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Thirty Years of the Single European Market

Stefano Micossi

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Abstract

Over the past thirty years, the Single European Market has been the core business of the European Union, and enormous progress has been achieved in both 'widening' the economic activities covered by EU legislation and 'deepening' the *acquis* to overcome emerging gaps in integration in areas already covered by legislation. And yet, empirical evidence indicates that market integration has stalled on many fronts and, more importantly, that the expected economic benefits of integration in terms of higher growth of incomes, jobs, and productivity have fallen short of expectations, notably in the long-established EU-15 member states. The situation has not improved since the introduction of the euro.

This paper reviews the main developments in Single European Market (SEM) legislation and regulatory activities over the past three decades; it summarises the results of the SEM programme in market integration, highlighting areas where gaps appear to be more evident; and discusses the impact of economic integration within the SEM, including aspects that play an important role in feeding popular resistance to integration.

Keywords: Single European Market, regulatory models, free movements, goods, persons, capital, services.

College of Europe
Collège d'Europe
Brugge
Natolin

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Stefano Micossi*

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Introduction

Over the past thirty years the Single European Market (henceforth SEM) has been the core business of the European Union, and enormous progress has been achieved in both 'widening' the economic activities covered by EU legislation and in 'deepening' the *acquis* to overcome emerging gaps in integration in areas already covered by legislation (Pelkmans 2011). And yet, empirical evidence indicates that market integration has stalled on many fronts and, more importantly, that the expected economic benefits of integration in terms of higher growth of incomes, jobs and productivity have fallen short of expectations, notably in the long-established EU-15 member states. The situation has not improved since the introduction of the euro.

The purpose of this paper is to review the main developments in SEM legislation and regulatory activities over the past three decades; to summarise the results of the SEM programme in market integration, highlighting the areas where gaps appear to be more significant; and to discuss the impact of economic integration within the SEM, including aspects that play an important role in feeding popular resistance to integration. Although SEM policies for financial services will be discussed, recent developments in the Banking Union and Commission proposals for a Capital Markets Union will not be covered, except for aspects of general relevance for the SEM's broad architecture.

The paper is written from the perspective of an economist who has devoted much of his professional life to matters of economic and monetary integration in Europe, and who, by necessity, has become keenly aware of the importance of legal and institutional arrangements in the functioning of economic systems. Particular attention will be paid to the issues of economic incentives in institutional design, while steering away from the detailed legal complexities and controversies surrounding SEM laws.

* Stefano Micossi is Director General of Assonime, a business association and think tank in Rome. He has taught at the College of Europe since 1991, with an interruption during his stint at the European Commission (where he served as Director General of Industry in 2005-08), until the academic year 2015-16. He chairs the LUISS School of European Political Economy (SEP) and is a member of the boards of CEPS, Cassa Depositi e Prestiti and the CIR Group.

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1. Overview

The goal of economic integration constituted the principal focus of the 1957 Treaty of Rome, in the specific form of the establishment of a *common internal market*, characterised by the freedom of movement of goods, services and productive factors (labour and capital). Its distinguishing feature was, in addition to being a free trade area and a custom union with a common external tariff, the aim of eliminating 'technical' barriers arising from national rules for the protection of health, safety and the environment, and to a limited extent of tax barriers as well.

Three features stand out in this regard (Craig 2003). First, integration entails not only the elimination of barriers ('negative' integration) but also the harmonisation of legislation that provides standards of protection of worthy goals of general interest ('positive' integration) applicable throughout the SEM. Second, the elimination and prevention of barriers also concerns behaviour that may distort the level playing field in the SEM after the market has been opened, i.e. by means of public subsidies and protections granted in the domestic market to national players or anti-competitive actions by national players. These distortions are addressed through competition policy and in particular state aid policy – a policy unique to the European construction that directly constrains the member states. Third, market opening and liberalisation do not preclude public intervention, e.g. environmental protection through the Common Agricultural Policy or cohesion policies to help weaker economies withstand the impact of market opening. Common policies will normally be administered by the Commission – often under Council oversight through specialised Council committees.

Already in the early years of the Economic Community, the European Court of Justice (ECJ) emerged as a fundamental player in the integration process through its adjudication of cases and 'preliminary' rulings on questions raised by national courts regarding the treaty's interpretation. Its central role in the development of the SEM came to the fore with early decisions establishing the direct effect[1] and the supremacy over national legislation[2] of Community rules in areas of Community competence. They laid the ground for landmark decisions such as Reyners,[3] Dassonville[4] and Cassis de Dijon,[5] with paramount consequences for the subsequent evolution of legislation.

The SEM programme was formally launched in June 1985 by the Commission *White Paper on Completing the Internal Market*, endorsed by the European Council in Milan at the end of the same month. Its main message, which built upon the Cassis de Dijon jurisprudence, was that there was no need to seek harmonisation when barriers to free movement would come down under the *rule of reason* of equivalent protection. Henceforth, harmonisation measures would be limited to restrictions that could be justified under the mandatory grounds allowed by the Treaty, and, therefore, could only be eliminated by legislation raising the common level of

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[1] Case 26/62, Van Gend & Loos vs. Administratie der Belastingen [1963].

[2] Case 6/64, Costa vs. Enel [1964].

[3] Case 2/74, Reyners vs. Belgian State [1974] recognizing direct effect to freedom of establishment to what is now Article 47 of TFEU.

[4] Case 8/74, Procurer du Roi vs. Benôit and Gustave Dassonville [1974].

[5] Case 120/78, Rewe-Zentrale AG vs. Bundesmonopolverwaltung für Branntwein [1979] establishing the principle of mutual recognition of national rules and thus opening the way to the application of Article 34 TFEU to indistinctly applicable national rules.

protection in that particular area, recognising the legitimate concerns of member states and restoring free movement.

The White Paper included proposals for Treaty changes that would simplify and speed up the legislative process. In the ensuing months, an intergovernmental conference swiftly reached an agreement on those proposals, leading to the Single European Act (SEA) that was signed in February 1986. After ratification by member states, it entered into force on 1 July 1987. The SEA provided the definition of the SEM as an "area without frontiers in which the free movement of goods, persons, services and capital is ensured" (now in Article 26 of TFEU)[6] and introduced (qualified) majority voting in the Council for SEM measures, together with a new cooperation procedure with the European Parliament, which later led to full co-decision under the Maastricht Treaty. Under the new legal basis for SEM measures (Article 100a TEEC,[7] now 114 TFEU) the Commission developed the New Approach to SEM legislation, limiting legislative measures to setting the essential requirements of protection, while confining technical specifications to voluntary standards developed by European standardisation bodies.

The economic rationale of the SEM programme lay in the belief that market opening would revive the feeble European economy by fostering concentration and the exploitation of economies of scale in industry, improving the allocation of productive resources, and raising productivity. The 1988 Cecchini Report described at considerable length the structural weaknesses of the European economy and its specialisation in sectors with low growth potential, and held out the promise that completion of the SEM programme would bring substantial economic benefits (ranging from 4.25 to 6.5% of GDP).

The White Paper tabled some 300 harmonisation measures, mainly in the domain of goods, which by and large were approved by the statutory deadline of 1992 (cf. Pelkmans 2008 and 2011); additional liberalisation directives were enacted in the ensuing years for opening to competition services – notably network industries (starting with telecoms and moving on to energy, transport, and postal services) and financial services.

In network industries, the presence of increasing returns and, sometimes, natural monopoly market structures, inevitably pushed SEM initiatives beyond market opening into the domain of regulation to ensure open access by competitors and a level playing field in the provision of services to final users. Network services were normally also services of general interest; Article 86 TEC[8] (now 106 TFEU) provided the flexible framework required to ensure that free movement and competition rules would apply to these services without compromising their specific mission (European Commission 2000b). The tensions with some member states on the delicate balance between national social preferences and SEM rules led, with the Amsterdam and Nice Treaties, to a new provision – Article 16 TEC, now 14 TFEU – reaffirming the special role of services of general interest in the "shared values of the Union". Protocol 26 to the treaties clarifies that this includes respecting the autonomy of national authorities, at all levels of government, in deciding on public services and organising their provision, although the Union will continue to scrutinise whether the means of provision are consistent with SEM rules.

[6] Treaty on the Functioning of the European Union.

[7] Treaty establishing the European Economic Community.

[8] Treaty establishing the European Community.

Further advancements in SEM policies were achieved by strengthening 'accompanying policies', e.g., with the approval of the Merger Regulation,[9] on the one hand, and the new economic cohesion policies and R&D policies, supported by substantial budgetary resources, on the other. These measures are complementary, as weaker economies are provided with extra resources to withstand increased competitive pressure stemming from market opening and the expected concentration of industry. The single currency was created to reinforce the integration and competition effects of the SEM by improving price transparency, reducing the costs of cross-border transactions, and eliminating the exchange rate risk.[10] For reasons that are not yet fully understood, while there have been positive effects on growth, market integration has been less pronounced than anticipated, with the productivity performance of many euro area members worsening rather than improving (more on this later).

Once the wave of legislation prompted by the White Paper was completed, it soon became evident that important economic activities were not covered and that, in many respects, existing legislation fell short of bringing about genuine integration (Pelkmans 2011). The changing economic environment, including globalisation, the development of new technologies and the increased prominence of environmental issues in public policy, also greatly contributed to the legislative agenda, with new demands from the public and member states ('widening'), and a continuing need to review and adapt existing legislation ('deepening'). This is reflected in the multiplication of strategic reviews and new plans to 'complete' the SEM (cf. Annex 1 in High-Level Panel of Experts, 2016). In fact, completion of the SEM has become a moving target, requiring continuing adaptation. A summary of the White Paper's main initiatives and subsequent legislation is presented in Table 1.

The Monti Report (Monti 2010) highlighted a strand of ideas that had been building up in SEM strategies over the previous decade; that is the socio-political legitimacy problems surrounding market opening and the need to (re-)build popular consensus around SEM goals. The Report stresses the importance of harnessing the SEM for the benefits of consumers, promoting green growth strategies and reviewing the appropriate balance between SEM freedoms and workers' rights and expectations, which had been especially strained by the SEM rules on the posting of workers and related ECJ decisions, e.g. Laval.[11]

Over time, these broader goals found Treaty recognition with new chapters on consumer protection, social policies and employment.[12]

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[9] Regulation (EEC) 4064/89, now Regulation (EC) 139/2004.

