

Industrial Policy: The Softer Side of Differentiated Integration

David Howarth

Please cite as: Howarth, D. (2010) 'Industrial Policy: The Softer Side of Differentiated Integration' in Dyson, K. and Sepos, A., eds., *Which Europe? The Politics of Differentiated Integration*, Basingstoke: Palgrave Macmillan, pp. 233-250.

Prior to considering differentiated integration in European Union industrial policy, it is first necessary to understand what this policy encompasses. EU industrial policy incorporates a range of policies that have a direct or indirect impact upon industry. The European Commission (2005) adopts an official definition of industrial policy that is narrow and focused upon manufacturing, effectively excluding service industries. In its view, industrial policy involves creating the conditions for manufacturing to thrive, complementing work at the member-state level. The EU's industrial policy officially includes seven cross-sector initiatives – on competitiveness, energy and the environment; intellectual property rights; better regulation; industrial research and innovation; market access; skills; and managing structural change – which is to benefit a wide range of industrial sectors. In addition, the Commission has introduced seven new initiatives targeted at specific sectors – pharmaceuticals, chemicals, space, defence, information and communication technologies, mechanical engineering, food and fashion and design industries.

EU industrial policy is officially geared towards proposing specific solutions to improve the competitiveness of European industry and prevent de-industrialisation, notably ‘in the light of increasingly strong competition from China and Asia’ (Commission 2005: 1). It is also ‘an important step in the delivery of the new Lisbon “Partnership for Growth and Jobs”’ (*ibid.*). The Lisbon Agenda focuses upon competitiveness, stimulating innovation and supporting small and medium-sized enterprises (SMEs) as part of the broader goals of transforming the EU into ‘the most dynamic and competitive knowledge-based economy in the world ... by 2010’. EU industrial policy covers a range of internal market legislation that regulates the operation of industry, including health and safety legislation and environmental legislation (see the chapter by Wurzel and Zito in this volume). It includes support for research and development (R&D) and, potentially, aid for ‘declining industrial regions’. Not least, it incorporates the application of EU competition policy and the restrictions imposed through this policy on national industrial policies.

EU industrial policy differs from what is traditionally known as industrial policy, which encompasses everything that governments can do to influence industry including financial and fiscal intervention. Until the 1980s, the concept of industrial policy was synonymous with market-distorting actions by national governments. EU state aid rules had little practical effect upon national practices because the Commission was unable to control the sheer volume of subsidies and other assistance to companies. The EU itself possesses few policy instruments, weak legal basis and little funding to intervene actively to promote particular industries outside of agriculture, coal and steel. The heyday of EU industrial interventionism was during the first half of the 1980s, when the Commission led schemes to cushion the

restructuring of the steel industry by enforcing production quotas. The Single European Act's Article 130 (Articles 163-173 TEC) sanctioned new EU funding to subsidize cross-border R&D. There is also a legal basis for exemptions to the application of EU competition policy to allow for interventionist national industrial policies. Provisions in the Treaty of Rome (Articles 87-89 TEC) specify categories of national state aid to industry that are not incompatible with the common market (i.e. those having a 'social character') or not necessarily incompatible (e.g. 'aid to promote the economic development of areas where the standard of living is abnormally low') and the possibility of creating new categories.

With the rise of economic liberalism and the decline (but not disappearance) of national interventionism, EU industrial policy was shaped by national preference for state withdrawal from the economy. The EU's less interventionist approach to industrial policy dates from the early 1990s and Martin Bangemann's takeover of the industrial policy portfolio. Bangemann (1992: 20) insisted that the 'old, sectoral industrial policy would be replaced by a modern, horizontal approach which would no longer support individual industrial [sectors] but competitiveness on a large scale'. This new policy corresponded to the reinforced application of EU competition policy rules. Nonetheless, in a limited range of areas, notably information technology, the Commission continued to push for major investment programmes. France and some other member states also continued to demand a more active EU policy. Provisions were inserted into the Maastricht Treaty (now Article 173 Consolidated Version of the Treaty) pledging the EU and its member states to ensure the 'conditions necessary for the competitiveness' of industry, to provide greater assistance to SMEs and to ensure improved industrial exploitation of the EU's research policies. Yet, because these

provisions outline a strategy more than they mandate a policy and require unanimity in the Council to adopt actions, strong constraints have been placed upon the potential development of EU-led interventionism (Peterson 1996).

