

**THE FRAGILE STATE OF THE EUROPEAN UNION (EU)  
- ITS BATTLE FOR SURVIVAL WITH THE MEMBER  
STATES.**

**A thesis submitted in fulfilment of the requirements for the Master of Arts  
(Honours) in Politics in the Division of Humanities at Macquarie University.**

**BY**

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## **Summary.**

This work covers research carried out on the most important aspects of the development of the European Union (EU) and will prove that due to its organisation is inherently fragile. Of special interest were the stresses and tensions inherent in an organization that is largely supranational but in certain areas is required to act in an intergovernmental fashion with the Member States. The European Union's lack of streamlined voting procedures which requires intensive negotiations and bargaining, leads to compromises which usually satisfy no one completely and are considered to be the cause for the inherent fragility of the European Union. The developments over the last two years, especially the failure of the referenda in France and the Netherlands, and the fierce arguments over the Member States' contributions to the Union budget, as well as the fight over the budget's allocations, confirm the author's assessment.

No part of this work has been submitted for a higher degree to any other university or institution.

James Fox

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## ABBREVIATIONS

ACP	African, Caribbean and Pacific Ocean countries
ADAPT	Communit initiative concerning the adaptation of the workforce to industrial change
AFSJ	Area of Freedom, Security and Justice
ALTENER	Alternative Energy Programme
BATNEEC	Best available technology not entailing excessive cost
CAP	Common Agricultural Policy
CARDS	Community Assistance for Reconstruction, Development and Stabilization (Western Balkans)
CEC	Commission of the European Communities
CEEC	Central and Eastern European Countries
CEEA	Common European Economic Area (EU- Russia)
CEP	Common Energy Policies
CCP	Common Commercial Policy
CCT	Common Customs Tariff (also CET)
CEP	Common Environment/Energy Policy
CFI	Court of First Instance
CET	Common External Tariff (also CCT)
CFP	Common Fiscal Policy or Common Fisheries Policy
CFSP	Common Foreign and Security Policy
CIS	Commonwealth of Independent States
CJ/ECJ	Court of Justice/European Court of Justice
CJHA	Common Justice and Home Affairs
CM	Common Market
CMS	Common Mediterranean Strategy
COP	Corporate Operational Plan
Coreper	Committee of Permant Representatives
CP	Community Programme
CR	Committee of the Regions
CSCE	Conference on Security and Cooperation in Europe
CSF	Community support framework
CTP	Common Trade Policy or Common Transport Policy
DG	Director -General
EAFRD	European Agricultural Fund for Rural Development
EAGGF	European Agricultural Guidance and Guarantee Fund
EAP	Environment Action Programme
EBRD	European Bank for Reconstruction and Development
EC	European Community
ECB	European Central Bank
ECLAIR	European collaborative linkage of agriculture and industry through research

ECOFIN	Council of Economic and Finance Ministers
ECSC	European Coal and Steel Community
ECU	European Currency Unit
EDF	European Development Fund
EEA	European Economic Area or European Environmental Agency
EEC	European Economic Community
EES	European Employment Strategy
EEZ	European Exclusion Zone
EIB	European Investment Bank
EIF	European Investment Fund
EMS	European Monetary System
EMU	European Monetary Union or Economic and Monetary Union
EP	European Parliament
ERDF	European Regional Development Fund
ERM	Exchange Rate Mechanism
ESC	Economic and Social Committee
ESCB	European System of Central Banks
ESF	European Social Fund
ESPRIT	European Strategic Programme for Research and Development in Information Technology
EQUAL	Community Initiative for combating discrimination
EU	European Union
EUR	euro
EUROMAR FOR	European Maritime Force
EUROSTAT	Statistical Office of the EU
FIFG	Financial Instrument for Fisheries Guidance
FRY	Former Republic of Yugoslavia
GDP	gross domestic product
GNI	Gross national Income
GNP	gross national product
IEA	International Energy Agency
IEM	Internal Energy Market
IMP	Integrated Mediterranean Programme
INTERREG	Community initiative concerning border areas
IRTE	Integrated road transport environment
ISPA	Investment for Structural Policies for Accession
JHA	Justice and Home Affairs
LEADER	Rural Development Community Initiative
LIFE	financial instrument for the environment
MAGP	Multi-annual guidance programme

MARIE	Mass transit rail initiative for Europe
MCR	Merger Control Regulation
MEP	Member of European Parliament
MFP	Multi-annual framework programme
MLG	Multi-level Government
MTF	Merger Task Force
NAP	National Action Plan
NATO	North Atlantic Treaty Organization
NCB(s)	National Central Bank(s)
NGO	Non-governmental organization
NUTS	Nomenclature of Territorial Units
OCA	optimum currency area
OECD	Organization for Economic Cooperation and Development
OSCE	Organization for Security and Cooperation in Europe
PCA	Partnership and Cooperation Agreement
PHARE	Poland-Hungary Aid for Reconstruction
PPP	purchasing power parity/Polluter Pays Principle
QMV	Qualified Majority Voting
RACE	R&D in Advanced communication Technologies for Europe
R&TD	Research and technological development
REACH	EU Chemical Analysis Directive
REGIS	Community initiative concerning the most remote regions
RIA	Regional Impact Assessment
SAA	Stabilization and Association Agreement
SAP	Social Action Programme
SAP	Stabilization and Association Process
SAPARD	Special Accession Programme for Agriculture and Rural Development
SAPS	Single Area Payment Scheme
SCENT	System for a customs enforcement network
SEA	Single European Act
SEM	Single European Market
SFOR	Multi-national stabilization force
SFP	Single Farm Payment
SGP	Stability and Growth Pact
SME	small and medium-sized enterprises
SMP	Single Market Programme
SNA	Sub-national Authorities
SPD	Single Programming Document
TAC	total allowable catch

TACIS	Technical Assistance to the Commonwealth of Independent States
TEEC	Treaty establishing the European Economic Community
TENs	Trans-European Networks
TEU	Treaty on European Union (Maastricht Treaty)
THERMIE	Programme for the Promotion of European Energy Technology
TREVI	Terrorism, Radicalism, Extremism and International Violence (EU Internal Security Group)
UCTE	Union for the Coordination of Transmission of Electricity
URBAN	Community initiative for urban areas
VALOREN	community programme for the development of certain less-favoured regions by exploitng endogenous energy potential
VAT	Value added tax
WEU	Western European Union
WTO	World Trade Organization

# **THE FRAGILE STATE OF THE EUROPEAN UNION (EU) - ITS BATTLE FOR SURVIVAL WITH THE MEMBER STATES.**

## **Introduction.**

The European Union (EU) is now largely a supranational organization, albeit with at times strong intra-governmental influence. Although only a limited number of policy responsibilities has been delegated to the EU, these have a significant impact in virtually all aspects of life in the Union. But even those policies under EU control require a huge administrative contribution by the EU Member States. Some Member States have objected to that aspect and some have been “eurosceptics” for a long time, but now the whole EU is rendered by doubt and resentment. Centrifugal forces are at work and ‘nationalization’ of certain policies (e.g. agriculture) is likely to happen.

This work will investigate the stresses and tensions in the EU, its institutions and the Member States and will demonstrate that the arrangement as it has evolved over the last forty years is inherently unstable.

Although the negative influences that have led to the current dangerous phase of the EU’s development will be stressed, the many positive and beneficent achievements can not be ignored and will be mentioned.

Throughout this work the term European Union (EU) will be used wherever possible. Material considered not essential, but illuminating the topic discussed, has been placed in footnotes and is shown by numbers in the lower case, ie (1), (2), (7).

The EU has grown from the original six Member States to now twenty-five members. Each of the Member States has a unique political, social, administrative, economic and legal framework. Overall, each of the Member states had to make sacrifices and surrender cherished ideals in order to become a member of the organization. The compromises that have been made are impressive. But now there are questions being

raised in a number of Member States, whether membership was worth these sacrifices and compromises. The latest enlargement (2004) and the proposed adoption of the EU Constitution have now led again to a questioning of the benefits and a searching for possible other options. (Schilly, 10. 5. 2005)

The history of the EU is one of periods of stagnation and then of dramatic changes. The present upheaval is a consequence of a dissatisfaction which, as shown by Eurobarometer surveys, has built up since 1990. Despite this, politicians and officials continued with the agenda of the 1980s. (Mueller, Henrick, 2005)

What the governments of the then twelve Member States agreed to in the Single European Act (SEA) in 1986 had been realized: a common internal market and a common currency. That the world had changed since then only encouraged the generation of politicians around Francois Mitterand, Helmut Kohl and Jacques Delors in their efforts to “deepen” and “widen” the EU. They saw no contradiction in this. But they failed to prepare their peoples for the more brutal competitive business environment which would be caused by the EURO since 1999 and the accession of the Central and Eastern European states since 2004. The result is that more and more citizens associate Europe with their worst fears. Europeans consider unemployment to be the EU’s biggest problem, but only some 25 per cent believe that the EU is helping to solve it. All over Europe some 85 per cent connect the EU with job transfers to low-wages-countries. This does not bode well for the EU. (IHT, 21. 3. 2005)

How the politicians misinterpreted the trend in the 90s is shown by the declaration of the Prime Minister of Rhineland-Westphalia, Clements, that the European States would become obsolete and powerless within a short time. The EU and the regions would more or less take over. The idea as shown in the preamble of the Constitution, of ‘an ever closer Union between the peoples of Europe’, was still alive and well then.

Now, in the age of globalization, the Nation State is experiencing a renaissance. The rapid structural changes in the economy cause increased insecurity in the citizens.

They look for support from structures that are emotionally close to them - and this are still the Nation States, not the EU. At this stage it appears that Charles de Gaulle's "Europe of the Fatherlands" will prevail. Henrick Mueller (11. 8. 2005), the economist and political scientist claims that the most likely development in the near future is a backsliding to a common internal market while in all the other political areas nothing much will happen for a long time.

The following paragraphs appear to confirm this:

EU Ambassador to the US, Bruton, declared on 27. 4. 2005 "It is far too easy to take the European Union for granted. It is far too easy to underestimate both the fragility and the scale of ambition of a project that seeks to hold 25 or more ancient nations together in a Union of pooled sovereignty. It is far too easy to avert one's eyes from the existence of forces that would sap the European Union of the mutual confidence that holds it all together. It is far too easy to forget that the European Union is the worlds greatest peace process, in a continent whose history has caused more wars than any other".

Jose Manuel Barroso, the President of the Commission of the EU, warned "The European Union (EU) is now in danger of destroying itself". Jean-Claude Juncker, the then President of the European Council, confirmed this, he stated that "The European public's willingness to compromise national interests in the name of the European Union project is fundamentally weaker than in past decades and may threaten the pace of future integration". And "Europe has stopped being an argument by itself". (IHT, 21.3. 2005)

Due to this lack of willingness to compromise national interests to EU interests the European Union (EU) has reached a decisive crisis point. It could be argued that the EU has survived many crises, and yes, its best achievements were always negotiated when it was in crisis and under pressure of time. However, now a stage has been

reached when too many negative forces come together and a break-down of the EU appears to be a distinct possibility. (Peterson & Shackleton, 2002, p. 11; p. 364)

The many crises the EU had to overcome in the past are a clear indication of its inherent instability. The fact that only limited authority has been delegated to it and that the Member States still can influence even previously established procedures through the Council act as serious constraint. Any proposal submitted by the Commission to Council, even if it was previously agreed upon by the Member States' Permanent Representatives in COREPER, could be subject to prolonged negotiation and compromises. In some cases - see the establishment of the Cohesion Fund due to pressure by Spain - agreement and cooperation had to be bought with the promise of financing of projects of interest to the uncooperative Member State. As for most decisions unanimity was required, Member States often abused this system by demanding benefits or compromises in return.

Being dependent on the concurrence of all the Member States, EU legislation often came down to its lowest common denominator. The new European Constitution would have changed this largely as most decisions would have been subject to qualified majority voting (QMV), alas this was not to be. The unstable characteristics of the EU's establishment are clearly demonstrated by the rapid change of public perception of the EU's performance. Everything appeared to proceed smoothly until the referenda in France and the Netherlands were rejected, this has now been followed by the undignified spectacle of the heads of government and state fighting over the 2007-2013 budget.

How quickly things can change is shown by an article by the distinguished academic and author Andrew Moravcsik (2005) which he presented at a European Union Studies Association (EUSA) conference in autumn 2004 at Princeton University. In it he clearly outlined the authorities delegated to the EU, the obstructionist attitudes of some of the Member States and succinctly described the tensions between the various EU institutions and the Member States. He made the following assessment: "What we

see now is what we get. *My central contentions here are that this arrangement is truly stable, due to lack of functional pressure and institutional opportunities, and that the result is arguably a democratically legitimate form of constitutional governance*".

What a bold statement to make with all the known uncertainties. And times have proved him wrong. To avoid this happening to this work and to keep up to date with the exciting, rapid development, recourse will be made to original EU documents, current declarations by EU officials and newspapers from all over the world.

As will be shown further on in this chapter and in the separate chapters for the main policies, friction can arise by the action, or non-action of the EU, but it is considered that most of the EU's difficulties are the result of obstructionist action by the national governments in the Member States. This can be either straightforward opposition in the Council or by delaying, or non-implementing of Community legislation in the national codes.

Another problem noted was the European citizens' astonishing ignorance about the EU. Equally astonishing is the hostile attitude of some of the European press. Referring to the current 'pension scandal' (the EU allows officials to retire from age 45 on, at a time when national governments are increasing retirement beyond age 65 due to financial cost), the Kurier (2005) questioned whether the EU was still able to be rescued. It also quoted the following: *"to learn from mistakes - this principle is in the EU institutions unknown. Distance from the public, wrong decisions, incompetence together with arrogance, lack of proportion, control and responsibility are attributes with which Brussels has been blamed. And these accusations are justified"*.

But it also stated that European citizens' thinking and emotions were guided and influenced by politicians of all political parties. Heads of governments of many EU Member States are spreading anti-EU sentiments. Whenever a difficulty was experienced, the EU was blamed. Now they are harvesting the storm. Doubts and rejection of the European projects are increasing. Undoubtedly, the above sentiments

are correct in some instances, but it clearly is a “europhobic” view, as it completely ignores the impact of the Nation States.(1)

Separate chapters will be submitted for the main policies, but in this chapter the number of areas/policies below will be investigated that can influence the relationship between the EU and its Member States.

<b>Supranational/strongly favouring the EU.</b>	<b>Neutral</b>	<b>Strongly favouring the Member States.</b>
The growth of the EU and the gradual transfer of powers from the Member States.	The increased powers of the European Parliament (EP) and its shortcomings.	The reluctance of national governments to adopt progressive attitudes.
The impact of the European Court of Justice (ECJ)		The national contributions to the EU budget.
The formation of Policy Communities and multi-level governance (MLG)		The taxation differences between the various Member States.
The Commissions sole right to initiate legislation.		The EU Constitution.
The all-powerful Competition Directorate.		The demographic development.

It should be noted that the topics listed under “Strongly favouring the Member States” should under normal circumstances favour the EU, but due to recent developments they are used to strongly assert the Member States’ interests.

The reasons for above classification are as follows:

### **The growth of the EU and the gradual transfer of powers from the Member States.**

After the desperate war and post-war years, by the early 1950 a small group of six Member States had emerged that shared objectives and a willingness to sacrifice national sovereignty to achieve them. They signed the Treaty of Paris in 1951 which brought the European Coal and Steel Community (ECSC) into existence. The six

(Italy, France, Germany, Belgium, Luxembourg and the Netherlands) thus launched the process of supranational integration in Europe (Bulmer, 2001, pp. 6-8). The Treaty had a duration of 50 years and was terminated in 2002. It had achieved one of the most important aims: Peace in Europe.

The ECSC had two outstanding characteristics:

It had a set of strong, supranational central institutions - a model which was later employed for the EEC and Euratom,

The Treaty of Paris spelt out most of the detailed arrangements and reduced thus the need for secondary legislation - while the later Treaties had only limited details and require/d a never ending stream of secondary legislation.

In 1957 the Treaty of Rome was signed bringing into effect the European Economic Community (EEC) and the European Atomic Energy Community (Euratom) from 1. January 1958. The establishment of the EEC was a significant development in supranational integration as it continued the ECSC's model of identifying functional bases for joint policy making. Considerable new powers were delegated from the Member States to the supranational EU. Some of the more important powers delegated and functions of this Treaty were: The creation of a Customs Union, Agriculture, Competition Policy, State Aid, and the harmonization of laws. (Bulmer, 2001, pp. 13-14)

Since then several amendments have been carried out through the enactment of new treaties as shown below. Details of these treaties are shown in the footnotes as to a large extent later treaties rendered earlier ones obsolete. The treaties were:

The Merger Treaty of 1965 <sup>(2)</sup>

The Single European Act (SEA) of 1986 <sup>(3)</sup>

The Treaty on European Union (TEU), (Maastricht Treaty) of 1992 <sup>(4)</sup>

The Amsterdam Treaty (TA) of 1997 <sup>(5)</sup>

In 2001 the Treaty of Nice (TN) was signed. It provided for the amendment of the numbers of MEPs, the allocation of votes in the Council of Ministers, additional functions were made subject to QMV, in general the Treaty attempted to get the EU into shape to be able to absorb the 10 new members in 2004. (Hitiris, 2003, p.35; Nugent, 2003, pp. 81-92)

### **The impact of the European Court of Justice (ECJ).**

The Community Treaties charge the Court with the task of ensuring ‘that in the interpretation and application of this treaty the law is observed’.(Article 220 TEC) (Bradley, 2002, pp. 119-136) This broad statement did not require the Court to simply apply EU law, but in effect enabled it to base its judgments on general principles of law when these have been deemed relevant and applicable. Some of these principles that have been cited by the Court are: proportionality (the means used to achieve a given end should be no more than is appropriate and necessary to achieve that end), non-discrimination, adherence to legality, and respect for procedural rights. (6)

There is no clear reference in the treaties to the primacy or supremacy of EU law over national law. The ECJ overcame this by ruling in the *Simmenthal v. Commission Case (92/78)*:

“Every national court must, in a case within its jurisdiction, apply Community law in its entirety and protect rights which the latter confers on individuals and must accordingly set aside any provision of national law which may conflict with it, whether prior or subsequent to the Community rule”.

The primacy of EU law has now been generally accepted by the national courts.

*Due to the lack of precision in much of the EU’s statute law the ECJ is deeply involved in interpreting laws to the advantage of the EU and is creating new laws and policies. The ECJ is much more involved with “judicial law making” than are national courts.*

The ECJ does not mince words and is not encumbered with excessive modesty. In Case 6/64, *Costa v. ENEL*, the ECJ stated:

“By creating a Community of unlimited duration, having its own institutions, its own personality, its own legal capacity of representation on the international plane and, more particularly, *real powers stemming from limitation of sovereignty or a transfer of powers from the states to the Community, the Member States have limited their sovereign rights*, albeit within limited fields, and have thus created a body of law which binds both their individuals and themselves”. (Nugent, 2003, pp. 235-258) The Commission readily takes Member State governments to the ECJ if it considers that EU laws have been ignored or broken.

### **The formation of Policy Communities and multi-level governance.**

“Policy communities”, also called “policy networks”, are explained as being arenas in which decision-makers and interests come together to mediate differences and search for solutions (Nugent, pp. 490-492). Factors identified as being conducive to policy networks are: the informal nature of much EU policy-making; the multiplicity of interests at EU level that are anxious to have access to policy-makers; the highly technical - almost non-political - nature of much EU policy content; the powerful policy positions held by senior officials, especially in the Commission and especially in the early stages of policy making; and the heavy reliance of officials on outside interests for information and advice about policy content and policy implementation.<sup>(7)</sup>

Peterson and Shackleton (2002, p. 359) report that the trend towards more collective governance in Europe has remained unbroken, despite the disappearance of the ‘permissive consensus’. But, with the current political situation, when everything is being questioned, it is considered that the above assessment has now been overtaken by more hesitant moves towards unification. The Member States’ desire to keep control of essential functions is indicated by “*Europeanization*”, instead of “*Communitarization*” of policies, the Common Foreign and Security Policy (CFSP), and Justice and Home Affairs (JHA) are examples of this process. By “*Europeanization*” is generally meant the delegating of powers to an

intergovernmental organization, while “Communitarization” means the handing over of powers to the EU and making them subject to EU legislation.

Fenna (2004, p. 261) argues that strong, autonomous interest groups create structural obstacles to policy-making and leave the state “weak”. In reference to the EU it is interesting that the Commission encourages the formation of representative sub-national groupings. These could be regional or even local and could be anything from NGOs to a temporary collection of private persons. The term multi-level governance (MLG) is used for these networks. *The Commission states it is doing this in order to ‘democratize’ decision making in the EU. However, there could also be the desire of the Commission to break down the strangle-hold nation states have in controlling dealings with the EU.* Some Member States definitely have been adverse to encourage MLG, see the hesitant adoption of this policy in especially the southern Member States. The Commission overcame this by making MLG compulsory if the Member State wanted financial assistance. (Majone, 2002, p. 320; Reg. (EC) No. 1783/99)

### **The Commission’s sole right to initiate legislation and its increased reference to “subsidiarity”.**

The Commission is by many Europeans considered to be a monster and the term “moloch” is often used. This wrong impression of its size is one of the many cases where the population is ignorant about the EU. Nugent (2003, p. 118) states that in 2002 the Commission had a staff of fewer than 22,000. (EU Member States average around 300 civil servants per 10,000 inhabitants as against 0,8 per 10,000 for all EU institutions). Of this number only some 6,000 were involved in policy-making. However, that relatively small number manages to churn out legislation by the thousands. There used to be 4,000 regulations, 2,000 decisions, and 120 directives per year, but since the completion of the Single European Market with a simplified legislative framework, only some 2,000 legal instruments were enacted in 2001. (Nugent, 2003, p. 241)

The Commission is fortunate that it can work away from the political pressures to which national governments are subject, it also restricts itself to policy-making while

the onus is on the Member States to adopt laws into the national legislation and to ensure that they are complied with. But the lack of this restraining influence appears to encourage excessive law-making by the EU. Schilly (10. 5. 2005) reports that many French voters fear that they would be exposed to an uncontrollable flood of laws from Brussels, which would destroy the social security net.

This becomes critical when some laws are passed that are not properly thought through and are either embarrassing for the EU or extremely costly for the Member States. An example is a directive issued regarding the size and weight of coffee and its packaging. This was brought to attention by the Commissioner for Industrial Development who said he could not see why the Commission should get involved in such ridiculous matters. This is especially baffling as the need for such legislation was supposed to have disappeared with the “Cassis de Dijone” case, which provided for the acceptance of a product by other states, if it was legally approved in a Member State. (Nugent, 2003, pp. 254-255) He promised to reign in such unnecessary legislation. (8)

It is unfortunate that the Commission also appears often insensitive to the political climate pertaining at the time. This is the case with a directive being forwarded to the EP regarding the protection of employees from “natural sources of optical rays” as they call it so quaintly in EU bureaucratize, sunshine is not good enough. The 42 page document is causing furor, but the Commission maintains that the matters covered are common sense and no special demands are made of employers. Industry representatives however feel that those vague rules could grow in praxis into an expensive programme as have so many others in the EU. Industry demands that Brussels should ease off and retract this latest potentially expensive and job limiting regulation. (SZ, 27. 6. 2005)

**The all-powerful Competition Directorate which has an influential section of economic purists.**

The Commission's Competition Directorate is without doubt the most powerful and also the most feared. Its determination to enforce a 'level playing field' in the EU, regardless of any negative results has often led to frustration and anger from Member State governments.

It is accepted that an effective competition policy is necessary for an open and integrated market. To try to improve this policy and ensure that it is sufficiently effective, the EU has adopted a twin-track approach. First, the Commission has become much more active in examining cases of apparent malpractice. Using its powers as investigator, prosecutor, judge and jury (though with its decision subject to appeal to the ECJ) it has been more willing to take action against Member States. Second, legislation designed to broaden the competition policy base has been approved. For instance, the 1989 Company Merger Regulation gives considerable powers to the Commission to disallow or set conditions on mergers that it judges will have an adverse effect on competition. Note, it was competition and not employment that was of greater concern. (Nugent , 2003, p. 303)

Kipping (1998, p. 499) already reported then that two officials of the Commission declared that "disputes about the shape of EU industrial policy have heightened among the policy-makers" and that there were "Two camps that were violently opposed. The first was in favour of an active industrial policy leading to the creation of pan-European champions able to compete on world markets. The second camp was in favour of a passive industrial policy, strictly limited to horizontal measures. It recommended firm adherence to market mechanisms and strong enforcement of policies that prevent the distortion of competition". It was stated that France and the Southern European countries were members of the first camp, while the UK represented the opposite view. Now, it can be fairly accepted that most of the Member States are in favour of more positive industrial action in order to boost employment.

However, the Member States' views have not yet penetrated Brussels, it is no wonder that EU citizens question the value of EU membership. The "Cross-Border directive" ( 9) and the phase-out of the "Multi-Fibre Agreement" demonstrate this. ( 10)

## **The increased powers of the European Parliament (EP) and its shortcomings.**

The European Parliament (EP) has come a long way from being the appointed ‘Assembly’ of the ECSC to the elected parliament of the EU. It is now the only directly elected multinational parliament in the world and the only directly elected institution in the EU. It is claimed that its actual and potential role is therefore central to arguments about the “democratic deficit”, and whether the EU is democratic and its decisions legitimate. (Shackleton 2002, p. 95) Members of the European Parliament (MEP) of course have strongly supported the idea and claim that more powers and responsibilities would make the EU more democratic. Consequently, Member States have gradually transferred more powers to the EP. Over the years the following powers have been transferred:

1. It has to approve the proposed President of the Commission,
2. it has to give its assent to the accession of new Member States,
3. it has to agree to the Budget proposal of the Commission.
4. it has to agree with legislation for it to be able to be passed into law under the *co-decision procedure*,
5. Under the *consultation procedure* the EP is asked for an opinion on Commission proposals for legislation. Once that opinion is given the Council may take whatever decision it wishes.
6. Under the *cooperation procedure* there is a further reading by the EP and it can reject the proposed law by an absolute majority vote. Council then has to have unanimous agreement if it wishes to proceed with the law.

In addition to above many suggestions have been made which it was claimed would solve the alleged problem of the ‘democratic deficit’, amongst them were:

- The establishment of a second chamber for the EP,
- the transfer of legislation making power from the Commission to the EP,
- the change of the Commission into the second chamber.

(Shackleton, 2002, p. 114).

Although each of those proposals has its merit it is considered doubtful that they would achieve much. As a matter of fact if all the powers that MEPs have demanded over the years were granted and the EP were to become the EU's sole parliament it would then be subject to political pressures as are currently the national parliaments. The expert input which the Commission now gets through its committee system and the established negotiation procedures would be lost. The unsatisfactory US example of "pork barreling" would take over, and with some 25 Member States with their different outlooks and expectations all that can at this stage be imagined would be total chaos.