[10] In the 2000s, the euro sovereign debt crisis reintroduced a re-denomination risk that widened the spreads between borrowing rates in the periphery and those prevailing in the 'core' countries, thus reversing integration and re-creating significant financial markets fragmentation.

[11] Case C-341/05, Laval un Partneri vs. Svenska Byggnadsarbetareförbundet, Svenska Byggnadsarbetareförbundets avdelning 1, Byggettan and Svenska Elektrikerförbundet [2007]. The Monti Report was followed by a flurry of measures under the hats of the Single Market Acts I and II, on a broad front of themes (consumer empowerment, social entrepreneurship and SMEs financing, business environment, and taxation) and activities (digital market, utilities, services, and IPR), which however did not significantly advanced integration.

[12] With the Lisbon Treaty, they came to full prominence in Article 3 TEU, setting the Union goals of a "competitive social market economy, aiming at full employment and social progress, and a high level of protection and improvement of the quality of the environment. ... [The Union] shall combat social

Table 1. Single European Market (1985-2015): Overview

Goods	✓ Mutual recognition (ECJ, *Cassis de Dijon* 1979) ✓ Under the Single European Act (1986), SEM a Community task; a new legislative procedure by QMV (with EP co-decision) and harmonisation of essential requirements ✓ Optional technical standards for compliance
Services (establishment and cross-border supply)	✓ ECJ: from discrimination to restriction → 'market access' test and 'general good' principle (Vlassopoulou 1989 and Gebhard 1994 on right of establishment; Sager 1990 and Gouda 1989 on freedom to provide services)
General Regime	✓ Framework Dir. 2006/123 → horizontal principles applicable to all services, except for services already harmonised and some specific activities
Financial Markets	✓ Single passport based on harmonised criteria for national licences ✓ Home country supervision of financial institutions; host country control for business conduct, consumer protection and 'systemic' stability of host market ✓ Investment services and financial market infrastructure (MiFID II 2014/65, MiFIR 600/2014) ✓ European System of Financial Supervision comprising: (*i*) the European Systemic Risk Board; (*ii*) the European Supervisory Authorities (EBA, EIOPA, ESMA) ✓ The Banking Union package: Single Supervisory Mechanism, Single Resolution Mechanism and Directives on national guarantees schemes and national resolution schemes; CRD IV package for capital requirements and prudential supervision
Services of General Interest	✓ Amsterdam Treaty introduces article 14 TFEU, further supported by Protocol 26 on SGI
Network Industries	✓ For telecoms, gas and electricity, postal services, rails: market opening (different progress) and pro-competitive regulation (access to network, separation of service provision from infrastructure); in some cases establishment of universal service obligations ✓ EU regulatory networks to complement national authorities (e.g., BEREC, ACER) ✓ Liberalisation measures for air, road and maritime transport
Capital	✓ Full freedom of movement (Dir. 88/361) ✓ Transparency and market integrity: Prospectus (Dir. 2003/71, under review); Transparency (Dir. 2004/109, as amended in 2013); Market abuse (Reg. 596/2014 and Dir. 2014/57 harmonising criminal sanctions); Shareholders' Rights (Dir. 2007/36) ✓ Market for corporate control: Takeover Dir. 2004/25 ✓ Company mobility: European Company Statute (Dir 2001/86 on workers participation; Reg. 2157/2001 on establishment and governance of the company→'real seat' approach, partly reversed by the ECJ) ✓ Capital Market Union Action Plan 2015

exclusion and discrimination, and shall promote social justice ... It shall promote economic, social and territorial cohesion, and solidarity among Member States ...".

Table 1. Single European Market (1985-2015): Overview

Persons	
Workers	✓ Workers' mobility and residence right, equal treatment in working conditions, and social and tax benefits (Reg. 492/2011) ✓ Supplementary pension rights (Dir. 98/49); coordination of social security systems (Reg. 883/2004) ✓ Posted workers Dir. 96/71 (under review)
Professionals	✓ Mutual recognition of professional qualifications with minimum training requirements; from sectoral directives to horizontal approach (Dir. 2005/36, as amended by Dir. 2013/55 → EU professional card)
Individuals	✓ Maastricht Treaty → introduction of EU citizenship, including the right to circulate and reside freely in the EU ✓ Comprehensive discipline of free movement and residence (temporary and permanent) for EU citizens and their families in Dir. 2004/38
Horizontal	
Public Procurement	✓ Coordination of the procurement procedures for the award of public works, public supply and public service contracts above certain value thresholds (with separate rules for public utility sectors): Dir. 2014/24 and Dir. 2014/25 ✓ New rules for concessions (Dir. 2014/23), imposing minimum requirements for selection and award criteria and limited duration
IPR	✓ Harmonised rules on copyright (Dir. 2001/29) trademarks (Dir. 2015/2436), industrial design (Dir. 98/71), biotechnological inventions (Dir. 98/44), and trade secrets (Dir. 2016/943) ✓ EU-wide rights: EU trademark (Reg. 207/2009 as amended by Reg. 2015/2424); Community design (Reg. 6/2002); Unitary patent (Reg. 1257/2012 and Reg. 1260/2012) ✓ Procedures to enforce IPR against counterfeiting and piracy (Dir. 2004/48); Unified Patent Court, not yet operational
Consumer and Data Protection	✓ Health and safety: general product safety Dir. 2001/95; food safety Reg. 178/2002 ✓ Consumers' economic interests: minimum harmonisation on liability for defective products (Dir. 85/374), sales and guarantees (Dir. 1999/44), consumer credit (Dir. 2008/48), unfair contract terms (Dir. 93/13), package travel (Dir. 2015/2302); maximum harmonisation approach for unfair commercial practices (Dir. 2005/29) and consumers' rights (Dir. 2011/83, including distance contracts and right of withdrawal) ✓ Cooperation among national enforcers of consumer law (Reg. 2006/2004, under review) ✓ General Data Protection Reg. 2016/679; e-privacy (Dir. 2002/58)
Digital Economy	✓ E-commerce (Dir. 2000/21): information requirements for online activities and contracts, transparency of commercial communications, limitation of service providers' liability ✓ Electronic identification (Reg. 910/2014), e-money (Dir. 2009/110), payment services (Dir. 2015/2366) ✓ Digital Single Market Strategy (2015) including legislative proposals on consumer protection in online sales, parcel delivery, geo-blocking

Two main market opening initiatives in the past decade concerned services in general and financial services specifically. The first one was prompted by a Commission Report on *The State of the Internal Market for Services* (European Commission 2002) which thoroughly described the sorry state of integration in this sector, the main legal barriers and their impact on the economy, notably on small-medium enterprises (SMEs) and consumers. The Services Directive,[13] approved by Council and Parliament in 2006 and expected to enter into force in 2009, provided an adequate response but, as will be shown, implementation has been wanting.

The second initiative is a decade-long attempt to integrate financial markets and set up a supranational regulatory structure for financial services, in response to repeated bouts of financial instability. Two reports, one prepared at the beginning of the last decade under the chairmanship of Alexandre Lamfalussy (leading to the so-called Financial Services Action Plan, to be completed by 2005) and the other prepared by Jacques de Larosière at the end of the decade, mapped out comprehensive interventions to remove remaining restrictions to securities markets and create a new regulatory system able to avoid a repeat of the dramatic financial crisis of 2008-09.[14] The euro area sovereign debt and banking crisis, at the beginning of this decade, convinced governments and regulators to raise the stakes and go for a full Banking Union (already well advanced at the time of writing) and Capital Markets Union (as yet at an early stage of design).

Horizontal legislative measures of increasing ambition have covered public procurement – for goods, services, public works and concessions – still stubbornly protected by national procurement authorities, and the markets for coded technology (IPR). The latter is obviously of paramount importance for encouraging Europe-wide circulation of new technology and its innovative applications, in a continent that has tended to privilege the protection of the investor over the diffusion of new ideas.

Finally, in recent years, a comprehensive initiative has aimed to establish a Digital Single Market, in order to allow the Union to exploit the full economic potential of ICT technologies (European Commission 2015a). The programme covers a broad range of themes and activities, organised around the three pillars of i) consumer and business access to online markets across the Union, ii) the legal and competitive environment and iii) secure and trustworthy infrastructures.

2. An Innovative Regulatory Model

The SEM is built on an innovative regulatory model that aims to open the markets of member states to free movement while respecting, as much as possible, the diversity of national institutions and regulatory approaches. It is a *sui generis* model of *integration with diversity* without precedent in regulatory history, enabling the different national rulebooks for safety, health and consumer protection to coexist and apply at the same time within each member state's jurisdiction.

[13] Directive 2006/123/EC.

[14] In line with parallel reforms on the US side with the Dodd-Frank legislation and the comprehensive review of prudential rules for banking agreed upon by the Basel Committee of Banking Supervisors, transposed at the EU level with the CRR/CRD IV package of 2013 (including Directive 2013/36/EU and Regulation (EU) 575/2013).

This approach was built on the landmark Cassis de Dijon decision by the ECJ (1978), which established the principle of mutual recognition of national rules. With one stroke a myriad of technical barriers to free movement of goods were made illegal, thus relieving the European Commission of the task of seeking new legislation to bring them down. The decision was followed by other decisions refining the principle and extending its application to services and to persons seeking to move to another member state to reside and work.

The next required building block was a more flexible legal basis to enable legislation on the SEM, and this was provided by the SEA with new the Article 100a TEEC (now Article 114 TFEU). Under this legal basis, harmonisation was based on three lines of action (Craig 2003):

(i) Substantive legislation to harmonise safety, health and consumer protection legislation by laying down essential health and safety requirements, and European standardisation to offer an optional means of compliance with harmonised requirements providing a presumption of conformity;

(ii) Procedurally oriented legislation to improve transparency of information on national technical standards and regulations, and later on for public procurement; with Directive 83/189/EEC,[15] failure to notify the EC network of mutual evaluation of these measures would make them null and void; the information network, originally conceived for goods, was later extended to cover technical measures for services;

(iii) Extension of mutual recognition by legislation, notably in the recognition of professional qualifications and the services directive.

The combination of the principle of mutual recognition with the three pillars of legislative activity brings about a radical shift in economic philosophy: market opening is placed at the centre of economic policies not only to foster growth, but also to improve the welfare of citizens (Barnard 2013, Weiler 1999). Majority voting means that governments may, sometimes, be obliged to accept substantial departures from their national policies and regulatory traditions. While the prevailing consensual culture in Europe usually translates into a reluctance to decide by majority voting, the very possibility of coming to a vote makes Council members better disposed to compromise.