Differentiated integration in this policy area is the result of one or more of five factors: differences in ideology among member states, domestic political circumstances, capacity (level of economic development), national economic structures, and technical preferences. There is a considerable degree of ‘capitalist diversity’ in the EU (Wilks 1996). Even among the ‘Original Six’ member states there are important differences in approach to economic regulation, even if they all embrace the EU system (Gerber 2000). Ideological difference may contribute to differentiation in that member states where economic liberalism holds more sway in government circles will pursue different policies than those pursued by member states where interventionist solutions to industrial problems are more acceptable. Different levels of economic development have repeatedly been used as a justification for temporary derogations for poorer member states in the implementation of EU legislation. Justifications stemming from ideology, economic development and structures can result in differentiated participation in EU-led or other European R&D projects. Technical preference has been a cited reason for delays in certain national programmes of sector-based market liberalisation.

In several areas these five factors overlap, and assessing their relative importance is difficult. Thus in energy market liberalisation, ideology and domestic political opposition have had a potentially significant role. There is an entrenched scepticism in certain member states about the desirability of liberalising the production and

supply of electricity and gas, on the grounds that these are public services which should be protected from market forces. Ideology is also likely to be of relevance with regard to national infringements of EU competition policy. However, the national rhetoric of protectionism versus liberalism does not correlate perfectly with the degree to which member states abide by EU internal market and competition policy rules.

Differentiated integration in industrial policy areas is largely ‘soft’ and unofficial and comes in three forms: varying national participation in EU and other European projects; the discretion permitted in the implementation of EU legislation; and varying levels of compliance with EU legislation. Legally entrenched, multi-speed differentiation is present principally in terms of temporary derogation on a limited range of EU legislation. The explicit legal sanction of more permanent differentiation in industrial policy areas is rare. The permitted provision of State Aids to poorer regions is, potentially, one example – to the extent that this permission contributes to differentiation in national practice. The penultimate section of this chapter presents one recent legislative development that effectively entrenches differentiation in energy markets and potentially undermines market integration in this sector.

It is necessary to draw a distinction between differentiated participation and differentiated integration. The former in, say, EU-led industrial initiatives and non-EU R&D and industrial projects does not necessarily result in differentiated integration. In some cases differentiated participation will reflect existing differentiated integration in linked areas (for example, defence industry cooperation). However, in others differentiated participation will simply reflect the reality of different national economic structures. Table 21.1 provides an overview of the various policy areas that

can be considered to be part of industrial policy and the kinds of differentiated participation and integration that have arisen in these areas. Rather than consider each in turn, examples will be drawn to demonstrate different forms of ‘soft’ and ‘hard’ differentiation.

<Insert Table 21.1 here>

Non-EU Projects and Differentiation

European R&D programmes and industrial projects involving some or many (but not all) EU member states potentially contribute to differentiated integration. These include the European Space Agency (ESA), ESPRIT, Eureka, JET, Airbus and Ariane. Differentiated participation reflects principally different levels of economic development and economic structures, but also, potentially, different ideology. Wallace and Wallace (1995: 53) note that the term ‘variable geometry’ was originally used in the late 1970s in industrial policy where different member states would participate in different consortia along functional lines, especially to enhance their technological capabilities. The term was used mainly because the member states chose to invest in a policy outside regular Community action. However, the authors did not consider these projects – namely, JET, Eureka, Airbus and Ariane – to be significant examples of variable geometry because they were not ‘Communitarized’ and did not play a major part in the overall dynamics of European integration.¹ While this is a valid claim, the developing links between some of these projects and EU

policies mean that they should be considered in terms of their potential contribution to differentiated integration.

Membership in Eureka (the European high technology research coordinating agency) has, over the more than two decades of its existence, differed from EU membership. Member-state participation has varied over time depending on the projects funded. The creation of Eureka in 1985 reflects in part the ideological preference of French (notably Socialist-led) governments seeking to increase the effectiveness of state intervention through multi-national European coordination. However, while French governments (joined by the Commission) pushed for more EC R&D funding, Germany and the UK were more reluctant to expand the EC's budget (Peterson 1993). Eureka was created as an intergovernmental framework for promoting cross-border collaboration in pre-competitive research and for keeping more funding at the national level rather than transferring it through the Commission and the EU Framework Programmes.

