



**SOCIAL
DEVELOPMENTS
IN THE EUROPEAN
UNION**



2005

EDITED BY CHRISTOPHE DEGRYSE AND PHILIPPE POCHET

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Christophe Degryse and Philippe Pochet

Seventh annual report

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European Trade Union Institute
for Research, Education and Health and Safety (ETUI-REHS)
Observatoire social européen (OSE)
The National Institute for Working Life and
The Swedish Trade Unions in Co-operation (SALTSA)

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Preface

Rarely has the European project been reassessed to the extent that it was in 2005. The rejection of the draft constitutional Treaty in France and the Netherlands prompted a whole raft of questions and controversies about the political, economic and social model being pursued. What model - but also what project - should that be, and what are its future prospects? Is the Europe of the founding fathers a thing of the past now, or will enlargement and the debate about the constitution force our political leaders to go back to basics?

The main issues under debate in 2005 – the constitution, accession negotiations with Turkey and Croatia, the 2007-2013 financial perspectives, the European social model, the future of the CAP – probe the very identity of the Union, and likewise the capacity of political, economic and social stakeholders to carry forward a coherent project for this political entity suddenly plunged into globalisation. In this new context, is Europe a fortress besieged from all sides, or is it the prototype of a different form of globalisation which seeks to expand and strengthen a specific social model?

There is no ready answer to this question; the answer will come from those responsible for the project. But expectations and hopes are running high among Europe's citizens. And many people in the wider world are vesting their hopes in the success of the European project. Thus there is a need to create European and transnational forums for debate, to encourage dialogue, disseminate information and engage in analysis so as to influence political decision-making.

To this end, the European Trade Union Institute and the Swedish trade union research programme SALTSA have once again joined forces with the *Observatoire social européen* to produce an assessment of European social policy for the year 2005. This volume, published in French and English, is aimed at a wide readership and seeks to promote reflection and debate about the state of social Europe and its future prospects. We hope you will enjoy reading it.

Maria Jepsen (ETUI-REHS), Lars Magnusson (SALTSA),
Philippe Pochet (OSE) and Christophe Degryse.

Foreword

The previous year, 2004, had been particularly eventful. European Union (EU) enlargement finally came about, and the draft constitutional Treaty was adopted by the Heads of State and Government. These two major events, it was thought, were set to relaunch European integration in both senses of the term: geographical widening and political deepening.

In complete contrast, 2005 was a year of setbacks and reappraisals. Everything appeared to be under control at the start of the year, when the highly experienced Prime Minister of Luxembourg, Jean-Claude Juncker, began his presidency by addressing three major issues: amending the Stability and Growth Pact, reviewing the Lisbon strategy and seeking a political agreement on the financial perspectives for 2007-2013. All three of these topics were supposed to build on the headway made in 2004 but were thrown off course by current events. Two national referendums, in late May (France) and early June (Netherlands), on the draft European constitutional Treaty disrupted discussion and sent an icy blast through the European edifice, slamming doors and windows behind it. The United Kingdom took over the EU presidency on 1 July, following an especially tense European Council meeting at which profound differences over the budget became still further entrenched, reflecting divergent views on Union policies and their level of ambition, as well as on how to share out the costs of enlargement. The European credentials of British Prime Minister Tony Blair, accused of being responsible for the unsuccessful outcome of the European Council meeting in June, were on the line. Mr Blair attempted to make amends with a profession of faith to the European Parliament at the beginning of his presidency, and by holding an informal summit in

October, devoted to the future of the “European social model”. In political terms, the significance of that summit was far from clear then and will become even less clear as time goes by. The UK presidency managed to clinch a last-minute success as it drew to a close in December, when the European Council approved the financial perspectives for 2007-2013. Some observers believe that this agreement will breathe new life into a Europe which is in very poor shape; it does at the very least prevent the EU from plunging into a spiral of setbacks and crises.

At national level, 2005 saw important elections take place in several countries. In May, the British Prime Minister won a third term in office, while in September Chancellor Schröder of Germany suffered a relative defeat at the hands of Angela Merkel, who was appointed Chancellor in November at the head of a CDU-SPD grand coalition. Voting likewise took place in Poland, Denmark, Portugal and Bulgaria. Regional elections held in Italy served to weaken Prime Minister Silvio Berlusconi one year ahead of the 2006 parliamentary elections: Italy is described in various quarters as the sick country of Europe. There were no elections in France, but the referendum on the draft constitutional Treaty considerably weakened President Jacques Chirac, who decided to carry out an extensive ministerial reshuffle. Furthermore, the prospect of the 2007 presidential election constantly looms large in French political circles. Spain was the only “large” EU country to experience a stable year politically. In February, a sizeable majority of the Spanish people came out in favour of the draft constitutional Treaty. In addition, Spain’s rate of economic growth throughout the year was exceptional (around 3.5%), and its unemployment rate fell dramatically, dipping below the European average at the end of the year after having been above 22% ten years ago. With the exception of the United Kingdom and Spain, it could be said that most of the “large” countries of the Union – Germany, France, Italy and Poland – experienced a period of uncertainty in 2005.

In this introduction we intend to recall the most significant events which took place on the political scene in 2005: the rejection of the draft constitutional Treaty in France and the Netherlands, the eleventh-hour agreement on the 2007-2013 budget, discussion of the European social model, the reform of the Stability and Growth Pact, the review of

the Lisbon strategy and the question of further enlargement (Turkey, Croatia). Then, turning to social policy matters, we shall look at three issues which we believe are symptomatic of the changes underway at European level: the “better regulation” initiative of the Commission President, Mr Barroso, developments in the European social dialogue, and the open method of coordination as applied to pensions.

1. The European constitution

The ink used by the Heads of State and Government to sign the draft constitutional Treaty was barely dry when it became evident that the process of ratifying the new text would be a lengthy obstacle course, particularly in countries having opted to hold referendums. In France, political debate was intense in the run-up to 29 May and, unlike the discussions prior to the Maastricht Treaty, revolved not so much around the real or presumed progress inherent in the new text as around the nature of the European Union itself – its foundations, political aspirations and borders. Very briefly, two extreme positions can be detected in this debate: one, on the left, rejecting the liberal economic foundations underpinning the European edifice; the other, on the right, taking issue with the supranational nature of this edifice and with a preference for national sovereignty. The debate in France and the ensuing referendum result indicate that part of the French population challenges – or at least has grave doubts about – these two historical components of the European bedrock: economic liberalism and a certain form of supranationalism.

As concerns the Netherlands, the possibility that the draft constitutional Treaty might be rejected by the people came to light relatively late in the day (only really in April, with the referendum scheduled for 1 June). On the one hand, the political debate – in the broad sense of the term – was less wide-ranging than in France; on the other, according to many observers, the French “no” campaign had a knock-on effect on Dutch public opinion, especially in the last few weeks and days. Some of the “no” arguments in the Netherlands were of course similar to those of the French campaign, such as the country’s loss of influence in an enlarged Europe, the prospect of Turkey’s accession, red-tape and the absence of a social Europe. Mainly, however, other more specific

elements came to the fore: the fact that the guilder was undervalued when it entered the euro, the country's excessive contribution to the Community budget, the impression that immigration was out of control, etc. The deciding factor seems to have been not so much the constitution as such, about which there was relatively little debate, as a general feeling of disenchantment among large segments of the population. Moreover, economic liberalism as the bedrock of Europe was not contested in anything like the same way as in France: whilst the "Bolkestein" directive for example figured prominently in the debate in France, it was totally absent from discussions in the Netherlands where it was on the whole unproblematical. It seems that the malaise in both countries also had to do with national politics and with the growing divide between the political elite and the electorate. But it would be over-simplistic to dismiss on these grounds the mounting and sometimes contradictory lack of comprehension about the purpose of European integration. The victory of the "no" camp was in the main a defeat of the "yes" camp, in that the champions of the constitutional Treaty were incapable of putting across coherent arguments in its favour.

Be that as it may, the dual rejection of the draft Treaty ushered in a period of great uncertainty throughout the EU, as shown by the huge amount of confusion over whether to press ahead with the ratification procedures in the other Member States or whether to call a halt. Was the constitution dead or not? If so, should it be replaced and by what? In the absence of an answer, the Heads of State and Government decreed a pause for reflection in all countries. A wide variety of scenarios was still being aired at the beginning of 2006: bringing into force certain aspects of the draft constitutional Treaty, renegotiating it in full, adding to it a declaration on the social dimension of the Union, purely and simply abandoning it, launching an enhanced "mini-Europe" consisting of just a few countries, etc. This proliferation of scenarios raised fears of a collective torpor rather than a pause, especially in the absence of leadership among the Member States and at the Commission – so much so that, after the German elections in September, many people felt it would be advisable to await the French presidential

election of 2007 for matters to become clearer. (To follow these debates in more detail, see the *Tomorrow Europe* newsletter (¹).

2. The financial perspectives

It was in this highly charged atmosphere that the Union suffered a second major setback, at the European Council on 16-17 June, concerning the budget for 2007-2013. Even though the Luxembourg presidency had put several compromise formulas before the Heads of State and Government, no agreement was reached. The two major stumbling-blocks were the “British rebate” and agricultural expenditure. UK Prime Minister Blair, who rejected proposals to freeze the rebate obtained by Mrs Thatcher in 1984, demanded that the very structure of the European budget be overhauled from top to bottom. He argued that the existing structure attaches excessive importance to agriculture, to the detriment of research, innovation and education. The French President, Jacques Chirac, for his part defended the agreement reached by the European Council in October 2002, whereby farm spending was set in stone until 2013. Beyond this very public “duel”, other countries were waiting in the wings, determined to reduce their own contributions to the European budget (Germany, Netherlands, Sweden); others still were afraid that the Community’s cohesion policy would pay the price for the skirmish between France and Britain (the central and eastern European countries). Drawing on all the tricks of the negotiating trade, the UK presidency put forward a fresh compromise on the financial perspectives in December. Although it was unanimously rejected, the compromise served as a basis for delicate tactical negotiations at the December European Council meeting. A political agreement was finally reached as a result of numerous compromises (see chapter by Cécile Barbier in this volume).

3. Debate about the “European social model”

At the very beginning of its six-month presidency of the EU, the United Kingdom announced its intention to hold an informal European Council devoted mainly to the future of the European social model.

¹ <http://www.ciginfo.net/demain/en/default.htm>

This “social summit” took place on 27 October. The British Prime Minister’s plan, following the French and the Dutch rejection of the draft constitutional Treaty, was to attempt to lay down some general principles by pooling the strengths of each national social model. The UK initiative received a muted reception at first, especially in France and Germany. Indeed, there were various reasons to be suspicious about the true intentions of the British presidency. First of all the timetable, considered by several Member States to be too tight to permit any serious reflection about such a sensitive issue as the European social model. Secondly, Mr Blair let slip some provocative remarks concerning a social model “*that does not have 20 million unemployed*”, in a fairly obvious allusion to France and Germany. Thirdly, there was also the fact that the initiative was launched by the United Kingdom, better known as an obstruction to the development of the European social dimension than as its promoter (on issues such as reducing working time in the Union, protecting temporary workers, strengthening European works councils, taking account of social dialogue, etc.). But the main point for London was to “adapt” the European model to the new circumstances of globalisation and competitive pressure. Europe’s capitals are deeply divided on this matter. The chapter by Philippe Pochet tells us what is at stake.

4. Reform of the Stability and Growth Pact

The reform of the Stability and Growth Pact went virtually unnoticed in this gloomy climate. Yet the anti-Europe liberal credo had turned the 1997 version of the Pact into the hate-figure of a monetary Europe dominated by high financiers and their allies in national central banks and the European Central Bank (ECB). The initial version of the Pact had the major shortcoming of focusing on cyclical economic factors – the level of budget deficit in a given year – rather than on structural data – overall debt. The latter indicator gives a clearer picture of a country’s medium and long-term strategy. For instance, a deficit of more than 3% does not have the same significance in Germany or France, where total debt is almost 60%, as it does in Belgium or Italy, where it is 100% or even more. This is why many economists believe that a country’s total government debt should become the most important criterion – even though that could cause a political problem

for countries such as Greece, Italy and, to a lesser extent, Belgium. The reform of the Stability Pact does not fundamentally alter the choice of criteria used for addressing recommendations to a country not complying with the requirements of monetary union, but it does lend added flexibility to the interpretation of these criteria. Andrew Watt's contribution sets out his analysis.

5. Will the “social model” expand or shrink?

As far as enlargement is concerned, one might have expected the debate to die down in 2005, in that the Europe of 25 had become a reality in May 2004. However, there has been no shortage of discussion – not to say controversy – both about the 2004 enlargement and also about those still to come (Romania, Bulgaria, Croatia, Turkey...). Thus the “Polish plumber” was catapulted into the French referendum campaign on the draft constitutional Treaty, while the Latvian employees of the company *Laval un partneri* were catapulted into the Swedish political debate, placing a question mark over the scope of that country's collective agreements. At the same time, the “threat” in social policy terms posed by Turkey's accession was an issue in several Member States. And so on. All of these elements are tending to give Europe, or at least some of its “old” Member States, the appearance of a social model under threat. If we add to this equation the restructuring and job losses related to existing or future decisions of the World Trade Organisation (Chinese textiles, Brazilian sugar, the forthcoming end of agricultural export subsidies), one cannot fail to question the viability of the European model in this era of globalisation, as well as its capacity to serve as a reference point for emerging countries. Pierre Defraigne describes a Europe which is finding it difficult to maintain this social dimension both internally and externally.

6. Ongoing debates

Three further topics covered in the following pages are ones which we consider symptomatic of the debates underway in 2005. The “better regulation” initiative launched by the President of the European Commission, Mr Barroso, is analysed and put into its political context by Éric Van den Abeele. Christophe Degryse examines the European

cross-industry social dialogue, which seemed at the end of 2005 to be grinding to a halt, while David Natali looks at discussions around the future of pensions in the context of the open method of coordination.

We trust that the various contributions to Social Developments in the European Union 2005 will make for interesting reading.

Brussels, January 2006.

Three ways of tackling Europe's social problems from the outside

1. Growing inequality in Europe

While the EU institutions are absolutely intent on attaining the goal proclaimed at Lisbon in March 2000, namely to close the one-point gap in GDP growth by which Europe has lagged behind the United States for at least a decade, a perhaps even more crucial challenge looms within the EU. The very cohesion of the European Union and the integrity of its social fabric are at stake. Confronted by the twin pressures of globalisation and enlargement, the EU is facing the dilemma of inegalitarian growth. Whereas European integration was long associated with a virtuous win-win scenario, another reality is now dawning: growth will only be increased at the cost of a fall in relative real wages as compared with income from capital. This discrepancy already exists and is mounting. It will moreover be perpetuated in retirement incomes in the long term: these will decline for the majority of poorly skilled workers who have insecure and patchy working lives, whilst they will grow for people on high professional earnings and those with savings.

This divergence in the distribution of primary incomes will gradually be compounded by a reduced capacity of governments to effect redistribution. On the one hand, income taxation is no longer as progressive as it once was, with consumption taxes being raised by way of compensation; on the other, there is growing pressure on social expenditure, both on expenditure geared to equal opportunities – education, housing and culture – and on that aimed at solidarity – unemployment, pensions and healthcare.

What is to be done? How can we prevent the social dislocation which is insidiously at work today in Europe and is a major reason for public disaffection with the EU?

The causes must be examined first of all. But, before that, we should point out that the debate is often skewed by two factors.

Firstly, the very fact that inequality is rising is deliberately played down or even denied by economists who readily overlook distribution problems to focus on growth, which they mistakenly see as a miracle cure for all social problems. There is moreover a lack of sound, up-to-date statistics: too few indicators of relative poverty exist; developments on the margins of society, if counted at all, are wrongly assessed; and it is difficult to evaluate the informal economy, sometimes verging on petty crime – which does of course prevent exclusion from the consumer society but only at the cost of appalling social marginalisation in the suburbs of our cities.

It is therefore difficult for experts to give serious consideration to these issues, while it is easy for politicians to evade them. The (ineffectual) discourse about growth and employment which has prevailed in Europe for the past twenty years thus appears to be a case of pressing on regardless despite the persistent, irksome reality that social indicators are deteriorating.

Secondly, the European level can easily offload these issues onto governments since its responsibilities are circumscribed by the Treaties: the EU is in charge only of the function of efficiently allocating resources for the entire EU, and of the stabilisation function for the euro zone. As concerns the third function of economic policy, redistribution with a view to equity, the EU is confined – with its budget of 1% of GDP – to peripheral activities, now with reduced funding, in support of convergence by the new Member States. On the other hand, it abstains in the name of subsidiarity from intervening in an area as central as interpersonal equity; this is left to governments, expected to exercise their social and fiscal sovereignty within a large market where factors and goods move around freely. In doing so, the EU sidesteps the consequences of integration and of opening up the single market (its responsibility) on the living conditions of the majority of European people.

Let us return to the deep-seated causes of the social dislocation process underway in Europe, whose political and institutional consequences will differ depending on whether the shocks currently confronting the European economy remain brutal or are in future cushioned by EU measures. EU-level politics bears a key responsibility here.

Before addressing the crucial role of the economy in creating inequality in Europe, let us look briefly at the impact of certain societal changes, themselves partly brought about by economic change.

European society is in crisis. How could we fail to notice? Grounds for optimism do of course exist: peace on the continent, rising standards of living for most people, longer life expectancy, remarkable technological progress, tolerance (despite the heightened tension between some Muslim communities and their host countries) and environmental awareness.

But some current developments give cause for concern: the link between single-parent families and poverty, the link between consumerism and excessive debt, rampant illiteracy, symptoms of depression especially among young people and the very elderly, and the onset of addictions related to behavioural and emotional disorders which add to the difficulty of getting a foothold in the labour market.

Europe is at present going through a period of doubt, and even pessimism, which is reflected in the increasingly widespread conviction that our children's future will no longer be better than the existence of their parents today. What a terrible admission for a rich, advanced society! How much of this European malaise is attributable to the economy and how much to the more fundamental crisis in society? We shall not explore this question here. Let us merely note that opinion polls have revealed such sentiments in very diverse countries: old and new Member States, countries where growth is rapid and others where it is slow.

Many observers dismiss this state of affairs from their radar screens because only a minority of people in our still well-to-do societies are affected; thus it is easy to gain the impression that with a bit of political will and social know-how one could return to square one and get back on track. That is a dangerous illusion: the three forces underpinning the

upsurge in inequality – technology, globalisation and social change – will keep nibbling away to such an extent that the social tension, anxieties and controlled political responses will filter through to the middle classes who ensure political balance and stability in our democracies. The more cynical commentators should at least factor in this risk of mounting populism.

Let us return now to the European economy and the origins of the new social question in Europe.

Among the changes liable to affect primary income distribution, reference is normally made to technological progress, a powerful element in both creating and destroying jobs, as well as to the distribution between capital and labour, and wage differentiation between skilled and unskilled workers.

Mention is also made of the changing balance of power between employers and employees resulting from a transformation in production structures: from large “Fordist” firms offering jobs for life, rising wages and social benefits to a strongly unionised working class, we are moving to companies which are fragmented into subcontracting and outsourcing networks and to more or less Schumpeterian – i.e. innovative – SMEs, where true industrial employment gives way to genuine or sham service jobs where trade union membership is scarce.

We have already spoken of sociological transformations, such as the breakdown of family structures which exacerbates poverty due to the existence of a single wage and a reduced capacity for intra-family solidarity. These changes no doubt also affect performance at school and mean that young people are less well prepared for the labour market.

Should we perhaps add the as yet little-known impact of temporary immigration, especially from the East, and permanent immigration, especially from the South, on jobs and wages? When these workers take up posts left vacant by the indigenous population, they contribute to growth; when they themselves drift into unemployment and/or operate in the informal economy, they adversely affect wage levels and employment. In addition, the very poorest ones swell the ranks of the

least well-off population groups, particularly because of their language and training handicap.

All these factors have a bearing on primary income distribution, but as a rule they are manageable because they arise gradually; they can be anticipated and dealt with, mainly by improving the quality of employment and social integration policies. The challenge is nevertheless immense, whether it be a matter of housing, education, training or access to a minimum amount of cultural knowledge, because improving the quality of social policies is an extremely complex matter. It is however worth a try, provided that the financial wherewithal exists. This is where the EU bears direct responsibility, because of the tax competition which it tolerates and facilitates.

Let us turn now to the external dimension of our countries' social problems: firstly globalisation, whose effects are augmented by European integration in the new context of enlargement; secondly, the prevalence of the financial sphere over the real sphere in the global economy; and thirdly the question of disparities in labour law between the North and the South.

The overlapping of these issues, coupled with their ever-increasing relevance, is currently provoking a wave of restructuring and relocation. This in turn has an adverse impact on most people's jobs and wages, both by creating unemployment where there is strong resistance to a reduction in real wages, and by pushing down wages elsewhere. And yet, like technological progress, the globalisation of markets and progressive "financiarisation" (see below) constitute undeniable sources of efficiency and factors of long-term growth.

In order to understand how factors of efficiency in allocating resources can result in a loss of well-being by exacerbating inequality and poverty, we need to grasp the means by which globalisation operates nowadays.

First of all, our adjustment to exports from countries with emerging economies, which has until now been a gradual and continuous process, is undergoing a step-change now that China – and more gradually India – is bursting onto the international labour market, knocking it off balance. These countries are opening up to foreign investment, massively so in the case of China, and their use of an export-driven

growth strategy is prompting an unprecedentedly large and rapid transfer of operations from industrialised countries to emerging parts of Asia.

Secondly, a new paradigm of international trade is coming to light: until now the South had an abundant supply of unskilled, cheap and relatively unproductive labour, while the North compensated for the high cost of labour through high productivity based on advanced technology. Today, thanks to multinational companies' investments and technology transfers into China, that country combines two hitherto contradictory comparative advantages: cheap labour on the one hand and cutting-edge technology on the other. All of a sudden, the North needs to create not only unskilled jobs to replace those lost but also even more highly skilled jobs, which presupposes a faster rate of innovation and of course sufficient protection for intellectual property.

Thirdly, there is now a marked dissociation between capital and labour in the process of adjusting to this globalisation dominated by foreign direct investment. For example, when businesses relocate to China or expand their operations there, the European or US shareholder wins out because he will obtain either additional dividends or capital growth. The worker, by contrast, whether skilled or unskilled, will lose his job. Net added value is created in Europe if the dividends and capital accumulation resulting from outsourcing exceed the wages no longer being paid, but the distortion of distribution patterns is severe.

It would of course be feasible to redress the balance: inasmuch as the income from capital is reinvested in new jobs in Europe or is subject to a tax levy to finance job creation in the non-commercial sector, then alternative jobs will be available to the dismissed workers; in that case the problem is confined to easing the worker's transition and retraining. There is no guarantee, however, that the real wages provided by these new jobs will be as high!

Nor is there any guarantee, in actual fact, that any such mechanism will be put in place: if the profits are reinvested on the spot in Asia, or in the United States, and moreover if capital gains tax is evaded, then – all other things being equal – there will not be any replacement jobs. In other words, now that China and India are bursting onto the global economic scene, we are experiencing new situations in which the

winners are on one side and the losers on the other. The compensation for gains and losses which used to be come from the market and from politics is no longer so readily available. Unemployment used to be transitional but is now becoming structural because the creation of replacement jobs is no longer keeping pace with the rate of job destruction.

EU enlargement reproduces this scenario on a smaller scale from the point of view of labour in the old Member States, but with one important distinction: the process turns full circle within the EU! Added value and business activity are indeed transferred from West to East, but it contributes to real per capita GDP convergence by the new Member States, so that eventually we can in turn expect growth to be stimulated in the old Member States and jobs to be created. In the meanwhile, though, the lot of the old Member States will be stagnating or even falling real wages, or else worsening unemployment. What is more, if tax incentives are used to attract investors from West to East, the shift in the tax base from an old to a new Member State will limit the capacity of the former to perform its role as provider of social safeguards.

And what of integration itself, which the Lisbon Strategy undertook to kick-start, above all in financial services and in the network industries? There can be no doubt that it improves efficiency, thanks to a combination of economies of scale and heightened competition, provided of course that competition is effective – which is far from being the case at present! But the growth generated in the twenty years since the 1985 White Paper on the Single Market of 1992 has not been sufficient to make significant inroads into structural unemployment, despite the jobs created both in the run-up to the single market and owing to the switch to the euro. Thus not even the policy at the very core of European integration is able to generate job-creating growth. Three factors counteract the effects of the micro-economic and structural dynamic of integration: the macro-economic policy mix does not fuel growth; the attempt to achieve competitiveness by lowering real wages has a deflationary effect; and, lastly, differing degrees of rationing still exist on labour markets, financial markets and in the utility sector.

2. The new distribution scenario

No economist doubts the link between growth – and hence employment – and global trade liberalisation: these two processes interact and are mutually reinforcing. By the same token, all economists point out that no country has ever developed in isolation.

The link between growth and trade liberalisation at the level of each country individually is a good deal more complex, however: the degree of success in opening up to trade is determined in particular by its size, specialisation and whether growth preceded liberalisation or vice versa. Moreover, the benefits and costs of opening up commercially are shared out according to an intractable law: national resources made rare by being exported gain in value, while resources made more abundant by being imported lose in value!

Finally, one crucial question arises here: are governments willing and able to arrange for solidarity between the winners and losers, in the form of transition incomes and retraining policies? Because in reality it is politics, and politics alone, which transforms growth into fair and sustainable development. On the other hand, if the market places excessive constraints on politics, efficiency gains will indeed be made but may be snapped up by the winners. “Winner takes all”, as they say!

When trade takes place between countries, for example ones in the North and ones in the South, which are differently endowed in factors of production – skilled or unskilled labour, high or low capital reserves, advanced or basic technology – the problem of sharing out efficiency gains arises above all within each partner. When trade occurs between countries at similar levels, such as for example the EU-6, what makes the difference is the specialisation of each economy: the main issues here are agglomeration effects linked to the status of “front-runner”, economies of scale and product differentiation. Distribution will in principle be easier to manage because the resources used in production are more mobile.

However, we are now seeing a new distribution between capital and labour, between skilled and unskilled labour, not only within but also between countries and even between continents, as a result of two major developments which go hand-in-hand with globalisation:

“financiarisation” of the economy and the rapid emergence of China in the world economy.

We should say at the outset that it is not a matter of pouring contempt on globalisation, which has distinct advantages, and less still of succumbing to protectionism, whose consequences would be unpredictable and probably disastrous for prosperity and peace in the world. But we must realise that if politicians, internationally and nationally, do not exercise proper control over globalisation, distribution problems will arise. Inequality will worsen as a result of structural unemployment and a relative drop in real wages for many people, if not most, and social cohesion in our countries will be at risk. History teaches us that, when confronted by a tear in the social fabric, governments take matters in hand and interfere in the self-regulating mechanism of the market: the collapse of the gold standard in the early 1930s was brought about by political decisions made in the wake of the 1929 stock-market crash. A unifying international system undermined by “beggar-thy-neighbour” policies was replaced by alternative and conflicting models: increasingly radical collectivisation in the Soviet Union, the New Deal in the United States, and the autarkic, militaristic models of Germany, Italy and Japan.

Let us not repeat the mistake of the past, namely dismissing the eventuality that nations or regions might withdraw into themselves on the grounds that economies are now so globally interdependent that conflict would be impossible. Alas, this argument does not stand up in the light of history.

We shall now make what is a difficult admission in this era when the economy reigns supreme: politics always takes back control from the market when a country's social integrity comes under threat. Therefore only a robust system of multilateral governance, based on solidarity including (this time) the social order, could halt the slide into protectionist behaviour and rivalry between continental blocs. Such an international system is still only in its infancy. Only a united and determined EU can hasten the advent of a system of global economic governance, the guarantor of fair and sustainable development, since the initiative will not come from either the United States or China.

Let us turn our attention to two systemic changes occurring in tandem with globalisation.

2.1 Finance holds excessive sway over companies

We now look at financialisation, without doubt a complex phenomenon but one whose complexity is in part a deliberate ploy to discourage researchers from analysing it and, even more, to deflect politicians' attention.

Let us attempt to keep things simple so as to explain what is at stake and reveal the scope for corrective action.

Finance in itself is of course a productive activity, in that it adds value to savings and makes it possible to invest at reduced cost: the provision of capital contingent on the soundness, liquidity and competitiveness of financial markets contributes significantly to development. Conversely, finance is at the same time an activity plagued by parasitism and speculation, where greed easily spills over into fraud and tax avoidance is rife.

Over the past two decades there has been a growing trend worldwide for the financial sphere to win out over the real sphere of the economy: the obligation on companies to obtain financial "best value" no doubt makes them more competitive in the short term, as measured by their profits; but that competitiveness comes at the cost of excessive restructuring, owing to the priority attached to short-term profitability rather than to long-term strategies determining corporate growth, job stability and rises in real wages. This pressure on companies is compounded by pressure on governments.

2.1.1 Pressure on companies

Financialisation is situated at the meeting-point of three developments: corporate governance, information technology and the international liberalisation of capital movements.

Since the 1980s, initially in the United States, immediately afterwards in Great Britain and then gradually throughout the EU, a new logic of governance has gained ground, whereby the shareholder and the stock market take over the place traditionally occupied by company managers and, at least in Europe, bankers. The concept of "stakeholder value",

where the interests of everyone having a stake in the company – shareholders, workers, suppliers and subcontractors, local authorities – are taken into account by managers seeking a compromise between competing interests for the sake of long-term growth, has given way to a form of governance oriented towards “shareholder value”, the creation of value for shareholders as demanded by new players on the financial markets.

These new players are institutional investors: pension funds and mutual funds. They now represent individual shareholders, and their presence in the financial game unsettles shareholders, who, formerly sedentary, have now become nomadic or even “fly-by-nights”, quick to pocket their profits and hence easily seduced for example by hostile take-over bids, whatever the long-term effects on corporate growth.

The combination of this mobile shareholding class and the pressure exerted on households by institutional investors through the financial markets over the past two decades is a key factor in the steady rise of capital as a share of added value in Europe and the United States, and consequently in the decline in the share of wages. This fundamental alteration in the pattern of distribution is a major cause of widening income disparities – along with the growing individualisation of pay.

But the effects of this “dissociation” of company ownership and corporate responsibility in the minds of shareholders and the importance of institutional investors would not have reached today’s dimensions if two other major changes had not occurred at the same time.

Information technology (IT) has first of all revolutionised accounting methods and has flushed out the unexploited potential of “shareholder value” at the core of the most complex companies, revealing it to the market-place. IT has also enabled profit opportunities based on risk transfer to be converted into financial products. Lastly, it has permitted the interconnection and real-time operation of global financial markets, heightening the pressure on industrialists and governments.

But what has created the operational framework for international financial markets is the liberalisation of capital movements, gradual initially until the mid 1980s and thereafter extremely rapid. The

principal function of this liberalisation is to reallocate global savings according to the yields offered on different national markets. At a stroke, the pressure exerted by institutional investors on companies with a view to producing (untenable) double-figure yields is redoubled as a result of the internationalisation of markets.

This liberalisation has occurred despite a lack of institutional supervision of financial markets in countries with emerging economies. Short-term capital flows have therefore had a destabilising effect on these economies, which were exposed to repeated financial shocks from 1982 (Mexico) to 1997 (Asia).

2.1.2 Pressure on governments

The globalised financial markets have another strategic function: to fund public deficits. In doing so, they use exchange rates as a means of influencing the nature of public finances because they reward financial orthodoxy. However, short-term capital movements also exert indirect influence on governments' macro-economic and financial policies, depending on the judgements they make about the sustainability of key equilibria (public debt, external deficit, inflation, currency reserves, unemployment). Such pressure not only promotes financial orthodoxy but can also be detrimental to the position of heavily indebted States by obliging them to adopt overly deflationary policies or reforms not conducive to development; it can have a destabilising effect by putting speculative pressure on exchange rates to begin with and then subsequently on interest rates.

But the financial markets do not treat all indebted countries in the same way. For instance, they do not – far from it - lessen major structural imbalances such as those now characteristic of the link between the US external deficit (which reflects a shortage of private and public savings) and the external surpluses in Asia (which reflect an excessive propensity to save). Thus Chinese savings finance excessive US consumption.

Above and beyond its ambivalent impact on governments' financial management, and in the absence of multilateral fiscal standards, liberalisation furthermore encourages tax avoidance on income from mobile factors: savings and company profits. The integration of tax havens into "normal" financial circuits and the fact that many

governments attempt to attract non-residents to invest in their countries, by offering favourable tax rates, now place unbearable strains on the ability of governments to tax income from capital.

These grave constraints on the redistributive function of governments is a crucial factor in exacerbating inequality in advanced countries, due to the under-provision of public goods and a loosening of solidarity. Taxes on labour and consumption cannot compensate for the erosion of the tax base deriving from financial savings and company profits; the result is a serious distortion in tax equity.

2.2 China's unbalanced growth strategy

The emergence of China alters the global economic order, which is only logical given its size and potential. In itself, China's rise to prominence is good news, both legitimate and, ultimately, a force for prosperity and peace in the world. But the transition from the inward-looking phase of the Mao years to the country's dramatic arrival on the international economic scene is too sudden and poses adjustment problems which may get the better of our countries.

Some historical background to the Chinese phenomenon may help to explain it.

On the one hand, after the Communist victory of 1949, a successful attempt was made to restore China's internal unity and to reconstruct a State which had long been stratified and corrupt. But all of this went on behind closed doors, in a repressive political climate and with a degree of economic self-sufficiency. The economy remained unchanged until it was transformed into a socialist market economy and until the Chinese Communist Party under Deng Xiaoping decreed in 1979 that it must open up to the world. That process culminated in China's accession to the WTO in 2001.

On the other hand, Japan underwent rapid reconstruction after the defeat of 1945, South Korea took off during the war of 1950-1953, and then, as from the 1970s, the "flying wild geese" of Japanese industry spread to ASEAN, Korea and Taiwan, marking the emergence of the Newly Industrialised Countries, the "Asian tigers", in the 1980s.

These two developments came together with China's simultaneous entry into eastern Asia's regional industrial integration networks and into the world economy. The key to its integration is foreign direct investment, coming from the region and from the West, which chose to use China as a platform for exporting manufactured goods, largely made from components imported from the area, mainly to the US and European markets.

The uniqueness of the Chinese model lies not only in the size of the new entrant but also in the new paradigm of international trade which provides the context for the country's integration. Technology brought in thanks to US, Korean, Japanese and above all European investment in the country means that China combines two advantages: low wages and high productivity. At a stroke, the phenomenon of China's enormous size becomes less of an issue for our markets: the problem for the EU increases in scale and complexity, and the challenge becomes much more difficult to meet in both quantitative and qualitative terms.

The (apparent) paradox is striking: China's success results from a previously unthinkable alliance between multinational companies, the spearhead of advanced market capitalism, and a Communist Party possessing the necessary powers to ensure a stable social and political environment for the activities of these companies. What the Chinese government has to do is in fact to manage the huge internal pressure caused by regional and social disparities, as well as by environmental difficulties, both of these generated by an exceptionally high pace of growth over an exceptionally long period of time.

Given the scale of the adjustments required of China's partners, two types of reaction are becoming apparent: one highlights the contradictions and conflicts being experienced by China's economy and society. It predicts an imminent end to the Chinese miracle, dangerously underestimating the adverse effects on the country, the region and the world if Chinese growth were to come to a halt. The other reaction emphasises the restrictions placed by the Communist regime on civil, political and trade union freedoms in order to justify applying pressure and defensive trading measures above and beyond legitimate anti-dumping actions and measures to protect intellectual property.

Curiously, this defensive reaction does not come exclusively from civil society or trade unions, but also from business circles whose members are active in China and have to an extent thrown in their lot with the regime. In actual fact, even though this point of view can claim to be rooted in high-minded principles, it overlooks the fact that the Chinese State is pursuing – in its own way, a way that is proving effective – a project which is fundamentally geared to long-term integration and sustainability. Without ignoring the undoubted problems of respect for human rights and of corruption which, alas, are by no means any more serious in China than in innumerable other countries supported by the EU and the USA, these problems must be viewed in conjunction with China's ambition to wrest an entire continent from poverty while lending an environmental dimension to this monumental undertaking. These efforts deserve encouragement from Europe, in that they are utterly legitimate and desirable: it is more certain that democracy will arise out of development than, sadly, out of what has happened recently by way of developing democracy in the emerging economies of East Asia.

3. Responses available to the European Union

Our societies are insidiously and inexorably reaching the point of social breakdown and its corollary, political instability followed by authoritarian repression.

Tackling the consequences of the drift into inequality is not enough. Moreover, it would be neither politically feasible nor economically desirable to radically alter primary income distribution, on account of the excessive distortions of supply which would result from prohibitive tax takes and excessive, dependence-inducing transfers.

We must therefore tackle the root causes of inequality. Let us rank them, without taking into consideration social changes only indirectly connected with the economy. Technological progress and European integration can be mentioned briefly, after which we need to focus on two factors with an important external dimension: China's growing power and the pressure exerted by finance over the real economy.

Technological progress is obviously a vital necessity for our economies, with their low birth-rates and prospects of a worsening ratio of active to

inactive populations. It must of course be stimulated by all useful development and innovation policies. But equally essential is a redressing of the balance between basic research work, necessarily in the public domain since it serves the collective good, and applied research whose results are liable to be appropriated and which may as a result be funded either out of taxation or by the market. Nowadays, especially under the Lisbon Strategy, there is too great a propensity to “privatise” research, especially by granting tax breaks or subsidies, rather than to properly fund public research. Adequate funding could improve Europe’s inadequate research output, caused by a lack of equipment and administrative and technical back-up for research activity worthy of the name.

In a knowledge-based society, the borderline between public and private becomes a major political issue in two senses: firstly in terms of efficiency, which means striking the right balance politically between research output and the dissemination of its findings; and secondly in terms of fair access to knowledge and its use. In other words, equal opportunities in accessing education and in enabling small operators – such as farmers – to share in technological progress are important factors in wage-setting and in primary distribution.

The appropriation of research results by large companies or by business start-ups serves in fact to heighten inequalities between the owners of knowledge and of commercial patents on the one hand and other economic operators on the other.

Economic integration in itself is a very good thing for Europe, strengthening its control over its own internal development and its capacity to interact with the wider world. Nonetheless, although in principle integration generates efficiency and hence growth, especially due to the combination of economies of scale and competition, its impact on primary distribution will differ according to whether it occurs on the basis of an upward harmonisation of social and fiscal standards or as a result of a social and fiscal race to the bottom. The more heterogeneous the Member States become due to the accession of increasingly outlying countries, the greater the risk that convergence between national economies will be achieved only at the cost of worsening inequalities within both the converging countries and the old

Member States. Conversely, the fact that the Bolkestein directive on freedom to provide services was adopted by the European Parliament only once the initially fundamental “country of origin” principle was abandoned – a wise decision under the circumstances – indicates the scale of that heterogeneity and the cost, in terms of freedom of movement, arising from the absence of harmonisation.

But let us concentrate here on the two truly external dimensions which we have identified as being closely connected with the issue of inequality: globalisation, dominated as it now is by the growing power of China, and financialisation, resulting from the combination of an international liberalisation of capital movements, where shareholders reign supreme and stock markets become volatile and unstable, with an unequal distribution between wages and profits within the company. We shall then raise the important matter of workers’ rights in the developing and emerging economies.

Let us resume our examination of these complex issues, which need to be tackled all together in order to deal with their underlying principles. Only in this way can the efficiency of globalised market capitalism be preserved while effectively halting its natural drift towards instability and unfair distribution.

3.1 China: stimulation of domestic development

The first way in which the EU can intervene is by reorienting the Chinese model of development from an export-led strategy to a more endogenous pattern of development.

The overall game-plan behind China’s industrial breakthrough is strategically brilliant: rapidly attaining a threshold of advanced and broad-based industrialisation by allowing multinationals from Japan, Korea, the United States and Europe to draw upon the country’s formidable pool of labour was a bold move. Only a country with an immense domestic market – a little like that of the United States in the 19th century while its population was being bolstered by immigration – could successfully pull off such a move. Where the United States brought in labour and capital at that time, China has attracted managerial know-how and technology.

The pace of change was a crucial factor of success: a high level of advanced, diversified industrialisation had to be reached right away, as a basis for a network of manufacturing and service industries gradually penetrating the entire country, and for establishing an appropriate institutional framework for Chinese companies themselves to pursue modernisation.

To have implemented this strategy without running the risk of incurring the massive external debt which a classic industrialisation process would have entailed – namely surplus imports of capital goods over exports of consumer or intermediate products – would have made China dependent on the G7 and the IMF. That would have been incompatible with its original political blueprint: a socialist market economy. The handling of the 1997-98 financial crisis in Asia by the IMF and the US Treasury demonstrated the reality of that risk. The US budget deficit and over-consumption by US households facilitated the industrialisation process, for which they would moreover be the macro-economic precondition. But this “blitzkrieg” style of industrialisation is today reaching its internal and external limits. Internally, there is tension between towns and countryside, between coastal and inland regions, and there is pollution. Externally, the pace and scale of the adjustments necessitated by the growing power of China, not only in advanced countries but also in developing countries – we need only think of textiles – are becoming excessive. We must of course, and we can, considerably improve our adjustment capacity, above all by creating replacement jobs, but we shall not be able to do so fast enough.

The protectionist pressures evident in the textile and footwear sectors will continue to mount. Just think what effect a Chinese breakthrough in the automobile sector could have on the international market.

In short, action must be taken at source. China must be encouraged to shift the centre of gravity from an accumulation of physical and immaterial capital, from exports, towards domestic demand for and consumption of collective goods and towards restoring the environment, which is in very poor shape. The Chinese leadership is well aware of the need to redress the social, regional and environmental balance; this will paradoxically only be possible due to a high rate of growth.

It does not take a genius to imagine the political tension which could be caused by an economic crisis in China. In actual fact the indebtedness of its State enterprises, and the potential public debt which that represents, is such that China is very vulnerable to a slowdown in its growth.

Reorienting that growth towards domestic demand, rather than slowing it down, is the only viable option for China today.

Such strategies would ease the pressure on our labour markets by reducing at source the rate of penetration of imports and by increasing the rate of our exports to China.

Another justification for this action derives from the need to curb excessive consumer demand in the United States. With an external deficit of 6.5% of GDP fuelling an external debt of between 2 and 3,000 billion dollars (the margin of appraisal is enormous), greater than the total debt of the South, the US is creating the conditions for a worldwide recession. Once investors lose confidence in their dollar assets, the corrections they make to their portfolios could send shock-waves through the European economy. Imagine what it would mean for the euro zone in terms of competitiveness and jobs if the dollar were suddenly to depreciate by between 25 and 30%. It is an urgent matter of priority for Europe that the US external deficit be cut and that the Chinese surplus be reduced at the same time. Yet, for the time being, the EU institutions are little exercised by this problem: no sound analysis and no sign of getting to grips with it.

The self-effacement of the EU as such within the G7-G8 shows that the world's number-one commercial power refuses to act as the number-one financial power that it also is in terms of savings and foreign direct investment. Of course, in order to express its views and take action, the EU would have to cut a path to the IMF Board and sit at the helm on a par with the United States. This could perfectly well be done immediately, as soon as the EU countries – all members of the IMF – or at least the twelve members of the euro zone decided to speak with one voice and vote all together. If they did so, they would out-vote the United States.

The EU's role in the IMF is critical because the IMF's role in correcting the binomial US deficit / Chinese surplus could be a decisive factor in re-establishing East Asian confidence in the international financial institution. If these countries, first and foremost China, have opted to accumulate currency reserves, the reason is that they are rightly distrustful of the IMF after its questionable handling of the Asian financial crisis from a growth perspective, serving the interests of US commercial and financial interests. They intend in future to shield their domestic development strategies from the Washington Consensus and the covetousness of Wall Street. A stronger European presence, developing a more pluralist and objective approach to crisis situations, could reassure China, encouraging it to export less and import more.

Could such a European strategy work? But of course it could! It is a matter of political vision, will and leadership. It is naturally not possible today to envisage a single seat for the EU in the Bretton Woods institutions, no more than it would be feasible to bring on board the United Kingdom, in hock to Washington, or the new Member States, not yet ready to play with the big boys. But an initiative by the twelve members of the euro zone, backed by one or other of the Nordic countries, would be quite possible. What is needed is an analysis and a capacity to join forces, and hence a unifying force to make the Eurogroup speak with one voice. Ideally that should be the Commission. But the Chairman of the Eurogroup, Jean-Claude Juncker, is perfectly able to mastermind this policy and create the political, institutional and operational conditions for its implementation.

By means of small, practical steps such as these the EU could assert its presence on the international stage and restore the confidence of the European people in its capacity to act. Institutionalisation will come later, once there are signs of movement and success has been reaped.

3.2 Financiarisation: prevention of unwarranted restructuring and payment of taxes

Under the organisational conditions currently taking shape on global markets, financial traders have excessive power to cream off a share of added value out of all proportion to its contribution. It is therefore necessary to reduce financial income at source, to enforce the payment of taxes on savings, and to prevent volatile and irrational stock-

exchange movements and unstable short-term international capital flows from disrupting and compromising the real economy, especially long-term corporate strategies.

We need to look at the trends underway to find those deriving from meaningful and irreversible changes, and those deriving from reversible political decisions. This is the key to our approach: establishing a new balance of power between capital and labour, between capital and governments, by reintroducing scope for negotiation and collective action at two levels, namely at the stages of primary distribution between capital and labour, and of secondary redistribution by governments.

To govern means above all else to anticipate: once they are up and running, certain market developments gather momentum and thwart the capacity of politics, and hence of democracy, to correct them. The inherent complexity of finance is compounded here by the additional difficulty for the political sphere to enter and appropriate the European dimension, the only relevant level for involvement in global economic governance.

What corrective action should be taken?

1) From international liberalisation to the traceability of capital flows

During the four decades following the War, the world experienced sustained growth and European countries achieved a high degree of shared prosperity under a system based on government controls of capital movements. It was the crisis in the international monetary system caused by financial laxity in the United States which led to the replacement of fixed exchange-rate discipline, based on national foreign-exchange controls managed with IMF assistance, by a globalised financial market discipline, in the form of floating exchange rates. This change was the product of an alliance between the United States and the United Kingdom, beginning with the creation of the Eurodollar markets in the 1960s and ending under the leadership of Reagan and Thatcher in the 1980s. The EU in turn completely abolished exchange-rate controls by Member States as from 1 July 1990, the first stage in the transition to the euro. Such liberalisation was unavoidable within

economic and monetary union. It is however optional, and theoretically reversible, in the EU's relations with the rest of the world: a Europe producing financial surpluses would not be deprived of capital.

But such an alternative would not be desirable from various points of view: efficiency, the remuneration of savings, competition between financial intermediaries, and pressure on governments to ensure a minimum degree of financial orthodoxy. Nor would it be necessary in order to correct the financial excesses underway. On the other hand, it is now technically conceivable to arrange for the traceability of international capital flows: that would make it possible to combat effectively not only financial crime and terrorism but also tax avoidance.

2) Stabilise shareholding to promote long-term corporate growth

Shareholders cannot claim, in the name of ownership rights, to exert exclusive control over the company while at the same time ensuring the liquidity of their investment.

That, of course, is precisely how pension funds and other institutional investors operate. But this construct, ingenious from the point of view of the “predatory” shareholder, runs counter to the legitimate interests of the other stakeholders, be they within the company – first and foremost the employees – or outside of it.

Very fortunately, the European company statute, which emerged from the work of the Davignon Committee and constitutes the founding matrix of a European conception of the company, allows for the establishment of companies constituted as partnerships and not only ones with shareholders. There is so much scope for interpretation when this legislation is transposed into national law that it will be possible to consolidate the partnership concept once the “case law” of the European directive becomes established.

If this concept does prevail, the full potential of company law and commercial law must be exploited: worker participation in oversight, prohibition of stock options for managers who collude with shareholders and stock-market traders, employee investment funds aimed at stabilising the shareholder group, measures to deter hostile take-over bids and share exchange offers, etc.; standardisation of

accountancy methods geared to long-term management and not to the creation of stock-market value.

The EU must develop at its level a full and well-integrated body of legislation to promote a model of corporate governance in Europe which returns to the concept of partnership and stakeholder value, and which puts value creation for shareholders in its proper place in a broader equilibrium taking due account of the interests of all other stakeholders.

The information technology revolution in corporate governance enables the financial markets to operate internationally, 24 hours a day and in real time with the productive economy and political decision-making by governments. It also means that, using the international accounting standards currently on the drawing-board, precise data on the internal life of a company can be provided in real time to financial-market traders, which places added constraints on the actions of company managers.

Owing to their highly technical nature, the definition of these standards is ignored by politicians, who rely on specialists coming mainly from the private sector in the US and the UK. Accounting standards founded on an exclusively shareholder-based notion of the company brings the stock market to the very heart of management practice.

It is rather surprising that the EU, which has experienced far fewer financial scandals and – apart from Parmalat – much less serious ones than the United States, should draw inspiration mainly from the new accounting standards and new forms of regulation in the US when establishing a European framework for the integration of financial markets. In particular, the “fair value” accounting principle in the US favours providing information to shareholders about opportunities to enrich themselves when market values rise by keeping an eye on the markets, rather than providing information to managers engaged in internal trade-offs and long-term development strategies.

The EU must redirect its standardisation of accountancy systems towards a concept where companies are partnerships and not shareholder vehicles.

3) Go back to sustainable rates of return

The double-figure rates of return demanded by institutional investors on behalf of opportunist and uncommitted shareholders are neither fair nor tenable. Nor are they in line with productivity trends, which constitute the real measure of return on capital in the long term. In a context of moderate economic growth, such figures are obtained at the cost of company restructuring for purely financial reasons, with no regard for long-term corporate objectives, or jobs and wages, or local and national communities.

Ultimately, this financial remuneration extorted from companies by shareholders in search of windfalls constricts growth and, by sending stock-market expectations to dizzy heights, feeds either stock-market bubbles or “creative accountancy”. It handsomely rewards an army of professionals – auditors, consultants, business bankers, market traders – who take huge commissions and fees, usually out of all relation to the company’s long-term performance. Half of all mergers/buy-outs take place for no other reason than to enrich financial intermediaries: they do not contribute in any way to raising the company’s long-term productivity and profitability.

Of course, stock-market values reflect not so much a company’s true output as its expected output. Savings grow more rapidly than companies’ tangible investments, in view of wage rises, extra social security contributions and pension contributions because of the current demographic balance; and there is a preference for shares in a climate where rates of return on bonds are lower. All of this creates a favourable, but perhaps only temporary, climate for rising stock-market values.