Common policies have been sensitive to member states' and citizens' concerns, and have developed their tools so as to strike an acceptable balance between the community goal of free movement and national preferences in shaping protections. To follow are some paramount examples of these frictions and the resulting balancing acts, which have often entailed remarkable creativity and innovation in drafting SEM rules. When referring to legal aspects of the SEM, I will mainly follow the outstanding volume by Catherine Barnard (2013), while steering away from interpretative debates.

(a) Market access

The building blocks of the new model of legislation prompted by the White Paper are in two landmark ECJ decisions, Dassonville and Cassis de Dijon, as already mentioned. Dassonville first established the definition of 'measures having an equivalent effect' to a quantitative restriction to trade prohibited by Article 34 (and 35) TFEU as follows: "all trading rules enacted

[15] Later on, directive 98/34/EC and now directive (EU) 2015/1535.

by Member States which are capable of hindering, directly or indirectly, actually or potentially, intra-Union trade …". Later decisions further clarified the term 'rules' as to include policies (such as a 'buy Irish' campaign by the Irish government) and administrative practices.[16] This very broad definition already anticipates the 'market access' principle extensively used later by the ECJ for the liberalisation of establishment, the cross-border supply of services and the recognition of professional qualifications.

A further building block is the distinction between 'distinctly applicable' measures,[17] which openly discriminate against imported products, and 'indistinctly applicable' measures which, while not discriminatory, may nonetheless create obstacles to free circulation. The latter lay at the core of the Cassis de Dijon case; they are the result of disparities in national legislations concerning the marketing of products. The ECJ ruled that those measures must be complied with by the product trying to enter a member state's market different from the member state of origin, only if they are recognised as necessary in order to satisfy *mandatory requirements* "relating in particular to the effectiveness of fiscal supervision, the protection of public health, the fairness of commercial transactions and the defence of the consumer".[18] Otherwise, they cannot be used to restrict free entry into the domestic market. Moreover, those measures should be proportionate to the aim in question and should satisfy a criterion of 'least restriction' to the free movement of goods in the choice between alternative measures that may achieve the same result.

Thus, after rejecting arguments by the German government wherein a national rule imposing a minimum alcoholic content for beverages was justified by mandatory requirements for the protection of health and consumers, the ECJ stated the basic principle of *presumption of equivalence*, or *mutual recognition*: it saw no valid reason why, "provided that they have been lawfully produced and marketed in one of the Member States, alcoholic beverages should not be introduced into any other Member State".

The direct implication of Cassis de Dijon is that the producer's home state regulation will, under normal circumstances, prevail over host state regulation where the product is sold and that the entry of a good can be refused only on grounds of the 'imperative' non-economic reasons listed in Article 36 TFEU, and the additional criteria developed in the ECJ jurisprudence on admissible mandatory requirements. The principle also has an important procedural implication: each member state must create a space for the evaluation of the rules of all the other member states within its administrative system, to ascertain whether a particular product qualifies for mutual recognition. Since the member states were less than enthusiastic disciples of mutual recognition, Regulation (EC) 764/2008 introduced administrative procedures to supplement judicial recourse when mutual recognition is denied. Under this procedure, the member state intending to prohibit the placing on the market of a product is obliged to explain the technical rule behind the prohibition and to set out the technical and scientific evidence justifying that decision.

[16] Case 249/81, Commission vs. Ireland [1982].

[17] Already stated in Article 2 of Directive 70/50/EEC.

[18] Later decisions clarified the fact that the mere existence of different rates of indirect taxation or any differential impact of national rules on competitive conditions would not represent *per se* a justification for restricting access to the domestic market under the consumer protection or fair trading grounds (e.g. Case 182/84, Miro BV. [1985]).

The 'discrimination' model implicit in Cassis de Dijon was gradually superseded by a stronger requirement of 'market access'. With Sager,[19] the Court ruled that the prohibition of restrictions to the supply of services in Article 56 TFEU required not only the elimination of all discriminations on grounds of nationality but also the abolition of restrictions "liable to prohibit or otherwise impede the activities of a provider of services established in another Member State where he lawfully provides such services".

Two further decisions, Kraus[20] and Gebhard,[21] struck down national measures limiting the domestic use by nationals of academic titles earned abroad and of domestic titles in the exercise of a profession by a foreign EU national. The measures were not qualified as discriminatory; rather they were struck down as "liable to hamper or to render less attractive the exercise by Union nationals ... of the exercise of fundamental freedoms guaranteed by the Treaty". In subsequent cases, especially for persons and capital, the Court has gone even further, replacing the reference to market access by the simple reference to 'obstacles' or 'restrictions' on free movement.

As emphasised by Barnard (2013), this evolution has placed tighter constraints on a member state's ability to regulate market access. Under the new approach any domestic regulation may be seen as an obstacle to access – whereas under the previous 'discrimination' approach certain restrictions to access could be maintained, provided they applied uniformly to all market participants. In fact, the principle of market access is so broad as to become ill-defined, opening the way to abusive exploitation of Treaty articles to oppose any national measure regulating economic activity, since almost by definition regulations may restrict profit margins and therefore reduce the attractiveness of pursuing one particular activity. The potential excesses of the market access principle have been addressed by the ECJ with a number of legal techniques, e.g. Keck[22] and two Commission vs. Italy cases.[23] But the problem refuses to go away, and has again come into full prominence with certain decisions limiting *de facto* the scope of union rights recognised under national legislation (cf. Laval, already mentioned, and Viking).[24]

Thus, one arrives at the crux of the matter. The principle of open access, which is the cornerstone of SEM policies and the condition for effective competition, puts pressure on domestic institutional arrangements in a wide range of very sensitive domains, including standards of protection of consumers and the environment, labour market rules, public services, and even cultural products such as television and cinema. As a result, when choosing between competing products and services, or between potential locations of a professional activity or enterprise, Union citizens are implicitly also choosing between the institutions underpinning those activities. This has major consequences for private economic incentives

[19] Case C-76/90, Säger vs. Dennemeyer [1991].

[20] Case C-19/92, Kraus vs. Land Baden-Württemberg [1993].

[21] Case C-55/94, Gebhard vs. Consiglio dell'Ordine degli Avvocati e Procuratori di Milano [1995].

[22] Joint cases C-267 and C-268/91, Keck and Mithouard [1993], where the Court recognised that 'certain selling arrangements' did not breach Article 34 TFEU.

[23] Case C-518/06 [2009] on motor insurance and Case C-565/08 [2011] on maximum lawyer fees.

[24] Case C-438/05, International Transport Workers' Federation and Finnish Seamen's Union vs. Viking Line ABP and OÜ Viking Line Eesti [2007].

and national institutions, which must adapt to the common policies and the resulting changes in the economic and social environment.

A major criticism levelled against this approach is that, by setting in motion a process of competition between institutions, it might foster a *race to the bottom* in the levels of protection, as countries seek to attract businesses to their jurisdiction. Of course, one must recognise that considerations related to the quality of products and locations normally play an important role in the expression of individual preferences. Price is therefore not the only variable taken into consideration. In other words, a higher quality of institutions may well determine the choice, even if this sometimes entails a higher price for a product or service, or a higher location cost. And yet, this criticism cannot be dismissed light-heartedly. Finding the right balance between SEM freedom and national societal preferences remains an unresolved issue and, on occasion, a source of severe tension between Union institutions and member states.

(b) Article 114 TFEU

Article 114 provides the 'residual' legal basis of SEM legislation, to be applied when the Treaty does not otherwise provide for a specific legal basis. It can only be used for the 'approximation' of laws and administrative practices, and not for other purposes related to the SEM.[25] Important ECJ decisions[26] on the so-called Tobacco Control Directive[27] further clarified that Article 114 can be used to enact measures that contribute to the elimination of actual and potential obstacles to the exercise of fundamental freedoms, as well to remove distortions (actual and potential) of competition arising from national rules. It also clarified the fact that, under Article 114, the Union does not have the general legislative power to intervene to correct market failure in the SEM.

A first important implication is that the need for SEM legislation only arises when there is a legitimate obstacle to trading within the SEM, as maintained under the imperative need exceptions recognised by the TFEU and the ECJ. When mutual recognition works there is no need to legislate. Moreover, legislation will target the elimination of those legitimate obstacles with measures adequate for removing the restriction, but goes no further. This opens the way to minimal harmonisation measures strictly commensurate with the restriction to be eliminated. It follows that, at least in principle, the Union's ability to act is circumscribed by considerations of subsidiarity, under which it will not act without an obstacle, and proportionality, requiring that the constraints imposed on member states are the strict minimum required to restore free circulation.

Two main issues were opened but not resolved by Cassis de Dijon. The first is how member states could demonstrate conformity to essential requirements (in a proportionate manner); the second is how member states could create sufficient trust in the incoming products claiming mutual recognition. This led to the development of a policy for conformity

[25] Case C-436/03, European Parliament vs. Council of the European Union [2006].

[26] Case C-376/98, Federal Republic of Germany vs. European Parliament and Council of the European Union [2000] and Case C-74/99, The Queen vs. Secretary of State for Health and Others, ex parte Imperial Tobacco Ltd and Others [2000].

[27] Directive 98/43/EC.

assessment. The response was a Resolution on a new approach to technical harmonisation and standards (the 'New Approach') adopted by the Council of Ministers on 7 May 1985.[28]

The principles of the New Approach laid the foundation for the establishment of the European standardisation system, as now defined by Regulation (EU) 1025/2012, built upon three pre-existing standardisation organisations (CEN, CENELEC and ETSI) that have evolved into the European Standardization Organizations. The strategic vision for European standardisation is illustrated in the European Commission (2011a) communication on standards, while the legal framework is set out in Regulation (EU) No. 1025/2012. Reliance on standards for technical specifications has become an accepted principle of the WTO, which promotes use of international standards through its agreement on Technical Barriers to Trade.

An important feature of European standards is that, following publication in the Official Journal of the Union, their use is open to any interested manufacturer; accordingly, their definition and approval must respect strict procedural requirements to ensure that all interested parties, notably including, together with manufacturers, consumers, trade unions, and environmental interests, are heard during the process of approval. Over time, non-EU producers have been granted access to the process on an equal footing. The EU has developed policies to ensure that the standard setting process remains open, transparent, and non-discriminatory.