Eureka membership presently includes all the EU member states, with the exception of Bulgaria which nonetheless possesses a national information point allowing it to participate in Eureka projects. There are an additional 13 non-EU members, including Russia and Turkey. Large amounts of public and private funding have been mobilised to support the R&D carried out within the Eureka framework. Although Eureka is not an EU programme, it has been closely linked with the EU and the objectives of the Lisbon Agenda. Most Eureka projects funded have tended to involve a limited number of big European firms (e.g. Thomson-SGS, Plessey, Siemens and Philips) – and, despite efforts to include more SMEs, the large firms tend to dominate decision

making (Peterson 1993). Most projects involve only a limited number of EU member states, and the larger member states will tend to be involved in funding more projects than others. Unlike Eureka, the European Strategic Programme for Information Technology (ESPRIT) was an EC/EU R&D programme and, from 1993, was managed by the Commission's Directorate-General for Industry. Operating from 1983-1999, Esprit facilitated a diverse range of partnerships and joint ventures among representatives of government, industry, universities, and research institutes, with differentiated levels of participation.

The impact of Eureka, Esprit and other R&D programmes upon European integration has been analyzed in terms of rejecting the old strategies of national champions, promoting close cooperation among European firms, facilitating the adoption of common European standards (thus eliminating important non-tariff barriers), and laying the basis for a lobby pushing for European market integration (Sharp 1990). Differentiated participation in these projects has also contributed to different influence in shaping certain aspects of European market integration, as well as reflecting differentiated integration into a European research community. However, differentiated participation has not contributed to differentiated integration *per se*.

There is considerable differentiation in the field of atomic energy research. All EU member states are members of Euratom. However, seven EC/EU member states have not in the past participated, or do not at present participate, in the principal centre for fundamental physics and computer science research, CERN, the European Organisation for Nuclear Research. While the industrial applications of research at CERN may be limited, CERN itself has involved significant industrial collaboration,

notably in the construction of the rapid particle accelerator. CERN was founded in 1954, and membership included all the Original Six in addition to several other European countries. Most, but not all, other European countries joined prior to their EC membership. Those member states that have more developed programmes in atomic energy research are equally those with a greater presence at CERN, and national funding contributions (on a per capita basis) have varied considerably. In 2009 eight EU member states were not members: Ireland, Romania, the three Baltic States, Malta, Cyprus and Slovenia.

Just under a third of the budget for the EC's Seventh Research Framework Programme – €2 750 million for the period 2007-2011 – is earmarked for research in the field of nuclear fission, to be carried out either by means of a programme of indirect actions or by the EU's Joint Research Centre (JRC), focusing on the safe exploitation and development of fission reactor systems, the management of radioactive waste, radiation protection and safety, and security related to non-proliferation. Nearly two-thirds of this funding will go towards research in the field of fusion energy, based on work taking place in the International Thermonuclear Experimental Reactor (ITER) project. This project in turn derives from previous work undertaken since the first EC research programme, which funded the establishment of the Joint European Torus (JET) at Culham, Oxfordshire. JET has frequently not involved all EU member states. Since 2000, the European Fusion Development Agreement (EFDA) has directed the activities of JET. With the exception of Estonia, all EU member states now participate in EFDA, although several still do not participate in JET research and development. Given the importance of nuclear research in terms of EU priorities, the differentiated participation of EU member

states in nuclear research projects can be said to contribute to differentiated integration.

The memberships of the European Space Agency (ESA) and EU have frequently not corresponded, and non-EU countries have also been members of the ESA. There is some 'multi-speed' differentiation in member state participation. In order to participate in ESA procurements and most ESA programmes, a country must sign a European Cooperating State (ECS) Agreement as a first stage of membership. While the financial contribution of such a country increases, it is still much lower than that of a full member state. The ECS Agreement is normally followed by a Plan for European Cooperating States (or PECS Charter), a five-year programme of basic research and development activities, aimed at improving a country's space industry capacity. At the end of the five-year period the country can either begin negotiations to become a full member state in the ESA or an associated state or sign a new PECS Charter. Only one of the twelve newest EU member states is at present a full member: the Czech Republic achieved this status at the start of 2009. Hungary, Poland, Estonia, Slovenia and Romania have signed ECS agreements, and Romania and Poland have signed the PECS Charter. Differing membership has an impact upon potential participation in the European space programme which covers all the activities and measures undertaken by the EU, ESA and national space organizations. The Ariane rocket system is manufactured under the authority of the ESA. While dominated by the French (the Centre National d'Études Spatiales) and the French company EADS Astrium, which is the prime contractor, a limited number of other EU member states and companies based in these countries have been involved in Ariane R&D.