Rising stock-market values must however be contained within sustainable limits: a new bubble could get the better of international growth this time round. The ECB and the FED still have a crucial role to play in curbing the irrational exuberance of stock markets.

4) Impose taxation on capital

An ageing society is developing a preference to save money for pension purposes based on (very inegalitarian) money purchase schemes rather than pay-as-you-go schemes, which offer greater solidarity. It is worth

noting that, in money purchase and pay-as-you-go schemes alike, there is always the same transfer of resources in the real economy from active to inactive persons.

Remuneration from capital (company profits and returns on financial savings) is boosted because they are less effectively taxed. The long-term trend is perfectly plain: the mobility of these two types of income enables them at one and the same time to play on the downward tax competition between States which it helps to strengthen, and also to illegally avoid taxation by exploiting the opportunities afforded by tax havens in Europe and elsewhere.

The results are twofold: first, increased taxation on a fixed basis (property, consumption and labour); second, a reduction in financial resources for governments to use in confronting the requirements of growth (supply of public goods) and a decline in solidarity (equal opportunities and safety nets).

The issue of company taxation and savings in Europe is stymied by the unanimous voting system and hence the right of veto. This institutional dysfunction is intolerable and incompatible with the ambition of a Social Europe.

Two possible solutions exist: fully-fledged harmonisation of both forms of taxation or, better still, the replacement of national taxes by European federal taxes. Either method would ensure that European public goods (research, defence, security, network services, convergence between States, etc.) were properly financed. Moreover, in cooperation with the United States, past masters at such policies, a fiscal EU would become an agent in the fight against tax avoidance by people moving their money to third countries and tax havens. Finally, in a context of global public goods, one could envisage the introduction of unitary taxation of capital on a worldwide scale, which would ensure tax equity especially in the countries of the South.

3.3 Effective promotion of fundamental workers' rights in the South

To what extent are low wages in emerging countries attributable to low productivity and a plentiful supply of labour, and to what extent can they be attributed to a lack of trade union rights and protection for

children, women and minority groups? Just as it is inevitable that low productivity will be reflected in low wages, it is equally intolerable that workers in developing countries do not receive their legitimate share of productivity gains. For that, they must in effect be granted the right to organise into trade unions and to negotiate their wages and working conditions collectively. Even a very poor country can ensure compliance with the framework Conventions of the International Labour Organisation on minimum social standards. Most countries have in fact ratified in these Conventions but do not enforce them on the ground.

The linkage of trade and human rights is thwarted by the refusal of developing countries, expressed clearly and unanimously at the WTO Ministerial Conference in Seattle in December 1999, to establish any such link. In the foreseeable future we can expect nothing from that quarter apart from technical cooperation and a dialogue between the ILO and WTO secretariats which will not lead to much. Indeed, the key problem still remains the fact that the ILO has no real powers of coercion.

During the term of office of Michel Hansenne (1989-1999), and now under Juan Somavia, the ILO has been attempting to devise methods of putting pressure on its members when they fail to comply with Conventions which they have ratified. There is however a long way to go, and progress is being made at snail's pace.

The EU for its part normally incorporates at least three aspects (politics, cooperation and trade) into its bilateral agreements with third countries, and is exploring the possibility of using these agreements as levers to promote the ILO Conventions. But only in extreme cases – such as Myanmar – does the loose connection between these three aspects allow human rights to be linked to trade preferences.

The political message is there, but the leverage effect is weak. It is in fact hard to imagine the EU using trade as a weapon to enforce compliance with workers' rights, even in a bilateral context on the basis of contractual provisions derogating from the WTO principle of non-discrimination.

Three practical approaches still need to be explored. First of all, fair trade, i.e. the establishment of a voluntary social label intended to guide the choices made by consumers. Secondly, compulsory codes of conduct, i.e. obliging European multinational companies to apply minimum social standards – particularly in respect of trade union representation – in all countries where they operate throughout the world. Thirdly, why not form a “good social governance club”, based on a multilateral pact, consisting of those countries which agree to subject trade among themselves to effectively monitored enforcement of the ILO Conventions, backed up by sanctions? The EU-25, the United States and Japan could set the ball rolling in the hope of expanding this club to take in the largest possible number of emerging and developing countries, and could take diplomatic action to that end.

Surely the Economic and Social Council and the European Parliament could push in all three of these directions?

Conclusions

Once again, we are taking issue not with market globalisation, in particular the gradual opening-up of markets to trade, nor with the legitimate and welcome emergence of China, nor even with financial liberalisation, but with the conditions for the implementation or occurrence of these phenomena.

At the heart of the debate is the neoliberal mindset which originated in the US and the UK and determines the rules of the game as well as the conduct of macro-economic and financial policies. This is what must be fought resolutely, and it is to this that an alternative must be found. Europe is suffering from a lack of serious debate about its responsibilities and its capacity to act at the level of global economic governance. Weak analysis and the resignation of the European social-democratic Left too readily discourage Europe from identifying the scope for reform inherent within globalised market capitalism: that scope can be exploited by the European Union, provided that the EU unites around these policies. Only by containing the social dislocation taking place today can we, in our European societies, protect ourselves from populism and its inevitable drift towards the instability and crises

that will thoroughly unhinge Europe's democracies with unforeseen international consequences.

Reform movements are never an overnight success, but if they all too often fail it is because their thinking was too timid, too partial and too lacking in coherence. The impotence of the reformist Left in Europe over the past two decades can be explained by its refusal to dream up and assert realistic alternative ideas. The trade union movement, itself motivated by damage control, has not yet found within it the necessary analytical resources and unity to back political action at the only appropriate level to exercise leadership, namely the European level. The EU is nowadays dominated by neoliberal thinking, bent on shaping economic and social Europe in the Anglo-Saxon mould, thereby further confirming the EU's status as a subset of an Atlantic entity improperly extended from the field of strategic security (where it makes sense) to that of a "civilisational bloc", with the inherent risk of a confrontation of blocs and a clash of civilisations.

Europe must act. One day the Commission will be the natural architect of this change in Europe's globalisation strategy. Indeed, only a strong European executive body can provide the requisite momentum and coordination. But the Commission too must drag itself away from the "Davos mania" which has overtaken the successors of Hallstein, Jenkins and Delors. It will only resolve to do so under pressure from the pan-European political and social groups organised and active within the European Parliament and the EESC. What has to be done is to arouse awareness and give heart to those women and men who aspire to reconcile freedom and justice in Europe. In that way it will be possible for the EU to enter the history books as the successor to a glorious and tragic European civilisation, whose aspiration today is modernity within its trademark humanist context.

European economic trends and economic policy in 2005: renewed disappointment on outcomes, incremental improvements in economic governance

Introduction

Both whole-hearted supporters of European integration and, from their different perspectives, the various critics of that project are broadly agreed that it has been characterised – and to some extent also driven – by a steady increase in the degree of economic integration of the economies of Europe. This shows up in a whole range of indicators of cross-border movements of goods, services, capital and labour. This process has been extended to the former Communist countries of central and eastern Europe, especially since EU enlargement in 2004, but actually much earlier. Clearly the integration process has gone furthest in the 12 countries which, since 1999 have shared a common currency (¹).

This integration process has been accompanied by an on-going debate on, and actual institutional changes in, European economic governance. This term is used as a catch-all to describe the sum of the institutions, legal mechanisms, and other informal norms (²) under and within which national and European actors and policymakers interact transnationally to set important parameters of economic policy. Examples of these

¹ The euro has *de facto* existed since 1997 when exchange rates were fixed irrevocably; the 12th country, Greece, joined in 2000.

² “Institutions” in this case is used in a narrow sense; sometimes the term is used in such a way as to encompass also legal mechanisms and other norms.

three constituent elements of “economic governance” include: the European Central Bank (ECB) (institution), the Stability and Growth Pact (SGP) (legal mechanism), and deliberations between the social partners on economic policy (informal norm).

The aim of this article is to set out both the debates on these issues and actual policy changes that occurred in the area of economic governance during 2005 ⁽³⁾. The emphasis is on the euro area, but the reader should be aware that, for instance, the Stability and Growth Pact applies, with some qualifications, to all EU Member States, while the Macroeconomic Dialogue is, in theory at least, also an EU-wide institution. The article begins by briefly reviewing economic developments, including wage developments, in Europe as the backdrop against which the debates took place. It then looks in turn at the performance of fiscal and monetary policy, and draws conclusions regarding the role of macroeconomic policy in explaining the outcomes described. It then proceeds to describe policy reforms and debates during 2005, focusing on the reforms to the SGP enacted in the spring, and the debates on governance and the policy mix that occurred in the context of the review of the Lisbon strategy, the rejection of the Constitutional Treaty, and the meetings of the Macroeconomic Dialogue.

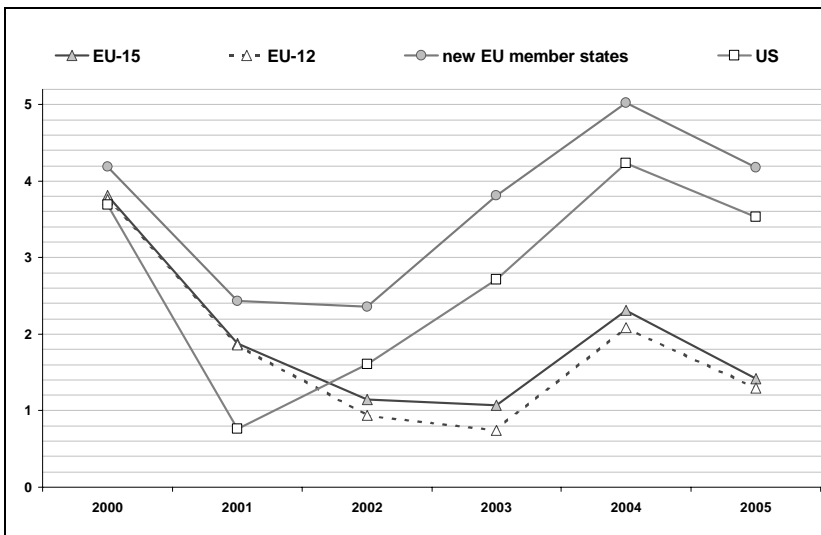
1. Economic developments in 2005: renewed disappointment

The economic recovery that, in western Europe, began in 2004 ran aground already in 2005. Higher oil prices in the course of the year – they peaked at around USD75 a barrel in the late summer, following a series of hurricanes that disrupted the oil industry in the Gulf of Mexico – were a major cause, along with the lagged impact of previous appreciation of the euro. Domestic consumer demand and investment continued to disappoint, not least reflecting anxiety regarding employment and pension prospects, and sluggish wage growth. The only bright spot was a further boost to net exports. Both the USA and

³ This article focuses on macroeconomic policy issues. Employment policy questions, in particular, and the Lisbon strategy more generally are dealt with in the article by Philippe Pochet in this volume.

the New Member States of the EU also suffered a similar reversal of growth compared with 2004, but maintained their substantial growth advantage over the EU15 (around 2 and 2½ percentage points respectively). It was only because of very sluggish productivity growth that this poor economic growth performance in western Europe actually translated into a small rise in employment and a marginal decline in unemployment rates in 2005 compared with 2004.

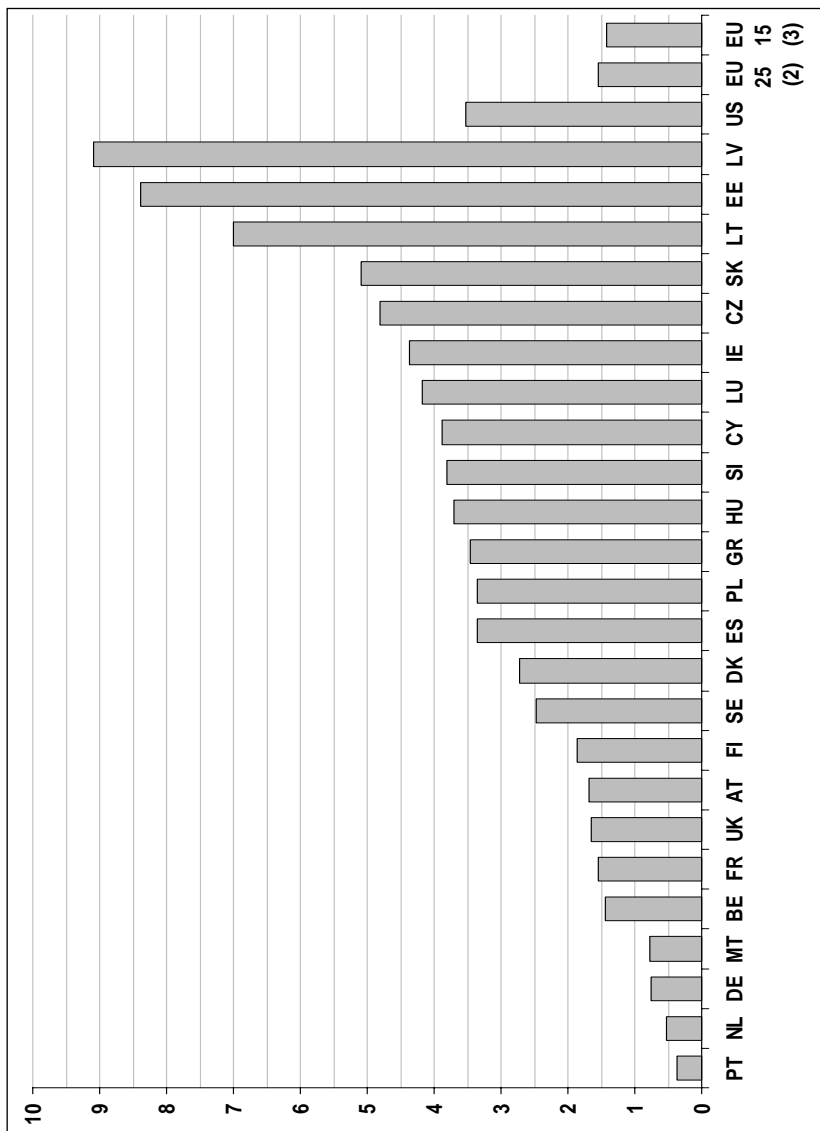
**Figure 1: Growth performance in the EU and the USA
(real GDP)**



Source: AMECO.

For 2006 prospects are set to improve in western Europe, however, whereas there are increasing signs that the US economy is slowing, as house prices there cease to rise and households become more concerned about rising levels of personal debt. Indeed, on the basis of once again more optimistic forecasts and confidence indicators at the end of the year, the European Central Bank raised interest rates in December 2005.

Figure 2: Real GDP growth 2005



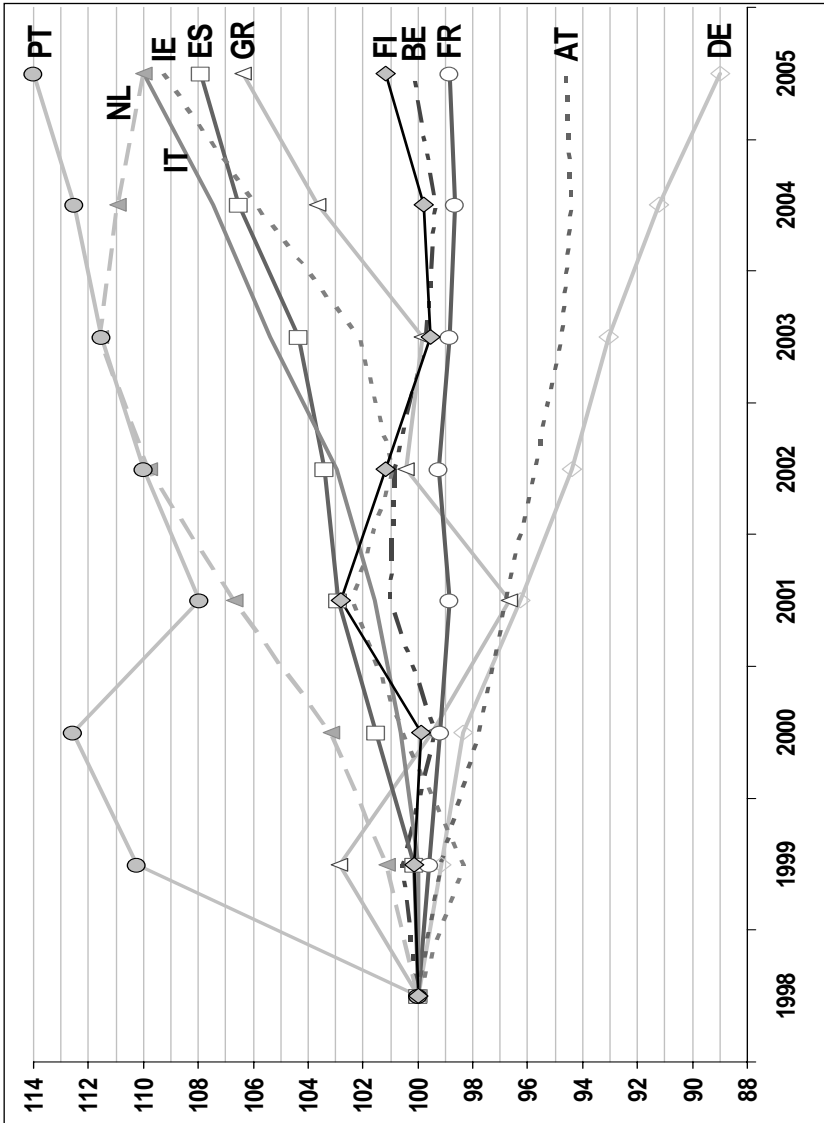
Source: AMECO.

It is noticeable that all the eight central and east European NMS grew faster than all the EU15 countries, except for Luxembourg and Ireland in 2005, marking the continuation of an established trend. The large west European Continental economies (IT, DE, FR) continue to languish at the bottom of the rankings (and because of their size drag the EU12 and 15 averages down); however, recently-successful Portugal and the Netherlands performed even worse. The three Baltic states again recorded the fastest growth. The UK's 2005 growth rate virtually halved compared with the previous year, leading to a substantial fall in the rankings; the UK faces similar imbalances to those in the US. Against the background of the overall growth slowdown, the differences in national economic growth rates widened further compared with 2004: five countries did not manage 1% growth – Italy virtually stagnated – while at the same time the best-performing countries put on an additional spurt, raising their already-high 2004 growth figures by more than one percentage point.

More generally there is evidence that relatively high-income countries in the EU25 have a low growth rate, and vice versa, implying a generalised trend towards convergence; notable exceptions are Ireland and Poland respectively.

At the same time, within the euro area there are worrying signs of increasing divergence, in terms of intra-EMU competitiveness, raising important questions for economic governance in the currency area.

Figure 3: Real effective exchange rates (1998 = 100)



Source: AMECO.

Economic and monetary union was supposed to lead to increased *convergence* between the participating countries: intensified trade links and competitive pressure would, it was argued, force a convergence of price (including wage) trends. Within a monetary union (i.e. in the absence of an exchange rate) this means that the competitive position – technically the “real effective exchange rate” – of each member state vis-à-vis the others would remain broadly constant. Figure 3 shows that, far from leading to convergence via competitive pressures and intensified trade, EMU appears to have led to increasing divergence.

Wages and prices in Germany have been relentlessly driven down compared with the EMU average, raising German competitiveness within euroland by more than 10%. Austria initially followed the same path, but more recently has corrected, moving back towards the average. Meanwhile Spain and Italy have steadily (and Ireland has more recently) lost competitiveness against the average to about the same extent (10-15%). This was initially the case with the Netherlands, but more recently a downward correction has occurred.

Worryingly, this seems to indicate that cumulative causation effects in both directions (vicious and virtuous circles) take fast and slow-growing economies in opposing directions for considerable periods of time. (Example: a fast-growing economy has higher inflation and thus, given a common nominal interest rate, lower real interest rates, which stimulates its economy further. This phenomenon is sometimes called the Walters’ critique.) A correction via deteriorating and improving trade balances, in fast and slow-growing economies respectively, takes considerable time and can only reliably be expected to work in small countries (Austria, the Netherlands).

If the EMU is not to come under intolerable strain, it seems unavoidable that prices will have to rise considerably faster in, notably, Germany, while the rate of increase in Spain and Italy will have to decline ⁽⁴⁾. There are some faint signs that, finally, Germany is

⁴ One reason why this might not be the case is that the higher inflation in, say, Spain is needed to bring up the price *level* up towards the EMU average (and vice versa in, say, Germany). To some extent this may reflect the Spanish situation, but not the German, nor the Italian.

recovering, and with it also the pace of nominal pay rises ⁽⁵⁾. Spain has been overheating and slower wage and price growth there is both needed and should be manageable. The real “problem child” is Italy, where prices have been steadily rising faster than the EMU average, despite very slow growth. Necessary unit-labour-cost (i.e. wages with respect to productivity) and price moderation may require an outright and painful recession, unless the Italian social partners can resolve the situation with a concerted prices and incomes policy (and/or measures to boost productivity growth). Italy is not usually considered a corporatist country in which social partner agreements could achieve the necessary outcome. However, the experience of the mid-1990s, when the country was desperate to fulfil the criteria for EMU accession – and the Italian Left was in power – shows that, under certain circumstances, such agreements are possible. Already voices have been raised calling for Italy to withdraw from EMU. It would be an understatement to say that this would throw not only the EMU, but also the European integration project as a whole into a major crisis.

This raises questions about the conduct of monetary policy, as it sets the overall benchmark (for inflation and implicitly growth) around which the member countries oscillate. If that is too low, the countries at the bottom of the distribution will be flirting with lasting recession and disinflation. More urgently, though, it poses questions to national fiscal policymakers, and the European fiscal framework within which they operate. We turn to this below. Yet those responsible for wage (and price) setting at national level – in short “the social partners” – and again any European-level framework within which they may act, are also clearly a key element in this problematic. This section concludes by briefly reviewing wage trends and collective bargaining, reflecting the relevance of wages both for the “competitiveness” issues just discussed

⁵ It should be noted that, here and in the following discussion, it is not absolute wage increases that are key, but rather wage growth with respect to productivity growth (i.e. unit labour costs), and that with respect to the change in the other EMU countries, Italian wages need not fall. The growth of Italian unit labour costs must be less than that in other countries. In theory this could also be achieved by boosting labour productivity while keeping wage growth constant.

and “social” issues that are the focus of other contributions to this volume (6).

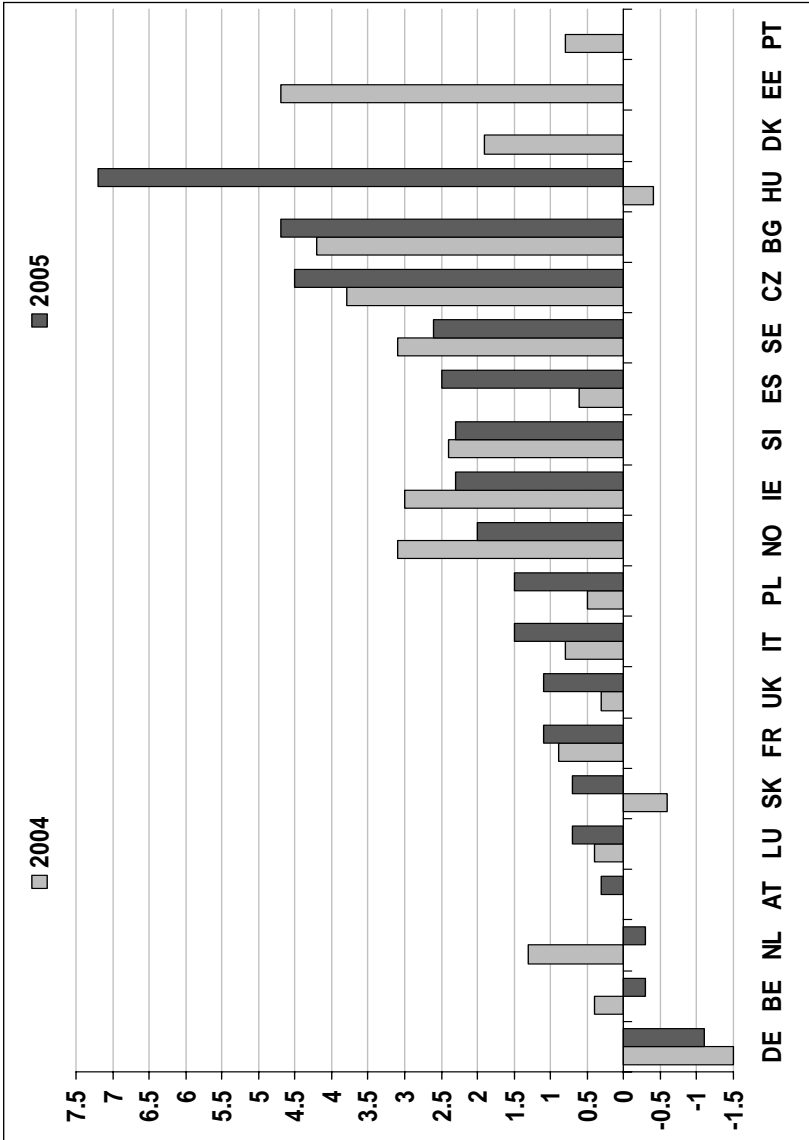
Within the context of slow growth, described above, high unemployment and employer demands for wage moderation with reference to competitive pressure from Asian countries or low-cost locations within Europe itself, collective bargaining on wages was a difficult process for trade unions in 2005, as in previous years. As a result, the real value of wages agreed in collective agreements has been under considerable pressure.

In most countries, in 2004–2005 total real wage growth was equal to or higher than collectively agreed wages, but: in Germany, Slovakia and the UK total wage growth was below that of collectively agreed wages. In 2005, only three countries achieved overall real wage growth above 3%: wage growth is again highest in some of the new Member States (Czech Republic, Hungary) and in candidate Bulgaria. In six countries wages grew by less than 1 per cent, and they were negative in Germany, Belgium and the Netherlands.

It is often argued that real wage growth should be determined by productivity improvements. To what extent is this the case? Figure 5 shows the change in real unit labour costs: this indicator measures total real wage growth (including employer contributions) against productivity growth. A negative number indicates that real wages have failed to keep pace with productivity growth (and, at the macroeconomic level, implies a shift in national income away from “labour” in favour of “capital”).

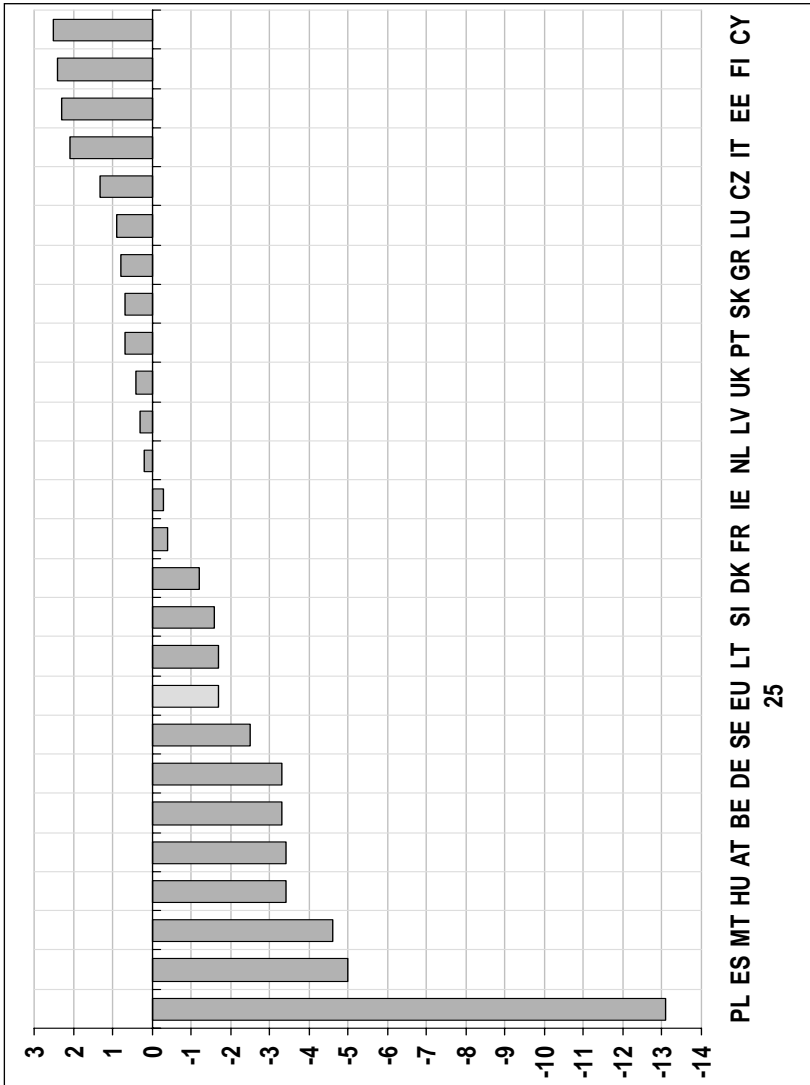
⁶ The following paragraphs draw on empirical work in Keune (2005).

Figure 4: Total real wage growth (2004-2005)



Source: Keune (2005).

Figure 5: Real unit labour costs, change over 2001-2005



Note: Ratio of compensation per employee to nominal GDP per person employed.

Source: AMECO.

Over the period 2001–2005, for the EU25 real unit labour costs declined by almost 2 per cent. The largest decline took place in Poland, followed by Spain and Malta. Major labour cost declines of about double the average can also be observed in Germany, Belgium, Austria and Hungary. These countries indeed improved their competitive position, as reflected – for the EU12 – in Figure 4 and the discussion above. Only in four countries do we observe an increase in real unit labour costs of more than 2 per cent over this five-year period. And even here this is not always linked to wage increases. For example, in Italy increased unit labour costs – and its loss of competitiveness – stem first of all from a decline in productivity.

Whatever the cause, these diverging wage-minus-productivity trends are what is largely driving the divergence within the common currency area identified above. The specific problem for EMU countries is that, in the absence of an exchange rate, and thus the ability to depreciate the currency, competitive balance can only be (re)attained via changes in actual wages and prices. Countries needing to reduce their wage/price level with respect to the other EMU countries basically have two analytically distinct options. (In practice they are combined in various ways). Either they use the national Phillips Curve or they must reach agreement on wage (and possibly price) moderation between national social partners and make it stick.

The former strategy simply means allowing (or even causing) a recession or at any rate slower economic growth in order to reduce wage and price claims. Clearly this has huge costs in terms of output and employment. The “effectiveness” of such a strategy can be enhanced by implementing “structural reforms” of the neo-liberal variety (reducing unemployment benefit, employment protection legislation, etc.). Countries with strong bargaining institutions, on the other hand, have the option of reaching agreement on wage moderation (and limiting price increases) while maintaining demand growth. In the past countries such as Ireland, the Netherlands and Austria have made use of this approach.

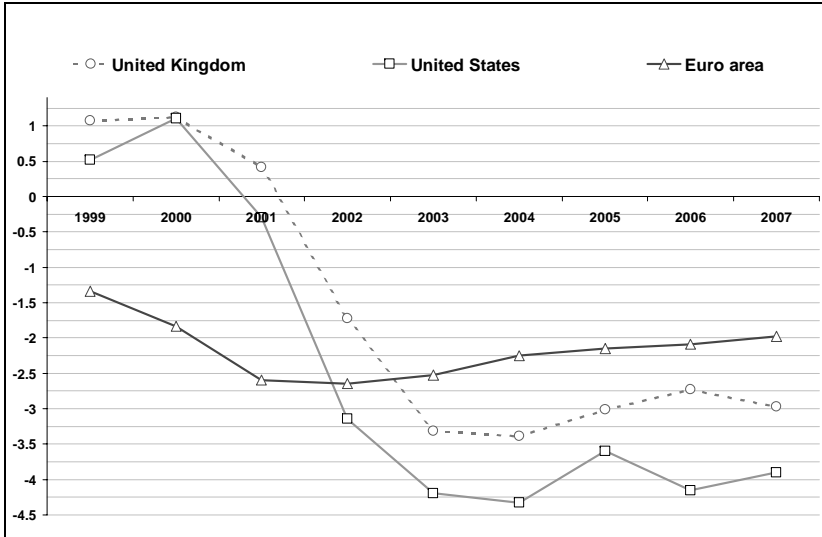
2. The role of macroeconomic policy

The standard explanation for the failure of western Europe, and especially the large eurozone economies, to grow fast enough to meaningfully reduce their high levels of unemployment is, of course, that these economies are sclerotic and in urgent need of labour market and other “structural” reforms. Space constraints prevent a detailed critique of that position here. Instead Figures 5 and 6 suggest the need to look for a complementary, if not alternative, explanation of the persistent failure of the euro area to recover from the 2001 downturn, and thus also the disappointing performance in 2005, in adequate macroeconomic policy. They compare the extent to which monetary and fiscal policy were used in the euro area, the US and the UK to offset the crisis. (For a fuller analysis of the role of macro policy see the contributions in Watt and Janssen, 2006).

2.1 Fiscal policy

Figure 6 shows the extent to which governments consciously reduce taxation or increase spending in order to offset an economic downturn (the “cyclically adjusted” figures take out the effect that the downturn itself has in raising spending and reducing revenues, the so-called “automatic stabilisers”). Faced with a major downturn, euro area governments barely reacted with discretionary fiscal policy measures: the cyclically adjusted deficit increased by only around 1 percentage point (p.p.) of GDP (a large part of which came in 1999/2000 when the economy was still doing well, and was thus actually pro-cyclical). Indeed, discretionary fiscal policy actually tightened in 2003 and 2004, despite the persistent weakness of economic growth, and this was maintained in 2005. By contrast the British and US governments responded energetically, swiftly expanding demand by a substantial 4-5 p.p. of GDP; in the US this was primarily the Bush tax cuts (and the so-called “war on terror”), in the UK higher government spending on public services. Even allowing for the larger “automatic stabilisers” in the euro area – where welfare states are more developed than in the English-speaking countries, and so public revenues and spending are more sensitive to the economic cycle – the difference in reaction by fiscal policymakers is striking.

Figure 6: Cyclically adjusted government balance



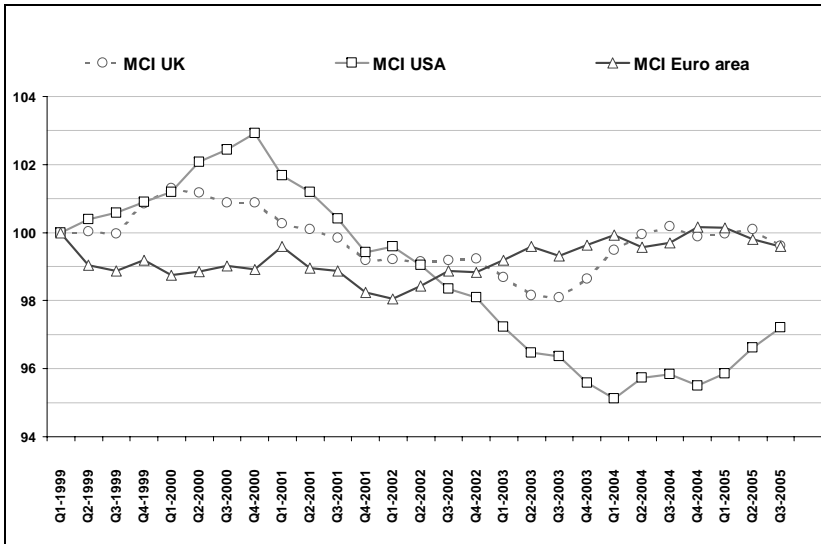
Note: 2006 and 2007 are forecasts.

Source: OECD.

2.2 Monetary policy

If anything, the picture is even clearer with respect to monetary policy, at least comparing the euro area and the USA. The aggressive interest rate cuts by the US Federal Reserve led to a sharp fall in short-term interest rates there; moreover this was supported by a substantial decline in the external value of the US dollar. As a result the monetary conditions indicator (MCI – see technical note) in the US plunged from 103 at the end of 2000 to just 95 in early 2004, giving the US economy a huge monetary boost that helped (together with expansionary fiscal policy) to pull the US economy out of its downturn. Once the economy stabilised, the Fed began raising interest rates (and the dollar appreciated during 2005), leading to a progressive tightening of the monetary conditions, while remaining well below their initial level.

Figure 7: Monetary conditions indicator
(1st quarter 1999 = 100)



Source: Own calculations: date ECB and BoE.

Technical note on MCI: The index is calculated using quarterly values for the percentage change in the nominal effective exchange rate and percentage-point changes in short-term interest rates. In line with econometric estimates of the expansionary effect on the euro area economy of a 1% fall in the NEER and a 1 p.p. fall in the interest rate, they are given a weight of 0.15 and 0.85. Clearly this weighting will differ for the US and the UK: the NEER is likely to have a smaller effect in the larger, more closed US economy, and a somewhat larger effect in the smaller, relatively open UK. However, experimenting with other weightings produced results that did not differ significantly from those presented in the graph using the same weighting for all three countries

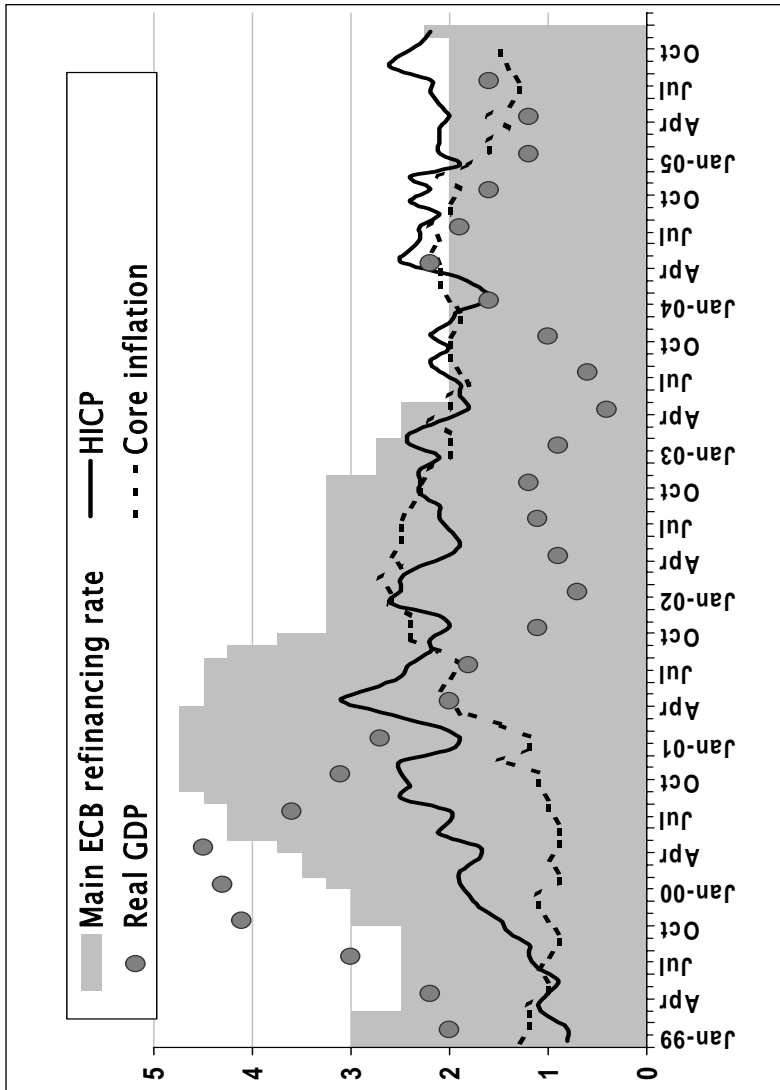
The euro area, by contrast, has been characterised by a roughly three-year initial gradual loosening of the monetary conditions – initially driven very largely by the sharp depreciation of the euro – but only

down to 98 points. This was equally gradually reversed over the subsequent three-year period, the index returning almost exactly to its starting point. Thus monetary conditions in the euro area began to tighten, despite the downturn, a full two years before this occurred in the US; in the UK the expansionary trend of the monetary conditions continued for 18 months beyond the euro-area turning point. On top of this come the very different magnitudes of the changes in the MCI in the US and the euro area, *prima facie* evidence of a more “activist” policy approach in the US (7). In the euro area 2005 saw a marginal loosening during the first three quarters, reflecting primarily the (surprising) depreciation of the euro against the US dollar.

As shown in Figure 8, in December the ECB raised interest rates for the first time in more than two-and-a-half years. Although the quantitative impact of a 25 point rise in base rates should not be exaggerated, the start of what is expected to be a series of rate hikes at this early stage in the recovery is clearly significant. Economic activity in the euro area as a whole has only just begun to recover and is still erratic (e.g. after a strong third quarter, fourth quarter figures disappointed). While headline inflation (HICP) is indeed above target and recently increased somewhat, this largely reflects higher oil prices, and HICP inflation has already fallen significantly. Even more importantly, core inflation, which strips out the volatile energy and food-related items, is substantially below target. On the basis of these growth and core inflation figures – the key indicators in a Taylor-rule type approach to analysing monetary policy decisions – the hike seems hard to justify when interest rates were not raised in the spring of 2004, for instance, when both growth and core inflation were higher than now.

⁷ While the ‘magnitude’ of the policy change in terms of economic effects cannot simply be equated with that in the MCI, because the impact of a given change in interest rates (or the exchange rate) varies from country to country, it is usually said that, in fact, a given change in monetary policy is more effective in the English-speaking countries due to the greater proportion of owner-occupied housing and the prevalence of variable mortgage rates there.

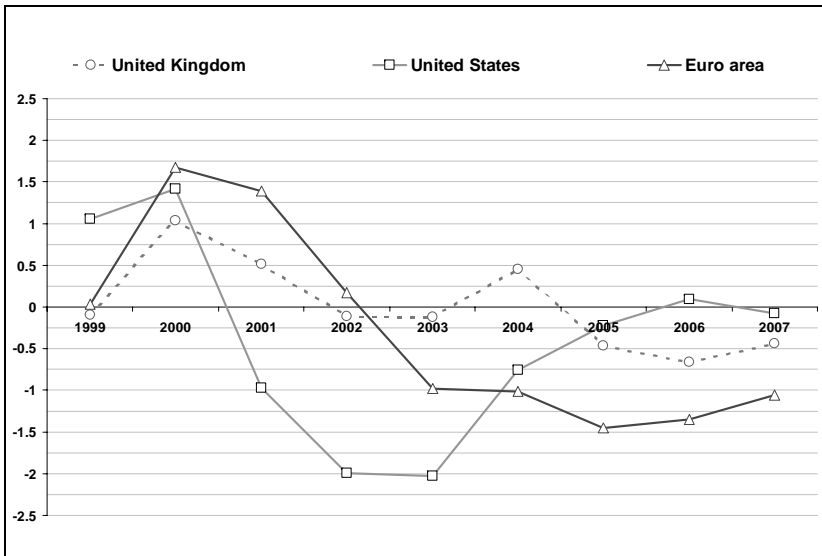
Figure 8: ECB main refinancing rates, inflation and real growth (1999-2005)



Source: ECB.

Of course monetary policy must be forward looking. The decision not to raise rates in spring 2004 proved justified by the renewed downturn in both growth and inflation. Yet the current outlook for recovery is also very uncertain. While confidence is up, the hard data are very mixed. There are many downside risks linked to global imbalances and possible euro appreciation, while the fiscal stance is expected to tighten noticeably at the start of 2006, when Germany (30% of the euro area) raises VAT by a massive 3 percentage points.

Figure 9: Output gaps



Source: OECD.

The impact of the different use of macroeconomic demand-side policies clearly shows up in the figures for the output gap. Put simply, this indicator – here, as estimated by the OECD – shows the “gap” between actual output and the level of output that, in the short run, the economy can produce without causing inflation to rise. The output gap has been negative since 2002 and is expected to remain so until and beyond 2007! This has nothing to do with structural factors – which, if at all, affect the rate of potential output growth – but solely the inability or

unwillingness of monetary and fiscal policymakers in the euro area to expand demand sufficiently to offset negative external influences and overcome sluggish domestic demand. The US was clearly hit harder by the global economic downturn, which originated in the US, but aggressive macro policies were much more successful, ensuring above-trend growth and thus a closing of the output gap within around three years.

Europe may well have structural issues that need to be resolved, and some painful reforms may indeed be necessary. But it is – to say the least – hard to understand the constant focus on such reforms when Europe is repeatedly sacrificing growth and employment opportunities simply by failing to deploy – painless! – tools of aggregate demand policy. This confirms the widely held belief that Europe is suffering not least from inadequate “economic governance”, that the institutions, legal provisions and norms established at EU level for the conduct of macroeconomic policy are inadequate. The remainder of this article discusses the debates and reforms in this area during 2005.

3. Reform of the Stability and Growth Pact – a step forward? ⁽⁸⁾

3.1 A new SGP?: the changes as of March 2005

As so often in economics, changes in policy came about less by force of intellectual argument than by (negative) developments in the real economy and, in this case, the political crisis that resulted from the stand-off between Commission and Council, and the deep split among Member States that reached a head at the end of 2003, concerning whether or not to open excessive deficit proceedings against Germany and France. The proposed solution to the crisis came in the form of European Commission proposals for reforming the Pact that were endorsed by the Council in March 2005 ⁽⁹⁾.

⁸ For a more extended discussion see Watt (2005a).

⁹ The text (Annex II) can be downloaded from http://europa.eu.int/european_council/conclusions/index_en.htm

Five areas for improvement in the working of the Pact were recognised as necessary by the Commission: the need to improve the “economic rationale” of the Pact, improve “ownership” (read: willingness to comply), avoid pro-cyclical policies in upturns and in downturns, and pay greater attention to debt and sustainability issues. This showed a recognition of at least the most obvious failings of the Pact and of the main elements of the sustained critique by economists of its operation.

Based on this diagnosis, the following key changes – alongside a number of more technical issues (more reliable data, better forecasts etc.) – were introduced:

- The medium-term objective (MTO) is no longer to be “close to balance or in surplus” for all countries; instead account is to be taken of national specificities (especially debt, potential growth and investment expenditure), leading to differentiated MTOs for each country. However, this is limited to allowing an MTO of a 1% cyclically adjusted deficit (in other words the leeway is just 1 p.p. of GDP).
- The convergence period to the national MTO has been extended and clothed in woolly language: while a benchmark adjustment of 0.5% of GDP each year is reiterated, more is expected in “good” and less in bad times. Moreover, Member States will only have to “explain” deviations from the recommended adjustment path.
- Major “structural reforms” that raise potential growth and improve public finances in the longer run may justify deviations from the national MTO. Pension reforms – the introduction of funded elements requiring tax incentives, and thus higher government deficits, in the short run – are explicitly mentioned as a case in point. However, the 3% reference limit remains valid.
- In applying the excessive deficit procedure, the Council has specified the “relevant factors” to be used in determining whether a country exceeding the 3% limit “really” has an excessive deficit.
 - * The previous exception of a severe economic downturn has been softened to allow for an accumulated loss of output due to protracted very slow growth

- * Spending on the Lisbon agenda, especially R&D and innovation policies
 - * Debt sustainability – which is to be given greater relevance – and public investment
 - * Financial contributions to international solidarity and European unification
 - * Pension reforms are again specifically mentioned as justifying a deficit, an allowance being made for up to five years for countries introducing fully funded systems.
- Last but not least, the deadlines before identifying excessive deficits, taking action following a policy recommendation, and for the deficit to actually be corrected have all been extended.

3.2 Evaluation: good for fiscal policy but not necessarily for economic governance

The response to the Council decisions was largely hostile. Many of those mainstream commentators that had criticised the Pact's rationale began to argue that it was no longer worth the paper it is written on.

In my view the evaluation is mixed. The reform has addressed some of the most obvious failings of the SGP as originally designed. There is no economic justification for a 3% limit. While that limit has been reiterated, countries facing difficulties in meeting the 3% ceiling or the close to balance medium-term target now have a whole range of possible factors that they can call upon to justify their inability to meet the targets. Considering fiscal policy alone, this is almost certainly a good thing: Europe has suffered job and output losses in past years as governments have tightened their belts in an already difficult situation and/or have failed to give an adequate fiscal boost when needed to bring the economy out of stagnation. The additional scope created to invest public money – as required under the Lisbon Strategy! – in areas such as infrastructure and education is an important step; it is disappointing, though, that controversial policies to “privatise” pension systems are specifically endorsed under the changed Pact as a means for governments to justify deficits.

However, fiscal policy cannot be considered alone. On the contrary, the Maastricht architecture is one in which it is the monetary authority that ultimately determines the level of nominal demand in the economy, based, amongst other things, on the stance taken by (or expected to be taken by) the fiscal authorities in aggregate. The ECB reacted very critically to the reforms announced. There must be concern – although there is little evidence that the fiscal stance plays a large part in ECB interest rate decisions – that real or imagined “fiscal uncertainty” will be used to justify tighter monetary policy. A looser fiscal but tighter monetary policy would be a bad deal for the European economy and particularly for non-owners of financial assets (i.e. most workers).

On the Left there were voices welcoming the “death” of the Pact in terms of (social democratic) governments throwing off the shackles of Brussels and being freer to pursue Keynesian fiscal policies. Yet, it needs to be underlined that the social-democratic vision for Europe is one of increased policy coordination and the establishment of Europe-wide “rules of the game”. Allowing national governments (of whatever political colour) to do what they will in such an important area as fiscal policy is incompatible with that vision. The Left in many countries will be glad of an ally in Brussels when right-wing governments are seeking to give tax cuts to their wealthy patrons.

What would have been the alternative? It would have been preferable to indicate clearly in advance those areas of spending which are considered to be public investment and then to exclude such spending from the deficit calculation: the remaining spending would have to be met from taxation over the economic cycle (i.e. a balanced cyclically adjusted current budget). This is the “golden rule” as practised, successfully so far, in the UK. In order to emphasise the rationale of the Pact (preventing inflationary pressure leading to tighter monetary policy) the national inflation rate – specifically whether it is above or below the ECB target – should have been emphasised as a central indicator of whether countries should be running tighter, or are able to loosen their, fiscal policy. Similarly, the savings behaviour of the national private sector is also important. Countries with high private savings – such as Germany – have more scope than those – such as the US or UK –

where private savings are low (or even negative). Indeed, they *must* run fiscal deficits, unless they get a major boost from net exports ⁽¹⁰⁾.

