Ever Tighter Union?

Brexit, Grexit, and Frustrated Differentiation in the Single Market and Eurozone

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Abstract
Many European political leaders and observers have argued that the European Union’s multiple recent challenges call for more “differentiated integration.” At first glance the EU may seem to lend itself quite well to such an approach, with already variegated memberships in the Euro area or Schengen borderless travel zone. What proponents of differentiation tend to overlook, however, is that the Union’s core commitments are not set up to permit much internal variation at all. Indeed, in the EU’s two flagship policy areas – the Single Market and the Eurozone – the defining institutional principles rule out differentiation to a striking degree. To substantiate this claim, we show that the rules in these areas are considerably more constraining of EU member states than are analogous federal constraints within the United States of America. We then highlight how these tightly limiting principles of EU economic governance have shaped recent negotiations with Greece in the Eurozone and the United Kingdom in the Single Market. While the EU’s core constraining principles make calls for differentiation all the more comprehensible, they also underscore that differentiated options may require rather fundamental change to the current institutional status quo.

Key words: differentiation, European Union, Eurozone, integration, Single Market, United States.
**Introduction: Towards a Differentiated EU?**

Differentiation is a hot topic in the European Union today. For good reason: Greek pain in the Eurozone, the UK’s vote to leave (‘Brexit’), the reintroduction of border controls in the Schengen zone of free movement, and central European challenges to the rule of law all seem to suggest that this diverse continent demands a more variegated framework. This theme is now common even among Europhiles who long argued against a piecemeal “Europe à la carte.” When the federalist European Commission President Jean-Claude Juncker published his five scenarios for “the future of Europe” in 2017, his central option – flanked rather obviously by less plausible extremes – was titled “Those Who Want More Do More” (European Commission, 2017). A wave of related commentary argued that Europe’s likely futures entail “variable geometry” or “different speeds” (e.g. Gotev, 2017; Blockmans, 2017; Russack, 2017). In the typically pithy summary of The Economist, “Europe’s future is multi-speed and multi-tier” (Economist, 2017).

At the same time, the EU’s recent challenges suggest that differentiation may be difficult to achieve. Certainly, the EU already features “variable geometry,” with nine of 28 members outside the Eurozone; six of 28 outside the Schengen area; two non-EU members using the euro; three non-members fully inside the Single Market; Turkey inside the customs union; and a bespoke deal for Switzerland. But within the EU’s two flagship policy areas – the Single Market and the Eurozone – the dynamic of the last decade has been one of ‘ever tighter union’ with political calls for differentiation being frustrated. Crisis-struck Greece sought accommodations in the Eurozone with the backing of a clear domestic majority. Not only were its demands rejected, the Eurozone actually tightened its overall fiscal oversight. British attempts in 2015 to renegotiate free
movement in the Single Market were similarly rebuffed. Since the 2016 referendum, the UK’s Brexit negotiators have been hitting the same wall with the EU maintaining that there is “no cherry picking” among Single Market arrangements. Its “four freedoms” of goods, services, capital, and people are “indivisible” (Barnier, 2017; 2018).

This article highlights that the institutional principles of the EU’s core economic policy areas rule out internal differentiation to a striking degree. We do so by comparing constraints on EU member states to analogous constraints within the United States of America. Relative to the EU, federal rules in the American market accord much broader autonomy to differentiated state regulation even if it impedes exchange and mobility. American states are subject to much less central oversight over fiscal policy, current account rules, and structural reform than Eurozone states. After laying out this basic comparison, we show how these tight EU rules have consistently frustrated Greek and British demands for differentiation.

Our aspirations here are descriptive rather than explanatory. We lack the space to look back and explain how this tight EU union emerged. Looking forward, however, this description carries analytic implications. We do not deny that the EU’s future holds more differentiation in policy areas outside the economic core. Even inside these core areas, we do not mean to suggest that any functional or political logic makes differentiation impossible. Were EU states to start from scratch, they could surely negotiate a workable Single Market with less free movement or a Eurozone that allowed more fiscal discretion. Our point is a simple institutionalist one: EU states are not starting from scratch, and future deals in these core areas are constrained by a very anti-differentiation status quo. Loosening these constraints would require unanimous renegotiation of fundamental treaty
elements, which seems unlikely at present. This simple fact has been a rude awakening for the Greeks and the British, and even many well-informed EU actors seem not to recognize it in their own discourse on differentiation.

**Difficulties of Internal Differentiation in the Single Market and Single Currency**

Differentiation in the EU context means the existence of varying institutional rules across states that participate in some EU arrangements. Reasonably enough, most discussion of EU differentiation has focused on states entering explicitly different arrangements: to what extent have they signed up for different deals, and what different deals might they seek in the future? In this issue, for example, Sergio Fabbrini’s emphasis on “multiple unions” foregrounds sectoral variations, with contrasting logics of governance across policy areas whether or not their membership varies. Vivien Schmidt’s image of a “soft core” Europe combines sectoral variations with more variation in national memberships. Another scenario mentioned in Fabbrini’s contribution extends the combined logic to an extreme vision of “institutional pluralism” akin to James Buchanan’s model of a “club of clubs” (Buchanan, 1965). Even this radical option attracts significant attention today, including an endorsement from influential EU scholar Giandomenico Majone (2014).

However, there is another less discussed way in which arrangements among European states can vary. Whatever the sectoral and geographical variation of EU deals, such commitments can be tightly constraining – barring participating states from some range of choices and/or requiring certain courses of action – or can set looser parameters that allow for considerable national autonomy. It is not surprising that differentiation discussions have downplayed such variation, since in the abstract we might see it as
“discretion” that is separable from “differentiation.” If our goal is to understand Europe’s current challenges and possible futures, however, we think these topics must be discussed together. For us, the tightness or looseness of EU constraints is a crucial aspect of future options for differentiation.