Anyway, it is considered that the demand for "more democracy" in the EU is to a large extent a furphy. Surely, the vast majority of political leaders in the EU know that *"The fundamental paradox of democracy is that empowerment undermines transparency"*. As Margaret Canovan (2002, p. 28) explains that democratic politics does not and cannot make sense to most people it aims to empower. The most inclusive and accessible form of politics ever achieved (democracy) is also the most opaque. It is considered that the only thing that would make the EU "more democratic" would be the Member States' acknowledgment that the EU is already democratic, perhaps more so than some of the Member States. After all, each decision is being submitted to representatives of the Member States in COREPER, and to elected political leaders in the Council of Ministers and finally in the European Council, where the heads of government and state give the final consent. In addition, the Commission is now closely liaising with the Member States' Parliaments with new legislation, and finally the European Parliament has to give its concurrence for most decisions.

Strangely, the one institution that is hoped would be the 'democratic' saviour of the EU has itself problems to solve. With its 732 MEPs the EP is experiencing stresses from the different factions and any embarrassing incidents are difficult to hide. It is considered that these shortcomings have a powerful impact on the citizens' perception

of the EU and that makes doubtful that the EP will become the supreme legislative body in the EU. (11)

All in all, it can be expected that until the MEPs clean up their act, there will be little further increases in the EPs' powers. (Shackleton, 2002, p. 114)

### **The reluctance of national governments to adopt progressive attitudes and to let the Commission change its policies and procedures.**

In a situation like the EU where everything has to be negotiated it is understandable if some governments try to gain as much advantage as possible. Some national governments have, generally speaking, been excessively partisan in their attitudes towards the EU, that is they were usually fostering their own ideas and to their benefit. Any change achieved usually took years and years of negotiations and compromises. Glaring examples are:

- a) France's refusal to agree to a radical overhaul of the Common Agricultural Policy, (Nugent, 2003, p. 399)
- b) The UK's refusal to sign up to the Social Charter, (Nugent, 2003, p. 313)
- c) Some Member States refusal to allow a prompt amendment to the Growth and Stability Pact. (BBCNews, 24. 3. 2005; profil, 27. 3. 2005)

Although the above matters have been gradually amended, their delayed implementation has led to considerable waste of funds and frustration. EU citizens do not see the possible difficulties some Member State governments may have in changing their policies, they see only the wastage. And as the wastage has to be paid by them they are not very enthusiastic in supporting the EU in its varied undertakings.

### **The national contributions to the EU budget.**

The Member States' contributions to the EU budget were relatively easy to accommodate when the economies were booming, but, now, with the major European economies being virtually in 'stagflation', things are different.

Member states are supposed to contribute 1,24 % of their GNP to the EU's budget, but as not all funds allocated are spent each year, the EU makes regular refunds and the contributions are therefore at some 1,20 % only. The Member States are now demanding that the contribution be reduced to 1 %. The Commission considers this to be insufficient and is prepared to accept 1,14 % and might even go below this percentage. (Kurier, 16. 5. 2005) This appears to be a rather reasonable, nay insignificant amount, however, if it is considered that the German GNP was in 2000 some 2,000 billion Euros its contribution therefore would be 24 billion Euros. (Artis & Weaver, 2001, p. 34) Of this amount some 14 billion flows back into Germany as part of the EU's payments for the Common Agricultural Policy, Regional Development and Social Assistance. So in effect, Germany's net payment is some 8 billion Euros per year. (New York Times, 30. 5. 2005)

The citizens see this huge amount but they are not told that the benefit of being in the EU is some 10% of the GNP. The German government is also playing petty politics for its local constituents. For example, Italy and Germany had proposed that the EU take over border protection, now however Germany says that Member States with outside borders should be responsible for the upkeep of the border protection system. (Financial Times, 16. 4. 2005)

The funding of the EU budget has now been blown out of all proportions.

French president Jacques Chirac has, in order to divert attention from France's torpedoing the new constitution, demanded that the UK give up their 'rebate'. (Currently some 4 billion Euro per year). The UK responded that they would be prepared to do so if the CAP (Common Agricultural Policy) was being reviewed and reduced. Stalemate. However, there is no need to panic at this stage, as the budget that is currently being negotiated is for the period 2007 - 2013. So there is still some 12 months time for a settlement. Even if no agreement is reached, payments based on the

current budget expenditure can be made in future. If no agreement is reached this will be critical for the new Members of the CEEC. For example, Poland can expect to get financial support of some 7 billion Euros in 2007, should no agreement be reached the payment then will be only some 3,5 billion Euros.

It is hurtful for the EU if Member States agree with certain programmes, but when it comes to funding the budget if they don't see a benefit for themselves they claim it is wasted. (Financial Times, 16. 5. 2005)

People also question why they should make hefty contributions to the EU budget when the EU can not control its expenditure. The EU has just advised that for the 2003 financial year a total of 922 million Euros has been misappropriated or disappeared. Investigations have revealed that it lost 270 million Euros in Custom Duties, (200 million is lost due to cigarette smuggling), 170 million Euros in Agricultural Subsidies and 482 million Euros in Structural Funds. (Kurier, 12. 5. 2005)

The Court of Auditors has advised the EP that it could only "sign off" on some 30 per cent of EU expenditure (up from 10 per cent only a short while ago), as the Member States have insufficient control and accountability as well as willingness to enhance their control and cooperation with EU authorities. (euobserver, 19. 11. 2005)

### **The taxation differences between the various Member States.**

Taxation is examined in detail in a later chapter. This chapter will therefore only highlight some of the negative developments which some of the Member States have inflicted on the EU and the EU's reaction.

Prior to the accession of the 10 new Member States on 1. May 2004, the fighting over taxation was a fairly low-key affair. As in so many other fields the national governments were intent on protecting their own interests and showed little concern

for other Member States. At that stage it was principally a fight over cross-border trade, especially with the duty-free imports of travelers. (12)

The EU's attempts to harmonize or equalize taxes were frowned upon. Especially the UK was adamant that taxation could only be leveled if the people had a right to vote. It was pleased to point out to visitors to Parliament that the last person who tried to raise taxation was beheaded and only Parliament had the power to deal with taxes. (Die Presse, 10. 3. 2005)

However, with the new Member States a new wind is blowing. The new states have a refreshingly open attitude towards taxation. (Profil, 13. 3. 2005) They are prepared to experiment and have Ireland with its low tax rates as an example. Taxation rates are generally between 10 and 20 % below the old established Member States' rates. They freely admit that this taxation level will attract investment and will help them to catch up with the rich, old Member States. (Commission Press Release, STAT/05/25)

The plan works. Huge investments in technology industries, but especially car manufacturing have been made in the Central and East European Countries (CEEC). And in 'old' Europe companies are closing down. The tax base in the old Member States is shrinking while payments for social services are climbing. Bitter accusations are already leveled at the new Member States. (13)

Reviews of the tax systems are now carried out in most European states. (IHT, 19. 3. 2005) It appears that the EU's attempts to "harmonize or equalize" taxes may now succeed after all.

### **The EU Constitution.**

This is currently one of the hottest topics in Europe. After years of negotiating a draft Constitution was finally agreed upon by the Heads of Government or State of all 25 Member States. However, some of them have now realized that they would possibly

not be able to get away with passing the Constitution in Parliament only and they decided to “let the people decide”. What folly. This opens the door to populist agitators - see Le Pen in France and Haider in Austria - who are virulently opposed to EU membership, and thus increases the likelihood of its rejection. (Surel & Mueller, 2002, pp. 139-175)

It is generally accepted that politics in the EU are elite driven. (The News-Press, 14. 4. 2005) All the politicians know the benefits they get from the EU, while the citizens only see the foibles and rorts that happen. The national governments tactics of blaming the EU for every shortcoming is now coming back to haunt them. (International Herald Tribune, 22. 4. 2005)

One could be forgiven if one suspected that some of the ‘leaders’ actually wanted the acceptance of the Constitution to fail. (Kurier, 20. 4. 2005) The history of plebiscites is rather depressing. Witness Norway, there a small majority prevented the country to join the EU. A similar case happened in Switzerland, there the reliance on so-called democratic referenda has led to frustrating delays and caused a certain legislative sclerotic state. There, some proposals have taken up to 20 years before being accepted. Small special interest parties can torpedo a sound proposition, and as mentioned above, populist politicians can and do frustrate the political process, even in Switzerland. ( Kitschelt, 2002, p. 15, pp. 191-193)

It is appropriate to conclude this chapter with some more words of wisdom from John Bruton, the EU Ambassador to the US:

1. The truth of history is that nothing is ever inevitable. Everything that is built can be destroyed. If this is true of physical buildings, it is even more true of habits of thought and action that have been built up in people’s minds. A habit of consultation, consensus and compromise is something that is all too easy to destroy.

2. Previous Treaties were the result of closed door diplomacy, this one was the result of an open dialogue with civil society. All those who are vocal today in their objections had the opportunity to put their views forward through their parliamentary representatives at both national and European level.
3. If a Member Country decides to have referenda on complex questions, it is asking voters to take the place of its elected legislators. One is asking the people to accept all the responsibility that goes with being a legislator. I challenge those who advocate a “NO” vote to say how they would fill the gap left by a rejection of the freely and openly negotiated Constitutional Treaty that is now before us for ratification.

But not all is gloom and doom, he also maintains that:

“As one looks at the facade of the European Union, everything looks fine and secure. Crises come and go of course, but knowledgeable insiders and historians reassure us that the Union actually thrives on crisis, and that each big step forward has usually been preceded in the past by the threat of major setback. The European Union is seen by such people as a benign inevitability”.

I pray he is right.

An interesting point in the EU is that due to their wide-spread impact many policies affect many people positively, but minorities are also often affected negatively. See the Chinese textile import and the Parliamentary salary decision as outlined in later chapters. So, as the saying goes, they are damned if they do, and damned if they don't. As these developments also reflect the peoples' acceptance of the EU, these will be shown where ever possible.

### **The demographic development.**

But there is another dimension to the problems Europe and the European Union face, the demographic development with its potential for explosive confrontations in all the

Member States. For many years already many have pointed out that the birthrate in Europe is insufficient to maintain the present population. Even the new Member States, the CEECs have diminishing populations. Due to the many different national, religious and social groups in the EU, the EU has developed powerful protective means in order to protect these groups. Its 'human rights' policies and 'multicultural' legislation are second to none. The citizenry has generally tolerated this and tacitly accepted the need that immigration might be necessary. As long as it did not hurt them. The violence and uprisings in France have now changed all that. But Europeans had already a foretaste through the murder of van Gogh in the Netherlands, the mass murders in Madrid and London and the "honour killings" of women in Germany.

For us here in Australia, so far away from all those places it seemed surprising that there were people who claimed that 'multiculturalism' in Europe was dead. Rod Liddle and Mark Steyn (The Spectator, 12. 11. 2005) in two excellent articles describe the immigrant situation in western Europe and the effect this has on the nation states of the EU. Rod Liddle states that there are many cities in the EU where the Muslim population is over 20 per cent, from Rennes in the south, through Lille, Brussels, Antwerp, Zeebrugge, Rotterdam, Bremen to Aarhus in Denmark. In France, the political aspirations of many Muslim organizations and especially the most important political Islamic organization on the Continent, the Arab European League, are for much greater segregation. The Arab European League likens assimilation or integration to rape and calls on Muslim to resist such cultural imperialism. The director of the Great Mosque of Paris, Dalil Boubakeur has requested the French Government that it grant Muslims autonomy within the state, to allow them, in effect to follow their own rules.

The population statistics in the foregoing and following paragraphs could not be proved 100 % satisfactorily, as France prohibits the collection of racial and religious details. This is a result of the Second World War, when the Vichy government was forced by the then victorious Germans to deport French Jews to concentration camps. The current law is to ensure that this will never happen again. Unfortunately the result

is that the French government is unable or unwilling to take appropriate remedial action. The percentages quoted appear to be the result of private research. A study of Arabic/Muslim and European statistics indicate that these figures are perhaps even too low. In France it is stated that Europe's largest Muslim population tends to live in urban ghettos mostly centered in the larger cities such as Paris and Marseilles. (Euro-Islam, 22. 11. 2005) While it is claimed that by 2010, the six largest cities in the Netherlands will have Muslim majorities. (American Muslim Voice, 22. 11. 2005) In view of the strong anti-French and anti-European sentiments expressed in these last two articles I am prepared to accept their message, even if one of them is only a forecast.

The above developments are offset by details in the 2004 World Population Prospects which show that all the European countries have declining populations. By 2050 it is calculated that for example the Ukraine will have a loss of 43%, Bulgaria 34%, Hungary 18% etc. (Web.inter.nl.net, 24. 11. 2005) In a news release Eurostat (31. 8. 2004) reported proudly that the EU25 population had increased by 0.4% in 2003. This was due to immigration (1,7 million) while the natural increase was 0.2 million. A detailed study of the report indicated that where there was an increase in fertility rates were countries with large Muslim populations.

Mark Steyn's article was a dissertation of the age groups. He showed that in France those aged 20 and younger about 30 per cent are said to be Muslim, while in the main urban centres they amount to about 45 per cent. Indications are that this demographic trend is accelerating. In France the tendency will be to accommodate them and to capitulate, but an unreconstructed minority (Le Pen? or another neo-nationalist strongman) will not be so obliging and will eventually act. In the meantime it will be the Muslims who develop a pan-European identity, because many have no particular attachment to France, Belgium or Denmark and they quickly grasp that cross-border parties and lobby groups will further enhance their status.

Steyn states that right now the US and the EU produce each about 25 per cent of global gross domestic product. Most analyst figure that by mid-century the US will

still be producing 25 per cent, as will India and China, but Europe will be down to 10 per cent. O'Sullivan of the National Review noted that the three global heavyweights are all strongly attached to traditional notions of national sovereignty, so European countries that have bet on EU-style transnationalism as a way out of their individual weakness are likely to find that, far from being the inevitable way of the world, it's already on the wane.

Steyn calls this development "the Eurabian civil war". He claims that the European governing class has failed and that conventional wisdom has run its course. If you carry on voting for the Euroconsensus, you are voting for a suicide pact. He states that this may be anti-European, but what matters is whether this prediction is right, and after the past couple of weeks that prediction looks better than the complaceniiks' view that there is nothing wrong with the EU that can't be fixed by more benefits, more regulation, more taxes, more immigration, more unemployment, more crime and more smouldering Citroens.

What a frightening prediction, he is right about the governing class being unable to rule decisively and the demographic forecasting also appears to be feasible, so could it happen? Yes, as long as the national leaders are so divided as they are presently this could well be the result.

### **Notes:**

( 1 ) There is now concern developing in the EU, and finally the Commission and Member States are trying to open up to the citizens. In Austria, the country with perhaps the lowest number of EU supporters, the Chamber of Commerce and the Government have combined with the Commission and financed a public relation bus which was to tour all over the country. It was supposed to spread the good news of the EU, alas the public interest was minimal. Spectators were mostly seniors. Some students of a nearby EU- college said that they never talked about the EU in class. The reasons were that Brussels was too far away and its operations were difficult to follow and rather boring.

( 2 ) In 1965 the Merger Treaty was signed with the effect of merging the principal institutions of the three communities from 1967. The three communities were then known collectively as the European Community. This merger indirectly increased the impact of the EU as the previously separate units were now able to present a focused entity. (Nugent, 2003, p. 57)

( 3 ) In 1986 the Single European Act (SEA) was signed which introduced the first systematic revisions to the founding treaties. Substantial additional competencies were transferred to the EU:

- the completion of the internal market,
- the reliance on the principle of mutual recognition of national product standards.
- the increased use of qualified majority voting (QMV) in the Council of Ministers.

- increased powers of the European Parliament (EP),
  - creation of the Court of First Instance.
- (Nugent, 2003, p. 58)

( 4 ) In 1992 the Treaty on European Union (TEU), (Maastricht Treaty) was signed. This Treaty entailed substantive revision and extensions to the existing treaties. It also shaped the EU into three pillars: the first pillar consists of EU activities and is thus supranational, its activities also come under the ECJ. The second pillar provides for a Common Foreign and Security Policy (CFSP), while the third pillar covers Justice and Home Affairs (JHA), i.e. police cooperation, combating drug-trafficking and fraud, regulating immigration and similar matters. The policies contained in the last two pillars were given greater prominence and were strengthened but they are “intergovernmental” and thus were outside the ECJ.

One of its main achievements was the introduction of Economic and Monetary Union (EMU) which was to be in operation by the end of the 90s. In return for agreement to this, the economically weaker Member States insisted on the creation of a Cohesion Fund to enable resource transfers to their economies. This was agreed to.

The TEU also introduced a ‘Social Charter’, from which the UK opted out. There were also policy developments regarding infrastructure, consumer protection and industrial policy. (Bulmer, 2001, pp. 19-20)

( 5 ) In 1997 the Amsterdam Treaty (TA) was signed. It introduced an ‘employment chapter’ partly to offset the impact of the EMU. Areas strengthened were environmental policy, public health and consumer protection. A programme was launched towards an “area of freedom, security and justice” (AFSJ), which involved moving some of the activities from the third pillar to the supranational first pillar. In addition the powers of the EP were enhanced and the provisions for majority voting in the Council were enhanced. (Nugent, 2003, p. 70)

( 6 ) It is interesting to note that albeit the EU law can be applied only to a limited number of activities such as the Common Commercial Policy, the Common Agricultural Policy, competition, the approximation of the laws of Member States to the extent required for the functioning of the common market, and the environment, the EU issues some 4000 legal instruments each year, and as they are required to be adopted by the Member States they now account for approximately 80 % of the Member States laws in the above mentioned areas, while over all the EU laws represent some 20 per cent of the total national laws.

( 7 ) In the EU there are numerous committees both permanent and even ad hoc ones in the European Parliament (EP), the Commission and Council. Lobby groups provide a welcome input from outside the EU. Rosamond (2000, p. 124) reports that Hussein Kassim suggested that the ‘elusive fluidity’ of the EU policy process means that there is little continuity and much fragmentation. However, Rosamond claims that policy network analysis requires situations of ongoing policy reproduction to work properly.

( 8 ) A costly directive is the recently proposed legislation that would require all items sold in the EU to have a chemical analysis provided. As this would involve everything from motor spare parts to milk products, businesses and Member State governments are objecting fiercely. They have estimated the cost of this directive would be some 5 billion Euros. This at a time when companies in most of the Member States are battling for economic survival due to the unprecedented pressure from the new CEECs and from China.

( 9 ) On 10. May 2005 the European Parliament has approved a cross-border merger law which had been proposed by the Commission some two years ago. The Commission has long argued for more cross-border deals to encourage the creation of a more competitive industrial landscape. Charlie McCreevy, the EU internal market commissioner stated: “The cross-border directive opens new ground. It is a major step in favour of EU businesses, which have been calling for the adoption of this text for many years”. (Financial Times, 10. 5. 2005)

( 10 ) This case shows where membership in the EU clearly is a disadvantage. Kobsak Chutikul of the Bangkok Post (11. 5. 2005) reports that with the phase out of the 1974 Multifibre Agreement on 1. January 2005, the Chinese textile industry started a major assault on the European market. It has been reported that imports of pullovers increased by 800 %, most other items by at least 50 %. China claims that it observes the principle of ‘free trade and the principle of comparative advantage’. However, its actions indicate more a well-planned attack on the world textile industry. Chinese companies had rented huge warehouses in the USA and in Europe in preparation for a ‘market invasion’

13 EU Member States are pressing the Commission to impose immediate restrictions without the mandatory two months of informal bilateral consultations and a further three months of formal talks under the aegis of the WTO. (Agence France Press, 9. 4. 2005)

China’s terms of accession to the WTO include a textile specific safeguard clause that allows WTO members to impose quantitative restrictions on imports of Chinese products if they are found to disrupt markets. Under this safeguard, members can limit specific products to an increase of 7,5 % above the preceding year’s import levels.

The WTO director-general Supachai Panitchpakdi suggested that countries struggling with a surge in Chinese textile exports should wait at least a year before taking protectionist measures. The EU trade commissioner Peter Mandelson said that the issue was complex. He has initiated investigations, but insisted that he did not intend to “start a trade war” with China.

In the meantime some 50 textile companies have closed their doors across Europe thus far this year. In Spain some 20,000 textile workers have lost their jobs in the first quarter of this year and Euratex, which represents the EU textile sector advised that it is expected that by next year a million jobs will be wiped out in the industry.

On the 11. June 2005 the EU reached an agreement with China to curb its massive textile imports into the EU. China complied by stopping all textile exports over a certain limit. Thousands of containers of clothes are now being held up in China. In Europe things are now slightly different. There, many companies tried to get on to the cheap Chinese textile bandwagon by ordering huge quantities of Chinese textiles. Most of them were prepaid. Some firms had spent huge amounts for national advertising campaigns, which of course is now a total waste. Now, many of the smaller firms face bankruptcy due to the cash payments made without getting the goods for sale. (faz-net, 21. 6. 2005)  
One case of be damned if you do, and be damned if you don’t.

If the Member State governments’ hands were not tied by having delegated international trade negotiations to the Commission, it is expected that they would have taken immediate action to stop this abuse of trade. No government could afford to let a large employer go bankrupt. Neither can the Commission afford to let the whole textile industry go bankrupt. (Chutikul, 2005)

( 11 )

- 1) In the EP the MEPs are grouped together according to their political association, that means that for example all socialists are sitting together and are supposed to vote as a block, but it has been found that national blocks are being formed in these groups. (Nugent, 2003, p. 223) This could be devastating if MEPs from a large Member State should decide to fight the established procedures.
- 2) The MEPs are nominated by their national parties but often do not seem to represent the present political establishment of their Member State. This is currently especially obvious as in the recent elections voters in the Member States actually voted for candidates from the opposition to the national government as a show of disapproval of the policies of the national governments. Until this feeling that the EP is not important and that the elections can be used as a protest against the national government, the latter will not delegate more powers to the EP.
- 3) There is a considerable number of “Euroceptic” MEPs, who are determined to destabilize the EU or to take their country out of the EU. They have relatively high publicity standing as they are prepared to highlight any shortcomings of their institution. This appears to be an ethical question,

if they do not support the EU, should they accept the emoluments to which being an MEP entitles them? But, as long as they inform the public of any shortcomings their presence might be beneficial for the democratization of the EU.

- 4) Due to the insistence of France, the EP has some sessions in Strasbourg and the larger part is now spent in Brussels. The moving from one location to the other several times each year is seen as a huge waste of time and money. The EPs apparent inability to stop this reflects poorly on it.
- 5) There was an attempt to agree to the payment of 9,000 Euros per month for each of the MEPs by the EU of the MEPs allowances, but, the Member States could not agree and MEPs are now paid by their national governments. The rates vary now from some 12,000 (Italy) to 1,000 (new members) Euros per month. The EP has now proposed a salary level for all MEPs of 7,000 Euros, this is supposed to take effect in 2007. In the meantime it has to be approved by Council. But there are already calls over lack of transparency and greed. The 'democratic' EP apparently tried to hide from the public the fact that each of the MEPs also gets a free superannuation amounting to some 1,900 Euros per month. This is supported by an extremely generous free health and medical benefit fund. Some claim that the above remuneration is a multiple of what parliamentarians or ministers get in the new CEECs. Thus it could cause friction. (Networld, 28. 6. 2005)
- 6) There are also highly lucrative daily allowances and extremely generous travel entitlements. The latter have now also been amended with the new salary scheme. From now on, MEPs get reimbursed actual travel expenditure. This means that from now on most of the MEPs will travel business class and thus cost the EU considerable money. The lack of control leads to rorting and the public finds it astonishing that such highly-paid legislators should find it necessary to rip-off their people.(Networld, 30. 6. 2005)

( 12 ) France refused to tax wine and had low tax rates on tobacco products, this led to a booming export trade with British travelers. France was the beneficiary.

Britain tried to stem the inflow of duty-free goods which cost it some 4 billion pounds per year by increasing customs personnel and strictly enforcing import regulations. France took the UK to the ECJ which ordered the UK to ease off on its travelers. (Associated Press, 8. 7. 2004)

Similar problems existed between Spain and the UK, (HM Customs, 10. 7. 2004; smokecheapnow, 10. 7. 2004) Scandinavia and the Baltics, Norway and Denmark with Germany. (Associated Press, 14. 7. 2004)

( 13 ) The German chancellor warned the new states that: "If they think they can get rich at the cost of others by having low tax rates and pinching jobs from them they have another think coming. It will not be tolerated". Due to Germany's precarious financial position which resulted mainly from its lack of reforms, the movement of plants to the East, the influx of lowly-paid workers and the tax short-fall of some 6 billion Euros for 2005, its government has indicated that it is not willing to be the paymaster of the EU. Especially so since it is now the eleventh in the EU's prosperity listing. (New York Times, 30. 3. 2005; FAZ.NET, 18. 5. 2005)

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## **REGIONAL DEVELOPMENT AND THE STRUCTURAL FUNDS.**

In this chapter the funds and financial instruments ( listed below ) used in the EU to foster regional development and cohesion will be examined. It should be noted that EU development policy is not static, but is constantly being reviewed and if required, amended. For example, the different funds were previously applied for one measure only, the Guidance Section of the EAGGF ( European Agricultural Guidance and Guarantee Fund ) would be used for agricultural development only, while now the Commission strives for 'complementarity and additionality' by combining several funds for one project.

For this reason the funds belonging to other EU Directorates will be included in this investigation. The historical background of the funds has largely been extracted from Andrew Evans' "The E.U. Structural Funds" (1999). Although it is now relatively

dated, the book admirably explains how political and economic developments necessitated the review and amendment of EU policies and shows how this resulted in the establishment of the various funds.

Although the 'Funds' have achieved considerable benefits and progress in some areas, there are many areas where results were not so beneficial, but perhaps were more intensifying certain existing negative conditions. Examples are: the modernizing of the fishing fleets when many areas are virtually fished clean; or providing IT training in remote, deprived areas and thus encouraging the movement to higher paying jobs in developed areas; the assistance to farmers in areas with poor agricultural soil, thus ensuring the area remains populated but is the money soundly spent? Such instances can be named for each of the EU funds. As is the usual story, anyone being supported keeps quiet, while dissatisfied people can jump up and down and loudly proclaim the "arrogance, stupidity and wastefulness" of Brussels. And they are the ones that get all the publicity. Brussels's attempts to publicize its contributions will never be able to compete with such negative reporting.

As will become evident, all funds are subject to environmental and competition policy considerations. Depending upon income levels, the Member States and the Commission have agreed to classify all areas in the EU in "OBJECTIVES". As these objectives play a role in all the EU Funds a short outline is considered essential here. Assistance can be given up to various levels and to meet varying needs.

***The objectives and their characteristics are:***

*Objective 1.* To promote the development and structural adjustment of regions whose development is lagging behind. Regions covered by Objective 1 are those where per capita GDP is less than 75 % of the EU average. A total of 69,7 % of Structural Funds is allocated to Objective 1.

*Objective 2.* To support the economic and social conversion of areas facing structural difficulties. Amongst areas covered are those under-going socio-economic change in

the industrial and service sectors, declining urban and rural areas, and depressed areas dependent on fisheries. A total of 11,5 % of the Structural Funds is allocated to this Objective.