Airbus, one of the world's two main large commercial aircraft manufacturers, also involves the participation of only a small number of EU member states. The bulk of Airbus staff is based at 16 sites in four EU member states: Germany, France, the UK and Spain. The governments of these countries initially developed Airbus as a consortium of publicly and privately-owned aerospace manufacturers to coordinate their R&D efforts. These companies were consolidated at the turn of the century, and since 2006 the French based-company EADS owns the entire Airbus company.

Wallace and Wallace (1995: 54) specifically list two industrial policy areas where different levels of participation have had a more direct impact upon differentiated integration: the Trans-European Networks (the TENS) and the reconfiguration of the EU member-state defence industries. The TENS were created under provisions introduced in the Maastricht Treaty (Articles 154-156 TEC) and involve EU funding for major infrastructural projects to reinforce European market integration and contribute to European social and economic cohesion. The projects under development as TENS are, by their nature, selective in membership and in competition for limited resources. Differentiation has arisen through the selection of particular projects and particular countries or groups of countries. Defence is considered below in the context of bi- and multilateral industrial cooperation because the various projects that have been developed only involve a small number of EU member states.

The Commission's cross-sector policy initiatives do not create much scope for differentiated integration. However, the seven sector-specific initiatives or actions do create scope for differentiated participation of the member states to the extent that

some member states are more involved than others by virtue of their presence in specific industrial sectors. The Steering Group of the Pharmaceuticals Forum, which held its first meeting in 2006, included representatives from only seven member states (although to ensure fairness these were representatives from recent and forthcoming Council presidencies). The High-level Group on the Chemicals Industry (meeting from 2007-09) was more exclusive and involved government representatives from only eight member states (principally the largest with a significant manufacturing presence in this sector). The Task Force on the Competitiveness of Information and Communication Technologies (meeting from 2005-06) did not include national representatives per se. However, its participants came for the most part from major corporations and organizations, effectively excluding participants from the majority of member states and almost all the newest member states.

Bi- and Multilateral Member State Industrial Policy as Differentiation

Non-EU, bilateral and multilateral industrial projects, funded by a limited number of national governments, are another form of differentiated participation. A large number of these projects have involved only France and Germany or have been led by these two countries. The impressive range of proposals over the past two decades suggests a Franco-German core in industrial policy. However, Cole's chapter demonstrates the failure of most of these initiatives, outside the realm of aerospace and defence where public procurement policies are of great importance. The recent collapse of the project to create a search engine Quaero is a good example of the limits of Franco-German bilateralism.

In defence procurement there are several examples of on-going Franco-German cooperation.² The merger of Aerospatiale-Matra (France) and Daimler-Chrysler Aerospace (Germany) in 1992 led to the development of Eurocopter that in 2000 became a subsidiary of EADS. Eurocopter produced the Tiger multi-role attack helicopter that began production in March 2003 and will be capable of providing air-ground combat support. The Organization for Joint Armament Cooperation (OCCAR) was established in 1996 to manage collaborative armaments programmes by France, Germany, Italy and the UK (joined by Belgium in 2003 and Spain in 2005). It has provided an important framework, enabling the cross-national coordination of procurement. Membership is open to other EU and NATO member states, which also have the option of participating in a procurement programme under a cooperative agreement (as is the case with the Netherlands, Luxembourg and Turkey). OCCAR has coordinated cooperation for several joint European ventures which reinforce the capacity of European states to undertake crisis-management operations within NATO/ESDP frameworks.

There are also several examples of projects not involving both France and Germany, undermining claims of a special relationship and a European 'core'. The Eurofighter alliance involves companies from the UK, Germany, Italy and Spain. The French-led 'nEUROn' UCAV (Unmanned Combat Aerial Vehicle) has, since 2005, involved the delegation of 50 per cent of the work to other European partners – Alenia (Italy); Saab (Sweden), Hellenic Aerospace Industry (Greece); EADS CASA (Spain) and UAG (Switzerland). The FSAF (Future Surface-to-Air Anti-Missile Family), launched in October 1998, resulted in the development by France and Italy of

common surface-to-air ground and naval-based anti-missile systems. The project has been developed under the Anglo-Franco-Italian Eurosam (ES) venture, established by Aerospaziale, Alenia and Thompson CSF in June 1989. Such bilateral and multilateral defence industrial projects are allowed because Treaty of Rome provisions exempted the armaments sector from Internal Market rules (Article 296b TEC).