The recent compromise on the SGP is imperfect but marks a step forward: it reflects a more realistic way of thinking about the economy over the previously dominant neo-liberal view. Having said that, fiscal policy is a secondary battle-ground. It is in a sense unfortunate that the SGP has attracted so much attention. Monetary policy is the core of the Maastricht system, and progress in European employment and economic growth depends on a growth-oriented monetary policy. If that is to be achieved without sparking higher inflation, improved coordination between monetary and fiscal policymakers and wage and price-setters – in short better “economic governance” – will be necessary.

4. Economic governance and Macroeconomic Dialogue: no end of debate

4.1 The review of the Lisbon Strategy

The spring of 2005 saw the culmination of a number of initiatives to revitalise the EU’s Lisbon Strategy – dealt with more fully by Philippe Pochet – with the publication of the Commission report “Working together for growth and jobs: A new start for the Lisbon Strategy”, adopted by the Brussels Summit of the European Council. The five-year review of the Lisbon Strategy should have been an occasion to reflect also on issues of macroeconomic policy and governance. After all, the role of macroeconomic policymaking (the “policy mix”) was explicitly mentioned as a key condition – one of three mentioned in paragraph 5 of the Lisbon Presidency conclusions ⁽¹¹⁾ – for the success of the strategy. Moreover, in paragraphs 22 and 23 “stimulating growth and employment” was explicitly stated as a goal of macroeconomic policies,

¹⁰ This is because of the mathematical identity that net private-sector savings (savings minus investment) plus the government deficit must be equal to the current account balance (cf. Godley *et al.*, 2005).

¹¹ http://europa.eu.int/ISPO/docs/services/docs/2000/jan-march/doc_00_8_en.html#1.

alongside “preserving macro-economic stability”; the importance of the Macroeconomic Dialogue (see below) in ensuring policy consistency was emphasised, as was the contribution of fiscal policy to growth and employment (reducing the tax burden on labour, raising public investment). In an attempt to push the issue up the political agenda, the ETUC held a major conference devoted to the role of macro policies in achieving the Lisbon targets shortly before the Brussels Summit (cf. Watt and Janssen, 2006).

Yet instead of an evaluation of the role of macro policies, the Commission document clearly revealed a further downplaying of the role of macroeconomic policy since the strategy was launched in 2000. There are merely two ritualistic references to “stability oriented” and to “sound” macroeconomic policies in the Commission report. The second reference calls for their “continued pursuit”. But if, as is implied, they have been pursued in the past, why is it the case that, although they have not brought the required results in terms of growth and employment in the first five years of the Lisbon Strategy, they are expected to do so in the second five? There is no discussion of monetary policy, the SGP, reorienting fiscal policies towards greater investment, adjusting the Community budget or the Macroeconomic Dialogue. One must assume that either these are not considered important for attaining the Lisbon goals, or they are already optimal. Given the analysis above, neither position appears tenable, all the more so as they were part of “Lisbon anno 2000”.

4.2 Implications of the rejection of the Constitutional Treaty for economic governance: Eurogroup strengthened anyway

2005 was also notable for the rejection of the Constitutional Treaty in ratification referenda in France and the Netherlands (although it received parliamentary or popular approval in a number of countries). In terms of economic governance issues, however, the implications of this are extremely limited, for a number of reasons. First, it had proved very difficult to reach a consensus within the European Convention’s working group on economic governance on changes in the Maastricht architecture (Schubert, 2003; Watt, 2005b), so that the reforms proposed in this area by the Convention were of a marginal nature. Arguably the only significant change is the formal establishment of the

Eurogroup – the group that brings together the finance ministers of the 12 EMU member states prior to monthly meetings of the ECOFIN Council – which until then had been little more than a gentlemen’s agreement, and the creation of an elected Eurogroup President, with a 2½ year term (rather than the former 6-month rotating presidency).

Second, the heads of state and government could not agree at the Rome Summit, at the end of 2003, on the draft proposed by the Convention (cf. Schubert, 2003); the text finally adopted by heads of state and government (July 2004) contained a number of amendments compared with the original draft, almost all of them of a regressive nature in terms of moving towards a “Social Europe” (ETUC, 2004). Noteworthy in the present context is, in particular, the inclusion of “price stability” as one of the goals of the European Union. This substantially bolsters the position of the ECB, as it now also has its primary goal, namely stable prices, as part of its secondary goal (promoting the goals of the Union), thus virtually immunising it from criticism that it has not paid enough attention to the real economy.

Thirdly, having said that, the failure to ratify the Treaty – as important as it may be in political terms – has, in turn had little effect in the area of economic governance. For it is striking that the one important change – the formalisation and strengthening of the Eurogroup – has been put into practice despite the failure to ratify the Treaty. It is one of those numerous Treaty provisions that have been enacted anyway on the basis of unanimous agreement in the Council.

Linked to this, two Council committees (the Economic and Financial Committee and the Economic Policy Committee), both of which prepare various aspects of the work of the EcoFin Council, have established “Eurogroup working groups”. This can be seen as a further small sign of incremental institutional progress in the area of economic governance and a further slight differentiation between the governance mechanisms for those countries in and those out of EMU.

4.3 Positions around the Macroeconomic Dialogue (MED)

The Macroeconomic Dialogue (MED) was established in 1999, just after the start of EMU, under the German Presidency (for a detailed description of the MED see Koll, 2005). It remains a little-known

institution. Its main characteristics can be set out briefly as follows. The MED forms part of the European Employment Pact – the other two pillars being the coordinated strategy for employment (focused on the employment policy guidelines in the so-called Luxembourg process) and the economic reforms (Cardiff process): thus its aim is to contribute, via an improved macroeconomic policy to a “sustainable reduction of unemployment” (Presidency conclusions), where sustainable can be translated into “consistent with price stability”. The specific contribution of the MED is to institute a dialogue between the actors responsible for the policy mix – monetary, fiscal and “wage” policies – to promote positive interaction between the actors. Importantly, the MED is the only institution that brings together all the relevant macro actors to discuss the policy mix.

The MED takes place twice a year at political level, in each case prepared by a meeting at technical level. The discussions are confidential and there is currently no provision for issuing formal statements or reports as an institution: “The substantive core of the MED is an exchange of information and ideas” (Koll, 2005: 183). In particular actors discuss their analysis of the economic situation and prospects, formulate their own intended responses to the unfolding situation with a view to the goals of higher employment and non-inflationary growth and, lastly, state their expectations of how other actors should respond. At no time is the autonomy of any actor called into question.

Macroeconomic developments and positions ⁽¹²⁾

Against the background of disappointing incoming data for the fourth quarter of 2004, concerns about the medium-run effects of the sharp euro appreciation of 2004, and uncertainty about the economic outlook in 2005, especially given major global imbalances. the ECB pointed in official statements to concerns on the inflation front from the pace of

¹² The reader is advised that both the technical and political level meetings are “confidential” in the sense that no official statements are issued. The following therefore merely gives some of the basic ex ante positions taken by different actors, as perceived by this author, and as represented also in public pronouncements. Disproportionate space is given to ETUC views.

credit growth and house-price increases in some areas. The social partners were united in taking a more sceptical view of the prospects for recovery. The ETUC rejected a focus on individual credit and real-estate markets, and emphasised the key role of wages and unit labour costs for the medium-run inflation outlook: collective agreements in important sectors pointed to continued wage moderation in 2005, while past wage moderation had led to a major increase in the profit share without, so far, leading to higher investment. Thus it was essential that interest rates were not raised, as exchange rate appreciation – which was expected to continue¹³ – had significantly tightened the monetary conditions (see above).

Against the background of the Commission's SGP recommendations, discussed above, there was substantial public debate on the SGP and economic governance issues. Opinions differed considerably on the need for reform of the Pact. The key ETUC demand was to "Lisbonise" the Pact, i.e. to enable member states to raise spending on the Lisbon priorities, without this being considered an infringement of the excessive deficit constraints. Under a common monetary policy, countries needed more, not less, scope to run fiscal policies appropriate to national conditions. On financial sustainability issues raising the pace of economic growth and employment rates was put forward as the best contribution to ensuring longer-run sustainability. There was some support for SGP reform along these lines from amongst the employers' associations, particularly to permit greater public investment. On SGP reform the ECB forcefully expressed its concerns that SGP reform would lead to Member States running more expansionary fiscal policies. The Commission drew attention to a number of practical difficulties in reforming the Pact, such as how to address the trade-off between allowing for country-specific factors and ensuring equal treatment of countries by the Commission.

¹³ Virtually all commentators were convinced that 2005 would see further euro appreciation and a decline – perhaps precipitous – in the value of the US dollar. In the event the euro fell back substantially during 2005 from a high of around USD 1.36 to below USD 1.20 (around 12%).

In the Autumn discussions took place in the shadow of the sharp rise in oil prices during the summer. There was concern that the dual effect of such rises – depressing demand and growth while raising prices and possibly also inflation expectations – would make the task of setting monetary policy, but also negotiating appropriate wage increases, more difficult. There was general agreement that higher oil prices should not be factored into higher wages (“second-round effects”), but equally that monetary policy should not be tightened in an attempt to curtail oil-induced price rises, unless there was evidence of such second-round effects. But so far, there was no sign of such effects.

The social partners were to a very large degree united in emphasising the downside risks (to output) rather than the upside risks (to prices), and calling on the Bank to delay interest-rate rises for as long as possible. The Bank stated in a number of press releases and statements that ongoing wage moderation had helped to ensure that the expansionary stance of monetary policy had been maintained despite upward pressure on the headline rate of inflation. Once again, though, developments on financial and credit markets were seen as a risk, and it was vital that the ECB did not lose the price-stability “capital” it had built up (low longer-run inflation expectations).

Thanks to cooperation between the Institut für Makroökonomie und Konjunkturforschung (Düsseldorf) and the European Trade Union Institute, the ETUC was, for the first time, able to present its own economic forecast to the meeting, in “competition” with those from the Commission, ECB and UNICE. On the basis of, amongst other things, a less sanguine forecast for the strength of the recovery in 2006 and different views on the extent to which (or whether) “potential growth” has declined, the trade unions called on the ECB to underpin the recovery and swiftly close the output gap by cutting its base rates (with fast-growing euro area economies offsetting by tightening fiscal policy).

Other discussions between MED actors

The year 2005 saw two technical-level meetings on the economic and employment situation between trade union and employer representatives and one top-level bilateral meeting between the ETUC and the ECB. All these meetings are informal in nature, but they are to be pursued in coming years and, it may be hoped, will contribute to

cementing a more trust-based relationship between key actors responsible for the macroeconomic policy mix at European level and, in tandem with the MED, potentially opening up scope for a more cooperative approach to policymaking.

4.4 Exchanges between policymakers through the media

Discussions on the economic developments described above, and more specifically on the interaction between the three central macroeconomic policy areas – monetary, fiscal and wage policy – also took place between policymakers in and via the media. The media debate broadly followed a long-established pattern, with some nuances during 2005.

Statements in the media tended to consist of appeals to other actors to “live up to their responsibilities”. The ECB, in its monthly press conferences and on other occasions called on the social partners to stick to the policy of moderate wage increases and on governments to promote structural reforms under the auspices of the Lisbon agenda and, in particular, to keep their fiscal house in order. Specifically the ECB was highly critical of the reform of the SGP described above. An ECB press release (21 March) stated that the Bank was “*seriously concerned about the proposed changes to the Stability and Growth Pact*” and insisted on the need to “*implement the revised framework in a rigorous and consistent manner conducive to prudent fiscal policies*”.

On the other hand a number of high-profile members of the Eurogroup took a strong public position during the last few months of 2005 that the ECB should not raise interest rates. They included the Eurogroup President, Jean-Claude Juncker, but also the French, German and other finance ministers. Ultimately, however, such efforts were to no avail: the ECB raised its main refinancing rate in December 2005.

It is tempting to interpret the proclivity of policymakers to make suggestions on the appropriate behaviour of other actors through the media as a sign that the institutional structures of policy coordination are not adequately developed in the EMU. Certainly such exchanges are not characteristic of the economic governance regime in, say, the UK.

Conclusions

The year 2005 marked yet another disappointment for the European economy, and another lost year in the attempt to reach the Lisbon employment targets and become “the most competitive” economy in the world by 2010. The analysis above suggests that inadequate stimulation from the side of macroeconomic policy was an important part of the reason for this, rather than the real or supposed lack of “structural reforms” beloved of mainstream discourse. This, in turn, lends credence to criticisms of the economic governance system in Europe, and especially in the EMU, as sub-optimal and part of Europe’s problem, rather than part of the solution. Perhaps the “structural reform” that Europe needs most urgently is reform of its economic governance structures? There are some signs that some former proponents of the Maastricht architecture, in the financial media, in academia and among some policymakers, have started to become disenchanted with economic governance structures and more open to debate on their reform.

And indeed, the review of policy developments and debates in the second part of the article did point to some incremental progress in 2005, most notably in the area of fiscal policy and the Stability and Growth Pact. In terms of fiscal policy itself, SGP reform is welcome; however, it cannot gloss over the fact that, at the aggregate level, it is monetary policy that largely determines the pace at which aggregate demand can expand. If the monetary authority offsets a looser fiscal with a tighter monetary policy, nothing will have been gained (indeed, on the contrary).

The Macroeconomic Dialogue remains, in principle, a useful forum for the sort of discussions between the actors responsible for the policy mix that are necessary if Europe, and especially EMU, is to enjoy faster economic growth while maintaining price stability. The concrete impact of this little-known institution is hard to measure, however, nor is it evident that it was strengthened in 2005, although some threats to it appear to have been thwarted.

Having kept interest rates flat for an extended period at a low level, at the end of 2005 the ECB took the first step on what is widely expected

to be an extended tightening cycle. It remains to be seen how strongly the European economy will recover from its long torpor, and how resilient that recovery will be to the shocks expected or possible in coming months. One thing is clear: the Lisbon employment targets will never be met if economic policy, out of exaggerated fears about inflation (and its supposed costs), prevents the dynamic growth of domestic demand in Europe. Without that, all the “structural reforms” in the world – and Europe has seen a lot of them in recent decades – will be of no avail in the battle to reduce employment and ensure decent, meaningful work, that promotes social inclusion, for all.

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Debate around the social model: evolving players, strategies and dynamics

Introduction ⁽¹⁾

Europe's economic and social model was the centrepiece of an informal European Council in October 2005. This debate built on the issues addressed in 2004 concerning the future of the Lisbon strategy, which we examined in last year's edition of *Social Developments* (Pochet, 2005a). The future of the European social model as such can be approached in several ways. Looking at it in terms of current affairs, one might draw attention to developments such as the comeback of right-wing governments in most European Union (EU) Member States, or the failure of the referendum on the constitutional Treaty in France and the Netherlands, a reflection of growing distrust in a Europe perceived especially in working-class circles as becoming increasingly liberal. One might also point to the German elections of September 2005, which some people – including British Prime Minister Tony Blair – hoped would result in an outright victory of the Right, with Angela Merkel and the radical privatisation agenda of the CDU.

But focusing on these different aspects of current events and taking a short-term perspective could mean losing sight of what is most important. In our opinion, what has been at stake since the launch of the internal market in the mid 1980s – and even more so since

¹ This contribution is the result of a current research project on the European social model funded by the Belgian Federal Public Service (SPF) “Social Security”.

monetary union – is the choice of an economic and social model for growth at European level and in the Member States (see chapter by Andrew Watt in this volume). It is a fundamental choice, of much greater magnitude than what was discussed at the extraordinary European Council in October 2005.

This chapter will not explore the debate about the social model in itself (see on this subject the excellent article by Jepsen and Serrano Pascual, 2005) or about its various dimensions (see Goetschy, 2006), or even about the various phases of European social policy (see Pochet, 2005b). What we propose to do here is evaluate the economic and social policies of the past fifteen years in an effort to better discern the different strategies deployed by the economic and social players with a view to (re-)discovering a European growth path. We have written elsewhere about European-level changes being the result of tension between two major groups of players, whom we have dubbed “economic” on the one hand and “social” on the other (de la Porte and Pochet, 2002). In this chapter we shall distinguish four groups of players, namely two in each “camp”. This will enable us to highlight the alliances and conflicts between and within individual groups.

We shall in addition identify the goals being pursued and the chosen level (global, European, national). Each group possesses its own underlying economic vision, which lends overall coherence to its actions in the economic and social field and at the chosen level. The reading which we propose is a political reading, where the different players attempt to assert their own ideas. We are not interested here in a reading based on the interests of governments (Franco-German axis, role of small countries, strategy of the United Kingdom, etc.).

Our analysis begins with a brief presentation of the different groups involved. We shall then identify three periods: from Maastricht to the Amsterdam Treaty (1991-1997); from then until the Barcelona European Council (1997-2002); and, finally, the current period (2002-2005). We shall conclude by outlining three scenarios for the future.

1. The four groups: a brief description

Our description of the different groups involved has more to do with ideal types than with clear-cut distinctions between real players. Reality is complex, as always, and situations are often more blurred or fluid than descriptions would lead one to believe. This applies in particular to the case of the European Union, where the decision-making process can be accessed and influenced in a number of ways, where there are major sectoral differences from one policy to another, and so on. Various interpretations are possible, and we would endorse those recent analyses (Falkner *et al.*, 2005; Manow *et al.*, 2004) which stress the importance of politics and of left/right splits when analysing European developments.

1.1 The “economists” group

This group, which we refer to generically as “economists” on account of their role in the Ecofin Council and its committees, can be subdivided into two.

Group 1: Mainstream economists and central banks

This is the dominant group among the economists. It was they who brought about the internal market and monetary union. They believe that an active monetary policy is ineffective in the medium term because agents anticipate events in a rational fashion. They start from the assumption that economic and monetary union (EMU) is not an optimal monetary area. Adjustments must therefore be possible when national economies are affected by asymmetric shocks; these must be made through labour markets (flexible employment contracts, but also flexible wages), although in the first instance this group emphasises above all the link between individual and/or regional productivity and wages – rather than calling for wages to be lowered in absolute terms. The labour market must go back to being a true market, and collective functions must be confined to cases of market failure. In addition, social security deductions should be reduced and social protection – regarded as a burden – should be scaled down.

The principal level of action is the national level, the aim being to deregulate it. As for the EU, its task must be to remove obstacles to the markets in goods, capital, services and persons.

Group 2: Analysts of endogenous growth theory

On many points, the second subgroup of the “economists” is not fundamentally distinct from the first. The main difference is that it believes in bolstering the growth rate by investing in research, education and lifelong learning. These proponents of endogenous growth theory provided, *ex post*, theoretical elements to substantiate Jacques Delors’ 1993 White Paper (CEC, 1993). Unlike the mainstream economists, they are not backed by any particular social group. Their importance derives mainly from the position they hold within the Commission.

Their principal level of action is the national level. National budgets must be redirected towards growth-producing areas; so must the European budget.

1.2 The “social” group

We have likewise subdivided the “social” group into two. Unlike the two groups of economists, which are fairly compatible, these two groups have gradually diverged to such an extent that their agendas and priorities are increasingly different and even, on the most radical fringes, irreconcilable.

Group 3: The traditional Keynesian Left

These people stress the importance of macro-economic policies for growth and employment. EMU must be altered in their opinion because, unlike the previous groups, they believe that monetary policy is always effective in reducing unemployment in the short and medium term. The Maastricht criteria must therefore be modified, and the European Central Bank, taking its lead from the US Federal Reserve (FED), must back the goal of full employment. They argue in favour of establishing a European economic government.

The principal level of action is the European level, the aim being to substantially alter the monetary side of EMU and ensure greater economic policy coordination.

Group 4: The moderate Left, ETUC

This group is not guided by as clearly identifiable an economic *corpus* as the others. The role of governments is defined in relation to market failure, seen from a broad perspective. Members of group 4 do not basically take issue with monetary union. Whereas, like the previous group, they would like to see more active demand-side management, they also point out the need for a supply-side policy (human capital). Political union, the indispensable basis and pre-requisite for a true social union, must be reinforced above all else. The aim is to add an employment/unemployment criterion to the Maastricht criteria. Lifelong learning is an appropriate response to globalisation. They focus on the issues of poverty and social exclusion. They accept globalisation, whose adverse social effects must be tempered.

In their opinion, the principal level of action is the European level, which should be supplemented in order to achieve political union. Well-balanced reforms should be carried out at national level.

Having rapidly described these four groups, let us now see how their interactions and alliances have evolved during the course of the past fifteen years.

2. Developments over the past fifteen years

Three periods can be distinguished. The first covers the establishment of EMU; the second is when the final touches were put to it; the third begins with the comeback of centre-right and right-wing governments in a majority of Member States.

2.1 1992-1997: from the Maastricht criteria to the Stability Pact

The inclusion in the Maastricht Treaty of the goals of monetary union and the attendant criteria marked a victory for those who advocated deepening the economic dimension, as opposed to the social and political dimension, of European integration. EMU was devised without any proper consolidation of political integration. In other words, progress made towards political union was no match for the step-change represented by the goal of a unified monetary area. As for the social dimension, it was relegated to a protocol containing the Social Policy Agreement from which the United Kingdom opted out, thereby

preventing the real progress written into it (qualified majority voting, role of the social partners) from becoming effective until the start of negotiations leading to Amsterdam.

The European Commission's 1993 White Paper on Growth, Competitiveness and Employment constituted the first attempt at an alliance between groups 2 and 4. It quite brusquely dismissed the idea of a collective reduction in working time, which had been central to the demands of the Left during the 1970s and 1980s and was to become the priority of the French Socialists in 1997.

That alliance was a pragmatic one: the White Paper sought to summarise the different approaches within the Commission, and some of its chapters are rather contradictory. Yet the document was after all masterminded by Jacques Delors (Ross, 1995) and sent out a coherent overall message.

It was not until later that a more theoretical basis (endogenous growth theory) was advanced to justify the Commission's approach. An article appearing in the journal "European Economy" in 1996 stated: "*Since the publication of the Commission's White Paper on growth, competitiveness and employment, the ideas contained in the latter report have been progressively incorporated into the Community's economic policy message (...). In this context, the present technical study tries to give a short synthetic description of current economic thinking relative to the White Paper*" (CEC, 1996: 33).

This line of reasoning was taken up in other documents, most notably the Green Paper on innovation (CEC, 1995: 9), which points out that: "*The new theories of growth (known as 'endogenous') stress that development of know-how and technological change – rather than the mere accumulation of capital – are the driving force behind lasting growth*".

But the Ministers of Finance stuck firmly to their radical positions, rejecting a policy of major infrastructure projects ("missing links") and insisting above all else on budgetary discipline.

2.2 1997-2002: from selection for EMU to the Barcelona European Council

In 1997, a majority of governments included social-democrat or socialist parties for the first time in the history of the EU (Manow *et al.*,

2004). New Labour in the UK tried to unite modern-day socialism with liberalism around the idea of a “third way”.

The negotiation of the Amsterdam Treaty opened up new horizons. Group 1 (mainstream economists) sought to set in stone the criteria for monetary union, and spearheaded the adoption of a Stability Pact.

Group 3 (and 4) tried unsuccessfully to alter the Stability Pact and added the word “growth” purely for the sake of form. Group 3 received backing from the German Minister of Economics, Oscar Lafontaine, when the SPD won the 1998 election, but he soon resigned from office. The main achievement was the macro-economic dialogue between the European Central Bank (ECB), social partners, Ministers of Economics and Finance, and Ministers of Social Affairs.

Group 4 achieved a Title devoted to employment in the Treaty, which constituted the point of departure for the European Employment Strategy (EES) (Goetschy and Pochet, 1997) and, more generally, for the open method of coordination.

Groups 1 and 2 were caught unawares by the insertion of the employment Title and by the push for a European Employment Strategy, since they thought monetary union could be used as a tool of social deregulation. As pointed out by Dyson (2002: 101) “*The ECB-centric eurozone policy community had to absorb and accommodate the so-called Luxembourg ‘process’ – with its annual employment guidelines and national action plans – and the Cologne ‘process’ – the Employment Pact and the macroeconomic dialogue. These developments opened up the dialogue about EMU by transforming the definition of who was in the policy domain*”. However, the “economists” fought back on the wages and labour-costs front and went on the offensive again regarding pensions, seen by them as problematical in terms of stabilising public finances in the medium term.

More generally, the long-term sustainability of public finances was to become the priority theme for group 2 (Sapir *et al.*, 2003).

Mention should also be made of the adoption in 1998 of the Cardiff process on freedom of movement for goods, services and capital. This process never gained a high profile and remained largely a paper exercise.

A Commission Communication on social protection, published in 1999, paved the way for using “open methods of coordination” in this area (CEC, 1999). Four major themes were addressed: pensions, poverty and social exclusion, healthcare, and making work pay.

It is interesting to contrast the positions of the four groups on this subject.

Group 4 regards social protection as a factor of production (Netherlands presidency of 1997) and, with support from the 1999 Finnish presidency, attempted to Europeanise this issue. Group 1 opposed the idea, on the grounds that social protection is above all a “burden” which should be offloaded and privatised as far as possible. Group 2 did not tackle this matter directly, focusing instead on the sustainability of public finances. However, inasmuch as it believed that budgets should constantly be balanced, deficits should not be allowed to accumulate and investment in the factors of growth (education and research, in its opinion) should be encouraged, it was only logical that the public share in social security should be cut back. Group 3 was opposed to these approaches and to the “marketisation” of social protection, especially because its prime objective was to get people into jobs whatever the cost. Strong social protection system is still seen as an alternative to capitalism.

2.3 Freeze frame: 2000, the Lisbon European Council

The Lisbon European Council of 2000 was a key moment. It took place in a context where social-democrat governments had a clear majority in Europe and where alliances were shifting. Group 2 was distancing itself from group 1 and aligning itself with group 4. This alliance between 2 and 4 was personified by Maria João Rodrigues, former Portuguese Minister of Social Affairs and holder of a French doctorate in economics, who played a crucial role as a broker. Investment in a knowledge-based society was the concern shared by both strands. According to Rodrigues (2002: 14), “*The Lisbon strategy launched by the European Council of March 2000 was precisely the elaboration of a European comprehensive strategy for economic and social development in the face of new challenges: globalisation, ageing, faster technological change. Its central idea is to recognise that, in order to sustain the European social model, we need to renew it well*”

as well as to renew its economic basis by focussing on knowledge and innovation. This should be the main purpose of an agenda for structural reforms”.

The open method of coordination (OMC) was the procedural brainchild of group 4 in an attempt to achieve European social convergence.

The compromise between groups 2 and 4 relates to levels of action as well, since the OMC contains both national reform programmes (priority of group 2) and a means of creating a social Europe (priority of group 4) (Vandenbroucke, 2001).

The European dimension was constructed by adopting joint European indicators (at one stage there were almost 150 for the EES) and by standardising the national data contained in the various national action plans. The aim was to facilitate comparisons and to continuously improve the indicators; the reason for the proliferation of indicators was to give a fuller picture of complex realities. This applies in particular to the fight against poverty and social exclusion (Atkinson *et al.*, 2002). Group 1 for its part focused on a smaller number of more classic structural indicators.

An undeclared war was also being waged between groups 1 and 4, especially on the subject of pensions (de la Porte and Pochet, 2002; Pochet and Natali, 2005). The response from group 4 to the offensive from the Finance Ministers and their committees on pensions was to create the “pensions OMC”, designed to highlight the social aspects of these.

Group 4’s preferences likewise lay behind the “poverty and social exclusion OMC”. It is worth noting that (subject to resource availability) measures to combat poverty and social exclusion are fully compatible with the views of the mainstream economists’ group, provided that this policy of combating poverty does not take centre-stage.

This alliance between groups 2 and 4 around the knowledge-based society deepened the divide between the two social groups. One of these (group 3) criticised the liberal thrust of the policies advocated in the EES, the absence of a clear European dimension with binding

measures, and the weakness and underlying prescriptive intent of the indicators (particularly the use of employment rates as a key indicator) (Salais, 2004). But group 3 became increasingly marginalised, above all because it had no strong mouthpiece within social-democrat inclined governments. Their only institutional achievement – macro-economic dialogue – was reduced to its simplest expression. Moreover, several heavyweight intellectuals (Esping-Andersen, Atkinson, Boyer, etc.) rallied to the cause of group 3 (Portuguese, Belgian and Greek presidencies but also the Commission). Group 4 had no such resources to validate its theses.

This consensus lasted for just over two years before several changes occurred. The first was political. In 2002, the Barcelona European Council signalled the end of the predominance of social-democrat governments and the start of a new liberal ideological offensive. The takeover happened by means of a streamlining process involving economic policy (broad economic policy guidelines - BEPGs) and employment (EES). The argument went that these processes needed to be simplified (it was easy to lose the plot) and better integrated. This resulted in a fresh balance of power in two senses.

First of all, the already weak links between employment and social security were now severed. The two communities/networks became structurally separate (even though some crossovers, or *passerelles*, were envisaged). Social security matters were now dealt with in a distinct process, and its component parts – pensions, poverty and social inclusion, healthcare – were to be brought together at a later stage, in 2006 (for a critical approach, see Marlier and Berghman, 2004). Secondly, a third element – the market in goods and services – was added to macro-economic policy and employment. The new process in fact incorporates under the heading “micro-economic policy” the objectives formerly contained in the Cardiff process.

On the grounds that the OMC was ineffectual, a general offensive was launched (both by groups 1 and 2 and by group 3, all of which had always been suspicious of the OMC).

The first Sapir report (Sapir *et al.*, 2003) on the (lack of) growth in Europe symbolises the change in group 2's approach. This report proposes organising the European budget around factors of

competitiveness and growth (research and development and investment in these activities), which are the priorities of group 2. On the other hand, it totally ignores the social dimension, including social cohesion and environmental concerns. It advances the hypothesis that in this configuration (without the common agricultural policy, whose budget would be slashed) a budget of 1% of Community GDP would be sufficient.

2.4 2003 onwards

The operation of the OMC first began to be discredited in the reports penned by former Dutch Prime Minister Wim Kok – the Kok 1 report (Kok *et al.*, 2003) on the EES and the Kok 2 report (Kok *et al.*, 2004) on Lisbon – and then in critical remarks by the Commission. (It should be remembered here that when the President of the Commission, José Manuel Barroso, took over from the Socialists in Portugal, he put a stop to all innovations related to the Lisbon strategy in his country). Then came the onslaught on the social model, of which the Sapir 2 report drawn up by the Ecofin Council is emblematic (Sapir, 2005). This report maintained that there is no such thing as a European social model, but only national social models, and that the Union must therefore concentrate mainly on structural reforms and on completing the internal market, especially in services.

The alliance between groups 2 and 4 collapsed over the European dimension of the OMC, with group 2 insisting that social affairs must be handled at national level.

Three different sets of changes were carried out. The first entailed grouping together the various processes, with a view to simplifying (“streamlining”) them and subordinating the European Employment Strategy to economic objectives. The second involved abandoning European aspirations and falling back on national reforms. The third consisted in addressing issues in terms of competitiveness and no longer in terms of a society based on knowledge and innovation. We shall now review these three areas of change.

a) Streamlining the various processes

The streamlining of the processes with a view to simplifying them led to the EES becoming increasingly subordinate to the BEPGs and to

internal market objectives. The players in the Cardiff process (which was not operating, as we have already said) discovered a new opportunity to enter into the dominant Lisbon process by way of a micro-economic approach. Commissioner Verheugen and his officials did not pass up this opportunity (2). One sign of the shifting balance of power was the fact that group 1 achieved two references to wages and one to overall wage costs in the 24 integrated guidelines (see last year's *Social Developments in the European Union*).

b) European aspirations are abandoned

The discourse on the OMC as a component part in the formation of the European social model came to an end. The sole objective now assigned to it is the implementation of reforms at national level. The Kok report makes no bones about this: all parties know what must be done (the diagnosis exists and is a good one); what is lacking is the political will at national level to do it (i.e. to implement reforms which may be politically and socially awkward). The OMC is designed to help overcome such obstacles. This strategy runs counter to the approach whereby the European level serves as a discussion forum for deciding which are the best national policies and attempting to generalise them (the "learning" and "bottom-up" aspects; for developments in this respect see Zeitlin, 2005).

This strategy, aimed at abandoning the European dimension, means not only diminishing the role of European indicators by making them fewer in number and less visible, but also diminishing the comparability of national plans. The European Employment Strategy is a case in point. Having spawned more than a hundred indicators, the EES downsized to sixty or so, consisting of basic indicators and contextual indicators. In November 2005, the Employment Committee tasked its "indicators" subgroup with drawing up a limited set of indicators (25 was the number suggested) for the new integrated strategy. The German delegation even proposed scrapping the so-called contextual indicators, whose purpose is to make more sense of the primary indicators. Having twenty or so indicators would mean getting back to the most traditional

² I am grateful to Jonathan Zeitlin for this comment arising out of his interviews.

indicators (which can be found in any OECD publication) and shelving the idea of including additional indicators to give a fuller picture of complex social realities.

Once greater flexibility is encouraged at national level in order to prioritise the issues of greatest concern to each country, one loses the database of information supplied by relatively standardised national action plans (i.e. covering all aspects of the EES). In its first review of the Lisbon programmes, the Commission identifies 290 priorities including 94 new ones.

There has been criticism regarding the number of indicators and the excessive rigidity of national plans, but a total lack of any alternative strategy. Basically, those Member States in favour of continuing the process have endeavoured to restrict the changes but have not put forward any persuasive arguments in favour of this approach. The Party of European Socialists decided at the end of 2005 to launch broad-based internal deliberations about the European social model.

However, the attempt to eliminate the social OMCs, or at least to make them entirely peripheral, has been a partial failure. The NGOs involved in the process and, to a lesser extent, the European Trade Union Confederation (ETUC) have been the most vocal critics of this attempt to sideline the OMCs.

As stated above, the continued existence of the poverty/inclusion OMC is not seen as a problem by groups 1 and 2, provided that it remains marginal compared with other policies.

c) Competitiveness – the number-one priority

The objective of competitiveness carries more weight than the knowledge-based society in the Lisbon reform. Along with this there is an offensive in favour of the “services” directive, which incites competition between one country and another (Van den Abeele, 2005), as well as initiatives related to “better regulation” (see chapter by Van den Abeele in this volume).

While the Commission’s document on the European social model (CEC, 2005) was in its preparatory stages, an internal memorandum clearly revealed the mainstream economists’ state of mind: “*Ensuring a*

sufficient level of investment in developing (education, training), preserving (health) and activating (child and elderly care, employment measures) human capital’. According to this way of thinking, social policies are nothing but a tool used in achieving economic performance. Healthcare is no longer a basic right but a means of producing healthy workers. Esping-Andersen’s idea (Esping-Andersen *et al.*, 2002) of investing in young people is viewed in terms not of equal opportunities but of reinforcing human capital: “*eliminating disincentives to work*” (even though governments have revised the benefits they provide in relation to net wages, this issue persistently returns to the agenda with particular reference to people who are disabled or on sick leave); “*enhancing the efficiency of social policies and services; and finally organising the financing in a way that minimises the negative impact on employment and growth*”. It says in the body of the text that this should be done by abolishing employers’ contributions and by giving workers a choice between social security contributions and net wages. All DG Employment did in the face of this steamroller was to issue a feeble text recalling priorities already agreed on.

The only new element is the proposal to establish a Globalisation Adjustment Fund, although we should recall here that such a fund has existed since the 1960s in the United States.

3. What of the future?

Circumstances appear to be particularly difficult for the two “social” groups. On the one hand, they are more divided than ever over their strategic vision of the future. On the other, enlargement has not strengthened the position of these groups. Let us look in more detail at both of these aspects.

The split between groups 3 and 4 about priorities has widened since the adoption of the draft constitutional Treaty. The rejection of the draft Treaty has radicalised part of the group in its criticism of Europe’s liberal leanings (see Fitoussi and Le Cacheux, 2004). Nevertheless, and this became especially plain in the wake of the French “no” vote, the members of group 3 are not proposing any well-structured alternative project, apart from enhanced cooperation around monetary union. A critical attitude to the conditions of enlargement makes it difficult for

this group to rethink its strategy in relation to an enlarged Europe which is continuing to expand (start of negotiations with Macedonia, Serbia and Turkey).

Group 4 not only supports the constitutional Treaty but is also seeking to salvage what it can of Lisbon. Maria João Rodrigues, who was the linchpin of the Portuguese presidency, acted as an advisor to the Luxembourg presidency and caused it to revisit the issues of innovation and the knowledge-based society. These themes are to be found in the conclusions of the Luxembourg European Council held in March 2005.

Enlargement heightens these centrifugal tendencies. It has produced three developments.

1. The social dimension does not emerge any stronger – neither its legislative, collective bargaining nor soft regulation component. Even though the central and eastern European countries constitute anything but a monolithic bloc, their shared experience of emerging from Communism hardly endears them to the notion of developing a supranational social dimension, especially since they do not enjoy full freedom of movement for workers (see chapter by Dalila Ghailani in this volume).
2. There is a wider diversity of social systems. It is difficult to slot the new Member States into the classic categories established by Esping-Andersen and others.
3. The law of large numbers dictates procedural changes (for example, peer review in the Cambridge process now takes place in four subgroups, with a plenary session to summarise the discussions).

By contrast, other changes have strengthened groups 3 and 4. They (together with group 2) prompted the revision of the Stability and Growth Pact. Admittedly, many economists – including some in the mainstream – had criticised the Pact for being rigid and inappropriate. Admittedly, it had been proposed that certain expenditure, such as investment in the future, should no longer be taken into account when calculating deficits. It nevertheless remains the case that the revision in itself (despite its imperfections - see below) signals a victory over what had appeared to constitute a strong consensus among the economic and

monetary elites (Watt, 2005). Be that as it may, a careful reading of the new Pact tells us two things. Firstly, whereas there was a consensus around amending the Pact, there is still no strong consensus about what it is authorised to do, nor about the margin of flexibility around the 3% threshold. Secondly, more than one page out of 14 is devoted to pensions, with a view to permitting/facilitating the transition from pay-as-you-go system to personal account (the cost of this switch is substantial: while contributing to their own pension pots, workers must still pay for today's pensioners) (see also the chapter by Andrew Watt in this volume).

4. Where do we go from here?

Having taken stock of the players involved and their ideas, let us now look ahead. In our opinion, three scenarios can be sketched out. They are of course over-simplified but do indicate three different ways forward. We have named them "Voice", "Loyalty" and "Exit".

4.1 Voice

This scenario entails a renewed alliance between "social" groups 3 and 4. This could for example take the form of promoting enhanced cooperation around EMU and the countries belonging to it. There would need to be a strong consensus on pushing social issues up to European level and constructing solidarity at this level.

One example in the social policy field would be the creation of a minimum wage proportionate to average earnings in all 12 countries. The main weakness of this scenario is the very unfavourable context (e.g. with the Netherlands now turning Eurosceptic). Its main advantage is the formation of a consensus about putting additional touches to monetary union. Moreover, the "voice" scenario reduces complexity because decisions are taken by 12 countries – or by 15/16 if some of the new Member States join EMU between now and 2010 – and not by 25, 27 or even more.

4.2 Loyalty

This second scenario relates to an alliance between groups 2 and 4 aimed at preserving Lisbon and returning to the initial project. The advantage is that, contrary to the first scenario, it is not in crisis. It

prolongs a trench warfare situation whereby each party attempts to have a phrase favourable to its position inserted into European Council conclusions. This is the usual method of resolving conflicts in the building of Europe. The limitation is that it would appear difficult to resurrect such an alliance because, despite the French referendum, the protagonists' positions have scarcely changed. However, the Commission's proposal of March 2006 to create a Globalisation Adjustment Fund may constitute a step towards re-establishing the alliance between groups 2 and 4. It is not a matter of declaring globalisation to be intrinsically good (group 1) or bad (group 4), but of attenuating its most obvious social consequences, namely restructuring.

4.3 Exit

This scenario starts from the assumption that the balance of power at European level is structurally unfavourable to social policy. The principle of subsidiarity should be reapplied to social affairs (the European Union should play no part in it), and the European institutions should focus on the changes needed in respect of economic and monetary affairs. They should for instance carry out a proper reform of the Stability Pact or else confront the issue of tax, especially company taxation.

The limitation of this approach is that it is hard to justify, because the discourse constructed about social Europe over the past few decades has been the need for it to be created. Its advantage is that it focuses on essentials and on the real sources of social tension, i.e. the chosen monetary and economic model. What is more, this scenario mounts a rearguard action against groups 1 and 2, which have always advocated a predominantly national social dimension.

Obviously none of these scenarios will be followed to the letter, but they do nonetheless illustrate all the potential choices, alliances and strategies.

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EU enlargement: from central and eastern Europe to Turkey

1. An unprecedented enlargement

In 2004 the European Union took in ten new Member States, including eight central and eastern European countries (Estonia, Hungary, Latvia, Lithuania, Poland, the Czech Republic, Slovakia and Slovenia) and two Mediterranean islands (Cyprus and Malta). Bulgaria and Romania are already scheduled to join in 2007; several Balkan states are waiting in the wings (Croatia, Bosnia, Macedonia, Montenegro and Serbia), and perhaps it will be Turkey's turn in a few years from now. Thus the Union has carried out an unprecedented enlargement, in terms of both the number of new members and their population size. The arrival of the Ten has contributed towards the political and economic reunification of a continent ravaged by the Second World War and then divided by fifty years of Cold War. But the absorption is by no means complete.

Enlargement has been a success on the whole, and the newcomers' economic results have outstripped the European average. There are still significant disparities, however, and enlargement is still causing concern after more than a year: fears of mass immigration, business outsourcing and institutional deadlock are only partially offset by the economic prospect of new markets.

1.1 Economic and social results

In spite of persistent unemployment, growth in the Ten is above the European average. The new Member States are experiencing high rates of growth, at an average of 5.2% in 2004 as opposed to 4.2% in 2003. The growth rate in Latvia reached 9.8% in 2004, the highest anywhere

in the European Union (the average rate being 2.3%). Lithuania, Estonia, Slovakia and Poland also grew very rapidly, by 7.0%, 7.8%, 5.5% and 5.3% respectively (Eurostat, 2004). The forecasts are fairly good for all of the new Member States. The economic catching-up process seems to have begun, but it does still remain vulnerable.

The optimism is in fact tempered by two factors. First of all, the CEECs (central and eastern European countries) still have low wages and high rates of unemployment. The unemployment situation and trend varies from one country to another. According to Eurostat data (2004), unemployment is particularly high in Poland (18.4%) and in Slovakia (18.2%), where it is a major social cause for concern. Overall, the narrowing of the economic gap seems to have had few benefits in terms of giving the population access to better-paid jobs. Secondly, this catching-up process is happening in a climate of mediocre growth for the old EU Member States; the Lisbon strategy has failed. Growth in the new countries is not stimulated by such a climate. Complementary patterns of production (participation by the old and new Member States in the same international division of labour; establishment of firms originating from the EU-15 in the CEECs with a view to securing their position on expanding markets) are liable to be transformed into conflicts of interest (new and old Member States competing on comparative costs to attract businesses; risk of sectoral overcapacity across the continent) (Fayolle, 2005).

Enlargement has also had a considerable impact in other spheres. Tourists are pouring into the region. For example, the city of Ljubljana in Slovenia saw its tourist traffic increase by 23% in 2004 compared with previous years.

The fears of farmers in the east have proved unfounded. According to Eurostat data, farmers' average earnings have risen by 50% even though they do not receive the same subsidy levels as their counterparts in the west. The Ten received almost €1.3 billion in 2004 and are net beneficiaries from the EU budget.

The Fifteen themselves have derived economic benefit from enlargement, thanks to the rise in trade and investment. Imports and exports between the Fifteen and the Ten have increased substantially since accession. Businesses in the old Member States have become the biggest investors in the east. Austria, for instance, is the largest foreign

investor in Slovenia, Romania and Bulgaria, and the third largest in Hungary, Slovakia and the Czech Republic.

But competition from the east, backed by favourable tax systems, could in turn lead to reforms in some of the old Member States. Germany has already reacted to this fiscal competition by lowering company taxation from 25% to 19%. State aids are a characteristic feature of the new Member States, as are much larger tax incentives for businesses than in the old Member States. These two measures do not have the same purpose: State aids are sectoral and geared primarily towards businesses which are ailing or undergoing conversion, while tax incentives aim to attract new investors. These measures are subject to debate and political scrutiny within the enlarged EU (Fayolle, 2005).

1.2 The risk of mass immigration

Freedom of movement for workers was one area where the EU Member States demonstrated a lack of transparency and solidarity during the accession negotiations. Yet a wealth of evidence indicates that there has not been a massive wave of immigration from the new Member States¹). What is more, the facts on the ground point to this same conclusion: low mobility within the EU, the experience of former enlargements and the limited migration seen after the accession of Spain and Portugal, as well as transfers of labour between the CEECs and the old Member States prior to enlargement (Math and Viprey, 2004). This evidence did not however deter the Union, under pressure from apprehensive countries – especially those having the most extensive shared borders with the new members (Germany and Austria) – from establishing transitional periods, postponing the introduction of the right of free movement for workers in respect of nationals of the new States (apart from Cyprus and Malta).

This policy measure aroused anger and disappointment in the east (Masson, 2001). And yet, as Daniel Vaughan-Whitehead makes clear, immediate freedom of movement would have had its advantages.

¹ See the report of the European Integration Consortium (DIW, CEPR, FIEF, IAS, IGIER), “The Impact of Eastern Enlargement on Employment and Wages in the EU Member States”, Brussels, 2000.

Coupled with free movement for capital, goods and services, it would have set a different political tone for the entire process, giving the new Member States a sense of being treated as equals by equals. By easing the flow on labour markets, mobility would have helped to plug the gap between skilled labour (which suffers least from transitional periods because it benefits from bilateral mobility agreements) and less-skilled labour, a victim of long-term unemployment. Immediate freedom of movement for workers would have enabled wages and working conditions to catch up more rapidly, limiting the temptation to engage in social dumping (Vaughan-Whitehead, 2003).

In reality, the accession of the CEECs was not accompanied by a significant wave of migration, neither into the countries which – like the United Kingdom, Ireland and Sweden – decided to open up their labour markets without delay, nor into those which only half-opened them during a transitional period provided for in the accession negotiations. Not one of the safeguard clauses (concerning the internal market, justice and home affairs and the economy) written into the treaties was invoked. An initial report produced by ECAS (the European Citizen Action Service) in September 2005 paints the true picture of these much-dreaded migration flows on the basis of the data available. We shall describe the situation in just three Member States.

In the United Kingdom, workers from the new Member States were obliged to register under the Worker Registration Scheme and apply for a national insurance number. The Home Office (Ministry of the Interior) used this as a basis for producing statistics on migration flows into the UK and drew the following conclusions for the post-accession period: 175,000 workers from the countries concerned were registered between May 2004 and March 2005. They were mainly male (60%) and aged between 18 and 34 (82%). The most widely represented countries were Poland (56%) and Lithuania (15%), and the sectors employing them included factories, farms and the cleaning industry. The British economy benefited to the tune of £500 million net from the presence of this additional labour force.

In Ireland, no limits were placed on access to the labour market for nationals of the new Member States, but they did have to apply for a short-stay residence permit. Ireland upheld its right to have recourse to the

safeguard clause if its labour market was seriously disrupted (Ughetto, 2004), but no such effects materialised and the country seems to have benefited from enlargement. The presence of eastern European labour is not a new phenomenon, since Irish employers and government agencies began actively recruiting non-EU nationals in 1999 to make up for a shortage of labour. According to the Department of Family and Social Affairs, 85,000 national insurance numbers were allocated to migrants from the new countries in the twelve months following enlargement. These included 40,000 Poles, 18,000 Lithuanians and 9,000 Latvians, mainly employed in construction and hospitals (medical and nursing staff).

Sweden is not applying any transitional measures and did not opt for a safeguard clause; it guarantees nationals from the new Member States equal access to its social protection system. In the year after enlargement, Sweden received just 21,800 requests for residence permits, 60% of them from Polish nationals (Traser *et al.*, 2005).

These figures show that there is no sign of the disaster predicted. It is now accepted that fears of a huge influx of migrants were unjustified. Studies using different techniques anticipate that fewer than 100,000 to 200,000 CEEC nationals will head west once the restrictions on free movement for workers are lifted (Barysch, 2004).

1.3 Outsourcing?

The subject of business outsourcing came under the spotlight during the enlargement process, just as it did in 1986 when Spain and Portugal joined the EU. Opinions differed about the likely consequences of such transfers. On the one hand, the trade unions were worried about the implications for jobs. On the other, it was felt that outsourcing might help European companies channel their resources into more productive jobs. Might this not also be a boon for the economies of the new countries, enabling them to catch up in economic and social terms?

This phenomenon began several years ago and has affected many European companies. Direct foreign investment (DFI) in the CEECs reached almost €150 billion at the end of 2003, and was concentrated mainly in Poland, the Czech Republic and Hungary. The bulk of this investment (60%) came from the EU. The volume of DFI, expressed as

a percentage of their GNP, was 35% in the eight new Member States, i.e. more than the average for the Fifteen (33%).

This DFI often corresponds to the relocation of companies from west to east, even though there has been little publicity about these shifts as the companies concerned know full well how unpopular any production transfers are with the trade unions. Numerous EU companies have decided to move into central and eastern Europe, and sometimes even to outsource part of their business (2). All sectors of activity have been involved: *IKEA*, *Audi-VW*, *Philips*, *Whirlpool* and *Nokia* have set up fully-fledged export platforms in the new Member States, the relocation process proving to be much more extensive than initially announced. All the central and eastern European countries have gained from such outsourcing moves, and it has affected most sectors: Hungary in respect of assembly and spare parts in the automobile sector (*Audi*, *Opel-GM*), the electrical infrastructure industry (*ABB*) and domestic appliances (*Philips*, *Lebel-Electrolux*); Poland in the automobile sector (*Fiat*, *Ford*, *VW*, *GM*, *Daewoo* and *Volvo*). Slovenia has benefited from transfers of production by the Swedish compressor firm *Danfoss*, the Italian paper company *Saffa* and the German household appliance company *Bosch-Siemens*. Estonia has managed to attract Sweden's largest textile company, *Boras Wärfveri*, resulting in a huge number of job losses, since 83% of total output now originates from its Estonian production unit.