The approval of a standard may become an important factor in defining the market for a given product or service, as for instance it famously happened with the GSM standard for mobile communications, which has developed into the *de facto* global standard for mobile communications covering a 90% market share and over 200 countries. This contrasts sharply with the US system, predominantly based on proprietary standards, where companies compete by trying to impose their own standards on the market.

Article 114 is a prime example of the care taken by the Treaty in seeking an appropriate balance between national concerns and the overriding goal of free movement.[29] The legal provisions

[28] The New Approach includes the following components: i) legislative harmonisation should be limited to essential (performance or functional) requirements that products must meet to enjoy free movement; ii) technical specifications meeting the essential requirements should be laid down in harmonised standards 'mandated' by the harmonisation directives; iii) products manufactured in compliance with harmonised standards would benefit from a presumption of conformity with the corresponding essential requirements, as well as a simplified conformity assessment procedure; iv) the application of harmonised standards was to remain voluntary, and the manufacturers could apply different technical standards to meet the requirements but would take upon themselves the burden of demonstrating their conformity with the directive's essential requirements.

[29] Thus, i) in its legislative proposals, the Commission will take as a base a high level of protection (para. 3); ii) the member states are allowed to maintain national provisions (para. 4) and to introduce new legislation (based on new scientific evidence, (para. 5) even after the adoption of harmonising legislation; iii) when this happens, the Commission normally has 6 months (12 months when the matter appear particularly complex and the delay does not endanger human health) to approve or reject the measure – a rather short time span, adopted in Amsterdam to make rebuttals more difficult; if it doesn't manage to respond, the measure is deemed approved and the Commission must propose new harmonising legislation that takes the member state concern into account; iv) the Commission can take the case directly to the ECJ, however, by derogating from the normal procedure of Articles 258 and 259 TFEU when it finds that a member state is making improper use of its powers under para.s 4 and 5; v) finally, harmonising legislation and even technical standards will normally contain safeguard clauses authorising provisional restrictions introduced for one of the non-economic reasons in Article 36 TFEU.

bounce back and forth between the member states and the European institutions, leaving considerable room for accommodation of special circumstances.

A further element of caution has been introduced with increasing application of the precautionary principle whereby, even in the absence of unambiguous scientific evidence, a measure may be rejected or justified in view of the nature of a risk or the irreversibility of its effects (European Commission 2000a). The principle has made its way into the TFEU with reference to environmental policies (Article 191, para. 2) and has played a significant role in many areas of health and consumer protection, perhaps not always in the best interest of consumers and the economy (Pelkmans 2012). For instance, the principle *de facto* led to the exclusion of all genetically modified products from European agriculture, including limited cultivations for research purposes. As a result, an important branch of modern industry for agriculture has been pushed out of Europe. Clearly, we are confronted here with a strong cultural element which the SEM rules were eventually forced to accept, even if not based on convincing scientific evidence.

(c) Agencies and networks of regulators

In the second half of the past century, the role of the state in the economy has been characterised by a remarkable development of administrative law-based approaches to achieve complex policy goals, whereby the state has become increasingly active in setting standards for economic, social, environmental, and other matters, as well as developing separate executive branches for the regulation and oversight of the implementation of legislation. In this context, the Union has also undergone a significant transformation from a mainly law-producing organisation towards an organisation actively engaged in the administrative implementation of Union law.

In the process, the Union has developed innovative instruments and approaches by building an array of regulatory networks and executive agencies entrusted with implementing tasks, with various forms of inclusion of national regulatory bodies. These bodies have emerged in an evolutionary process that has created 'policy islands' in diverse areas such as food safety, chemicals, medicines, financial market regulation, aviation safety, and border controls (Hofmann 2016), normally based on Article 114 TFEU. The policy approaches, regulatory and enforcement powers and institutional design have responded flexibly to the specific sector's requirements, without a unifying model.

Table 2 summarises the main agencies and regulatory networks of the Union, with an indication of their nature (forum, network, agency), organisation and regulatory powers. As may be seen, these bodies, while performing tasks of considerable importance for the functioning of the SEM, do not normally have their own supervisory and regulatory powers, with limited exceptions such as ESMA, which can, under certain circumstances, forbid short selling operations in financial markets and the European Data Protection Board, which approves the criteria for the accreditation of certification bodies. The mode of operation, then, is that agency acts are adopted under the Commission's implementing powers delegated by the Council – with unwritten rules of the game whereby the Commission will normally ratify the agencies' decisions without interfering, except under special circumstances.

A feature worth mentioning concerns governance arrangements: decisions may be less incisive when the agency's governing body is made up exclusively of representatives of national authorities, e.g., for the ESAs for financial markets supervision. The meagre results achieved by these agencies in the promotion of common standards of supervision may be due precisely to this feature. Similar arrangements have been adopted for the Supervisory Board of the Single Supervisory Mechanism, raising the risk of politically influenced decisions in individual cases. This contrasts sharply with the model set by the governing council of the ECB, which has, at its centre, an executive board composed of independent officials (appointed by the Council).

An important issue in the development of the agency model at the Union level has been the 'non-delegation' doctrine based on early decisions by the ECJ whereby i) a delegation of power that is too broad and insufficiently defined is prohibited (Meroni)[30] and ii) agencies cannot adopt normative measures (Romano).[31] The reason behind these judgments was that, besides possibly upsetting the institutional balance established by the Treaties, delegation to the agencies could subject their acts to the scrutiny of the ECJ.[32]

[30] Cases 9/56 and 10/56, Meroni and & Co., Industrie Metallurgiche Spa vs. High Authority of the European Coal and Steel Community [1958].

[31] Case 98/80, Giuseppe Romano vs. Institut National d'Assurance Maladie-Invalidité [1981].

[32] This argument is now less relevant, since the Lisbon Treaty permits judicial review of the agencies' acts (cf. Article 263 para. 1 TFEU).

Table 2. Main EU Agencies and Networks

	NATURE	ORGANISATION/ GOVERNANCE	REGULATORY POWER	SUPERVISORY POWER/ ENFORCEMENT IN INDIVIDUAL CASES
BEREC *Body of European Regulators for Electronic Communications*	Forum for cooperation among NRAs and Comm.; no legal personality; new proposal to transform BEREC into a fully fledged agency	Board of Regulators + staff	**No**: guidelines, best practices and non-binding opinions on draft NRAs' and Comm. measures; advice to the EU institutions	**No**: opinions in cross border disputes and on some draft decisions of the Comm.
ACER *Agency for the Cooperation of Energy Regulators*	EU body with legal personality	Board of Regulators + staff + Board of Appeal	**No**: contribution to network codes; non-binding guidelines, opinions and advice to the EU institutions	**Yes**: individual decisions on technical issues in specific cross-border cases, to be challenged before the Board of Appeal and then the ECJ
CPC Network *Consumer Protection Cooperation Network*	Network of national authorities; no legal personality	No board, no staff	**No**	**No**. The 2016 proposal of new CPC Reg. provides for a common enforcement action, coordinated by the Comm., for cases of EU dimension
ECN *European Competition Network*	Network of Comm. and NCAs; mainly a discussion and cooperation forum; no legal personality	No board, no staff	**No**: recommendations and best practices	**No**: EU competition law is enforced by the Comm. and the NCAs. The Comm. intervention relieves NCAs of their competence
Article 29 Data Protection Working Party **European Data Protection Board** established by the 2016 Reg., not yet operational	Advisory body, no legal personality Independent EU body with legal personality	Secretariat provided by DG Just. Board + staff	**No**: opinions to the Comm. + recommendations and guidelines **Yes**: in addition to soft law acts, the Board approves the criteria for the accreditation of certification bodies	**No**: only national authorities are competent to enforce EU data protection rules **Yes**: legally binding decisions in disputes between supervisory authorities
EBA *European Banking Authority* **ESMA** *European Securities and Markets Authority* **EIOPA** *European Insurance and Occupational Pensions Authority*	EU agencies with legal personality	Each ESA has: a Board of supervisors [national authorities, Comm., EU Systemic Risk Board, the other ESAs (+ECB in EBA)] + staff The Board of Appeal is a joint body of the three ESAs	**No**: draft regulatory and implementing standards (not involving policy decisions), to be examined and formally adopted by the Comm.; opinions to the EU institutions	**Yes**: in some circumstances ESAs adopt individual decisions addressed to financial market participants; they settle disagreements between national authorities in cross-border situations ESMA has a limited direct enforcement power for Credit Rating Agencies and Trade Repositories

A recent decision by the ECJ[33] seems to indicate some 'mellowing' of the non-delegation doctrine (Pelkmans and Simoncini 2014). The British government was seeking the annulment of Article 28 of the ESMA regulation, empowering the agency to forbid short selling in certain specific circumstances. The ECJ rejected the request, arguing that the delegation of powers is lawful as long as it indicates objective criteria and circumscribed conditions for their exercise, and these criteria are subject to judicial review. It further argued that the Council may delegate specific powers to EU bodies with specific technical expertise and broadened the scope of delegation under Articles 290 and 291 TFEU.

While this is a welcome development, it still falls far short of what would be needed to develop fully fledged independent European regulatory agencies (Pelkmans 2012).

(d) Public services

The Monti Report notes that "since the nineties, the place of public services within the single market has been a persistent irritant in the European public debate" (p. 73) but believes that the discussions 'within the Treaty' should have been settled by the 2007 Treaty of Lisbon with the reformulation of Article 14 and Protocol 26 on services of general interest (SGI). The Report sees these services as an important building block for reconciling the single market and the social and citizenship dimension – as a component of the 'highly competitive social market economy' that the Lisbon Treaty has identified as a main objective of European integration.

The central Treaty provision is Article 106 TFEU, which sets out the principle of (proportional) exemption of services of general economic interest (SGEI) from competition rules when their application might endanger the fulfilment of their mission. Over the years, a set of policies and legal principles has been developed to allow member states full freedom in deciding what is public service but restrictions have been placed on the means of implementation.[34] Article 106 has provided an important instrument for dismantling special and exclusive rights protecting national monopolies in telecoms, postal services, energy and transport. Universal service has been the key to political compromises underlying liberalisation: under competitive conditions a vastly superior range and quality of services would be made available, compared to the previous situation of state monopolies.

Discussions and controversies have flourished, especially on the application of state aid rules. The problem has been largely resolved by the ECJ with its Altmark decision, under which public service compensation does not constitute state aid when certain standards are respected,[35] and by the Commission's subsequent efforts to design a comprehensive set of rules on compensation of public service obligations (with the Monti-Kroes package in 2005 and the Almunia package in 2012).[36] SEM rules also fully apply to the selection of the provider

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[33] Case C-270/12, United Kingdom vs. European Parliament and Council of the European Union [2014].