*Objective 3.* To support the adaptation and modernization of policies and systems of education, training and employment. This Objective provides for formal assistance outside the areas covered by Objectives 1 and 2. A total of 12,3 % of the Structural Funds is allocated to the Objective.

Five per cent of the Structural Funds are set aside for what are known as *Community Initiatives or specific innovatory projects*, which are schemes managed by the Commission that might not otherwise attract funding. They are: INTERREG - cross border, trans-national and inter-regional cooperation. URBAN - revitalizing of depressed urban areas. LEADER - rural development and EQUAL - combating discrimination and inequalities in the labor market. (Nugent, 2003, pp. 312-313) Statistics relating to the objectives will be outlined further on.

The impact of environmental conditions on any programme is currently being reviewed. Industry and the states are asking for milder, more considerate new plans. The Commission has recently proposed the chemical composition regulation REACH which would require every chemical component in any of the EU's products to be shown. Industry maintains that this regulation's costs far outweigh its potential benefits and strongly objects to it. As will become obvious in this chapter, I consider the impact of the competition policy rules on any development proposal excessive. Perhaps stronger reliance on industrial policy could solve this problem. The requirement that aid for development for larger projects can virtually only be given if it is in the area of 'Objective 1' or if it has specific EU approval, is economic madness. This may have been acceptable when the EU economies were booming, but in recessionary times this should not be a requirement.

Attention is drawn to the fact that nearly all the EU funds had been anticipated as short-term intermediate measures, which were supposed to cease within a few short years. But as with so many of the EU activities, the funds became 'indispensable' for efficient economic management, took on a life of their own and kept on growing and growing - agriculture, social, and regional development, are proof of this.

It should be noted that many of the reported EU plans and forecasts had been made in anticipation of smooth adoption of the new EU Constitution and stable financial arrangements for the next seven years, from 2007 to 2013. Both these expectations did not come to fruition and will seriously affect the EU's future. This aspect will be treated more fully in the conclusion to this chapter.

The numbers given to the various paragraphs are not to imply their relative importance, they have been given for purely clarifying reasons.

In this chapter:

1. A short historical outline explaining the change in the policies will be made,
2. The funds will then be listed and explained. Each fund and instrumentality will then be investigated, its historical development and its application will be shown,
3. The Member States/regions with their entitlements will be outlined,
4. The administrative requirements in the Member States will be shown,
5. The impact of Regional Development policies on the states' multi-level governance (MLG) will be reviewed,
6. The impact of Regional Development policies on the Member States' economies will then be considered,
7. Recent developments and changes in the Commission's thinking regarding the best use of the funds will be examined.
8. Conclusion.
9. Addendum.
10. References.

Each of the EU's funds has its own characteristic, but what they have in common is that they provide financial assistance designed to support the attainment of objectives favoured by the Union. The provision of such assistance is said to be modification of the existing economic structure, in order to direct market forces towards an improved configuration. In this case it is the promotion of what the EC Treaty (1957) calls 'economic and social cohesion'. According to Article 159 of the Treaty, the Union funds are all to support the achievement of such cohesion. (1)

In its "Agenda 2000", the Commission reports that social demands on the funds were then pressing because of the moves towards admission of the Central and Eastern European (CEE) countries. Major reforms of EU legislation governing the funds are now essential to ensure more efficient use of EU assistance. (Evans, 1999, pp. 1-2)

## **2. The Funds and Financial Instruments.**

### ***"EAGGF, Guidance Section"***

Funds involved : Euros 4,300 million per annum  
Evans (1999, pp. 10-11, 115-144)

The Guidance Section of the European Agricultural Guidance and Guarantee Fund was created as an integral element in the establishment of the Common Agricultural Policy. It was expected that some of the common organizations of agricultural markets might not measure up to the objectives of this policy as listed in Article 39 of the EEC Treaty (1957) and thus could endanger market stability in a part of the Community. The Guidance Section was therefore established in order to enable the objectives of Article 39 to be achieved, and especially for the structural changes in agriculture, such as improvements to agricultural structures and the marketing of agricultural products necessitated by the establishment of the common market, to be effected. *This was supposed to be a transitional fund with a limited period of 12 years, but increasing needs were noted and had to be rectified. This became especially urgent when the lesser developed southern European states became members.*

Regulation 25/62 created the European Agricultural Guidance and Guarantee Fund (EAGGF), but development problems, such as the establishment of the common agricultural organizations and the possibility that old solutions might be prohibited, then made it necessary that the Fund be divided into two sections, the Guidance Section and the Guarantee Section.(Regulation 17/64)

The Guarantee Section sought to affect market development through price support, while the Guidance Section sought to affect adaptation and improvement to structural conditions of agricultural production and marketing. Only the Guidance Section was constituted as a Structural Fund. (2)

The difficulties encountered in trying to assist regions in need is demonstrated by the requirement of Regulation 729/70 that assistance should be limited to farmers capable of reaching at the end of a development programme an income level comparable to that of average non-agricultural workers. This limitation reflected concern that the modernization of holdings could be jeopardized if, on the basis of social or regional considerations, assistance was granted to farmers with few development possibilities. If they were assisted, those with better possibilities would not be given enough incentive to undertake structural improvements. So, assistance should be limited to farms from which 'the best results were to be expected from the point of view of structural policy'. *A consequence was that assistance tended to be more readily available in developed regions than in regions where agricultural structures were backward and overall imbalance existed.*

Recognition of this problem led to removal of this limitation to eligibility in Directive 75/268.

The following paragraph shows that even a programme designed with the best intentions does not always work and can negatively impact on another programme. The assistance granted by the Guidance Section was only a small proportion of total EAGGF spending. Price-support measures, financed by the Guarantee Section, used as their direct reference the quantity produced and thus tended to favour large, productive farms. Moreover, in general, comparatively developed northern regions of the

Community, because of the composition of their agricultural production (cereals, milk, and sugar), benefited from a higher level of support from the Guarantee Section than southern regions. In the latter regions production of fruit, vegetables, and wine were dominant. In 1989, for example, assistance from the Guarantee Section was ECU 3,751 million for the Netherlands, where 4.7 % of the working population were engaged in agriculture. Only ECU 174 million was granted to Portugal, where 20.7 % of the population were so engaged. *Hence, the impact of the Guidance Section was outweighed by the general tendency of the common agricultural policy to perpetuate, if not exacerbate, regional inequality.* At the same time, additionality requirements meant that assistance from this Section was, in practice, more accessible to Member States with strong economies and administrative organization. (Evans, p.123)

By 1983 the Committee on Regional Policy and Regional Planning concluded that the Guidance Section needed to be radically strengthened, only then could the structural changes which would make it possible to reorganize and modernize farms instead of abandoning them, be effected.(EP Doc 1-768/83, 31) This has led to a gradual shift from price support to structural support. This shift has been accelerated with the accession of the ten new Member States in 2004.

Article 42(a) of the EEC Treaty provided that Council might authorize assistance for farmers handicapped by structural or natural conditions. In accordance with this provision, Directive 75/268 was enacted with the objective to ensure the continuation of farming. (3)

The Guidance Section of the EAGGF provided assistance over a huge geographical area and in many different fields. (4)

Considerable changes are expected in this fund over the next few years due to the gradual change of the Common Agricultural Policy (CAP) from support for production to support of environment-friendly farming practices and income

maintenance for farmers. The expansion to the CEE countries will also change the operations of the fund.

***“ESF”, the European Social Fund.***

Evans (1999, pp. 145-171)

Funds involved: Euros 60 billion for the period 2000-2006.

As outlined below, aid under the ESF is given to individuals, companies and organizations in regions under Objectives 1 to 3. This aid is considered an essential part of regional development.

According to Article 123 of the EEC Treaty the European Social Fund was to facilitate the establishment of the common market by ‘improving the employment opportunities of workers in the common market’. By assisting migration it would contribute to realizing the potential of the common market to reduce unemployment in the less developed regions and to improve the welfare of individual workers and the general economy. It would counter distortions of competition associated with the ‘imperfect mobility of labour as a factor of production’.

The ESF was originally intended to alleviate the social costs of establishing the common market. *Assistance was to be provided during the transitional period for establishment of the common market and could be abolished by the Council at the end of this period. This thinking proved to be too optimistic as the fund is still operating some forty years later. This is due largely to the huge differences in development and income levels in the poorer regions of the Member States, but also the accession of relatively poor new members over the years.*

The fund provides assistance in a wide field, from the relief of unemployment to training long-term unemployees in new techniques, vocational training, research in the provision of IT services to underdeveloped regions and for assistance generally to individuals and SMEs to enable them to cope with new technologies or changes in market conditions.

***“ERDF”, the European Regional Development Fund.***

Evans (1999, pp. 35-114)

Funds involved: 195 billion Euros for the period 2000-2006.

1975 saw the establishment of the last of the major structural EU funds the “ERDF”, (Regulation 724/75) (OJ 1975 L73/1). Its main aims were the correction of regional imbalances within the community resulting in particular from agricultural preponderance, industrial change, and structural underemployment. Article 6(1) added that the imbalances to be corrected were those likely to prejudice the attainment of economic and monetary union. The Fund was thus conceived as a means of ‘compensating’ weaker Member States for the cost of their participation in such a union.

It was anticipated that growth associated with the establishment of the common market would resolve regional problems. In reality, the establishment of the common market deprived Member States of protectionist instruments, such as tariffs and quotas. These instruments had been used to further national growth and, in so far as protected industries were regionally concentrated, regional growth. If they could no longer be used it was feared that states’ control of their economies might be weakened. Such fears may explain why Member States increasingly resorted to state aid and sought to outbid one another with escalating offers to attract mobile investment. This was a race that the poorer, worse-equipped, peripheral regions were bound to lose. The Commission drew the conclusion that the provision of Community assistance to such regions was necessary, if overall economic growth was not to be endangered.

Eligibility for assistance has over the years been reviewed and refined. Originally ‘agricultural problem areas’ and ‘areas suffering from industrial change’ were to be considered.(Bull EC, Supp 8/73) ‘Agricultural problem areas’ were defined as those which had a greater share of the workforce in agriculture than the Community average

and a relatively low per capita income. They tended to be on the periphery of the Community and had experienced a sharp decline in employment in agriculture.

‘Areas suffering from industrial change’ were defined as those with at least 20 % of employment in declining industries, such as coal and textiles with persistently high unemployment. Once again, regions chosen would be those that benefited from a national system of regional aids and where the per capita gross domestic product was below the Community average.

Regulation 1787/84 added two new criteria for allocating assistance to projects. They were: specific problems due to the island, landlocked, or peripheral character of the area in which the project was located, and the effects of the project on the region’s natural resources. This Regulation also provided for the Fund’s assistance to Community programmes (CP) and that CPs should have priority in Fund operations. Such programmes were defined as a series of consistent, multi-annual measures directly serving Community objectives and the implementation of Community policies. Examples are: CP for the restructuring of the steel industry, shipbuilding, textile and clothing industry, the Star Programme which was established to supply advanced tele- communications services and by establishing them into large networks. (Evans, 1999, pp. 60-64)

Regulations 2052/88 and 2081/93 provided for the classifications of regions into ‘Objectives’, already indicated in the opening paragraphs, and the use of NUTS. These two matters are dealt with in detail below.

### **Scope for assistance.**

The Fund may assist productive investment, to enable permanent jobs to be created or maintained. However, the regional development impact of such investments may be limited, because the proportion of supplies bought within the assisted regions may not be significant. Hence, a substantial part of the income-multiplier effect of assistance to these regions may effectively benefit advanced regions. The assistance may do little to secure self-sustained growth of these regions. It may even adversely affect local labour markets, jeopardizing the small, local industrial activities already in existence.

Assistance may also be given for the creation or modernization of infrastructure which contributes to the development or conversion of the regions concerned. Where appropriate, investments contributing to the establishment and development of trans-European networks (TEN) in the areas of transport, telecommunications and energy infrastructures may be included. Where the need is demonstrated, financing may also be provided for investments in education and health which contribute to structural adjustment.

The Fund may assist measures to exploit the potential for internally generated development of the regions concerned. (5)

### **ERDF - Conclusion.**

The next few paragraphs presented here show how problems perceived lead to amended procedures.

Evans (1999, p. 112) claimed that *the practice regarding the European Regional Development Fund focuses more on questions of the distribution of assistance as between Member States than on ensuring that these resources are effectively used to promote cohesion*. The basic criterion for eligibility for assistance from the Fund and, more particularly, for selection of Objective 1 regions, is per capita gross domestic product relative to the Union average. In principle, to qualify for Objective 1 assistance, regions must have a per capita gross domestic product which is less than 75 % of this average.

Application of this criterion has the advantage of apparent objectivity. In determining eligibility for assistance from the Fund, the Council and Commission have been concerned to use figures which are available throughout the Union on as nearly as possible a comparable basis. Figures are available, unreliable as they are admitted to be, for gross domestic product.

The criterion may also be claimed to secure the concentration necessary to ensure that limited resources are not so thinly spread as to lack real impact. More particularly, it enables the assistance to be concentrated on regions in Member States which have

sought ‘side payments’ for acceptance of the deepening of integration envisaged in the Single European Act and the Treaty on European Union. In this connection, it is notable that Ireland, Greece, Portugal, and Spain as well as Italy, favour a strict application of the 75 % criterion for determining eligibility under Objective 1.

It appears that relaxation of criteria based on per capita gross domestic product may be necessary for the development of a Fund which genuinely addresses the diversity of cohesion problems within the Union.

At the same time, adoption of more sophisticated criteria may be necessary, to curb the intergovernmental haggling over the designation of Objective 1 regions and over the eligibility criteria for Objectives 2 and 5b. Such haggling underscores how Union assistance can be abused by the Member States. As the Commission admits, the distribution of such assistance reflects ‘political compromises’. For example, the whole of Ireland was classified as objective 1. The Commission responded by strictly limiting eligible regions to those where the Commission authorizes Member States to grant regional aid under Article 87(3) of the Treaty. Thus, eligibility is ultimately to be determined by reference to competition policy requirements rather than by reference to cohesion requirements.

*Little attention is paid to ensuring that assistance, once it has been allocated to a Member State, is used effectively to promote cohesion. For example, much assistance concerns physical infrastructure, even though such assistance may not be the most appropriate for regional development. Equally assistance to productive investment may not necessarily be an effective means of reducing disparities between regions. Comparatively limited resources are devoted to ‘endogenous growth’ measures, which may be more successful in reducing such disparities.*

**“EIB”, the European Investment Bank.**

Evans ( 1999, pp. 211-217)

Funds involved: 42.3 billion Euros in 2003, of which 34.2 billion were for Member States and 4.6 billion Euros for the then future Member States. It has a balance of 235 billion Euros, with lendings of 207 billion and an outstanding debt of 195 billion.

The European Investment Fund (EIF) which has been created to be a venture capital fund provided last year 135 Million Euro for participation in other early-stage financing funds.

Many observers fail to realize the importance of the EIB in regional development. As shown above the EIB contributed over Euro 34 billion in 2003 to Member States' development. It has to be considered that the EIB provides financial assistance for projects undertaken in conjunction with community approved programmes. Most of the finance provides only a fraction of the total cost, but other banks then provide the remainder of the finance, because the EIB's contribution indicates that it is a sound proposition. Also long-term loans can be obtained, at low interest rates which can even be refunded by the Commission. It is clear that many projects would not have proceeded if this financing were not available. Article 130(b) of the EEC Treaty gave the Bank the task of financially supporting 'projects for modernizing or converting undertakings or for developing fresh activities called for by the progressive establishment of the common market'. Such support was expected to be consistent with the free competition sought through establishment of the common market, because the Bank only provided finance through interest-bearing loans.(Evans, 1999, p. 11)

Although the Bank was completely independent, it was expected that its principal task was assistance to the less developed regions. This expectation reflected recognition that 'mechanical integration' of the Member States could harm such regions. The inference drawn was that assistance from the Bank was necessary to counter the tendency of the common market to increase the differences between developed and less developed regions.

Projects for assistance had to be of such a size or nature that they could not be entirely financed by the various means available in the individual Member States and they had

to be fresh activities called for by the progressive establishment of the common market. *The expression 'progressive' was seen as implying that assistance from the Bank should be limited to the transitional period for establishment of the common market.*

The Bank also assisted projects of common interest to several Member States. These projects also had to be of such a size or nature that they could not be entirely financed by the various means available in the individual Member States. Such projects included, in particular, those which would contribute to the integration of the economies of the Member States.

Originally assistance was allocated to infrastructure projects and large industrial projects. However, in 1968 global loans, passed on through sub-loans to small and medium-sized enterprises, were introduced. The bulk of the assistance went to the poorer regions, especially Italy. (6)

The Bank also established several new financial instruments. They were the 'European Investment Fund', a 'Temporary Lending Facility' and a 'Special Action Programme'. They all were designed to provide aid for specific purposes, but they all were designed to provide assistance to Small and Medium Sized enterprises. SME enterprises which obtained such loans receive interest subsidies from the Union Budget.

### ***The Cohesion Fund.***

Evans (1999, p. 230)

Funds involved: 18 billion Euros for the period 2000-2006.

The Cohesion Fund was created in 1993 to assist the lagging member states to upgrade their infrastructures while consolidating their budgets to meet the Maastricht criteria. It was limited to Ireland, Spain, Portugal and Greece. The Fund provides assistance to projects concerning environmental protection or trans-European networks in Member States which meet two conditions. First, they must have a per

capita gross domestic product of less than 90 % of the Union average. Secondly, they must have a programme leading to the fulfillment of the conditions of economic convergence, as set out in Article 104 of the Treaty. In effect, the Fund is designed to assist Ireland, Portugal, Spain, and Greece in meeting economic convergence requirements for participation in the third stage of monetary union. Participants in this stage replace their national currencies with the Euro. This is the official line. (Evans, 1999, p. 230)

However, there was considerable argument and eventual compromise. The main actor here was Spain. She threatened to block other proposals unless aid was provided as she wanted. Spain demanded that the eligibility requirement was 90 % GDP of the state, not the regions as usually. This meant that the Mezzogiorno in Italy and the East German Laender, which would be equally eligible for assistance as a region, were excluded, because the whole state had a higher GDP.

***“FIFG” the Financial Instrument for Fisheries Guidance.***

Evans (1999, pp. 181-185)

Funds involved: 1,11 billion Euros per annum.

Assistance under the FIFG is provided mostly in combination with other funds such as the ERDF, ESF and EAGGF as most areas in difficulties with their fishing industry are located in economically deprived regions. Its impact on regional development can therefore be substantial. Regulation 4028/86 (OJ 1986 L376/7) established the FIFG with its objective being assistance with the balanced exploitation of internal resources in community waters. Broad account was to be taken of the economic and social environment of the industry and especially of the diversity and seriousness of structural problems at regional level.

Prior to the establishment of the FIFG in 1986 assistance to fisheries was provided by the Guidance Section of the EAGGF, the European Agricultural Guidance and Guarantee Fund. However this proved unsatisfactory as certain demands made for the

restructuring of the fishing industry and declining employment, could not be covered under the EAGGF.

The FIG provided assistance for a large number of different areas in the fishing industry. (7)

Assistance is to be provided within the framework of Community programmes. As the regions with fishery difficulties would be situated in regions which are subject to the various Objectives, they are also involved in solving the problem. Assistance can only be provided under the rules agreed to for the various objectives. Once again competition policy shows its influence.

***“ECSC” Assistance for the European Coal and Steel Community.***

Evans (1999, pp. 185-193)

The declining coal and steel industries are located in regions which are now some of the more problematical areas in the Union. Assistance to these regions is provided by all the other structural funds, consequently the mentioning of this fund is warranted. This fund was created to provide assistance especially for the coal industry, although undoubtedly important in its early days, the fund and the ECSC have now ceased to exist and its functions have been taken over by general union authorities. Consequently, this fund will not be delved into any further.

***Numerous small financial instruments.***

Such as for:

- Trans-European Networks in transport, telecommunications and energy,
- Euratom Loans and Guarantees,
- Environment Friendly Farming
- Shipbuilding, Textiles, Armaments
- Research and technology etc

Due to their limited impact, these financial instruments will not be investigated any further, but they are shown here to demonstrate the EU’s far-reaching influence.

### **The regions and their entitlements.**

The European Regional Development Fund is now treated as the principal instrument for achieving cohesion. Assistance given by any of the EU's funds are based on the procedures and guidelines established for this fund. It is therefore essential that a detailed study is made of them. Hitiris (2003, pp. 231-235) states that the broad aims of Community regional policy are two: 'Solidarity, which will ensure that all regions and their citizens can take full advantage of the single market and economic and monetary union', and 'assistance to the weak regions to help them alleviate the restructuring pressures associated with enhanced competition in the single market'. This resulted in the 1988 reforms of the Structural Funds (EAGGF, ESF and ERDF). It was also agreed that, for increasing the effectiveness of the programmes, the intervention operations of all the structural funds should be based on five principles:

- 1) *concentration* of the employed resources geographically and in relation to people for the benefit of those regions and groups which are genuinely in need;
- 2) *programme planning* drawn up by the Member States and approved by the Commission;
- 3) *additionality* of the finance provided by the funds to the corresponding national measures;
- 4) *partnership* in carrying out the programme by the Member State and the Commission;
- 5) *effectiveness* by monitoring and evaluation to ensure that the objectives are observed.

Additional elements in the application of the policies are (1) *consistency and complementarity* with other policies, such as competition, environmental protection, equality of men and women, and other provisions of the treaties, and (2) concentration of expenditure on the areas of greatest need. To comply with the latter, the regions were classified under categories ( called objectives ), with the bulk of spending focused on the most disadvantaged regions of objective 1.

In 1981 the Commission introduced priority treatment for operations jointly financed by two or more funds, in the Guidelines for the Management of the European Social Fund (paras 1.1.2 of the Guidelines for 1981-82 (OJ 1981 C110/2). Regulation 1787/84 decreed the same for the ERDF, integrated operations or programmes might have priority for assistance. The schedule below gives an indication how this works.

**Regional and social Aid Budgeted for 2000-2006 (billions of euros )**

	<b>Objective 1</b>	<b>Objective 2</b>	<b>Objective 3</b>
	Regions lagging behind in Development	Regions in Structural Crisis	Regions needing support for Training/Jobs
EU funds available ( Billions of Euros )	135,90	22,50	24,05
EU funds used	ERDF, ESF, EAGGF, FIFG	ERDF, ESF	ESF
Percent of population covered	22,2	18,0	na.

Total funds allocated for structural assistance for the period 2000-2006 (Amounts in Euros at 1999 prices).

<b>Structural Funds</b>	<b>195,00 billion</b>
Priority Objectives	182,45 billion
Objective 1	135,90 billion
Objective 2	22,50 billion
Objective 3	24,05 billion
Community Initiatives	10,44 billion
Fisheries	1,11 billion
Innovative Actions	1,00 billion
<b>Cohesion Funds</b>	<b>18,00 billion</b>
<b>Total Funds</b>	<b>213,00 billion</b>

(EU Regional Policy - Inforegio, policy/intro/regions4\_en.htm Dec. 2002)

For statistical reasons the EU classifies the regions according to the “Nomenclature of Territorial Units” (NUTS), which distinguishes the regions into:

78 regions at NUTS level 1 (this comprises amongst others the German Laender and larger units).

210 regions at NUTS level 2 (this comprises the Austrian Laender, German districts etc.)

These regions account for 22% of the EU-15 population and are the regions eligible for ‘*objective 1*’ assistance.

1093 regions at NUTS level 3, they comprise 18% of the EU-15 population and are eligible for ‘*objective 2*’ assistance. (Hitiris, 2003, p. 234)

After one and a half years of negotiations the new regulations for Structural Funds for the period 2000-2006 were adopted. The new regulations take into account the effects of globalisation, enlargement, fulfill the Amsterdam Treaty and try to reduce bureaucracy. As a result the different objectives have been reduced to 3 (formerly 6+1) and the Community Initiatives from 13 to 4.

The schedule below further develops details provided above and makes allowances for NUTS regions.

**The 3 new Objectives.**

<b>Objectives</b>	<b>Eligible Regions</b>	<b>EU-Funds</b>	<b>Financial Allocation</b>
<b>1:</b> promoting the development and structural adjustment of regions whose development is lagging behind.	NUTS II regions whose GDP is less than 75 % of the EU average, with some exceptions.	ERDF, ESF, EAGGF, FIFG	69,7 %
<b>2:</b> supporting the economic and social conversion of areas facing structural difficulties.	Regions in structural crisis on NUTS III level or adjacent areas.	ERDF, ESF	11.5 %
<b>3:</b> supporting the adaptation and modernization of policies and systems of education, training and employment.	All regions, except Objective 1 areas (because all Objective 3 measures are part of Objective 1 also).	ESF	12.3 %

**The 4 new Community Initiatives:**

<b>Community</b>	<b>Contents</b>	<b>EU-Fund</b>	<b>Financial</b>
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<b>Initiatives</b>			<b>Allocation</b>
<b>INTERREG III</b>	Cross-border, trans-national and inter-regional cooperation intended to encourage the harmonious, balanced and sustainable development of the whole of the Community area.	ERDF	2,5 %
<b>URBAN</b>	Economic and social regeneration in urban areas	ERDF	0,4 %
<b>LEADER+</b>	Rural development	EAGGF	1,03 %
<b>EQUAL</b>	Trans-national co-operation to promote new means of combating all forms of discrimination and inequalities in connection with the labour market.	ESF	1,46 %

(Schicker, 2000, EU Regional Policy, Inforegio, 2002)

### **The administrative requirements in the Member States.**

In view of the large amounts involved and the possibility that any Commission decision could be challenged in Court, the Commission has enacted a number of procedures and guidelines which Member States have to adhere to if they wish to partake in the EU's assistance for development. The Commission conveys its requirements to the Member States by issuing the following:

#### ***Periodic Reports.***

Periodic reports are being produced by the Commission. They enable the Commission to seize from Member States the initiative in regional planning. Regulation 2083/93 states that the Member States must supply the Commission with the relevant information enabling it to make an analysis of all the Union regions on the basis of statistics which are as comparable and as up to date as possible. Every three years the Commission is to submit a report to the European Parliament, the Council, the Economic and Social Committee, and the Committee of the Regions on the progress made towards achieving cohesion. The report must detail the manner in which Union funds have contributed to this progress.

***Guidelines.***

Guidelines produced by the Union institutions have the explicit function of regulating the operations of the Union funds. They deal with similar details as the Regional Development Plans below. The Commission is now laying down regional policy guidelines, they are to be applied in the various stages of planning, notably in establishing the Community Support Frameworks and in the operations of the European Development Fund. Regulation 2083/93, Art 8 (2) refers.

***Administrative Decisions and Contracts.***

Decisions generally entail applications of pre-existing rules. Decisions were required for intervention programmes within a Community programme as well as decisions determining eligible regions in each Member State.

Contracts may be seen as a suitable legal form for giving content to administrative decisions. The implementation of Integrated Mediterranean Programmes was regulated by programme contracts. Due to the limited capacity of contracts, the Commission now relies instead on ‘declarations of intent’ associated with Community Support Frameworks and Single Programming Documents.