But are wage costs really the number-one reason for these relocations? Some analysts believe that outsourcing on grounds of low wage costs could not take place on a large scale, in that the low wage levels would be cancelled out by lower levels of productivity. It is true, on the one hand, that an investor's decision to relocate must take into consideration the productivity rates which can be expected in future. On the other hand, productivity levels are low throughout the central and eastern European

² It is sometimes difficult to detect what motivates a foreign investor: outsourcing or fresh investment. If the foreign investor seems mainly to be motivated by the local market but, after a year or two, chooses to export more than 80% of its output, this means that its prime strategy is to use its subsidiary in the new host country as a platform for exporting to external markets, generally those of the EU.

countries, which implies that the comparative advantage diminishes once unit production costs are taken into account. But that is not to reckon with new investor's desire and capacity to alter those production levels by investing heavily and by exporting to its new subsidiary all the requisite production techniques and technology of the parent company to achieve higher productivity rates as soon as possible. Thus investors take account not of local productivity rates but of those which can be achieved by installing their own production techniques. Wage levels therefore represent the key variable in a relocation. The availability of skilled labour on the spot is a vital element in raising the productivity of the new subsidiary to a higher level.

Is outsourcing now a thing of the past? All the indications are that large-scale manoeuvres will not cease in the enlarged Europe. Better exchanges of information are likely to encourage new operators to try their luck in the CEECs. *Toyota-Peugeot* decided in 2002 to invest in the Czech Republic; *Ikarus-Renault* decided at the same time to move into Hungary. More recently, the *Siemens* group has decided to relocate up to 10,000 jobs to eastern Europe over the next few years, beginning with 2000 telephony jobs to Hungary. The airline *Lufthansa* has announced its intention to outsource the bulk of its accounting and purchasing operations to Poland. The American domestic appliances firm *Whirlpool* announced in February 2003 ⁽³⁾ that it was to relocate its washing-machine production unit from Amiens in France to Slovakia (with the loss of 225 jobs). In January 2004 it was the turn of the Iberia subsidiary of *Philips* to announce the closure of an industrial lighting factory in La Garriga (100 jobs lost) and its relocation to Poland ⁽⁴⁾. The South Korean firm *Samsung*, based in Barcelona, decided in late January to transfer part of its production to Slovakia ⁽⁵⁾. Such outsourcing will without doubt continue in coming years (Vaughan-Whitehead, 2005: 103-119).

³ <http://www.humanite.fr/journal/2002-04-15/2002-04-15-32287>.

⁴ http://www.slovakradio.sk/rsi/fr/economie/txt/040204_Zapfirmy.html.

⁵ http://www.expatica.com/source/site_article.asp?subchannel_id=83&story_id=8713&name=The+multinational+exodus.

1.4 Democratic, political and institutional aspects

Political reforms were the *sine qua non* for EU accession. The establishment of lasting democracy is one of the greatest achievements of enlargement, and even of the post-enlargement period, given that its effect is snowballing. Indeed, the prospect of joining the EU has spurred on democratic movements in other eastern European countries such as Georgia, Ukraine and the Balkan states. The new Member States have in addition made their voices heard within the Union, influencing in particular its policy towards Russia. Poland and Lithuania were the first countries to back the “orange” revolution in Ukraine, playing a crucial role in making the EU – which was slow to react – take a stance. The Ten, reputedly more liberal than most, do not hide their differences on sensitive issues. They argue alongside the United Kingdom in favour of free movement of services. Many misunderstandings have also arisen. Discussion of the Bolkestein directive has reawakened fears of social dumping in view of the continuing sluggish growth in France and Germany. The outsourcing debate has provoked tension, with the new countries believing that it can assist their development while the old Member States are worried about the absence of tax and social harmonisation.

The EU institutions have not suffered the paralysis that some predicted. Nevertheless, the institutional reforms set out in the constitutional Treaty (put on ice following the “no” votes in the French and Dutch referendums) and devised in order to facilitate decision-making in the Council – a relaxation of qualified majority voting and an extension of this system to various other spheres – and in the Commission – a reduction in the number of Commissioners – may well prove necessary in future. Europe’s leaders also acknowledge that discussions in both Council and Commission are more complicated with 25 members, and that the interests of the ten newcomers frequently diverge from those of the Fifteen.

2. Turkey on the road to EU accession

In December 2004 the European Union took the historic decision to open accession negotiations with Turkey. The official talks began on 3 October 2005, even though European public opinion had major

reservations ⁽⁶⁾. Turkey's application to join the EU is one of the major debates marking out the process of building Europe, others being the European Defence Community, entry of the United Kingdom, the Maastricht Treaty and the single currency, and the constitutional Treaty. Whether or not Turkey belongs to the Union means much more than the accession of one more Member State: it provokes debate about the very nature of European construction, raising at one and the same time issues to do with borders, power, values and aspirations. Enlargement has hitherto been predicated on a logic not of agglomeration but of conversion. Future Member States have been expected not merely to be geographically or historically close, but to share the same values, institutions and aspirations. By envisaging the integration of a country which is very different in terms of its history, institutions, political life and economic and social development, the EU is launching a debate about its own identity and future. Turkish accession therefore represents, for the years ahead, a gamble on the capacity of the EU to undergo a thorough and geographical transformation.

2.1 Pitfalls aplenty

Europe granted Turkey applicant status at the Helsinki summit in 1999 (European Council, 1999). Under Prime Minister Recep Tayyip Erdogan, the country rushed through democratic reforms so as to comply with the accession criteria. The EU-25, Austria included, called on the European Commission in December 2004 to draw up a strict negotiating framework, which it did in June 2005 (European Council, 2004). All that remained for the Council to do was reach an agreement on this framework with a view to opening the negotiations on 3 October 2005. But controversy resurfaced at the end of July when, in a declaration annexed to the protocol extending its customs union with the EU to the new Member States, Ankara asserted that its initialling of the document did not signify recognition of Cyprus. Furthermore, public hostility to the accession of a Muslim country was one of the reasons for the failure of the referendums on the European Constitution in France and the Netherlands in May/June 2005. The

⁶ Only 35% were in favour according to the July 2005 Eurobarometer survey.

French and Dutch “no” votes dampened the politicians’ enthusiasm. Animated discussions took place in France and in Germany, where Gerhard Schröder’s successor Angela Merkel has come out against Turkish accession. The European Parliament, dominated by the hostile European People’s Party (EPP), dug in its heels. The UK presidency for its part expressed concern about the split which would occur if Turkey’s application were rejected: this religious and political divide could further widen the gulf between those countries with a Christian tradition and those with an Islamic tradition.

Turkey did not conceal its disappointment, and its political leaders expressed their views in no uncertain terms. Mr Erdogan called on the Europeans to face up to their responsibilities: “*either the Union will demonstrate political maturity and decide to become a force, a global player, or it will confine itself to being a Christian club*”, he stated on 2 October to officials of his own party, the Justice and Development Party, at its congress in the spa town of Kizilcahaman (7). The accession negotiations did nevertheless open on 3 October 2005, at the cost of negotiations being opened with Croatia too (8), those talks having been delayed until then due to Croatia’s lack of cooperation with the International Criminal Tribunal in The Hague.

The negotiating framework set out for Turkey does however include a number of conditions, laid down by the European leaders at their Brussels summit in December 2004. The European Commission expects the talks to last for approximately ten years. There are 35 chapters to be discussed, and every Member State will have a right of veto for each one. The mandate adopted by the Commission states that admission is the ultimate objective, but that the process remains open-ended and without any guarantee. The negotiations can also be suspended in the case of a serious and lasting infringement of the principles of freedom, democracy and respect for human rights and fundamental freedoms (no such clause had ever before been included in

7 *La Libre Belgique*, 3 October 2005, page 8.

8 Austria, Slovenia, Hungary and Slovakia were emphatic that the start of negotiations with Turkey and with Croatia must be linked.

a negotiating framework). Permanent safeguard clauses or waivers could be envisaged in the most sensitive areas, such as freedom of movement for workers or agricultural subsidies. France has moreover announced its intention to hold a referendum at the close of negotiations. French President Jacques Chirac, who is personally in favour of Turkish accession, made this concession to his own party, the UMP, which twice came out against accession and in favour of a special partnership with Ankara (⁹).

2.2 The political situation: increased compliance with the Copenhagen political criteria

Turkey has introduced several constitutional reforms since 2001, especially in its judicial system, and has adopted numerous laws making major headway in the field of respect for human rights. The pace of reform slowed in 2005 because the country embarked on a less visible phase of reform, namely practical and day-to-day implementation by the governmental and administrative authorities.

As concerns the role of the army, Turkey has reorganised the National Security Council and given more power to civilians. Various measures have strengthened parliamentary scrutiny over military expenditure. Yet the armed forces still play a prominent role in society and exert significant political influence in current debate

Several laws which entered into force on 1 June 2005 reinforce the structural reforms undertaken in the judicial sphere and bring the country closer to European standards. Reports by non-governmental and lawyers' organisations speak of a sharp decline in acts of torture and violence, although practice varies from one region to another. Greater attention is being paid to the rights of women, especially regarding crimes of honour. The entry into force of new laws and new codes has not yet been digested by all judicial authorities and, while new case law is being enacted by the Supreme Court and the Council of State, the next challenge in the reform of Turkey's judicial system will be to disseminate this embryonic case law throughout the judiciary.

⁹ Joint press conference of J. Chirac and G. Schröder, 1 October 2004, Strasbourg (<http://www.elysee.fr/documents/discours/2004/0410ST01.html>).

Improving human rights, minority rights and religious freedom has been at the centre of constitutional reforms and of the reform packages adopted by Parliament since 2001. Considerable progress has been achieved. A number of legislative changes have been made concerning freedom of expression. There is however still cause for concern regarding freedom of the press, where the reforms are not being enforced in a uniform fashion. Severe penalties, including prison sentences, can still be handed down to journalists, editors and publishers who criticise the institutions. Despite the new criminal code, certain articles are still being enforced restrictively by some prosecutors and judges. Those articles will need to be amended if the dissemination of case law by the Supreme Court and the Council of State is insufficient to protect freedom of expression. One example is the trial of Orhan Pamuk, accused of “insulting Turkish identity”, which has been deferred until 6 February 2006 ⁽¹⁰⁾.

The principle of security also lies behind the handling of freedom of association: the relevant law is in fact one of 600 adopted during the period of military rule following the 1980 coup d'état, and until the constitutional reform of October 2001 it could not be appealed against. The restrictions on freedom of association have been eased, but it is still strictly controlled by the government.

Turkey is the only secular Muslim state in the world. Secularism was laid down by Atatürk as the inviolable founding principle of the Republic of Turkey: the Constitution stipulates that no constitutional reform may ever infringe a certain number of principles, including secularism. Secularism in Turkey does not mean a separation between Church and State. It is the Turkish State which organises and totally controls the community of the faithful: the 72,000 imams are civil servants, paid and trained by the State, whose weekly sermons are written by officials at the Ministry of Religious Affairs. Secularism in Turkey means that religion is relegated to the private sphere and is completely absent from public life.

¹⁰ The author stated in an interview with a Swiss magazine in February 2005 that “a million Armenians and 30,000 Kurds were killed in this country, but no-one apart from me dares to say so”.

As far as freedom of religion is concerned, Turkey does not recognise the religious minorities specified in the 1923 Treaty of Lausanne: Jews, Armenians and Orthodox Christians (Del Picchia and Haenel, 2005).

The question of Cyprus

The EU Foreign Ministers, meeting in Newport on 1-2 September 2005, had to discuss both the negotiating framework proposed by the Commission and the declaration by the Turkish government indicating that, while agreeing to sign the protocol extending its association agreement with the EU to the new Member States including Cyprus, it still refused to recognise the Republic of Cyprus ⁽¹¹⁾. Together with the reform of the judiciary, the signature of this protocol was one of the two conditions laid down by the 25 for the start of negotiations. The protocol was signed on 29 July 2005. But the Turkish authorities immediately pointed out that their signature did not imply recognition of the Republic of Cyprus (Akgönül, 2005).

This matter had been at the centre of debate at the December 2004 European Council, which set the date of 3 October. Ankara's intransigence over Cyprus almost scuppered the agreement. The European leaders finally accepted, in exchange for the promise to sign, that Turkey's signature constituted a significant step towards recognition of Cyprus but not formal recognition. While hoping that Ankara would recognise Cyprus in due course, they refrained from making such a gesture a prerequisite for the opening of talks ⁽¹²⁾. The negotiating framework does however specify that efforts by Turkey to contribute to an overall settlement of the Cyprus problem and to normalise its relations with all Member States, including Cyprus, will be one of the factors determining the progress of the discussions.

It should not be forgotten, moreover, that UN Secretary General Kofi Annan has intervened in the complex question of Cyprus in an attempt to negotiate an overall agreement leading to reunification of the island.

¹¹ See *Le Monde*, 1 September 2005, page 6.

¹² Paragraph 19 of the Council conclusions is so vague that it shows how difficult it was for was for the Heads of State and Government to reach a compromise.

Turkey and the Turkish Cypriot community accepted the Secretary General's proposals in 2004, but they were rejected by the Greek Cypriots⁽¹³⁾. There are however reasons to believe that Mr Annan will resume his good offices and will find a positive solution to the problem prior to Turkey's possible EU accession in 2015⁽¹⁴⁾.

2.3 A mixed economic picture

Turkey, a country with some 70 million inhabitants, has a sizeable but underdeveloped internal market. Its demographic situation is gradually stabilising and, even allowing for the probable decline in Germany's population over the coming decades, the Turkish population is barely likely to exceed that of Germany by the decade 2030-2040. National per capita wealth is just 28% of the Community average for the EU-15. In terms of volume, Turkey's GDP was €242 billion in 2004 (Eurostat). These figures must however be put into perspective, since statistics on Turkey reveal only part of the country's economic life. Its hidden economy is in fact extensive, accounting for between 40 and 60% of GDP. The Turkish economy has by no means achieved its full potential owing to significant structural difficulties: a succession of rapid growth phases and crises; endemic inflation. This inflation has hampered all medium-term prospects, compelling the government to finance itself in the short term by means of high interest rates, greatly curbing the capacity of businesses to invest in the economy. Companies tend either to lodge their assets with the government, on account of the high interest rates paid for public borrowing, or to send them abroad.

Despite its scale, the economic crisis of 2001 did not have the social effects which might have been expected. Much of the Turkish economy in fact relies on the hidden economy, family solidarity remains strong and bank deposits are guaranteed by the government. Consequently, the government extended the reforms it had previously launched, but in doing so made extensive structural changes to the economy. These reforms have so far produced extremely positive results: inflation fell to

¹³ At the referendum on 24 April 2004, 64.9% of the Turkish Cypriots approved the peace plan whereas 75.8% of the Greek Cypriots rejected it.

¹⁴ See *La Libre Belgique*, 2 September 2005, page 21.

around 10% in 2004 after standing at 57% in 2001 (Eurostat), the currency is relatively stable and the banking sector has largely been overhauled. This strategy is based on a very tight budgetary policy, whereby the government compels itself to earmark a substantial primary budget surplus of 6.5% of GNP (imposed by the IMF) in order to service its debt repayments. The Turkish economy seems to have embarked on a virtuous circle of growth: reform brings about a return of confidence, a reduction of interest rates and normal financing of the economy by the banks; this in turn bolsters production, investment and consumption. Nevertheless, consolidation of this pattern is uncertain as yet because the trend is a recent one (Del Picchia and Haenel, 2004).

2.4 Social issues are lost from sight

Little attention has been paid to social issues on the Turkish political scene, and the very liberal-minded government does not pay much heed to the requirements of a changing society. The explosion in the urban population is one illustration of those changes: it shot up from 46% to 74% of the total population between 1985 and 2000, without industrial jobs and services being able to absorb this new labour force. A third of the working population is still employed in agriculture, which produces only 14% of added value. The unemployment rate remains high, at 10.3% of the working population (Eurostat, 2004), and the rate of employment (46.1% in 2004) is low by European standards (63.3% in the EU-25 in 2004), especially among women (24.3%). Yet according to some estimates half of all jobs are undeclared. In this economy dominated by small firms and small farms, the wage-earning class is less widespread than self-employment and undeclared family employment, especially for women.

This weakness of the wage-earning class does not lend itself to the development of a welfare state, which is virtually non-existent in Turkey, and problems are now starting to arise in that the rural exodus has eroded traditional networks of solidarity in villages and families. As a result, the country is languishing at 88th position in the world in terms of human development, whereas its GDP puts it in 19th place (2004). The national budget is primarily used to pay interest on debt, to restructure the banking system and for military expenditure. More is spent on the military than on education, which is incomprehensible in a

country where half of the population is aged under 25 (Moatti, 2004). The government, which despite everything was elected on a ticket of social promises, did nevertheless decide to raise the minimum wage by 34% and pensions by 21% on 1 January 2004. Yet the budgetary impact of these symbolic measures is limited and offset by further budget cutbacks.

2.5 Likely consequences of accession

2.5.1 Benefits for the EU: an unmatched strategic and geopolitical location

Turkey's accession would be irrefutable proof that Europe is not an exclusive "Christian club" and would confirm its tolerant nature. At a time when the "clash of civilisations" has come to the fore, the fact of offering an alternative to the intolerant, sectarian and inward-looking model of society advocated by radical Islamists would enable the Union to engage itself in future relations between the West and the Muslim world. Firstly, Turkish accession would prove that Islam and democracy are compatible, even though the case of Turkey is unique and not transferable to other Muslim states (Everts, 2004). Secondly, it would enable the Union to become a major foreign policy player. The new European security strategy and the concept of a "wider Europe and neighbourhood" (CEC, 2003) emphasise the importance of Europe's southern flank to its security and stress the need to ensure the stability of regions adjoining the continent. Owing to its geostrategic location, Turkey would lend a new dimension to EU foreign policy efforts in regions as vitally important as the Middle East, the Mediterranean, Central Asia and the southern Caucasus. What is more, Turkey's huge military capability and its potential as an advanced military base would constitute significant and much-needed assets for the European Security and Defence Policy. Turkey has in fact made major contributions to peace-keeping operations in Croatia, Bosnia and Kosovo, and it participated in the EU-led military and police mission in Macedonia. It headed up the International Security Assistance Force in Afghanistan until December 2002 (Emerson et Tocci, 2004).

In addition, Turkey could further boost the EU's economic clout in the world. The country's economy has huge potential even though it is still weak and inegalitarian. Turkey is a large country with substantial

resources and a young, skilled labour force. With a population of almost 70 million inhabitants and the prospect of a steady rise in purchasing power, it represents a growing potential market for goods from EU Member States. Following the emergence of the Caspian Sea basin as one of the largest oil and natural gas deposits in the world, the construction of the Baku-Tbilisi-Ceyhan oil pipeline also highlights Turkey's role as a key transit country for energy supplies. Its geopolitical location and its close links with tens of millions of Turkish-speakers in neighbouring countries would help to secure Europe's access to the vast resources of Central Asia and Siberia. Thus, Turkey would become a vital factor in securing energy supplies to Europe from the Middle East, the Caspian Sea and Russia (Independent Commission on Turkey, 2004).

2.5.2 Impact on the European Union

In institutional terms

If the negotiations are successful, Turkey's accession will not become effective until about 2015, by when the EU and Turkey will have changed significantly. The Union will have at least 27 Member States. The adjustments allowing for a better response to the needs of an enlarged Europe will have been made, and the end of the 2007-2013 budgetary period will have led to an evaluation and modification of the EU's regional and agricultural policies in the light of experience gained with the new Member States. Turkey's population will probably be equal to that of Germany by 2015; it will therefore have the same weighting in the European Parliament and in the Council. The impact of this sizeable presence in the Parliament will nevertheless be greatly curtailed by the fact that voting takes place along party rather than national lines. Furthermore, the principle of seeking consensus in important spheres of EU action (Common Foreign and Security Policy, defence, taxation) will still apply, attenuating the significance of national population size in the EU decision-making process. On the other hand, Turkey's entry would strengthen the camp of large States as opposed to the many small States which joined in previous enlargements; it would at the same time lower average economic standards in the EU, putting more pressure on the richer Member States. Finally, Turkey will probably have a preference for the intergovernmental approach, thus

helping to preserve the *status quo* in respect of the balance between the European institutions (Hughes, 2004).

In economic terms

Given the weakness of its economy (less than 2% of EU GDP in 2004), Turkish accession would have only a minimal impact on the economy of the Union. Yet for Turkey the consequences would be significant and beneficial. Full access to the internal market, including for agricultural produce not covered by the 1996 customs agreements, and the removal of administrative and technical barriers to trade could enhance bilateral trade by roughly 40%. The more favourable investment climate created by embedding the Turkish economy in a stable system would act as a strong stimulus for local and foreign investment, leading in turn to job creation and a high level of economic growth.

In terms of migration

The effect of Turkey's accession on immigration is difficult to predict. It will depend on several factors: demographic developments in Turkey and in the EU, the economic situation in the country of origin and the relative income levels, job prospects and economic opportunities, foreign demand for labour and the trend in immigration policies in European countries. Migration into Turkey from neighbouring countries, and the legal provisions needed in order to cope with this phenomenon, will have to be addressed. Lengthy transition periods will probably be negotiated with Turkey so as to put back by several years the introduction of total freedom of movement for persons. Another factor is that the Turkish birth-rate has fallen sharply in recent years and is likely to decline further as standards of living improve. This will be an even more important element ten years from now (Independent Commission on Turkey, 2004: 33).

In financial terms

The Commission and the countries making the largest contributions to the EU budget have assessed the cost of Turkish accession on the hypothesis that the measures adopted for the new members in 2004 and the next new arrivals in 2007 would be applied to Turkey. Thus the number-one budgetary heading would relate to so-called cohesion

expenditure, the bulk of which is earmarked for poor regions of the EU. With an average per capita income of around 28% of the current Community average, Turkey would be in line to derive full benefit from this solidarity-based policy financed out of the European structural funds. The Commission estimates that these funds will amount to €22.4 billion per year (at 2004 prices), i.e. a sum comparable to the average amount allocated annually to the ten new members for 2007 onwards. Turkey would also receive agricultural appropriations representing approximately 25% of European expenditure in the new Member States. This spending is put at €8.2 billion. Internal expenditure, focused in particular on border protection schemes, is estimated at €2.6 billion. The estimate of total net outlay is between €25 billion and €28 billion per year, or €75 per inhabitant of the old Member States. This sum is similar to the annual cost of the 2004 enlargement (Brehon, 2005).

The indirect effects of accession by Turkey are also very substantial. As was the case in 2004, Turkish accession would serve to diminish per capita GDP in the Community. The reduction, estimated at 9%, would follow an initial reduction of 12% which occurred in 2004. Given that the structural funds are earmarked above all for poor regions (defined as those with a per capita GDP of less than 75% of the Community average), certain regions which are currently eligible for European funding would no longer be eligible after enlargement.

Conclusions

Enlargement to take in the central and eastern European countries as well as Cyprus and Malta already belongs to the past, and a preliminary assessment can now be made. Without being unreservedly positive, it can be said today that the disaster scenarios foretold have not really materialised. Economic performance in the ten new Member States is remarkable, but unemployment remains a significant problem. Wages still lag well behind average earnings in the Fifteen, and the newcomers still have a long way to go to catch up economically and socially.

Contrary to some people's predictions, the Fifteen have not been swamped by nationals from the eastern countries. The experiences of the three old Member States which, unlike the others, did not adopt transitional measures on freedom of movement for workers, indicates

that the fear was greater than the damage done. And there is no sign that matters will be any different once these barriers are lifted throughout the Fifteen.

The other misgivings expressed ahead of enlargement related to the phenomenon of outsourcing. The process was already underway prior to accession and cannot therefore be regarded as a direct consequence of enlargement on 1 May 2004. Outsourcing has in any event enabled the new Member States to make economic progress, albeit admittedly in some cases to the detriment of jobs in the old States. These transfers are highly likely to continue.

Finally, enlargement is perceived differently from one country and social group to another. Farmers and business circles in the new Member States are generally satisfied, whereas for the unemployed nothing has changed. To a certain extent, inhabitants of the new countries feel that they are being treated as second-class citizens of the Union, since they cannot move freely around the Schengen area until 2006 and are still not entitled to work in most of the Fifteen. The disappointment is relative, however, and there is no desire to return to the past.

The subject of enlargement will still be on the agenda in the coming years: of all the accessions carried out hitherto, that of Turkey will be by far the most ambitious. The duration and outcome of the accession negotiations will depend on progress made in relation to the economic criteria and the existing body of Community legislation. The process will probably be a very lengthy one, illustrating the magnitude of the difficulties confronting this vast country and the need for Europe to pause for breath after having absorbed ten new Member States. This time-lapse will enable both parties to solve urgent problems and compensate for any adverse effects likely to be caused by Turkish accession – from which both parties would stand to gain a good deal. For the Union, Turkey's unique geopolitical location, its importance for Europe's security of energy supply and its political, economic and military clout are major assets. For Turkey, EU accession would confirm that its longstanding pro-western leanings were the right choice and that it is accepted by Europe; the country's transformation into a modern democratic society would become irreversible. If the process

were to fail, however, Turkey could suffer a serious identity crisis, and political instability and unrest could be brought to Europe's door.

Despite the country's size and nature, Turkish accession would probably not fundamentally alter the EU and the functioning of its institutions. The existing differences of opinion about the future of the integration process might be heightened, but the debate would not change at all in qualitative terms. Member States' political influence in fact depends just as much on their economic power as on their size or demography. By contrast, Turkey would play an important role in EU foreign policy, given that it borders on the Middle East, the Caucasus and the Black Sea. Admitting Turkey would also mean having to offer something new to the Mediterranean countries, to Georgia, the republics of the former Soviet Union, Ukraine, Azerbaijan and Uzbekistan (Guigou, 2003).

Accession by Turkey will nonetheless also engender numerous difficulties in terms of poverty, regional disparities and security. The most developed western regions, which already benefit from tourism and trade with the rest of the world, will gain most. The gulf between the west and east of the country will widen. For instance, the Marmara region produces a third of Turkish GDP and employs almost half of all declared industrial workers in the country. Per capita income there is five times higher than in the poorest parts of the eastern regions, where it is no more than 8% of the EU average. Moreover, Turkey is considerably poorer than the average newcomer of 2004, with a per capita GDP equal to half of theirs. Even if the negotiations last for ten years or so, this gap is unlikely to be closed. Assuming annual growth of 4% more than the EU average, the country's per capita income should reach 32.3% of the Community average in 2014, i.e. the equivalent of that of Latvia in 2004; higher than that of Romania but still well below European standards.

From a security point of view, the Iraq war has plunged the entire Middle East into an era of considerable uncertainty, and has at the same time cast a new and stark light on the risks which Europe would run by incorporating Turkey. Surprisingly enough, political commentators have not drawn attention to this aspect. One need only glance at a map of Turkey to realise that the eastern part of the country is more or less

surrounded by the five countries with which it shares borders: Georgia (250 km), Armenia (300 km), Iran (400 km), Iraq (250 km) and above all Syria (750 km). This proximity with three major Middle East countries which are regarded as unstable – Iran, Iraq and Syria – could lead to serious difficulty. If Turkey one day belongs to the European Union, it could draw the Union into the armed conflicts affecting that part of the world. Relations between Ankara and two of its neighbours, Iran and Armenia, are extremely tense at times. Under these circumstances, would it be acceptable for the EU, by virtue of having integrated Turkey into its midst, to be dragged into conflict between Turkey and Iraq, Turkey and Syria, Turkey and Iran or Turkey and Armenia? The European Union has not yet answered this awkward question.

Last of all, problems could arise in several Member States when it comes to ratifying an accession treaty with Turkey, if public opinion were to persist in its opposition and if governmental policies continued to be at odds with popular sentiment.

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The financial perspectives and the structural funds

In June 2005 the European Council proved unable to adopt the new financial perspectives for the period 2007-2013. This setback, coming soon after the rejection of the European Constitution in both France and the Netherlands, highlighted the difficulty of devising funding priorities for the enlarged Union and, hence, exacerbated the existential crisis and growth pangs afflicting the Union. Following on from the budget cuts decided by the Berlin European Council in 1999, the European Commission's proposals represented a compromise between those who backed a thorough overhaul of EU spending in favour of "future-oriented" expenditure and those who defended the goal of economic and social cohesion in the enlarged Europe. In 2002 the European Council had frozen the level of resources available to fund the Common Agricultural Policy (CAP) until 2013. It was feared under these circumstances that the so-called cohesion policy might become the adjustment variable of negotiations in 2005. The agreement reached in December 2005 heightens the budgetary austerity initiated in 1999 while paving the way towards reforming the structure of the budget on both the revenue and expenditure sides. In this chapter we shall begin by looking at the complex negotiations which resulted in that agreement for the period 2007-2013. We shall then examine in detail the future of the European economic and social cohesion policy.

1. The 2007-2013 financial framework

Two factors influenced the thinking behind the 2007-2013 financial framework: first of all, the Sapir report drawn up by a group of experts at the request of Romano Prodi, President of the European

Commission. This report, entitled “*An agenda for a growing Europe: making the EU economic system deliver*”, was critical of the effects of the cohesion policy and the CAP. It called into question the structure of the EU budget, which it said should be remodelled by renationalising the CAP and reassessing the principles behind the Union’s cohesion policy (Sapir *et al.*, 2004). Under the proposed system, the EU budget should be completely restructured and limited to 1% of gross national income (GNI) in commitment appropriations. EU expenditure should also be redirected towards enhancing competitiveness.

Secondly, the six main “net contributors” to the EU budget (Germany, France, the UK, the Netherlands, Austria and Sweden) sent a letter to Mr Prodi, the Commission President, in December 2003. In their view, expenditure in 2007-2013 “should add real value, and aim more actively at transforming the EU into the most competitive and innovative area worldwide. Other key tasks are further developing the Common Foreign and Security Policy, protecting our external borders (...)”. Spending should not exceed 1% of GNI, “including agriculture spending within the ceiling set by the European Council in October 2002” (Gaillard and Sutour, 2004: annexe 4). This initiative underpinned the logic of a “fair return” (Le Cacheux, 2005) and is an accountancy-based approach to the European budget.

1.1 The “fair return”

A bit of background is needed to understand the notion of fair return. Back in the early 1980s, traditional own resources proved inadequate to fund the European budget on account of a fall in revenue from customs duties – linked to international trade talks at the GATT, precursor of the World Trade Organisation (WTO) – and due to the cost of the CAP. After the United Kingdom acceded to the Communities in 1973, the British government pointed out that its contribution to the budget greatly exceeded its share of Community expenditure. Agricultural spending accounted for 60% of the budget at the time, and the UK derived little benefit from that expenditure whilst making a substantial contribution to the budget owing to the proportion of gross national product (GNP) represented by VAT. That was the first “fair return” crisis, symbolised by Mrs Thatcher’s alleged cry of “I want my money back”. The Fontainebleau European Council of June 1984 solved the problem by

granting the UK a “rebate”. It also recognised the principle that “any Member State” may apply for a general correction to its contribution. Such a correction would be granted on two conditions: the scale of the budgetary imbalance (“excessive”) and the wealth of that Member State compared with the EU as a whole (“relative prosperity”). Several other countries have since become “net contributors”. Since the introduction of traditional own resources (TOR) and of an additional funding stream based on Member States’ GNP/GNI, the proportion of resources based on GNI has risen steadily. From 29.6% in 1996 it rose to 74.5% in 2005 (see table 1). The structure of the Community budget is therefore based mainly on the payment of national contributions (VAT revenue and GNI). The preparation of the financial perspectives was dominated by the “fair return” logic, which fuelled the controversy to such an extent that it caused the Dutch people to reject the Union. Indeed, the Netherlands’ excessive contribution to the EU budget is regarded as one reason why the European Constitution came to grief.

**Table1: The composition of EU own resources
(in % of total own resources; cash basis)**

Own resources 1996-2005 (%)										
	1996	1997	1998	1999	2000	2001	2002 ¹	2003	2004 ²	2005 ³
TOR	19.1	18.8	17.2	16.8	17.4	18.1	11.9	13.0	12.0	11.4
VAT	51.3	45.5	40.3	37.8	39.9	38.7	28.8	25.4	14.6	14.1
GNP/GNI	29.6	35.7	42.5	45.4	42.7	43.2	59.3	61.6	73.4	74.5
Total own resources (€ billion)	71.1	75.3	82.2	82.5	88.0	80.7	77.7	83.6	93.3	108.5

¹ As from 2002, the % of TOR retained by Member States as a compensation for their collection costs was raised from 10% to 25%. This difference represented about €2.2 billion in 2002 as well as in 2003.

² Preliminary draft amending budget 8/2004 (EU-25).

³ Preliminary draft budget 2005.

Source: CEC (2004a).

1.2 The 2007-2013 financial perspectives

1.2.1 The Commission's proposals in 2004

The Commission put forward two main ideas in a Communication published in February 2004 entitled “Building our common future” (CEC, 2004b). Firstly, the budget should be capped at an average of 1.14% of Community GNI in payment appropriations, i.e. a ceiling higher than that demanded by the “six net contributors”. The difference between 1.14% and 1% may seem insignificant, but we should bear in mind that every 0.1% of EU GNI represents €10 billion. The Commission was therefore calling for a greater overall budget than the six, but without raising the current own resources ceiling of 1.24% of GNI. With respect to economic and social cohesion, this would mean re-allocating aid between the regions of the new Member States and the poorest regions of the Fifteen (mainly in the so-called cohesion countries of Portugal, Greece and Spain, whose per capita GDP is less than 90% of the EU15 average). The number of budget headings was reduced to five, reflecting the Union’s major policy objectives, namely promoting competitiveness and cohesion for sustainable growth; sustainable management and protection of natural resources; citizenship and the area of freedom, security and justice; the Union’s role in the world; and administrative expenditure. The table showing the financial perspectives was subsequently updated (CEC, 2005a).

**New structure of the financial perspectives
(Commission proposal)**

Heading 1: *sustainable growth*, including competitiveness for growth and employment (heading 1a) and cohesion for growth and employment (heading 1b). The funds available under this heading in commitment appropriations would rise by 62.8% in 2013 as compared with the forecast for 2006, including an *increase* of 32% for the old regional policy and 212% for activity in the fields of research/development and employment. Commitment appropriations under this heading would constitute 46% on average of the total Community budget for 2007-2013.

Heading 2: *sustainable management and protection of natural resources* (including agricultural expenditure). Agricultural funding would be reduced by 3% between 2006 and 2013, and this expenditure would decrease from 37% of the budget in 2006 to 26% in 2013.

Heading 3: *citizenship, freedom, security and justice*. The overall budget would increase by 182% between 2006 and 2013, rising from €1.381 billion in 2006 to €3.620 billion in 2013.

Heading 4: *the EU as a global partner*. Funding would rise by 38% from 2006 to 2013, i.e. from €11.232 billion in 2006 to €15.740 billion in 2013.

Heading 5: *administration*.

The *European Development Fund* (EDF), which accounts for 0.03% of EU GNI (gross national income), is incorporated into heading 4 and the *Solidarity Fund for natural disasters* into heading 1b).

The Commission proposed payments of 1.14% (€943 billion) and commitments of €1,022 billion.

By way of a response to the demands of the “six net contributors”, the Commission suggested introducing a generalised correction mechanism based on the UK correction. As concerns the British rebate, the Commission recalled that the reasons why the United Kingdom alone was granted a correction were less pertinent now than at the time of the Fontainebleau European Council, since several other Member States could now legitimately claim to be in a comparable situation to the UK. It would seem unjustifiable to grant London a correction, especially in view of the fact that – according to the Commission’s estimates – the correction would turn the UK (along with Finland) into the smallest net contributor to the EU budget during the period 2007-2013, even though it is one of Europe’s most prosperous countries. That is why the Commission proposed generalising the correction mechanism, which would be triggered for any Member State once it reached a certain threshold expressed as a percentage of GNI (CEC, 2004c). Such a system may appear at first sight to conflict with the principle of equity and solidarity among Member States. The new Member States, whose average revenue equals less than half of that of the six net contributors, wondered whether they would have to hand back to those wealthier countries a share of what they had received from the EU budget.

As regards the system of own resources, the Commission announced that it would not be making any proposals for the period 2007-2013. In the face of criticism, for example that the system was over-complex and

lacking in transparency, it was of the opinion that contributions based on GNI could perhaps be replaced by a visible fiscal resource payable by EU citizens and/or businesses. Three hypotheses were aired, none of which would increase the tax burden on citizens: a tax on corporate income; a genuine VAT resource; an energy tax.

1.2.2 Position of the European Parliament

The European Parliament adopted a resolution on the Union's financial perspectives ahead of the June 2005 European Council (European Parliament, 2005a). The figures put forward in the Böge report (PPE/DE, DE) were 1.18% of GNI in commitment appropriations (€975 billion over the seven years) and 1.07% of EU GNI in payment appropriations, or €883 billion over the seven years. Unlike the Commission, the Parliament chose not to incorporate the European Development Fund (EDF, €21.876 billion), which is currently outside the Community budget, into the financial framework. The MEPs felt that other policies should not lose out through the incorporation of the EDF. On the grounds that creating a flexibility reserve was a non-negotiable element of the agreement, the Parliament proposed setting that overall flexibility at 0.03% of GNI. A certain number of reserves should, in its view, be created outside of the financial framework, so as to be able to confront situations which are unforeseen or hard to plan for in advance (cohesion, emergency aid, solidarity fund, guarantee fund) and to facilitate the EU's economic adaptation in terms of competitiveness. (This would be done by establishing a competitiveness reserve, endowed with a maximum of €7 billion, replacing the Growth Adjustment Fund proposed by the Commission – see Box. Those monies could be used to strengthen growth and competitiveness and to enable the Union to react to economic change.) There should also be reserves for cohesion (€3 billion), emergency aid (€1.5 billion) and the Solidarity Fund (€6.2 billion). The Parliament also called for both the loan guarantee reserve (€3 billion) and the flexibility reserve (increased by €500 million to €3.5 billion) to be maintained, but outside of the financial perspectives.

The Growth Adjustment Fund

In its Communication on the financial perspectives the Commission justified the establishment of this Fund as follows: “*A more proactive approach to competitiveness will be provided by the creation of a Growth Adjustment Fund. Each year, when the Union assesses progress in the implementation of the Lisbon strategy at the Spring European Council, it could channel resources, if necessary, to boost particularly effective initiatives to accelerate progress in objectives running behind schedule (such as TENs or large environmental or research projects) or help respond to unexpected shocks – such as trade disputes or unexpected consequences of trade agreements, or exceptional calls for urgent actions like, for instance, the necessity to top up financial needs to carry out nuclear decommissioning obligations without delay. The Fund would not require a separate instrument: it would use existing programmes and delivery mechanisms*” (CEC, 2004d: 15). In its Communication entitled “*Restructuring and employment. Anticipating and accompanying restructuring in order to develop employment: the role of the European Union*” (CEC, 2005b), the Commission once again defended the establishment of this Fund which several Member States did not want (Council of the European Union, 2004: 19 and 2005a: 3).

1.2.3 Failure of the June 2005 European Council

Just a few days after the two unsuccessful referendums in France and the Netherlands, the President of the European Council, Jean-Claude Juncker, suffered a fresh setback. The Luxembourg presidency’s compromise proposal earmarked 1.06% in commitment appropriations (roughly €873 billion) (Council of the European Union, 2005b) and 1% of GNI in payments. As for own resources, it proposed freezing the British rebate at €4.6 billion in 2007 and then decreasing it gradually so as to meet the concerns of the three largest net contributors (Germany, the Netherlands and Sweden). Luxembourg’s proposals were supported by most delegations, and the negotiations ran aground not so much on the level or distribution of this expenditure as on the way in which it was to be funded. France demanded that the British rebate be abolished; the United Kingdom wanted the review of CAP funding to begin in 2009, contrary to the decision reached by the European Council in October 2002. Two net contributors, the Netherlands and Sweden, backed the UK, as did Spain, thereby causing deadlock. The principle of scaling down the financial allocation for research and development was already included in the Luxembourg compromise.

1.3 The Commission's proposals of October 2005

In its fresh proposals, put forward on 20 October in the run-up to the informal European Council at Hampton Court (under the UK presidency), the Commission appealed urgently for an agreement to be reached in December 2005. The proposals contained no figures but pressed the point that the cohesion policy should account for at least a third of funding under the “new” Lisbon strategy focusing on the objectives of growth and employment. The Commission again proposed the establishment of a growth adjustment fund, now renamed “Globalisation Adjustment Fund”. Its aims would be specific: the Fund would finance training and the redeployment or reintegration of workers, i.e. the costs of activities serving to find a new job. But not all forms of restructuring would be budgeted for; this would be a crisis mechanism designed to compensate only for economic and social shocks resulting from globalisation. It would not be triggered until a set proportion of workers in the sector and region concerned had suffered redundancy, and account would also be taken of the local unemployment level. This Fund would not form part of the financial framework (as had been demanded by the European Parliament and as is already the case for the Solidarity Fund); its use would be purely needs-based. The decision to draw on it would be taken by the Parliament and Council together. British Prime Minister Tony Blair endorsed this plan.

Other aspects concerned compliance with the commitments made by the Fifteen in 2002 regarding agriculture, namely that CAP expenditure would be set in stone until 2013 and that the 2003 reform would be followed through. According to the Commission, however, the 1% per year acceleration in the redirection of funding earmarked for direct aid to farmers towards rural development as from 2009 should free up additional resources and have a direct impact on growth and employment in rural communities. These monies would also help fund NATURA 2000, the Union's nature conservation network. The Commission likewise proposed carrying out a complete review of all the organisational aspects of its budget – expenditure, revenue and structure – and promised to publish in 2009 a White Paper on modernising expenditure and revenue. Finally, with a view to meeting the Union's commitments in respect of the Millennium Development

Goals, the Commission requested an overall budgetary sum higher than that contained in the last Luxembourg presidency compromise.

1.3.1 The UK presidency's proposals

A media campaign was launched against the CAP just a few days ahead of the European Council in December 2005. It claimed that CAP financial aid, especially in France and the UK, benefited large-scale producers and even big agri-food businesses, not small farmers. In the absence of reliable data about such finance operations, these concordant press reports brought discredit on future funding of the CAP – especially as, at the WTO, the Member States had offered to slash their subsidies to farmers. Before its proposal was aired, the UK suggested reviewing the CAP in 2009.

The UK presidency's initial proposals, circulated in early December, were designed to build the financial perspectives around the preservation of its rebate. This would be done to the detriment of funding earmarked for the new Member States, by scaling back the structural funds. Total expenditure (in commitment appropriations), calculated on the hypothesis that the Union will have 27 members as from 2007, would be €846,754 million or 1.03% of EU GNI: more than €10 billion less than the amount contained in the last costed proposals put forward by the Luxembourg presidency. These proposals were rejected both by the President of the Commission and by the European Parliament, whose approval of the financial perspectives is vital for renewal of the interinstitutional agreement on budgetary discipline. It is noticeable that the figures for expenditure to fund the CAP were those of the Luxembourg presidency. These were in line with the October 2002 decision on CAP funding up until 2013, and incorporated the €6 billion allocated under the CAP for Bulgaria and Romania. The 14 December proposal maintained the cut in the cohesion policy and allocated a sum of €849,303 (instead of 846,754) million in payment appropriations.

1.3.2 Financial perspectives adopted by the European Council in December 2005

The main adjustment variables of the 2007-2013 financial framework were the maintenance of a minimum amount of cohesion policy expenditure and the British rebate. This translated into the level of spending approved under the “sustainable growth” heading of objective 1b – “cohesion for growth and employment” – and the country-by-country breakdown in the financial perspectives.

The financial perspectives eventually adopted by the European Council in December comprise an amount of €862.4 billion (in commitment appropriations), or 1.045% of GNI of the EU27 (the present 25 plus Romania and Bulgaria) (Council of the European Union, 2005c). This represents 0.99% of GNI on average in payment appropriations. In June 2005 Luxembourg had proposed €871.5 billion (in commitment appropriations), or 1.06% of GNI; the European Commission’s initial proposal had been €1,022 billion. The budget for 2006 is €121.2 billion in commitment appropriations, which represents 1.09% of Community GNI and €111.9 billion in payment appropriations (1.01% of EU GNI). The Brussels European Council set the cohesion policy allocation at €307.619 billion for the seven years of the financial perspectives (compared with €309.4 billion proposed by the Luxembourg presidency and €338.710 billion by the Commission). The European Council moreover acknowledged the inadequacy of the sum earmarked for external action and called on “the Budgetary Authority to ensure a substantial increase in the Common Foreign and Security Policy budget from 2007”.

The sums shown in the table below do not include the European Development Fund, which will be endowed with an amount of €22,682 billion for the period 2008-2013 based on national contributions.

Table 2: Financial perspectives 2007-2013: Brussels European Council agreement (15-16 December 2005)

COMMITMENT APPROPRIATIONS (€ millions)	2007	2008	2009	2010	2011	2012	2013	Total 2007-2013
1. Sustainable Growth	51 090	52 148	53 330	54 001	54 945	56 384	57 841	379 739
1a. Competitiveness for Growth and Employment	8 250	8 860	9 510	10 200	10 950	11 750	12 600	72 120
1b. Cohesion for Growth and Employment	42 840	43 288	43 820	43 801	43 995	44 634	45 241	307 619
2. Preservation and Management of Natural Resources	54 972	54 308	53 652	52 021	52 386	51 761	51 145	371 244
of which: market related expenditure and direct payments	43 120	42 697	42 279	41 864	41 453	41 047	40 645	293 105
3. Citizenship, freedom, security and justice	1 120	1 210	1 310	1 430	1 570	1 720	1 910	10 270
3a. Freedom, Security and Justice	600	690	790	910	1 050	1 200	1 390	6 630
3b. Citizenship	520	520	520	520	520	520	520	3 640
4. EU as a global player	6 280	6 550	6 830	7 120	7 420	7 740	8 070	50 010
5. Administration	6 720	6 900	7 050	7 180	7 320	7 450	7 680	50 300
6. Compensations	419	191	190					
Total appropriations for commitments	120 601	121 307	122 362	122 752	123 641	125 055	126 646	862 363
as a percentage of GNI	1.10%	1.08%	1.06%	1.04%	1.03%	1.02%	1.00%	1.045%
Total appropriations for payments	116 650	119 535	111 830	118 080	115 595	119 070	118 620	819 380
as a percentage of GNI	1.06%	1.06%	0.97%	1.00%	0.96%	0.97%	0.94%	0.99%
Margin available	0.18%	0.18%	0.27%	0.24%	0.28%	0.27%	0.30%	0.25%
Own Resources Ceiling as a percentage of GNI	1.24%	1.24%	1.24%	1.24%	1.24%	1.24%	1.24%	1.24%

Source: Council of the European Union (2005c).

Resources

The own resources ceiling determines the maximum sum for EU budget revenue and is set by a decision of the Council. The ceiling will be kept at its level under the decision currently in force (Council of the European Union, 2000), namely 1.24% of Community GNI for payment appropriations and 1.31% for commitment appropriations.

The UK rebate will be reduced by €10.5 billion out of an estimated total of between €50 and 55 billion if it had remained unchanged. The compromise excludes from the calculation of the rebate a percentage of regional aid for the new Member States, which will gradually rise to 100% over the course of the period.

The rate of call of the VAT resource (in effect the uniform rate) is fixed at 0.30%. Three net contributors will enjoy temporary relief: the rate will be 0.225% for Austria, 0.15% for Germany and 0.10% for the Netherlands. The Netherlands and Sweden will be granted an annual GNI-related reduction in the resource of €605 million and €150 million respectively. These trade-offs reached in the European Council are to be set down in a new Council decision on own resources. Other elements, particularly concerning the flexibility reserves, may be introduced when the interinstitutional agreement on budgetary discipline is renewed.

Reform of the European budget

The idea of rethinking the entire structure of revenue and expenditure was backed by the Luxembourg presidency. The Commission announced in October 2005 that it would publish in 2009 a White Paper on modernising budget expenditure and revenue. The European Council called on it to “*undertake a full, wide ranging review covering all aspects of EU spending, including the CAP, and of resources, including the UK rebate, to report in 2008/9*”. The European Council may then base itself on that reappraisal to take decisions on all the issues dealt with in it. The reappraisal will likewise be taken into account during preparatory work on the next financial perspectives. Thus the UK presidency obtained a date for the start of the reflection period. Following through the reform of the CAP is one of the demands put forward by several countries in the context of the WTO talks. The European Trade Commissioner,

Peter Mandelson, announced in mid December that agricultural subsidies would end in 2013. Some Member States envisage that the CAP will quite simply be abolished. The UK Chancellor of the Exchequer, Gordon Brown, for instance published a document in early December stating that 10 to 15 years from now the CAP must include “*no price guarantees, no support for exports and no producer or consumer subsidies*”.

Renewal of the interinstitutional agreement on budgetary discipline

The financial perspectives constitute “soft law” since neither the EC Treaty nor the legislation in force makes any provision for them. They are made official by means of an interinstitutional agreement concluded between the European Parliament, the Council and the Commission, reflecting a consensus among the institutions (1). Once agreed, the ceilings established in the financial perspectives must be adhered to. The interinstitutional agreement currently in force allows for them to be modified in certain cases: revision, flexibility for the purposes of enlargement, establishment of a solidarity fund, etc. The European Parliament, dissatisfied with the December 2005 agreement, was preparing in early 2006 to embark on tough negotiations with the Council of the EU over this interinstitutional agreement.

2. The future of the cohesion policy

Despite some criticisms (Jouen, 2001), there is widespread support for maintaining the cohesion policy in a Union of 25 and more. The European Commission’s third report on economic and social cohesion, adopted in February 2004, took stock of the existing regional disparities measured in terms of per capita gross domestic product (GDP). In 2003 the level of GDP per inhabitant, measured at purchasing power parity, ranged from 41% of the EU average in Latvia to 215% in Luxembourg. Ireland was the second most prosperous country by this yardstick, with a GDP of 132% of the EU average. Per capita GDP in all the new Member States was less than 90% of the average, and did not even reach half of this level in Poland, Latvia, Lithuania and Estonia. The same applied to Romania and Bulgaria. The new Member States

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therefore have high expectations of the CAP and the structural funds. Of the old Member States, Spain is the main beneficiary of these funds in the Europe of Fifteen and is counting on continuing to receive structural aid in the future.

A reorganisation of the structural and cohesion policies around the objectives of the Lisbon strategy, as proposed in the Commission's report, is what prompted the reform of the structural and cohesion funds, for which the first legislative texts were issued in July 2004. Regional aid currently accounts for 37% of Community expenditure. In its July 2004 Communication on the financial perspectives, the Commission recalled that "*the current phase of enlargement will add 5% to the Union's GDP – and to its revenues – but with 30% extra population. It follows that expenditure will increase more than revenue*" (CEC, 2004d: 3). With respect to the CAP, enlargement adds another 4 million farmers, an increase of 50%, and doubles the earnings gap between richest and poorest.