[34] Cf. European Commission (2011b) and, for the groundbreaking approach to the liberalisation of telecoms, Sauter (2015).

[35] Case C-280/00, Altmark Trans GmbH and Regierungspräsidium Magdeburg vs. Nahverkehrsgesellschaft Altmark GmbH, and Oberbundesanwalt beim Bundesverwaltungsgericht [2003]. For the Altmark exception to apply, there must be a service in the pursuit of a legitimate public interest objective; the parameters for compensation are set in advance, and they are based on a reasonable rate of return of an efficient undertaking. Cf. Sauter (2015).

[36] Cf. European Commission (2013).

of public services. The case law of the ECJ has consistently maintained that fundamental Treaty freedoms also apply to the provision of public services, placing constraints on the selection of providers. Accordingly, the exception for in-house provision has been narrowly construed and a set of principles has been developed for the selection of the providers. Recently, the new package of directives for public procurement of 2014 has included for the first e a specific directive on the award of concessions – setting for instance rules on their duration. [37]

The revised Article 14 TFEU has made the member states and the Union institutions jointly responsible "that such services operate on the basis of principles and conditions, particularly economic and financial conditions, which enable them to fulfil their mission"; it goes on to state that "the European Parliament and the Council, acting by means of regulations ... shall establish these principles and set these conditions without prejudice to the competence of Member States, in compliance with the Treaties, to provide, to commission and to fund such services". Thus, a paradoxical result of ten years of squabbling over the issue is that European institutions have acquired the power to regulate the matter; while Protocol 26 has reaffirmed the sole competence of the member states "to provide, commission and organise non-economic services of general interest" (Article 2).

(e) Establishment and company mobility

Thanks to the early recognition of direct effect to the Treaty freedoms under Articles 49 and 53, freedom of establishment represented an important advance in liberalisation in the IM well before the SEA. Two key ECJ decisions adapted the Cassis de Dijon test for restrictions to freedom of establishment (Gebhard, already mentioned) and the recognition of qualifications (Vlassopoulou),[38] opening the way to subsequent 'horizontal' liberalisation directives.[39]

Freedom of establishment, however, only goes so far as to allow the incoming entity to enter and operate without restrictions – subject to the safeguard of measures adopted on grounds of public policy or public health provided for by Article 52 TFEU – "under the conditions laid down for its own nationals by the law of the country where … establishment is effected".[40] In other words, freedom of establishment liberalises entry into domestic markets, thereby increasing competition in the markets defined by existing national rules, but does not entail *per se* either the mutual recognition or the harmonisation of those national rules. Therefore, in service markets, where significant restrictions still limit the free supply of cross-border services, freedom of establishment alone wouldn't have guaranteed full market integration; to this end, directives liberalising the provision of specific services, and eventually the Services Directive, were also needed.

The provision of certain services is subject in most countries to regulatory requirements and constraints on the quality and competence of the provider, natural or legal person. A major regulatory innovation has been the establishment of common licence arrangements – the 'European passport' – for the main categories of financial services, based on minimal

[37] Directive 2014/23/EU.

[38] Case C- 340/89 Vlassopoulou vs. Ministerium für Justiz, Bundes- u. Europaangelegenheiten Baden-Württemberg [1991].

[39] Directives 2005/36/EC and 2013/55/EU.

[40] Article 49 TFEU.

harmonisation of national licences. Under this system, an institution meeting the minimal prudential requirements (capital, reserves, quality of management, etc.) can set up branches and subsidiaries freely throughout the Union without further authorisation.[41]

On company mobility, the Treaty approach was predicated on outright hostility to companies moving the main centre of operation to another member state, but a number of ECJ decisions have opened broad breaches into restrictions on the free choice of legal seat by EU corporations. At the root of this contradiction lies a fundamental difference in national legal systems between those adhering to the so-called 'real seat' doctrine (e.g. France, Germany and Italy) whereby the legal seat of a company coincides with its headquarters and main centre of operations, and the 'incorporation' doctrine, whereby the legal seat is simply where the company was incorporated (adopted e.g. by the UK and the Netherlands).

Earlier ECJ decisions (i.e. Daily Mail and Cartesio)[42] had confirmed the power of national authorities to regulate companies maintaining their legal seat in the country. Therefore, they could legitimately impose restrictions on companies wishing to transfer of the main centre of operation while maintaining their legal seat (primary establishment) in the country of origin, could not prevent a company from converting into a company of another member state. Moreover, national authorities cannot require the winding up or liquidation of a company wishing to exit.

With Centros,[43] the ECJ went much further with regard to the freedom to combine primary and secondary establishment so as to minimise the costs and legal requirements of incorporation, while exercising its activities elsewhere. Centros was a private company incorporated in the UK, whose branch in Denmark was its only centre of activity. This arrangement had been designed to escape costly capital requirements under Danish law. The Danish registrar of companies refused to register the company's branch on grounds that it really was its main centre of activity. However, the ECJ ruled that the registrar's refusal violated freedom of establishment. It said that it wasn't a case of abuse since the rule that was being circumvented concerned the formation of the company and not the pursuit of certain trades. The decision has called into question the continuing applicability of the real seat doctrine; some have seen this decision as opening the door to a Delaware-style race to the bottom.

The Commission has been pondering what to do about this situation, but has been unable to decide on a legislative initiative to clarify matters. The issue is broader than the transfer of the legal seat, as it also involves questions of cross-border mergers and divisions.[44]

Resistance to making progress on this road is motivated by the potential impact on established forms of protection of workers' rights, e.g. the German system of workers' participation in

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[41] The system has now been extended to virtually all institutions offering financial and investment services: starting in the 1990s with the banking and insurance directives and private investment funds (UCITS), and continuing in the 2000s with 'occupational' pension funds and alternative investment funds (hedge funds and private equity), security issuance (the prospectus directive), and investment services – with directives covering stock exchanges (MiFID) and post-trading actors (CSDR).

[42] Respectively Case 81/87, The Queen v H. M. Treasury and Commissioners of Inland Revenue, ex parte Daily Mail and General Trust plc. [1988] and Case C-201/06, Commission vs. France [2008].

[43] Case C-212/97, Centros Ltd vs. Erhvervs- og Selskabsstyrelsen [1999].

[44] For a comprehensive review of these matters, see Schmidt (2016).

corporate supervisory boards. The European Company Statute is a case in point: the eventual agreement, reached after twenty years of stalemate, includes the regulation providing for limited harmonisation of corporate rules (e.g. minimum capital, the choice of dual vs. single board, the transfer of legal seat) [45] and a tightly prescriptive Directive on workers participation.[46] The European company may be created only by transformation of existing companies, rather than creation of a new company; and the legal seat can be transferred but must coincide with the 'central administration' (i.e. the main centre of operation). In any event, the European Company may be constituted only after reaching an agreement on a model for worker involvement in management decisions, entailing the 'grandfathering' of existing statutory protections. In the event of a transfer of the legal seat to another country, the transfer project must indicate the consequences for workers.

Similarly, the Takeover Bid Directive[47] was emasculated in frantic last-minute negotiations with provisions allowing member states and individual companies not to apply its key provisions – i.e. the 'passivity rule' preventing the board from adopting defensive measures without the consent of shareholders, and the 'breakthrough rule', suspending all limitations on the exercise of voting rights by shareholders on the occasion of the bid.

All this draws attention to the limits placed on the integration process by rigid labour market institutions: as long as labour is protected by rigid hiring and firing rules, then mobility of capital for direct investment will likely be restrained, so as to limit cross-border mergers and acquisitions that may endanger existing protections. As convincingly argued by Hall and Soskice (2001), changes in market institutions are sometimes complicated by complementarities between them; changing one in isolation therefore becomes quite difficult.

(f) On the posting of workers

A source of persistent tension between free movement and national protective arrangements is the Posted Workers Directive;[48] it impinges directly on the most sensitive issue of labour mobility, which in the European environment of rigid labour markets remains deeply unpopular and is strongly resisted.

In Rush Portuguesa[49] the ECJ affirmed that Articles 56 and 57 TFEU "preclude a Member State from prohibiting a person providing services established in another Member State from moving freely on its territory with all of his staff", notably including non-EU nationals, to carry out a service contract. Posted workers cannot seek access to the host labour market and must return to the place of origin or residence once the contract is completed. The decision, however, maintained that Union law does not preclude member states from extending their own labour legislation, or collective labour agreements, to workers employed temporarily in the country. The directive went further and removed that discretion, establishing instead that the member state must apply to posted workers a 'nucleus of mandatory rules' relating to the minimum

[45] Regulation (EC) 2157/2001.

[46] Directive 2001/86/EC.

[47] Directive 2004/25/EC.

[48] Directive 96/71/EC.

[49] Case C-113/89, Rush Portuguesa Ld. vs. Office national d'immigration [1990].

wage, working time, and equal treatment, and only collective agreements satisfying certain conditions.

Then the Laval dispute arose, setting a Latvian firm that had won a contract in Sweden against local labour unions. The ECJ ruled that the host state could only insist on the application of national labour laws for matters exhaustively listed in Article 3(1) of the Directive; this did not cover certain supplements and insurance premiums, and in addition Sweden had failed to establish the minimum wage in that activity with the procedure of the directive.[50] More broadly, local unions' demands fell outside the scope of the directive and, therefore, industrial action to enforce national collective agreements was incompatible with Article 56 TFEU.

Viking was a Finnish company wishing to reflag to reduce labour costs; the decision was met with a seamen's union strike. The ECJ again ruled that the trade union's proposed strike was a restriction on freedom of establishment. It stated that, while in principle action to protect the jobs and conditions of employment by union members liable to be affected by reflagging could be justified in order to protect workers, such a view would no longer be valid if it were established that the jobs and employment conditions were not jeopardised or threatened in practice.[51]

These cases have exposed deep fault lines between the SEM and the social dimension at national level (Monti 2010). With the progressive liberalisation of services, the divergent social and employment conditions in member states offer fresh opportunities to reduce labour costs, calling into the line of fire the more generous protections. The implication that union strike rules would have to adapt to SEM requirements invites enormous controversy and opposition.