Wallace and Wallace (1995: 54) argue that the development of Eurocorps in the early 1990s would have industrial implications which, in turn, would 'bear on the debate about the "core" group for defence'. The subsequent development of ESDP in the 1990s and 2000s and industrial developments further suggest that certain member states are more likely than others to be involved in bi- and multilateral industrial projects linked to the construction of a European military capacity. However, given that the countries involved to date in these projects are diverse, it is problematic to talk of the reinforcement of a 'core'. Franco-German bilateralism in defence industry developments has been limited. There is potential relevance of varying participation in these projects to member-state participation in European military cooperation and the construction of ESDP. However, national economic capacity and industrial strategy – as in France's refusal to participate in the Eurofighter project – is of much greater relevance. The majority of EU member states have not participated in these projects. The creation of the European Defence Agency (EDA) in 2004 (as called for under Article 28D Lisbon Treaty) has reinforced the contribution of differentiated participation in joint defence research and industrial projects to differentiated integration, to the extent that EDA promoted projects become more closely tied to the construction of European military cooperation more broadly. Membership of the EDA is not a requirement for EU member states, although all except Denmark –

which has an opt-out on the Common Foreign and Security Policy – have chosen to join. Article 28D2 of the Lisbon Treaty makes it clear that differentiated participation will shape the organization and activities of the Agency:

The European Defence Agency shall be open to all Member States wishing to be part of it. The Council, acting by a qualified majority, shall adopt a decision defining the Agency's statute, seat and operational rules. That decision should take account of the level of effective participation in the Agency's activities. Specific groups shall be set up within the Agency bringing together Member States engaged in joint projects.

Temporary Derogation as Differentiation

Legal temporary derogation is provided for either through specific legislative provisions and accession treaty provisions adopted with regard to the application of policies that have significant cost implications for industry. Present or future member states argue that factors specific to their national industry (or broader economy) justify derogation. Notably, the poorer countries of Central and Eastern Europe have argued that many sectors of domestic industry were financially unable to comply with EU environmental and health and safety regulation. Thus, for example, the 2004 accession treaties permitted a delay until the end of 2005 for the implementation of EU health and safety legislation. To provide a more specific example, temporary derogations were granted to seven of the ten 2004 applicants permitting the delayed implementation of certain provisions of the directive relating to waste electrical and electronic equipment (2002/96/EC). Existing member states have also benefited from specific provisions in EU legislation allowing for delayed implementation. The Packaging and Packaging Waste Directive 1994 (94/62/EC) allowed the then four

poorest EU member states (Spain, Portugal, Greece and Ireland) a delay to achieve the waste recovery and recycling targets. The 2004 amendment to the directive which established new targets granted a revised derogation to Ireland, Portugal and Greece.

Discretionary Differentiation

Andersen and Sitter (2006) widen the use of the term differentiated integration ‘to capture both the formal and informal arrangements for policy opt-outs as well as the differences, or discretionary aspects, associated with putting EU policy into practice’ (313). They emphasise, in effect, the heterogeneity of integration. Given that member states implement directives differently, the result can be considerable intra-sector variation. Discretionary differentiation is particularly relevant with regard to the implementation of internal market, health and safety, and environmental legislation.

There are two main sources of this kind of differentiation. First, member states can design directives to be less specific in order to allow for greater national margin of manoeuvre in implementation. Even those member states without considerable reservations about a directive may take advantage of the scope for discretion written into a directive (Andersen and Sitter 2006). When flexibility and voluntary measures replace strict requirements, the result is that states are effectively allowed – if not encouraged – to go their own way. Second, there are pressures for ‘de-coupling’ within member states, notably from regional and local governments, and institutional resistance, which can prevent governments from implementing policies that they have agreed at the EU level. Thus national governments may be committed to a directive

and its implementation, but local resistance will result in its distorted implementation. Differentiation via discretion should be distinguished from differentiation through non-compliance, although pushing the boundaries of discretion can result in non-compliance.

There are several forms of discretion found in EU legislation. In addition to deliberately vague wording, allowing for the continuation of national practice, there is discretion for national room to manoeuvre in the achievement of a broad goal (e.g. sector-based liberalization). The liberalization of the telecommunications sector can be described as an example of multi-speed differentiation. EU directives allowed member states to liberalize at their own pace. The Commission adopted a gradualist approach that allowed considerable margin of manoeuvre to member states in terms of domestic organizational solutions and the timing of liberalization (Eyre and Sitter 1999). However, in this sector a strong coalition of actors had incentives to pursue the goal of rapid liberalization in order to meet international market and technological challenges.

