two-dimensional space in which “Europeanization” and “National Autonomy” describe the vertical axis of European integration, while the socio-economic distinction between “Social Regulation” and “Liberalization” defines a horizontal axis that is generally ignored in the Euro-Law and Europeanization discourses. These can then be used to construct a two-dimensional diagram for locating the consequences which the transfer of competences from the national to the European level will have for member states

45 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 U.S.

whose existing institutions differ in the socio-economic dimension (Figure 1).

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



From what has been shown above, it should be clear that the institutions and practices of Liberal Market Economies will be least affected by the liberalizing and deregulatory impact of the Court's enforcement of economic liberties. By the same token, the governments of these member states (which by now include not only the UK and 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 areas which elsewhere had been reserved for the public sector or in other ways shielded against competition. They can thus be expected to profit from negative integration and to support whatever additional liberalizing and deregulatory initiatives the Commission will propose.

The situation is very different for countries located near the other pole of the socio-economic dimension. "Coordinated market economies" have built their comparative advantages in international competition on domestic institutions and practices that have in part complemented and in part displaced the mechanism of pure market interactions. Given their different production profiles, these coordinated economies are no less efficient than the liberal economies - 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 deregulatory effects of negative integration and liberalization. Thus the extension of competition law and the prohibition of state aids have removed many of the former tools of national industrial policy, and they have weakened or destroyed the role of public banks as an infrastructure of small and medium sized production firms. The Court's interpretation of the freedom of establishment does allow firms

to evade national rules of corporate governance by incorporating in a different jurisdiction.⁴⁶ And if, in the *Volkswagen* case, the Court saw the freedom of capital movement potentially impeded by a statute defining the blocking minority in the shareholder assembly,⁴⁷ there is every reason to expect the same verdict once the ECJ will 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. They are in effect enforcing a convergence of the political economies of all EU member states to the ideal type of a liberal market economy (Höpner/Schäfer 2007).

The situation is similar with regard to the characteristic features of different types of welfare states (Falkner 2009). Again, the privately provided social services, pensions and health care, which are characteristic of liberal welfare states, are not affected by the Court's interventions to ensure free mobility, undistorted competition and non-discrimination. Social Market Economies, by contrast, use a wide variety of institutional arrangements, including tax financed basic pensions, publicly provided social services and health care, social services provided by subsidized non-profit or private organizations, health care by public, non-profit or private providers financed by compulsory insurance or by subsidized private insurance, compulsory pension insurance, or subsidized private pension funds, etc. The capacity to finance such solutions is of course affected by the impact of European law on the revenue obtained from taxes on 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 non-discrimination rules.

In all cases where services and transfers are not exclusively financed by general taxation and provided by the state itself, European rules on the freedom of service provision, the right of establishment, state aids, public procurement and competition law may be invoked by potential providers to gain access to service and insurance functions whose organization differs, in one way or another, from the model of undistorted market competition. Of course, not all these challenges have already been launched, and not all will succeed. But the pressure of ECJ and Commission decisions⁴⁸ has, for instance, been sufficient to require the market-oriented reorganization of the traditional system of social services provided by publicly subsidized charities in Germany. And the Commission has plans to create competition regimes for social services that emulate the market-maximizing models established for the telecommunications, transport and energy markets (Ross 2007).⁴⁹ 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 by 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

46 C 212/97, 09.03.1999, Centros; Roth 2008.

47 C 112/05, 23.10.2007.

48 See e.g. Commission 2005

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

health care to avail themselves of more attractive or more timely services offered abroad at the expense of domestic taxpayers or insurance funds (Martinsen and Vrangbaek 2008), and the Commission has proposed a “directive on the application of patients’ rights in cross-border health care”⁵⁰ that would systematize and generalize the case law. Beyond that, the Court’s extension of the rights of personal mobility, non-discrimination and EU citizenship has reduced or eliminated the control of member states over the access of EU-migrants to nationally provided public and social services and transfers (Hatzopoulos/Do 2006; Wollenschläger 2007).

From the perspective of 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 which 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 are allowed to claim benefits which Danes and Austrians moving the opposite direction could not obtain. By weakening or eliminating the nation state’s control over the balance of contributions and benefits and the boundaries of its generosity in the name of transnational solidarity, the Court does indeed create incentives for transnational mobility and it may thus contribute to the interleaving of European societies. At the same time, however, it also creates special burdens on national welfare states providing high levels of collectively financed services and transfers, and it thus tends to favor 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 “Liberal Market Economies” with relatively low levels of social regulation and minimal welfare states. At the same time, the competitive opportunities of LMEs will increase as negative integration will open up and deregulate formerly protected markets in other member states. In Social Market Economies, by contrast, existing economic institutions will be systematically weakened by the deregulatory effect of negative integration and by the competitive pressures of mutual recognition while their welfare-state institutions will be challenged by European competition law, mobility rights and nondiscrimination law. In the diagram, therefore, the existing socio-economic regimes of SMEs will be pushed to the right toward a more “liberal” configuration.