Following the Monti Report, the Commission undertook to propose revisions to the Posted Workers Directive, e.g. by setting time limits (twenty four months) after which the host country's remuneration and other labour laws would automatically apply to the contract in question, and excluding temporary agencies posting workers from the application of the directive. However, perhaps predictably, the proposal met with strong opposition from East European member states: fourteen chambers of national parliaments from eleven member states issued a 'yellow card' against the Commission's proposal, for violating subsidiarity (under Treaty Protocol 2).

3. The Economic Impact of the Single European Market

Almost thirty years have elapsed since the enactment of the SEA, which brought about a jump in integration in the EU through the creation of the SEM. The preceding exposé shows the enormous progress achieved through legislation now covering all the main sectors of activity, as well as horizontal inducements for innovation and new technologies. And yet, the performance of the EU economy remains far from satisfactory and the legacy of the economic and financial crisis still looms large. Output and productivity growth have been unsatisfactory, unemployment remains high in a number of countries, investment levels have not recovered to pre-crisis levels, and financial markets are fragmented by confidence factors,

[50] Case 341/05.

[51] Case C-438/05.

reflecting large sovereign debts and dubious capital and asset positions in parts of the banking system (OECD 2016).

Of course, the SEM policies cannot be held responsible for all that does not work, nor could they claim all the merit for what seemingly works well in economic integration. The creation of the SEM was expected to bring about distinct economic benefits on a number of fronts, including cost reductions through the elimination of border tariffs and regulatory barriers; economies of scale, as companies restructure and merge to exploit the larger market size and optimise their cross-border productive structure and logistics; efficiency increases due to stiffer competition; increased labour and capital mobility for cross-border direct investment; and lower financial transaction costs as a result of the liberalisation of capital flows and greater financial integration, possibly with an increased role of capital markets in the direct financing of business (equity and bonds). The euro was expected to boost the beneficial effects on all of these fronts, thanks to full price transparency.

While there has been progress on all of these fronts, the attendant benefits seem to have been less than hoped for and, moreover, to have affected some countries, regions and activities quite diversely. This was to be expected. Large countries are better positioned to gain from economies of scale, given the larger size of their companies, while small open economies would benefit more from the reduction in transaction costs engendered by falling barriers to trade. Adjustment costs would be higher in countries with closed markets and protected industries. The twin forces of globalisation and technical change have also played a major role in changing the economic environment, magnifying the different capacities of EU member states to meet the challenge. Again, company size significantly influences the ability to manage new technologies and distributed production organisations made possible by globalisation.

Labour market flexibility is a critical variable in determining a country's ability to meet the challenge of a rapidly changing economic environment. The labour market economic literature describes the differing levels of efficiency of four labour market protective arrangements, observed in managing labour relocations when companies and activities in Europe need restructuring: the Anglo-Saxon flexible model, the flexi-security model of Nordic European countries, the consensual corporatist model practised in Germany and other continental countries, and the 'Southern' model (Sapir 2003). The last one is characterised by the rigid defence of existing jobs and the maximum resistance to industrial restructuring, leading most often to chronic unemployment and public sector deficits to support ailing companies and no longer viable jobs. More generally, the benefits of market opening measures can be profoundly affected by domestic policies, which can aid competitive adjustments or tame them with countervailing protective measures.

Against this background, disentangling the specific economic impact of the SEM is almost impossible. A less ambitious substitute is to examine the degree of success of SEM polices in fostering market opening reforms in EU countries on the one hand, to review countries' growth and productivity performance to identify areas of more visible weakness, on the other.

(a) Market opening under Single Market legislation

Over the past three decades progress in enacting market opening legislation in the SEM has been impressive, as has been shown, and most economic activities are now covered by SEM rules. A new ambitious strategy for the digital market aims to extend market opening to online transactions, which would in itself represent a leap in market integration.

However, implementation of legislation has been uneven, as shown by extensive reviews of remaining SEM barriers undertaken by the OECD, the European Commission and private analysts (cf. Europe Economics 2013, European Commission 2015(b) and (c), Ilzkovitz et al. 2007, OECD 2016, Pelkmans 2012).

Mutual recognition plays an important role in the functioning of the SEM for both manufactured products (covering about one quarter of intra-EU trade) and services, especially in the recognition of qualifications. However, its practical implementation is hampered by legal uncertainties, bureaucratic resistance and a lack of awareness among individuals, companies and public administrations – despite strengthened efforts to streamline its application with Regulation (EC) 764/2008. The services directive has not yet succeeded in clearing the ground of excessive or outright illegal authorisation requirements to start businesses, limitations to the duration of authorisations and requirements to register with local chambers or professional associations. Extensive restrictions are still reported for legal, accounting, engineering and architect services. The implementation of procurement directives has remained uneven, with a number of countries falling well below average in the share of public procurement contacts published for open bidding. Retail establishment rules remain very restrictive in some countries. Lack of adequate physical interconnections hampers the establishment of a functioning SEM for energy. Excessive red tape still impedes market entry across the board.

The quality of regulation is also not always satisfactory, imposing sometimes disproportionate burdens on businesses without adequate evaluation of expected benefits, e.g. the REACH regulation for tracing chemical products or the rules for clinical trials. The Commission's efforts to base new legislation on adequate impact assessment have often been frustrated, owing to the Council's and Parliament's lack of willingness to cooperate. Regulatory instability has been high, in response to contingent political demands by the member states, creating uncertainty and higher risks for investors, especially for projects with long time-horizons.

OECD analyses have also highlighted the adverse impact of 'regulatory creep' – national actions that add to the burden of regulation by adding unnecessary requirements ('gold plating') or failing to remove inconsistent higher level regulations. Regulatory fragmentation and disproportionate restrictions across the SEM continue to hamper the opportunity to expand business in specific sectors, notably in the transport sector overburdened by load and size limits, traffic restrictions, local restrictions in ports and complex administrative procedures. In rail transport, lack of interoperability between systems holds back cross-border freight.

Several barriers continue to impede the development of e-commerce – which will hopefully be dealt with by the new programme for the Digital Single Market. In this regard, data localisation requirements that force companies to store and process data in servers physically located inside particular member states are very detrimental to the development and growth of new businesses. Some member states are also unduly restricting or forbidding the online sale of certain products, e.g. veterinary products.

An issue that deserves continuing attention is the limited cross-border mobility of productive factors, labour and capital. Labour mobility in the EU remains low, reflecting cultural and linguistic barriers on the one hand, and the lack of harmonisation of professional qualifications and supplementary pension entitlements on the other (OECD 2016, Dhéret et al. 2013, Ilzkovitz et al. 2007).

Under the revised professional qualifications directive, member states are now held to stricter requirements of justification when they want to limit access to professional activities, but the number of recognitions remains low, relative to employment, and the process of recognition appears slow and cumbersome, with great variation amongst member states. A paradoxical result of differing rules is that nationals from countries with a more liberal regime of recognition may confront greater hurdles when trying to enter the market of another country with a more restrictive regime. For example, engineering is not a regulated profession in some member states while in others is regulated through licensing.

The Union also seems rather ineffective at attracting high-skilled personnel from third-country nationals. Effective deployment of the new European Professional Card (for EU residents) and the Blue Card scheme (for third-country nationals) could improve matters on all these fronts. The risk of losing supplementary pension rights and long vesting periods for acquiring new rights are strong disincentives to seek work abroad; Directive 2014/50/EU (to be transposed by 2018) improves matters somewhat by establishing certain minimum standards for the protection of mobile workers' rights.

In general, differing protections of unemployment and health risks and low portability of attendant rights represent a major barrier to the free movement of labour. On this, Pelkmans (2012) called attention to the fact that Article 3 TEU includes among the founding values of the Union free movement of 'persons', rather than 'workers'; that Article 45 TFEU has been regarded as less of a priority by the Council and Parliament; and that the workers employed abroad will operate normally under a broad form of host-country control, whose effect is that of protecting national labour market regulations. This is the main motivation behind the Parliaments' rejection of the country-of-origin principle in the Services Directive, which was included in the Commission's original proposal. It is also the reason behind growing demands to change the Posted Workers Directive to include stronger enforcement of local (host-country) working conditions.

Of course, the preservation of national protective systems is inconsistent with the creation of an integrated market for labour. An important consequence, sometimes overlooked by SEM analysts, is that whenever SEM legislation comes too close to challenging rigid labour market institutions, implementation may become very slow – as has often been the case with free establishment, which still largely relies on host country control for business conduct rules and the free cross-border supply of services (on this see also Pelkmans 2008).

This is also in all likelihood an important explanation for the general disfavour for unfettered (real) capital mobility, as reflected in the treaty and legislative provisions on company mobility, as has been discussed. This has not prevented a significant increase in intra-EU direct investment, within a global trend of strongly rising FDI flows, as well as cross-border M&A operations. Cross-border flows were especially significant in the early years of the SEM programme and, later on, for the new entrants with the 2004 enlargement, reflecting the outsourcing of manufacturing activity and the acquisition of substantial stakes in domestic banks by EU-15 corporations. However, important components of the corporate structure, especially in the EU-15, remain closed to foreign acquisitions, e.g. in the network utility services, where in some member states the state still holds large stakes in national monopolies and foreign acquisitions of incumbent 'champions' would be discouraged.

Financial market remains fragmented along national lines as a result of the financial crises in 2008-09 and 2011-12, which have left a legacy of high public and private debts, as well as lack of confidence in the sovereigns and the banking systems of the southern periphery of the euro area. Banking Union, already quite advanced with the establishment of the Single Supervisory System and the Single Resolution Mechanism, and the ongoing project for the creation of an effective Capital Market Union, are expected to remove these market segmentations, which for the time being still play a significant role in constraining SME access to financing and depressing growth.

(b) Economic effects of the Single European Market

The economic literature generally agrees that the SEM has had a positive effect on the economy of its members, although there is wide disagreement on quantification.

Strong positive effects are evident in intra-EU trade for goods (Eichengreen and Boltho 2008), which between 1992 and 2012 increased from 12 to 22% of GDP; the increase had been even stronger in the preceding decades, characterised by intensive trade liberalisation measures internationally, and actually slowed down afterwards (Vetter 2013). It has been estimated that since 1960 exports and imports within the Union have climbed to a level 8% higher than they would have been without the SEM (Straathof et al. 2008). Fournier et al. (2015) have estimated an overall impact of accession to the European Economic Area of roughly 60% increase in trade intensity; however, they also find that regulatory restrictions and regulatory heterogeneity still represent an important impediment to trade.