**The Member States are complying with the Commission’s requirements by submitting the following:**

***Regional Development Programmes/Plans.***

They are to be drawn up by competent authorities designated by Member States at national, regional, or other level. But the plans must be presented by the Member State itself. The role played by regional authorities depends on national law. But the ‘partners’ must now be consulted.

Regional development plans concerning Objective I regions must, according to Regulation 2083/93, include: a succinct analysis of the socio-economic situation of the region, indicating its demographic outlook, a description of the development strategy envisaged by the Member State, with an indication of the national and regional financial resources to be used, and the priorities for action of the Member State and

regional development measures for which it intends to request Union assistance, together with the estimated sums to be requested. As a rule these plans are now to be for a period of seven years. Slightly different requirements exist for the other objectives.

***Community Support Frameworks.***

The “Community Support Frameworks” in this paragraph and the “Single Programming Documents” in the next section represent the EU’s main disbursement documents. It can be seen that the outcome of the negotiations between the Member State and the Commission depends on a number of crucial details, such as 1) statistics available for the Member State and its administrative capability, 2) the Commission officers’ experience and cooperation. And as they cause the most problems and frustrations as outlined further on, a detailed examination of them is warranted. (Evans, 1999, pp. 267- 271)

A “*Community Support Framework*” can be defined as the document approved by the Commission following appraisal of the development plan submitted by a Member State and containing the strategy and priorities for action, their specific objectives, and the contribution of the European Regional Development Fund and other financial resources. It shall be divided into priorities and implemented by means of one or more operational programmes.

These Frameworks are a response of the Commission to requests for assistance in the plans drawn up by Member States. The information to be included in the Frameworks is specified by Article 8(3) of Regulation 2082/93. There must be: a statement of priorities for joint Union and national action in relation to the Objectives of the Structural funds, together with information concerning their consistency with the economic and social policies of the Member State concerned; an outline of the assistance which is to be provided but is not decided at the same time as the Framework, including the specific objectives of operational programmes and the main types of measure involved; an indicative financing plan specifying the financial allocations envisaged for the various forms of assistance and the duration thereof,

including those of the Structural Funds, the European Investment Bank, and other financial instruments, where they contribute directly to the financing plan concerned; where appropriate, information concerning the means available for any studies or technical assistance relating to the preparation, implementation, or adaptation of the measures concerned; the procedures for verifying additionality and an initial valuation of the latter; and appropriate information concerning the transparency of the relevant financial flows, particularly those from the Member State concerned to the recipient regions. For Objectives 1, 2, and 5b the arrangements for associating the environmental authorities designated by the Member States in the implementation of the Framework must also be indicated.

The Frameworks are said to constitute ‘*programme contracts*’, which bind the Commission and the national authorities. While the Frameworks adopted may incorporate the outline legislative requirements, their content is left to depend largely on negotiations between the Commission and the Member States. Legislation merely authorizes and structures such negotiations. The results of the negotiations may be controversial because the Commission is prepared to be flexible and may approve for example the inclusion of an area in *Objective 1* which would not be eligible based on income levels alone, but other reasons such as economic changes in progress may be the decisive factor.

### ***Single Programming Documents.***

“Single Programming Documents” must be approved by the Commission and contain the same information as Community Support Frameworks and operational programmes. Under existing legislation they may replace Community Support Frameworks. Member States may submit in such documents the information required in the plans and in applications for assistance. They are to be adopted by the Commission under Article 10(1) of Regulation 2082/93.

Their use, instead of Community Support Frameworks, highlights the favourable attitude of the Union legislature towards linking formulation of regional policy by Member States and operations of the Union funds. However, ‘red tape’ may lessen the

attractiveness of such documents. Their adoption requires just as much data and preparatory work as does separate presentation of plans and applications for assistance. Hence, their negotiations may be lengthy. At the same time, their preparation involves no greater guarantee of regional participation than does the preparation of Community Support Frameworks. Single Programming Documents are now being drawn up for the new Objectives 2 and 3.

Attached as addendum 1 and addendum 2 are reports on the programming experience for *Objective 1* funds by Austria. They outline the time requirements, difficulties and details required to satisfy the Commission. Intensive cooperation between the Member State and the Commission is essential for the period of the programme, now 7 years.

**The impact of Regional Development policies on the states' multi-level governance (MLG).**

Regional Development policy is the policy where through its practice of “partnership”, multi-level governance (MLG) has been officially encouraged and promulgated. From suggesting that regional and local authorities be consulted by the Member States in Reg. 1787/84 to the actual requirement for their inclusion in Reg. 2081/93 and 2083/93 the idea of a partnership between Member States, regional, and local authorities has been evolving and is now fully established.

Evans ( 1999, pp. 284-293 ) states that the concept of ‘partnership’ has emerged as the principal basis for participation by individual regions in committee work concerning operation of the Union funds. It is consistent with ideas of endogenous development. According to these ideas, regional development depends on a local organizational structure, which enables firms to generate successive innovations or to handle the implementation of technology effectively. Such a structure depends, in turn, on collaboration between public and private bodies at the regional level and, hence, on sufficient autonomy being enjoyed by the former bodies, how deficiencies due to insufficient autonomy affect the funding is outlined further on. (Tondl, 2001, p.204).

At the same time, partnership may be decisive for the articulation of cohesion requirements such as providing income levels at the Community average and equal employment opportunity. If a genuine partnership where the various levels of government cooperate fully, is established, their articulation may be adapted to the diversity of regional problems within the Union.

The above thoughts have also influenced the European Parliament. Already in resolution of 27 June 1966 (JO 1966 2427) it has stressed the need for the involvement of representatives of local and regional authorities in the development of Union regional policy and also for trans-frontier institutions to be established by Union acts. This 'partnership' gained steadily in acceptance until it was finally established in Article 4 of Regulation 2081/93 which provides for operations of the Union funds to be conducted on the basis of 'partnership'. 'Partnership', is defined in Article 4(1) of this Regulation as 'close consultations between the Commission, the Member State concerned, and the competent authorities and bodies, including within the frame work of each Member State's national rules and current practices, the economic and social partners, designated by the Member States at national, regional, local, or other levels, with all parties acting as partners in pursuit of a common goal'. It must, according to the same provision, 'be conducted in full compliance with the respective institutional, legal and financial powers of each of the partners'. (8)

The Commission and the European Parliament recognized the problems of resource deficiencies. It was obvious from the performances of some of the regions that, where there was an insufficiently developed relationship between the national government and the regions, the results would be unsatisfactory. For example, the Commission considered that implementation of the Integrated Mediterranean Programmes would have been facilitated by the 'strengthening of public administration structures, centrally and regionally, through improved management training, technical support, and information processing'. This has now been recognized by Article 4(3) of Regulation 2081/93, which allows the Commission to contribute to the preparation, implementation, and adjustment of operations of the Union funds. But as already

mentioned above, such help is subject to the provision that the Member State's national law and sovereignty not be prejudged. (Evans, 1999, pp. 292-293)

### **Partnership ( MLG ) in EU 15.**

The idea that responsibilities in a state should be shared amongst several layers of government was only readily accepted in the decentralized, 'federal states'. Austria, Belgium and Germany are the examples par excellence. In the latter especially, the West German 'Laender' ( states ) were interested in increasing their political clout in the West German political system. For this reason they insisted that they be given representative rights in Brussels. This was granted, as a matter of fact, high politicians from the Laender can replace federal ministers in Brussels under certain circumstances. In the early 80s Germany strongly supported the extension of decentralization in the European Union. The impact is reflected in the EU's adoption of the 'Partnership Principle'. Interestingly, with the progressive transfer of responsibilities which were previously the prerogative of the Laender to the EU, the Laender are now objecting to the diminution of their rights. (Gerstenlauer, 1995, pp. 192-193)

In the southern cohesion countries, Greece, Portugal and Spain, 'partnership' was a new experience. The three states were severely centralized and partnership had difficulties in being accepted. All three had difficulties in establishing regional and sub-regional authorities, the delegation of authority was hesitant and as a result the states had problems in claiming the funds they were entitled to under the Structural Funds regime. And as the time for which funds had been allocated was exceeded, some funds were canceled. (The thematic evaluation of the Partnership Principles, Dec. 2002)

Partnership has now been accepted, but, as can be expected due to national and political differences the outcome is to some extent different in each country. An interesting case is Spain, where the ongoing process of federalization has resulted in the wide-scale devolution of powers from the state to the Autonomous Communities

(CCAA). The latter have sought to centralize power at the regional level and have demonstrated reluctance to decentralize power to the sub-regional levels. This has meant that in Spain often examples are found of closed partnerships which are not especially open to the wider participation of social partners and municipalities.

The schedule below shows the relative strength of role of regional partners in the 15 Member States in 2002.

<b>Example</b>	<b>Central Government</b>	<b>Regional Government</b>	<b>Social Partners</b>	<b>Municipalities</b>
Austria	moderate	moderate	moderate	moderate
Belgium	moderate	moderate	moderate	moderate
Denmark	strong	moderate	moderate	moderate
Finland	strong	moderate	moderate	moderate
France	strong	strong	weak	weak
Germany	strong	strong	moderate	weak
Greece	strong	weak	weak	weak
Ireland	strong		weak	weak
Italy	strong	strong	weak	weak
Luxembourg	strong		moderate	weak
Netherlands	strong	moderate	moderate	moderate
Portugal	strong	weak	weak	weak
Spain	strong	strong	weak	weak
Sweden	strong		moderate	strong
UK	strong	weak	weak	moderate

EU Tavistock report (2002)

### **Partnership in CEE.**

Bachtler and Downes (1999) question whether sufficient thought has been given to the kind of regional policy appropriate for central and eastern European (CEE) countries at their present stage of transition. In the rush to qualify for accession, there was little questioning of the relevance of the principles of the Structural Funds. Even Western Europe which has long experience of regional policy is still undergoing fundamental shifts in paradigm and governance of regional development.

The territorial administrative structures of CEE countries are highly varied in terms of the hierarchies of territorial units, the number and size of administrative units and the form of administrative organization. In the pre-transformation period, territorial organization was arranged to facilitate central planning and fragment potential power bases of political opposition. In the wake of transformation, a fragmentation of territorial units took place as localities sought to regain control over local settlement affairs. (10)

I expect that, for years, the new Member States will have 'teething problems' like the former cohesion countries experienced. The establishment of new institutions and structures, together with the transfer of authority, is a monumental task which can not be decreed and expected to happen over a few years.

#### **A short study of the EU's policies impact on the Member States' economies.**

The reforms of the Structural Funds in 1989 have been successful: for instance per capita income in the cohesion-countries ( Greece, Spain, Portugal, Ireland ) increased from 65% in 1986 to an estimated 78% of the EU 15 average in 1999. Also, the poorest regions could increase their per capita income by 9% points. Unemployment could not be reduced, but even increased in the 25 poorest regions to 24 %. As the Commission concluded in its Cohesion Report the Structural Funds and the Cohesion Policy were able to help reduce disparities between Member States, but the problems of unemployment and disparities between regions could not yet be solved.(Schicker, 2000)

As the Commission and Council have declared recently, they consider unemployment a serious problem for the EU and that every effort to solve the problem should be made. (Nugent, 2003, pp. 313-315) However, the impact of the EU will only be limited, as some of the most intractable difficulties are the responsibilities of the Member States. Here there are the powerful Unions who refuse to accept the smallest changes to working conditions, and outdated social and administrative systems which

were suitable for periods of strong economic growth, but are now fatal. These conditions apply mainly to the largest EU Member States, Germany, France and Italy.

In order to reduce the unemployment levels the Member States will have to change the above mentioned policies. Changes to the above mentioned problems are now being implemented in most of the EU Member States, but none of the major economies is prepared to make the necessary bold decisions required.

The EU will have to:

Reconsider and change its Competition and Industrial Policies,

Review and change aid policies. Are funds spent without getting the desired benefits, like payments made to facilitate the establishment of new companies, or the provision of infrastructure in underdeveloped regions instead of supplying funds for the creation of lower skilled employment opportunities?

It appears that the EU finds it easier than some of the larger Member States to amend, change and improve its policies. This process is being carried out continuously as evidenced by the hundreds of regulations, directives and decisions every year.

In the new CEE Member States the problems are much more severe. Since the beginning of the transformation to the market economy, the uneven spatial impact of intense economic reform has become more apparent. The overall picture is one of widening disparities between and within countries. The following paragraphs clearly show these disparities. Research on regional differences in several CEE countries reveals that disparities have increased significantly since the start of transition, with a fragmentation of regional economies (Bachtler & Downes, 1999). The patterns of regional development between and within CEE countries are highly varied, but four interrelated types of regional disparity stand out:

1. the contrast between urban and rural areas,
2. a core/periphery disparity, especially in countries with a monocentric urban structure,

3. a west/east difference, particularly evident in border areas,
4. concentrations of restructuring problems in old-industrial areas.

In all of the transition countries, the major agglomerations and urban centres are leaders in the transformation process. ( 11 )

Beyond the cities, many rural areas, characterized by increasing unemployment and falling employment opportunities within and outside agriculture, are not sharing the economic benefits of transition. ( 12 )

There is an important west-east dimension to the above situation, especially as far as the peripheries of the CEE countries are concerned. Whereas from an EU perspective the CEE-EU border is seen in terms of regional disadvantage ( owing to the steep income differences between Germany or Austria and neighbouring Poland, Hungary and the Czech Republic ), for the transition countries it presents new opportunities. In the pre-transformation period, the western border areas of the CEE countries were in an unfavourable position (tote Grenze) and neglected under socialist planning, but since 1989 they have been able to take advantage of inflows of productive investment, tourism, cross-border shopping and cross-border economic development initiatives. The result is low unemployment, rising wage levels and in-migration as well as stimuli for the housing The ‘*Special Action Programme*’ established in 1998 allowed the Bank to extend its assistance in the areas of education, health, urban environment and environmental protection, and to also step up its intervention in relation to large infrastructure projects and small and medium-sized enterprises. Once again, any interest subsidy from the Member State concerned must comply with Article 87 of the Treaty, concerning state aid, that means that competition policy again has a dominant influence.

market and construction industry.(Bachtler & Downes, 1999)

For the eastern peripheries of CEE countries the situation is reversed. Termed the ‘eastern wall’, the eastern border regions tend to have relatively poor infrastructure,

little investment and unfavourable economic structures - a predominance of agrarian activity, high unemployment, low educational attainment and low qualifications among the labour forces and unfavourable age structures. (Gorzalak, 1996, p. 152)

However, the 1st of May 2004 has changed the economic outlook completely. Instead of all efforts to uplift the economies going into the former cohesion countries, over the next few years this will go to the new CEE Member States. For example, in 2002, ten of Spain's seventeen regions qualified for regional aid, but after the eastern enlargement reduces the average per capita income in the EU by 16 %, only two Spanish provinces

( Extremadura and Andalusia ) will qualify. There should also be a few regions in the former East Germany, the Mezzogiorno in Italy and one or two regions in Greece.

Spain objected bitterly to this reduction in assistance and threatened to block the free movement of labor from eastern Europe.

Although the new CEE Member States agreed to a very limited aid package as part of their accession agreement, it is considered doubtful that they will not demand an upward revision of their entitlements. At the Copenhagen summit in December 2002, the EU agreed to provide about 40,8 billion Euros to the ten accession states between 2004 and 2006. Regional aid money tends to go to projects like road building that may take years to finish, or the money may be lost to the candidate countries when they find such projects difficult to administer. (Poole, 2003, pp. 115-117)

The EU has increased its budget for 2004 from Euros 99.6 billion to 111.3 billion in order to be able to finance the enlargement of the Union. 3.3 billion Euros are being contributed by the new members. As part of the accession agreements the cost of enlargement for the EU from 2004 to 2006 has been fixed at 40.85 billion Euros. However, the Commission calculates that only some 27 billion Euros will be paid out. The reasons for this are that the new member nations lack the administrative capacity to distribute the funds correctly. Some of the EU contributions demand co-financing by the national governments, which the new members can't afford yet. With the

exception of Cyprus, Prague and Bratislava the new Member States are wholly 'objective 1' regions, entitled to the highest assistance.

(Die Presse, 28. April 2004)

The Commission suggested the possibility of limiting regional aid to the accession countries by invoking an existing EU rule that no country can receive regional aid that is more than 4 percent of its gross domestic product. The rationale for the limit was that any more aid could probably not be absorbed. Given the small size of the accession countries' economies, this would leave most of the regional aid budget to be divided among the current Member States. The Commission estimated that by 2006 the new Member States would be receiving regional aid worth 137 Euros per person, compared with 231 Euros per person for Spain, Portugal, Greece and Ireland. (Poole, 2003, pp. 115-117)

An interesting development occurred in Austria and Germany. As a result of the "Marshall Plan", (the European Recovery Plan of 1948) the two countries accumulated originally "Counterpart Funds" of some 3 billion US \$ (Germany) and some 600 million US \$ (Austria). Due to strict lending practices they have now grown to 12 billion Euros for Germany and 3 billion for Austria. The funds could be used for the development of industries, agriculture and regional development, as the governments thought fit and subject to the ERP Funds rules. However, in Germany the fund's contributions became subject to the EU's competition rules as they developed, and Austria had to comply with them from 1995 when it became a member of the EU. The Commission agreed to use aid from these funds as the Member States "additionality" contribution to EU funding. They are now mainly used for the financing of Regional Development, SMEs, promotion of technology and promotion of investments in foreign countries. (Bischof, 2000, pp. 53-55)

Germany is now trying to incorporate the German funds of 12 billion Euros into its national budget. This would mean the dismantling of the Fund and would jeopardize support for SMEs and technical development. (Spiegel, 23. 11. 2004)

The Stability and Growth Pact of the EU in support of monetary stability requires that the national deficits are below 3 per cent. This had an unfortunate impact as many governments curtailed their funding for productive investment by some 30 per cent. As a result the Mezzogiorno in Italy's south instead of catching up with the EU average, actually showed a decrease of its per capita income from 76 per cent to 67 per cent. The other less developed Member States escaped this development by having access to the Cohesion Fund, which was denied to Italy.

There is an abundance of financial facilities and funds that can provide assistance to SMEs and the Commission continuously claims the importance of SMEs and its desire to assist them. *However, there is considerable disquiet in the EU about its impact. SMEs claim that the system works most satisfactorily for larger enterprises who can employ experts in EU matters to prepare the necessary applications. The cumbersome application procedures are unfortunately too difficult for many smaller SMEs who therefore miss out.* The Commission is now trying to simplify these application procedures. (SMEs in Europe miss out. 25. 11. 2004)

### **Recent developments and changes in the Commission's thinking regarding the best use of the funds.**

Many changes occurred during the last two years in the EU, some have become obvious right away, while others are only now being implemented. For Regional Development two of the recent developments with the greatest impact are considered the changes brought about by the increased powers for the Committee of the Regions (CoR) and the enhanced financial authorities for the European Investment Bank (EIB). These will now be studied.

The Committee of the Regions (CoR) was established only in 1994, its functions then being basically one of consultancy. It was to advise the Commission, Council and the European Parliament about matters relating to regions and other sub-national authorities. As many of these also had access to EU organizations via the national

organs of the Member States or had their own representation in Brussels, there were originally doubts about the CoR's value and long-term benefits. (Jeffery, 2002, p. 344; Mitchell & McAleavey, 1999, p. 178) But the CoR managed to quickly assert itself and provided valuable advice, this was especially appreciated by the EP and the Commission.

During the Constitutional debate most people's attention was drawn to the difficult points of numbers of Commissioners, qualified voting and several others like veto powers of Member States. Little attention was paid to the fact that the CoR was to get the authority to ensure that "subsidiarity" was being observed in the EU, not just between Commission and Member State, but down to regional, sub-regional and municipal level. If the CoR considers that the subsidiarity principle was infringed it can take the case to the European Court of Justice (ECJ). (CoR newsletters No. 44 & 45) A vast increase in power. Its eventual impact can now only be guessed, but it appears that it may help in breaking the stranglehold which the national governments currently have in their relations with the Commission.

There are currently some 250 regions and 1000 regional and local authorities in the EU, they are represented by 317 members in the CoR. (Commission's communication of 19. 12. 2003) The Commission is actively encouraging the closer involvement of these authorities in Union matters. Advice has been given that the CoR will already take up these additional powers, prior to the acceptance of the new EU Constitution.

As outlined above, the second major development is the EIB. The European Investment Bank was established in 1958 and since then it has grown spectacularly, it now lends more than the well-known World Bank. However, the public knows little about its functions and there is considerable concern about its transparency, accountability, and how it addresses environmental and social issues in its work. (Bankwatch, 9. 9. 2004) This is rather astonishing as the EIB advised in its Corporate Operational Plan ( COP) for the period 2002-2004 operational priorities that impact on virtually every aspect in the EU. (13)

The EIB is trying to overcome the apparent lack of transparency with hesitant boldness by spreading its influence further and further. Some examples are:

The European Investment Fund - the EIB's socialized venture capital arm - provided a total of 2,2 billion Euros in guarantees for SME financing.

Loans totaling 6,2 billion Euros were granted in 2003 under the Innovation 2010 Initiative.

The EIB plans to lend up to 40 billion Euros for R & D and innovation under the Action for Growth agenda for the period up to 2010. (14)

In support of the Action for Growth and as part of a new Trans-European Network Investment Facility, the EIB plans to provide some Euro 50 billion in financing for TENs projects in the years 2004-2010; Up to Euro 25 billion of the total will be made available over the coming three years for transport TENs, particularly for schemes under the Quick Start Programme. These are projects that can be proceeded with at this stage without any delay, as preliminary work has already been finalized, the new Member States are especially targeted here. **In special cases it will be possible for loans to be granted for up to 75% of the investment costs and for periods of up to 35 years, with flexible repayment terms.**

The Bank has set itself the target of devoting 30-35% of its total annual individual loans to environmental projects.

As the EIB will part-finance projects only or provide guarantees it is expected that the Bank's annual loan provision of some 40 billion Euros will result in actual project financing of some 200 to 300 billion Euros. Truly, an all-Europe affecting amount. (Dow Jones Business News, EIB loans, 5.2. 2004)

It is now a condition of any assistance provided by the EU, that the Member States and other beneficiaries acknowledge this with every project.

## **CONCLUSION.**

A fascinating topic, the many structural funds, the hundreds of various schemes and programmes and the many thousands of beneficiaries, from unemployed fishermen to

SMEs and large infrastructure projects. As has been shown in the report on the Austrian aid application - see addendum 1 & 2 below, there simply is no chance to ascertain the final number of beneficiaries.

A report from Saxony, a state in the former East Germany, is revealing. From 1991, when the EU assistance started to the end of 1996 a total of 9,929 disbursements were made. Out of the total of some 24 billion Euro subsidy some 4,3 billion only came from the EU. (Vehse, 2002)

The reasons for this are quite logical. The Commission, in conjunction with the Member State works out in protracted negotiations the aid level for each region. The details however, are then left to the Member State, it is assumed that the Member State will comply with Union rules, after all the states are required to contribute to the various aid schemes anything from 15 % in remote and desolate areas, to maybe 80 % in relatively prosperous regions. So it is doubtful that the states would want to cheat, after all any aid is still subject to Commission review and has to comply with competition rules (state aid).

The writer has progressed from pure, undiluted enthusiasm at the beginning of this study to a state of serious concern.

This is mainly due to the fact that:

1. Aid is not distributed to where it is mostly needed, but is shared out so that no Member State would be a net-contributor without some benefits.
2. Matters of aid and finance have to be agreed to by all Member States unanimously to be accepted. This allows individual governments to pressure the Union to either give in to the demand or grant some other benefit in lieu. In the United States the term “pork barreling diplomacy” is used, but in Europe, being so civilized, this is termed “constructive cooperation”. Spain’s behaviour in relation to the ‘cohesion fund’ is the best example of brutal selfishness.

3. Many aid programmes have not been thoroughly thought through. Aid could actually lead to a loss for a region if for example training leads to people then moving to higher paying jobs in the metropolitan areas.
4. Massive infrastructure projects are carried out, but they provide little permanent long-term employment opportunities, the former East Germany is a good example.

At the end of 2004 it was thought that not all matters were subject to doom and gloom as new developments outlined below could be expected.

1. the environment is now being given considerable standing, even in agriculture  
environment-friendly farming is now being encouraged.
2. as part of the new Constitution qualified majority voting will be the norm, albeit in a  
few years only, and it will first have to be accepted and incorporated in the  
Member States law.
3. steps are being taken to ensure sustainable economies are achieved, for example in  
fishing and farming.
4. the enlargement on 1. May 2004 has brought ten new Member States, their  
desperate  
needs will force the old Member States to moderate their demands and change  
the  
assistance provisions for the new Member States.

But this was not to be. The new EU Constitution has currently been put on ice and could in all likelihood be impossible to achieve. The Commission's optimistic expenditure planning is currently up in the air as all budgeting proposals have been thrown into disarray. The limit of the EU budget is unknown, the Member States' contributions are unknown and consequently the projects to go ahead, are unknown.

Many Member States want reduced percentage contributions - anything from 1 per cent to 1,24 per cent is being discussed. Many want the agriculture's CAP to be reduced or discontinued and want instead more funding for research and development. Calls have also been made for the Commission to leave more work and responsibility to the Member States and to butt out from many areas that could equally, or maybe even better be handled by the states. 'Subsidiarity' is being called to limit Brussels's influence.

Although the EU Regional Development Policy is not perfect, like anything based on the give and take of compromise, it is clear that the development of the Member States' economies would not have progressed the way it has without it. For some forty years now the EU has strived to increase its prosperity and to foster cohesion. The vast changes during the last few years show that the EU is aware that it still is a long way from achieving its final goal, which incidentally no one knows, or wants to know. After all why announce a goal and thus limit its future potential?

Several matters outlined above, such as the transfer of authority to enforce "subsidiarity" down to the regional level, delegating more direct control of regional development aid to the Member States, the funds' and the EIB's programme of cooperation with the provision of cash, loans and guarantees and the publicity requirements, will help the EU to become more transparent and accountable. They will also lead to a transfer of responsibility from the EU to the national and sub-national authorities. So we can say that the future of the EU could be bright. However, due to its legal restraints regarding unanimous/qualified majority voting, the whole machinery can still be brought to a complete standstill by the objection of one, or several of the 25 governments if they decide that their national interests should be considered to be more important than the Community's.

#### **Addendum 1.**

In April 2000 a conference was held in Glogow, Poland, called “EU Membership - a Challenge for Local and Regional Authorities”. A report on ‘EU - regional Policy in Austria, Austrian Experiences in Access to EU Funds’ was presented by Rudolf Schicker of the Austrian Regional Planning Conference as part of Austria’s assistance to the new CEE accession states. As Austria itself only became a member of the EU in 1995 it had to overcome similar problems to what the new members experience now. Some of the advice given is considered most valuable for the new members, but also highlights the problems and frustrations that can be experienced when assistance from the Structural Funds is requested. This will be shown by some extracts of the report.

The Accession Treaty for Austria stated that Austria would receive 1,623 million Euros for the period 1995-1999.

