The Economics & Politics of European Integration
Chapter 2: Facts, Law, Institutions and the Budget

Chapter Overview
- Economic integration: elements & omissions
- 3-pillar structure
- EU law
- Institutions: the "Big-5"
- Legislative processes
- The budget

1. Economic integration in the EU
- 1958 Treaty of Rome (ToR) is fountainhead of economic integration:
  - Most economic integration up to 1992 Maastricht Treaty was agreed in ToR; subsequent treaties fostered the implementation of policies agreed in principle in 1957.
  - ToR now called "Treaty Establishing the European Community";
  - Under the Lisbon Treaty ToR will be called "Treaty on the Functioning of the EU".
- Best to think of ToR's economic integration as a plan for 'unified economic area' (from 1950s perspective).
  - "4 freedoms": goods, service, workers & capital agreed in ToR.
  - Common policies where necessary (1950s perspective).

Main Elements
- Free trade in goods.
  - Eliminate tariffs, quotas and all other barriers that act like tariffs or quotas.
- Common trade policy with the rest of the world.
  - Formation of a Customs Union necessary to avoid controls inside EU (Rules of Origin); also forces a degree of supranationality.
- Ensuring undistorted competition (to avoid other policies offsetting trade barrier removal). Main ones:
  - State aids regulated by Commission (most prohibited),
  - Anti-competitive behaviour regulated by Commission,
  - Approximation of laws (i.e. harmonisation) necessary to ensure free movement of goods,
  - Taxes (weak restrictions aimed at preventing subsidies via lower tax rates for some firms); no explicit harmonisation or coordination.

Main elements (cont’d)
- Unrestricted trade in services.
  - ToR established principle of freedom of movement of services, but implementation has been hard.
    - Barriers are domestic economic regulations (e.g. banking regulation may raise barriers to foreign banks);
    - these are not explicitly coordinated by ToR, so EU cannot mandate liberalisation.
    - Single European Act made some progress, 2006 EU Services Directive made more.

Main elements (cont’d)
- Labour and capital market integration.
  - Free movement of workers (not people) in ToR.
  - Free movement of capital was in principle but many loopholes.
    - 1950s economists sceptical about capital mobility (Inter-war problems);
    - most EU nations retained capital controls until the Single European Act.
Main elements (cont’d)

• Exchange rate (ER) & macroeconomic co-ordination
  – ToR includes mechanisms for macro coordination, and ER are ‘matter of common interest’, but coordination informal.
  – SEA brought EMS into Treaty framework
  – Maastricht Treaty made big step to ER & macro coordination (Chapters 13 and 15).

• Common agriculture policy (CAP).
  – Commitment in ToR but no details; CAP set up in 1962.
  – Used to be a much more important sector than it is today
    • In France about 1/3 of population was involved in agriculture in 1950s; today less than 5%.
    • See Chapter 12.

Omitted elements

• Social policies.
  – Argument was that ‘general policies’ (i.e. not sector specific) did not distort competition and so did not need to be harmonised (contrast with competition policy).
    • Gains to harmonisation small.
  – Political costs of harmonisation very high.
    • Social policies touch workers lives and EEC6 had very different approaches.

• Single currency.
  – 1950s economists very sensitive trade integration & ER stabilization connection (avoid competitive devaluations).
  – EU founders believed fixed ER important to economic integration and political support for free trade.
    • e.g. inter-war experience of link between ER volatility and protectionist pressures.
  – But EU members were embedded in IMF’s worldwide fixed ER system “Bretton Woods” so no need for strong measures in ToR.
  – Still, 1st plan for single currency came in 1970 (“Werner Report”) as pressure on Breton Woods began to grow.

Maastricht: 2nd ‘foundation treaty’

• The Maastricht Treaty (known as Treaty Establishing the European Union) was:
  – Massive step up in economic integration
    • Monetary union, further capital market and financial market integration.
  – Massive institutional change that delimited extent of future EU integration more clearly (the pillars).
  – Beginning of explicit variable geometry (e.g. UK opt out of the common currency).