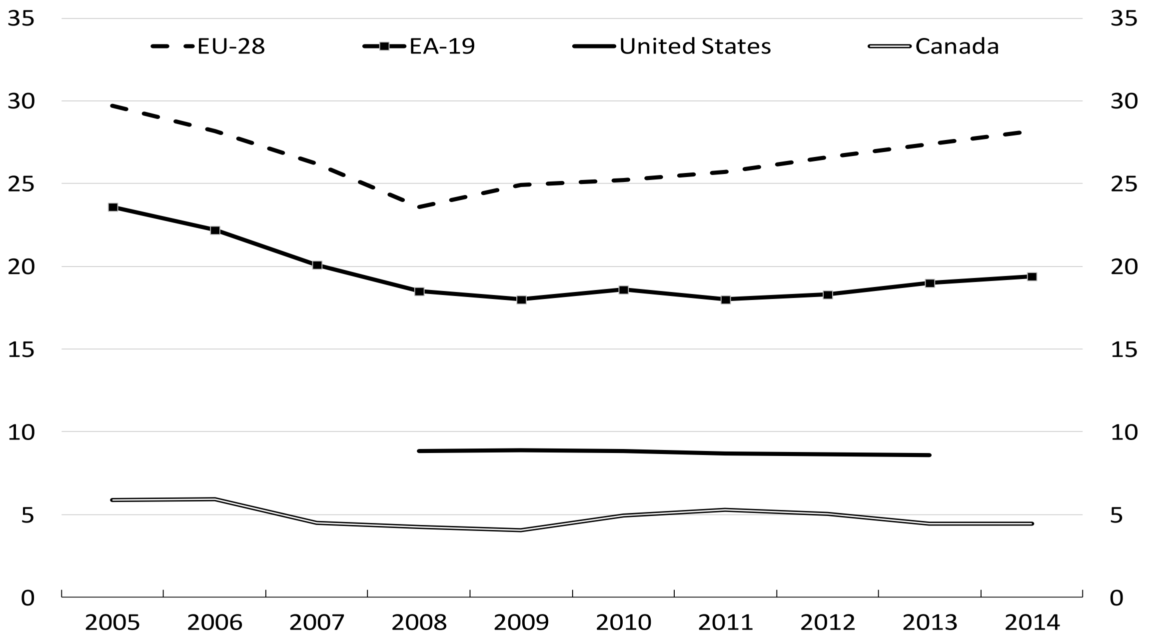
The numbers are much smaller for trade in services, which represent about 6% of Union GDP, but have shown steady increases in recent years, with little adverse impact from the twin crises of the past decade. Business services have been one of the most dynamic components.

In the 2000s, intra-EU trade between EU-15 countries has remained unchanged at around 20% of GDP, while strong increases were observed for the incoming EU-13 countries; thus, in recent years the latter countries account for much of the trade creation in the SEM (European Commission 2015c).

Foreign direct investment (FDI) has been the most important driver of internationalisation and integration of the European economy, with yearly flows rising from around 1% of GDP in the 1980s to around 5% of GDP till the financial crisis. FDI inflows have also represented an important component of total fixed capital formation, some 10%, with a peak of 40% in 2000. The launch of the SEM programme and the two enlargements (in 1995 and 2004) resulted in substantial anticipation effects, which subsided once the main integration steps were accomplished. The increasing share of intra-EU FDI flows in total flows suggests that the SEM has played a role; indeed, in the middle of the 1990s and the middle of the 2000s, the share of intra-EU-15 flows rose from around 50% to 68% of total FDI outflows, and to 78% for FDI inflows (Ilzkovitz et al. 2007). As with trade, the financial crises have taken a heavy toll for EU-15 FDI investment flows, while those to the EU-13 (new entrants) have been fairly steady. The latter have been dominated by mergers and acquisitions of existing companies, while green-field investment has been more important for the EU-15.

The degree of integration is normally gauged by the observed degree of convergence of prices, wages and productivity. The aggregate price level convergence has slowly improved through the 1990s and the 2000s until the financial crisis; afterwards, it stabilised in the euro area and has even gone into reverse in the EU-28, probably reflecting exchange rate adjustments between the euro and the non-euro currencies (Chart 1). However, as may be seen, price dispersion remains well above that observed for the United States and Canada – confirming once again that integration in the SEM still is still far from fulfilling its potential.

Figure 1. Aggregate price level convergence (coefficient of variation, %)



The coefficient of variation indicates the extent of variability relative to the mean of a series. Here the series shown are the price level index of household final consumption expenditure for the EU-28 and EA-19, the implicit regional price deflator for the US and the intercity index of price differentials of consumer goods and services for Canada.
Source: OECD Economic Surveys: European Union 2016.

Wage data show increased convergence within the EU-15 form the early 90s, and a considerable increase in dispersion with the enlargement to the EU-13 in the 2000s (Europe Economics 2013).

Financial services show greater variation in the covariance index, with a rapid convergence between the 1970s and the late 1980s, then a sharp increase in divergence until 1993-4, followed by a sharp decline through 1997, and mildly increasing dispersion up to the middle of the 2000s. The explanation of this greater variability may perhaps lie in the sharp movements in exchange rates in the early 1990s, followed by the inception of the euro. It is not unreasonable to think that these momentous changes may have affected the remuneration of staff in the financial services industry, with larger gains in the financial centres. In any events, wage dispersion remains substantial and seems to go well beyond what could be expected in a well-integrated SEM.

Productivity, on the other hand, did not converge at all, and in fact showed growing divergences within industries and across countries, especially within the euro area (cf. total factor productivity indexes in Figure 2, upper quadrant). This seems to have been mainly the result of applying one monetary policy to areas with different price and cost dynamics. On the one hand, the inception of the euro all but eliminated risk premia over borrowing in higher inflation countries, whose borrowers could thus get loans at negative real interest rates for low quality projects. On the other hand, the rise in the relative price of manufactured products in higher inflation countries encourage a shift in the allocation of resources towards services and construction, typically characterised by lower productivity.

Table 3 reports some sectoral data of productivity growth in the EU and the US in 1980-95 and 1995-2005. As may be seen, the labour and total factor productivity (TFP) slowed down between the two periods in the Union and accelerated in the US. The disaggregated data for labour productivity indicate that the main component of the gap with the US was in distribution (retail) services, where in the US fierce competition was set in motion by the application of the new ICT technologies to logistics, parcel delivery and inventory management. The last line of the table brings together the contributions to labour productivity increases of technology – from changing labour skills, ICT capital per hour worked and TFP. This highlights the growing technology gap that has developed relative to the US, in a period of dramatic technological change, owing to insufficient competition and closed markets in the Union.

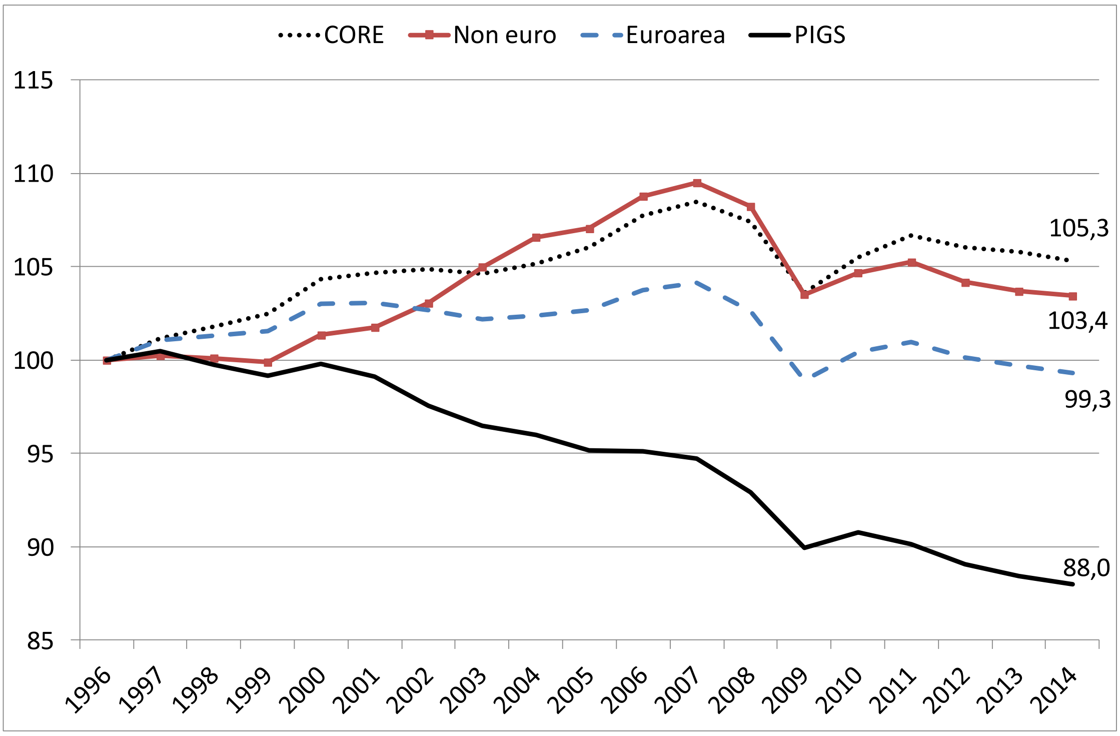
Table 3. Productivity growth in the market economy (annual average growth rates, %)

	EU		**US**	
	1980-1995	**1995-2005**	**1980-1995**	**1995-2005**
Labour productivity	2.5	1.5	1.9	2.9
TFP	1.0	0.3	0.7	1.3
Market services labour productivity	1.4	1.0	1.5	3.0
of which due to:				
distribution services	1.1	0.7	1.2	1.5
finance and business services	0.2	0.4	0.2	0.5
personal services	-0.1	-0.1	0.2	0.2
Contribution of the knowledge economy to labour productivity growth	1.7	1.1	1.6	2.6

EU refers to: Austria, Belgium, Denmark, Finland, France, Germany, Italy, Netherlands, Spain and UK. The contribution to the knowledge economy includes TFP, improvement in labour skills and ICT capital per hour worked.