2.1 The Cohesion Fund

The Cohesion Fund was established by the Maastricht Treaty with the aim of contributing financially to the realisation of environmental projects and the trans-European networks (transport infrastructure projects). It was originally intended for the four countries whose per capita GNP was below 90% of the Community average (subject to the creation of a stability programme in the context of economic and monetary union). The Fund consisted of €18 billion between 2000 and 2006, and was expected to cover between 80 and 85% of the cost of projects backed. The distribution key for the four countries concerned was set at 61-63.5% of the total for Spain, 16-18% for Greece and for Portugal, and 2-6% for Ireland. Since EU enlargement on 1 May 2004, the Cohesion Fund has covered the ten new Member States, as well as Spain, Portugal and Greece, for the end of the 2000-2006 period. Ireland ceased to be a beneficiary on 1 January 2004. Spain, for its part, will no longer meet the funding eligibility criteria as from 1 January 2007.

2.2 Reform of the cohesion policy

The legislative package on cohesion consists of a general regulation (CEC, 2004e) as well as individual regulations for each source of finance: the European Regional Development Fund (ERDF), the

European Social Fund (ESF) and the Cohesion Fund. There is also a proposal to create a cross-border authority to manage cooperation programmes (CEC, 2004f, 2004g, 2004h and 2004i).

The Commission proposes that activity should henceforth focus on a limited number of Community priorities reflecting the Lisbon agenda (growth, competitiveness and employment) and the Göteborg agenda (environment). On this basis, a short list of themes was drawn up for the operational programmes: innovation, the knowledge economy, environment, risk prevention, accessibility and services of general economic interest. The implementation principles remain as before: programming, partnership, co-financing and evaluation. All rural development measures are grouped together for all regions – including the least developed Member States and regions – in a single system of funding, programming, financial management and control, with the same degree of concentration as currently exists for the regions covered by the convergence programmes (European Agricultural Fund for Rural Development - EAFRD). A European Fisheries Fund will also be created. These two funds will not however form part of the structural funds. A new financial instrument for the environment would replace the existing environmental funding programmes.

2.3 The Globalisation Adjustment Fund

In addition, with a view to making spending more responsive to changing circumstances, the Commission proposes under its expenditure heading 1a (“sustainable growth”) the establishment of a *Growth Adjustment Fund*. The Brussels European Council of December 2005 gave the go-ahead for a Globalisation Adjustment Fund tasked with providing extra assistance to workers who lose their jobs due to major alterations in the structure of world trade. The maximum sum disbursed will be €500 million per year. However, no provision is made for this fund in the financial perspectives; it will be financed out of underspent amounts and/or out of funds freed up under other headings.

2.4 New objectives

Existing objectives 1, 2 and 3 disappear, making way for three new ones: “convergence”, “regional competitiveness and employment” and “territorial cooperation”. For the purposes of the financial perspectives,

the Commission proposed that the cohesion policy be entered in a single budget heading for the enlarged Union of 27. In financial terms it proposed a budget corresponding to 0.41% of EU GNI, or €336.3 billion, 78% of which would be allocated to convergence, 18% to regional competitiveness and employment and 4% to territorial cooperation. Some believed that these sums were minimum amounts below which it would be difficult to conceive of a policy which better integrates the cohesion dimension into the implementation of numerous Community policies.

At the close of the 2005 Brussels European Council, the cohesion policy accounted in total for 35.7% of the financial perspectives, or €307.619 billion. 51.4% of these funds will go to the new Member States and 48.6% to the old. Some “gifts” were deliberately handed out to old Member States. Thus Spain receives two billion, plus 50 million for the enclaves of Ceuta and Melilla in Morocco; Italy 1.4 billion; France 100 million (for Corsica and the Nord-Pas-de-Calais region); Germany 225 million for the eastern Länder and 75 million for Bavaria. The European Council also spelled out the funding allocation for the new cohesion policy objectives.

2.4.1 The “convergence” objective

The “convergence” objective aims to speed up the convergence of the less developed regions and Member States. Eligible regions are ones where the per capita GDP is less than 75% of the EU25 average (the current NUTS level II regions, according to the common classification of territorial units for statistics - NUTS).

Under the financial perspectives adopted by the European Council in December 2005, 81.7% of cohesion policy funds (€251.330 billion) will be allocated to the “convergence” objective, including 24.5% (€61.518 billion) for the Cohesion Fund and 5% (€12.521 billion) for the regions and Member States where aid is being phased out. (Phasing out applies to regions which would have been eligible under the “convergence” objective if the eligibility threshold had remained at 75% of average GDP for the Union of 15, but which are no longer eligible because their nominal per capita GDP will now exceed 75% of the new average for the Europe of 25.) The aid disbursed to these regions under the “convergence” objective will gradually disappear. Those regions

currently eligible for cohesion funding which would have remained so if the eligibility threshold had stayed at 90% of average GDP for the Union of 15, but which are no longer eligible because their nominal per capita GDP will now exceed 90% of the new average for the Europe of 25, will receive transitional support until the aid has been fully phased out.

2.4.2 The “regional competitiveness and employment” objective

This objective, a composite of existing objectives 1 and 2, is intended to strengthen the competitiveness and attractiveness of regions as well as boosting employment. The entire territory of the Community will be eligible, with the exception of those regions eligible for structural fund finance under the “convergence” objective and regions benefiting from transitional arrangements.

With respect to the operational programmes financed by the European Social Fund, the Commission proposes four priorities in keeping with the European Employment Strategy: improving the adaptability of employees and firms; improving access to employment and increasing labour market participation; strengthening social inclusion and combating discrimination; and undertaking reforms in the fields of employment and inclusion.

Based on the financial perspectives adopted by the European Council in December 2005, 15.8% of these funds (€48.789 billion) will be allocated to the “regional competitiveness and employment” objective, of which 21.3% (€10.385 billion) will go to regions where aid is being phased in. (Phasing in applies to regions currently eligible under objective 1 which will cease to be so because natural growth has taken their per capita GDP to more than 75% of the EU15 average, corresponding to more than 82.19% of the EU25.) Aid to these regions will be introduced gradually under the “regional competitiveness and employment” objective.

2.4.3 The “European territorial cooperation” objective

This objective seeks to step up territorial cooperation at cross-border, transnational and interregional level, to establish cooperation networks and to promote exchanges of experience at the most appropriate territorial level. Regions eligible are ones at NUTS level III situated along internal land borders, as well as all NUTS level III regions situated along

external land borders and along maritime borders separated, as a general rule, by a maximum of 150 kilometres, taking into account potential adjustments needed to ensure the coherence and continuity of the cooperation action. The list of eligible transnational regions will be drawn up by the Commission in conjunction with Member States. The entire territory of the Community will be eligible for funding in respect of interregional cooperation, cooperation networks and exchanges of experience. This new objective aims to increase cooperation at cross-border, transnational and interregional level on the basis of the current INTERREG initiative. It will be financed out of the European Regional Development Fund. As the Commission puts it, the aim will be to promote joint solutions to common problems between neighbouring authorities, such as urban, rural and coastal development and development of economic relations and networking of SMEs. Cooperation will focus on research and development, the information society, the environment, risk prevention and integrated water management.

Under the financial perspectives adopted by the European Council in December 2005, the “territorial cooperation” objective will be allocated 2.4% of these funds (€7.5 billion).

2.4.4 Amendments of the general regulation

Other amendments have also been made to the general regulation so as to set the co-financing rate for the ERDF and the ESF at 85% for all operational programmes in countries whose per capita GDP was less than 85% of the EU25 average for the period 2001-2003. This rate will be 80% in countries eligible for cohesion funding as from 1 January 2007 for regions falling under the “convergence” objective and for regions where aid is being phased in under the “regional competitiveness and employment” objective.

Generally speaking, the Brussels European Council relaxed the deadlines for disbursing resources coming from the structural funds. Appropriations must now be used within three years, as opposed to two (the $N + 2$ rule is replaced by $N + 3$ for the release of the funds) for Member States whose average per capita GDP was less than 85% of the EU25 average during the period 2001-2003, but only for the years 2007 to 2010. This applies to the new Member States as well as to Greece and Portugal.

Cohesion 2007-2013

The objectives and instruments proposed by the Commission

2000-2006		2007-2013	
Objectives	Financial instruments	Objectives	Financial instruments
Cohesion Fund	Cohesion Fund	Convergence	ERDF
Objective 1	ERDF		ESF
	ESF EAGGF – Guarantee and Guidance FIFG		Cohesion Fund
Objective 2	ERDF	Regional competitiveness and employment - regional level	ERDF
Objective 3	ESF		- national level: European employment strategy
Interreg	ERDF	European territorial cooperation	ERDF
URBAN	ERDF		
EQUAL	ESF		
Leader+	EAGGF – Guarantee		
Rural development and restructuring of the fisheries sector outside Objective 1 EAGGF – Guarantee	EAGGF – Guarantee FIFG		
9 objectives	6 instruments	3 objectives	3 instruments

Source: CEC (2004j: 8)

Finally, an economy cannot absorb public subsidies amounting to more than a limited proportion of its GDP in any given year. The critical absorption threshold for subsidies of this type is estimated at 4% of GDP. The programming arrangements for 2000-2006 already exclude annual transfers to any country of EU funds in excess of 4% of its GDP, and it has now been agreed that this rule will be carried over for the 2007-2013 programming period. The December 2005 European Council laid down the maximum level for these transfers according to the wealth of Member States.

INTERREG is the European Regional Development Fund (ERDF) Community initiative in favour of cooperation between European Union regions for the period 2000-2006.

URBAN is the European Regional Development Fund (ERDF) Community initiative in favour of the sustainable development of crisis-hit towns and neighbourhoods in the EU for the period 2000-2006.

EQUAL is a test-bed of ideas serving the European Employment Strategy and the social inclusion process. Its purpose is to promote a more inclusive working life by combating discrimination and exclusion based on sex, racial or ethnic origin, religion or faith, disability, age or sexual orientation. EQUAL is implemented by the Member States and financed by the European Social Fund.

LEADER + falls under the European rural development policy, the second pillar of the common agricultural policy (CAP).

2.4.5 Strategy

The Commission proposes a more strategic approach to programming, centring on the Community's "strategic guidelines for cohesion policy" and the new "national strategic reference frameworks". The strategic guidelines for cohesion policy are designed to transpose the Community's priorities, taking into account the Broad Economic Policy Guidelines (BEPG) and the European Employment Strategy. They are the basis for the formulation of each Member State's national strategic reference framework.

The national strategic reference framework will set out the Member State's cohesion policy priorities for the period after 2006 and plan the resource utilisation. It will replace the existing Community support

frameworks (CSF) and the single programming documents (SPD), as well as the programme complements. The document will give a brief description of the Member State's strategy and the main guidelines arising from it, and will constitute a political charter for the elaboration of operational programmes (national and regional). This national strategy will be followed up by a progress report, which must be submitted by the Member State annually by 1 October at the latest. The European Employment Strategy guidelines will likewise be evaluated every year at national level.

The ERDF and the ESF may finance, in a complementary manner and subject to a limit of 5% of each priority of an operational programme, measures falling within the scope of assistance from the other Fund, provided that they are necessary for the satisfactory implementation of the operation and are directly linked to it. Programmes must be drawn up in close cooperation with economic, social and regional partners. The European Investment Bank (EIB) and the European Investment Fund (EIF) may participate in preparing the national strategic reference frameworks, the operational programmes, major projects and public-private partnerships (PPPs). If the Commission considers it appropriate, the Funds may also finance activities in respect of preparation and monitoring, administrative and technical support, evaluation, auditing and supervision.

For the first time in 2009 and at the beginning of each year, the Commission will report to the Council, which will adopt conclusions on the implementation of the strategic guidelines, to be monitored by the Commission. The draft Community guidelines on cohesion, growth and employment were adopted by the Commission on 5 July 2005.

This proposed reform of the cohesion policy has been welcomed on the whole by the Member States and the social partners. The ETUC had been very keen to see the EQUAL initiative preserved. As for the European Parliament, *Notre Europe* drew attention in a report produced for its Committee on Regional Development to the risk that the cohesion policy might spill over into the realm of the open method of coordination (European Parliament, 2005b).

Conclusions

The budgetary negotiations confirmed that enlargement would be financed in minimalist fashion. The agreement now exists but still has to be translated into a new interinstitutional agreement on budgetary discipline. The UK rebate and the enlarged Union's cohesion policy were the main adjustment variables in the negotiations. Their conclusion gives the green light to the legislative process putting into practice these reforms and the other changes – especially relating to the EAFRD – introduced by the European Council of December 2005. After all, the adoption of the financial perspectives at the end of 2005 was not just about approving the minimum amount of resources necessary for this key EU solidarity mechanism, but also about planning it properly. Other adjustments will be required in the future. The European Council has already acknowledged that the funding allocation for the Union's role in the world was inadequate. The sums proposed by the Commission to finance the Lisbon objectives on research and development were not granted. The funding of these policies is a matter of national responsibility and therefore depends above all else on the Member States themselves and the wishes of their political leaders. For instance, the German Chancellor, Angela Merkel, decided in early 2006 to increase significantly the resources allocated to these policies.

More fundamentally, the agreement of December 2005 opens the door to a thorough rethink of both the structure of the budget and its financing. How should the international trade talks impact on the structure of the budget? How should the funds freed up from the CAP after the abolition of agricultural subsidies be reallocated? How should the objectives of this policy be redefined whilst preserving all the elements which contribute to food safety, given that the CAP has been lambasted for benefiting rich landowners more than small farmers? What form will rural development policy take in future?

The debate ahead will be difficult, given the continuing existential crisis and growth pangs highlighted by the twofold rejection of the European Constitution, which proposed giving greater recognition to the regional level. Will the cohesion policy help to foster a sense of belonging and of sharing a common European destiny? Only on this condition will progress be made in the debate about introducing tax revenue as a

means of financing the EU. That would put an end to the pernicious logic of the “fair return” and put solidarity-based policies on a permanent footing, thereby helping to demonstrate that the European Union is more than just a free-trade area.

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The “better regulation” agenda: a challenge to the Community method?

Introduction

A number of factors have thrown the European project into profound turmoil: the “pause for reflection” on the European Constitution, the difficulty in agreeing a 2007-2013 budget to finance an ambitious policy for Europe, an enlargement which called into question both the rules governing the European Union (EU) and the balance of power amongst Member States, and new challenges flowing from globalisation, to name but a few.

In this context, recent Communications from the European Commission on “better regulation” mark a break with the established direction of Commission policy. Even those responsible for this policy area within the Commission express the view that the aim of the Commissioners responsible (G.Verheugen and C. McCreevy), under the guidance of President Barroso, is to focus on competitiveness and to give this whole policy area a “business oriented” look. The “better regulation” agenda – also sometimes referred to as “better law-making” – has moreover become one of the Barroso Commission’s top priorities (1): “*One core area*

¹ The Commission President, José Manuel Barroso, has always indicated a personal preference for the liberal view of Europe, preferring to give free reign to the markets and to business. In an interview with the Financial Times on 13 September 2005, he stated: “*I’m not against regulation at a European level, but we are no longer in the heroic era of Jacques Delors, completing the single market with a new piece of legislation every day*”.

of the Lisbon Agenda is better regulation” (Barroso, 2005). In vain do the Commissioners protest that the aim is not to bring about a policy of deregulation: certain attitudes will, by their very nature, sow the seed of doubt as to the actual intentions of those promoting this policy agenda.

The Herculean task facing certain EU countries – France and Belgium in particular – bears witness to this. At Council after Council they seek to reintroduce references to the three pillars of sustainable development (economic, social and environmental development), to the need for harmonisation and for respecting the Community method. Are the *acquis communautaire*, the Interinstitutional Agreement and the principle of balance between these three pillars actually part of a framework of reference which should reassure, or rather a delusion which veils the true nature of a completely different agenda?

For those yet to be convinced of the relevance of the question, one has but to consider three underlying trends within the European Union:

- 1) The liberalisation of services of general economic interest (SGEI) is inexorable, and the demarcation line between liberalisation and gradual privatisation is becoming increasingly blurred ⁽²⁾, sometimes as a reaction to the market, sometimes in anticipation of events. In the wake of full liberalisation of the aviation, telecommunications and energy sectors, liberalisation is proceeding in a number of other sectors: the railways, postal services and port services ⁽³⁾;
- 2) State aids are mentioned in the Treaty as being measures deemed incompatible with the Treaty, to the extent that they distort or threaten to distort competition, with the exception of waivers authorised by the Treaty itself ⁽⁴⁾. Nevertheless, the Commission

² And that notwithstanding Article 295 of the Treaty (ex Article 222) which provides that European Union provisions shall in no way prejudice the rules in the Member States governing the system of property ownership.

³ NB the rejection by the European Parliament of the second proposal for a Directive seeking to liberalise port services on 18 January 2006.

⁴ It would appear that there is increasingly rather a narrow interpretation of Article 87(1) of the EC Treaty, which is becoming ever further removed from the concept of competition.

appears to be becoming more radical. All State aids are being phased out except for those deemed by the Commission, exercising its sovereign authority, to be in the common interest. Furthermore, a Member State may only have recourse to State aids to the extent that they offset a “market defect”, a concept unknown in the Treaty which recognises the primacy of the market;

- 3) Reliance on public procurement procedures has become the norm. The competitive tendering procedure, which is compulsory when local public service contracts are being awarded, is leading to creeping privatisation in this area. Direct public sector management or State control is becoming the exception ⁽⁵⁾.

In these three instances, the State is generally requested to make way for private sector investors who are thought to be more competitive and perform better economically.

The “better regulation” agenda is part of a whole range of converging policies. How could one fail to see the links between the three trends mentioned above and “better regulation”? The introduction of “better regulation” – which to its proponents means less legislation (cf. the recurring theme “*less State aid but better aid*”) and alternative methods of regulation (voluntary codes, co-regulation, self-regulation or deregulation) – is part of an overall context of “less State” with regulation left to market forces. It will become apparent that the proposal for a Services Directive is indeed an exemplar of the concept of “better regulation”, as are both the Directive on professional qualifications (European Parliament and Council of the European Union, 2005) and the REACH Directive.

The convergence between the overlapping and in part mutually reinforcing agendas mentioned above is a powerful tool in bringing about deregulation. In our opinion, it also threatens to bring about an unprecedented fragmentation of the *acquis communautaire* and the Community method. This article will focus only on the elements of “better regulation” contained in the various “packages” of initiatives put

⁵ See in particular recent ECJ case law: the rulings in Teckal, Stadt Halle, Commune di Cingia de’Boti and Parking Brinxen. See also Van den Abeele (2006).

forward by the Commission: simplification of legislation, “screening” of Community legislation, impact assessment of the Commission’s intended legislative proposals and an estimate of administrative costs. Some tentative conclusions will then be advanced, in an attempt to identify a central theme linking different policy areas of this agenda.

1. Terms of the debate

The evolution of the European Union over the past fifty years has given rise to a considerable number of legislative texts. The *acquis communautaire* now encompasses some 80,000 pages covering 220 different legal bases and some 1,400 legal acts across that spectrum. This is a substantial amount, and yet it is not excessive in comparison to US legislation, which runs to greater length. EU enlargement has necessitated the translation of all these legal acts into the 20 official languages of the Community, a huge amount of work.

The principal justification for the “better regulation” agenda lies in the fact that Community and Member State regulation is often said to be too heavy-handed ⁽⁶⁾, and to constitute a major barrier to the competitiveness of the Union, stifling European companies, particularly by comparison with their US competitors but also as compared to competitors from the emerging economies.

A number of studies commissioned by the European Commission suggest that European firms feel they are hampered by the poor quality of regulation. The EOS/Gallup study (CEC, 2001a: 2) carried out for the Commission found that regulatory costs amounted to 4% of Community GDP. Around 15% of those costs, some 0.6% of GDP, could be avoided by better regulation, which would bring about savings of the order of €50 billion, according to EOS/Gallup. A very recent study by George M.M. Gelauff and Arjan Lejour (CEC, 2006), based on a method known as the “Standard Cost Model” ⁽⁷⁾, estimates costs for business in the Netherlands alone at €16.4 billion, or 3.7% of Dutch

⁶ The expressions most frequently used in this context are “Brussels red tape” and “EU over-regulation”.

⁷ See explanation in point d of section 2.2.3.

GNP. Gelauff and Lejour estimate that 40% of this total is generated by international legislation, most particularly Community legislation. In 2002, the Dutch Government therefore decided to cut the “administrative burden” by 25%, equivalent to 0.9% of GNP (€4.1 billion). The OECD embraced this initiative which subsequently became one element of its overall strategy. The European Union in the shape of the Economic Policy Committee (EPC) followed suit, though without any critical study assessing the quality of the arguments put forward by EOS/Gallup and by the Dutch *Centraal PlanBureau*.

There are three facets to the “better regulation” agenda. They correspond to the “stages” of the “legislative” process: simplification and improvement of the quality of texts, screening of existing legislation (ongoing assessment) and monitoring of legislation pending. The outcome of this work is normally incorporated into the legislative programme of the Commission, which comprises only straightforward pieces of legislation meeting the needs of the EU. The assessment of how the legislation impacts on competitiveness, and the calculation of administrative and regulatory costs, are the final stage of the process, the purpose being to ease the administrative “burden” on companies and on EU competitiveness in general.

It is useful to point out at this stage that there is an inherent ambiguity here. Firstly, the simplification of texts does not necessarily equate to improvement, nor vice versa ⁽⁸⁾. These are disparate objectives, which must be seen against the backdrop of enhanced legal certainty. Secondly, a causal link is established between a level of regulation and EU competitiveness. This structural link is not directly proportional. Competitiveness depends on a whole range of factors which go far beyond the realm of regulation: for example, management ⁽⁹⁾, the level of education and training of

⁸ “It is this pressing need for simplicity to convey what is inherently complex that is deceptive. One cannot avoid the conclusion that it is used systematically, even dogmatically and has been elevated to the status of an indispensable rule of political engagement for some years now” (Monjal, 2003: 349).

⁹ See in this context the recent study by Dorgan *et al.* (2006: 1): “Managers are more important than the industry sector in which a company competes, the regulatory environment that constrains it [our emphasis], or the country where it operates”.

entrepreneurs, productivity, infrastructure quality, technological and non-technological innovation, creativity and inventiveness of business. It will later be appropriate to reflect on why the “better regulation” agenda has been identified as one of the key features of the competitiveness agenda, whilst it is in fact only one amongst a range of elements in a global strategy, and probably not the most crucial at that.

Within this agenda, the Commission divides the improvement of Community legislation into two parts: simplification ⁽¹⁰⁾ and regulatory amendment.

1.1 Simplification

The aim here is to simplify the substance of a regulation and ensure that it is more user-friendly. There are four parts to this exercise.

a. Repeal

Repeal means the withdrawal of legal acts which are “superfluous, insignificant or archaic”. Quite a number of legislative acts adopted since 1957 are now irrelevant or obsolete by virtue of technical or technological progress, developments in Union policy, changes in the way in which the general Treaty rules are applied, or the introduction of international regulations or standards. Many of the outdated legal acts have been repealed already. Some, however, continue to impose obligations, mainly of an administrative nature, on both authorities and businesses. The Commission intends to continue its efforts to repeal legal acts which are irrelevant or obsolete ⁽¹¹⁾. Hence 28 of the 56

¹⁰ It should be noted in this context that the Belgian Central Economic Council finds the term “simplification” somewhat infelicitous and prefers to use the term “improvement of existing legislation” (Opinion of the Central Economic Council on “Better Law-making”, Brussels, 21 December 2005 <http://www.ccecrb.fgov.be/txt/fr/doc05-1392.pdf>).

¹¹ Consideration has been given to the possibility of including “sunset clauses” in the Commission’s legislative proposals to avoid acts becoming obsolete, and more generally to oblige the legislator to check regularly the relevance, effectiveness and proportionality of regulations in force. Without precluding this option, the Commission is nevertheless of the opinion that a review clause fulfils the same objective whilst presenting a lower risk of legal lacunae.

Directives on vehicle type-approval will be repealed and replaced by regulations of the UN Economic Commission for Europe.

b. Codification/consolidation

Codification⁽¹²⁾ is a procedure whereby all the provisions of an act and all its amendments are brought together in a new binding legal act. This act repeals the legislation it replaces, but without changing the substance of those provisions. For example, the 1976 Directive on cosmetics: 7 consecutive amendments and 37 Directives introducing amendments reflecting technical progress will be codified and simplified to form a single new Directive. The Commission will continue its codification programme⁽¹³⁾, with a view to completing the codification of the *acquis communautaire* by 2007. The translation and subsequent consolidation⁽¹⁴⁾ of the acts across the 20 official languages will substantially increase the number of codified texts to be adopted from the end of 2005. Codification is intended to eliminate duplication. It should however be noted that although this method is generally presented as neutral in terms of substance, a number of reservations have been expressed in this regard. Evidence of this can be seen in the way Member States reacted to the Directive on "professional qualifications" (European Parliament and Council of the European Union 2005), presented by the Commission as a consolidation of previous texts, but deemed by Member States to go beyond what could be described as a legal tidying-up exercise.

c. Recasting

Recasting is a procedure whereby a new binding act repeals and replaces certain acts, combines amendments to the substance of the legislation and codifies the remaining unamended sections. A single piece of

¹² Codification is of great assistance in reducing the volume of Community legislation and simultaneously produces clearer and more readable legal texts. This in turn facilitates transparency and enforcement.

¹³ In November 2001, the Commission launched a major drive towards codifying all secondary Community legislation (CEC, 2001b).

¹⁴ Consolidation is a procedure whereby the provisions of an act and all its amendments are gathered together mechanically without any intervention whatsoever.

legislation is then adopted which incorporates substantial amendments, codifies both these and the unamended provisions of the previous act, and repeals the previous act. Health and safety of workers, for example, is covered by 20 Directives. The revision of these texts will allow harmonisation of the frequency of reporting. Acts which are codified, revised or simplified must be submitted to the legislature for adoption, since the structure or substance of the acts has been altered.

d. Use of Regulations

On occasion, the Commission considers the best method of simplification to be the replacement of Directives with Regulations. The latter are applicable with immediate effect, and guarantee that all parties affected are subject to the same rules at the same time. The Commission has been keen to emphasise that Directives will be replaced by Regulations on a case-by-case basis. It will encourage replacement “whenever possible”, particularly in respect of technical rules, so as to ensure better implementation of texts.

1.2 Modification of the regulatory approach

This heading covers what is modestly referred to as “alternatives to legislation”. There are essentially two variants here: self-regulation and co-regulation ⁽¹⁵⁾.

a. Self-regulation

Self-regulation gives economic operators, the social partners, non-governmental organisations and associations the opportunity of acting jointly. They themselves are free to adopt, for their own purposes, common guidelines at EU level, such as voluntary codes of conduct or sectoral agreements (cf. § 22 of the Interinstitutional Agreement).

b. Co-regulation

Co-regulation is a mechanism whereby a Community legal act entrusts recognised parties involved in the sector with the responsibility for

¹⁵ This article will not cover the “new approach” Directives on technical harmonisation, which combines legislative and non-legislative elements, nor the open method of coordination (OMC). On this, see Zeitlin and Pochet (2005).

achieving certain goals set down by the legislative authority, (in particular economic operators, the social partners, non-governmental organisations or associations) (cf. § 18 of the IIA). The setting of standards by independent bodies is an example of a recognised form of co-regulation. The Commission actively encourages this type of arrangement as an alternative or in addition to the legislative method (CEC, 2004a and 2005a). It has moreover indicated its wish to extend co-regulation to new areas, such as cosmetics, the automobile and tractor sector and the banking sector.

2. Role of the institutions

2.1 Role of the European Council

2.1.1 Impetus given by the Lisbon European Council (2000)

The Edinburgh European Council, in December 1992, recognised simplification and improvement of the regulatory environment as one of the main priorities for the European Union. However, it was the Lisbon European Council on 23 and 24 March 2000 which decided that the strategic goal for the decade to come was: *“to become the most competitive and dynamic knowledge-based economy in the world, capable of sustainable economic growth with more and better jobs and greater social cohesion”* (European Council, 2000: point 5). The European Council observed that: *“The competitiveness and dynamism of businesses are directly dependent on a regulatory climate conducive to investment, innovation, and entrepreneurship. Further efforts are required to lower the costs of doing business and remove unnecessary red tape, both of which are particularly burdensome for SMEs. The European institutions, national governments and regional and local authorities must continue to pay particular attention to the impact and compliance costs of proposed regulations, and should pursue their dialogue with business and citizens with this aim in mind”* (European Council, 2000: point 14).

2.1.2 Confirmation at the Brussels European Council (2005)

The European Council regularly restated this goal in its conclusions ⁽¹⁶⁾, until the Brussels Summit on 15 and 16 December 2005 under the

¹⁶ The mandate conferred by the Lisbon European Council was restated at the European Councils in Stockholm (23 and 24 March 2001), Laeken (8 and 9 December 2001) and Barcelona (15 and 16 March 2002).

British presidency, when it expressed a carefully measured view on the matter. On the one hand it gave a commitment to the countries most attached to the Community method, recalling that it was committed to the *acquis communautaire* and the Interinstitutional Agreement which underpins it: “*Taking due account of the principle of subsidiarity and proportionality and the importance of respecting the acquis communautaire, the European Council stresses that an improved regulatory framework in the European Union, at Community and Member States level, is key to delivering growth and jobs. Emphasis should be placed on implementing commitments already made by all institutions, including the provisions of the Interinstitutional Agreement on Better Law-Making of 16 December 2003*” (European Council, 2005: point 20). It equally makes a commitment to the more liberal countries keen to push ahead with the “better regulation” agenda: “*On that basis, the European Council welcomes the significant progress made since its last meeting and agrees on the importance of further work as set out in the attached annex covering i) reducing burdens on business and citizens through simplification and screening; ii) the revised impact assessment system and iii) EU common methodology for assessing the administrative costs of legislation*” (European Council, 2005: point 20).

2.2 Role of the Commission

Strengthened in its resolve by the mandate from the European Council, the European Commission now plays a pivotal role in shaping the policy agenda in this area. It translates the intent and decisions of the European Council and the Council of Ministers into actual programmes. Since the Lisbon European Council, the Commission has really taken control of the agenda here and has put forward three packages of texts for the co-legislators to consider.

2.2.1 The 2001 “package”

“Renewing the Community method” (CEC, 2001c) became the Commission’s mantra when in 2001 it published the first Communication on the subject. For the European Union executive, the renewal of the Community method is a necessary “response to globalisation and enlargement”: the world has changed. In the words of the Commission, one must therefore reflect on how the Union’s powers are used, and how to ensure compliance with the principles of subsidiarity and proportionality. Democratic legitimacy and the

efficiency of the European institutional system must be enhanced. There are four parts to the 2001 package:

- an initial interim report for the attention of the Stockholm European Council, in March 2001, assessing the situation and outlining some possible avenues for further exploration (CEC, 2001d);
- a White Paper on European governance adopted in July 2001 (CEC, 2001e);
- a Communication ⁽¹⁷⁾ on the future of the Union entitled “Renewing the Community method” (CEC, 2001c);
- a more political Communication, submitted to the Laeken European Council, seeking to consult the Council, the European Parliament and the Member States on the central themes of this Action Plan (CEC, 2001a).

In the first package, the Commission’s basic premise is that the legislative method is often only one part of a wider solution which combines formal rules with other, non-binding, rules such as recommendations, guidelines or even self-regulation within an agreed common framework. It makes the case for an increased use of Regulations in cases where uniform implementation and legal certainty are required throughout the Union. The more frequent use of “Framework Directives” would be advisable. Irrespective of the type of legislative instrument selected, greater use should be made of “primary” legislation, pared down to the bare essentials (basic rights and obligations), so that the executive retains the responsibility for

¹⁷ This very brief 9 page document is interesting to the extent that it contains several statements of fact: “(EU) overall coherence has gradually been lost” and “the world has changed”. The Commission goes on to observe that if “the collective interest requires that the results and overall coherence of 50 years of European integration should not be called into question, we are fully justified (...) in examining closely the current situation with regard to our powers in order to refocus them if necessary. It would in any event be worthwhile seeking as rational a presentation as possible of the respective responsibilities of the Union and the Member States and clarifying them (...). The Commission therefore recommends paying particular attention to monitoring the principles of proportionality and subsidiarity which require action to be taken at the most appropriate level” (CEC, 2001c: 6).

monitoring technical compliance through the application of rules of secondary law.

The Commission's view is that implementing measures may on occasion be part of a co-regulation framework⁽¹⁸⁾. This combines binding legislative or regulatory measures with measures implemented by those most involved in the sector, taking advantage of their practical experience⁽¹⁹⁾.

2.2.2 The June 2002 "package"

Following its initial Communications in 2001, the Commission confirmed its approach through a set of three documents, which formed the basis for the Community's work over three years:

- a Communication on European governance (CEC, 2002a)
- a Communication on impact assessment (CEC, 2002b)
- an Action Plan entitled "Simplifying and improving the regulatory environment" (CEC, 2002c).

¹⁸ It is interesting to observe that the Commission takes great care to provide for the use of co-regulation: "*Co-regulation implies that a framework of overall objectives, basic rights, enforcement and appeal mechanisms, and conditions for monitoring compliance is set in the legislation. It should only be used where it clearly adds value and serves the general interest. It is only suited to cases where fundamental rights or major political choices are not called into question. It should not be used in situations where rules need to apply in a uniform way in every Member State. Equally, the organisations participating must be representative, accountable and capable of following open procedures in formulating and applying agreed rules. This will be a key factor in deciding the added value of a co-regulatory approach in a given case. Additionally, the resulting co-operation must be compatible with European competition rules and the rules agreed must be sufficiently visible so that people are aware of the rules that apply and the rights they enjoy. Where co-regulation fails to deliver the desired results or where certain private actors do not commit to the agreed rules, it will always remain possible for public authorities to intervene by establishing the specific rules needed*" (CEC, 2001e: 21).

¹⁹ Co-regulation has already been used in areas such as the internal market (adoption of product standards via Directives using the so-called "new approach") and the environment (reduction of pollutant emissions from automobiles).

The particularly new aspect to this package is the Commission Communication on impact assessment and the adoption of the Action Plan, the fundamentals of which were established in 2001.

2.2.3 The 2005 “package”

The Commission continued in the same vein with the publication of a package of four Communications on:

- a strategy for the simplification of the regulatory environment (CEC, 2005b)
- impact assessment guidelines applicable prior to the adoption of any major new legislation (CEC, 2005c);
- outcome of the screening of legislative proposals pending before the legislator (CEC, 2005d).
- an EU common methodology for assessing administrative costs imposed by legislation (CEC, 2005e).

a. Communication on the simplification of the regulatory environment, October 2005

This Communication (CEC, 2005b) is the result of extensive consultation amongst Member States and stakeholders plus internet-based consultation. The Communication is the beginning of an evolving process which is to be taken forward beyond the three-year working programme established by the Commission. The simplification programme comprises 220 basic texts. The Commission envisages five methods of simplification:

- repeal (10);
- codification (25 texts);
- recasting of texts with a view to ensuring coherence and effectiveness (140 measures);
- revision of texts in order to simplify them (30 texts);

- modification/update of texts to ensure compatibility with “modern management”⁽²⁰⁾ (15 texts).

The Commission has stated that it will incorporate measures to enhance competitiveness into its simplification proposals. This aim emerges clearly from the internet consultation. The Commission adds, however, that it will have to face up to the consequences of this approach, particularly in terms of social and environmental objectives and consumer protection.

It is interesting to observe that the Commission underlines in its document that “*Better regulation is (...) not de-regulation*” and that “*The review of the acquis must become a continuous and systematic process*” (CEC, 2005b: 3). One should note furthermore that “*To pursue the evaluation of the acquis beyond the present simplification programme, the Commission will identify the need for simplification from a sectoral perspective. It will include an analysis of the benefits and the costs, administrative and others, of the legislation in question*” (CEC, 2005b: 5). In contrast, the Commission observes that “*It is important that the repeal of Community instruments are followed by the repeal of the corresponding national implementing measures in order to have the desired practical effect. It needs to be ensured that the advantages of a lighter Community regulatory environment are not cancelled out by new national rules and new technical barriers. In this regard, the Commission sees its proposal to repeal the pre-packaging directive as a test of the political willingness of the co-legislator to take up the simplification challenge*” (CEC, 2005b: 6). This last proposal (CEC, 2004b) effectively embodies a mechanism which prevents Member States from regulating at national level matters which are deregulated at Community level. Some observers have reacted critically to this provision, to the extent that it restricts the regulatory powers of Member States.

²⁰ For example compatibility with modern electronic methods in the customs sector or public procurement.

b. Communication on impact assessment, March 2005 ⁽²¹⁾

In its Communication issued in March 2005 (CEC, 2005f), the Commission defines a new approach aimed at improving regulation still further with a view to enhancing competitiveness. It concentrates on three points:

- 1) improving and extending the use of impact assessment for new proposals, including the establishment of a method for quantifying administrative costs (CEC, 2005d);
- 2) screening of pending legislative proposals;
- 3) introducing a new method for simplifying existing legislation.

This Communication is intended to be a direct follow-up to the mid-term review (CEC, 2005g) of the Lisbon strategy; its priority objective is “*improving European and national legislation in order to promote European competitiveness and thus stimulate growth and employment*” (CEC, 2005f: 3). The Commission makes an ever closer link between the level of legislation and competitiveness, which in our view is likely to lay the whole exercise open to abuse. Whilst it may be clear that an excess of ill-judged legislation will have an adverse impact on competitiveness, it is harder to see that clearer and more transparent legislation or the use of alternative methods will necessarily enhance competitiveness, since that depends in the first instance on factors such as management, productivity, innovation, the quality of infrastructure, and the tax system. Moreover, many open questions remain. What elements will be taken into account for the purpose of impact assessment and cost analysis of a piece of legislation? How will the economic factors be weighted as against social and environmental considerations? Who will be responsible in practice for carrying out this analysis, and for subsequent dispute resolution? An unsustainable link is sometimes made between “bureaucratic administrative burdens” and the “necessary level of regulation”. There is inevitably a risk that

²¹ The Commission’s major independent review of the impact assessment system is due to start in March 2006 and to be completed towards the end of that same year, despite the cumulative delays.

methodological expedients may be used in the collection and collation of data, especially if the assessor makes assumptions or uses a false premise in his or her research. Moreover, this reform seems to be driven by considerations of short-term competitiveness.

c. Outcome of the screening of legislative proposals pending before the legislator

In its Communication of 16 March 2005 (CEC, 2005f) ⁽²²⁾, the Commission indicated that it intended to select legislative proposals which it had adopted prior to 1 January 2004 and which remained pending. This it did in on 27 September 2005, in the Communication entitled “Outcome of the screening of legislative proposals pending before the legislator” (CEC, 2005d) ⁽²³⁾. After reviewing 183 proposals pending before the European Parliament and the Council, the Commission announced that it intended to withdraw one third of these measures: 68 legislative proposals. Its view was that a number of these proposals either no longer chimed with the objectives of the New Partnership for Growth and Jobs (the Lisbon Strategy) or did not meet the standards required for better regulation. A number of texts were withdrawn from the list, such as the proposal on banning heavy goods vehicle traffic at the weekend, or the protection of workers from over-exposure to the sun’s rays. In other cases the Commission’s view was that the legislative process was not moving ahead rapidly enough or that the proposals were simply no longer relevant.

The publication of the 68 measures withdrawn by the Commission was discussed at the Competitiveness Council on 29 November 2005, when France and Belgium took issue with the withdrawal of two proposals

²² The Commission Communication and the comprehensive list of proposals to be withdrawn are available on the following site: http://europa.eu.int/comm/enterprise/regulation/better_regulation/docs/en_br_final.pdf.

²³ The tidying-up of the *acquis communautaire* has been underway for some time. The most recent edition dates from the period 2004-2005. It is not unusual for the Commission to carry out a tidying-up exercise of this type. What has changed however, is the publicity given to it, and also the fact that the terms of reference appear to be different from those in previous editions.

respectively on European associations and European mutual societies. This initiative also aroused suspicion amongst MEPs, who had not been consulted on which proposals were to be withdrawn (24). Hence, of the 68 texts, 20 were obsolete or null and void, but 40 were blocked in the Council due to opposition by one or more Member State. Only seven texts met with opposition from the European Parliament. Many other proposals for legislation at European level, which would unquestionably have been useful and indeed desirable in the opinion of those involved in the sector, were abandoned: for example, provisions on the use of diesel for business purposes, working conditions for temporary workers, protection of cod and herring stocks in the North Sea, and the ban on heavy goods traffic at weekends. It would therefore appear that the Commission joined forces with the Council against the European Parliament. Does this approach on the part of the Commission herald a shift in alliances within the institutional triangle of the Union? It is still too early to say for sure.

c. Proposal for a Regulation establishing a statute for the European Mutual Society (25)

Even though Council work on this text had effectively ground to a halt in 1996, the Commission's withdrawal of the proposal for a Regulation on the European Mutual Society was immediately opposed. The withdrawal of the text appeared unjustified to backers of mutual societies and to the progressively-minded, but also to France and Belgium. With the recent introduction of the European Company and the European Cooperative, the regulation on the European Mutual Society was really necessary in order to complete the legal framework within which companies are authorised to operate in the internal market.

Mutual societies indeed appear to be a structural part of the internal market. This statute exists in twenty of the 25 Member States of the

24 The Commission, which alone has the right to initiate legislation, may withdraw its text so long as it has not received final approval by the European Parliament and the Council.

25 1991/0390/COD.

Union ⁽²⁶⁾. Mutual societies account for a substantial part of the European market. In insurance for example, they represent almost 20% of the European market.

Secondly, these companies must be able to benefit from the advantages of the internal market in the same way as others with a discrete statute. The lack of a European Statute places these companies at a competitive disadvantage by comparison with, for example, limited companies. A merger of mutual societies at European level, or the creation of European-scale groups of mutual societies are in practice hindered by the lack of common rules.

Finally, the draft Directive on cross-border mergers does not appear to take this situation into account, particularly because it does not provide clear and discrete rules for mutual societies. A European Regulation would enable harmonisation of the rules which would in turn pave the way for consolidation of mutual societies.

At the Competitiveness Council on 29 November 2005, France and Belgium intervened in order to explain to the Commission that they did not wish this text to be withdrawn, and to request that fresh discussions be initiated on the matter. Finally Vice-President Verheugen promised that the Commission would draft a new proposal ⁽²⁷⁾.

The cost of a piece of legislation is very difficult to determine. Some experts, including the Commission, believe that the analysis of Dutch legislation was done in an “approximate” way, using the interview method. Is this a scientific method?

²⁶ This statute does not exist in Estonia, Lithuania, the Czech Republic, Slovakia or Greece.

²⁷ To date, consultations are still underway between the Commission and the EP. The list has not yet been published in the OJ, which means that the proposals on the European Mutual Society and the European Association remain on the table.

d. Communication on an EU common methodology for assessing administrative costs imposed by the 2005 legislation

Besides impact assessment, the Commission engaged on a second front, namely calculating the impact of legislation on competitiveness and on companies ⁽²⁸⁾. On 21 October 2005, it presented favourable conclusions on the pilot study it had carried out between April and September 2005 on a common methodology for assessing administrative costs imposed by legislation ⁽²⁹⁾.

The common approach would be based on the Standard Cost Model, which has attracted interest from an increasing number of Member States ⁽³⁰⁾. This method, used for the first time in the Netherlands in 2002, was conceived as a tool which could be used to quantify progress in reducing administrative burdens at national level. It consists of a detailed evaluation of the different legislative texts, based mainly on direct discussions with business and expert opinion (micro-evaluation). This method requires the collection of data on the time and wage costs involved in meeting the information obligations imposed by a legislative act, as well as data on the number of entities concerned. It should be noted that the “standard cost” method focuses exclusively on wage costs incurred by the company in order to comply with legislative obligations, without factoring in any possible favourable impact of the legislation in terms for example of legal certainty.

²⁸ The issue of reducing administrative costs for business is being addressed under the auspices of the Ecofin Council on the basis of texts forwarded to it from the Economic Policy Committee. Ecofin has discussed this issue on several occasions.

²⁹ The importance of quantifying these costs has been highlighted regularly by the Ecofin Council and the European Council.

³⁰ For instance, the Netherlands and Denmark have assessed all their legislation and systematically analyse the impact of all new measures. The UK and the Czech Republic are preparing to follow suit, and at least seven other Member States have taken measures to test the Standard Cost method in one or two sectors.

The Commission has reached a favourable conclusion regarding the feasibility of an EU-wide common method. Fortunately, it has accompanied its recommendation with a number of caveats, namely that (1) all EU Institutions and Member States use the same definition, core equation and reporting sheet when assessing administrative costs at EU level; (2) the EU common methodology is applied in a proportionate manner; (3) that more Member States coming from all parts of the Union are willing to contribute and (4) adequate level of staffing and financial resources are available within the Commission for assessment and evaluation. The Commission nevertheless states in its document that “*a number of methodological points could not be fully addressed and there were problems with the availability and accuracy of basic data*” (CEC, 2005e: 4). This admission by the Commission itself should surely inspire caution on the part of its co-legislators.

Finally, the Commission is proposing to work on the assessment of net administrative costs (new costs imposed by an act minus costs eliminated by that same act), in order to avoid the need for costly periodic evaluation. At this stage, the Commission has not yet decided to add the assessment of administrative costs to the impact assessment of each new legislative provision. It will do so once certain sectors have been identified for simplification purposes. To this end, the Commission has embarked on a pilot study ⁽³¹⁾ to test methods for the quantitative assessment of burdens imposed by both existing and proposed Community legislation. First results should be available in early 2006.

2.2.4 Legislative programme for 2006

In 2005, the Commission increased the pace of work on improving the regulatory environment. It intends to continue with this in 2006 and to roll out implementation of better regulation. In the new legislative programme for 2006 (CEC, 2005h), it undertakes to achieve the following progress:

- *Subsidiarity and proportionality* (act only where necessary and using the “lightest possible touch”).

³¹ See SEC (2005) 175. The pilot projects will include areas such as statistics and construction materials.

- *Consultation* (use of existing tools to involve citizens in the decision making process and will encourage new forms of consultation),
- *Impact assessment* (to be implemented systematically for all legislative and policy-defining proposals contained in the Work Programme for 2006; impact assessments conducted during 2006 will be preparatory work for the 2007 programme) ⁽³²⁾.
- *Legislative simplification* (new phase in simplifying legislation launched in October 2005; setting out a 3-year rolling programme to examine legislation. In the first phase, the focus will be on the automotive, construction and waste sectors).
- *Administrative simplification* (review of internal procedures of the Commission to deliver significant internal simplification, notably regarding administrative, financial management, and tendering and public procurement).

In 2006, the “better regulation” agenda will be central to the Commission’s activities. Its work programme will be subject to a mid-term review in the summer of 2006, and will be subject to amendment at that point if necessary.

An observer cannot fail to be struck by the drastic reduction in the number of legislative initiatives proposed by the Commission in its 2006 work programme, and the resultant “pride” on the part of both Commission President José Manuel Barroso and Commissioner McCreevy.

2.3 Role of the EU Council

The EU Internal Market Council played an important role as intermediary and coordinator firstly in approving the final report ⁽³³⁾ of the high-level advisory group known as the “Mandelkern Group” which was established by Civil Service Ministers in November 2000.

³² The sole cases where impact assessment is not required are Green Papers and consultation with the social partners. In these cases impact assessment is carried out at a later stage if the initiative is to be taken forward.

³³ Final report by the high-level advisory group chaired by Mr Mandelkern, published on 13 November 2001 under the Belgian Presidency.

The so-called “Mandelkern report” was drafted by an advisory group consisting of experts at European Union level. The group was established in order to give effect to the conclusions of the European Councils of Lisbon and Feira in 2000. The conclusions from both of these summits highlighted the importance of high-quality regulation in the EU, and asked the Commission, the Council and the Member States to coordinate efforts in order to define a strategy for simplifying the regulatory environment, including public administration, at both national and Community level. This group’s report identifies areas conducive to a coordinated approach and defines a common method for assessing quality of regulation. Similarly, the group was also given the remit of studying the systematic use of impact assessment, transparency in the consultation process when texts are being drafted, simplification of legislation in force, the more widespread use of codification and the establishment of structures intended to guarantee the implementation of high-quality regulation. Its remit covered both national and Community levels.

Thereafter, in the wake of the reform of configurations of the Council introduced under the Spanish presidency (2000), the Competitiveness Council inherited overall responsibility for piloting proposals under heading of “better regulation”. In December 2004, the Ministers of Finance and Economic Affairs of six Member States⁽³⁴⁾, representing their countries in the Ecofin and Competitiveness Councils, signed a joint letter seeking to impart fresh impetus into the process of improving regulation. Since then, the Ecofin Council has been dealing with the budgetary aspects, whilst the Competitiveness Council retains overall responsibility for the management of this agenda. Under each EU Presidency, the latter has adopted Council conclusions calling on the Commission to continue its work, bearing in mind a series of political imperatives: respect for the *acquis communautaire*, the Community method, the Interinstitutional Agreement, the principles of subsidiarity and proportionality, the balance between the three pillars of sustainable development etc.

³⁴ The four original members (Ireland, the Netherlands, Luxembourg and the United Kingdom) have been joined by Austria and Finland, the Member States holding the Presidency in 2006.

2.4 The European Parliament: in retreat?

In the motion for a resolution on the European Parliament report by Sylvia Kaufmann MEP (GUE), which was adopted on 28 November 2001, the European Parliament “*considers that the drafting of an “action plan for better regulation” by a Council working party (Mandelkern group on better regulation) and, at the same time, by a Commission working party with a similar brief, represents a serious breach of the Community method [our emphasis], for Parliament, as co-legislator, was neither informed of, nor involved in, the work of these working parties*” (European Parliament, 2001: point 30).

Since then the European Parliament has considered the matter on several occasions ⁽³⁵⁾. When the parliamentary committees were consulted for their views on the Commission’s priorities for simplification in 2006, they stressed that “*this approach should not lead to a re-writing of the *acquis communautaire* outwith the scope of democratic accountability*”. They pointed out that “*simplification should not be used as a pretext for calling into question policies which have been adopted, and stand by the distinction between technical simplification and simplification of policy*”. Finally, some committees “*deplored the lack of analysis of the true impact of simplification in real terms, since it could imply changes of substance which should be subject to democratic scrutiny, however minor*” ⁽³⁶⁾.