2. Organisational structure: 3 pillars & a roof

• Member State concern over “creeping competencies” led to pillars and creation of EU.
  – EU’s tendency to expand integration to new areas.
  – ToR goal “ever closer” union = Commission & Court interaction produced progressively deeper & wider integration.
• EC (old EEC) is now 1st pillar.
• The EU’s 3-Pillar Structure
  – 1st: Economics
  – 2nd: Security & Foreign
  – 3rd: Justice
• EU is ‘roof’ over the three pillars.
• The Lisbon Treaty will remove the pillar structure.

3 pillars & a roof

• Pillar structure limits the authority of EU Court and Commission to 1st pillar issues.
• Makes it clear that Member States in charge of 2nd and 3rd pillar issues.

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### 3. EU Law

- One of the most unusual features is EU legal system.
  - No other regional integration arrangement even close to extensiveness of supra-national law.
  - Formally 'EC Law' is part that has strong supranational elements, while 'EU Law' is more inter-governmental.
- EC Law applies only to first pillar (under the Lisbon Treaty, Court jurisdiction indicated for each issue).
- Basics of EU law is critical to understanding past & future developments of European economic integration.

### “Sources” of EC Law

- The EU Court created by the Treaty of Rome
  - Court then established the Community’s legal system.
  - Two landmark cases in 1963 and 1964.
- EC law was established on the basis of:
  - The EU institutions ensuring that actions by the EC take account of all members’ interests, i.e. the Community’s interest.
  - The transfer of national power to the Community.

### Key principles of EC Law

1. **Autonomy**
   - System is independent of members’ legal orders.
2. **Direct Applicability**
   - Has the force of law in member states so that Community law can be fully and uniformly applicable throughout the EU.
   - Regulations
   - Directives (to some extent)
3. **Primacy of Community law**
   - Community law has the final say: e.g., highest French court can be overruled on matters pertaining to intra-EC imports.
   - Necessary so Community law cannot be altered by national, regional or local laws in any member state.

### Types of EU legislation

1. **Primary legislation.**
   - Treaties.
2. **Secondary legislation.**
   - Collection of decisions made by EU institutions "acquis communitaire."
3. **5 types of secondary law**
   - **1. regulation**
     - Applies to all member states, companies, authorities and citizens. Regulations apply as they are written, i.e., they are not transposed into other laws or provisions. They apply immediately upon coming into force.
   - **2. directive**
     - May apply to any number of member states, but they only set out the result to be achieved.
     - Each member state what needs to be done to comply with the conditions set out in the directive (e.g., new legislation, or change in regulatory practice).
   - **3. decision**
     - Is a legislative act that applies to a specific member state, company or citizen.
   - **4. & 5. Recommendations and opinions**
     - These are not legally binding, but can influence behaviour of, for example, the European Commission, national regulators, etc.

### 4. Institutions: The “Big-5”

- There are dozens of EU institutions.
- Only 5 are really important:
  - European Council
  - Council of Ministers
  - Commission
  - Parliament
  - EU Court
- Other institutions matter in specific areas or at particular moments.
  - E.g. Court of Auditors.
(1) European Council

- (N.B. This is not the Council of Europe!)
- "Political guidance & leadership"
- Consists of the leader (prime minister or president) of each EU member plus the President of the European Commission.
- By far the most influential institution.
- Provides broad guidelines for EU policy
- Thrashes out compromises on sensitive issues, e.g.
  - reforms of the major EU policies,
  - the EU’s multiyear budget plan,
  - Treaty changes,
  - final terms of enlargements, etc.

(2) Council of Ministers

- Usually called by old name Council of Ministers (CoM)
  - formal name is now “Council of the EU” but Lisbon Treaty will switch it back to old name “CoM”
- Confusingly, the European Council and the Council of the EU are often both called “the Council”...
- Consists of representatives at ministerial level from each Member State, empowered to commit his/her Government
  - Typically minister for relevant area
    - e.g. Finance ministers on budget issues,
    - Council uses different names according to the issue discussed.
      - EcoFin (for financial and budget issues)
      - Agriculture Council (for CAP issues)
      - General Affairs Council (for foreign policy issues).