A third form of discretion allows exemptions from legislative requirements for specific reasons. One recent example is in the REACH directive which allows for the application of a 'socio-economic analysis' to permit derogation (Articles 62(5)(a) and 69(6)(b) and Annex XVI). To the extent that 'socio-economic analysis' might create a national bias (for example, allowing more flexible application of the rules in poorer member states), the result is scope for more patterned and permanent differentiation.

Compliance and Non-compliance as Differentiation

EU industrial policy can be described as ‘horizontal’, to the extent that policy seeks to compensate for the failure of national governments to provide open competitive markets (Nicolaidis 1993; Peterson 1996). EU competition policy is thus a core element of the EU’s industrial policy. To the extent that levels of compliance by EU member states with EU competition policy and internal market rules on the free movement of capital differ, there is persistent differentiation in industrial policy. Different national compliance levels can also reflect the persistence of different national forms of industrial policy, interventionism and protectionism. These forms include the provision of state aid, intervention in mergers, protection of sectors from foreign ownership (including the ownership of companies based in other EU member states), and the maintenance of state ownership. There are also substantial differences in terms of member-state responses to decisions on infringement by the Commission and rulings by the European Court of Justice.

<Insert tables 21.2 and 21.3 here>

Although decreasing, the provision of state aid to industry – some of which contravenes EU rules – varies considerably from country to country. Table 21.4 categorises state aid in terms of amounts provided. Sweden, Austria, Germany can be placed in the large provider category, while Britain provides relatively little. In terms of state aid for companies as a percentage of GDP (excluding agriculture, fisheries and transport), only six member states provide more than 0.6 per cent of GDP (notably, Germany, Austria and Sweden). Five provide less than 0.2 per cent of GDP

(including the UK which provided .16 per cent in 2006. There are significant differences between member states in the sectors to which they direct state aid. However, prior to the international financial crisis and recession starting in 2008, the bulk of state aid in most member states has gone to manufacturing (60 and 66 per cent in Italy and Germany, with far higher percentages in smaller member states, including Sweden). In terms of aid to SMEs allowed under block exemptions, the amounts granted by Italy far exceed amounts granted by other member states (in terms of spending as a percentage of GDP) and comprised 45 per cent of the total. As a percentage of GDP, Irish, Belgian and Czech state aid was particularly high. On pending recovery cases, Spain, Italy and Germany are the worst offenders (in terms of total number of cases), while the majority of member states (including the UK) have no cases brought against them.

<Insert Table 21.4 here>

Several EU member states intervene regularly to encourage or block potential mergers and takeovers. France, Italy, Germany and Spain have engaged in interventionism on mergers with the aim of maintaining national ownership in particular sectors. Other member states – notably the UK and the Netherlands – pursue a more *laissez-faire* position. Several member states (but not all) have outlined a range of sectors that should be protected from foreign ownership. Several national governments maintain state ownership or control (through golden shares) of companies, which is not necessarily contrary to EU rules. Despite large privatization programmes over the past two decades, France and Italy in particular have large state-owned sectors. The governments of both countries have delayed the privatisation of state-owned former

energy monopolies. National competition law (affecting the operation of companies which are located primarily in the national market and thus not subject to EU competition policy) continues to be distinct, which also reflects differing attitudes to the application of EU competition policy. Eyre and Lodge (2000) provide a detailed account of the Europeanization of competition law, describing the tension between convergence and divergence as countries have increasingly come to play a 'European melody', but with distinct 'national tunes'.

Since the launch of the Single Market Programme, the European Commission has sought to challenge public procurement by national governments that discriminate in favour of protected national firms and against foreign competitors. Total public procurement in the EU – i.e. the purchases of goods, services and public works by governments and public utilities – was estimated at about 16 per cent of the EU's GDP or €1500 billion in 2002. Its importance varies significantly between Member States ranging between 11 per cent and 20 per cent of GDP (http://ec.europa.eu/internal_market/publicprocurement/index_en.htm). An evaluation of the public procurement market demonstrates persistent differentiation. Those member states with relatively informal procurement legislation – notably Germany, the Netherlands and Denmark – before the adoption of EU directives and those which had more decentralized procurement practices (again Germany and the Netherlands) had more problems with compliance and more compliance costs. A list of infringement cases brought by the Commission against EU member states for failing to follow public procurement rules demonstrates differentiation (Table 21.5). This list provide the best indication (albeit incomplete) of different government action with regard to respecting EU public procurement rules. The trends seen in the

implementation of EU competition and internal market policy rules apply. The Scandinavian countries are the most compliant, whilst Germany and Italy have the greatest difficulty following EU rules, followed by Spain and France. Member states with strongly centralized procurement policies (like the UK or Portugal) are more likely to respect EU rules.