In conclusion, it is appropriate to look at two draft reports currently under discussion. The first (European Parliament, 2006a) is by the Italian MEP Giuseppe Gargani (PPE-DE). He endorses, *inter alia*, the Commission’s view that “*the repeal of irrelevant and obsolete acts*” should go hand in hand with a Community act “*to prevent Member States regulating matters that have been deregulated at Community level*” (point 3). The other report (European Parliament, 2006b), by the Dutch MEP Bert Doorn (PPE-DE), “*notes that much secondary legislation comes into being via the ‘comitology procedure’; considers that such legislation must meet the same quality requirements as primary legislation and that it must therefore also be subject to impact assessment*” (point 6).

³⁵ See in particular the report of 25 September 2003 by the Italian MEP Monica Frassoni (Greens/ALE) on the conclusion of the Interinstitutional Agreement (European, Parliament 2003).

³⁶ Position of parliamentary committees on the Commission’s priorities for 2006, unpublished document, February 2006.

2.5 The Interinstitutional Agreement of 23 September 2003

An Interinstitutional Agreement (IIA) on Better Law-making⁽³⁷⁾, adopted in December 2003 by the three European institutions (European Parliament, Council, Commission), establishes a global strategy for better regulation within the framework of the overall legislative process of the EU. While recalling the undertakings made by the Commission in its Action Plan for improving regulation, the IIA also sets out the commitments made by Parliament and the Council in terms of improving the legislative process. Amongst the principal features are improved coordination and greater transparency in interinstitutional arrangements and the creation of a stable framework for “non-binding instruments”⁽³⁸⁾, which should facilitate their future use, increased use of impact assessment in Community decision-making, and changes by Parliament and Council to their working methods so as to accelerate the adoption of legislative proposals on simplification. It is worth noting that the IIA is very cautious in respect of alternatives to legislation: “*The three Institutions (...) recognise the need to use, in suitable cases* [our emphasis] *or where the Treaty does not specifically require the use of a legal instrument, alternative regulation mechanisms*”⁽³⁹⁾.

Follow-up to the Interinstitutional Agreement

The Interinstitutional Agreement sowed important seeds in terms of improving legislative cooperation. The Irish and Dutch presidencies embarked on follow-up work, which during the second half of 2004 focused particularly on two aspects of the Interinstitutional Agreement, namely impact assessment and simplification.

In terms of impact assessment, a wide-ranging consensus has emerged behind the view that the Council should discuss the Commission’s impact assessment more systematically. The Commission is called upon to flag up, in its impact assessment, any probable substantive modifications and

³⁷ Interinstitutional Agreement on Better Law-making, OJ C 321 of 31 December 2003, pp.0001-0005.

³⁸ The “non-binding instruments” are co-regulation and self-regulation.

³⁹ Interinstitutional Agreement on Better Law-making, 23 September 2003, point 16.

amendments, so as to restrict the number of impact assessments required whilst the other institutions are carrying out their legislative role (to avoid delay and duplication). Henceforth, impact assessment at Council level should be coordinated by the respective presidencies in close cooperation with the Commission (in particular as concerns technical and methodological support), the General Secretariat of the Council and the Member States.

The Council believes that the Commission’s impact assessment should as a rule form the basis and the reference point for impact assessments generated by the other institutions, and that in general, and in broad terms at least, these should follow Commission methodology, so as to ensure a degree of comparability for the purpose of assessing the various options for political decision-making.

As to simplifying and reducing the volume of legislation, the Interinstitutional Agreement provides for close coordination between the three institutions on the adoption of simplified proposals. After a first “round” in which priorities were identified, the Luxembourg and British presidencies embarked on a second phase of consultations with Member States in the wake of the European Council of spring 2005. The presidency of the Council gave priority within Council bodies to the 23 simplified proposals pending in January 2005, independently of the fact that a pilot project was underway (2nd Company Law Directive) aimed at adopting the simplified proposal before the end of 2005.

3. The Services Directive: an illustration of “better regulation”?

Much has been said in the context of the Services Directive about the aspects relating to the country of origin principle (COP), introduced by the Commission in Article 16 of its original proposal. The original version of Article 16 provides that “*Member States shall ensure that providers are subject only to the national provisions of their Member State of origin which fall within the coordinated field*” (CEC, 2004c: 55) ⁽⁴⁰⁾. The COP thus defined

⁴⁰ This related to national provisions on access to and provision of a service, in particular those governing the conduct of the service provider, the quality or content of the service, advertising, contracts and service provider liability.

would naturally tend to bring about liberalisation in the services sector. As it stands, it is effectively an illustration of a potential form of competitive deregulation. The legislation of the country of origin becomes *de jure* the standard applying in the country of destination. At least as far as the coordinated field is concerned, the way ahead is clear for competitive deregulation since companies might be tempted to establish their base in countries with less stringent regulations and to operate their services from there. In this scenario, the most stringently-regulated countries would be penalised by comparison with those which had more lax requirements, and this could lead to a form of deregulation on the basis of the “lowest common denominator” (on this point see Van den Abeele, 2005).

The effect of the section of the Directive dealing with freedom of establishment may perhaps have been underestimated. This section will undoubtedly have much further-reaching effects than the country of origin principle in terms of the “better regulation” agenda. Notwithstanding the European Parliament’s extensive amendments to the “Establishment” section of the draft Directive during its first reading on 16 February 2006, this chapter nonetheless bears the hallmark of “less regulation”.

Article 9 ⁽⁴¹⁾ stipulates that “*Member States shall not make access to a service activity or the exercise thereof subject to an authorisation scheme unless the following conditions are satisfied*”:

- a) the authorisation scheme does not discriminate against the provider in question;
- b) the need for an authorisation scheme is objectively justified by an overriding reason relating to the public interest;
- c) the objective pursued cannot be attained by means of a less restrictive measure, in particular because an *a posteriori* inspection might take place too late to be genuinely effective.

⁴¹ The European Parliament replaced the negative wording (“shall not”) with a positive (“shall”).

Article 10 requires that authorisation schemes comply with criteria which preclude the competent authorities from exercising their power of assessment in an arbitrary or discretionary manner. Schemes must be non-discriminatory; objectively justified by an overriding reason relating to the public interest; proportionate to this overriding public interest; precise and unambiguous; objective and made public in advance.

Article 13(4) ⁽⁴²⁾, which covers authorisation procedures, provides specifically that if no reply is forthcoming within a reasonable period fixed and published in advance, then the authorisation shall be deemed to have been granted.

Article 15 requires Member States to “screen” ⁽⁴³⁾ their legal system in order to ensure that it complies with the principles of non-discrimination; necessity (measures must be objectively justified by overriding considerations of public interest) and proportionality. It should be noted that Article 15(6) requires Member States to notify the Commission of any new legislative, regulatory or administrative provisions which set requirements such as fixed minimum or maximum tariffs, requirements fixing the number of employees, or an obligation on a provider to take a specific legal form, in particular to be a legal person or a non-profit-making organisation.

Article 31 sets out accompanying measures to encourage providers to take action on a voluntary basis in order to ensure the quality of service provision, in particular by having their activities certified or assessed by independent bodies, or by drawing up their own quality charter or participating in quality charters or labels drawn up by professional bodies at European level.

⁴² This paragraph was deleted by the European Parliament and replaced with a less binding form of words.

⁴³ This “screening” was upheld by the EP, but it was set aside in respect of services of general economic interest (SGEI). Paragraphs 5 (“standstill clause”) and 6 (compulsory notification of new provisions) were withdrawn by the EP.

Article 39⁽⁴⁴⁾ provides that “*Member States shall, in cooperation with the Commission, take accompanying measures to encourage the drawing up of codes of conduct at Community level, in conformity with Community law, in particular in the following areas: the content of and detailed rules for commercial communications relating to regulated professions, as appropriate to the specific nature of each profession; the rules of professional ethics and conduct of the regulated professions which aim in particular at ensuring, as appropriate to the specific nature of each profession, independence, impartiality and professional secrecy; the conditions to which the activities of estate agents are subject*”.

It is only in Article 40 that mention is made of a provision on additional harmonisation, stipulating that “*The Commission shall assess, by [one year after the entry into force of this Directive] at the latest, the possibility of presenting proposals for harmonisation instruments on the following subjects: the detailed rules for the exercise of cash-in-transit services; gambling activities which involve wagering a stake with pecuniary value in games of chance, including lotteries and betting transactions, in the light of a report by the Commission and a wide consultation of interested parties; access to the activity of judicial recovery of debts*”.

Thus it is clear that the Services Directive is a “deregulation machine”: it increases exponentially the prohibitions on authorisations and legislative, regulatory and administrative requirements, and restricts harmonisation to sectors which, although not insignificant, are not the most sensitive.

⁴⁴ The EP has retained the principle of codes of conduct but has deleted all references to the areas listed.

4. Risks flowing from the “better regulation” agenda

The following table is an attempt to summarise the current situation and the risks for the future.

Summary table of risks for the EU

Current situation	Risks for the future
<i>Acquis communautaire</i> (point 35 of the IIA) – Legal predictability and tools for protection of public interest	Dismantling or rewriting of the <i>acquis</i> – Deregulation
Balance between the three pillars (economic, social and environmental)	The economic pillar is dominant. Competitiveness is the real issue at stake here
Primacy of the Community method (points 16 and 17 of the IIA)	Self-regulation, co-regulation and standardisation: the alternatives to legislation take hold
Exclusive right of initiative on the part of the Commission	Parallel initiatives of the High Level Group, the Mandelkern Group and the Directors of Better Regulation
Interinstitutional balance and common approach by the three institutions. The co-legislators (Council and EP) amend and steer the Commission’s work downstream, once outlines are established.	Interference from Member States, lobby and interest groups in the legislative and non-legislative process. Upstream consultation of interest groups via internet influences the Commission’s proposals directly.
Global agenda global linked to the three main policy dimensions: social, economic and environmental	“Business-oriented” agenda
Independence and specificity of the various Council configurations, with the General Affairs Council playing the role of arbiter	Pre-eminence of Ecofin Council, the Economic Policy Committee (EPC) and the Competitiveness Council
Codecision procedure where the EP has the final say	“Fast track” procedure where the EP is ignored or bypassed

Conclusions

The stakes are high where the competitiveness of the European economy is concerned. That is self-evident. However, the quality of regulation is no less important. Quality is best gauged by looking at the objective underlying each piece of legislation and the impact it will have on each of the areas identified by the Lisbon strategy: economic, social and environmental. However, one must not overlook the environmental and social costs, the indirect costs nor the costs of non-regulation in terms of risk for business and citizens alike. In opting for an approach based on business costs (cf. the net model based on the Standard Cost Model), the Community runs the risk of overturning the traditional equilibrium between efficiency, competitiveness, productivity and global security and social cohesion in the widest sense of the term. The public interest must prevail over individual interests.

It is unquestionably right to seek to legislate better and to eliminate bureaucratic hurdles. That too is self-evident. So it is perfectly appropriate to take pride in efforts made to simplify and improve legislation. It is also vital that the objectives, scope and extent of the overall drive for better regulation be made more transparent. However, the objective of the “better regulation” agenda cannot be to question the very principle of Community regulation nor the need to use it to achieve public interest objectives, especially a high level of social and environmental protection as required under the EC Treaty. In this respect the use of “alternatives” to regulation (self-regulation and co-regulation) should, in our opinion, be secondary to the Community method, and care should be taken to ensure that they are subject to democratic scrutiny by the EP.

The “better regulation” agenda must not be used to challenge the *acquis communautaire* in the guise of “simplification”. National public authorities must retain their power to act. The principles of subsidiarity and proportionality underlying the acts of the Union and enshrined in the EC Treaty must be respected.

Particular attention should be devoted to the interinstitutional balance at Community level, to the powers and the specific role of each institution. The power of Council and Parliament to make decisions and

to amend must remain intact, even where an impact assessment proves unfavourable. The legitimacy of the co-legislators is at stake. The various compositions of the Council (Environment, Employment, Social Affairs, etc.) must retain their independence and their specific remit, even if it is right that a role of arbiter and an appeal function be devolved to the General Affairs Council.

The involvement of “outside expertise” or “independent consultants” to assess progress made by the institutions is an issue which requires careful consideration. There is no doubt that both have a useful role to play, but they cannot be a substitute for the Commission’s right of initiative nor for the decision-making powers of the other two institutions.

Simplification and improvement of the *acquis communautaire* must go hand in hand with a rethink of harmonisation. It is not a question of less legislation, but of better legislation ⁽⁴⁵⁾. As was said during a working session by one well-informed participant, “*The EU must remain a relevant framework for both regulation and solidarity*”.

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⁴⁵ Paragraph 3 of the conclusions of the Competitiveness Council on 29 November 2005 reads as follows: “*Calls on the Commission to build upon this legislative screening process to also clearly identify where further harmonisation is needed, and take this into account in its future proposals*”.

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The Green Paper on demographic change and the challenge of ageing for Europe's welfare states

Introduction

The Green Paper published by the Commission in March 2005, with the title “*Confronting demographic change: a new solidarity between the generations*”, has been the source of an open debate about the present and future impact of demographic trends on the sustainability of the European social model.

The comparison of both the Commission's paper and the stakeholders' replies allows us to address some questions about the plausibility of the “ageing alarm”. In the following contribution, we make reference to the key “messages” from the Commission about ageing, fertility trends, immigration, and activation of young, female and older workers. The second section focuses on the contribution to the debate by some of the European actors having a stake in the policy fields affected by demography. In particular, we focus on comments from the European Trade Union Confederation (ETUC), the European Federation of Older People and Pensioners (FERPA), as well as from the Union of Industrial and Employers' Confederations of Europe (UNICE). In section three, we briefly summarise the response from the European Older People's Platform (AGE), one of the civil society actors in the field. Sections four and five will propose some further investigations into the nature of the “demographic crisis” and its potential impact on welfare institutions.

This article aims to contribute to a richer and more complex approach to the vulnerability of European welfare programmes. While ageing will certainly affect socio-economic institutions, the comparison of statistics

about past experience and future projections shows a less radical and more manageable impact. The need for reforms will be consistent with innovations to quantitative and qualitative aspects of social programmes that affect both their financial viability and social adequacy. A further underestimated complication is that, while the European population will face major changes in the future, these will be unevenly distributed between countries and regions, and welfare institutions as well. Decision-makers need to take such differences into account to define effective strategies for reform.

1. The Green Paper on demographic change

The Green Paper aimed to launch a wide-ranging debate on demographic change and the strategies to meet that challenge. In this section, we briefly look at the key messages from the Commission about both problems and solutions related to population trends.

1.1 The challenge: economic growth without a “demographic motor”?

According to the Commission, demographic changes are the result of three basic phenomena. The first dynamic concerns the progressive increase in longevity as a result of progress made in the average standards of healthcare and quality of life in European countries. On the one hand, it is an historic success of the European welfare states. But, on the other, it will probably lead to a new (problematic) balance between generations, with a growth in the number of elderly people and hence in the non-active population. The demographic dependency ratio, that is the ratio of the population aged 0-14 and over 65 to the population aged between 15 and 64 years, will rise from 49% in 2005 to 66% in 2030. In particular, in the period 2005-2050, the age group between 55 and 65 (older workers) will increase by 8.7%, while the number of individuals aged between 65 and 79 (elderly people) will grow by 44.1%, and very elderly people (aged 80 and over) will rise by about 180% (CEC, 2005a: 3-4) (Table 1).

The second factor which contributes to the “demographic crisis” is the continuing growth in the number of workers over 60 (at least until 2030) when the so-called “baby-boom” generation will become elderly. That generation is particularly numerous and when it reaches

retirement, the balance between the active and non-active population will be adversely affected.

Table 1: European demography in the next decades in EU-25

	2005-2050	2005-2010	2010-2030	2030-2050
Total population	-2.1%	+1.2%	+1.1%	-4.3%
Children (0-14)	-19.4%	-3.2%	-8.9%	-8.6%
Young people (15-24)	-25.0%	-4.3%	-12.3%	-10.6%
Young adults (25-39)	-25.8%	-4.1%	-16.0%	-8.0%
Adults (40-54)	-19.5%	+4.2%	-10.0%	-14.1%
Older workers (55-64)	+8.7%	+9.6%	+15.5%	-14.1%

Source: CEC (2005a: 4).

Thirdly, low birth rates will further impact on population trends. A number of elements, such as difficulties in finding jobs, housing costs, new study, working and family life choices have all contributed to decreasing fertility well below the population replacement level (equal to 2.1 children per woman). The worst situation is that of southern European countries, where the replacement level is around 1.3 children per woman, while the average level in the EU countries is 1.5. On that basis, it is possible to foresee, in the period 2005-2050, a decrease of 19.4% in the number of children between 0 and 14 years, parallel to an even more negative trend of people aged between 14 and 24 (-25%) and young adults between 25 and 39 (-25.8%). Consequently, total EU population will grow slightly until 2025 before starting to decrease. The active population (between 15 and 64) will diminish by about 20 million between 2005 and 2030. As a consequence, the potential GDP growth per year in EU countries would fall from 2-2.25% to an estimated 1.25% in 2040. The Green Paper refers to similar trends for the new Member States (¹).

¹ The last communication from the Commission on the Social Situation in the European Union (CEC, 2005b) gives information about demographic trends in new EU members.

According to the Green Paper, the combined effect of these dynamics will produce a huge challenge to the European social model as we know it. The Union no longer has a “demographic motor”, and “*never in history, has there been economic growth without population growth*” (CEC, 2005: 5).

1.2 The solution: a new solidarity between the generations

For the Commission, in order to cope with that source of problems, the European Union has “(…) *to invent new ways of liberating the potential of young people and older citizens*” (CEC, 2005: 6). In the introductory notes, the paper focuses on the Lisbon Strategy as a way to meet these challenges. Reforms should be introduced to get people into jobs (especially women, younger and older people), to improve innovation and productivity, and to modernise social protection programmes. Moreover, the role of the family, the institution having a decisive role in promoting solidarity between generations, is important to improve fertility and to encourage the reconciliation of life and work.

New policies to increase fertility are the first measure envisaged by the Green Paper. While fertility in Europe is particularly low and insufficient to replace the present population, surveys prove the gap between the number of children Europeans want and those they actually have. Thus, new measures should favour a rise in birth rates through: incentives to earlier access to employment, more job stability, reduced housing costs, and more benefits for families (e.g. parental leave, childcare, etc.) ⁽²⁾.

Immigration from outside the EU could further help to mitigate the effects of negative demographic trends, the key goals being to boost the population in general, and more particularly to supply manpower. At the Thessaloniki European Council of 2003, the EU proposed a common integration policy for immigrants to meet economic challenges through an effective and transparent administration of the admission mechanisms for third country nationals, and took a decision on the inclusion of migrants in host societies.

According to the Commission, the third strategy is that of a “better integration of young people”. Despite the increase in the level of education and training potentially leading to productivity growth, youth

² The Commission put huge emphasis on this point, see also Vignon (2005).

is an underestimated resource of Europe. Some indicators reveal the present limits: unemployment rates for people under 25 in 2004 were above 17%, compared to 7% of people aged 25 and over. The risk of poverty was 19% for people between 16 and 24, compared to 12% for people aged 25-94 and 17% for people over 65. To eradicate these forms of exclusion, education systems are expected to raise the level of training and education, reduce the number of young people who leave school with no qualifications or drop out of school early. More efforts are therefore proposed to alternate education and work and professional training to meet the changing needs of the economy. Social partners, public authorities and local players have the task of improving the integration of all these measures for the inclusion of young people.

The rapid transformation of the labour force, with a growing role for experience and skills of older workers, should favour a new approach to the “working life cycle”. For the Commission, the increase of employment rates for people over 55 is thus a key target. This can be implemented through a number of strategies: more flexible organisation of working time, and new technological developments to improve the quality of jobs and the working environment. At the same time, the definition of lifelong learning strategies and raising the retirement age are promoted as potential solutions. This is what the European Foundation for the Improvement of Living and Working Conditions (2005) has called a new “life course” approach to social and employment policy.

The increasing number of elderly people is expected to represent both an opportunity and a burden. The former corresponds to the better health of elderly people (especially those between 65 and 79). This is consistent with growing consumption of goods and services and greater mobility across Europe, and new opportunities to provide services to help younger generations (children and grandchildren). The reform of pension programmes is proposed to define more favourable and flexible “bridges” between work and retirement. According to this argument, the employment rate of people aged between 65 and 74 (in 2003 at 5.6% in the EU, compared to 18.5% in the US) should increase through new opportunities to combine part-time work and pension revenues. On the other hand, the projected burden of ageing is related to the rising number of very elderly persons (aged 80 and over): from 18.8 million to about 35

million in 2030. This portion of the European population will need appropriate care, especially high intensity care. Families will not on their own be able to provide the services needed; they will need support from networks of solidarity within local communities.

Having indicated the key policy measures to be implemented, the Commission then refers to the key instruments the EU can activate. New legislative measures but also financial instruments like the Structural Funds, and social dialogue, civil society dialogue, and the open method of coordination (OMC) are expected to play a strategic role.

At present, the Broad Economic Policy Guidelines (BEPG) and the Stability and Growth Pact have already focused on the impact of ageing on public finances. The European Employment Strategy (EES) and educational and vocational training policy are already mobilised to combat school drop-out and to raise the level of young people's initial training, to promote active ageing and to improve job quality. The OMC on social protection and social inclusion have set key objectives for the reform of pension systems and of policies to eradicate family poverty and tackling child poverty. Gender mainstreaming has informed different policy initiatives, to respect equality between men and women: the social dialogue, for instance, has concluded agreements on parental leave and part-time working, subsequently implemented through directives. In a broader perspective, since 2000, a legislative framework has covered all discrimination in employment. Finally, the Social Fund has supported the EES and the Regional Development Fund has promoted the development of childcare and better "age management" in companies. And the research framework programme is aiding projects associated with ageing, like clinical research, and studies on demographic trends.

2. Contributions to the debate: the position of Europe's social partners

The Green Paper has represented the opportunity for a wide consultation of key actors having a stake in the impact of population ageing. It proposed, in fact, 35 open-ended questions on all the issues briefly introduced above. The Commission then organised a conference (with the same title as the Green Paper) in July. We refer below to some

of the key responses from the European social partners and civil society (Table 2). They have contributed to enriching the analysis of demographic change, through quite varied arguments, some in contrast to those of the Commission.

Table 2: European social partners' and civil society contributions on demographic trends

	ETUC	FERPA	UNICE	AGE
Key reference	Lisbon Strategy	EU, UN and UNECE reports	Kok reports	EU and UN documents
Issues	Demographic cycle rather than crisis (no need for exaggeration)	Challenges and opportunities related to demographic trends	Demographic ageing as one of the biggest challenges for Europe; high spending on pensions and health-care	Challenges and opportunities related to demographic trends
Solutions	<ul style="list-style-type: none"> - More and better jobs; - Reforms to welfare state financing; - Better employment for women; - Youth initiatives; - Immigration (partial solution) 	<ul style="list-style-type: none"> - Better social integration for young and older people; - Full employment; - More investment in social policy; - Lifelong learning; - Active role of elderly in a context of work-life balance; - Support for families; - Immigration (a resource but not a solution) 	<ul style="list-style-type: none"> - Sound public finances; - More efficient education and training; - More favourable context for entrepreneurs; - Modernising social protection and labour markets; - Increase employment rates of older workers; - Immigration (partial solution) 	<ul style="list-style-type: none"> - Better integration of younger people; - Lifelong learning; - Better jobs; - Develop services for older people; - Solidarity for the very elderly
EU role and instruments	Key EU role: Lisbon Strategy; Structural Funds; social dialogue	Key EU role: OMC; Structural Funds; social dialogue and civil society dialogue	EU role as a catalyst for action Key role of the State Key role of social dialogue	Key EU role: OMC; Structural Funds; Youth initiative; civil society dialogue

2.1 The response from ETUC: a demographic cycle rather than a demographic crisis

The ETUC Executive Committee adopted a contribution to the debate in June. The first remarks concerned the risk of exaggerating the demographic challenge. More than a crisis, it is defined a foreseeable cycle related to problems and opportunities as well. What is more, projections from the Commission do not consist of realities and thus cannot be used to justify overarching policy solutions (ETUC, 2005). While the Green Paper addresses some of the key determinants and outcomes of demographic trends (such as social protection policies, reconciling work and family etc.), other issues are under-analysed (for example housing conditions).

For the ETUC, a first concern on demographic change is related to the need for new labour market policies. Measures like those allowing for a combination of retirement and employment, more innovative work organisation, more limited obstacles to regional mobility and better working conditions can be pursued through legislative intervention, the activation of resources from the Structural Funds but especially social dialogue (Table 2).

A second issue consists of the impact of ageing on social protection programmes. Here the approach proposed by the ETUC contrasts with those of many other influential actors. Financial strains on pensions and other social policies are defined as the consequence of recent measures introduced in many countries to reduce social contributions, rather than the effect of demographic trends. Moreover, the low employment rates of both young and older generations contribute to reduce financial resources for social protection. The main strategy thus consists of the revision of methods for financing welfare programmes with more focus on profits made by companies rather than on labour. This is with a view to achieving the key social goals of social protection systems, that are to improve social cohesion and solidarity.

A further policy tool is immigration. Policy-makers at national and European level should interact with social partners to develop more pro-active policies on the entry, residence and protection of migrant workers. This is to deal with potential problems of migration flows. Gender inequalities are another central issue to cope with in addressing

negative demographic trends. Women, in fact, are an “under-utilised pool of labour”, a crucial source of formal and informal care for children and the elderly, and at the same time are expected to give birth to more children and take their share in active ageing. The solution proposed by the European trade unions is to boost female employment in parallel with high-quality services and infrastructures encouraging coordination between work and family life. The Scandinavian countries prove that these factors are correlated to high fertility rates. New shared care responsibility between partners within the family unit should be improved through parental leave and care provision, the availability of negotiated flexible working arrangements and more universal forms of access to care infrastructures.

The ETUC also identifies some priorities for achieving a fair inter-generational contract. The issues of security, stability and quality of jobs are among the most urgent. As its contribution states, for two thirds of young Europeans employment means short-term, part-time, seasonal, or undeclared work. And all this has important consequences on their daily lives: financial dependency on the state and/or their parents, living with a partner and starting a family later, etc. Encouraging young people to become independent means implementing measures to prevent them from dropping out of school, improved opportunities for better jobs, and access to social protection. Older people represent a source of opportunity to develop new and better jobs (related to the provision of care services), given the impossibility for families to give all the care needed.

At the EU level, the Lisbon Strategy (with its emphasis on growth, employment, social cohesion and sustainable development) is defined as the key agenda to deal with all the dimensions of the new demographic cycle. It can be pursued through different instruments. Specific reference is made to the need to optimise the Structural Funds and the EURES network (the European Job Mobility Programme), the renewed European Employment Strategy, and social dialogue.

2.2 The response from FERPA: “a society for all ages”

Among the key stakeholders having an interest in demographic trends, the European Federation of Retired and Older People (FERPA) is one

of those participating in the recent debate⁽³⁾. The communication adopted in July demanded a “society for all” in a changing demographic context and opposed any form of exclusion for both workers and pensioners.

The first and broader critique of the Green Paper concerns the lack of emphasis on the opportunity, rather than the risk, of population ageing. Rather than the uni-dimensional understanding of demography as a problem of low fertility and an increased elderly population, a multi-dimensional perspective is proposed (see Table 2 above). Life expectancy gains are in fact a major change with a potential for better integration of aged persons in social and economic activities. In that respect, FERPA has stressed the key contribution made by the Second World Assembly on Ageing in April 2002 and the United Nations Economic Commission for Europe (UNECE) conference in Berlin in the same year. As its document puts it: “*retired and older people are a resource for society, not a burden to be borne and blamed*” (FERPA, 2005: 3).

FERPA fixes some key objectives: to create a society for all ages, to increase inter-generational solidarities, to promote a high quality of life and high standard of health, and full employment. These goals are defined as “mainstreaming”, in that they should be implemented through consistent policy measures on social protection systems, but also on employment, work organisation, health and safety at work, lifelong learning, etc.

To achieve a fairer distribution of family and domestic responsibilities, a number of actors should work together. The family is recognised as a key provider of elderly and child care, but needs the support of a broader system of care services. To provide a continuum of care and support is a social duty. In that context “*any attempt to restore the traditional role of the family and women would be hugely misguided, because that kind of family no longer exists*” (FERPA, 2005: 5). By contrast, a constructive dialogue

³ FERPA is a member of the European Trade Union Confederation (ETUC). It was founded in 1993 and has a 10 million membership. It coordinates its policy with that of the ETUC, especially on social security and social protection, with a strong focus on pensions, healthcare, and action against social exclusion and poverty.

between institutions, social service providers, patients' associations, and family associations at local, regional, and national level would be vital for an effective care and services policy. Public authorities are asked to support families that are willing to provide care for their members. Financial support for family carers, the extension of pension rights for caring activities, and specific training should be given. In this document, the establishment of a whole system of social services is defined as an investment (more than a cost) that will grant universal social rights for people in need of care, and a source of good quality jobs for younger cohorts.

The European Federation of Pensioners and Older People proposes a more pro-active role for the elderly in planning social assistance and care. The elderly population is expected to be a resource. They have a key role as buyers of good and services. Hence, pensioners' income should be safeguarded especially through tax incentives for innovative technologies (e.g. telemedicine) to improve the quality of their lives. They are particularly active in voluntary activities, within the family (especially childcare) and in the broader social context (in not-for-profit organisations). In line with the need to safeguard universal access to social protection, the public pension and health systems should be improved, with a special focus on combating poverty, and to develop disease prevention and palliative care. What is more, public authorities at all levels should reinforce opportunities for the participation of the elderly in social life: voluntary activities to give care, but also non-formal education schemes and life-long training, are examples of a broader social (rather than just economic) activation. Schools could therefore promote joint training activities while retired teachers could be made tutors for young students. Social dialogue and new forms of civil society dialogue should be implemented to increase labour force participation for people aged 55 and over, to invest in human resources, and to introduce flexible retirement arrangements enabling part-time work with partial pensions.

Regarding the present and future role of the EU, FERPA concentrates on some main lines of action. The first consists of tax incentives and especially a reduced rate of VAT (an area of EU competence) to help families to provide care and to boost solidarity between generations.

Secondly, the Structural Funds should support lifelong learning, the use of new technologies and help combat old and new forms of social exclusion. A wide-ranging process of exchange of good practices is another issue to be dealt with by the EU: especially through the URBAN action plan for the organisation of social services at local level. The Commission is asked to establish specific forms of civil society and social dialogue, as a vital asset for the economic and social development of Europe. The open method of coordination is proposed to improve learning on minimum quality standards, especially in healthcare and long-term care.

2.3 The response from UNICE: accounting for company needs

While FERPA has based its comments on the arguments of the United Nations on demographic changes, UNICE has made explicit reference to the report of the High-level Group on Mid-term Review of the Lisbon Strategy (or Kok group) (UNICE, 2005).

The response from Europe's employers firstly consists of a critical assessment of the Green Paper in two main respects. UNICE expressed its deepest concern about the fact that the Commission approached the challenge exclusively from the point of view of individuals and thus lacked a sufficient account of companies' needs. This leads to the lack of a proper identification of responsibilities of all the actors concerned: not only employers, but also public authorities, individuals and social partners in general. Then, the paper is defined as a source of bias towards emphasising work-life balance policies to the detriment of other dimensions of the problem: especially the long-term sustainability of pensions and healthcare systems, and labour market reforms (Table 2).

In terms of the challenge to be confronted, the first reference is to the growing strains on public finances that will lead to increased taxation and labour costs if no reforms are carried out. This, in turn, is related to the alarming dependency ratio that will affect some countries more than others (e.g. Italy shows the highest level for the next decades). Consequently, decreased labour market participation will further affect the EU. A second source of concern is declining productivity rates, often not reflected in wage formation. This element is indicated as one of the reasons for the lack of competitiveness in Europe. Third, the

aggravation of the skills gap of the workforce and the lack of effective lifelong learning and training activities.

An appropriate response to these challenges should consist of a number of measures consistent with two key lines of argument: the need for an inter-generational approach to ageing, and the revision of the working-life cycle perspective. The former is to inform reforms of public finances, with the progressive removal of public deficits to avoid shifting the burden to future generations, improving the efficiency of education and training, as well as that of labour-markets (to improve employment rates in the older population), and offering a more favourable economic and social context to young and older entrepreneurs. An explicit focus is on the innovation of social protection with a twofold goal: reduce its impact on the state budget, and remove unemployment and poverty traps.

As for the revision of key aspects of the working life-cycle, this is defined through three key issues. Life-long learning is defined as a necessity for individuals who have to improve their skills to adapt to labour market changes. Making learning more attractive and flexible should be a priority for each Member State. The second aspect is the reconciliation of family life and work. Here UNICE criticises the key reference in the Green Paper to the development of parental leave as the main solution. By contrast, measures to further increase the role of childcare facilities and “all-day” schools are identified as more promising instruments to favour new balances without negative effects on social policy and labour-market costs.

As for the role of the European Union, UNICE’s view seems more cautious than those of the other social partners. The EU should act as “*a catalyst for action in the context of the European strategy for growth and jobs*” and promote a genuine debate based on the exchange of experiences on solutions found in different countries. Yet, the “ingredients” of the policy mix to cope with that challenge can only be decided by Member States (Table 2). The key focus is thus on the Lisbon Strategy to improve synergies between policy areas and processes. The new Integrated Guidelines for growth and jobs (IGs) together with the open method of coordination on social protection and on education and training are explicitly defined an important instruments for the

monitoring and evaluation of progress made in national implementation and as a source of inspiration for effective solutions. Explicit reference is made to the role of the European social dialogue to tackle the issue, as proved by the framework of actions on gender equality adopted in March 2005 (UNICE, 2005: 6). More flexible working arrangements are to be mutually acceptable for both companies and employees.

3. Proposals from civil society: the response from AGE

The European Older People's Platform, AGE, is one of the most active social policy NGOs with a specific mandate concerning the conditions of the elderly. In 2005, that organisation contributed to the debate through a consultation of its national members and the organisation of a seminar at the European Parliament with the participation of the Inter-group on Ageing and of other relevant NGOs, such as the European Youth Forum and the European Women's Lobby. All these efforts fed into its response to the Green Paper.

AGE firstly made some preliminary critical remarks on the Commission's approach. First, the response to demographic challenges should be realistic without implicit alarmism. Like the FERPA document, AGE defined ageing as "*one of the proudest achievements of recent social and economic development in Europe*" (AGE, 2005: 1). A broader approach to demographic trends is needed, through both attention to the quantitative effects (increased social protection expenditure, etc.) and qualitative outcomes (the transformation of social institutions, etc.). This must be combined with a more subtle analysis of the changing nature and diversity among the elderly, for example through a clearer distinction between old (between 65 and 79) and very old persons (aged 80 and above).

As far as longer life expectancy is concerned, for AGE this is not a problem in itself, in that it is the effect of better living and working conditions, and medical progress. Demographic projections by the Commission do not take on board the foreseeable impact of stress and environmental pollution, and of new lifestyle-related risks for today's young generation (e.g. obesity, cancer, abuse of drugs, alcohol and tobacco). This means that projections vary depending on the assumptions they are based on. Another critical remark concerns the

most effective response to population ageing. Here the European Older People's Platform stresses the importance of two concepts: choice and confidence. On the one hand, citizens should have a real opportunity to choose how to reconcile work and family life through appropriate employment and social policies. On the other, this is possible through building widespread confidence in welfare programmes to secure their old-age. Explicit reference is made to some measures: increased childcare and eldercare facilities, financial compensation for care duties (e.g. care credits and pension rights for informal carers), as well as support and training for informal carers, development of elderly care structures to promote employment in this field, etc.

The document then gives a particular emphasis to the problematic nature of immigration. Migrants are not to be considered just an economic factor. Rather, the social dimension of the phenomenon and the consideration of needs of individuals and their families should be addressed by policy-makers to avoid risks of creating "second class citizens". In that respect, a common policy on migration must provide the same level of social protection to migrant populations and to EU nationals, and deal with two key issues: the exploitation of migrant labour (through low pay, low status, unsocial working conditions), and the risk of the brain drain and economic loss in the countries of origin (Table 2).

Different strategies are thus identified for building inter-generational solidarity. The first line of action is related to the social and economic integration of younger generations. The best way to avoid poverty in old age is to be engaged in well-paid work throughout working life, in good working conditions, and in good health. The second issue is about making training accessible to those most in need of it (e.g. young, older and female workers) in parallel with more flexible arrangements able to meet the wishes of employees (e.g. mentorship, gradual retirement, etc.). AGE proposes the raising of the average retirement age through incentives rather than a mandatory retirement age. A significant number of older people (and especially women) face poverty and social exclusion. And this problem will be even more alarming in the future because of more fragmented careers and recent reforms shifting the

method of calculation of old-age benefits now increasingly based on average earnings of the entire career rather than on the “best years”.

As for the role of the European institutions, AGE’s response has stressed the need to discuss demographic change and inter-generational solidarity at the EU level because all these issues have a tremendous impact on policies under the competency of the Union. AGE has asked for more coordination between economic, employment and social policies and migration, transport, housing, research and education as well. “EQUAL-like” initiatives could also contribute to innovative approaches to extending working lives, with a parallel focus on both young and older workers. “Making work pay” is judged to be not enough to face up to labour market changes. The EU should increase efforts for more quality jobs.

AGE finally recommends that the Commission publish an annual report on the European response to demographic change, with a summary of what individual members and EU institutions are doing about the issue. The annual report should be debated in a yearly roundtable on demographic change with the active participation of stakeholders and national policy-makers and the European Parliament. All this will help prepare the post-Lisbon Agenda.

4. Nature of the demographic challenge: some critical remarks

The comparison of the Green Paper and some of the contributions to the European discussion on demographic trends shows varied perceptions of present and foreseeable changes. Hence, a more precise definition of the challenge and strategies to deal with it seems necessary. Will future population ageing consist of a “demographic crisis” or a less alarming “demographic cycle”? And what will be the impact on the European welfare states? Some recent scientific contributions help us to carry out a more in-depth analysis (see Castles, 2004; Jepsen, 2005; Morley *et al.*, 2005).

Firstly, as argued by some of the stakeholders involved in the debate, long-term projections are highly fluid and questionable. It is almost impossible to forecast accurately what society will look like in 30 or 40 years. These efforts are usually based, in fact, on a huge number of assumptions about: productivity, technological development, but also

employment, fertility rates, etc. (Jepsen, 2005). While the European Union is clearly entering a new demographic era, the precise degree of alarm has still to be defined.

A second issue is related to the misuse of the old-age dependency ratio to express the demographic threat to socio-economic institutions. As shown by the ETUC communication and De Swert (2005: 25-27), ageing (in relation to the baby-boom generation) is a transition more than a long-standing shock. Once the “baby-boom’ wave comes to an end, our population will be more balanced. What is more, the old-age dependency ratio, that is a simple measure of ageing, does not refer to the proportion of the population that is productive. It ignores the number of people of working age who do not work. Taking account of the population actually in work can provide a more useful indicator that reflects more fully the productivity capacity of a given population. This is the economic dependency ratio: the number of those who are out of work to those who are in work (regardless of age). According to recent calculations from the DG for Economic and Financial Affairs (Ecfm), the old-age dependency ratio is expected to worsen in the period 2003-2025 and 2025-2050 (Table 3).

Table 3: Dependency ratios in EU-15 and EU-10

	Economy dependency ratio			Old-age dependency ratio		
	2003	2025	2050	2003	2025	2050
EU-15	132	126	145	25.23	35.9	51.6
EU-10	159	124	158	19.4	32.7	50.4
EU-25	136	125	147	24.2	35.4	51.4

Source: Carone (2005).

Yet the economic dependency ratio will improve between 2003-2025 and will then (rapidly) decrease in the following decades (Carone, 2005). The two projections are thus not consistent with each other, the first one about the old-age ratio being much more alarming. Moreover, while all of Europe is undergoing radical changes in the age composition of its population, many important differences still exist. The comparison between Old and New Member States already adds complexity to the

analysis (Carone, 2005: 2-3). The New Member States (EU-10) did not experience a ‘baby-boom’ after WWII like western Europe did. Fertility and death rates shows different trends as well. It was only in the 1980s that fertility started to decrease in the new countries, while life expectancy is lower than in western European countries and has decreased in the last 15 years of economic transition (Jepsen, 2005). As a result, recent data reveal differences between individual parts of the EU. In 2003, life expectancy at birth, for instance, was 76 years in the EU-15 and 70.5 years in the EU-10. Total fertility rates were 1.52 in EU-15 and 1.29 in EU-10, while the old-age dependency ratio was 25.2 in the former and 19.4 in the latter (Eurostat, 2005; Carone, 2005).

At the national level, the variation in each of the indicators is even bigger. In 2003, the proportion of the population aged 65 and over to the total population varied from 11.1% in Ireland to 19% in Italy. Life expectancy at birth varies as well: from 77.9 years in Sweden to 65.7 years in Latvia. In terms of fertility, while in Ireland it was 1.98 in 2003, it was 1.18 in the Czech Republic. Hence, even if the broader trends are similar, present and future variations persist (Table 3).

A further difference is related to welfare spending (and implicitly to social conditions) in the different parts of the EU. In 2003, the average public spending on social protection was about 28% of GDP in the EU-15 and 18% in EU-10 (Eurostat, 2005). That wide variation allows us to introduce a further dimension of the demographic issue. Social protection programmes are not the same across Europe. Their generosity, the level of protection, but also their methods of financing, institutional instruments and other traits differ from one country to another, as well as their interaction with employment and labour market policies. The impact of new demographic trends on each individual model will consequently vary. For the countries providing a lower degree of protection, therefore, ageing will have consequences on the financial sustainability of welfare programmes (like pensions and healthcare) but also on the adequacy and effectiveness of welfare programmes, benefits and services.

5. Impact on European welfare states: some lessons from the past

International organisations like the World Bank (1994) and the OECD (1996) have contributed hugely to the depiction of ageing as a massive challenge for economic growth and for the financial viability of welfare programmes in particular. Whereas a widespread consensus has emerged around the need to face that challenge, and consequently to reform economic, employment and social institutions, it seems interesting to propose here a somewhat less alarming viewpoint. We refer to the recent contribution by Castles (2004) on the future of the welfare state and the concrete (and hypothetical) source of its crisis.

The argument usually put forward by international organisations is that a “greying” population leads to increased budget constraints, with a direct impact on income maintenance expenditures. In particular, costs related to pensions but also health spending and care services are expected to grow rapidly.

Castles tells us a different story. He has adopted a peculiar approach: instead of using predictions based on economic models and assumptions, he has examined evidence from the past to assess what has been the impact of demographic trends on welfare and public spending in the three decades between 1965 and 1995. In that period, in fact, the elderly population (aged 65 and over) in OECD countries increased by about 4.3% points. Even if past growth was more limited than that expected in the near future, it represents a good case for assessing the true financial impact of ageing.

In actual fact, parallel to that growth in the elderly population, the average increase in public pensions spending was about 1.9% of GDP, equal to 16% of the change in total social spending. If we assume that the ratio of pensions spending change to population ageing will remain constant, in the period 2000-30 the average level of pensions in the OECD countries should go up of around 3.8% of GDP. Precisely 50% of the variation in public spending between 1965 and 1995 was due to ageing, while the remaining part was the effect of both coverage and generosity of public programmes. In other words, decisions about the type of institutions, their financing mechanisms and entitlements are

decisive as well as ageing. This seems to prove a strong relationship between population change and pensions spending, but it is a long way from demonstrating the extremely alarming effects of ageing in future decades (4).

Recent statistics about the future evolution of public pensions in the EU countries, moreover, confirm the ability of national policy-makers to introduce reforms and to contain future expenditure. Italy is a paradigmatic example of effective reforms. As Schludi (2005) puts it, OECD calculations at the end of the 1980s projected for that country a pensions spending increase up to 35% of GDP in 2040. However, more recent projections by the EPC (2003) show a top level of spending at 15.7% of GDP in 2030 with a subsequent decline. Reforms implemented in Italy in the last decade at least partly explain this less worrying scenario.

As proved by Castles (2004), apart from old-age programmes, other social schemes have revealed a lack of correspondence between population changes and welfare spending (that is the case of healthcare) or a weak positive correlation (in the case of services for the elderly). To sum up, data about total social spending suggests that the age effects were relatively modest, and inversely the room for manoeuvre and the incidence of policy decisions remained quite important.

Morely *et al.* (2005), have recently proposed some data consistent with that general conclusion. As far as pensions are concerned, success in raising the EU average level of employment according to the Lisbon objectives would reduce public outlays by about 30% in the period to 2050. At the same time, the raising of the effective retirement age by one year would decrease public pensions spending by a further 20% by 2050.

Conclusions

The Commission's Green Paper and the contributions summarised in this chapter all refer to future demographic trends as a challenge to the socio-economic institutions of Europe. The combined effect of low fertility, increased longevity, and the exit of the "baby-boom" generation

4 The same argument is put forward by De Swert (2005) in his recent work on the "forged" political messages on ageing.

from the labour market will put present institutions under stress. Yet the magnitude and intensity of the challenge is still open to question. While the Green Paper stresses the “demographic crisis” and the need for a wide-ranging renewal of the rules affecting the labour market, social protection programmes, education, training and several other policy fields, European social partners and civil society organisations have stressed different dimensions of the issue. For ETUC and FERPA, more than a demographic crisis we will face a new demographic cycle entailing both constraints and opportunities for our society. For both these organisations, population ageing is the result of the big success of the European Social Model, its institutions and values. They thus put at the top of the agenda the need to update social, labour and economic institutions rather than to radically revise (and reduce) their ambition. European trade unions and the European Older People’s Platform propose implementing the same lines of action in the near future: more and better jobs, a more inclusive labour market (especially for young, female and older workers), efficient training and education, as well as a more inclusive society for all. The multi-dimensionality of the challenge leads to the need for a comprehensive approach based on the interaction of policy domains and levels of governance.

As regards social protection programmes, all these actors agree on the parallel need for their rationalisation and improvement. Social expenditures are defined as an investment rather than a cost or a burden on economic competitiveness. AGE, for example, proposes raising the retirement age but also improving the social adequacy of public pension schemes, while FERPA regards elderly people as a resource to provide support and caring and to implement a more cohesive society. ETUC for its part clearly identifies a strategy to cope with future financial strains on old-age and healthcare systems: to diversify financial resources more (with a shift from labour to company profits) and to increase employment rates among the female and young population.

In the view of UNICE, by contrast, demographic changes are synonymous with a key source of constraints for public budgets and social protection schemes. European countries have to introduce

pension and healthcare reforms, especially to discourage early exit from the labour market, to support more flexible working arrangements in the interests of employees and employers as well, and to reinforce the financial sustainability of welfare states.

Recent works in the scientific literature also help to enrich the debate. As for the assessment of the ageing trend, some contributions prove that there is no unequivocal evidence of a massive financial crisis confronting welfare programmes. First of all, negative trends affecting the old-age dependency ratio will not be paralleled by the equivalent negative impact on the economic dependency ratio. At least in the medium term (until 2025) the ratio between the active and non-active population will improve rather than worsen. Secondly, common broader trends at the EU level mask big differences at both national and supra-national level (especially as concerns the divide between EU-15 and EU-10). Present and future challenges vary in many different respects: fertility, life expectancy, and especially the adequacy of social policies. In some countries, where social protection schemes are not well developed, the risk is to face huge problems of social cohesion rather than in respect of the financial viability of their welfare budget.

Moreover, if we look at the past evolution of welfare outlays (rather than making predictions about the future), population ageing trends did not have a dramatic impact on social spending. Data gathered on the period 1965-1995 proves that some of the most alarming projections may be exaggerated, while some reasons for scepticism arise. Demography did directly impact on pensions. Yet other social spending (e.g. healthcare) did not show such explicit effects. Any concern therefore has to be contextualised. Recent innovations introduced in some Member States (e.g. on pensions) should reinforce the awareness that managing the new demographic regime is possible and policy-makers can devise effective reforms.

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European cross-industry social dialogue in crisis

Introduction

We shall attempt in this chapter to analyse the main developments in the European cross-industry social dialogue in 2005. We begin by giving our verdict on the 2003-2005 work programme which the social partners set themselves in 2002, before examining the framework of actions on gender equality and the European Commission's consultation on company restructuring and European Works Councils. Next we turn to the launch of fresh negotiations on the subject of violence and harassment at work, along with the Commission consultation concerning the occupational health and safety directives, and also the joint submissions made by the social partners in 2005. Before closing the chapter we shall take a look at the social partners' new work programme for 2006-2008.

This overview of European social dialogue, seen from a perspective of the past few years and of European Union (EU) enlargement, reveals a number of what we regard as significant changes: firstly, there has been a gradual transformation in the role of some of the players in this dialogue, with in particular a tendency for the European Commission to take a back seat; secondly, the general political climate has been inauspicious for the development of Europe's social dimension.

1. Verdict on the 2003-2005 work programme

2005 was the final year of the first work programme jointly adopted by the social partners (for more details see *Social Developments in the European Union 2002 and following*). This programme covered the

years 2003-2005. Once the framework of actions on gender equality was adopted at the end of that period, in 2005, all the themes on the agenda had been addressed. Some items were still under discussion at the end of 2005.

**The 2003-2005 work programme:
state of play at 31 December 2005**

EMPLOYMENT	
Theme/calendar	Action taken
Employment Guidelines (2003-2005)	1 st joint report presented at the March 2004 Tripartite Social Summit 2 nd joint report finalised February 2005 and presented at the March 2005 Tripartite Social Summit
Lifelong learning (2003-2005)	1 st joint Follow up report 14/03/2003 2 nd joint Follow up report March 2004 3 rd joint Follow up report March 2005 Overall joint evaluation report adopted by Social Dialogue Committee January 2006
Stress at work (2003)	Seminar: 25-26/02/2003 Start negotiations: 18/09/2003 Framework Agreement signed by ETUC-UNICE/UEAPME-CEEP on 8/10/2004 ETUC Follow up project(start September 2005)
Gender equality (2003)	Seminar: 13-14/03/2003 Start negotiations: 01/12/2003 Framework of actions signed March 2005
Restructuring (2003)	Seminars: October 2002/ March and May 2003 EU social partners text "Orientations for reference in managing change and its social consequences" (finalised 16/10/2003); the ETUC Executive only took note of the document.