(2) Council of Ministers

- Two main decision-making rules.
  - On the most important issues, unanimity.
    - e.g. Treaty changes, enlargement, multi-year budget plan, Council decisions.
  - On most issues (about 80% of all Council decisions), majority voting
    - qualified majority voting (QMV).
- QMV is complex and is changing.
- Three sets of rules:
  - 1. Procedure that applied until mid-2004,
    - basic form unchanged since 1958 Treaty of Rome
  - 2. Procedure defined in Nice Treaty after 2004 until Lisbon Treaty is ratified,

Procedure that applied until mid-2004:
- Each member’s minister casts a certain number of votes
  - more populous members have more votes,
  - many fewer than population proportionality suggests
    - e.g. France (60 million citizens) has 10 votes, Denmark (5 million citizens) has 3
  - Total number of votes in the EU15 is 87.
- The threshold for a winning majority is 62 votes
  - This is called a “qualified majority,”
  - i.e. the majority rule is that about 71% of all votes are required to adopt a proposal.
(3) The Commission

- European Commission is at the heart of the EU’s institutional structure.
- Driving force behind deeper and wider European integration.
- Has three main roles:
  - propose legislation to the Council and Parliament,
  - implement EU policies
  - surveillance and enforcement of EU law
  - “guardian of the Treaties”

Commissioners are chosen by their own national governments.
- subject to political agreement by other members.
- Commission, the Commission President individually, approved by Parliament.

Commissioners are not national representatives.
- should not accept or seek instruction from their country.
- Appointed together, serve for five years
  - current Commission’s term ends in Jan 2010, runs in parallel to European Parliament terms but 6-month lag.
- Each Commissioner in charge of a specific area of EU policy.
  - Directorate-Generals or DGs

Executive powers.
- Commission executive in all of the EU’s endeavours,
- power most obvious in competition policy and trade policy.
- Manage the EU budget, subject to EU Court of Auditors.
- Decision making:
  - Decides on basis of a simple majority, if vote taken.
  - Almost all decisions on consensus basis.

Two main tasks:
- Oversees EU institutions, especially Commission;
- Shares legislative powers, including budgetary power, with the Council and the Commission;

Organisation:
- 785 members (MEPs) in EU27;
- Directly elected in special elections organized by member nation.
- Number per nation varies with population but rises less than proportionally.

Democratic control:
- Parliament and Council are the primary democratic controls over the EU’s activities.
- MEPs directly elected so in principle a way for Europeans to have a voice.
- In practice, however, European Parliamentary elections dominated by standard left-versus-right, and purely local issues rather than by EU issues.
- Voter turnout for EP elections has been falling since direct elections began (even thought EP getting more powerful).
- The Lisbon Treaty makes few changes for the Parliament.

MEPs per Members (EU27)
5. Legislative processes

- Main procedure: **codecision procedure.** Gives the Parliament equal standing with the Council after a proposal is made by Commission.
  - used for about 80% of EU legislation.
- The codecision procedure requires:
  - Commission’s proposal to be adopted by the Parliament (deciding by simple majority) and Council of Ministers (deciding by qualified majority).
  - If the Parliament and/or the Council disagree, proposal only adopted if a Council-Parliament compromise can be reached.
- Lisbon renames this **“Ordinary Legislative Procedure” (OLP).**

5. Legislative processes

- Other procedures
  - **Consultation procedure**
    - used for few issues. Parliament only gives opinion
  - **Assent procedure**
    - e.g. decisions concerning enlargement
    - Parliament can veto, but cannot amend proposal
  - **Cooperation procedure**
    - historical hang-over
    - Quite similar to codecision procedure
    - Like codecision procedure but Parliament’s power to amend is less explicit.
- Lisbon Treaty eliminates all but **unanimity and OLP (with minor exceptions).**

6. The budget: Expenditure

- Expenditure is on 3 things:
  - Agriculture (about half).
  - Cohesion (about one third)
  - All else (rest), of which
    - Other Internal Policies, External Policies, Administration
- Note: 2007-2013 Financial Perspective changes names:
  - Ag = ‘Preservation and management of natural resources’ (CAP, fishing policy, etc).
  - Cohesion = Cohesion for growth and employment.
  - Other internal policies = ‘Competitiveness for growth and employment & Citizenship, freedom, security and justice.’
  - External policies = ‘The EU as a global partner.’

6. The budget: Expenditure

- EU’s budget must balance every year (**no debt**)
- Financing sources: four main types
  - Tariff revenue
  - ‘Agricultural levies’ (tariffs on agricultural goods)
  - VAT resource:
    - Like a 1% value added tax (reality is complex).
  - GNP based contributions:
    - tax paid by members based on their GNP.

Funding of EU Budget
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