<Insert table 21.5 here>

Differentiation has persisted in the energy sector despite on-going efforts of the European Commission and certain member states to bring about liberalization (Andersen 2001). Article 90 of the Treaty of Rome (now Article 86 TEC) equipped the Commission with the legal power unilaterally to break up national monopolies. Some member states, notably the UK, supported the Commission's push for liberalization. Others, notably France and Germany, were sceptical if not hostile to full liberalization and the unbundling of production and supply. As a result, some member states have moved quickly towards liberalization, while others have dragged their heels. German and French governments stuck to the minimum requirements of the 1996 and 1998 directives to liberalize, respectively, the electricity and gas sectors (96/92/EC and 98/30/EC, revised in 2003), while EU-level legal action forced some action. In addition to ideological opposition to liberalization, there has been persistent domestic political opposition, with strong trade-union, party-political and public hostility – encouraged by the fear that gas and electricity prices would rise after liberalization. Third-party access to transmission networks for electricity and gas was blocked by several member states through the discretion allowed in the 1998 directive: a combination of ambiguous wording and omissions. Member states were

allowed to choose between regulated and negotiated third-party access, and to develop or maintain their national regulatory models. The Commission, encouraged by Britain and a minority of EU member states, pushed for a complete unbundling of production and supply. In several member states, public take-up of alternative energy providers has been minimal and market access restricted. Homogenous integration worked only with respect to limited policy initiatives in the energy sector such as price transparency for electricity and gas contracts.

Legislated Differentiation

In January 2008 the European Commission proposed a new directive on unbundling energy production. Previously, the Commission had demanded that energy producers sell off transmission networks. Because this demand met the intransigent opposition of several member states (the so-called Group of Eight: France, Germany, Austria, Bulgaria, Greece, Latvia, Luxembourg and Slovakia) and the EU continued to lack a clear legislative framework on energy, the Commission decided to change tack. Its proposed directive would effectively allow member states that had not decoupled to avoid doing so. Energy companies would not have to sell grids and pipelines. However, they would face tougher regulation and a requirement for more independent management. The Commission proposed the establishment of an independent system operator (ISO). Big energy companies would retain ownership of the transmission lines, but hand managing control over networks to an entirely separate operator which would be required to have a different group of shareholders from the parent company.

This proposed compromise gesture was still rejected by the Group of Eight. In June 2008, member-state governments reached a compromise, agreeing to embed into EU law the right for individual governments to choose one of three different models of unbundling: full ownership unbundling, when a parent company sells its transmission networks to a different firm; the independent system operator (ISO) option proposed by the Commission in January that allows big energy companies to retain ownership of the transmission lines, but requires them to transfer managing control over networks to an entirely separate operator (which would not share any shareholders with the parent company); and a third option – very close to the one preferred by the Group of Eight – the creation of a so-called independent transmission operator (ITO) which permits a parent company to retain ownership of transmission networks which would be heavily supervised by a national regulator. Under this new third option, the directive imposes additional requirements upon the parent company and the ITO to reinforce the independence of the latter, including a mechanism preventing top management from moving freely between a company's production and transmission wings. Furthermore, the national regulator would examine the transmission operator's development and investment plans and could demand changes.

While the new directive will bring about a change in national practice in the eight member states which have to date opposed unbundling, on-going differentiation in the organization of national energy markets and regulation has been explicitly recognised. The result is the adoption of an unprecedented piece of EU legislation which explicitly recognizes differentiation in the operation of national energy markets. Opponents of the directive have argued that it effectively endorses the practices in

certain member states which undermine full market liberalization and European market integration.

Conclusion

A complete study of differentiated integration in industrial policy would have to cover potentially all the policy areas mentioned in the introduction. Official opt-outs exist in none. On specific pieces of legislation or in particular policies, clauses may be inserted allowing for temporary derogation. These derogations are never intended to be permanent, even if they arguably demonstrate a *de facto* recognition that some member states are not really expected by the others to implement the piece of legislation in the foreseeable future. Only very recently in EU history have legislative provisions been adopted – in the field of energy market liberalization – that officially recognise differentiation in the rules that govern the operation of an industrial sector.