Austria allocated this funding in 38 programmes:

- |                                       |                |
|---------------------------------------|----------------|
| • Objective 1 programme - Burgenland  | 166 mill. Euro |
| • Objective 2 programmes              | 101 mill. Euro |
| • Objectives 3 and 4 programmes       | 395 mill. Euro |
| • Objective 5a programme              | 388 mill. Euro |
| • Objective 5b programmes             | 411 mill. Euro |
| • programmes on Community Initiatives | 146 mill. Euro |

With these programmes Austria stimulated public and private investment or educational programmes with a capacity of approximately 6,000 million Euros.

In order to achieve clear-cut territorial definitions for different statistical reasons, Austria had to divide its territory following EUROSTAT’S “Nomenclature des Unites Territoriales Statistiques”(NUTS):

NUTS I: 3 groups of Austrian Laender

(East: Burgenland, Niederoesterreich, Vienna,

South: Carinthia, Styria

West: Upper Austria, Salzburg, Tirol, Vorarlberg)

NUTS II: each of the 9 Austrian Laender

NUTS III: 35 subdivisions of Austrian Laender.

“As these regions are not only defined for the reason of establishing eligibility to Structural Funds, it is advisable to take into considerations historical and functional conditions. Our experience is, that there always is a chance for negotiations for eligibility of parts of not accepted NUTS-regions”.

The following text does not only report on the procedures that are required but also gives advice to the new members, it is presented in a somewhat colloquial way. As the paper was presented to relative novices in the field this form of presentation is considered correct and is retained:

The second step on our way to suitable conditions for our regional programmes was to identify and negotiate the regions which should be eligible under regional objectives. For this exercise it is important to have available statistical data which have been negotiated between EUROSTAT and the national statistical services - but you should not rely only on these data. Very often Commission services don't know the country they have to deal with. You have to give them a clear picture of the structural and/or geographical situation of your favoured regions and present especially short term statistical figures. Usually the Commission is willing to adopt national priorities, when they are not prejudging.

The third challenge for a new Member State is the preparation of the Communal Support Framework (CSF) or the Single Programming Document (SPD). It is essential to start preparations already parallel to the negotiations on eligible regions. Both, the CSF and the Operational Programmes (OP) or SPDs have to follow clear regulations and have to contain clearly defined points.

The programmes have to contain:

- SWOT-analysis of the region
- specific regional objectives
- realistic development strategy
- the programme's priorities and measures
- and Ops and SPDs, also financial tables for the whole programming period.

The phase of programming is the most important for introducing regional or local measures or operations to the programmes. Regional and local authorities should be prepared to introduce their ideas and projects to the programming coordinator. They also should monitor carefully the programming process to avoid the loss of projects, which are of high regional or local importance.

For Austria's first period of Structural Funds activities the Austrian Conference on Regional Planning (OEROK) provided so-called "Regional Development Concepts" which identified the region's problems and lined out possible development strategies and measures. In this process all levels of administration and the economic and social partners were involved.

The preparation of the Operational Programmes was the duty of the Laender. They were obliged to co-operate with the federal ministries and the communities.

Retrospectively, we strongly advise accession countries to take their time for this process and plan their future impact of Structural Funds very carefully and in good time.

When following the Commission's Guidelines on programming and the programmes are completed, negotiations in partnership with Commission services are

comparatively easy, but time-consuming. Some of the Austrian programmes took almost a year until adoption.

On implementing the programmes, the Austrian experiences were, and they recommend that the new Members adopt the same procedures:

- ◆ find clear responsibilities within your administration as close as possible to the regions (to avoid never ending discussions within the administration)
- ◆ start programming in good time ( to have the opportunity of involving as many regional 'players' as possible and creating a realistic programme)
- ◆ don't involve too many services and national or regional funding-institutions (Otherwise co-ordination between them will be much too time-consuming)
- ◆ don't write too sophisticated programmes ( or you will lack flexibility during implementation )
- ◆ use a good mix of traditional and innovative measures ( for avoiding poor results especially at the beginning of the period )
- ◆ make a big effort in training the involved administration ( all levels )
- ◆ create a management structure on regional or sub-regional level ( to support the implementation in the region itself )
- ◆ establish effective systems for monitoring, financial management and control ( to have a clear picture of the programmes' input at any stage of implementation and to be prepared for following the financial rules )
- ◆ stay in close contact with the Commission's services ( very often it is the desk officer's interpretation of the regulation that is important for your programme )

In general, Austria's experiences are positive as are especially the experiences of cohesion countries and Objective I regions. The Austrian regions gained better opportunities and continuity in their regional policy. The importance of regions increases clearly, regional development improved and created excellent results.

Negative impacts were the high bureaucratic burdens and the large number of programmes ( 38 for a small country like Austria ).

For the period 2000 to 2006 the programming period has been increased to 7 years which simplifies programming work. There is also a higher degree of subsidiarity in the field of programme management. The number of programmes in Austria will be reduced from 38 to 22.

A few general requirements are:

The Member States have to designate a managing-authority which is responsible for implementation and monitoring of the programmes.

The Member State also has to establish a paying authority, which has to handle financial transactions between the Commission and the Member State. The most

important role of the paying authority is in particular the allocation of funding within the Member State to the financial beneficiaries.

Both authorities together have to organize the financial management and the monitoring of payments. This is a challenging task for Member States as commitments by the Commission will be automatically de-committed 2 years after commitment.

The Member State also has to implement a financial control system which controls financial allocations in accordance to eligibility criteria.

The next section covers an actual submission.

## **Addendum 2**

The effort and detailed work involved on both parts, the Member State and the Commission are demonstrated by the 17 page Single Programming Document by Austria for EU assistance for its only objective 1 region - the Burgenland - for a total EU assistance of Euros 271 million, which incidentally required Austrian government contribution of Euros 99 million and private co-financing of over Euros 494 millions.

1. The submission provided first a description of the Burgenland showing all the necessary statistics.
2. This was followed by a statistical comparison with the other Austrian states.
3. This was then followed by a development strategy with three basic aims: 1) to make the Burgenland into a modern Central European region, 2) prepare the Burgenland for the enlargement of the EU, 3) reduce internal disparities within the Burgenland.
4. Then came 'horizontal objectives: to improve the region's economic performance and the competitiveness of its businesses to catch up with the rest of Austria and the EU; to increase the technology level and the educational level of the labour force; the application of the principles of sustainable development; the focus will be on SME sector and business starts, innovation, technology transfer and the development of business co-operation networks.
5. Then came five priority areas and technical assistance measures; 1) Business and industry, 2) Research, technology and development (RTD), 3) Tourism and culture, 4) Agriculture, forestry, fisheries and nature conservation, 5) Human resources, 6) Technical assistance.

The cost of the above "Business and industry" priority area to the structural funds was 88 million Euros, total cost of the scheme was 340 million. The assistance was to go to 5 'measures':

- 1) strengthening the economic development,
- 2) support to SMEs for structural changes and marketing,
- 3) economic infrastructure supporting priorities of the SPD,
- 4) information technology, telecommunications,
- 5) new financial instruments to increase equity capital of SMEs

Similar detailed information was provided for the other 4 priority areas, some showing several of the structural funds contributing.

The document then gives management and contact details:

The Managing Authority of the programme is the Office of the Burgenland government.

The Monitoring Committee is made up of the federal ministers concerned and the implementing bodies involved in part-financing. The social partners and the representative organizations for equal opportunities and sustainable development are also members of the committee.

The Administration is run by OROK - the Austrian regional planning conference.

The Commission requires that one central body be appointed to arrange the liaison with the Commission and the 'implementation/disbursement' of funds to the management authority concerned. Interestingly, in Austria there are several implementing agencies dealing with various fields of assistance. Each fund is monitored by the individual ministry responsible:

ERDF (Euros 173,8 mill ) : the Federal Chancellery, ESF (Euros 55 mill.): the Ministry of Economic Affairs and Labour; EAGGF ( Euros 41,3 mill. ) and FIFG (Euros 0,8 mill.) the Ministry of Agriculture, Forestry, the Environment and Water Management. All relevant data is forwarded from the managing authority and the implementing bodies responsible.

Monitoring is to be carried out over the period 2000-2006. For the first half of this period the following indicators are to be reviewed:

1. To increase GDP per capita for the region from 71% to 77% of the EU average;
2. to create 1500 new jobs;
3. to safeguard 3250 jobs;
4. to change the balance in the labour market in Burgenland in total by + 7000 jobs with special focus in high quality in IT and business services;
5. to increase the economic strength of Mid- and South Burgenland by 4% towards the EU average;
6. enterprises ( 50 from Burgenland ) to participate in competence and cluster networks.

For the second half the indicators are as follows:

1. to create 700 business start-ups;
2. to increase the overnight stays in tourism sector by 4%, and number of quality beds by at least 400;
3. to increase the female activity rate by 2%;
4. to generate and strengthen the private initiatives through public investments;
5. to make sustainable preservation of natural resources as a basis for social and economic development;
6. to identify positive, neutral or negative effects for every single project ( score system based on composite and aggregated data/indicators ).

The above information was provided from DG REGIO/Unit D3/PL, it is interesting but does not allow to ascertain how many disbursements were made, although the Burgenland authorities were required to keep detailed records of all such disbursements. These records were also regularly forwarded to Brussels for auditing.

## Notes.

( 1 ) Cohesion is not defined in the Treaty. However, Article 158 of the Treaty makes it clear that cohesion requires, 'in particular', the reduction of disparities between levels of development of the various EU regions and the backwardness of the least favoured regions or islands, including rural areas. The implication is that pursuit of cohesion and, therefore, the operations of the EU funds are bound up with the concept of equality. However, perceptions of the requirements of cohesion and equality may evolve and may vary as between EU institutions and Member States. In other words, the meaning of the relevant provisions may not only vary in time. Their meaning may also vary depending on the institutional context of their operation. Such variations may be attributable to differences in legal interpretations of social demands, for example, citizens of the 'cohesion countries' may be used to minimal social services and could be prepared to accept them, while in the more advanced economies the expectations for social services are much higher. For this reason it is essential that attention be paid to the social context of the law. What are the present entitlements and what will be expected when the level of per capita GDP reaches the Community level?

( 2 ) Assistance was to be granted to projects, which were supposed to come within the frame work of a Community Programme. The programmes were to be adopted by the Council. Each programme was to specify: the objective to be achieved and the nature of the projects to be undertaken; the region in which assistance should be concentrated; the percentages of assistance for each category of projects and the total cost and estimated duration of the programme. Projects would have priority for support, when they formed part of a comprehensive system of measures to encourage the harmonious development of the overall economy of the region concerned.

( 3 ) A minimum population level or the conservation of the countryside in three categories of regions was thereby to be maintained. This Directive applied firstly: to mountain areas suffering permanent handicaps; secondly less favoured areas in danger of depopulation and finally other areas affected by specific handicaps where farming had to be continued to ensure the conservation of the environment, to maintain the countryside, to preserve the tourist potential of the area, or to protect the coastline.(Evans, p. 126)

( 4 ) EAGGF assistance was provided for:  
restructuring and conversion of vineyards in Mediterranean France,  
improving the rearing of beef cattle in less favoured areas of northern France,  
flood protection programme in the Herault Valley,  
agricultural development in the French overseas departments,  
irrigation in Corsica,  
collective irrigation operations in the Mezzogiorno,  
agricultural development in less favoured regions of northern Italy,  
agricultural development in certain Greek regions,  
improving the structures of the wine-making sector in Greece,  
vine growing in Portugal,  
drainage operations in Ireland,  
the development of sheep farming in Greenland,  
agricultural development on Scottish islands,

agricultural development in the less favoured areas of Northern Ireland.

( 5 ) Such measures are those which encourage and support local development initiatives and the activities of small and medium-sized enterprises. They may include: assistance towards services for firms, particularly in the fields of management, study and research of markets, and services common to several firms, financing the transfer of technology, particularly the collection and dissemination of information and the introduction of innovations in firms.(Evans, 1999, p. 93)

( 6 ) For example, loans were made for irrigation and other rural projects in the Mezzogiorno, and numerous transport and industrial rehabilitation schemes benefited. However, these loans apparently had only a marginal impact on employment in such regions.(Evans, 1999, p. 212) This was mainly due to the kind of projects supported, like irrigation works and SMEs. In the first when actual construction work was completed there was no need for any additional labour, while in the latter, the small loans would have been used for the purchase of modern equipment and could in the end result even in a reduction of the labour force.

( 7 ) The FIFG provided assistance for the re-deployment and reduction of capacity, early retirement from the fishing industry generally, the payment of unemployment benefits for fisherman made redundant as a result of restructuring sponsored by Commission assistance, vocational training and the maintenance or creation of jobs for fisherman in disadvantaged regions. Regulation 4028/86 provided further assistance to: the restructuring and renewal of the fishing fleet through the purchase or construction of new ships, the modernization of the fishing fleet, the development of aqua-culture and structural works in coastal waters, exploratory fishing, joint ventures, adjustment of capacities, provision of facilities at fishing ports and the search for new markets. Its scope has now been further extended. It covers now also: the achieving of a sustainable balance between fishery resources and their exploitation, strengthening the competitiveness of structures and developing economically viable enterprises in this sector, improving market supply and the value added to fishery and aqua-culture products, and revitalizing regions dependent on fishing.

( 8 ) The Commission's insistence that 'partnership' be conducted within the framework of the Member State's national rules and current practices (see above) can lead to the partnership principle to be undermined by national constitutional arrangements, which may allow the central governments of Member states to 'exercise authority' over regional authorities. This happened in Italy where the central government has been criticized for laying down centralized guidelines to be followed by the regional bodies in the drawing-up of regional development plans. Regulation 2088/85 set out that Integrated Mediterranean Programmes were to be drawn up at the relevant geographical level by the regional authorities or other authorities designated. In Italy the designated authority was the region. However, the 'Corte Costituzionale' ( Constitutional Court ) ruled that the Italian Government could alter the programmes drawn up by the regions, because only the Government had knowledge of the national economy and because the Government took much of the financial burden. (Evans, 1999, p. 291) Due to disagreements between the central government and the regions, as well as within the regions themselves, Italy failed to fully utilize the Structural funds available. This lasted throughout the 90s.

( 9 ) In a massive 'Final Synthesis Report' on "The Thematic Evaluation of the Partnership Principle" by the Tavistock Institute in conjunction with eminent leaders in the Member States and the Commission (modified 20th December 2002) which covered the review of 54 Community Support Frameworks (CSF) and Single Programme Documents (SPD) in all 15 Member States, confirmed the above developments. It was further stated that although there were several cases where there were some problems encountered, overall the experience with the partnership principle was beneficial for the satisfactory performance of the projects.

The participation of a large number of "partners" has a considerable impact on the development of project selection criteria, but it is especially important at the programme preparation stage. Unfortunately, some of the partners drop out at this stage altogether, while others then participate in the Monitoring Committees.

The report stated that throughout the fifty-four case studies, a progressive expansion of the partnership principle over time can be observed, from a relationship between the Commission and the Member State; to the Commission, the Member State and the Region; to the Commission, the Member State, the Region and the Social Partners. In about half the cases partnerships are credited with an “increased expression of the principle of subsidiarity”.

The importance of subsidiarity will be highlighted below, as there are now considerable new developments.

At this stage the Member States still have a prominent say as to composition and participation of the partners involved and it is claimed that the Commission’s continuing presence in a ‘day to day’ basis may be needed for the partnership principle to succeed. Member States are in such a dominant position as they negotiate the aid agreement with the Commission and usually provide most technical assistance. As the partnership principle is subject to national legal and administrative practices, there is a wide variety of different implementations. This is further aggravated by the fact that constitutional arrangements are in flux in a number of Member States - the UK, France, Germany, Austria, Spain and Italy.

( 10 ) In Hungary, the local government reform act of 1990 introduced a ‘one settlement, one local government’ principle, which doubled the number of municipalities to over 3000. Similar developments were in the Czech Republic where more than 2000 new municipalities were created ( to produce more than 6000 municipalities ) and in Poland where there are 2483 municipalities.

While the above changes were implemented, intermediate regional or district administrative units were abolished or downgraded. The eight Czech regions were abolished in 1991, while in Hungary the six regional State Representatives of the Republic were abolished in 1994. The outcome of these processes is a vacuum between central and local government. To overcome these problems, different approaches were taken in the various CEE countries, while Hungary, Estonia and Slovenia have taken a ‘top-down’ approach to creating sub-national implementation structures, the reverse is the case in Poland. The absence of national regional policy institutional leadership and also the weakness of public institutions at the voivod level led to the ‘bottom-up’ creation of regional development agencies by varying combinations of regional and local partners. They have attempted to fill the vacuum between public administration and the private sector in economic development tasks and to generate new financial resources. This lack of clear responsibilities is a matter of concern as information is not guided efficiently to where it is needed. For example, Poland’s farmers were entitled to some 800 million Euro assistance, but only some 12 million had been claimed at the end of the application period, the Commission extended the application period by one month to August 2004 and started an awareness campaign in order to help the farmers.

( 11 ) Most prominent is the dominant role of core and capital city regions; indeed, in countries such as Hungary, the Czech Republic, Estonia and Latvia there is no centre which rivals the capital city. In the Czech Republic, Prague is the only region with a GDP above the national average, and the disparity between the capital and remaining Czech regions is increasing; all other regions have a GDP below the national average. A similar story applies to Hungary with increasing disparity between Budapest and the remainder of the country. Budapest accounts for 40% of the total urban population ( two million inhabitants, compared to the next largest centre which has only 200,000), 35% of service sector employment, and an unemployment rate less than half the national average. Budapest has more joint ventures than the rest of the country combined and accounts for nearly two-thirds of all FDI flowing into the country. Similar figures apply in the other CEE countries.

( 12 ) The privatization of agriculture has, in some CEE countries, left farmers in a precarious position. There has been a partial return to subsistence farming on small, uneconomic plots, lacking fertilizers and other costly resource inputs, and unviable for mechanized farming. The ‘playing field’ for competition is not always fair, with the remaining state-owned farms still receiving preferential government support, and with agricultural supply or marketing enterprises still under state control. Alternate employment opportunities are often limited or non-existent, foreign investment is lacking and

unemployment rates are consequently high. Demographic factors also play a part. De-population and out-migration are characteristic of some rural and underdeveloped agricultural regions. Migrants are often the younger or better-qualified people who rarely return, exacerbating already imbalanced age-sex structures. The problem of an aging population in a number of countries (Slovenia, Czech Republic, Hungary) tends to be concentrated in rural and peripheral areas.

( 13 ) EIB operational priorities:

Regional development and economic and social cohesion within the Union,  
Implementation of the “Innovation 2000 Initiative”,  
Environmental protection and improving the quality of life,  
Preparing the Accession Countries for EU membership,  
Community development aid and cooperation policy in the Partner Countries.

Alongside these main priorities, the COP also defines policies for:

financing SMEs via global loans and venture capital operations,  
trans-European transport and energy networks (TENs),  
human capital formation.  
(EIB - Objectives Dec. 2001)

( 14 ) In 2003 the EIF was commissioned for the first time by a third party to invest venture capital on behalf of the German Federal Ministry of Economics and Employment which is making available a Euro 250 million “ERP Facility” ( funded from Counterpart Funds of the former European Recovery Programme). The resources from this facility, supplemented by a further Euro 250 million from the EIB /EIF, will be invested exclusively in venture capital funds focusing on German high-tech companies.

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The Structural Funds Regulations for the period 2000 to 2006 are:

- I. Council Regulation (EC) No 1260/1999 of 21 June 1999 lays down general provisions on the Structural Funds.
- II. Regulation (EC) No 1783/1999 of the European Parliament and of the Council of 21 June 1999 on the European Regional Development Fund.
- III. Regulation (EC) No 1784/1999 of the European Parliament and of the Council of 21 June 1999 on the European Social Fund.
- IV. Council Regulation (EC) No 1263/1999 of 21 June 1999 on the Financial Instrument for Fisheries Guidance.
- V. Council Regulation (EC) No 1257/1999 of 17 May 1999 on support for rural development from the European Agricultural Guidance and Guarantee Fund (EAGGF) and amending and repealing certain Regulations.

EU Partnership Review (Tavistock Report)

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2. The Thematic Evaluation of the Partnership Principle, final Synthesis Report.

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## **COMPETITION POLICY.**

In this chapter the impact of the European Union's Competition Policy on the Member States will be reviewed. To achieve this, legislation that introduced new rules and the political climate that led to its creation will be considered. How the Commission implemented the rules and how they affect the various layers of government (multi-level government -MLG) in the Member States will be examined and finally an assessment will be made of the overall economic impact of the competition decisions on the European economies. The separate EU Competition Policy subdivisions of Merger Section, Antitrust Section, State Aid Section, and Regulated Industries Section have been reviewed individually to ensure their separate impact is shown and to allow for a clearer overview.

It is my view that when the Treaty of Rome (1957) was signed, the heads of government and state had no idea how far competition policy would develop and impact in virtually every aspect of Community life. Like so many other cases in the EU (Environment Policy, Agriculture, Area of Freedom, Security and Justice etc.), it started to grow and now nearly has a life of its own. It is considered that the ambition to establish a "level playing field for everyone" is sheer economic madness - after all, no one else is so unconditionally opening up its market for its competition, neither the Japanese, Chinese or, for that matter the United States. The consequences of this irresponsible action can now be seen - some 20 million unemployes and economic stagnation. To be sure there are many other causes, but Merger Policy especially is to my thought largely responsible. Why are mergers approved when the companies concerned openly state that in order to achieve maximum benefit some 5000 employees will be terminated? The limitations on State Aid and the privatization of public companies come a close second in these culpability stakes. A number of distinguished authors specialising on the EU support this view: Elie Cohen, Jacques

Bourgeois, Paul Demarel, Nikolaos Zahariades as well as Lee McGowan and Michelle Cini.

Competition policy in the Community deals not only with private sector abuses in the market place but also with massive government financial assistance to national enterprises and with utility services - such as electricity, water, and telecommunications - which European governments have traditionally controlled. By including efforts to curb state subsidies to industry and confront government monopolies, therefore, Community competition policy involves much more than anti-trust. As well as policing the market place, Community competition policy seeks to break down barriers between national markets, thereby promoting European integration. ( Dinan, 1994, p. 373 )

Moreover, competition policy has a political purpose in the Community that goes far beyond the economic objective of say, the United States. Cacciato states (Cacciato, 1996) that American anti-trust law says nothing about state aid or about pre-emptive control of subsidies by any level of government. He finds this paradoxical, as the ideology behind anti-trust is clearly an exaltation of free competition in a market economy one would expect an explicit and stringent restriction of subsidies in American anti-trust law. But, since a 'single market' has existed in the US to a certain degree since the establishment of the Union itself, legislators only saw the need to protect this market against the most powerful actors, namely the large industrial corporations.

The Treaty Establishing the European Community (Treaty of Rome, 1957) instructed the Commission to ensure the application of the principles laid down in Article 85 - which prohibits as incompatible with the common market the following: all agreements between undertakings, decisions by associations of undertakings and concerted practices which may affect trade between Member States and which have as their object or effect the prevention, restriction or distortion of competition within the common market.- and Article 86 - which prohibits as incompatible any abuse by one or more undertakings of a dominant position within the common market or a

substantial part of it in so far as it may affect trade between Member States. The necessary Regulation was to be adopted within three years of the entry into force of the Treaty. (Rudden & Wyatt, 1996, pp. 56-59). These guidelines were to be the foundation of the EU's Competition Policy. Article 85 became Article 81 and Article 86 became Article 82 from Regulation No 4064/89.

The aims of this Policy are to create a level playing field for all in the common market and to ensure that there are no impediments to trade between the Member States.

The progress achieved was relatively minor until the mid 1980s. However, there was one development of crucial importance. In 1979 the Court of Justice ruled in the celebrated '*Cassis de Dijon*' case that if a product was lawfully produced and marketed in one member state it must then be accepted in any other Member State. This meant that non-tariff barriers such as technical specifications, could not be used in an effort to exclude some products from markets in other Member States. The principle of "mutual recognition" was thus established, with the result that the need for legislation to harmonize standards in order to facilitate trade was much reduced. (Nugent 2003, pp. 254-255).

In 1985 the European Council agreed to what became known as the Single European Act (SEA), which came into force in 1987. Its aim was to remove all tariff and non-tariff barriers, and so complete the internal market by 1992. This act introduced a number of new policy areas, which the entrepreneurs were quick to realize for their potential profit promises. (1)

As indicated above, developments after 1985 are considered the relevant part of the European Union's competition policy, this date will therefore be the starting point for this research.

## Mergers.

At this stage it has to be noted that the Treaty of Rome omitted merger control from its competition rules. The Commission realized from the outset that this needed to be rectified and submitted Merger Control draft regulations in 1973, 1982, 1984 and 1986, but they all failed to get Council approval.(McGowan & Cini, 1999)

The prospect of losing the protection of national markets plus the challenges in a huge borderless market led business leaders to seek enlargement by mergers and acquisitions. The number of cross-border mergers increased from 115 in 1982-83, to 208 in 1984-85, to 492 in 1988-89 and to 622 in 1989-90. Due to these developments the Council finally began to perceive European merger control as a priority.

Fortunately, at this stage the European Court of Justice (ECJ) came to the assistance of the Commission through its controversial 1987 Philip Morris judgment (Cases 142 and 156/ 84 1987 ECR 4487) in which the ECJ ruled that under certain circumstances Article 85 (81) as well as Article 86(82) might be used to regulate mergers. (McGowan & Cini, 1999)

It is hard to believe that this case which started as a minor complaint would lead to the establishment of the powerful competition policy. The Philip Morris case had begun with the complaints made to the Commission by two tobacco companies, BAT Industries and RJ Reynolds, about an agreement between two of their competitors, Philip Morris and Rembrandt. This agreement not only gave Philip Morris control over one of Rembrandt's subsidiaries, Rothmans International, but also provided the company with first refusal on any future sale of Rothmans' shares. The Director-General, Competition (DGIV) insisted that the agreement had to be altered. In Philip Morris's appeal, not only was the Commission decision upheld, but the ECJ also commented on Article 85(originally 81)'s (restrictive practices) applicability to mergers. It was stated that this Article could be used if a concentration occurred as a result of agreements entered between two or more companies. In other words, the ECJ affirmed that an agreed share transaction could be classed as a restrictive agreement under Article 85(81), thus giving the Commission the right to intercede in so-called 'friendly' mergers.