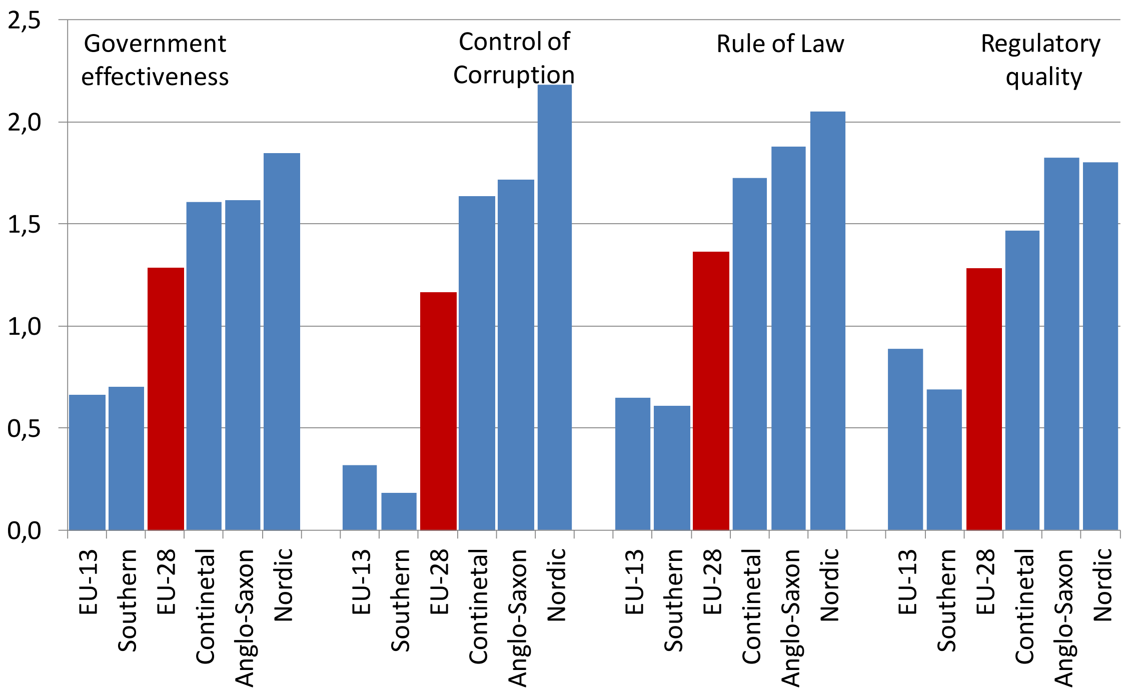
Source: Timmer M.P., R. Inklaar, M. O'Mahony and B. van Ark (2010), *Economic Growth in Europe*, Cambridge University Press.

Figure 2a. Total factor productivity (1996=100)



Source: The Conference Board.

Figure 2b. Quality of institutions (2014, %)



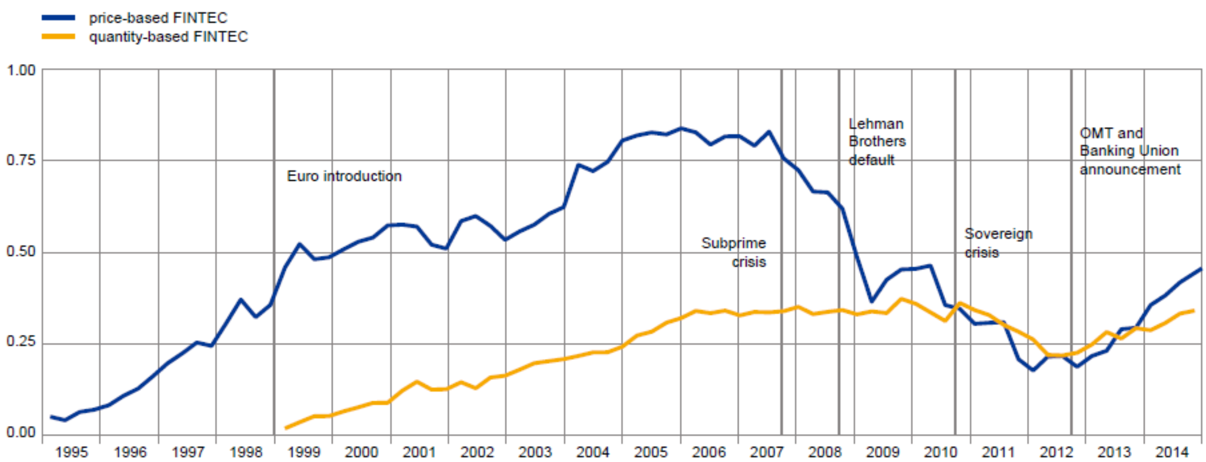
Estimate of governance ranges from approximately -2.5 (weak) to 2.5 (strong) governance performance.
Source: Our updating and reclassification of figure from Boltho and Carlin (2012).

As a result, labour costs and competitive conditions showed large and increasing divergences, leading to growing external imbalances and, eventually, to Europe-specific acute financial instability. This must reflect, in turn, structural divergences in national macro-economic policies and national protections able to insulate markets and industries from the competitive pressures stemming from the SEM. Thus, the ultimate obstacle to reaping the full benefits of the SEM lie in national economic policies sustaining inflation differentials and market segmentations, in direct contrast to integration in the SEM.

The increasingly divergent course of national policies within the euro area is also confirmed by observed changes in the quality of institutions, as measured by World Bank indicators (Figure 2, lower quadrant). The figure reports four indicators, namely respect of the rule of law; the control of corruption; the quality of regulation; and the effectiveness of government, and for each indicator compares the 'core' and the 'periphery' (PIIGS) of the euro area.[52] The striking feature is that the periphery not only had a worse quality of institutions than the core from the start, but the gap widened over time.

Further evidence pointing in the same direction is provided by the new composite indicators of financial integration developed by the ECB (FINTECs), focusing on the four most important segments of the financial markets, namely money, bonds, equity and banking markets (ECB 2015); the indicators, which separately cover prices (interest rates) and quantities (portfolio flows), are reported in Figure 3. As may be seen, the price-based indicator shows higher volatility, rising continuously from the second part of the 1990s (clearly, in anticipation of monetary union), falling precipitously with the global financial crisis (2008-09) and crushing with the euro area sovereign debt crisis (2010-12). It still is well below the pre-crisis level. The quantity-based indicator appears more stable; it is interesting that it flattened, but did not fall after the global financial crisis, while it did recede after the sovereign debt crisis (which indeed saw an interruption of money market and interbank financial flows between core and periphery). It is now slowly recovering.

Figure 3. Price- and quantity-based FINTECs



FINTEC stands for FINancial INTEgration Composite. The price-based FINTEC aggregates ten indicators covering the period 1995-Q1 – 2014-Q4, and the quantity-based FINTEC aggregates five indicators available from the 1999-Q1 to the 2014-Q3. For a detailed description of the FINTEC and its input data, see Statistical Annex of ECB (2015).
Source: ECB (2015).

[52] The core includes Austria, Belgium, Finland, France, Germany and the Netherlands; the periphery (PIGS), Portugal, Italy, Greece and Spain.

Banking Union has been successful in turning both indicators upward again; however, the ECB policies of quantitative easing may be overstating the return of integration to the extent that they artificially swell asset prices and depress yields on riskier assets from the periphery. In this regard, the Capital Markets Union initiatives can play a complementary role in fostering truly integrated capital markets by pushing the development of the cross-border bond and equity market segments, thus increasing the scope of private risk sharing in cushioning the impact of new idiosyncratic financial shocks.

While market opening and integration are expected to set in motion beneficial micro-economic effects – mainly by increasing competitive pressures and improving resource allocation – a number of factors previously described may impede the translation of these stimuli into improved macro-economic performance.

The Cecchini Report (1988) held the promise that the removal of frontier controls, the liberalisation of public procurement and financial services, and the supply effects deriving from market responses to the new competitive environment, would raise EU-12 GDP by between 4.25 and 6.5% and create 2 million jobs. Most subsequent analyses have come to the conclusion that the actual outcome was smaller, around 2% (Vetter 2013, Ilzkovitz et al. 2007); but higher estimates have not been absent. Most notably, Eichengreen and Boltho (2008) gauged that European integration has added at least 5% of extra GDP growth, although they recognise that much trade opening would probably have happened anyway.

Mariniello et al. (2015) pointed out two developments that may help explain why the outcome has fallen short of expectations. One is the dramatic increase in the share of the economy of services, which are largely non-tradables, and now typically represent some 70% or more of advanced economies' GDP. The other, already recalled, is that national policies in many domains have not been supportive of the goal of integration. They mention in this regard undue rents, rigid labour market rules, industrial policies supporting national champions, including monopolistic supply of network services, and cumbersome procedures to set up new businesses, among the main factors hampering the competitive process and its 'creative destruction' dynamic effects.

They point out the fact that SMEs are often protected from the competitive forces within the SEM as a potentially counterproductive policy, arguing that they could not otherwise survive. However, the question arises as to whether these policies are leading to sub-optimal results, e.g. by reducing the ability to exploit economies of scale. Similarly, inefficient regulation of network utility services (e.g. in telecoms) may create fresh market segmentations, rather than removing those already there.

Conclusions

Over the past thirty years, the SEM has made impressive progress, growing to cover the main economic activities, from manufactured goods to all categories of services, network utilities and public services, public procurement and the recognition of professional qualifications, as well as the market for codified technology, that for long lagged behind. A new ambitious initiative now aims to establish a fully fledged online digital market.

Implementation, however, has been wanting. Globalisation, technological change and the financial crises have impoverished the working classes and seemingly drained all appetite for further market opening. National policies have all too often been insufficiently supportive, if not downright hostile, towards the goal of market integration. As a result, the past ten years have seen little progress in market opening within the Union, even in areas where there would be low-hanging fruit to pick – e.g. the completion of the SEM for natural gas and electricity. The Monti Report (2010) has called attention to the need to address social resistance to further integration by aiming for a more acceptable equilibrium between market opening and the protection of the rights and interests of working classes, thus re-establishing the full meaning of the Union's goal of a highly competitive *social* market economy.

The ambition to push forward the goal of a *genuine* Single European Market – harnessing the joint commitment of EU institutions and national governments and administrations – has not been abandoned, and still finds powerful advocates in academia (cf. Pelkmans 2016) as well as the European Parliament (see the High Level Panel of Experts 2016). But resuming progress will continue to be an uphill battle as long as the Union fails to lift its growth rates and show greater ability to combat unemployment and bring relief to the standards of living of working classes.

Herein lies a paradox: while the SEM would in itself be a powerful engine for higher growth and better employment prospects, without higher growth it is not likely to find sufficient support among European citizens. This increases the risk that protectionism will return and that the Union will slide into a phase of regression.

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CEPS, Place du Congrès 1, B-1000 Brussels, Belgium
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