Disability (2003)	Joint Declaration of the EU Social Partners for the European Year of People with Disabilities (20/01/2003)
Young people (2003-2005)	Start early 2006
Racism (2004)	Start early 2006
Ageing workforce (2004)	First joint meeting on 14/09/2005
Harassment (2004-2005)	Issue also identified for eventual future negotiations in Framework agreement on Stress at work 1 st Commission consultation on “Violence at work” (including harassment in all its forms) launched 23/12/2004; joint EU social partner seminar on 12/ May 2005, negotiations start 7/2/2006
Telework (2003-2005)	Information exchanges on new developments at each Social Dialogue Committee-meeting; ETUC/ETUI-REHS regular and ongoing own monitoring report
Undeclared work (2005)	Joint Seminar 19/09/2005

ENLARGEMENT	
Theme/calendar	Action taken
Industrial relations (2003-2005)	Preparatory Project meeting: 9-10/12/2003; Start-off Conference: 9-10/01/2004 (Ljubljana); Several joint seminars were held in 5 new member states during 2004; next steps for 2005 are to expand the project to the other new member states and a second round of seminars in the “first group of countries” to evaluate the implementation of the adopted action plans
Social dialogue (2003-2005)	“Enlarged” SDC meetings: 29/01/2003, 01/10/2003, 05/03/2004, as from 05/2004 full member of each meeting

Restructuring (2003-2004)	Project outline adopted in autumn 2004; 6 seminars took place in 2005 (HU, CZ, CY, MT, LT & PL); 4 other national seminars + 2 thematic ones + final report envisaged before June 2006
Lifelong learning (seminar 2004/reporting 2005-)	Seminar May 2004
Implementation of legal acquis (2004)	Two case-study seminars on EWCs (22-23/10/2004; 27-28/10/2004); joint conclusions March 2005
EU social and employment policies after enlargement (2004-)	Forms now part of reporting on employment guidelines and LLL (see above * and **)

MOBILITY	
Theme/calendar	Action taken
Action plan on skills and mobility (2003-2005)	Seminar Commission and Social Partners (13/02/2003 – Brussels), no concrete follow up foreseen

Source: ETUC and ETUI-REHS (2006).

Overall, therefore, the European social partners completed the programme which they had set themselves in 2002. The main objective of that programme, it will be remembered, was to make them more autonomous of the European Commission's policy-making agenda when negotiating with their opposite numbers. The programme centred on the Lisbon agenda and on EU enlargement and, as such, represented a compromise between the views of the trade unions, who at that time wished the negotiations to be more binding (above all on restructuring, corporate social responsibility, data protection, etc.), and the views of the employers, who were more in favour of using the instruments provided by the open method of coordination (OMC).

Thus the years from 2003 to 2005 were devoted in the main to organising joint seminars, studies, reports and discussions. Negotiations as such were held on just three themes: the social consequences of restructuring (2003), stress at work (2004) and gender equality (2005).

What is more, only stress at work took the form of an “agreement” in the meaning of Article 139(2) of the EC Treaty. Since it was an autonomous agreement, the question of how its provisions are to be implemented and monitored remains somewhat open-ended, and it will not be possible to assess the quality of that implementation until 2007. As concerns the social consequences of restructuring, we should point out that the social partners, in a rather confused fashion, adopted a text (entitled “reference guidelines”) which is not legally binding and whose status and scope still remain far from clear. Furthermore, the ETUC Executive Committee merely took note of the existence of this document, by way of a “working basis”, considering that work on this topic was not yet complete. Finally, the third theme, namely gender equality (examined below), took the form of a framework of actions – modelled on the framework of actions for the lifelong development of competencies and qualifications – the instruments for which are borrowed from the open method of coordination: studying good practices; defining and disseminating priorities for joint action.

Assessment criteria

If the overall outcomes of the work programme were to be judged according to the binding nature of the texts adopted, its achievements could be considered rather meagre: not one framework agreement designed to be transposed into legislation, and just one autonomous framework agreement. Equally, if we look at this 2003-2005 programme in the broader context of cross-industry social dialogue since the entry into force of the Maastricht Treaty (¹), its outcomes appear even more meagre: not a single binding instrument has been adopted since the conclusion of the legally enforceable framework agreements in 1995 (parental leave), 1997 (part-time work) and 1999 (fixed-term contracts). All of these elements raise questions about the future of negotiated legislation in the European Union. Nevertheless, the question of whether or not the texts adopted have binding effect is not necessarily the only yardstick. European social dialogue should be judged, more specifically, by the verifiable changes which it makes to labour relations

¹ The Treaty which marked the start of contractual relations between the European social partners.

in the workplace. And in this sense, the impact of the new instruments used by the social partners (autonomous agreements and frameworks of actions) has yet to be assessed.

Moreover, an assessment of the recent outcomes of European social dialogue must also take account of other aspects: efforts made to involve the relevant parties in the new EU Member States; extensions to the range of themes covered by this dialogue; and a desire to integrate more closely the European and national levels of dialogue.

2. Framework of actions on gender equality

The cross-industry social partners (ETUC, UNICE/UEAPME and CEEP) adopted a framework of actions on gender equality on 22 March 2005. This joint document was the fruit of negotiations launched in April 2004 and concluded in February 2005 (ETUC, UNICE/UEAPME and CEEP, 2005a). During this period the social partners examined a number of case studies and identified various practical measures and tools worth inserting into their document. Gender equality may seem to be a surprising topic for collective bargaining, in that both the European Union and the Member States have already adopted a substantial body of legislation in this area. In the minds of the social partners, however, the problem lies in implementing this legislation. Therefore the purpose of the text adopted, in their opinion, is to add an extra layer of compulsion. To this end they drew on current practices in various Member States and companies, and selected examples on which they could base their activities throughout Europe.

Four priorities for action were defined by these means and scheduled to be put into practice over a five-year period: addressing gender roles, promoting women in decision-making, supporting work-life balance and tackling the gender pay gap. Identifying these priorities was no easy matter, however, since they and the context surrounding them were not viewed in the same way by both sides of industry. As concerns addressing gender roles, for example, the European Trade Union Confederation (ETUC) would have liked to place more emphasis on the question of gender segregation on the labour market, whereas the Union of Industrial and Employers' Confederations of Europe

(UNICE) wished to confine the talks to stereotypes. Another subject of divergence was labour flexibility in conjunction with the work-life balance. Whereas the ETUC sought to show that such flexibility needs to be negotiated in terms of both work organisation and working time, UNICE initially refused any explicit reference to such negotiations (and, more generally, to any other collective bargaining). But the principal difference of opinion related to the wage gap between men and women. This theme was a priority for the employee representatives, but the employers refused at first to include it in the framework of actions. More generally, the ETUC attempted in its negotiating stance to keep some coherence between the various priorities for action because, according to an internal document, “*tackling the wage gap also means tackling gender segregation, in other words solving the problem of the work-life balance*” (2).

Content of the framework of actions

The framework of actions takes the form of a reciprocal commitment by the social partners based on a joint analysis of priorities for action and of good practices. The range of actions contained in this text goes beyond what is strictly speaking the social partners’ field of responsibility and action: over and above the world of business, there are actions linked to the world of education, education authorities, parents, public authorities, nursery schools, social security systems, etc. Like the framework of actions on competencies and qualifications, the working method followed here borrows from the open method of coordination as applied to the social dialogue. The idea was to lay down “guidelines” at European level (the four priorities), adding to these the good practices identified as such, involving the various stakeholders in their implementation, in particular the national players (companies, public authorities, education authorities, etc.), and making provision for annual assessment reports possibly leading to an update of the priorities identified.

² ETUC Executive Committee, Brussels, 15-16 March 2005, agenda item 7b.

The framework of actions has the following structure:

1. Social partners' approach;
2. Challenges;
3. Priorities for action
 - a) addressing gender roles;
 - b) promoting women in decision-making;
 - c) supporting work-life balance;
 - d) tackling the gender pay gap;
4. Actions and follow-up.

Part 1 describes the common ground defined by the social partners for negotiation with respect to general principles. As stated above, the compromises reached between the European employers and employees can be found here.

Part 2, relating to challenges, draws a direct link with the Lisbon strategy. The main issues covered are numerical targets for the participation of women in the labour market, for employment rates and for narrowing the pay gap between men and women. The social partners assess the successes and failures so far in these areas, primarily on the basis of the Commission's 2004 report on gender equality. They conclude that the female workforce is a key resource that tends to be under-utilised or undervalued, that anti-discrimination legislation exists but in itself does not bring about gender equality, and lastly that the social partners are determined to live up to their own responsibilities. To this end they "*undertake to encourage social partners at all levels and in all EU countries to step up their involvement in devising and implementing integrated strategies in favour of occupational gender equality*", and to do so over the next five years (ETUC, UNICE/UEAPME and CEEP, 2005a: 4).

Part 3 contains the substantive part of the social partners' reciprocal commitment. Sixty or so practical measures are set out below the four above-mentioned headings. There are too many to list them all, so we shall confine ourselves to showing only the chapter headings (see Box).

Key elements of the framework of actions on gender equality (2005)

1. Addressing gender roles

- Non-gender biased education in schools, universities, non-stereotyped careers advice services;
- attract young women into technical and scientific professions;
- recruitment and retention of women and men in sectors and occupations where they are underrepresented better career opportunities for women;
- promote equal opportunities for all employees throughout the employment relationship;
- promoting entrepreneurship as a career option for both women and men;
- competence development for adults to allow evolve in their careers throughout life.

2. Promoting women in decision-making

- Competence-based gender neutral recruitment in enterprises;
- retaining women in enterprises, to avoid loss of competence;
- encouraging career development of both women and men;
- promoting female entrepreneurship;
- promoting women's role in the social dialogue at all levels.

3. Supporting work-life balance

- Flexible working arrangements that can be taken up on a voluntary basis by both women and men, designed in a way that does not undermine their long term participation and position on the labour market;
- more balanced take-up of possibilities to ease work-life balance;
- help increase the availability of accessible and affordable child care facilities of good quality and seeking innovative ways of providing essential private household or caring services.

4. Tackling the gender pay gap

- Informing about existing legislation on equal pay and giving guidance on how to help closing the gender pay gap at different levels;
- developing clear up to date statistics to enable social partners to analyse and understand the complex causes of pay differentials;
- ensuring that pay systems, are transparent and gender neutral and paying attention to the possible discriminatory effects of secondary elements of pay.

Source: ETUC, UNICE/UEAPME and CEEP (2005a).

Finally, Part 4 of the agreement concerns actions and follow-up. The text's signatories undertake to promote the framework of actions in the Member States at all appropriate levels, and to transmit the document to all relevant players at European and national levels, including EU sectoral social partners, EU and national public authorities etc. As with the framework of actions on competencies and qualifications, they will draw up – for four years (until 2009) – annual reports on the actions carried out in the Member States on the basis of the joint text. The European Social Dialogue Committee will then be entrusted with the preparation of the overall European report. After four annual reports, the European social partners will evaluate the impact on both companies and workers. Then, if necessary, they will update the priorities and/or assess whether or not additional action is required.

3. Company restructuring and European Works Councils

There was a revival of interest in the debate about restructuring in 2005, owing to external factors such as the opening of the textiles sector to competition, the forthcoming liberalisation of the sugar sector, and also the more political debate about outsourcing and what is sometimes referred to as Europe's "industrial decline". These factors led the European Commission to adopt, on 31 March 2005, a Communication regarding restructuring and employment. This public document likewise constitutes the second phase of its consultation of the social partners on company restructuring and European Works Councils, under Article 138 of the EC Treaty (CEC, 2005). The Commission carries out a 14-

page analysis of restructuring, describing it as a “*permanent reshaping of the fabric of production under the effect of numerous factors*” (CEC, 2005: 3) (single market, international economic liberalisation, technological innovation, etc.). It has no intention of attempting to curb this phenomenon, which it regards as indispensable to the survival and development of businesses. What is more important is to “*to accompany these changes in such a way as to ensure that their effects on employment and working conditions are as short-lived and limited as possible*” (CEC, 2005: 3). Some parts of the Commission’s analysis make for interesting reading, especially when it notes that the costs and benefits of market opening (the benefits are deemed to be greater than the costs, according to unspecified “empirical studies”) are not evenly distributed in time or space, and that there is a “mismatch” (CEC, 2005: 5) between the types of costs and benefits. For this reason, among others, the Commission proposes the development of a Community capacity to intervene in a crisis and the establishment of a growth adjustment fund.

While recalling that restructuring is largely managed at sub-European level (national, regional and local), the Commission considers that the EU can nonetheless play a part by stepping up its coordination of European policies (cohesion, industry, competition, etc.), and by reforming the European employment strategy as well as the Community’s financial instruments (e.g. the role of the Structural Funds at times of crisis). The Commission likewise invites the European social partners, above all at sectoral level, to do more to anticipate structural change and to become involved in informing and alerting public authorities at all levels. Furthermore, for the first time ever the Commission uses a (public) Communication to launch a second phase of social partner consultations, this time on restructuring and on European Works Councils.

As concerns company restructuring, readers will remember that the Commission launched an initial round of consultations in 2002 (see Degryse, 2002). That resulted in 2003 in the joint definition by the social partners of a set of “reference guidelines”, i.e. a document setting out major strategies and good practices for handling restructuring in a socially responsible manner (see Degryse, 2003). The status of that document was uncertain and it was never formally adopted by the

ETUC Executive Committee. Now the Commission wishes to embark on a new phase aiming “*to ensure that these guidelines are put into practice and developed further*” and, in particular, to “*encourage the adoption of these guidelines*” (CEC, 2005: 11).

With respect to European Works Councils, the Commission initiated the first consultation in 2004, to which the social partners responded (see Degryse, 2004). Following on from that, the two sides of industry held some joint seminars with a view to conducting case studies and establishing some principles or guidelines based on those studies. Here too, the Commission calls on the social partners to promote “*best practice in the way that European works councils operate, with a view to making them more effective, more especially as regards their role as agents for change*” (CEC, 2005: 11).

Reactions of the social partners

The ETUC Executive Committee reacted to the Communication and to the Commission’s twofold consultation at its meeting on 14-15 June 2005 (ETUC, 2005a). Whereas on the whole it is pleased to see a reopening of the debate about restructuring and its social consequences, the Committee is more critical as to the procedure. In its opinion, the Commission was not really “consulting” the social partners about a legislative initiative but merely encouraging them to adopt a joint text on restructuring and to promote best practices in respect of Works Councils. The consultations should be based on a “proposal”, pursuant to Article 138 of the EC Treaty, but the Commission had not made any suggestions for revising the directive – even though it admitted that only 45% of the companies covered by the directive have established a European Works Council. In this context the ETUC recalls its longstanding demand that the present European Works Councils Directive be revised ⁽³⁾.

UNICE, for its part, was glad to see restructuring recognised as a process of adaptation to change which should not be impeded or prevented. It does not support the proposed creation of a Community capacity to intervene in a crisis, and expresses strong reservations as to

³ The ETUC’s demands concerning the content of this revision are described in detail in Social Developments 2004.

the added value of a new forum on restructuring. With regard to the twofold consultation, the employers still believe, as they did in 2003 and 2004, that this is “*neither desirable, nor necessary*” (UNICE, 2005a). According to UNICE, the “reference guidelines” for managing the social consequences of restructuring are adequate in themselves, as are the “lessons learned on European Works Councils” (see below). In other words, Europe’s employers believe that they have done what is required of them on this front.

Lessons learned on European Works Councils

On 7 April 2005 the social partners adopted a joint document entitled “Lessons learned on European Works Councils”. For the record, the European Works Councils Directive, adopted by the Council in 1994 ⁽⁴⁾, made provision for its content to be revised after ten years. To this end, the Commission launched the first phase of social partner consultations in April 2004 (see Degryse, 2004). The two sides of industry decided to hold two joint seminars in September and October 2004 with a view to carrying out nine case studies. Around 750 transnational companies and groups have so far established a European Works Council or similar body, representing approximately 45% of all such companies and groups of companies, or 70% of the workers potentially affected. The “lessons learned” by the social partners from the case studies can be summarised as follows (extracts):

1. EWCs can help management and workers to build a corporate culture and adapt to change in fast-evolving transnational companies or groups, when changes concern the group’s strategy and affect sites in several countries;
2. The establishment of a climate of mutual trust between management and workers’ representatives in the EWC is important for a good functioning of this body;
3. The ability to understand complex issues discussed in the EWC determines the quality in communication. Investing in language as well as technical/content training helps to optimise the functioning of the EWC and to reduce overall functioning costs;

⁴ Directive 94/45/EC on the establishment of a European Works Council in Community-scale undertakings and Community-scale groups of undertakings (Council of the European Union, 1994). It aims in particular to improve information flows between the company’s workers and management, to enable the workforce to be consulted on cross-border matters affecting the group, and to develop entrepreneurship in transnational undertakings.

4. Finding ways of reconciling different national industrial relations practices, occupational traditions and addressing an increasingly diverse workforce is a constant challenge;
5. The case studies demonstrated that ensuring a real sense of ownership of the EWC by the whole workforce was a considerable challenge. However, the practical issues to be addressed varied depending on the structure of the company, the range of its activities, its geographical coverage and possible numeric dominance of the workforce of some countries, the existence of a restricted steering committee, the dissemination of EWC activities, the possible role of European sectoral federations or other external experts, etc.;
6. Some companies have anticipated the enlargement of their EWC and do not seem to have encountered insurmountable difficulties in identifying worker representatives from those countries;
7. A complexity encountered by both management and worker representatives is to organise meaningful information and/or consultation without creating undue delays and uncertainties. Tensions can also arise from the fact that even if some decisions on the strategy of the group are taken at European level, managing its social consequences remains local and governed by national rules;
8. Case studies underlined that the good functioning of EWCs is a learning and evolving process through fine tuning over the years (ETUC, UNICE/UEAPME and CEEP, 2005b).

4. Violence at work

The 2003-2005 work programme included the holding of a joint seminar on harassment at work with a view to perhaps reaching an autonomous agreement. When, on 17 January 2005, the Commission launched its first round of social partner consultations on this topic, the social partners informed the Commission of their intention to hold a seminar about it. The seminar took place in Brussels on 12 May 2005. The two sides of industry set out to examine together the ways in which the issue of violence at work is handled in national practice, and to decide whether or not there were sufficient grounds for tackling this problem at European level. A number of differences emerged from the very start of their discussions. Some countries have adopted legislation specifically on violence at work, whilst others deal with the matter by means of non-specific legal texts (criminal law, civil law, legislation on health and safety in the workplace); others still have collective agreements on this subject

and/or regulations and codes of conduct. One subject of debate was even how to define violence at work. Together, the two sides identified three categories: physical violence, mobbing and/or bullying, and sexual harassment. These different forms of violence may originate within the company (from colleagues or superiors) or outside of it (customers, visitors, etc.). The victims most commonly belong to specific groups: women, young workers, staff in uniform and immigrants. Certain sectors of the economy are more at risk than others: hotel and catering, transport, public administration and defence.

Reactions of the social partners

It seems obvious to the ETUC that joint action at European level can complement what is done nationally. Given the complexity of this matter, the trade union confederation argues strongly for its own definition of “violence” and for the need to find specific solutions for each category. It believes that violence in the workplace is linked to aspects of work organisation, the working environment and the type of work done. The ETUC sets great store by preventive measures to identify the primary causes of violence, and wishes to see the issue of violence at work linked to legislation not only on health and safety but also on combating discrimination.

The employers, for their part, see no point in any specific European legislation being drafted in this field. They believe that the European and the Member States’ legal systems are already sufficiently extensive and diverse to be able to cope, either directly or indirectly, with the issue of violence at work. Another major difference of approach between the employers and employees is that, according to the former, violence at work pertains not to health and safety but to human resource management: an area over which the EU has no competence. They nevertheless think that it might be useful to have talks with the trade unions about the different forms and sources of violence, and how commonly it occurs, but also about false accusations and how to deal with them (after all, this was one of the themes included in the 2003-2005 work programme).

UNICE and the ETUC therefore decided to ask their respective decision-making bodies to grant them a mandate so as to embark on negotiations before the end of 2005 with a view to reaching an agreement on the basis

of Article 139(2) of the Treaty (a framework agreement for transposition into legislation or an autonomous agreement). The ETUC mandate was approved at the Executive Committee meeting on 19-20 October 2005. The negotiations are scheduled to begin in 2006.

5. Consultation on the health and safety directives

On 1 April 2005 the Commission launched a first phase of consultation of the social partners on simplification of the European legislation concerning health and safety at work. It asked the following questions:

- [Should there be] a single report for all existing directives in the field of health and safety at work, or specific reports for each directive, but subject to the same periodicity?
- How often should national reports to the Commission be prepared and submitted – every five years or every six years?
- Should this exercise cover all existing health and safety at work directives, or should it be confined to those which already prescribe an obligation to report to the Commission?
- What measures should be taken to ensure that the social partners contribute to uniform and equivalent national reports?

Was this “just” a technical exercise aimed at streamlining the output of European documents, or was it an attempt to relax the constraints associated with the provisions of these directives, in keeping with the “better regulation” initiative of the Barroso Commission? The debate immediately came to revolve around this question, perceived differently by employers and employees.

Reactions of the social partners

Whilst UNICE backs the Commission’s proposal to align the frequency of follow-up reporting, it cannot accept the idea of harmonising the social partners’ reports. The employers stress in particular that “*what is mostly needed is a genuine simplification of the complex regulatory environment for companies, alongside a true commitment to better regulation*”⁵. The ETUC, on

⁵ Unice@news, July 2005, page 9.

the other hand, favours the idea of streamlining the reports, which “*is the result of a very different line of thinking to that expressed in the majority of calls for legislative simplification or for better regulation*” (ETUC, 2005b: 2). The trade union confederation denounces the fact that health and safety measures are explicitly regarded as burdens and costs for businesses; in its own opinion the reports resulting from implementation of the directives are part of a prevention strategy which necessitates regular and detailed monitoring of the situation in Europe. Moreover, the ETUC fears that, in the name of fighting bureaucracy and red-tape, the Commission may take issue with certain Member States for going beyond the minimum provisions enshrined in the directives. The ETUC likewise calls on the Commission to step up the resources earmarked for drafting its own synthesis reports on the application of the health and safety directives: “*so far huge backlogs have built up, and some of the reports drawn up have only provided a very superficial overview*” (ETUC, 2005b: 4). The Commission is also urged to refer to the reports on pregnant workers, and on the health and safety of temporary workers and workers on fixed-term contracts.

6. Other joint activities

Among the other activities carried out jointly by the social partners in 2005 it is worth mentioning:

- the joint declaration on the mid-term review of the Lisbon strategy (15 March 2005), which mainly contains a joint interpretation of the concept of “competitiveness in a sound macro-economic environment”: innovation, employability, social protection, environmental policies, a supportive public environment and sound macro-economic policies (ETUC, UNICE/UEAPME and CEEP, 2005c);
- the adoption of the third follow-up report on the Framework of actions for the lifelong development of competencies and qualifications (22 March 2005), whose main innovation is the inclusion of initiatives in this field taken by social partners in the new Member States (ETUC, UNICE/UEAPME and CEEP, 2005d);

- the adoption of the second joint report on social partner actions for the implementation of the employment guidelines in Member States (22 March 2005), which describes the key actions of the social partners in four areas (increasing adaptability of workers and enterprises, activation policies under the heading “making work a real option for all”, investing in human capital, and better governance) (ETUC, UNICE/UEAPME and CEEP, 2005e);
- the joint contribution on the EU youth initiative (22 March 2005), in which the social partners stress the importance of an “intergenerational approach” to labour markets, i.e. to develop active ageing strategies while at the same time helping young people to enter the labour market (ETUC, UNICE/UEAPME and CEEP, 2005f).

7. The 2006-2008 work programme

Before concluding this chapter, we should just mention the European social partners’ second work programme for 2006-2008. This programme was not finalised until the end of January 2006, and it needs to be adopted formally ahead of the Tripartite Social Summit on 23 March 2006.

At its meeting on 14-15 June 2005, the ETUC Executive Committee adopted proposals for a programme stretching from 2006 to 2010, pointing out from the start that “*the period covered in this proposed joint work programme (...) is longer than the current one (ed.: 2003-2005). This is being proposed on the basis that the employers’ side agrees that this programme is flexible and non-exhaustive. Should this not be the case, we will revert to a shorter time period*” (ETUC, 2005c: 1). Over and above the initiatives from the 2003-2005 not yet fully implemented (continuing work on the ageing workforce, young people, racism, harassment and violence, undeclared work and restructuring), the ETUC Executive Committee proposed launching the following new initiatives:

- enhancing the quality of the European social dialogue, which mainly entails: clarification of social dialogue instruments; interpretation and monitoring instruments; mediation/conciliation/arbitration systems, including access of EU social partners to the

European Court of Justice; transnational consultation and collective bargaining processes;

- annual reporting, including the idea of drawing up one overall report covering all employment-related subjects handled by the social partners (employment guidelines, lifelong learning, gender equality, etc.), as well as reports on the implementation of framework agreements (telework, stress at work, harassment/violence);
- evaluation of former framework agreements (parental leave, part-time work and fixed-term work)
- joint social partner contributions to a series of new themes, including: flexi-security, innovation, worker mobility, equality, combating exclusion and poverty, follow-up to the 2003 joint social partner declaration on the European Day of Disabled People.

In addition, the Executive Committee wonders whether or not to include the following themes in the new work programme: sustainable development, trade union rights (especially in SMEs), “atypical work”, protection of employee data, the external dimension of employment, social policy and decent work, financial participation of workers and, lastly, supplementary pensions.

An initial “joint draft” of a social partner work programme for the period 2006-2008 was drawn up in November 2005 and submitted to the Social Dialogue Committee at its meeting on 8 November 2005, but the text left a good deal to be desired. It became immediately obvious – from the period covered – that the ETUC’s proposal had not been endorsed by the employers. This two-page draft consisted in the main of:

- joint recommendations to be forwarded to the European institutions concerning macro-economic and labour market policies, demographic change and undeclared work;
- a framework of actions on employment, including flexi-security, productivity and innovation, mobility and migration, life-long learning, active ageing and the integration of young people;

- the updating of studies on economic and social change in the enlarged Europe, particularly with the aim of rethinking the reference guidelines on managing change and its social consequences;
- the continuation of actions already underway: assistance for the development of social dialogue in the new Member States, follow-up reports on agreements already negotiated, and the development of a “mutual understanding” of the new instruments of European social dialogue.

This draft was less substantial than the 2003-2005 programme. It held out no hope of any new framework agreements, the only reciprocal commitment being to prepare a framework of actions on employment. The document had very limited aspirations and in essence took the stance that the purpose of social dialogue was to lobby the European institutions and make recommendations to them, rather than to serve as a forum for negotiating reciprocal commitments. The programme also focused more on what had already been achieved – evaluating the scope of the joint texts previously adopted – than on new themes. These weaknesses made the draft text unacceptable to the trade union side, which explains why, at the end of 2005, there was still no work programme covering the period from 2005 onwards.

The compromise eventually reached in January 2006 opens the door to negotiations on a new autonomous framework agreement, relating either to the integration of disadvantaged groups on the labour market or to lifelong education and training. We shall look in more detail at the content of this work programme in the next edition of *Social Developments in the European Union*.

Conclusions

The title of this chapter draws attention to the fact that the European social dialogue is in a state of crisis. This judgment may without doubt appear overly pessimistic, given the significant progress made over the past few years: increased autonomy of the social partners, their desire to devise multi-annual work programmes, a gradual broadening of social dialogue activities and a diversification of the instruments in use – all of this despite a difficult context (EU enlargement, economic stagnation and persistently high unemployment).

There has indeed been a proliferation of initiatives and an assertion of autonomy. Nevertheless, it is justifiable to ponder on the current weaknesses of the European cross-industry social dialogue in terms of the quality of its outcomes and the instruments used. Since the entry into force of the Maastricht Treaty, the social partners have been partly responsible for devising a common bedrock of social regulations. After an initial, relatively promising start-up phase (the framework agreements on parental leave, fixed-term employment and part-time work), the wheels of the social dialogue seem gradually to have ground to a halt, on account of the increasingly restrictive attitude of the employers. On the one hand, the subject matter and content of the texts adopted reflect a less ambitious approach, with the exception of the autonomous agreement on telework – although the practical implementation of that agreement has yet to be assessed, in 2006. On the other hand, many questions can be asked about the true import of the joint documents drawn up in recent years.

The prime purpose of EU social policy is to define a common bedrock of regulations aimed at preventing competitive mechanisms within the internal market from eroding working conditions, which would ultimately mean that not companies but Member States were in competition with one another. If this is the case, and if social dialogue forms part of this vision of social policy, then it might be expected to produce texts which are mandatory and apply *erga omnes*. Yet, owing to pressure from the employers, it would appear that social dialogue is now headed more in the direction of defining standards which are not legally binding and are enforced differently from country to country, and even within one and the same country.

How can this state of affairs be explained? Two factors may well be responsible: first, a change in the role of the protagonists (and hence in the alliances between them); second, and more generally, a certain crisis of legitimacy in the European Union. The two factors are without doubt interconnected.

Concerning the role of the protagonists, one illustration of our case would be the issue of the social consequences of restructuring and European Works Councils. As we have seen, the European Commission has not exercised the role of initiative expected of it under

the Treaties. Indeed, the Treaties stipulate that the Commission must play an active part in European social dialogue: it must put forward proposals for action in the social policy field and consult the social partners on the thrust and content of these proposals, while allowing them the possibility of negotiating the content themselves. That has not been the case in this instance. Rather than signalling a Community initiative, the Commission has simply said that it will “*follow the work of the social partners and will look at the progress made between now and the 2006 Tripartite Social Summit*” (CEC, 2005: 11). Many observers have long emphasised the importance of the “shadow of the law” (see in particular Dølvik, 1999) in advancing the social dialogue and especially in energising the employers, whose reluctance to engage in social dialogue can only be overcome by using the threat of legislation. This shadow is now gradually disappearing, with two consequences: the ETUC is losing its traditional ally, the European Commission; and UNICE, freed from the threat of legislation, can take refuge in a social dialogue which is more or less confined to going over old ground. As for the Council of the EU, even though it asserts that “*the social partners share responsibility for finding a balance between flexibility and security in employment and making it possible for enterprises to be adaptable*” (Council of the European Union, 2002: 7), it is evidently incapable of stepping in when the two sides of industry fail to reach agreement (on temporary agency work, the organisation of working time, etc.). With the European Commission in retreat, the employers holding back and the Council paralysed, the dynamic envisaged in the Social Policy Agreement of the Maastricht Treaty has been seriously undermined. The ETUC, by contrast, argues in favour of a fully-fledged system of European collective bargaining capable of regulating European integration from a social policy perspective.

With respect to the European Union’s crisis of legitimacy, the most obvious manifestation of which in 2005 was the French and then the Dutch rejection of the draft constitutional Treaty, it engenders a political climate which is less and less propitious for the laying down of standards – including social standards. “Excessive regulation” seems to be under fire from all sides nowadays, even within the Commission, which launched its “better regulation” initiative in September 2005. Streamlining regulation may well be useful, but this initiative clumsily

fuels criticism of European bureaucracy. The danger, as pointed out above, is that measures aimed for example at ensuring employees' health and safety in the workplace may ultimately be regarded as burdens and costs weighing down on companies.

This combination of changes in the role of the protagonists and a crisis of legitimacy make for a difficult climate. If the European social dialogue is to remain a key instrument of European integration and its social regulation, it must without any doubt rediscover the spirit of the Maastricht Social Policy Agreement.

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The European Court of Justice and social policy case law in the EU: an overview

The Court of Justice of the European Union (CJEC) is often considered to be the driving force behind European integration. The Treaties establishing the European Union bestow on it a crucial role in ensuring that they function properly. The Court is the guarantor of institutional equilibrium: on the one hand the arbiter between Member States and the European Union, and on the other between the institutions themselves. From the outset, the Court has remained true to its vocation and has unfailingly charted a pro-European course towards European integration; hence the case law shaping the development of Community law in areas such as the relationship between Community law and national law, fundamental rights in the Community legal order, the functioning of the single market, and so on. It also plays an important role in social policy. Frequently consulted by national courts for preliminary rulings, it has had the opportunity, through its rulings, of defining fundamental concepts such as equal pay for men and women, the place of family benefits in a co-ordinated framework of social security systems, the concept of transfer of undertakings, employers' insolvency, working hours, etc. 2005 has been no exception in terms of the CJEC's activities. This chapter seeks to give an overview of recent case law, albeit based on a fairly small number of rulings. The three-part structure common to previous editions has been retained, but there is greater focus on equal treatment, in order to give the reader an overview of the principle prohibiting discrimination on grounds of age and nationality.

1. The principles of equal treatment and non-discrimination

The principles of equal treatment and non-discrimination are at the heart of the European social model. They are one of the key elements of the fundamental rights and values which are the cornerstone of today's Union. Great progress has been made over a short period since the Member States agreed on the need for concerted action at European level to combat discrimination on grounds of racial or ethnic origin, religious or other convictions, age, disability and sexual orientation. The action taken in this area has been based on the Union's experience in combating gender-based discrimination (CEC, 2004a).

1.1 Equal pay for men and women: the *Vergani* case

The Court of Justice has played a central role in developing the principle of equal treatment of men and women. It ruled that Article 119 of the Treaty of Rome (now Article 141 EC) on equal pay has direct effect, affirming that this article was part of the social objectives of the Community. It has given rulings which have helped to combat discrimination against women, particularly in the area of indirect discrimination, which is defined as the application of a criterion which is neutral in appearance but in fact affects more members of one gender. It defends genuine equality between men and women, thus excluding protective measures which cannot be justified by objective differences between men and women (Joannin, 2004). Despite the legal arsenal it has established both at the heart of the Union and in the Member States, and well-established Community case law, there are referrals to the Court each year for rulings on the parameters of this principle. In this context, we shall look at the *Vergani* case, decided earlier this year by the Court.

Italian law ⁽¹⁾ provides for a system of early retirement particularly for the benefit of employees of firms which have been declared to be in crisis. Women are entitled to seek early retirement as of age 50, whilst the threshold is 55 for men. As a voluntary redundancy incentive, the law provides for tax concessions in respect of sums paid by the

¹ Article 17(4)(a) of decree no. 917 of the President of the Republic, of 22 December 1986, as amended by decree law no. 314 of 2 September 1997.

employer on cessation of the employment relationship. Taxation is at a rate reduced by half that applicable upon retirement at the normal age. Mr Vergani ⁽²⁾, aged 51, had ceased employment, received the payment to which he was entitled, and found that he was being denied the tax concession in question to which a woman in his position would have been entitled. He brought proceedings before the *Commissione tributaria provinciale di Novara*, challenging this decision of the tax authorities, which refused him the concessionary tax rate in respect of personal income tax. The court decided to stay the proceedings and refer to the CJEC for a preliminary ruling the question as to whether Article 141 EC and Directive 76/207/EEC (Council of the European Communities, 1976) preclude the provision of a voluntary redundancy incentive consisting of taxation of sums paid in connection with the cessation of employment relationships at a rate reduced by one half, for workers over the age of 50 in the case of women, and the age of 55 in the case of men.

The Court first of all considers whether the grant of an age-related tax concession, in respect of the taxation of a voluntary redundancy payment, is covered by Article 141 EC or Directive 76/207. The concept of pay, referred to in Article 141 EC, comprises any consideration, whether in cash or in kind, whether immediate or future, provided that the worker receives it, albeit indirectly, in respect of his employment from his employer ⁽³⁾. A tax concession is not being paid by the employer and therefore is not a consideration within the terms of Article 141. The Court then affirms that under Article 5(1) of Directive 76/207, application of the principle of equal treatment with regard to working conditions, including the conditions governing dismissal, means that men and women are to be guaranteed the same conditions without discrimination on grounds of gender. This Article also applies to the conditions governing dismissal which obtain in those States. The term “dismissal” must be widely construed, so as to include termination of the employment relationship between an employee and his employer,

² CJEC, Case C-207/04, *Vergani*, 21 July 2005, not yet published.

³ Judgment of 17 May 1990, Case C-262/88, *Barber*, ECR I-1889, point 12, and of 9 February 1999, Case C-167/97, *Seymour-Smith and Perez*, ECR I-623, point 23.

even as part of a voluntary redundancy scheme. A tax rule determined by reference to a worker's age, constitutes a condition for dismissal within the meaning of Article 5(1) of Directive 76/207. A difference in treatment resulting from the taxation, at a rate reduced by half, of sums paid on the cessation of the employment relationship, which applies to workers over 50 in the case of women and 55 in the case of men, constitutes unequal treatment on grounds of a worker's gender.

Is such a difference in treatment covered by the derogation provided for in Article 7(1)(a) of Directive 79/7/EEC (Council of the European Communities, 1979), by virtue of which the Directive is without prejudice to the right of Member States to exclude from its scope the determination of pensionable age, for the purposes of granting old-age and retirement pensions and the possible consequences thereof for other benefits? This exception to the ban on discrimination on grounds of gender must be strictly interpreted. It can only apply to the determination of pensionable age for the purposes of granting old-age and retirement pensions and the possible consequences thereof for other social security benefits. It does not therefore apply to a tax concession which is not a social security benefit. The difference in treatment therefore constitutes direct discrimination on grounds of sex, contrary to Directive 76/207 (4).

1.2 The principle of non-discrimination on grounds of age and nationality: the cases of *Mangold* and *Ionannidis*

In the *Mangold* case, the CJEC deals with the question of differences in treatment based on age (5). The principle of prohibiting discrimination on grounds of age is a general principle of Community law. Directive

4 We refer the interested reader to the following judgments: the case of *McKenna* deals with equal treatment in the context of illness occurring prior to maternity leave and pregnancy-related illness, CJEC Case 191/03, *McKenna*, 8 September 2005; not yet published. In the case of *Nikoloudi* the Court deals with positive action in the context of part-time work. The judgment in *Mayer* covers the inclusion of periods of maternity leave for the purpose of the calculation of rights to an insurance annuity, CJEC Case C-356/03, *Mayer* ECR I-295, 13 January 2005; CJEC Case C-196/02, *Nikoloudi*, 10 March 2005, ECR I-1789.

5 CJEC, Case C-144/04, *Mangold*, 22 November 2005, not yet published

2000/78/CE (Council of the European Union, 2000) seeks to lay down a general framework for combating certain forms of discrimination in respect of work and employment, particularly discrimination on the grounds of age. Differences in treatment directly based on age are in principle prohibited by Community law. However, the Directive does state that Member States may provide that differences of treatment on grounds of age shall not constitute discrimination, if, within the context of national law, they are objectively and reasonably justified by a legitimate aim, including legitimate employment policy and labour market objectives, and if the means of achieving that aim are appropriate and necessary.

The *Arbeitsgericht München* referred several questions to the Court for a preliminary ruling on the interpretation of Directive 2000/78, in the context of a dispute regarding a German law on part-time work and fixed-term contracts ⁽⁶⁾. This law authorises the conclusion of a fixed-term contract without restriction up until 31 December 2006, if a worker has reached the age of 52, except in the case where there is a close connection with a previous employment contract. The case concerns *Werner Mangold*, aged 56, who had been offered a seven-month employment contract with a lawyer. He was unable to negotiate on the duration of the contract because of the law in force, but subsequently challenged it before the courts.

The Court of Justice recognises that the purpose of the legislation is plainly to promote the vocational integration of unemployed older workers, insofar as they encounter considerable difficulties in finding work. Such an objective therefore in principle justifies, objectively and reasonably, a difference of treatment on grounds of age. However a national regulation such as that contained in the TzBfG goes beyond what is appropriate and necessary to the attainment of the legitimate objective. The Member States unarguably enjoy broad discretion in their choice of measures conducive to attaining their objectives in the field of social and employment policy. However, the view of the Court is that the application of national legislation such as that at issue here, leads to

⁶ *Gesetz über Teilzeitarbeit und befristete Arbeitsverträge und zur Änderung und Aufhebung arbeitsrechtlicher Bestimmungen* (TzBfG).

a situation in which all workers who have reached the age of 52 may lawfully be offered indefinitely renewable fixed-term contracts of employment until the age at which they may claim their entitlement to a retirement pension. This applies without distinction, irrespective of whether they were unemployed before the contract was concluded and whatever the duration of any period of unemployment. This substantial category of workers, defined solely on the basis of age, is thus in danger, during a substantial part of its members' working life, of being excluded from the benefit of stable employment which, in fact, constitutes a major element in the protection of workers. Moreover, it has not been shown that fixing an age threshold as such, regardless of any other consideration linked to the structure of the labour market in question, or the personal situation of the person concerned, is objectively necessary to the attainment of the objective, namely the vocational integration of unemployed older workers.

The Court, in this judgment, comments on the interpretation of Directive 2000/78 and the effect thereof on national law, even though the period allowed for the transposition of the Directive into national law had not expired when the fixed-term contract in question was concluded. It is the view of the Court that these circumstances are not sufficient to call into question the finding that the German legislation is without justification under Article 6 of the Directive. The Court refers to the judgement in the *Wallonie* (7) case in 1997 when it held that Member States to which a Directive is addressed must refrain, during the period laid down therein for its implementation, from adopting measures liable seriously to compromise the result prescribed. This view applies to provisions of national law adopted after a Directive comes into force, irrespective of whether they pertain to its transposition. Directive 2000/78 implies that the Member States must progressively take the measures necessary to ensure the approximation of their national legislation in line with the provisions of the Directive. This obligation would be rendered ineffective if, during the period for implementation of the Directive, Member States were able to take measures inconsistent with the objectives of that Directive.

⁷ CJEC, Case C-129/96, *Wallonie*, ECR I-7411, 18 December 1997.

The exception provided for by German legislation expires on 31 December 2006, essentially at the same time as the period for transposition (2 December 2006). However, workers subject to the system introduced in Germany during the period for transposition will continue to be subject to this exception even after the expiry of the period in 2006. A worker in this category is thus in danger, during a substantial part of his or her working life, of being permanently excluded from the benefit of stable employment, irrespective of the fact that the age restriction ceases to apply in 2006. For these reasons, the Court of Justice has concluded that Directive 2000/78 precludes the application of national regulations which authorise the conclusion of fixed-term employment contracts without restriction once the worker has reached the age of 52, even if the period for transposition of the Directive has not expired. The judgment in *Mangold* illustrates the Court's commitment to ensuring effective protection of individuals against violations of the principle prohibiting age-related discrimination enshrined in Directive 2000/78, which was adopted pursuant to Article 13 EC. This judgment also indicates a degree of flexibility in the Court's approach to two issues pertaining to the application of Community Directives, namely the effect of a Directive prior to the expiry of the period for transposition, and the right to rely on a Directive in a dispute between private parties when it has not been transposed, or has been incorrectly transposed. In recognising that a Directive is directly effective in a dispute between individuals prior to transposition, the Court has gone a step further than it did in the judgment in the *Wallonie* case which only involved one Member State. It would appear that henceforth, in a dispute between individual parties, national jurisdictions are obliged to set aside national provisions which run counter to a Community Directive, even prior to the expiry of the period for transposition.

The *Ionannidis* case involves a Belgian regulation (the Royal Decree of 25 November 1991 on unemployment benefit), which provides unemployment benefit in the form of an "*allocation d'attente*" or jobseeker's allowance to young people who have just completed their studies and are seeking their first job. In order to be eligible for the allowance, a young person who has completed a course of study or training in another Member State of the European Union must be able to prove

that the course of study or training course was of a level equivalent to one available at an institution run, funded or recognised by one of the Communities in Belgium. At the time of applying, he or she must also be a dependent child of migrant workers residing in Belgium. Having completed his secondary schooling in Greece, Mr Ionannidis, of Greek nationality, arrived in Belgium in 1994. His Greek secondary leaving certificate was recognised as equivalent to an authenticated higher leaving certificate which in Belgium gives access to the shorter type of higher education courses. After three years of study, he obtained a graduate diploma in physiotherapy. He also took a grant-funded course in France on rehabilitation of the vestibular system. On his return to Belgium in 2001, he applied to the National Employment Office (ONEM) for a jobseeker's allowance. His application was rejected on the grounds that he had not completed his secondary education in an institution organised, funded or recognised by one of the three Communities in Belgium. The *Cour du Travail* (Labour Court) in Liège referred to the CJEC the question as to whether European Community law precluded a Member State from refusing to pay a jobseeker's allowance to a national of another Member State seeking their first job, for the sole reason that he or she had completed their secondary studies in another Member State.

According to the Court, nationals of a Member State seeking a job in another Member State fall within the scope of the EC Treaty and benefit from equal treatment. The principle of equal treatment prohibits ostensible discrimination on grounds of nationality and any form of covert discrimination which through the application of other criteria, leads to the same result. The Belgian regulation introduces a difference in treatment between citizens who have completed their secondary education in Belgium as opposed to another Member State: the former alone are entitled to a jobseeker's allowance. This condition is likely to be more easily met by nationals, and therefore threatens to penalise nationals of other Member States. Such a distinction could only be justified if it were based on objective criteria, independent of nationality and proportionate to a legitimate objective in national law. It is legitimate for the national legislator to seek to ensure that there is a real connection between an applicant for a benefit and the geographical labour market. Nevertheless, the condition based solely on the place

where the secondary leaving certificate was obtained is too general and too exclusive. It gives undue weight to a factor which is not necessarily representative of the real and effective connection between the applicant for the benefit and the geographical labour market, to the exclusion of any other more representative factor, and goes beyond what is necessary to reach the desired objective. The fact that Mr Ionannidis' parents were not migrants resident in Belgium could not be grounds for refusing the application. Nor could this condition be justified by the aim of ensuring a genuine connection between the applicant and the geographical labour market, since it would serve only to exclude someone who had completed their secondary studies in another Member State, had obtained a diploma there, was able to demonstrate a genuine connection with the labour market of that State, but was not a dependent of migrant workers residing in that State ⁽⁸⁾.

2. Social security and migrant workers

Social security for migrant workers is a necessary and inevitable corollary of the principle of freedom of movement for workers, which is one of the cornerstones of the European Union. Regulation No. 1408/71/EEC, adopted on 14 June 1971, effectively codified the law in this area, incorporating new information, the benefit of experience and CJEC case law. The implementing provisions are contained in Regulation No. 574/72/EEC of 21 March 1972. These regulations do not seek to establish an independent social security system based on harmonisation of the very disparate systems in force in the Member States, but rather to establish mechanisms coordinating these national systems. The Court of Justice is frequently consulted for a preliminary ruling on the scope and application of these provisions.

⁸ The interested reader may also wish to refer to the case of *Bidar*, in which the Court held that student maintenance grants also fell within the scope of the EC Treaty in terms of prohibiting discrimination on grounds of nationality, CJEC, Case C-209/03, *Bidar*, ECR I-2119, 15 March 2005.

2.1 The reimbursement of health care costs incurred in a third country: the case of *Keller*⁹⁾

Ms Keller, a German national resident in Spain, applied to the Spanish body responsible (Insalud) for an E111 form valid for one month for the purposes of travelling to Germany. During her stay there, she was diagnosed with a malignant tumour likely to prove fatal at any moment. She applied to Insalud for an E112 form in order to be able to continue her medical treatment in Germany. The period of validity of this form was extended on several occasions. Following an in-depth analysis of possible treatments, the German medics decided to transfer Ms Keller to the University Clinic in Zürich, which was the only hospital where there was a realistic chance that the operation she needed could be carried out successfully. Ms Keller paid the costs of her medical care in Zürich herself, and subsequently applied to Insalud for reimbursement. Her application was refused, so she initiated court proceedings. The national Court sought a ruling from the Court of Justice on the interpretation of the 1971 Regulation (Council of the European Communities, 1971) in respect of the possibility of reimbursement of hospital costs incurred in a third country. The Court firstly recalls that one of the purposes of the Directive is to facilitate freedom of movement of insured persons who require medical care during a stay in another Member State, or who have been authorised to receive care in another Member State.

In this context, Forms E111 and E112 are intended to assure the institution of the Member State of stay, and the doctors authorised by that institution, that the holders of those forms are entitled to receive in that Member State, during the period specified in the form, treatment whose cost will be borne by the Member State of which he or she is a national. The Court recalls that the doctors established in the Member State of stay are clearly best placed to assess the treatment required by the insured. During the period of validity of the certificate, the institution of the Member State of which the insured is a national relies on the institution of the Member State in which it has allowed the insured person to stay for medical purposes, and on the doctors

⁹⁾ CJEC, Case C-145/03, *Keller*, ECR I-2529, 12 April 2005.

authorised by the latter institution, as offering a guarantee of professionalism equivalent to those of doctors established in its own territory. That institution is bound by the findings as regards the need for urgent, vitally necessary treatment made by doctors authorised by the institution of the Member State of stay, and by the decision of those doctors to transfer the patient to another State for urgent medical treatment, even if that State is not a member of the European Union. The competent institution is not entitled to require the person concerned to return to the competent Member State in order to undergo a medical examination there, nor to have him examined in the Member State of stay, nor to make the above findings and decisions subject to its approval. As to the issue of costs incurred in respect of medical treatment received in a third country following a decision by doctors to transfer a patient, the Court recalls that the governing principle is that the cost of the treatment is initially borne by the institution of the Member State of stay, in accordance with its own legislation, and that it is then for the competent institution of the Member State of residence to reimburse the institution of the Member State of stay. Given that the cost of medical treatment received in Switzerland by Ms Keller had not been borne by the German medical insurance company, but it is established that Ms Keller was entitled to have the cost paid, and that the treatment is among the benefits provided for by Spanish social security legislation, the Court ruled that it was for the competent Spanish social security body to reimburse the cost of that treatment directly to Ms Keller's heirs.

2.2 The concept of family benefits: the case of *Dodl & Oberhollenzer*⁽¹⁰⁾

In order not to deter workers who are nationals of the Member States from exercising their right to freedom of movement, Regulation No. 1408/71 guarantees them equal treatment in the context of differing national legislation and social security benefits, irrespective of their place of employment or residence. The general rule is that the Member State in which the worker is employed is responsible for the payment of family benefits to a salaried worker, even if he or she and their family

¹⁰ CJEC, Case C-543/03, *Dodl & Oberhollenzer*, 7 June 2005, not yet published.

are resident in another Member State. However, in the event that benefit entitlements from the State of employment might overlap with those of the State of residence, there are rules to avoid overpayment of family benefits. Ms Dodl and Ms Oberhollenzer, both Austrian nationals, work in Austria but live in Germany, with their husband and partner respectively, both of whom have German nationality and work full-time in Germany. Following the birth of their children, Ms Dodl and Ms Oberhollenzer took unpaid parental leave for the duration of which their contract of employment was suspended. In their capacity as fathers, their husband and partner respectively received family allowance in Germany, which was equivalent to Austrian family allowance. However, they did not receive the German child-raising allowance (AFE), since they were working full-time. Ms Dodl and Ms Oberhollenzer had their applications for the child-raising allowance in Germany and the corresponding childcare allowance in Austria refused, on the grounds that the other Member State was responsible. They brought proceedings before the Austrian courts, and the *Oberlandesgericht* Innsbruck stayed proceedings and sought a preliminary ruling from the Court of Justice on two questions: firstly, whether Ms Dodl and Ms Oberhollenzer had lost the status of “employed persons” within the meaning of Regulation No. 1408/71 as a result of the suspension of their employment relationship, during which they were not required to pay social security contributions, and secondly which Member State is primarily responsible for paying the family benefit in question.