Varying EU member-state participation in European R&D programmes and industrial projects can contribute to differentiated integration. However, the degree to which the two are linked must be seen as limited. Some differentiation can be detected in the context of bi- and multi-lateral industrial initiatives developed by specific EU member states. Even so, the contribution of this differentiation in participation to differentiated integration is unclear. Derogations and different levels of compliance (as measured by Commission notification, court cases brought against member states and other statistics) demonstrate differentiated integration.

However, it is discretion allowed in the implementation of EU legislation that remains the greatest source of differentiation. An exhaustive study of differentiation through discretion is beyond the scope of this chapter. Further research is necessary to determine the extent to which this differentiation reflects a persistent ideological division in Europe about the meaning of market integration and the desirable nature of EU and national industrial policies, rather than temporary differences that better reflect different levels of economic development, economic structures and technical preferences.

References

Andersen, S.S. (2001) 'Energy policy: Interest articulation and Supranational authority', in Andersen, S.S. and Eliassen, K.A. (eds) *Making Policy in Europe* (London, Sage).

Andersen, S. and Sitter, N. (2006) 'Differentiated Integration: What is it and How Much Can the EU Accommodate?', *Journal of European Integration*, Vol. 28, No. 4, September, 313–330.

Bangemann, M. (1992) *Meeting the Global Challenge: Establishing a Successful European Industrial Policy*, London: Kogan Page.

European Supply Agency (2008) *Annual Report 2007*, Luxembourg: Commission, <http://ec.europa.eu/euratom/ar/last.pdf>, accessed 13 January 2009.

Eyre, S. & M. Lodge (2000) "National Tunes and a European Melody? Competition Law Reform in the UK and Germany", *Journal of European Public Policy*, 7:1, 63-79.

Eyre, S. & Sitter, N. (1999) 'From PTT to NRA: Towards a New Regulatory Regime', in: Eliassen, K.A. & Sjøvaag, M., eds, *European Telecommunications Liberalisation: Too Good to be True?*, London: Routledge, 39-52.

Gerber, D. (1998) *Law and Competition in the Twentieth Century: Protecting Prometheus*, Oxford, Clarendon Press.

Nicolaides, Ph., ed. (1993) *Industrial Policy in the European Community: A Necessary Response to Economic Integration?*, Dordrecht: Martinus Nijhoff, Norwell, MA: Kluwer.

Peterson, J. (1993) *High Technology and the Competition State: An analysis of the Eureka initiative*, London: Routledge.

Peterson, J. (1996) 'European Union Industrial Policy', in Barbour, Ph., ed., *The European Union Handbook*, London: Fitzroy Dearborn Publishers, pp. 177-186.

'Regulation (EC) No. 1907/2006 of the European Parliament and of the Council, 18 December 2006', in *Official Journal of the European Union*, L 396/1, 30.12.2006.

Sharp, M. (1992) 'Technology and the Dynamics of Integration', in W. Wallace, ed., *The Dynamics of European Integration*, London: Pinter, pp. 50-66.

Stubb, A. (1996) 'A Categorization of Differentiated Integration', *Journal of Common Market Studies*, 34, 2, June, 283-295.

Wilks, S. (1996) 'Regulatory Compliance and Capitalist Diversity in Europe', *Journal of European Public Policy*, 3:4, 536-559.

Wallace, H. and Wallace, W. (1995) *Flying Together in a Larger and More Diverse European Union*, W87 Working Documents, The Hague: Netherlands Scientific Council for Government Policy.

¹ Wallace and Wallace (1995:53) write: ‘The preoccupation belongs to the period in which the R&D and technology programmes of the EC were being developed, closely linked to groupings of countries and companies with a particular stake in specific high-tech industries. Current EU policy is more diffusely construed and the consortium principle of self including groups of countries seems less pertinent, especially given the ambivalences of European industrial policy. Some elements of the discussion linger on in other frameworks, such as the European Space Agency or Eureka. Here we should note in passing that efforts to “communitarise” these consortia have not succeeded and thus that their patterns of varied participation impinge relatively little on the discussions within the EU as such.’

² Information on bi- and multi-lateral armaments projects has been drawn from T. Dyson, ‘Differentiated Cooperation in Defence and Security Policy: Reformed Bandwagoning in the Context of Systemic Unipolarity’, paper presented at the Workshop on Differentiated Integration, Cardiff, 10-12 September 2008.