Two weeks after this judgment, on 17. November 1987, the Council finally gave the Commission concurrence to proceed with a draft merger regulation. After protracted and often passionate negotiations, a radically altered version of the Commission's original draft regulation was agreed on 21 December 1989, after two years of negotiations. (McGowan & Cini, 1999)

The Merger Control Regulation (MCR) became effective as of 21. September 1990 (Council Regulation (EEC) No 4064/89). As mentioned before, this Regulation had an extremely difficult and long gestation period and as it was the result of compromises, no one was totally satisfied. One of the main problems was the definition of Community dimension. From what level on should a merger become the responsibility of the Commission? This was a crucial point, as the member states wanted as high a level as possible as this would give them power to control the enforcement of the merger policy in most cases. The agreed level of 5,000 million Euros had this effect. Industry on the other hand wanted a lower level as this would enable companies to be investigated under EU Commission rulings if, for example, their merger affected more than two states. A 'one-shop' enforcement operation was preferable to a complicated operation if more states were involved. In the negotiations the Commission proposed originally 10,000 million Euros as a starting point, while the Member States demanded 5,000 million. An agreement to the latter level was made, subject to review after 4 years. Industry complained that this level was too high, the Commission agreed, but they suggested that the excess would be eliminated in a few years due to inflation. Following industry representations this was reduced to 2,500 million at the review date. Below this level and subject to other minor restrictions the Member States were responsible for implementing merger rules. The Commission could intercede in a case if it thought that Community interests were in danger, in addition Member States could invite the Commission to undertake a merger investigation on their behalf, where a merger does not fall within the EU's jurisdiction. This can be useful where national laws are weaker than those at the European level or where national authorities are seeking guidance from Brussels. (McGowan & Cini, 1999)

The Commission and the Member State Competition Authorities could now either:

1) approve a merger outright, 2) approve a merger with conditions 3) prohibit the merger.

Also from 1990 the responsibility for merger investigations in the Commission rested with the Merger Task Force (MTF) within the Director-General, Competition (DGIV). According to the Merger Control Regulation (MCR) all mergers exceeding the before mentioned thresholds must be notified to the MTF. The MCR includes an explicit timetable which sets out when the MTF must initiate, research and complete its investigation. The MCR has two time frames, Phase I, which is to be completed within 4 weeks and Phase II which is required to be completed at the latest within 5 months. This system appears to be working well: by the end of 1998 the MTF had received 913 notifications and taken 822 final decisions. 711 were cleared after the initial investigation, 19 were referred to a national authority, 52 became subject to a Phase II investigation while 10 had been prohibited. (McGowan & Cini, 1999)

These powers were further amended in 1998 (Commission Regulation No 447/98). The Commission was now allowed to accept relatively early in an investigation an undertaking of the parties concerned to make the nature of the post-merger firm acceptable to the Commission. This in effect allows the Commission to review and to make arrangements with the interested parties during the negotiations, the applicants do not have to wait until the hearing is completed before they find out if their case is successful. This is one of the reasons why the DGIV can finalize nearly all his/her cases in the time prescribed. (Martin, 2001, p. 135 )

The latest amendment to the rules has been made on the 20. January 2004 in the Council Regulation (EC) No 139/2004. This clarifies the meaning of 'concentrations'. Companies requesting merger approval are now required to submit the total annual turnover for all companies involved, on a 1) world-wide basis, 2) Community-wide basis, 3) EFTA-wide basis, 4) in each member state, 5) in each EFTA state.

This Regulation became effective from 1. May 2004.

Finally, it should be noted that the Competition Commissioner (DGIV), although having a powerful position, has in the end to rely on his fellow Commissioners if the prohibition of a merger becomes an issue. Politicization has thus been built into the EU merger control. Even though the DGIV works extremely carefully to ensure the right decision is made, occasional problems do occur. One is the famous ‘De Havilland’ case. The Italian Alenia and the French Aerospatiale wanted to take over the Canadian DeHavilland aircraft manufacturer. Leon Brittan, the UK DG IV claimed that the merger was violating the EU Merger Regulation. Fierce arguments ensued. The Italian and French Commissioners wanted the merger to proceed, but Brittan prevailed. The media took over the battle. The claim was that the merger was blocked because Brittan wanted to protect the British Aerospace Corporation which at the time was vulnerable to takeover. The French Foreign Minister Dumas claimed that competition policy should be used ‘to strengthen, not hinder, the competitiveness of European industry’. There also ensued a public confrontation between DG IV and DG III, Martin Bangemann, the Commissioner of Industrial Policy, who attacked the competition officers in DGIV as “ayatollahs”, arguing that they ruled on merger cases without taking into account economic reality. (Laudati, 1996, pp. 236-237).

Some of the merger cases that the Commission has stopped are:

The 1999 judgment against Gencor/Lonrho, the merger was stopped as it was considered that the companies, together with another company, Amplats, would have a combined world market share of 60-70 % in platinum and rhodium.

The 1999 Airtours/First Choice decision pushed the collective dominance doctrine further by blocking a takeover that would have reduced the number of leading firms in the UK travel operator market from four to three. The Commission estimated the combined 1998 market shares of Airtours and First Choice at 34.4 %, with the next two leading firms being 30.7% and 20.4% respectively. If these market shares remained unchanged, the post-takeover market would have been one in which the leading three firms had a combined market share of 85%. For the Commission, this

was sufficient to justify a finding of collective dominance under paragraph 54. ( Martin, 2001, p. 136 )

In March 2000 the Commission blocked Swedish truck and bus maker AB Volvo's \$ 6,95 billion merger with rival Scania. It was considered that the combined company would have 90 per cent in the Swedish market and 75 per cent in the Nordic market, but only 30 per cent in the EU market. The ruling was controversial as the merger was blocked on a country-specific basis rather than looking at the EU as a single market. ( Hitiris, 2003, p.71 ).

Further merger cases are shown in footnote ( 2 ).

### **An Assessment of EU Merger Policy.**

As the merger clearance statistics (see previous paragraphs) indicate, merger control policy appears to be an exemplary success. Not everyone agrees with that assessment. For example, McGowan and Cini (1999) report that important questions have been raised about the future development of merger control practice. Should the Commission be striving for a neutral, objective, rule-bound system of regulation which allows only a limited discretion for decision-takers, or should officials be permitted a certain degree of flexibility when reaching merger decisions? Should the encouragement of competition be the only consideration, or might other factors, such as European competitiveness or social and regional implications be taken into account?

Zahariadis (2002) maintains that the 345 mergers and acquisitions in 2000 in the EU totaled 326 billion Euros and that monopoly abuses, such as predatory pricing, tying agreements, and discriminatory pricing, or at least the potential for such behaviour, are most likely to take place when firms are expanding by acquiring or merging with other firms. It would be fairly simple to carry out any of the foregoing abuses while the companies are in turmoil due to the merger. As the Commission finalizes its action on the approval of the merger - provided there is no 'commitment' by the companies to take some further action, any of the above abuses could be easily hidden. Especially as

it takes experienced officers with insight in the company, or a “whistleblower” to note/report such activities. For these reasons Zahariadis’ conclusion is concurred with.

I am strongly of the opinion that merger policy should be changed from largely supporting mergers and having the interests of the business world at heart, to one that encourages employment and development in the Member States. Current economic circumstances with an unemployment rate of over 10% in the EU have surely been affected by mergers. After all, companies usually claim improved productivity and profitability by retrenching sometimes thousands of employees. The latest of this was the Spanish Santander Bank which proposed buying a Scottish bank and indicated that some ten thousand would be retrenched. It should be noted that not a single ‘European champion’ has emerged from this merger policy. As Elie Cohen (1996, p. 142) explains, there were quite a few ‘national champions’, alas, they were state companies, Bull, Renault and Air France are some of them. But he claims that the state company is condemned to disappear. The reason for this is that a public service first has to mutate into a universal service, then into a delegated service, and finally into a marketable service. This is the fate of all public service undertakings: deregulation leads to privatization which reduces the public service to a suitable size. These were apparently also the terms accepted by the French government when it negotiated plans for the recapitalization of state-owned companies, like the above mentioned Bull, Renault etc.

The Commission has lately claimed (Barcelona Declaration, 2002, the job summit in Luxembourg in November 1997 and the European Council meeting in Lisbon in March 2000) that full employment was its main aim. Some specific goals were: for the Union to become the most competitive and dynamic knowledge-based economy in the world, and to increase the employment rate from an average of 61 % in 2000 to as close as possible to 70 % by 2010. However, it appears at this stage that industrial policy is still running a long second after competition policy. Elie Cohen (1996, p. 144) stated in rather forceful language that in European industrial policies generally - see above for details - and in relation to European HDTV specifically, in which the

EU's policy clearly failed: "that this relates to the EU's idiosyncratic stance: the obsession with competition, which puts pre-competitive research on a pedestal, which is interspersed with financial incentives and egalitarian ideology, whilst showing open hostility to all forms of policies promoting national leaders without making the means available to promote European champions, a dramatic lack of means and inability to react". Whether his description is still fully applicable will be revealed in later chapters.

### **ANTITRUST**

The original anti-trust legislation was provided in Council Regulation No 17 of 6. February 1962, which implemented Articles 81 and 82 of the Treaty. This has allowed a Community competition policy to develop that has helped to disseminate a competition culture within the Community. Since then, several Regulations have been issued with limited application, as they refer only to certain categories of agreements. They are 19/65/EEC, (EEC) No 2821/71, (EEC) No 3976/87, (EEC) No 1534/91 and (EEC) No 479/92. The Commission considered that in the light of experience, that Regulation No 17 of 1962 should be replaced by legislation designed to meet the challenges of an integrated market and future enlargements of the Community. Council Regulation (EC) No 1/2003 of 16 December 2002, which came into force on 1. May 2004 is now meeting this requirement.

As the Commission can impose hefty fines for infringements of Articles 81 and 82, it found now that the threat of such fines was a serious deterrent for companies to report cartels. It has therefore issued a notice which allows immunity from fines or a considerable reduction if the firm cooperates with the Commission. (Official Journal C45, 19.02.2002)

A short view of the two Articles will give an indication of how important eradication of such infringements is.

Article 81 of the EC Treaty prohibits agreements and concerted practices between firms which “may affect trade between Member States and which have as their object or effect the prevention, restriction or distortion of competition within the common market”. The practices which are prohibited almost without exception are shown in footnote (3).

Under Article 81 certain forms of cooperation agreements between enterprises, which are considered beneficial for the consumers by improving production, distribution, or technical progress, are deemed not to restrict competition and therefore they are exempted. (Hitiris, 2003, p. 68 )

Article 82 of the Treaty states that “Any abuse by one or more undertakings of a dominant position within the common market or in a substantial part of it shall be prohibited as incompatible with the common market in so far as it may affect trade between Member States”. Such abuses may consist in:

- directly or indirectly imposing unfair prices or other unfair trading conditions;
- limiting production, markets or technical development to the detriment of consumers;
- applying dissimilar conditions to equivalent transactions with other trading parties;
- making the conclusion of contracts subject to acceptance by the other parties of supplementary obligations which have no connection with the subject matter of such contracts.

A few important cases show the Commission’s impact:

The ‘United Brands’ decision shows how complicated competition policy can be. In the early 1970s, the United Brands Company (UBC) was the leading banana producer in the world and had a market share of some 40 % in the EU. The company’s operations were vertically integrated, from banana plantations through ocean shipping to destination markets. In those markets it employed networks of banana ripeners and distributors that were subject to vertical restraint. These restraints had the effect of

partitioning the EU into national sub-markets. The Commission argued that UBC had abused its dominant position by charging unfair prices. After appeal, the ECJ found that there was abuse of a dominant position, but it also found that the Commission should have made direct investigations of UBC's costs and reached a conclusion about unfairness by comparing costs and prices. The Commission's finding was set aside. However, UB was still fined 3,077,000 Dutch Guilders. This is a fifty page judgment. Case 27/76 of 14. 2. 78.

The 'BA' case, CFI T 219/99. In the late 1990s British Airways used incentive schemes for payments to travel agents under which the agents were paid more, the greater the increases in their customers' bookings with BA over the level of the previous year. The Commission found that BA's loyalty payment scheme was an abuse of a dominant position, and fined BA 6,8 million Euros. CFI case T 219/99(Martin, 2001, pp. 133-134).

In June 2001 the European Commission decided to impose a fine of 19.76 million Euros on the French tyre maker Michelin for abusing its dominant position in replacement tyres for heavy vehicles in France during most of the 1990s. After a careful and lengthy investigation, the Commission has come to the conclusion that Michelin's complex system of quantitative rebates, bonuses and other commercial practices illegally tied dealers and closed the French market to other tyre manufacturers.

In October 2001, the Commission imposed a fine of 71.825 million Euros on DaimlerChrysler AG., for three infringements against article 81 of the EC Treaty. The infringements were: 1) obstacles to parallel trade ( cars could not be sold outside the dealer's territory). 2) sales to independent leasing companies were restricted and finally 3) a price-fixing agreement in Belgium. ( Hitiris, 2003, p. 69 )

The far reaching, all embracing impact competition policy has in the EU is shown by the number of case rulings in the field of 'Restrictive Agreements and Concerted

Practices' that were covered during the first three months of 2004, some of them have been listed in footnote (4).

### **Regulated Industries.**

Governments have sheltered certain industries from competition because of those industries' fundamental economic importance. Thus telecommunications, energy (electricity and natural gas ), banking, insurance, and transport have traditionally been highly regulated. In many cases they are wholly or partly government-owned. In close association with the single market program, the Commission has begun to apply competition law to liberalize those sectors. ( Dinan, 1994, p. 379)

The rulings of concentration and dominant market position can be brought into action in this field, Article 86, 81 and 82 refer. Action is normally taken under the Director General for the particular area, for example DG Energy. The latter has for example issued a publication stating that most of the Member States had missed a deadline to adopt the laws into the national legal system by the 1. July 2004 which would boost competition in gas and electricity markets. A referral to the ECJ would be considered if the Member States failed to comply. (Associated Press 3. 7. 2004, 'EU Scolds Nations for Missing Deadline')

The idea that market liberalization in energy was a boon for consumers has also not come to fruition. Austria reports that the expected increase in the number of suppliers and thus reduced prices has not materialized.(Kurier, 23. 8. 2004) While in Germany the 900 odd suppliers had announced price increases of up to 20%, this matter has now been taken over by the Chancellor. The national control authority RegTP is incapable of carrying out the job of review and control. (Spiegel, 11.9.2004)

It appears that the application of competition policy to the energy sector at this stage has not had the desired effect. Instead of leading to lower prices for consumers, the energy supply companies seem to abuse their positions in an essential sector by

increasing their prices. The expected move of consumers to the lowest priced supplier did not eventuate. However, this will be investigated in detail as part of the Trans European Networks for Energy, (electricity and gas) and Transport in a later chapter.

## **STATE AID**

Control of state aid is an even more politically sensitive subject than merger policy. Although member states agreed in Article 92 of the EEC Treaty of 1962 that state aid should be prohibited in most circumstances, in practice they have allowed themselves broad latitude under the exceptions included in the treaty - notably aid to poorer regions - especially during economic recession and when facing political and social fallout from the precipitous decline of industries. State aid conditions are sufficiently clearly set out in the Treaty, it appears that the Member State governments are aware of all the requirements relating to state aid.

Prohibited state aid is summarized as follows:

Article 87 of the Treaty states that “any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, in so far as it affects trade between Member States be incompatible with the common market”. Any advantage granted by the state or through state resources is considered to be state aid where:

- it confers an economic advantage on the recipient;
- it is granted selectively to certain firms or to the production of certain goods;
- it could distort competition; and
- it affects trade between Member States.

Permitted state aid:

Article 87(2) and (3) lists state aid which is compatible with the internal market:

- state aid having a social character, granted to individual consumers, provided that it is granted without discrimination related to the origin of the products concerned;

- aid to make good the damages caused by natural disasters or expected occurrences;
- aid granted to areas of Germany affected by the division of the country.

The Commission may also declare the following to be compatible with the internal market:

- aid to promote the development of certain activities or regions;
- aid to promote the execution of an important project of common European interest or to remedy a serious disturbance in the economy of a Member State;
- aid to promote culture and heritage conservation;
- other categories of aid specified by the Council.

The Commission has also granted “group or block exemptions” which are not subject to notification, they are: aid in favour of:

- small and medium-sized enterprises;
- research and development;
- environmental protection;
- employment and training;
- aid that complies with the map approved by the Commission for each Member State for the grant of regional aid.

In order to comply with the Commission’s requirements :

Member States must:

1. Notify the Commission in sufficient time of any plans to grant new aid.
2. Forward to the Commission summaries of the information regarding systems of aid or individual cases of aid not covered by the notification requirement as soon as they are implemented.
3. Keep detailed records of any group exemptions and forward these annually to the Commission.
4. Prepare and update the aid map in cooperation with the Commission.

The ‘aid maps’ show the per capita GDP in each region of a Member State and aid can be provided on the basis of that income level. It is considered that the following aspects of development called “Objectives” are worthy of aid:

*Objective 1.* To promote the development and structural adjustment of regions whose development is lagging behind. Regions covered by Objective 1 are those where per capita GDP is less than 75 % of the EU average.

*Objective 2.* To support the economic and social conversion of areas facing structural difficulties. Amongst areas covered are those under-going socio-economic change in the industrial and service sectors, declining urban and rural areas, and depressed areas dependent on fisheries.

*Objective 3.* To support the adaptation and modernization of policies and systems of education, training and employment. This Objective provides for formal assistance outside the areas covered by Objectives 1 and 2.

The Commission has agreed with each Member State on the permissible state aid, say if one state has been authorized to provide aid up to 30%, this can then be arranged, but usually the aid provided falls below the authorized level.

A weak Commission and a deep recession combined in the 1970s virtually to end Community-level efforts to control state aid. The introduction of the single market (SEM) from 1985 on revealed that strict control of state aid became as vital as the vigorous application of anti-trust law.

No new regulations were issued, but in 1992 the new Competition Commissioner Leon Brittan, reviewed state aid requirements, and with the old tools of Article 92 started to enforce the requirement that state aid was to be reported to the Commission before being granted. A Commission survey of state aid in 1992 showed that public assistance had fallen slightly from an annual average of 93 billion ECU in 1986-1988 to 89 billion ECU in 1988-1990. Most of the state aid went to the Community’s better-

off regions. This represents some 4 % of the value added in manufacturing and shows the immensity of the problem.

At this stage, if the Commission considered that the Member State failed to fully comply with the rules, it could demand that the aid be repaid to the government concerned and ultimately the firm could be taken to the ECJ. (Dinan, 1994, p. 378) But even this proved insufficient as 21 per cent of 1997 aid cases were not notified to the Commission. In many cases firms kept aid after a decision that it was incompatible with the common market. Nearly 10 per cent of the recovery decisions are not executed 10 years after they have been taken, in the majority of cases because of pending procedures before national courts. (Sinnaeve 1998:80)

The Commission finally was able to issue new regulations which clearly set out permitted and prohibited state aid and the actions required by the Member States in Council Regulation (EC) No 994/98 and Council Regulation (EC) No 659/1999.

Some state aid cases are listed in footnote (5).

### **Assessment of State Aid.**

The annual amount of some Euro 90,000 million provided for State Aid by the 15 Member States before 1. 5. 2004, indicates that the governments are either unable or unwilling to drastically curtail this aid. Older industries have a well established base of employees, unions and suppliers which can provide pressure on governments and thus are able to obtain state aid. For large companies, governments will have to be very careful in ensuring that all EU requirements are met, competitors will make sure of it. However, the Commission has granted many “block exemptions”, for example for Small and Medium Sized companies (SME) with up to 250 employees. This allows the member governments ample room for aid. The newly acceded CEE members do have a much more serious situation, with the near collapse of their economies in 1989, governments were forced to provide state aid in order to maintain political power. It has been advised that in the enlargement program until 2002, 222 state aid measures had been accepted by the Commission and the new Member States for inclusion in the

Accession Treaties. From the beginning of 2003 until the end of February 2004 a further 288 measures had been received by the Competition DG from the acceding countries. 40 per cent of them have been approved by the Commission, while 60 per cent were still under assessment due to their recent submission or because of being modified by the acceding countries.(Lowe, 2002) The Commission's effort may lead to a reduction in legitimate state aid, but as the Member States have lost the power to influence their economies with tariffs and non-tariff barriers, I consider it more likely that Member States will bow to pressure from powerful interests and provide state aid, either legally or illegally.

### **Competition Policy effect on the multi-level governance (MLG) in the Member States.**

Effective with the 1. May 2004 the Commission has further delegated responsibilities to the now 25 Member States (Council Regulation (EC) No1/2003). Regions and other local authorities, as well as private people or companies are now encouraged to assist in the enforcement process of competition control. The Commission desires that it now virtually act as a supervising or guardian agent, it can so concentrate on the more important cases and assist the Member State authorities with their work. It can be claimed that the principle of subsidiarity is being observed, but interestingly the authority has not been devolved back to the states, but to more or less independent institutions - the courts and national competition authorities. This will eventually result in a transfer of loyalty from the state to the lower levels, thus weakening member state powers and therefore indirectly enhancing the EU's powers. Nugent (2003, pp. 473-4) claimed that the EU will continue to expand the creation of additional layers of responsibility and thus create a multi-level governance system (MLG). This appears to be happening.

To ensure that these organizations can work effectively and independently a "European Competition Network" has been set up between the Commission and all the Member States' competition authorities. This is expected to strengthen them, as

officers in the Member States can refer to other states' officers or to the Commission for support and help if required.

### **The impact on European Economies.**

Competition policy has had a significant impact on the European economies. Actions to remove all barriers to trade in the EU, as well as the elimination of cases of dominant position with unfair pricing practices have helped the consumers. But, this has gone further than many would have preferred as competition policy has also been extended to trade outside the European Union. Level playing fields were to be granted to foreign companies. This was exacerbated by some officials advocating the primacy of competition policy in the strict sense of the term without regard to industry needs. (Glais, 1995, p. 254)

Some industrial areas in the European Union have not been subject to the general open industry/competition policy usually applicable in the EU. In many cases there was heavy interference by the Commission, but there were also many cases of huge financial subsidies. The main areas that come to mind are, agriculture, the automobile industry, the chemical fibres industry and the steel industry. The latter will now be looked at in some detail as I consider that the steel industry is the industry that has first been encouraged and then subjected to stringent competition policy with enhanced Commission input in the Member States.

Concern about steel and coal was the reason for establishing the European Coal and Steel Community (ECSC) in 1951. In the 1950s and the 1960s the problem of the steel industry was how to respond quickly to rapidly expanding demand, but since the 1970s the problem has been how to contract under the pressure of declining demand and rising foreign competition. The difficulties of the industry stem from the sudden change in demand after a long period of growth (6,6% per year during 1960-74) to a rapid collapse as a result of the first oil price shock in 1974. Economic growth resulted in a steady expansion of demand in the 1960s, which induced major capacity-increasing investment programmes. This activity continued even after the first

economic crisis of 1974, under the assumption that the difficulties of the industry were cyclical and temporary. High fixed costs and entry and exit barriers combined to bring about chronic market failure - the inability of the sector to make timely adaptation to changes in demand and competition. This led to massive under-utilization of capacity (62% in 1980), staff reductions (by 50% between 1974 and 1986) and a slump in prices (50% within two years). Accumulating financial losses had adverse effects on new investment for modernization. The industry could not compete effectively with technologically advanced new foreign producers. Consequently, between 1974 and 1976 steel imports to the Community rose by 133%, while exports fell by 32%. (Hitiris, 2003, pp. 300-301)

Quotas enforced by the Commission led to a reduction in capacity of 32 million tonnes by 1986. But at this time there was still an EU over-capacity of some 30 million tonnes (Glais, 1995, pp. 231-232). Further introductions of quotas, plus the provision of 50 billion ECU/Euros in aid for restructuring and reduction in capacity, in 1993, corresponded with the opening up of the European economic area to steel products from the countries of the former socialist Eastern bloc. This proved problematical as they could supply steel goods at prices of 40 to 50% below community producers. (Glais, 1995, p. 242)

To control the situation a more stringent competition policy was enforced - beam producers were fined more than ECU 100 million on concerted practices. (OJ No. L116 of 16 February 1994)

Glais (1995, pp. 252-3) reports that then, although the CEE countries had already substantially reduced their supply in the last 4-5 years, these countries still had considerable production capacity and output, particularly since the previous economic system did not encourage them in any way to economize on steel. In the 1980s, per capita steel consumption in Eastern Europe was 100 kg higher than in Western Europe. However, these per capita consumption figures fell from 274,5 kg in 1987 to 107,6 kg in 1992 in Hungary and 316,5 kg in 1987 to 112,5 kg in 1992 in Poland.

Suppliers in these countries were trying to maintain a minimum capacity utilization rate by exporting to the West. In 1993 measures were taken to control the flood of steel products from some of them.

The fixation in the EU with “the primacy of competition policy” is reflected in professor Michel Glais’ (1995, p. 219) statement: ‘Despite substantial aid granted to firms in the industry, the restructuring process is far from complete since there is still ample excess capacity. In addition, continuing intervention in support of the industry is clearly at odds with the creation of an open and competitive environment’. ‘No objection can be raised regarding the choice made in favour of the primacy of competition policy’.

Since then, production capacity has been reduced in all the EU states, see example below, and it was reported in July, that an Austrian specialty steel pipe manufacturer had to close down the plant for several weeks due to a shortage of steel. This was the result of steel exports being directed to the booming Chinese market. It appears that restructuring has gone too far. Has competition policy gone too far? The question is, was the privatization of most steel companies the only solution? If a privatized company announces unused excess capacity this is reflected right away in its share price. In a state-owned enterprise this would have no effect.

However, the “corporatizing” and “privatizing” of many state undertakings is in many cases problematical. This is especially so in the CEE member states, for example one steel works in Poland had to reduce its work force from some 32,000 in 1990 to some 4,000 in 2000 in order to find a buyer.(Cohen, 1966, p.142; Hudson, 2002, p. 274)

The unfettered merger storm has been most beneficial for the shareholders of companies. However, in every case management stresses the future increased profitability due to down-sizing. The number of unemployees thus created raise little concern.

## **Conclusion.**

Member States' economies and administrations have been revamped considerably by the implementation of the European Competition Policy. Business is now aware of the requirements needed to comply with EU rules (Monti, 2000), border tariffs and many non-tariff barriers have been abolished while a high level of harmonization of national competition laws has already occurred spontaneously in the Member States.( Majone, 1996, p. 273) The Spanish and Italian competition enforcement policies have been based largely on the Union policy, the German competition policy has been adapted considerably, while the UK policy is to some extent different as it relies more on consultation and ministerial input.

Competition Policy is the most advanced area in the EU due to the DGIV's virtual independence from Council or Parliament which allows him/her to take pro-active action, but the DGIV is also vested with special powers, since he/she has the sovereign decision whether to bring an action, and to be involved in both the examination and the sanctioning stages; there is also the implied threat of transfer to the Court of Justice. Most decisions are subject only to a Member State Advisory Committee advice. However, the Commission is aware that any of its decisions could be referred to ECJ. Nonetheless, the policy impacts on many other policy areas, especially the Internal Market, the Regional Development, the Energy and the Environment DGs.

The many infringements and abuses by European firms that have been investigated and prosecuted by the Commission - fines of some 2 billion Euros are being handed down each year - clearly show the need for a vigorous competition policy. As outlined above, competition policy has assumed a dominating role in the industrial policy field in the European Union. This dominant position is shown by the new provision in the Maasstricht Treaty, Article 130, which was introduced in the EC Treaty to specifically deal with industrial policy. Article 130 states that industrial policy measures must comply 'with a system of open and competitive markets' and also stresses that it may

not serve as ‘a basis for the introduction by the Community of any measure which could lead to a distortion of competition’. It can therefore be argued that industrial policy measures leading to results inconsistent with competition rules would be invalid under the EC Treaty.(Bourgeois & Demaret, 1995, pp. 68-69)

According to this argument the European Airbus corporation and the Ariane rocket project would be invalid. In the case of Airbus, states used aggressive strategies to obtain financing through a system of reimbursable advances, protectionism, and commercial promotion of national aeronautical industries, with the stated aim of breaking Boeing’s hegemony not by market techniques but by political will.(Cohen, 1996, p. 143)

Airbus and Ariane, the only two European ‘champions’ were a political creation by the governments concerned, they could not have been established under the EU’s competition policy.