The view of the Court is that a person has the status of “employed person” within the meaning of Regulation No. 1408/71 where he or she is covered on a compulsory or optional basis by a general or special social security scheme, irrespective of the existence of an employment relationship. The Court handed down this judgment on the facts to the referring court. It furthermore observed that in Austria the mother, in her capacity as an employed person in that Member State, is entitled to childcare allowance. Assuming that Ms Dodl and Ms Oberhollenzer, who were living with their respective families in a Member State other than the State of employment, were deemed to be “salaried workers”, then under Community law they would also acquire the right to family allowance in the State of employment, in this case Austria. Ms Dodl and Ms Oberhollenzer are also entitled to comparable family allowances in

Germany, their State of residence. In Germany, any parent is entitled to receive a child-raising allowance on the basis of the fact that the parent and his or her child are resident there. In the case of overlapping entitlements to family benefits, for the same member of the family and the same period, the Member State of employment (Austria) is in principle responsible for making the payments. However, where a person having the care of children, in particular the spouse or partner of the employed person, carries out a professional or trade activity in the Member State of residence, the family benefits must be paid by that Member State. The activity need not necessarily be carried out by the individual personally entitled to these benefits. In that situation, the payment of family benefits by the Member State of employment is to be suspended up to the sum of family benefits provided for by the legislation of the Member State of residence (11).

3. Rights and obligations of employers and workers

3.1 The concept of the date of transfer of an undertaking:

Celtec Ltd (12)

Until 1989, the *Department of Employment* ran training programmes for young and unemployed people in England and Wales through local agencies. In 1989, the Government decided to transfer some of their professional training responsibilities to the *Training and Enterprise Councils* (TEC). The staffs employed by local agencies were invited to volunteer for a temporary three-year secondment to a TEC, during which they would retain their status as civil servants. In December 1991, the government proposed that, by the end of their fifth year of operation at the latest, the TECs should take over the status of employer of the staff working for them. In Wales, the activities, premises, information

11 The interested reader is referred to the case of *Effing* in which the Court of Justice decided that national legislation making the grant of family benefits to the members of the family of such a Community national subject to the condition that he remain a prisoner in that State did not run counter to the principle of equality, CJEC, Case C-302/02, *Effing*, ECR I-553, 20 January 2005; see also CJEC, Case C-101/04, *Noteboom*, ECR I-771, 20 January 2005; CJEC, Case C-153/03, *Weide*, 7 July 2005, not yet published.

12 CJEC, Case C-478/03, *Celtec Ltd*, ECR I-4389, 26 May 2005.

systems and database of the local agency in Wrexham were transferred to *North East Wales TEC*. *Newtec* opened in September 1990. Another TEC, *Targed*, took over the activities and premises of the local agency in Bangor. On 1 April 1997, *Newtec* and *Targed* were merged to form *Celtec*. When *Newtec* was established, the local agencies from Wrexham and Bangor seconded 43 civil servants to this TEC for a three-year period. At the end of their period of secondment, eighteen of them left the public service and became *Newtec* employees.

Mr Astley, Ms Hawkes and Ms Owens respectively entered public sector employment on 31 August 1973, 4 November 1985 and 21 April 1986, and were seconded to *Newtec*. At the end of their period of secondment, they chose to resign from the public service and to work for *Newtec*. The date of their resignation was identical to the date of their recruitment by *Newtec*. Their contract of employment commenced on 1 July 1993 in the case of Ms Hawkes and Ms Owens, and on 1 September 1993 in the case of Mr Astley. In 1998, Ms Hawkes was dismissed by *Celtec*, which refused to accept that she had been in continuous employment since the date on which she joined the Civil Service. The other two respondents feared they would be dismissed shortly as well. All three therefore sought a determination by the *Abergele Employment Tribunal* as to the length of the period of continuous employment on which they are able to rely, arguing that this should include their periods of service with the Civil Service as well as those with *Newtec* and *Celtec*. After losing the appeal, *Celtec* then went to the *House of Lords* on appeal, arguing that the transfer of undertaking was completed in the month of September 1990, which was well before the respondents were recruited by *Newtec*. The *House of Lords* decided to stay proceedings and make a referral for a preliminary ruling to the Court on the following question: Within the terms of Article 3(1) of Directive 77/187/EEC (Council of the European Communities, 1977), is there is a particular point in time at which the transfer of the undertaking concerned, and that of the rights and obligations of the transferor arising from employment relationships linking the latter with the workers it employs, is deemed to take place and, if the answer is in the affirmative, how can that particular point in time be identified?

The Court recalls that Directive 77/187 seeks to uphold workers' rights in the event of a change of the company management, by enabling them

to continue to work for the new employer subject to the same conditions as those agreed with the transferor. Article 3(1) covers the transferor's rights and obligations arising from a contract of employment or an employment relationship existing on the date of the transfer and entered into with employees who, in order to carry out their duties, were assigned to the undertaking transferred or to the part of the undertaking or business transferred. The reference to "date of transfer" in Article 3(1) is intended to identify the workers who may rely on the protection established by that provision. That protection therefore covers workers assigned to the unit affected by the transfer whose contract of employment or employment relationship is in force on the "date of a transfer" and not those who have ceased to be employed by the transferor on that date nor those who were recruited by the transferee after that date. For reasons of legal certainty, these workers must be identified at a particular point in the transfer process and not in relation to the length of time over which that process extends.

Under Article 3(1), the term transfer in the expression "date of transfer" to which that provision refers is to be understood within the meaning of Article 1(1). The deciding factor in defining a transfer is whether the new employer continues or resumes operation of the business, and whether its identity is retained. The term "date of transfer" in Article 3(1) of Directive 77/187 must therefore be understood as the date on which responsibility as employer for carrying on the business of the unit transferred moves from the transferor to the transferee. Contracts of employment or employment relationships existing on the date of transfer between the transferor and the workers assigned to the undertaking transferred are deemed to be handed over as of right from the transferor to the transferee, by virtue of the transfer alone. The Court has moreover already ruled that allowing the transferor or the transferee any choice in respect of the date of transfer of the contract or employment relation would amount to an acceptance that employers may derogate from the provisions of Directive 77/187, whereas in fact these provisions are mandatory and allow no derogation which might be detrimental to workers.

Thus, the date of a transfer is the date on which responsibility as employer for carrying on the business of the entity transferred moves from the transferor to the transferee. That date is a particular point in time which cannot be postponed to another date at the will of the transferor or transferee. Contracts of employment or employment relationships existing on the date of the transfer between the transferor and the workers assigned to the undertaking transferred, are deemed to be handed over from the transferor to the transferee on the transfer date, irrespective of any arrangements made between the parties in this respect ⁽¹³⁾.

3.2 The classification of on-call duty: the case of *Dellas* ⁽¹⁴⁾

Night duty carried out by a teacher in an establishment for persons with a disability must be taken into account in its entirety for the purpose of ascertaining whether the rules of Community law laid down to protect workers – in particular the maximum permitted weekly working time – have been complied with.

Directive 93/104/EC on working time sets down minimum health and safety standards in this field ⁽¹⁵⁾ (Council of the European Union 1993). It sets down minimum rest periods to which workers are entitled on a daily and weekly basis, and also defines adequate breaks. It also fixes the maximum weekly working time at 48 hours, including overtime. For these purposes, the Directive distinguishes between “working time” and “rest periods”. It does not provide for any intermediate category, and strikingly the definition of “working time” does not depend on the intensity of the work done ⁽¹⁶⁾.

¹³ The reader is referred to the judgment in *Junk* on collective redundancy, a subject which is not covered in this year’s review: CJEC, Case C-188/03, *Junk*, ECR I-885, 27 January 2005.

¹⁴ CJEC, Case C-14/04, *Dellas*, 1 December 2005, not yet published.

¹⁵ Directive 93/104/EC of 23 November 1993 was codified by Directive 2003/88/EC (European Parliament and Council of the European Union, 2003).

¹⁶ The Court of Justice has already ruled that, under the Directive, on-call services of doctors, nursing staff of emergency services, emergency workers and fire-fighters which are carried out at the place of work should be considered in their

In France, periods of night duty by workers in certain social and medico-social establishments are determined in accordance with a decree, which establishes a weighting mechanism for the purpose of calculating pay and overtime. It is intended to take into account the fact that there are periods of inactivity during on-call duty. The decree establishes a ratio between the hours of attendance at work and hours actually worked, a 3 to 1 ratio for the first nine hours followed by a 2 to 1 ratio for subsequent hours. Mr Dellas, a special needs teacher in residential establishments for young people with disabilities, was dismissed by his employer as a result of disagreements relating to the definition of actual work and remuneration due for hours of night duty on-call in a room on the premises. Mr Dellas and a number of trades unions brought proceedings before the *Conseil d'Etat* (Council of State) seeking the annulment of the decree in question. The *Conseil d'Etat* referred the issue to the Court of Justice, for a ruling as to whether such a regulation is compatible with the Directive.

The Court first of all finds that the Directive does not apply to the remuneration of workers. On the other hand, the hours of presence at work in question must be counted in their entirety as working time for the purpose of ascertaining whether there has been compliance with all minimum requirements laid down by Directive 93/104, to protect the health and safety of workers effectively. The flat-rate weighting mechanism in question takes the hours of presence of workers into account only in part. The total working time of a worker may thus amount to or even exceed 60 hours a week. Consequently, such a national system of calculating on-call time exceeds the maximum weekly working time set by the Directive at 48 hours.

The French Government had already anticipated the decision, as it had rescinded the disputed legislation in October 2004, before the Court ruling and the Decision of the Council of State had even been issued.

entirety to be working hours, irrespective of actual work carried out during that period. The judgments in the case of *Jaeger* (Case C-151/02) and *Pfeiffer* (Case C-397/01) are covered respectively in the 2003 and 2004 versions of *Social Developments in the European Union*.

As to the Community Directive, it is currently the subject of a proposal for amendment by the Council and the European Parliament (CEC, 2004b). This proposal provides, *inter alia*, for new definitions of on-call duty and of the inactive part of on-call duty. The latter periods will not be considered as working time unless national legislation, a collective agreement or an agreement between the social partners provides to the contrary. The periods during which a worker is actively carrying out his duties or activities will, in their entirety, be considered as working time within the meaning of the Directive. The new proposal has also provided for an “opt-out” in Article 22 which allows Member States to opt out of applying Article 6 on the maximum duration of the working week by virtue of a collective agreement, or an agreement concluded at an appropriate level between the social partners with the agreement of the worker. On 19 April 2005 the Employment and Social Affairs Committee of the European Parliament voted by a majority to abolish the opt-out and to consider on-call time, including rest periods, to be working time. After an initial rejection at the Employment and Social Affairs Council on 3 March 2005 (Council of the European Union, 2005a), the Ministers failed to agree on the revision of the Directive at the Council on 8 December (Council of the European Union, 2005b; Lhernould and Moizard, 2005). The torch will now be handed over to the Austrian Presidency.

Conclusions

The pace of activity at the Court has been intense to say the least. Whilst there have been no sensational decisions, the rulings which have been given afford us greater insight into the social policy dimension of Community law. Other issues will be decided in 2006. They will be many and varied. The following is a brief overview. The case of *Herrero*¹⁷ concerns a contract worker who is on maternity leave when she obtains a permanent post and becomes entitled take it up. The issue is whether she is entitled to become a civil servant with all the concomitant benefits which that position carries, such as the calculation of seniority with effect from that point, subject to the same conditions

¹⁷ Opinion of AG Stix-Hackl delivered on November 10th 2005, Case C-294/04, *Herrero*.

as all the other applicants who have obtained posts. Is she entitled to do this notwithstanding the fact that the exercise of the rights associated with the actual performance of work may be suspended until such time as she actually commences work? On the question of working time, the Court will have to rule on the following question: does Directive 1999/70/EC (on the Framework Agreement between ETUC, UNICE and CEEP on fixed-time working) preclude provisions of national law (which pre-date the implementation of the Directive) which differentiate between employment contracts signed with the public authorities and contracts with private sector employers, by excluding the former from the protection afforded by establishing an employment relationship of indefinite duration in the event of an infringement of binding rules on successive fixed-term contracts (18)?

Finally, the case of *Laval* (19), which was already centre-stage in 2005, will again be the focus of great interest in 2006. In June, a Latvian company *Laval un Partneri Ltd*, recruited Latvian workers under Latvian law to carry out renovation works on an old school in the community of Vaxholm in Sweden. The company refused to sign the construction sector collective agreement with the Swedish trade union *Byggnads*, though this was a precondition to the carrying out of any economic activity in Sweden. *Laval* brought proceedings before the Swedish Labour Court, the court of highest instance in respect of labour disputes, arguing that the trade union action and sympathy action, which had resulted in a blockade of the site, were illegal. The company also sought an interim order pending the final resolution of the dispute, to the effect that the trade unions concerned must suspend their union action. The Labour Court rejected the application for a provisional order, but made a referral to the Court of Justice for a preliminary ruling.

One of the main issues in this case concerns the implementation in Sweden of the Directive on the posting of workers. The problematic article is Article 3.1.C, on the minimum wage. *Laval* maintains that

18 Opinion of AG Maduro delivered on 20 September 2005, Case C-53/04, *Marroso & Sardino*.

19 CJEC, Case C-341/05, *Laval*, pending case .

Sweden is not applying the rules adequately, and that there is therefore no obligation on *Laval* to pay the minimum wage laid down in the collective agreement negotiated with *Byggnads*, even if it is the trade union most representative of construction workers in Sweden. *Laval* calls into question the right in Swedish law of *Byggnads* and other trade unions to embark on union action in order to conclude a collective agreement in Sweden with a company which already has a collective agreement in another country, in this case Latvia. *Laval* cited the EC Treaty: Article 12 (prohibition on discrimination on grounds of nationality) and Article 49 (prohibition of restrictions on freedom to provide services within the Community in respect of nationals of Member States who are established in a State of the Community other than that of the person for whom the services are intended).

However, the most important aspect, which may have more serious repercussions, is the question as to whether the system operating in the Swedish labour market is compatible with the EC Treaty. During a recent visit to Sweden, on 5 October 2005, the Commissioner for the Internal Market, Charlie McCreevy, criticised Swedish collective agreements. He expressed the view that they are incompatible with the European Treaties, and that they represent a barrier to freedom of movement of workers within the internal market. He stated that he would refer the *Vaxholm* case and the question of Swedish collective agreements to the Court. When asked to expand upon his comments at the European Parliament on 25 October 2005, he altered his position slightly, and stressed that the Commission was not taking issue with collective agreements which were a matter for Member States, but that the Commission did have to ensure that the freedoms established under the Treaties were respected, and also to reconcile the internal market with the social models in place. He expressed the view that the debate should not focus on whether a social model is under threat, nor whether it should be replicated by others, but rather on the issue of what the internal market actually is, since maintaining barriers and holding back competition behind national frontiers is not an option ⁽²⁰⁾.

²⁰ http://www.europarl.eu.int/news/expert/infopress_page/047-1705-298-10-43-908-20051019IPR01656-25-10-2005-2005--false/default_en.htm.

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CEC (2004b), Proposal for a Directive of the European Parliament and of the Council amending Directive 2003/88/EC concerning certain aspects of the organisation of working time, COM (2004) 607 final of 22 September 2004 (http://europa.eu.int/eur-lex/lex/LexUriServ/site/en/com/2004/com2004_0607en01.pdf).

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Council of the European Communities (1979), Council Directive 79/7/EEC of 19 December 1978 on the progressive implementation of the principle of equal treatment for men and women in matters of social security, OJ L 6 of 10 January 1979, pp.0024- 0025.

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treatment in employment and occupation, OJ L 303 of 2 December 2000, pp.0016-0022.

Council of the European Union (2005a), 2663rd Council meeting “Employment, Social Policy, Health and Consumer Affairs”, 89/80/05 (Presse 117), Luxembourg, 2-3 June 2005 (http://ue.eu.int/ueDocs/cms_Data/docs/pressData/en/lisa/85263.pdf).

Council of the European Union (2005b), 2699th Council meeting “Employment, Social Policy, Health and Consumer Affairs”, 15201/05 (Presse 336), Brussels, 8-9 December 2005 (http://ue.eu.int/ueDocs/cms_Data/docs/pressData/en/lisa/87464.pdf).

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Joannin, P. (2004), “L’Europe, une chance pour la femme”, *Notes de la Fondation Robert Schuman*, May 2004.

Lhernould, J.-P. and Moizard, N. (2005), “Actualité du droit de l’harmonisation sociale en matière de rapport d’emploi”, *Droit social*, No.5, May 2005, pp.509-525.

Future prospects

Two fundamentally contradictory readings of the building of Europe were possible in 2005: first, that the initial project had been abandoned; second, that it was being redefined.

According to the first reading, this was the year when all of the Community's achievements to date were being reconsidered: rejection of the constitutional Treaty, rejection of the very foundations of European construction (economic liberalism and supranationalism), reappraisal of a "European social model" deemed no longer suited to the current climate of competition and globalisation, reappraisal of the common policies and especially the common agricultural policy and the economic and social cohesion policy, controversy over future EU enlargements to take in Turkey, Croatia... Even monetary union has been called into question in speeches by certain politicians in the aftermath of the referendums in France and the Netherlands. The French and Dutch "no" votes thus appear to have opened up a Pandora's box.

According to this reading, such an uncertain climate has a major impact on the conduct of the institutional players concerned. The European Commission is in retreat, unable to offer political leadership in this crisis situation and making more use of its right of initiative to deconstruct than to construct – in the name of fighting paperwork and red-tape. The Council is divided into factions (old members and new members, conservatives and progressives, contributors and beneficiaries, etc.), which can only reach agreement at the cost of repeated diplomatic contortions and convoluted compromises – witness the saga over the 2007-2013 financial perspectives. As for the European Parliament, finally, even though it is becoming more assertive in the legislative

process, it is being forced to revise its rules of procedure on account of a proliferation of incidents in its midst – taunts, altercations, insults and even blows (!) Such an approach inevitably concludes that all this spells the end of the European spirit which inspired the founding fathers of the Community fifty years ago: a spirit of solidarity among Member States, connected with an awareness of a shared destiny. All that can be done now, therefore, is to found Europe anew around a reduced number of countries, with the euro zone sometimes posited as the most appropriate terrain for more intensive political integration.

The other reading, however, would have it that in 2005 the European Union spent the year stabilising the democratic, economic and – to a lesser extent – social institutions of the new Member States while strengthening its economic competitiveness. Contrary to the doom-mongers' predictions, the consequences of enlargement have largely been mastered. The French and Dutch “no” votes on the draft constitutional Treaty had the merit of finally opening up a fresh, no-holds-barred debate about the European project and its integration methods. The debate that was missing at the time of enlargement in 2004 has, in a sense, come back in “through the window” in 2005. Discussion about the accession of Turkey has also opened up the debate about Europe's geographical and cultural limits. It is a difficult debate, but one which is crucial to the future identity of the European project. What is meant by “we Europeans”? Where does “the other” begin? How much solidarity is there among us? And with the outside world?

According to this second approach, the institutions of the enlarged Union are still bedding down, but the agreement on the financial perspectives at the December European Council demonstrated their capacity to function. Ultimately, are budgetary negotiations really any more arduous nowadays than in the 1970s and 1980s? This optimistic

¹ European Parliament (2006), Report on the amendments to be made to the European Parliament's Rules of Procedure relating to standards for the conduct of Members of the European Parliament, Final report A6-0413/2005, Committee on Constitutional Affairs, Rapporteur: Gérard Onesta, 16 December 2005.

vision maintains that Europe should now undertake reforms in order to adapt to the demands of economic competition and globalisation, whilst preserving the key characteristics of its unique social model, an alternative to the US model. Far from fading away, the European model is looked up to as an example in several regions of the world and is likely to gain ground bit by bit.

One thing does become obvious from this brief presentation of both readings: the initial project devised for a Europe of Six is no longer able to meet the challenges of a Europe of 25. What follows is that either the building of Europe will grind to a halt or its aims and methods will be redefined: the former scenario is inevitable if the latter does not happen (but the latter does not guarantee that the former will be avoided).

Thus, if it has become indispensable to redefine the European project, the main reason is that some of the post-war dreams of a peaceful and economic reunification of Europe have materialised. Another reason is that an integrated market has almost entirely been achieved: the internal market has become a routine matter and is no longer a political driving-force. Champions of economic liberalism will of course highlight delays in the transposition of directives concerning the internal market, bureaucratic headaches and “obstacles” to Europe’s competitiveness. Basically, however, it has to be admitted that, twenty years on from the White Paper on the internal market, the bulk of the groundwork has been done – indeed, more than had been expected, as far as deregulation and network industries are concerned ⁽²⁾, on account of changes in the wider world.

In our opinion, the redefinition of the European project took two opposing forms in 2005. The first was the attempt to endow the enlarged Union with a constitutional Treaty. Beyond the inherent limitations of any compromise, the purpose of this project was essentially to redefine broad principles for building Europe and

² It is nevertheless worth noting that, unlike the internal market, the euro has not yet found its point of balance, as illustrated by the renegotiation of the rules of the game (the Stability Pact) and by the desire in some quarters to put it at the heart of enhanced cooperation.

strengthening its institutions. It was most certainly a compromise – an inevitable source of dissatisfaction – but one which gave Europe’s political, economic and social stakeholders some clearly defined rules of the game underpinned by shared values and objectives. The political instability of this compromise probably arose from the fact that this draft constitution, this institutional construct, preceded the emergence of a European “demos” vital to our coexistence. In other words, what this constitution lacks is a social vision of our coexistence which could have helped, in the medium term, to forge a European identity.

The second manifestation of a new project for Europe strikes us as more insidious: this is the one which unobtrusively produced the “services” directive (prior to the European Parliament’s amendments) and the “better regulation” initiative. What is the underlying approach behind these two elements? The services directive initially contained a vision of European construction whose intention, in addition to establishing a large market in services, was to oblige not companies but national legislations to compete with one another. That vision radically alters the rules of the game and hence the conduct of the political, economic and social stakeholders. The same applies to “better regulation”: it serves not so much to bring about a qualitative improvement in public action as to discredit political regulation in itself.

It is therefore obvious that, in their ideal types, both of these political projects pervert nothing less than the two founding principles of European construction, namely economic liberalism and supranationalism. As concerns the services directive, in its ideal type national legislations are forced to compete with each other in the name of a certain form of economic liberalism, so any notion of solidarity and shared destiny is destroyed. As concerns the “better regulation” initiative, in its ideal type supranational regulation is abandoned in the name of European competitiveness, by making economic interests take precedence over public action (e.g. in the field of health and safety).

Both of these initiatives emanate from the European Commission, under pressure from certain Member States, and they both carry within them the wherewithal to pervert the two founding principles of the Community. Under these circumstances it is hardly surprising that, in several Member States, 2005 signals a return to national “economic

patriotism”: if Europe is to be about competition, then everyone will look after their own interests and reject the other; if Europe does not guarantee the same rights, then the “Polish plumber” and the Estonian labourer should stay at home!

We would make another point here. It seems to us that the European agenda has undergone a fundamental change in recent years as a consequence of enlargement and globalisation. Briefly, we have moved from an internal agenda (common agricultural policy, internal market, euro, etc.) to an external agenda (Europe’s role in the world, international trade, asylum and immigration, common foreign and defence policy, etc.). Europe is much more deeply immersed in the world now than it was in the past.

As a result of enlargement there are new borders to be managed with Russia, Ukraine and Belarus, and new responsibilities to be borne in terms of regional stabilisation. Migration flows have likewise become more complex, and Europe now has greater responsibility towards Africa. The negotiations with Turkey can only intensify this process. Such changes naturally pose questions about the European model – including the social model – in the context of globalisation. The appointment of Pascal Lamy to the top job at the World Trade Organisation might reveal Europe’s capacity, or incapacity, to develop its own consensual agenda. The emergence of China and, to a lesser extent, India signals the start of a period when both diplomatic and foreign trade relations become crucial.

In a sense, if twenty years after the launch of the internal market Europe has managed to integrate economically and, in part, politically, then the time has now come to demonstrate its ability to project its model of political integration to the outside world, incomplete and fragile though that model still is. This new challenge could lead to one of two scenarios. In the first case, the shock of external developments could help destroy the internal political achievements already made; that is, the edifice is not sufficiently robust to withstand the external challenges and these serve to undermine political integration (the scenario of political dilution in commercial globalisation). In the second case, these challenges help strengthen the internal dynamic by enabling Europe to carve out a specific role at global level. This does not mean

that external challenges will bring about a federal Europe in the classic sense of the term, but that the European preference for resolving conflict through dialogue and for establishing common standards can also be found at international level ⁽³⁾.

What will be Europe's place in the world ten years from now? What contribution will it make to stabilising the world? How open will it be to immigration? And what vision of global development will it offer? While economic and monetary integration is still underway, external political factors will force the European project to reinvent itself.

The question of leadership is central in this new environment. In the recent past, key figures such as François Mitterrand and Helmut Kohl managed to clinch compromise deals to finalise the internal market and the single currency. Which European leaders will be able, today and tomorrow, to set out a coherent European vision in the face of these external challenges? For want of such a vision, there is a risk that the present leaders may fall back on an approach to the Union consisting in deregulating national economies and compelling citizens to accept change in the name of a Europe which imposes such constraints that they can no longer identify with it. "Better regulation" and the services directive were striking examples of this phenomenon in 2005.

³ Laïda, Z. (2005), *La norme sans la force. L'énigme de la puissance européenne*, Presses de Sciences Po, Paris.

Chronology 2005

Key events in European social policy

JANUARY

11 January: the European Commission presents a **Green Paper** as a basis for reflecting on an **“EU approach to managing economic migration”**, COM (2004) 811 final of 11 January 2005.

27 January: the European Commission publishes its **“Second Implementation Report on the 2003-05 BEPGs”**, COM (2005) 8 final of 27 January 2005. It also unveils its **“Draft Joint Employment Report 2004/2005”**, COM (2005) 13 final, as well as the **“Draft Joint Report on Social Protection and Social Inclusion”**, COM (2005) 14 final of 27 January 2005.

FEBRUARY

2 February: the President of the Commission, Mr Barroso, proposes a review of the Lisbon objectives and strategy. **“Working together for growth and jobs. A new start for the Lisbon Strategy”**, Communication to the Spring European Council from President Barroso in agreement with Vice-President Verheugen, COM (2005) 24 of 2 February 2005.

8 February: Commissioner Spidla puts forward a proposal for a directive on the working conditions of railway workers, which gives binding force to the agreement signed by the social partners.

“Proposal for a Council Directive on the agreement between the Community of European Railways (CER) and the European

Transport Workers' Federation (ETF) on certain aspects of the working conditions of mobile workers assigned to interoperable cross-border services", COM (2005) 32 final of 8 February 2005.

9 February: the European Commission adopts the Social Agenda. **"Communication from the Commission on the Social Agenda"**, COM (2005) 33 final of 9 February 2005.

14 February: the European Commission adopts the second **"Report on equality between women and men, 2005"**, COM (2005) 44 final of 14 February 2005, which covers all 25 EU Member States.

MARCH

3 March: at the Employment and Social Affairs Council, the Ministers emphasise the importance of the social aspects of the Lisbon strategy and express their hope that an agreement on **maximum weekly working hours (the "opt-out")** will be reached at the Council of 3 June. 2664th Council meeting – Employment, Social Policy, Health and Consumer Affairs – Brussels, 3 March 2005 (6479/05 - Presse 38).

8 March: the European Commission proposes an **Institute for Gender Equality** (IP/05/266) (<http://europa.eu.int/rapid/pressReleasesAction.do?reference=IP/05/266&format=HTML&aged=1&language=EN&guiLanguage=en>).

15 March: the European social partners adopt a joint contribution on the Lisbon strategy. ETUC, UNICE-UEAPME and CEEP, **"Joint declaration on the mid-term review of the Lisbon strategy"**, 15 March 2005 (http://europa.eu.int/comm/employment_social/news/2005/mar/lisbon_review_en.pdf).

19 March: the ETUC stages a **Euro-demonstration** ahead of the Spring Summit (<http://hesa.etui-rehs.org/uk/newsevents/files/tract%20en.pdf>).

20 March: the Ecofin Council and the enlarged Eurogroup propose a renewed Stability Pact with greater room for interpretation. Council of the European Union, **"Improving the implementation of the Stability and Growth Pact"**, Brussels, 20 March 2005 (7423/05), (<http://register.consilium.eu.int/pdf/en/05/st07/st07423.en05.pdf>).

22 March: the social partners adopt a “**Framework of actions on gender equality**”, ETUC, UNICE-UEAPME and CEEP, Brussels, 1st March 2005 (http://www.etuc.org/IMG/pdf/framework_of_actions_gender_equality_010305-2.pdf).

Tripartite Social Summit: Jean-Claude Juncker and José Manuel Barroso call on the European social partners to express their views on the **relaunch of the Lisbon process** and on an EU Youth Initiative. The social partners back the Commission’s proposal for a review of the Lisbon strategy. (IP/05/353) (<http://europa.eu.int/rapid/pressReleasesAction.do?reference=IP/05/353&format=HTML&aged=1&language=EN&guiLanguage=en>).

The European social partners adopt their third follow-up report on the “**Framework of actions for the lifelong development of competencies and qualifications**”. ETUC, UNICE-UEAPME and CEEP, 1st March 2005 (http://www.etuc.org/IMG/pdf/LLL-en-3rd_follow-up_report_final_010305-2.pdf).

The social partners adopt their “**Joint report on employment actions in Member States**”, ETUC, UNICE-UEAPME and CEEP, “2005 Report on Social Partners’ Actions on Employment in Member States”, March 2005 (http://www.etuc.org/IMG/pdf/2005_Joint_Report_on_Employment-3.pdf).

The social partners adopt their “**Joint contribution on the EU Youth Initiative**”, ETUC, UNICE-UEAPME and CEEP, 22 March 2005 (http://europa.eu.int/comm/employment_social/news/2005/mar/youth_en.pdf).

22-23 March: the **European Spring Summit** is mainly devoted to the directive on services in the internal market and to the reform of the Stability and Growth Pact. The 25 stress that the “services” directive must fulfil two imperatives: liberalisation of the market in services and respect for the European social model. They approve without change the Finance Ministers’ report on the Stability and Growth Pact, Brussels European Council, *Presidency Conclusions*, 23 March 2005 (http://ue.eu.int/ueDocs/cms_Data/docs/pressData/fr/ec/84331.pdf).

31 March: the Commission adopts a Communication on restructuring and employment, which also constitutes the second phase of the social partner consultation on company restructuring and European Works Councils. Communication from the Commission “**Restructuring and employment. Anticipating and accompanying restructuring in order to develop employment: the role of the European Union**”, COM (2005) 120 final of 31 March 2005.

APRIL

1st April: the European Trade Union Institute (ETUI), the European Trade Union College (ETUCO) and the Trade Union Technical Bureau for Health and Safety (TUTB) merge to form the **European Trade Union Institute for Research, Education and Health and Safety (ETUI-REHS)**. (<http://www.etuc.org/a/1039>).

1st April: the Commission launches the first phase of its consultation of the European social partners concerning “**simplification of the provisions of the health and safety at work directives**”. (http://europa.eu.int/comm/employment_social/social_dialogue/docs/simplification_hs_en.pdf).

6 April: the Commission adopts the legislative proposals concerning the **Financial Framework 2007-2013**, *Press Release*, IP/05/389, Brussels (<http://europa.eu.int/rapid/pressReleasesAction.do?reference=IP/05/389&format=HTML&aged=1&language=EN&guiLanguage=en>).

7 April: the social partners discuss “**Lessons learned on European Works Councils**”, ETUC, UNICE-UEAPME and CEEP, 7 April 2005 (http://europa.eu.int/comm/employment_social/social_dialogue/docs/ewc_en.pdf).

11 April: the European Commission publishes its 2005 report on **Progress towards the Lisbon Objectives in Education and Training** (IP/05/410). “Commission Staff Working Paper. Progress towards the Lisbon Objectives in Education and Training”, SEC (2005) 419 of 22 March 2005.

12 April: the Commission presents its **employment guidelines and BEPGs for 2005-2008**. “Integrated guidelines for growth and jobs

(2005-2008), including a Commission Recommendation on the broad guidelines for the economic policies of the Member States and the Community (under Article 99 of the EC Treaty) and a Proposal for a Council Decision on guidelines for the employment policies of the Member States (under Article 128 of the EC Treaty)", COM (2005) 141 final of 12 April 2005.

18 April: the Council of the EU adopts its **common position on health and safety protection of workers exposed to optical radiation**, "Common Position (EC) No.24/2005 of 18 April 2005 adopted by the Council, acting in accordance with the procedure referred to in Article 251 of the Treaty establishing the European Community, with a view to adopting a directive of the European Parliament and of the Council on the minimum health and safety requirements regarding the exposure of workers to the risks arising from physical agents (optical radiation) (19th individual Directive within the meaning of Article 16(1) of Directive 89/391/EEC), OJ C 172 E of 12 July 2005, pp.0026-0050.

19 April: the draft **Gebhardt report on the "services" directive** is submitted to the European Parliament's Internal Market Committee. It seeks to abolish the country of origin principle and exclude services of general interest. "Draft Report on the proposal for a directive of the European Parliament and of the Council on services in the internal market (COM(2004)0002 – C6-0069/2004 – 2004/0001(COD))", Rapporteur: Evelyne Gebhardt (http://www.europarl.eu.int/comparl/imco/services_directive/050525_pr_gebhardt_en.pdf).

The European Parliament's Committee on Employment and Social Affairs votes by a majority for an **ending of the opt-out** ("working time" directive, Cercas report) and for **on-call time**, including its inactive period, to be regarded as **working time** (<http://www.eurofound.eu.int/2005/05/feature/eu0505205f.html>)

20 April: launch of the **European campaign against noise in the workplace** by the European Agency for Safety and Health at Work (<http://ew2005.osha.eu.int>).

MAY

9 May: the European Trade Union Confederation (ETUC) and the European Transport Workers' Federation (ETF) call on the Council of Social Affairs and Labour Ministers to adopt the **draft directive on certain aspects of working conditions for mobile railway workers assigned to cross-border interoperability services**. ETF and ETUC, *Press Release*, 9 May 2005 (<http://www.etuc.org/a/1234>).

10 May: the European Commission puts forward a draft **detailed programme for the freedom, security and justice policy for the period 2005-2010**. This programme represents the implementation of the Hague programme, adopted by the European Council on 4-5 November 2004. Communication from the Commission to the Council and the European Parliament "The Hague programme: Ten priorities for the next five years. The Partnership for European renewal in the field of Freedom, Security and Justice", COM (2005) 184 final of 10 May 2005.

11 May: the plenary session of the European Parliament adopts the **Cercas report on the "working time" directive**, which calls for the opt-out to be abolished and for the rulings of the Court of Justice concerning on-call time to be complied with. "Final Report A6-0105/2005 on the proposal for a directive of the European Parliament and of the Council amending Directive 2003/88/EC concerning certain aspects of the organisation of working time (COM (2004)0607 – C6-0122/2004 – 2004/0209(COD)), rapporteur: Alejandro Cercas, 25 April 2005.

17 May: in its **third progress report on cohesion**, the European Commission proposes the establishment of a solidarity fund. Communication from the Commission "Third progress report on cohesion: Towards a new partnership for growth, jobs and cohesion", COM (2005) 192 final of 17 May 2005.

29 May: a referendum of the French people rejects the ratification of the draft European constitutional Treaty by 54.87% to 45.13% of the vote (<http://www.interieur.gouv.fr/avotreservice/elections/rf2005/index.html>).

JUNE

1st June: 61.6% of voters in the Netherlands reject the draft European constitutional Treaty. *Bulletin of the European Union*, No.8960 of 3 June 2005.

2-3 June: at the Employment and Social Affairs Council, Commissioner Vladimir Spidla puts forward his **proposal for an amendment to the “working time” directive**, which attempts to reach a compromise between the European Parliament’s report of 11 May and the Council’s common position. “Amended proposal for a Directive of the European Parliament and of the Council amending Directive 2003/88/EC concerning certain aspects of the organisation of working time”, COM (2005) 246 final of 31 May 2005. 2663rd Council meeting – Employment, Social Policy, Health and Consumer Affairs – Luxembourg, 2-3 June 2005 (8980/05 - Presse 117).

The Employment and Social Affairs Council makes no headway on the proposed amendment to the “working time” directive.

The Ministers do reach a political agreement on the directive concerning the agreement between the Community of European Railways (CER) and the European Transport Workers’ Federation (ETF) on certain aspects of the working conditions of mobile workers assigned to interoperable cross-border services.

2-3 June: at the meeting of the Justice and Home Affairs Council, the European Commission announces intention to **withdraw its proposal for a framework decision defining and sanctioning racism and xenophobia**. After four years of lengthy, unproductive debate, the Member States and the Commission conclude that the positions of the various Member States are irreconcilable. 2664th Council meeting - Justice and Home Affairs – Luxembourg, 2-3 June 2005 (8849/05 - Presse 114). The Justice and Home Affairs Council adopts the 2005-2010 programme for the freedom, justice and security policy, as proposed by the Commission on 10 May. This programme represents the implementation of the Hague programme, adopted by the European Council on 4-5 November 2004.

6-7 June: the Competitiveness Council adopts the **directive on the recognition of professional qualifications**, 2665th Council meeting – Competitiveness – Internal Market, Industry and Research – Luxembourg, 6-7 June 2005 (9501/05 - Presse 133).

16-17 June: the European Council fails to agree on the **2007-2013 financial perspectives**. Brussels European Council, *Presidency Conclusions*, 17 June 2005 (http://ue.eu.int/ueDocs/cms_Data/docs/pressData/fr/ec/85324.pdf).

28 June: the Council of the EU adopts without debate the amendments to Regulations 1466/97 and 1467/97, finalising the legislative revision of the Stability and Growth Pact. “Council Regulation (EC) No.1055/2005 amending Regulation (EC) No.1466/97 on the strengthening of the surveillance of budgetary positions and the surveillance and coordination of economic policies; Council Regulation (EC) No.1056/2005 amending Regulation (EC) No.1467/97 on speeding up and clarifying the implementation of the excessive deficit procedure”, *Bulletin of the European Union*, 6-2005, (<http://europa.eu.int/abc/doc/off/bull/en/200506/p103004.htm>).

JULY

1st July: Ernest-Antoine Seillière, president of the French employers’ organisation Medef (Mouvement des entreprises de France), takes over from Jürgen Strube at the helm of **UNICE**, *Bulletin of the European Union*, No.8981, 1st July 2005.

5 July: the European Commission presents its “**Strategic Guidelines**” for the economic and social cohesion policy in 2007-2013, Communication from the Commission “Cohesion Policy in Support of Growth and Jobs: Community Strategic Guidelines 2007-2013”, COM (2005) 299 final of 5 July 2005.

12 July: the informal Employment and Social Affairs Council in Belfast opens the debate about the **European social model**, in preparation for the informal European summit scheduled by the Council presidency for 27 October. UK presidency website – *Press Release* (<http://www.eu2005.gov.uk/servlet/Front?pagename=OpenMarket/Xcelerate/ShowPage&c=Page&cid=1115145051733>).

20 July: the European Commission publishes its “**Community Lisbon Programme**” in which it sets out “eight key measures” on employment and growth. Communication from the Commission to the Council and the European Parliament, “Common Actions for Growth and Employment: The Community Lisbon Programme”, COM (2005) 330 final of 20 July 2005.

27 July: Council Directive 2005/47/EC of 18 July 2005 on the Agreement between the Community of European Railways (CER) and the European Transport Workers’ Federation (ETF) on certain aspects of the **working conditions of mobile workers engaged in interoperable cross-border services in the railway sector** is published in the Official Journal (OJ L 195 of 27 July 2005, pp.0015-0018).

SEPTEMBER

1st September: following on from the Hague action plan approved by the Council on 3 June, the Commission adopts a package of measures in the field of **asylum and immigration**, containing in particular a proposal for a directive on common standards applicable to the return of illegal immigrants and three Communications relating respectively to integration, regional protection programmes, and migration and development. Communication from the Commission on regional protection programmes, COM (2005) 388 final; Communication de la Commission “A Common Agenda for Integration. Framework for the Integration of Third-Country Nationals in the European Union”, COM (2005) 389 final; Communication from the Commission “Migration and Development: Some concrete orientations”, COM (2005) 390 final, “Proposal for a Directive of the European Parliament and of the Council on common standards and procedures in Member States for returning illegally staying third-country nationals” COM (2005) 391 final of 1st September 2005.

7 September: the European Council adopts at second reading the Csaba Öry report on the **protection of workers exposed to optical radiation**, introducing amendments meeting the concerns of the PPE-DE and ALDE groups. “Recommendation for second reading on the Council common position for adopting a directive of the European Parliament and of the Council on the minimum health and safety

requirements regarding the exposure of workers to the risks arising from physical agents (optical radiation) (19th individual Directive within the meaning of Article 16(1) of Directive 89/391/EEC) (5571/6/2005 – C6-0129/2005 – 1992/0449B(COD))”, Final A6-0249/2005, rapporteur: Csaba Öry, 20 July 2005.

27 September: the European Commission adopts a Communication aimed at withdrawing 68 outstanding legislative proposals (“**Better regulation**”). Communication from the Commission “Outcome of the screening of legislative proposals pending before the Legislator”, COM (2005) 462 final of 27 September 2005.

A social dialogue summit celebrates the **20th anniversary of the European social dialogue** (http://europa.eu.int/comm/employment_social/news/2005/sep/socialdialogue_summit_flash_fr.pdf).

The European Parliament approves, with over a hundred amendments, the proposal for a directive on the **granting and withdrawing of refugee status in EU Member States**, “Final Report A6-0222/2005 on the amended proposal for a Council directive on minimum standards on procedures in Member States for granting and withdrawing refugee status (14203/2004 – C6-0200/2004 – 2000/0238(CNS))”, rapporteur: Wolfgang Kreissl-Dörfler, 29 June 2005.

OCTOBER

4 October: the European Parliament’s Internal Market Committee, which was to have debated amendments to the **Gebhardt report on the “services” directive**, postponed its vote until 20-21 November; the vote in plenary will not take place until January 2006, *Bulletin of the European Union*, No.9042 of 6 October 2005.

The Secretary General of the European Confederation of Independent Trade Unions (CESI) announces that his organisation has obtained the **status of European social partner** thanks to its representativeness in the field of central public administration (http://www.cesi-bxl.be/_en/).

12 October: the European Commission adopts a Communication entitled “**A strategy on the external dimension of the area of freedom, security and justice**”, COM (2005) 491 final of 12 October 2005.

18 October: the European Commission presents its Communication on **“Fighting trafficking in human beings – an integrated approach and proposals for an action plan”**, COM (2005) 514 final of 18 October 2005.

19 October: the European Commission adopts its new **employment report**, which largely demonstrates the effectiveness of the employment policies pursued under the European employment strategy. European Commission, *Employment in Europe 2005 – Recent Trends and Prospects*, Office for Official Publications of the European Communities, Luxembourg, 2005.

20 October: the European Commission puts forward a proposal for a directive on the **portability of supplementary pension rights**, “Proposal for a Directive of the European Parliament and of the Council on improving the portability of supplementary pension rights [SEC (2005) 1293]”, COM (2005) 507 final of 20 October 2005.

In preparation for the informal European summit devoted to the future of the European social model, the Commission presents a Communication on **European values in the era of globalisation**, Communication from the Commission “European values in the globalised world. Contribution of the Commission to the October Meeting of Heads of State and Government”, COM (2005) 525 final of 20 October 2005.

24 October: at the Tripartite Social Summit, the EU presidency, the Commission and the social partners forward a message to the informal European summit on the **future of the European social model** so as to achieve the EU’s economic and social objectives against a background of globalisation, competition and population ageing. (<http://www.etuc.org/a/1680> and <http://europa.eu.int/rapid/pressReleasesAction.do?reference=IP/05/1337&format=HTML&aged=1&language=EN&guiLanguage=en>).

27 October: at the **informal European summit on the future of the European social model**, the 25 define priority fields of action for responding to globalisation, but give a lukewarm reception to the proposal to create a Fund for adjusting to globalisation (http://ue.eu.int/cms3_fo/showPage.asp?lang=en&id=965&mode=g&name=).

NOVEMBER

15 November: the Commission adopts a **Communication on public-private partnerships (PPP)**, taking stock of the policy options conceivable at Community level to ensure healthy competition in this area. Communication from the Commission on Public-Private Partnerships and Community Law on Public Procurement and Concessions, COM (2005) 569 final of 15 November 2005.

21 November: the social partners EFFAT and GEOPA-COPA belonging to the European sectoral social dialogue committee on agriculture sign an agreement on the “reduction of workers’ exposure to the risk of work-related **musculo-skeletal disorders (MSD)** in agriculture”. (http://www.effat.org/5/5_2/5_2_4/Files%20EN/051121%20Final%20Agreement%20signed%20EN.pdf).

22 November: the European Parliament’s Internal Market Committee adopts, by 25 votes in favour, 10 against and 5 abstentions, the **report by Evelyne Gebhardt** on the proposal for a “services” directive. *Bulletin of the European Union*, No.9074 of 24 November 2005.

30 November: the Commission puts forward a Communication setting out priority actions for improving the handling of **immigration**. Communication from the Commission, “Priority actions for responding to the challenges of migration: First follow-up to Hampton Court”, COM (2005) 621 final of 30 November 2005.

DECEMBER

1st December: Europe’s Ministers of the Interior, meeting in the Justice and Home Affairs Council, adopt the directive on the **granting of refugee status in the EU**, thereby completing the first phase of the establishment of a common European asylum system. 2696th Council meeting – Justice and Home Affairs – Brussels, 1-2 December 2005 (14390/05 – Presse 296).

6 December: the European Parliament and the Council conclude an agreement on the draft European legislation to improve **working time and rest periods for lorry drivers** and to tighten checks on lorries. “Joint draft adopted by the Conciliation Committee provided for in

Article 251(4) of the EC Treaty, PE-CONS 3671/05 of 8 December 2005” (http://www.europarl.eu.int/omk/sipade3?PROG=JOINT-TEXT&REF_C=C6-2005-0416&F_REF_C=C6-0416/2005&NAV=X&L=EN&LEVEL=2&SAME_LEVEL=1).

At a meeting of the Conciliation Committee, the Council and European Parliament formally give the green light to the directive on the **protection of workers against the risks of exposure to optical radiation**. “Joint text approved by the Conciliation Committee: Exposure to optical radiation. Provisional version. C6-0001/2006”. (http://www.europarl.eu.int/code/dossier/2005/1992_0449b_optical_radiation/default_en.htm). (http://www.europarl.eu.int/omk/sipade3?PROG=JOINT-TEXT&L=FR&REF_C=C6-2006-0001&F_REF_C=C6-0001/2006).

8 December: the Employment and Social Affairs Council fails yet again to agree on the **revision of the “working time” directive**. The challenge now falls to the Austrian presidency. 2699th Council meeting – Employment, Social Policy, Health and Consumer Affairs - Brussels, 8-9 December 2005 (15201/1/05 REV 1 – Presse 336).

16 December: the European Council reaches a **political agreement on the financial perspectives** for 2007-2013. Brussels European Council, *Presidency Conclusions*, 17 December 2005 (http://ue.eu.int/ueDocs/cms_Data/docs/pressData/en/ec/87642.pdf).

**Chronology drawn up by Christophe Degryse
with the assistance of Dominique Jadot.**

List of abbreviations

ASEAN	Association of Southeast Asian Nations
BEPGs	Broad Economic Policy Guidelines
CAP	Common Agricultural Policy
CEC	Commission of the European Communities
CEEC	Central and eastern European countries
CEEP	European Centre of Enterprises with Public Participation
CFSP	Common foreign and security policy
CJEC	Court of Justice of the European Communities
COP	Country of origin principle
CSF	Community support frameworks
DG	Directorate General (of the Commission / the European Parliament)
DFI	Direct foreign investment
EAFRD	European Agricultural Fund for Rural Development
EAGGF	European Agricultural Guidance and Guarantee Fund
EC	European Community
ECAS	European Citizen Action Service
ECB	European Central Bank
ECOFIN	Council for Economic and Financial Affairs
EDF	European Development Fund

EDC	European Defence Community
EEC	European Economic Community
EES	European Employment Strategy
EESC	European Economic and Social Committee
EIB	European Investment Bank
EIF	European Investment Fund
EMU	Economic and Monetary Union
EP	European Parliament
EPC	Economic Policy Committee
ERDF	European Regional Development Fund
ESDP	European Security and Defence Policy
ESF	European Social Fund
ETUC	European Trade Union Confederation
EU	European Union
EUROGROUP	Group of 12 Member States having adopted the euro
FERPA	European Federation of Older People and Pensioners
FIFG	Financial instrument for Fisheries Guidance
GATS	General Agreement on Trade in Services
GATT	General Agreement on Tariffs and Trade
GDP	Gross domestic product
GNI	Gross national income
GNP	Gross national product
IIA	Interinstitutional Agreement
ILO	International Labour Organization
IMF	International Monetary Fund

MED	Macroeconomic Dialogue
MCI	Monetary conditions indicator
MTO	Medium-term objective
NEER	Nominal effective exchange rate
NGO	Non-governmental organisation
OECD	Organisation for Economic Co-operation and Development
OMC	Open method of co-ordination
PPP	Public-private partnership
SGEI	Services of General Economic Interest
SGP	Stability and Growth Pact
SME	Small and medium enterprise
SPC	Social Protection Committee
SPD	Single programming documents
TEN	Trans-European Networks
TOR	Traditional own resources
UEAPME	European Association of Craft, Small and Medium-sized Enterprises
UNECE	United Nations Economic Commission for Europe
UNICE	Union of Industrial and Employers' Confederations of Europe
UNO	United Nations Organization
VAT	Value added tax
WTO	World Trade Organization

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