Hence member states with SME institutions and political preferences would 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). But if they do so, they are confronted with a second structural asymmetry: European legislation, even after Lisbon, continues to be impeded by very high consensus requirements - which will generally favor status-quo positions. But this status quo has been re-defined by negative integration in favor of LME member states. Since they do not depend on European legislation in order to maintain their own socio-economic regimes, they are free to veto any European initiatives that would impose more demanding regulations on their liberal economies. As a consequence, the “European Market Economy” that could at best be brought about through positive integration will also resemble the socio-economic regimes of LMEs, rather than recreate a Social Market Economy at the European level. In other words, the top-left quadrant of the diagram, where the aspirations of pro-European Christian Democrats

50 COM (2008) 414 final.

and Social Democrats would have to be realized, cannot be accessed under the structural constraints of European integration.

6. Conclusion

In the end, therefore, 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, since member governments had initially remained in control of economic integration. So they were also able to preserve the conditions of "embedded liberalism" and thus to protect the integrity and diversity of national institutions and policy legacies against the pressures of economic competition. In fact, European "Social Market Economies" had been able to reach the peak of their development and of their institutional diversity precisely during the first two decades of the Community's existence. "Integration through Law" changed all that, and as consequence, European law, judge-made and legislative, is now cutting deeply into the substance of the socio-economic regimes of Social Market Economies.

Given the Court's interpretation of primary European law, combined with the diversity of socio-economic 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. The reason is that the legitimacy of judicial law-making, - 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 pre-existing 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 it in general terms which, in principle, could be applied in 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 "socio-cultural" concerns discussed by the German constitutional court vary in their normative and political salience from one country to another, and the socio-economic 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:

Obviously, 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 define European economic competences far too narrowly, whereas an equally general rule that would be acceptable in the most liberal member state might massively interfere with the political identity and legitimacy of SME member

states. And if the rule would aim at a compromise between these extremes, it would merely combine both problems at the same time. In other words, in the face of a normatively salient diversity of national institutions or policy legacies, a fair vertical balance could not be established by any general rule. It is thus entirely understandable that the Court never tried to 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 it with the possibility of exceptions granted pretty much at the Court's discretion.

But even if these exceptions were guided by principles, it should be clear that the *Cassis* formula could not accommodate the diversity of normative and politically salient national concerns. The "*mandatory requirements of public interest*" which 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 national measures, rather than to their normative significance and political salience.

In other words, the Court has no criteria for dealing with and assessing the "legitimate diversity" (Scharpf 2003) of the national institutions and policy legacies that are affected by its decisions. In each country, these have often been shaped by intense political conflicts and historical compromises. Individuals have come to take them for granted and to base their life plans on them. Thus the expectation is that policy changes will also be highly controversial in national politics and need to be legitimated by democratic processes. These national political processes may be short-circuited by judicial interventions from the European level. But if these are to be accepted as legitimate, the balance which they strike between European and national concerns must be extremely sensitive to the specific socio-cultural, political-economic and normative conditions in individual member states. 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 better placed as an umpire of European-national controversies. Emboldened perhaps by its own record of maintaining (or upsetting) the federal-Länder balance in Germany, it not only urged both houses of parliament to ensure that European legislation will not exceed the powers conferred to the Union, but it also reasserted its own competence to guard these limits. On the one hand, these are defined by an *ultra-vires* criterion that defines the outer limits of powers that have been delegated to the Union. And on the other hand, they are defined by the core elements of the national "constitutional identity" over which national control could not be relinquished in the absence of a referendum that would legitimate a new and very different national constitution. What matters more in the present context, however, is that the German court will apply these criteria not only to European legislation (or its transposition into national law), but also against extensive interpretations of Treaty clauses (2 BvE 2/08 at 238-241). In other words, the supremacy of European law and the ECJ's monopoly of interpretation are seen to be constrained by the "principle of conferral" (Art. 5 ECT; Art. 5 TEU Lisbon) and by the need to respect the constitutional identity of member states - which is defined by the national constitution and the national constitutional court's monopoly of

its interpretation.

Being embedded in the German political and normative culture (which has to a considerable extent been shaped by its own decisions), the *Bundesverfassungsgericht* has of course no difficulty in identifying a hard core of institutions and policy areas which ought to be shaped by democratic self-determination at the national level and guarded against European interventions. At the same time, however, the court emphasizes the “integration openness” and “Europe-friendly” character of the German constitution which it is interpreting and it takes pains to show that it fully shares and supports this basic commitment to the values of European integration. In other words, the *Bundesverfassungsgericht* avers its own ability and willingness to strike a fair balance between European and national concerns in its future decisions.

On the basis of its past record, there is 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, and 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 the cumulation 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 dual 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 re-establish a workable balance between “community and 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 civil war - as the assertion of John C. Calhoun’s “nullification” doctrine had done in the United States (Bancroft 2008; Ellis 1989). But it may still have severely disruptive effects in the European Union as well.

Needed instead are procedures that facilitate the mutual accommodation of European and national concerns. In this, it makes sense to leave the definition of fundamental national concerns to national governments or courts, rather than to the uncertain empathy of the ECJ. But there must be a possibility of review in the light of similarly 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 seen 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 will 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 socio-economic regimes at the national level and it also exerts a continuing liberalizing pressure on European legislation. Moreover, they should understand that the socio-economic asymmetry of European law is caused by structural conditions whose effect does not depend on the ideological orientations of members of the Court or of the Commission. For the same reason, it cannot 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 the unquestioning acceptance of policy choices dictated by non-accountable judicial power 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 “Integration through Law” can be contained.

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