It is astonishing that with the present (July 2005) economic and political difficulties with some 20 million unemployees, competition policy seems to sail along without any noticeable change of course. The economic purists, trying to create the ideal “level playing field” are still creating havoc. Mergers are still being approved, regardless whether thousands of employees are laid off. And Europeans are worried about their jobs. Due to the magnitude of the lay-offs people take note of them, even if it actually happens in Germany and the spectator is, say in Portugal. It is no wonder that the EU’s claim to provide for employment is suffering.

I consider that Member States might find that under the present economic conditions of stagnating economies and high unemployment, decisive action like that used with Airbus is justified and should be used aggressively and more widely. As a result Competition policy, and especially Merger policy should be relegated to a minor role, or at least as part of the merger approval the Commission should make it a requirement that jobs be protected for say, two years.

It is doubtless that during the next twelve months things will continue to change and develop. Due to the fierce struggle between the open market “Anglo-American” policy

and the more protective “continental” economic policies, together with the enhanced prestige of the Member States due to the collapse of the Constitutional procedures, an easing of the competition rules can be envisaged.

### **Notes.**

( 1 ) The new policy areas were environment, research and technological development, and ‘economic and social cohesion’. The SEA changed administrative and voting procedures, but overall the SEA provided a major boost to the European integration process.(Nugent, 2003, pp. 58-59, Cini, 2002).

( 2 ) For the first 3 months of 2004 the Commission ruled on the following merger cases, based mainly on the aspect of “concentration and dominant position” in (Commission Regulation 447/98). It is interesting how often the Commission insisted on ‘divestments’ of some assets in the merging companies. (EU Competition Policy 2004)

Alcan/Pechiney: Permission was given for the Canadian Alu company to buy the French Pechiney Group, but both companies were required to divest considerable parts of their activities.

BAT/Tabacchi Italiani: British American Tobacco requested permission to purchase the Italian tobacco giant. Upon request by the Italian competition authority, the Commission decided to transfer it to them, as the dominant market position only affected one country. The merger was subsequently approved by the Italian authorities, case COMP/M3248 BAT/ETI, 23. 10. 2003.

ECS/Sibelga : The Belgian Competition Department requested transfer of the case to them as the dominant market position between the energy supplier and distributor was in the Brussels area only. The Commission concurred.

GE/AGFA: GE was given the go ahead to buy Agfa’s ‘non destructive testing’ technology. Approved under Article 6(2) of Council Regulation (EEC)No 4064/89, case No COMP/M3136 GE/AGFANDT.

GE/Instrumentarium: The US firm GE was given permission to buy the Finnish firm Instrumentarium, but considerable divestments had to be made. Approved under Regulation (EEC) No 4064/89, case No COMP/M3083.

Lagadere/Natexis/VUP. The Commission approved the merger in the French book market, but required the divestiture of a large component of the publishing houses.

Prisa/Polestar : The Spanish printing group Prisa and British media group Polestar were given permission to merge, but had to divest some activities.

SEB/Moulinex: Following a decision by the CFI which annulled a previous Commission decision allowing the merger of the two French appliance makers, it came to the conclusion that there were no negative impacts of the merger.

( 3 ) Practices prohibited under Article 81.

horizontal or vertical agreements that fix prices directly or indirectly;

agreements on conditions of sale;

agreements that partition market segments, concerning price reductions, for example, or seeking to prohibit, restrict or, on the contrary, promote imports or exports;

agreements of production or delivery quotas;

agreements on investments;

joint sales offices’ market-sharing agreements’

agreements conferring exclusive rights to public service contracts;  
agreements leading to discrimination against other trading parties;  
collective boycotts;  
voluntary restraints (agreements not to engage in certain types of competitive behaviour).

( 4 ) Anti-trust cases:

Carbon and graphite products. The Commission imposed fines of from 1 million to 43 million Euros on 5 companies for forming a cartel. Leniency notes were given for cooperation.

Gazprom/ENI. The Russian and Italian gas companies were found to have had a territorial restriction - Russian gas supply was to be limited to the north-east of Italy - and were forced to cease it.

Industrial copper tubes: The Commission found that European copper tube manufacturers had formed a cartel and fined them a total of 79 million Euros.

NLNG: The giant Nigerian liquefied gas supplier was found to have territorial restrictions with one European country and was required to cease it.

Organic peroxides. ( Used for plastic and chemical industries ) The Commission imposed fines of nearly 70 million Euros on a number of companies Europe-wide, for forming a cartel.

Sonatrach : The Algerian gas supplier informed the Commission that it would cease including territorial limitations in its contract.

Sorbates: A number of chemical companies were fined 138 million Euros for having formed a cartel for the distribution of sorbates, a preservative. Hoechst, being the largest and having been prosecuted before for similar actions was fined the largest amount 99 million Euros. All the companies received leniency rulings for having fully cooperated.

( 5 ) Some state aid cases..

Altmark: It was ruled that if a company carried out a public service, assistance could be arranged in such a way that the company did not gain a competitive advantage.

EDF : Electricity de France was found not to have to refund aid, as that aid did not discourage new actors in the energy field.

Netherlands: energy tax exemptions : The Netherlands introduced a tax that was supposed to reduce energy consumption, the requested tax waiver was considered to be state aid, it was allowed for a limited period.

Netherlands: non-profit harbors: The Commission decided that assistance to such harbors did not reflect a commercial advantage.

Public service broadcasting : The commission ruled that state aid to public broadcasters is allowable under certain conditions.

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## **THE COMMON AGRICULTURAL POLICY. (CAP)**

Shortly after its conception and implementation in the 1960s, agriculture in the EU has become a constant subject of controversy and dissension. The main reason for this was the fact that some ten years after the implementation of the CAP the shortages in wheat, corn, barley, beef, milk etc. had been overcome, but by this time the larger producers of these items managed to 'hijack' the system. Despite the ever-increasing surpluses the agricultural lobbies, under the influence of the large producers maintained their dominant position. And the costs of buying and storing the surpluses continued. But this was not the only problem area.

*The many areas which raised the EU citizens' ire were:*

The continued support for the production of surpluses and its hugely expensive storage and disposal expenses.

The unequal payments to larger producers, while the smaller farmers largely missed out.

The lack of support for other products to those listed above, namely fruits, vegetables and pigs.

Support for farmers in less developed or inhospitable areas to ensure that the population remained on the land, this raised the comment that the money should have been spent on more 'worthy' targets.

The huge usage of fertilizers and pesticides.

The cost of agricultural products to the consumer.

Farmers complained about the difficulties and time-consuming effort required to claim support.

Member States complained about the large number of staff required to administer the scheme.

For these reasons it is surprising that the agricultural lobby and the Member States kept up the support for this policy. The UK's Prime Minister's challenge to this set-up in June 2005 is therefore no surprise. These matters and more will be in detail handled further on.

In this chapter the reasons for the establishment of the CAP, its introduction and gradual development over 45 years will be examined. It is proposed to arrange this work in the following sub-chapters to allow assessment of the CAP's impact on the Member States.

1. Historical Background.
2. Introduction of CAP.
3. Early Procedures and requirements.
4. Commencement of Reforms: the introduction of Supply-control mechanisms.
5. The MacSharry Reform Program of 1992.
6. Agenda 2000 Reforms.

7. 2004 Reforms
8. New Member States' Entitlements.
9. The Empowerment of Social and Environmental Groups.
10. Conclusion.

Agricultural policy has for a long time been one of the most important features of the EEC. It has been created as part of the Treaty of the EEC in 1958. Already then there were difficulties experienced as each of the original six members had different social, historical and economic experiences and requirements, produced different crops, and showed different levels of agricultural development. The need for compromise has therefore been created as part of the CAP, and this became more essential when new members joined the EEC.

During the 1960s agriculture had a great impact on the economies and the political life of the Member States. Some 20% of the labour force was engaged in agriculture and the various farmers' associations presented powerful lobby groups. The French and German governments especially did not want to antagonize their farmers as they needed their political support.

The CAP benefits each country in different ways. Those that export food surpluses gain, while importers lose out and become net contributors. The CAP has markedly uncommon impacts on member countries. The key to whether they gain or lose is their trade balance in the products the CAP protects. This is clearly demonstrated by the figures given in the schedule below, although it should be noted that they are for structural assistance only and not for price support:

**Receipts by Member States under the Guidance Policy of the CAP.**

<b>Member State</b>	<b>1989 Mio. ECU</b>	<b>1990 Mio. ECU</b>	<b>1992 Mio. ECU</b>
Belgium	31.6	23.1	28.2
Denmark	17.2	16.9	23.5
Germany	133.0	204.1	253.8
Greece	235.3	270.2	392.2
Spain	203.9	301.8	633.6

France	179.8	383.8	554.3
Ireland	121.9	125.0	194.5
Italy	263.6	282.7	375.9
Luxembourg	3.6	4.6	6.3
Netherlands	20.7	11.4	21.9
Portugal	179.4	241.6	289.8
UK	78.0	102.8	100.8

(Marsh, 1997, pp. 401-437)

The operation of the CAP is highly complicated and requires a huge administrative establishment. But this is provided by the Member States and at their cost. The Commission's staff number is relatively small.

The nature of the program led to the early commencement of reviews and hesitant changes in procedures of the CAP, this and especially the exciting changes in 2004 will be treated in separate chapters below.

### **Historical Background.**

During the difficult post-war years the European states tried to combat the many problems such as food shortages, unemployment, low productivity and shortage of foreign currency, by protecting their own markets by the raising of protective tariffs. They all attempted to keep imports out while trying to earn foreign exchange by exporting. (1)

With considerable compromises by all parties the ECSC (European Coal and Steel Community) was founded in 1952. The idea being the creation of a Common Market, albeit only in the coal, steel and related sectors. Supplies were to be ensured through the removal of quotas and customs duties.

The success of the ECSC led then to the creation of the European Economic Community (EEC) in 1958. Belgium, Netherlands, Luxembourg, Germany, France and Italy agreed to create a common market by removing all interstate tariffs. Part of the Treaty was the Common Agricultural Policy. France considered that Germany would benefit more than she from the industrial opportunities and thus insisted on the

adoption of the CAP as this would give her considerable advantages. France also gained a considerable advantage by the inclusion of all its overseas territories in the EEC and thus gaining the benefits of considerable financial support and protection under the CAP.

It should be noted that at this stage the Treaty did not specify the highly regulated and protectionist policy which the CAP became. (Bulmer, 2001, pp. 12-14)

### **Introduction of the CAP.**

In the early 1960s the six Member States were still net importers of cereals and oilseeds and were barely self-sufficient in livestock products. So a productivist emphasis of the founding member countries was understandable. Article 39 of the Treaty of Rome set out a number of objectives of the CAP, including ensuring supplies to consumers at reasonable prices, but until the mid-1980s the emphasis was “to increase agricultural productivity by promoting technical progress” and “to ensure a fair standard of living for the agricultural community”. This was achieved by adopting import tariffs, which were an effective means of raising agricultural prices. With this background of external protection the movement to a common external tariff (CET) for agriculture became possible.

It should be noted that for agriculture, instead of fixed tariffs, the EEC adopted a variable import levy or tariff system. (Coleman, 2001, p. 98)

### **Early Procedures and Requirements.**

Article 39 of the Treaty of the EEC outlined the CAP’s general objectives:

increase agricultural productivity
ensure a fair standard of living for farmers
stabilize agricultural markets
guarantee regular supplies of food
ensure reasonable prices for consumers

To ensure these objectives were achieved it was necessary to have intense negotiations for some five years. By January 1962 a package was agreed to which provided for a

common system of price support covering 85 percent of total EC agricultural production, a framework to raise levies on imports into the Community, and the establishment of the European Agricultural Guarantee and Guidance Fund (EAGGF) to underwrite the entire operation.

A further five years, to 1967, were required to achieve agreement on establishing a fixed price for wheat and feed grains throughout the Community. This resulted in a rise of the price for French farmers and a reduction in nominal prices for German farmers and was considered by them to be a “national disaster”.

From its implementation in the late 1960s, the CAP operated through instruments and mechanisms that varied from commodity to commodity but generally included: guaranteed prices, with the Community purchasing surplus produce; quotas, levies, and tariffs on imports to prevent external supplies from undercutting Community produce; and support for Community exports, mainly by refunds, to allow them to compete on world markets.

*This produced the following problems:*

The guaranteed prices bore no relation to demand and encouraged overproduction.

Surplus produce had to be stored in “intervention”, at additional cost to Community taxpayers.

Big farmers produced more and thereby earned more money, whereas small farmers, who most needed assistance, earned less.

In order to produce more on their already overworked land, farmers used more herbicides, pesticides, and artificial fertilizers, thus accentuating the Community’s acute environmental problems.

(Dinan, 1994, pp. 325-328)

Prior to the reforms of the 1990s, agriculture was a highly distinctive policy-making sphere in the EU. This was mainly because many key decisions were made as part of a regular, and usually highly complicated, process: the annual price review. Many non-price elements were swept up in the reviews and became components of what

customarily were highly complex and interconnected packages by the time final agreements were made. The core of the packages usually consisted of a range of price increases, adjustments to produce regimes, and statements of intent about future actions. (Nugent, 2003, p. 400)

The CAP's price support policy induced farmers to increase their supply, irrespective of market demand, which under this sort of policy is irrelevant. A consequence of this is that higher support prices benefit disproportionately the large producers who realize economies of scale and in general are not those in dire need of better living standards. **It is estimated that 80% of the CAP support accrues to the richest 20% of the farmers.** These are the large producers of output which takes up the largest share of CAP expenditure. Their output consists of products in excess supply which the Community accumulates in 'mountains of surpluses'. (Hitiris, 2003, p.170) By 1980 the CAP represented 73% of the EU budget. It is the cost of agricultural surplus management which dominated the budgetary expenditure of the EAGGF. Export restitution alone regularly accounts for over 30% of total EAGGF cost, with the bulk of the 'other expenditure' being on costs for surplus storage and subsidized market disposal within the EU. (Colman, 2001, pp. 101-2)

#### **Commencement of Reforms: the introduction of Supply-control mechanisms.**

Throughout the existence of the CAP, its policy instruments and regulations have been adapted to meet changing economic and political circumstances. For example, during the 1970s, in response to the growing surpluses of some commodities, the EU introduced several new measures to the CAP designed to encourage domestic consumption; including subsidies to certain categories of final consumers, subsidies to industrial users of food products, and even 'denaturing premiums' (whereby product was dyed and in other ways made unfit for human consumption) to encourage the use of grain in livestock feed. Attempts to decrease budgetary cost were also made by limiting the period of 'intervention buying', by raising the quality standards for acceptance and by reducing the price paid for such buying. However, these ad hoc

measures did nothing substantial to alleviate the mounting pressures for more radical reform of the CAP. (Colman, 2001, p. 108)

Significant changes were implemented in the dairy industry. In 1981 the EU introduced a system of 'maximum guaranteed thresholds' which, should milk deliveries in any year exceed the quantitative threshold, would trigger action to offset the additional costs of the regime caused by excess production. (2)

### **The MacSharry Reform Program of 1992.**

The above mentioned budget-inspired reforms proved ineffective, and in the meantime pressures for further reforms were mounting due to:

- the EU decision to complete the single market by 1992;
- the GATT Uruguay Round for trade liberalization.

A far-reaching restructuring of EU agricultural policy was therefore undertaken in 1992. The EU reforms aimed to slash overproduction by reducing the guaranteed prices by up to 30 % and switching the CAP policy from *price support* to *compensatory payments* in the form of direct income supplements linked to farm size and average yields. To qualify for these payments arable farmers of all but the smallest holdings were compelled to *set aside* 15 % of their land and with the help of generous grants to turn land over to forestry and ecological or recreational uses ensuring protection of the environment and natural resources. The agreement aimed to bring CAP prices closer in line with world levels so that export subsidies would fall, thus reducing the CAP distortions in international trade and increasing market access for third-country producers. Guaranteed prices and Community preferences continued, though at a lower level, but the Community agreed to change protection from variable levies to fixed tariffs, thus re-establishing a link between EU prices and world market prices. These changes reduced price support and lowered consumer prices by shifting the burden from the consumers to taxpayers with direct payments from the EU budget.

For the first time they also included environmental considerations, by linking payments of farm support to compliance with some pre-agreed environmental improvements. Moreover, since environmental payments, afforestation and structural measures in agriculture are all targeted actions, responsibility for their implementation was moved from the Commission to local authorities with the costs shared equally by the Member States and the CAP budget. (Hitiris, 2003, p. 177)

By 1994 about 190 agri-environment programs had been approved, 12 of them were national and 165 were regional. These changes emphasize the long-recognized role of the CAP in securing environmental goals. This was strengthened by the 1993 Treaty on the European Union (TEU) which requires that all Union policies, including the CAP, take environmental impacts into account.

The schedule below shows the main points of the MacSharry CAP reforms.

Commodity	Cuts in support	Compensation and other gains	Production control
Cereals	<ul style="list-style-type: none"> <li>Target price cut by 29 % from 91/92 buying-in price.</li> <li>Price reduction phased in over three years.</li> </ul>	<ul style="list-style-type: none"> <li>Per hectare compensation - payments available provided set-aside is implemented.</li> <li>Producers of less than 92 tonnes of cereals are exempt from set-aside.</li> <li>Compensation payments based on historical yield levels for regions of the EU.</li> <li>Co-responsibility levy abolished from 92/93.</li> </ul>	<ul style="list-style-type: none"> <li>Annual set-aside required for producers to receive compensation payments.</li> <li>The minimum % of base arable area to be set aside varies from year to year.</li> <li>Controls over which land can be set aside.</li> </ul>
Oilseeds and pulses	<ul style="list-style-type: none"> <li>No price support 93/94 onwards.</li> </ul>	<ul style="list-style-type: none"> <li>Per hectare area payments available but cut from 92/93 levels.</li> <li>Linseed added to list of eligible crops.</li> </ul>	<ul style="list-style-type: none"> <li>Controlled by same set-aside schemes as cereal production.</li> </ul>
Sheep	<ul style="list-style-type: none"> <li>Payment of ewe premium restricted by producer quota.</li> <li>Producer quotas based on number of ewe premiums paid in 91.</li> </ul>	<ul style="list-style-type: none"> <li>Quota has market value.</li> <li>Special extensification premiums for reduced stock levels.</li> <li>Lower feed grain costs.</li> </ul>	<ul style="list-style-type: none"> <li>If quota sold without land 15% of quota taxed to national reserve.</li> <li>No transfer of quota outside existing Less Favoured Areas.</li> </ul>
Beef	<ul style="list-style-type: none"> <li>Intervention price cut</li> </ul>	<ul style="list-style-type: none"> <li>Beef and suckler cow</li> </ul>	<ul style="list-style-type: none"> <li>Beef premium</li> </ul>

	<ul style="list-style-type: none"> <li>by 15% from 93/94.</li> <li>350,000 tonnes limit set on intervention purchases from 1997.</li> </ul>	<ul style="list-style-type: none"> <li>premium increased but made contingent on stocking rates below minimum level.</li> <li>Suckler cow quota has marketable value.</li> <li>Lower feed grain costs.</li> </ul>	<ul style="list-style-type: none"> <li>limited by regional ceiling equal to number of premiums paid in 1991. If exceeded producer payments reduced pro rata.</li> <li>Suckler cow premiums restricted by producer quota.</li> <li>Beef and suckler cow premium payments subject to stocking-rate restrictions.</li> </ul>
Dairy	<ul style="list-style-type: none"> <li>5% cut in butter intervention price by 94/95.</li> </ul>	<ul style="list-style-type: none"> <li>Milk quota and associated value to last at least to 2000.</li> <li>Co-responsibility levy abolished from 92/93.</li> </ul>	<ul style="list-style-type: none"> <li>Cuts in quota may be made.</li> </ul>

(Colman, 2001, pp. 112-113)

### Agenda 2000 Reforms.

The MacSharry reforms were basically allowed to run to 1999 when further reforms became necessary. They were required for ‘deepening and extending the 1992 reform through further shifts from support to direct payments and developing a coherent rural policy’ (Commission 1997) and *were induced for four main reasons:*

budgetary constraints caused by the closer link of budgetary revenues and GNP;  
the difficulties of extending the current CAP into central and eastern European countries after EU enlargement;  
EU commitments under the World Trade Organization (WTO) agreements regarding export subsidies and the forthcoming start of further trade liberalization talks;  
the reform of the EU structural funds which included the funds financing CAP expenditures. (Hitiris, 2003, p. 182)

The reforms adopted introduced further direct payments and cuts in support prices. For example:

Arable crops: The intervention price was reduced by 20 % in 2000.

Beef: The market support level has been reduced by 30 % in three equal steps starting in 2000 while from 2002 the intervention system was replaced by a private storage regime. Direct payments have been substantially increased, for example for bulls it was increased to 310 ECU per head (+130%), this figure includes a contribution by the Member States which has a certain flexibility. There are regional ceilings which limit total cattle numbers.

Dairy Regime: The intervention price for butter and skimmed milk was reduced by 15 %.

Further measures introduced were:

- *Cross compliance*: With respect to integrating better the environment into the CAP, Member States should apply appropriate environmental measures concerning the particular market support schemes.
- *Modulation*: The distribution of direct payments among farmers might cause specific problems within certain Member States which call for a subsidiarity approach. Member States were therefore authorized to modulate direct payment per farm within certain limits and relative to employment on the farm.
- Funds made available from aid reductions - either under cross-compliance or modulation remains available for the respective Member State as an additional Community support for agri-environmental measures.
- Ceilings on aid payments: Payments to individual farmers have been reduced by 20 % for payments between ECU 100,000 and ECU 200,000 and 25 % reduction on amounts above ECU 200,000. (Agenda 2000, March 18th. 1998)

The above changes led to a reduction of the CAP's share of the EU budget from 73 per cent in 1982 to below 50 %. The problems of production surpluses have also largely been brought under control.

*Agenda 2000 may be seen as representing a step towards reducing central EU funding (and collective financial responsibility) for agricultural support, and a move towards re-nationalizing agricultural policy. (Colman, 2000, p. 119)*

## **2004 Reforms and new Member States' Entitlements.**

The Agenda 2000 reforms did ease the financial pressure of the CAP and also led to a control of the surpluses. However, they clearly were not enough to allow for:

- 1) The extension of the CAP to the ten new Member States
- 2) Comply with the desires of agricultural exporting countries and thus allow for successful negotiations at the WTO.

On 26 June 2003, the EU farm ministers adopted therefore a fundamental reform of the CAP. The Commission claimed that this reform would completely change the way the EU supports its farm sector.

*The new CAP would be geared towards consumers and taxpayers, while giving EU farmers the freedom to produce what the market wants.*

In future, the vast majority of subsidies will be paid independently from the volume of production. To avoid abandonment of production, Member States may choose to maintain a limited link between subsidy and production under well defined conditions and within clear limits. These reforms were to be implemented over 2004 and 2005. The main elements of the reformed CAP are:

- A 'single farm payment' for EU farmers, independent from production, but based on historical production data; limited coupled elements may be retained to avoid abandonment of production.
- This payment will be linked to the respect of environmental, food safety, animal and plant health and animal welfare standards, as well as the requirement to keep all farmland in good agricultural and environmental condition ( 'cross-compliance').
- A strengthened rural development policy with more EU money, new measures to promote the environment, quality and animal welfare and to help farmers to meet EU production standards starting in 2005.
- A reduction in direct payments (modulation) for bigger farms to finance the new rural development policy.

- A mechanism for financial discipline to ensure that farm budget fixed until 2013 is not overshot.
- Revisions to the market policy of the CAP:
  - ◊ Asymmetric price cuts in the milk sector: The intervention price for butter will be reduced by 25 % over four years ( an additional 10 % over the Agenda 2000).
  - ◊ Reduction of the monthly increments in the cereals sector by half.
  - ◊ Reforms in the rice, durum wheat, nuts, starch potatoes and dried fodder sectors.
 (EU CAP reform - a long-term perspective for sustainable agriculture, 26. 6. 2003)

Legislation has now been adopted to ensure that the EU's budget discipline is maintained. These rules cover in particular the fixing of the amounts available annually for the EAGF expenditure, forecasts relating to the payment deadlines imposed on the Member States, reductions and suspensions of payments.

To meet the vastly increased demand for agricultural development to satisfy the EU standards, especially in the new Member States, the European Agricultural Guarantee and Guidance Fund is being closed and two new funds are set up, they are:

*a European Agricultural Guarantee Fund (EAGF)*

and

*a European Agricultural Fund for Rural Development (EAFRD)*

(Proposed Council Regulation on the financing of the CAP, 14. 7. 2004, COM(2004)489 final, 2004/0164 (CNS))

### **Applying the CAP in new Member States.**

After the collapse of Communism in 1989 most of the previously nationalized agricultural properties were handed back to their former owners ( in Poland and Slovenia most farms had not been nationalized ), but generally, the farms were underdeveloped and the private farmers lacked capital to modernize the properties. But already in 1991 the European Bank for Reconstruction and Development was established, its task was to foster the transition towards open market oriented

economies and to promote private initiative in the CEECs. In addition, some 3,120 billion Euros were provided annually to the CEECs in pre-accession aid since 2000.

For agricultural development in the new Member States some 520 million Euros per year were provided under the “Special Accession Programme for Agricultural and Rural Development (SAPARD) which helped them to deal with the structural adjustments in their agricultural sectors and rural areas. (Hitiris, 2003, p. 213; Tondl, 2001, p. 186)

With the accession to the EU on 1st. May 2004 it is important to stress that, in general, the new Member States will apply the agricultural elements of the *acquis communautaire*. Despite the progress toward alignment with the EU-15 that has already taken place over recent years, some of the CAP’s mechanisms will not apply immediately. This is partly because the new Member States and farmers need time to establish and adapt to the necessary administrative procedures, and partly because the continuing disparities in farm prices, structures and food industries mean that immediate implementation of the CAP as a whole could have provoked sudden disturbances and chaos.

Consequently, there are some policy areas where full application will come in over time, most notably, direct payment to farmers will be phased in over 10 years (starting at 25 % of the EU level in 2004). Incidentally, this was strongly resented by Poland, it was claimed that this would make them second class citizens, however, the EU Agriculture Commissioner has advised in her newsletter No. 111 of 18.1.2005 that the income of the Polish farmers has increased by 74 % over the last year, while the EU-15 increase was only some 6%. It should be noted that the new Member States have the possibility of “topping up” the actual direct aid payment rate in the first three years of EU membership to 55 %, 60 % and 65 % respectively of EU-15 levels, if the Member States decide to use the topping up option to the full.

Due to the less-developed situation of agriculture and rural areas in the new Member States the CAP is providing an enhanced rural development strategy for the new

Member States which is specifically adapted to their requirements and which is more favourable than those applying to the EU-15. The amount available for EU funding for rural development from the EAGGF Guarantee Fund for the new Member States has been set at Euros 5,76 billion for 2004-2006. An additional 2 billion Euros has been allocated from the EAGGD Guidance Fund for rural development measures. A wide range of rural development measures is being co-financed by the EU at a maximum rate of 80 % (and 85 % for agri-environment and animal welfare measures). (Commission's communication of April 2004, p. 9)

*Single Area Payment Scheme (SAPS).*

Special arrangements have been granted to the new Member States which do not apply to the EU-15. It was considered that:

- The new Member States had little experience of complex farmer support schemes.
- Given the short time between conclusion of the accession negotiations and the accession itself it was difficult for national administrations to set up the necessary control systems for the standard EU schemes.
- The new single farm payment (see above) posed problems for the new Member States as it was not possible to calculate payment entitlements for their farmers on the basis of the same historical reference period as used in the EU-15 (2000-2002).

For these reasons the EU offered the new Member States the option of operating a simplified system of direct payments - the Single Area Payment Scheme (SAPS).

SAPS involves payment of a uniform amount per hectare of agricultural land. The level of the per hectare payment is being calculated by dividing the national financial envelope by the utilized agricultural area. Farmers in the new Member States that apply the SAPS system have no obligation to produce, but they must keep the land in good agricultural and environmental condition. SAPS is simpler to administer than the single farm payment or the standard direct payments used in the EU-15 as less information is required from the farmer ( no information is needed on the use of the land, number of animals etc.). The new CAP reform rules on cross-compliance are optional under SAPS.

SAPS is an option for five years, then the new Member States must opt for the scheme in force in the EU at the time.

Malta and Slovenia are the only new Member States that have chosen to apply CAP as it is applied in the EU-15. All others have opted for the simpler SAPS. (Commission's communication of April 2004, p.16)

*Special transitional arrangements have been negotiated for a number of new Member States to assist sensitive sectors to adapt gradually to the EU acquis, for example:*

Different quality criteria for cereals aid.
Special import quota for sugar.
Specific vine planting rights.
Extra time to meet EU livestock density requirements.
Temporary maintenance of national laws on land acquisition.
One year transition period for the allocation of milk quotas.

*In addition to the existing measures in EU-15 rural development programmes, new measures are available in the new Member States, footnote ( 3 ) refers.*

### **The Empowering of Social and Environmental Groups.**

Farmers in Europe have had for a long time a powerful influence in the national governments, and with the inception of the EU this influence was extended to Brussels. National ministers have a powerful impact in the (Agriculture) Council of Ministers, while national officials work in the Council working groups, Regulatory Committees and Management Committees. Agricultural experts and members of the civil society only are forming the Advisory Committees.

But this appeared not to be enough for the various agricultural bodies. They found it necessary/desirable to establish representative offices in Brussels. At this stage there are some 130 offices representing various agricultural interests. Due to the often technical nature of agricultural business and the overwhelming organizational capabilities of the farming lobby, other organizations made little headway against them.

This started to change in the 1990s when environmental degradation and animal health concerns became matters of concern. To overcome this the Commission started to actively encourage the participation of other groups and organizations. See above, where the Commission had approved over 165 agri-environment programs at the regional level. The Commission is also widely canvassing animal health, environmental and social organizations for input in new regulations. All agricultural legislation is now also submitted to the Committee of the Regions and the European Economic and Social Committee. Clearly, the emphasis has now changed from the once all powerful agricultural lobby groups to the consumer.

### **Conclusion.**

*Many of the Common Agricultural Policy's aims have been achieved during the last forty years, for example:*

Adequate food supply has been achieved.

Farm output has greatly increased.

Farmers' incomes have been increased in line with industrial income.

Early retirement of farmers has been facilitated.

Many smaller farms have been rationalized and modernized.

Huge amounts of money have been poured into lesser developed regions.

Population in some less favoured areas has been maintained.

*Negative aspects of the CAP that remain to be solved are:*

The huge financial benefits that accrued to large producers of temperate crops.

Degradation of the environment through the use of excessive quantities of fertilizers, pesticides and herbicides.

Destruction of natural habitats through the removal of hedges, wetlands etc.

The complicated procedures established to control the CAP and its susceptibility to fraud.

The CAP, as so many other initiatives of the EU, is a child of compromise and changes are difficult to make due to the need for compensating measures. Fortunately,

when the situation becomes serious, such as the financial demands outstrip the funds available, or, as recently, the huge enlargement to the CEECs, the EU and the Member States are prepared to act. Indications are that the EU is already tackling the above negative aspects. This was the situation until June 2005 when the British Prime Minister Blair threw into turmoil the whole financial arrangement for agriculture, which had already in 2003 been agreed to for the period 2007-2013. Beneficiaries of agricultural support payments were of course most upset about this, notably French President Chirac.

The EU has ‘de-coupled’ payment of assistance to farmers from actual production, it has substantially increased the payments per hectare to smaller farmers and reduced payment to the larger holdings by 25 per cent. But this still is not sufficient, the larger agricultural enterprises still receive the major part of the support. French farmers are especially irritated that HM the Queen receives an annual average of 800,000 Euros for her estates, while Prince Charles receives some 500,000 Euros. Here is an interesting detail, when reports are made about agricultural negotiations, the “French agricultural lobby” is always presented as a monolithic block of firm supporters. Unfortunately, for many smaller French farmers the CAP is more or less useless. (4)

The reductions of aid for larger agri-businesses will eventually weaken the agricultural lobby groups, as the smaller farmers, who still are the largest number in Europe, will gladly accept the larger contributions, while the larger farmers will withhold their financial contributions to the lobby groups as they can’t expect any benefit from supporting them. Thus, other groups, such as consumers, environmentalists or civil society generally, will be able to demonstrate effective opposition and will be able to break the agricultural stranglehold on national governments and the EU.

Degradation of the environment is now actively combated. Payment to farmers is only made if pre-arranged environmental measures are met. Farmers can get the highest assistance by using agri-environmental procedures. Farmland is now to be left idle, being farmed in a way that benefits nature, or is converted to forests. The use of

fertilizers and pesticides is now also discouraged, it was ascertained that in 2002, farmers in the EU used 2.5 times as much fertilizers per hectare than the American farmers did. This policy will also stop or reverse the destruction of natural habitats.

As mentioned before, many of the EU's procedures are complicated and require considerable input and staff to administer them. Some successful action has already been taken to remedy this, see the above mentioned "Single Farm Payments" in the EU-15, but even they are still rather complicated as they are based on historical data and perhaps a "Single Area Payment Scheme" as was granted to eight of the new Member States may be more appropriate. As the SAPS is based on the whole Member State's acreage and all farmers get the same financial support per acre, it will be much simpler to eventually reduce such payments. On the other hand the EU is now trying to reduce EU funding by allowing the Member States to increase their subsidies within certain limits. As previously mentioned, EU agricultural policy is now gradually being re-nationalized. In future the EU will be more the monitor and not the financier. The national governments have consistently paid much more in subsidies for their farmers than has the EU.

The annual budget for the CAP is some 45 billion Euros, this amount appears to be tremendous, however, it represents only about a half percent of the EU's GDP. Of this some 3 billion Euros per year were lost due to frauds, but in 2003 this amount has been reduced to 170 million Euros. This was the result of new procedures and stricter scrutiny of claims. Farmers have complained that in order to get their entitlements it is now necessary to engage expert consultants, as it was impossible for an ordinary farmer to provide the details required. Smaller farmers will be further discouraged and simply forgo the subsidies. Larger entities of course can afford all the expert assistance they need.

It is astounding that the EU managed through this small amount to control agriculture in all the Member States. If it is considered that in the 1960s agricultural employment in most states was around 20 per cent, it is no wonder that national governments were willing to delegate responsibility for agriculture to a central body. None of the

national governments could have taken on the powerful agricultural organizations, which did not hesitate to use violence in order to obtain their 'rights'. In France there were even some fatalities in farmers' demonstrations. National governments found it convenient to blame "the Brussels bureaucracy" for any necessary decision which they themselves would have been loath to make. The national governments could never have achieved this development on their own.

There is a little known aspect of European agriculture, there are some 325,00 sugar beet growers, most of them in France, Germany and Poland. As a result of the subsidies sugar price in the EU is about four times higher than the global market rate. Import tariffs protect this market and Brussels pays out export subsidies to get millions of tons of sugar a year of its market.

The Commission has now proposed to cut 39 per cent of the subsidies, which may be necessary, but this shows again the sometimes lack of flexibility. If this reduction would be implemented over say 5 years, there would hardly be any complaint. The drastic reduction resulted in some 6,000 farmers demonstrating in Brussels. They claim that the proposal would cost each European sugar grower the equivalent of 6,500 Euros potential income, close over 80 sugar factories and destroy some 150,000 jobs.

The farmers were supported by representatives of some of 70 or so poor Caribbean, African and Pacific countries which have preferential trading agreements with the EU and which would lose their access to this lucrative market.

The main beneficiaries of this change would be Brazil, Australia and Thailand. (Canadian Press, 19. 7. 2005)

The EU is now planing to reform its sugar market, which should be in effect by next year. The Agriculture Commissioner Mariann Fischer Boel stated that under this reform there will be no exports- the EU will just be consumers. To achieve this the current subsidy per ton of sugar, 631,90 euros, which is three times the price on the world market, will be reduced by 39 per cent to help eliminate surplus production. It

should be noted that this price is payable only for certain quotas, any sugar produced beyond these quotas is called “C” sugar which was exported on to the world market without a refund from the EU. In 2004-2005 the EU produced and exported 2,557,520 tons of this “C” sugar without any refund. The Commission is now considering reclassifying another 2,5 million tons of EU sugar to “C” class and throw it onto the world market. The World Trade Organization (WTO) declared that export of this non-quota sugar violates trade rules and must be ended. It appears that the EU has another twelve months to adapt to the new rules. Up to now the EU also exported 1,273 million tons annually of *subsidized* sugar under an agreement with the predecessor of the WTO.

The EU’s generous attitude towards poorer countries can also become problematic. The EU signed the “Everything But Arms” agreement with the world’s 50 least-developed countries which allows them to export sugar to the EU free of any tariff or quota. The EU is already paying attention to ‘country of origin’ to ensure that no ‘triangular trade’ happens. (5)

To summarize, the CAP has affected every European, the farmers by ensuring their standard of living kept rising, and all the citizens through the high prices they had to pay for essential food supplies, but they also had secure food supplies. Overall it is considered that the CAP’s impact was mostly beneficial. Unfortunately the average EU citizen does not perceive the positive results. Negative reports are as always much more powerful than positive ones.

In the CEECs the CAP is ensuring farmers’ prosperity, especially for those semi-subsistence farms. The most recent reports indicate that the policy is working.

Finally, the EU has advised that further reforms would be carried out in several areas in the near future - the rice, durum wheat, nuts, potatoes and dried fodder sectors. Will the current financial upheaval accelerate re-nationalization of agricultural subsidies, and will the EU simply become a ‘supervisor’, or will the EU maintain its all-

embracing impact with its much-maligned CAP? The next few years promise to be exciting.

### **Notes.**

( 1 ) The Americans saw the futility of this system and encouraged the opening of the European borders and the opening of markets as part of their “Marshall Plan - European Recovery Program” in 1948. With limited success. However, the idea had been planted.

Negotiations continued especially between Germany and its occupying powers, the USA, UK and France. The main points of discussion were the security needs of France and Germany’s re-incorporation in the European trading system.

( 2 ) However, again, this proved insufficient and in 1984 ‘marketing quotas’ were introduced. A ‘super-levy’ was charged on excess deliveries beyond the quota. This had the effect that the cost to the CAP for the milk industry fell from 29.7% of EAGGF expenditure in 1984 to 18.2% in 1992. (Colman, 2001, p. 109)

( 3 ) Income support for semi-subsistence farmers undergoing restructuring.

Setting-up of producer groups.

Support for meeting EU standards with an additional derogation for new Member States to finance investments.

Technical assistance.

Topping-up direct payments.

Leader+ type activities, in particular capacity building at local level.

The provision of extension and advisory services.

(Commission’s communication of April 2004, pp. 17-18)

( 4 ) Thomas Fuller (IHT, 1. 7. 2005) reports that a French vegetable farmer with a greenhouse ‘the size of two football fields’ receives not a single cent of aid. While a dairy farmer with 40 cows received aid of 13,595 Euros last year, a large part of his net income of 21,960 Euros. Most of the ‘aid’ goes to prosperous, huge agricultural enterprises.

( 5 ) Such a case happened recently in the Western Balkan states when the EU granted them free access to the EU sugar market to help them recover from the devastations of war. Some Balkan states sent their entire national sugar production to EU markets to benefit from the high EU prices, while they were meeting their domestic sugar needs with imports, especially of cheaper cane sugar from Brazil. (Bloomberg, 12. 9. 2005) Surely, it could be expected that the EU could devise a system which would prevent such abuses.

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## **COMMON ENVIRONMENT POLICY (CEP)**

This is another topic which demonstrates the fragility of the EU and the surprising steps taken by the EU to make the environment the all-encompassing sector which it is now. And yet its importance is depending on the political climate that prevails at the moment. Now it is again being challenged by the economic imperative to create jobs.

This chapter will give a short historical outline, but will emphasize the more recent developments and especially the monumental changes that have occurred in 2004. It should be noted that the numbers given to the various titles in no way indicate any importance, they are simply given to indicate chronology and to facilitate oversight of the topic.

The following topics will be covered:

- 1) Original Treaty of Rome.
- 2) Early environmental programmes in the 1970s.
- 3) The Single European Act (SEA) 1987.
- 4) The Maastricht (1993) and Amsterdam (1997) Treaties.
- 5) 2000 Reforms.
- 6) 2004 Reforms.
- 7) The CEE enlargement.
- 8) The CEP's impact on Multi-level governance.
- 9) Conclusion.

### **1. The original Treaty of Rome.**

Article 2 of the 1957 Treaty of Rome defined the purpose of the European Economic Community as follows:

‘The Community shall have at its task, by establishing a common market and progressively approximating the economic policies of Member States, to promote throughout the Community a harmonious development of economic activities, a continuous and balanced expansion, an increase in stability, an accelerated raising of the standard of living and closer relations between the states belonging to it’.

Connelly and Smith (2003, p. 261) argue that *the primary role of the Community was not only economic in intention, but anti-environmental in practice* in the sense that it gave a clear priority to the promotion of economic growth. The environment was not mentioned.

## **2) Early environmental programmes in the 1970s.**

The lack of any provision of the environment in the treaty did not prevent the Community from passing environmental legislation. From the early 1970s environmental policy programmes were formulated and legislation was approved. The Commission used as its authority Articles 100 and 235 of the EEC Treaty. The former allowed the Community to issue directives for the approximation of laws ‘as directly affect the establishment or functioning of the common market’ and the latter enabled it to take ‘appropriate measures to ‘attain, in the course of the operation of the common market, one of the objectives of the Community’’. (Nugent, 2003, p. 296) This is considered to be a weak treaty base. It is surprising that none of the Member States challenged the Community’s using of the two Articles for environmental purposes.

By 1973 the EU had developed an environmental policy in the form of the ‘First Environmental Action Programme’. (1)

## **3) The Single European Act (SEA) 1987.**

The SEA was particularly important for European environmental policy making as it established for the first time the principle that environmental policy should be one of the direct concerns of the Community itself. It is one of the four policy areas - together with consumer protection, culture and health which are recognized as a

component in all EU policy making. A new Title VII was inserted in the treaty with the new articles 130 r-t, which introduced explicit powers for making environmental law.

But the SEA also introduced the principle of subsidiarity, that means that ‘The Community shall take action relating to the environment to the extent to which the objectives... can be attained better at Community level than at the level of the individual Member States’. This has resulted in the Member States being responsible for the introduction and monitoring of environmental legislation. (Connelly & Smith, 2003, p. 276)

#### **4) The Maastricht (1993) and Amsterdam (1997) Treaties.**

These two Treaties further strengthened the measures outlined under the SEA above. There are two key TEC articles in this respect:

1) Environmental protection requirements must be integrated into the definition and implementation of the Community policies and activities referred to in Article 3, in particular with a view to promoting sustainable development. (Article 6)

2) Community policy on the environment shall aim at a higher level of protection taking into account the diversity of situations in the various regions of the Community. It shall be based on the precautionary principle and on the principles that preventative action should be taken, that environmental damage should as a priority be rectified at source and that the polluter should pay. (Article 174 (2)) (Nugent, 2003, pp. 318-319)

#### **5) 2000 Reforms.**

Since environmental action began in the EU in 1972 every ‘Environmental Action Program’ (EAP) has resulted in various progressive changes, and yet these actions were not sufficient to prevent further degradation of the environment. The ‘Fifth EAP’ for the period 1992-2000 marked the beginning of a ‘horizontal’ Community approach

which would take account of all the causes of pollution - industry, energy, tourism, transport, agriculture etc.

The Community institutions are now obliged to take account of environmental considerations in all their other policies. This has now been taken into account in various Community acts, particularly in the fields of employment, energy, agriculture, development cooperation, single market, industry, fisheries, economic policy and transport.

The ‘Sixth EAP’ sets out the priorities for the Community up to 2010. Four areas are highlighted: climate change, nature and bio-diversity, environment and health, and the management of natural resources and waste. One innovation here is the ‘integrated product policy’. This aims to develop a more ecological product market by making products more environmentally sustainable throughout their life cycle. (EU 1, p. 1-2, 11. 12. 2001)

The EU has been able to expand the environmental instruments available as environmental policy has developed. In order to provide high level environmental protection and to guarantee the operation of the internal market a financial instrument (the LIFE programme) has been introduced, as well as the following technical instruments: eco-labelling, the Community system of environmental management and auditing, system for assessment of the effects of public and private projects on the environment, and the criteria applicable to environmental inspections in the Member States. (2)

During this time emphasis has been placed on diversifying environmental instruments and, in particular, on introducing environmental taxes (the “polluter pays” principle), environmental accounting and voluntary agreements. (EU 1, p. 2, 2001)

Numerous directives have been issued and adopted in regards to:

Waste management, Noise pollution, Water pollution, Air pollution, Nature conservation and Natural and technological hazards.
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(EU 1, pp. 3-5, 2001)

## 6) 2004 Reforms.

The 2004 reforms too are impressive in their overall reach into virtually every aspect of the Community. The most effective ones are in the *agricultural* and the *cohesion* policy. The former will have great impact as it will:

- ◆ reduce price support in favour of direct payments, which will enhance the economic performance of producers and lead to more balanced use of polluting inputs;
- ◆ enable Member States to ensure that direct payments are conditional on compliance with environmental requirements;
- ◆ lead to rural development programmes and access to environmental protection.

The latter, *cohesion policy* is being reformed by:

the introduction of systematic scrutiny of the environmental impact of projects over 50 million Euros;

the adoption of a degraded environment as one of the criteria for defining eligible urban areas within the new Objective 2 regions;

the integration of the environment as an objective for assistance from the Structural Funds in the framework of proposed new Structural Funds regulations;

the appraisal by the Commission of regional development plans as regards environmental protection;

the introduction of a partnership involving environmental bodies and non-governmental environmental organizations for the preparation of Cohesion Policy intervention programmes.

(EU 2, p. 2, 2004)

In the 2003 Environment Policy Review of 3. 12. 2003 the Commission asserted that further action and effort is required in order to meet commitments undertaken. (3)

But the new “*Greenhouse Gas Emission Allowance Trading Scheme*” will most likely be the most important development in the long run. Effective from the 1.

January 2005 any installation carrying out any activity in the: energy sector, iron and steel production and processing, the mineral industry, the wood pulp, paper and card industries is required to have a gas emission permit.

Each installation is allocated an 'allowance', based on previous years' emission. Allowance in this case means the entitlement to emit a tonne of carbon dioxide or an amount of any other greenhouse gas with an equivalent global warming potential. At least 95 % of the allowances for the initial three-year period are allocated to the installations free of charge. Each year, on 30 April at the latest, the Member States will make sure that the operators of the installations surrender the correct quantity of allowances commensurate with the total emissions over the previous year. The surrendered allowances are subsequently canceled.

Any operator failing to surrender the appropriate allowance will be fined 40 Euro for each tonne of carbon dioxide, after three years this amount rises to 100 Euros. Enterprises reducing their greenhouse gas emission below their allowance are entitled to sell this quantity. The total emission in the EU is some 5.6 billion tonnes of carbon dioxide. It has been estimated that by trading the allowances EU wide will result in annual savings of 1.3 billion Euros. This is a saving equivalent of some 35 % of the abatement costs if there were purely national abatements.

The Commission has indicated that the scheme could be extended to further sections after 2008, in that case the savings could be substantially higher. (EU 4, pp. 1-5; Marin, 2004, p. 300)

The Member States are responsible for the implementation of the scheme, the installations' registration, its operation and monitoring, they must also report the scheme's progress annually to the Commission. This will be a considerable task for the Member States.

## **7) The CEE enlargement.**

The accession of the eight CEE countries to the EU has brought tremendous problems and changes for their governments and citizens. It will be many years before they can fully comply with their commitments as per their *acquis communautaire*. However, it is not only the Member States that will have to change, but also the EU. For example the EU made rather one-sided comments, such as: “Today, the environment in the countries of CEE is in a very poor state” (EU 5, 2001, p. 5) - this fails to appreciate the huge and magnificent nature reserves and parks which had been established under the communist system. Nevertheless, there were huge environmental problems in urban and industrial areas due to air and water pollution and chemical contamination of industrial sites and army bases.(von Homeyer, 2004, p. 63)

There was a considerable reduction of pollution in the early 1990s which was due to an economic slowdown in the ‘socialist’ countries. (von Homeyer, 2004, p. 62) However, now with increasing economic activity there appears a tendency to invest more in production than the environment. Considerable assistance was provided by the EU for infrastructure and environmental development under the Phare programme to prepare the CEE countries for EU membership. This however, sent conflicting messages to the recipient, as the massive funds (for cash strapped CEEC) provided for road building for example, had to be spent in a hurry and environmental considerations were neglected. Similar cases happened in Spain, Portugal, Greece and Ireland, where the huge funds from the Cohesion Fund were also sometimes used detrimentally for the environment. (Beckmann & Dissing, 2004, p. 140)

There are also concerns that in many and most respects the EU’s present way of doing things is fundamentally unsustainable, in both economic as well as biological terms. This is shown by the impact of the “Instrument for structural policies for pre-accession fund” (ISPA) which provided for major infrastructure projects in transportation and environment. Much of the environmental spending within ISPA has focused on supporting sewage and wastewater treatment projects with the emphasis on big projects of 5 million Euros and upwards - suitable for large cities. In response to complaints that the size limit failed to address the challenges in rural areas, the

Commission permitted communities to form associations in order to submit common projects. The result has been that small communities have come together to build traditional, over-dimensional sewage treatment plants, pumping their sewage for kilometres across fields to reach the treatment facility. Low-tech, low-cost and more sustainable biological projects have not been considered. (Beckmann & Dissing, 2004, p. 140)

Now there are concerns that the rapid commercialization and increased prosperity in the new Member States is causing a huge increase in wastes (paper, bottles) which at this stage can not be properly disposed of. Another problem is the huge increase in the number of cars which are causing near permanent grid-lock in the capital cities, while improvement to public transport is being neglected.

The ‘socialist’ production philosophy of increasing production regardless of the cost of inputs has caused tremendous waste. (Gille, 2004, p. 124) This is still shown today as underpriced utility costs are cause for pollution. For example in most of the new Member States the ‘energy intensity’ - that is, tons of oil equivalent consumed per \$1,000,000 of GDP - is upward of four to nine times higher than the EU average. Most of this energy is produced in coal fired or nuclear power stations and both of them are problems for the environment. The solution to this would be a substantial increase of the cost of electricity and water. (Gille, 2004, p. 118)

The ‘europianisation’ of environment policy and the weak standing of environmental organizations in the new Member States have resulted in a system of “top-down” implementation. That means the EU is issuing new procedures which are passed down to the States while little if any information flows the other way.(Carmin & Vandever, 2004, p. 13)

It has been estimated that to adopt the environmental *acquis* now, would range from 80 to 100 billion Euros, which would require the new Member States to spend an average of two to three percent of their GDP to implement the environmental *acquis*.

(Carmin & Vandever, 2004, p. 8) The Commission has therefore granted extended implementation times for the full adoption by the new Member States.

### **8) The Common Environmental Policy's (CEP) impact on Multi-level governance.**

Unlike the well organized, Europe-wide organizations that represent the interests of farmers, unions, industrialists etc. with representative offices in Brussels, the environment failed to create a similar climate. The fact that environmental matters are often very technical, such as carbon dioxide content, results in professionals being largely involved, while ordinary citizens without technical knowledge tend to leave the organization after a short while.

The Commission has now taken steps to change this:

it encourages and funds local environmental NGOs;

it has actually set up a Europe-wide environmental organization;

it demands that NGOs be involved in any planning for EU support. (4)

It is considered that the importance of NGO's and other sub-national authorities (SNA) will continue to grow with the above-mentioned encouragements. In relation to the EU generally, Hooghe and Marks (2001b:78) argue that SNAs will adopt a number of strategies, but of course they apply even more so to the environment, they will:

establish their own offices in Brussels, intensify their contacts with each other, demand more information from central governments about developments in Brussels, demand formal channels to influence ministerial representation in the European Union, form direct links with Commission officials,
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(George, 2004, p. 115)

### **9) Conclusion.**

At its founding in 1957, the European Economic Community (EEC) did not have any laws, policy or bureaucracy dedicated to environmental issues. Any environmental/health policies that existed were formulated and implemented by the

Member States. Some 45 years later, the EU has created some of the strongest and most progressive environmental policies of any polity in the world. This has been achieved with the involvement of a variety of state and non-state actors at different levels of governance, ranging from central government departments, regional and local government authorities, national regulatory agencies, firms and environmental interest groups. (Fairbrass and Jordan, 2004, p. 147)

It is a strange arrangement whereby the Commission can initiate new policies and oversees the implementation of minimum common policies at the national and sub-national level, but it has to rely on the Member States' reports confirming implementation and monitoring of environmental legislation. When shortcomings about compliance or infringement are reported, frequently by NGOs or private persons, the Commission can take remedial action. If a Member State fails to remedy the problem the case is being referred to the European Court of Justice (ECJ). The result is that if in a Member State environmental organizations are strong and well organized and report shortcomings to the Commission it will act more frequently against that state, than a Member State with relatively weak environmental organizations.

*In the EU there has always been the competition between growth and environmental policy. When there is poor economic growth there is a tendency to ease of with environmental requirements. El-Agraa (2004, p. 306) reports that in 1992 it seemed that EU environmental policy might be put in reverse. Similar difficult economic conditions now may also lead to a slow-down or non-compliance with environmental regulations. However, it is expected that environmental protection and enhancement will continue due to:*

The Commission's commitment to this policy,

The strong influence of the 'Greens' in the Parliaments, both EP and national.

The ECJ's power to enforce Community law,

The requirement now for environmental groups to be consulted and environmental impact studies to be made if EU assistance is requested,