Why? In conceptual terms these kinds of variation address the same question: to what degree does (and will) the EU allow or empower member states to do things differently? More concretely, these kinds of institutional variation belong in the same discussion because they are entangled functionally and politically. In functional terms, the more tightly EU rules constrain states in certain areas, permitting little internal variation, the harder it presumably is to negotiate gradations of participation therein. More constraining rules typically create more “cliff-edge” separation between “ins” and “outs,” limiting options for “partials.” This interaction of kinds of differentiation is easy to see in political terms. In the Brexit example, a call for differentiated membership responds to tight EU rules in the Single Market. It seems fair to say that the political actors involved in Brexit, like those who considered Grexit, perceive these kinds of variation as forming a single rough spectrum of differentiation. Tight EU rules form one pole. Increasing differentiation from that point extends from looser rules, to opt-outs, to selective partial participation (“opting in”), to the other pole of full exit.

Once we acknowledge the tightness of the EU’s core economic rules, then, we see that options for differentiation are not nearly as open-ended as much current discourse seems to suggest. In Fabbrini’s terms, our description of the Single Market and Eurozone best fits what he calls a “federal state.” These EU rules reject the “dual” conception of shared sovereignty with its members that defines Fabbrini’s model of “federal union.”

2
Schmidt’s terms, we suggest that the EU has a very hard core. While some EU policy areas are amenable to differentiation, these core rules maintain a stark separation between ins and outs on the EU commitments that matter most. As for scenarios like Majone’s “institutional pluralism,” they seem far-fetched. Indeed, his own main complaint about the EU echoes our central argument: the EU is built around what he calls “legal centralism” in the Single Market and Single Currency, with tighter rules than the more flexible arrangements of other regional organizations or Anglo-Saxon federations (Majone, 2014). Yet Majone focuses on criticizing these rules rather than explaining how they could plausibly be altered. As Frank Schimmelfennig’s contribution to this issue notes, bargaining over EU differentiation occurs within an institutional arena that strongly empowers defenders of the status quo. We can see in the Grexit and Brexit cases that even massive, democratically mandated political pressure for differentiation will tend to be frustrated in the core areas of EU economic governance.

**Single-Market Constraints on EU States in American Perspective**

Consider first a comparative US perspective on how much the EU allows differentiated member state regulations that bear on the Single Market. We begin with some broad points about current regulations on the ground and then sketch the legal, legislative, and political principles behind them. Even most EU experts do not seem to realize how much more the United States allows its states to choose to impede interstate exchange.

In *goods*, a variety of US federal agencies oversee sector-specific standards for many products – like toys, vehicles, food, alcohol, tobacco, many chemicals, and medical devices. Many goods have no federal standards, however, so states typically adopt
standards voluntarily from international standard setting bodies or professional associations. Decentralized adoptions create a varying patchwork. For elevators, for example, manufacturers must make tailored models for different US jurisdictions (Hoffmann, 2011). Even for federally-regulated goods, states can set higher standards, and no principle of “mutual recognition” exists in American law to mitigate such differences. California has its own standards for 800 substances.³ Overall the US standards landscape makes it “by far the most institutionally heterogeneous and fragmented of all advanced industrial countries” (Tate, 2001: 463). In Europe, meanwhile, states are subject to an extensive regulatory apparatus that combines harmonized standards for many goods with broad application of mutual recognition. The EU has been working for decades to cover all goods. The elevators example is typical, with a framework of standards and mutual recognition defined in the 1995 Lifts Directive (Hoffmann, 2011).

In services, nothing requires US states to recognize other states’ professional qualifications or licenses, and they generally do not (Egan 2015, 206). Apart from exceptional areas covered in a hodgepodge of state-to-state agreements, even experienced architects, lawyers, electricians, contractors, or hairdressers typically start from zero when qualifying to practice in another state. Temporary provision of interstate services (where someone licensed in one state sells services in another) is impossible: providers must be fully licensed in each state to practice even for one day. The EU, on the other hand, has an elaborate regime that generally requires recognition of other states’ qualifications and licenses. Each member state must also maintain an online “Single
Point of Contact” where outside providers can receive any authorizations necessary for temporary provision of services or establishment of a business.

In the special area of public procurement, which combines goods and services, US states are routinely protectionist. Forty-seven states award preferences to in-state providers. A common format is a 10 percent advantage for locals in all public tenders. Another is to require use of local workers. Some laws set outright bans: Pennsylvanian agencies may only buy coal in-state, period (Hoffmann, 2011). In the EU, on the other hand, states must tender all but small or specially exempted contracts EU-wide and cannot discriminate by nationality. As of 2018, all tenders over the threshold must be advertised Europe-wide through single national websites.

Behind these regulations on the ground stand different legal principles, despite constitutional-level foundations that are similar in spirit. The EEC treaty of 1957 bans “[q]uantitative restrictions on imports and all measures having equivalent effect,” and further commits member states to the “abolition… of the obstacles to free movement of persons, services and capital,” with possible exceptions for reasons of public policy, public security, or public health (Article 3). The American Commerce Clause phrasing is much vaguer – authorizing the federal Congress “to regulate commerce… among the several states” – but all sources agree that the point of the Clause was to authorize federal action to maintain free-flowing interstate commerce. Even conservative “originalists” like Robert Bork point out that “given the text of and purpose behind the [Commerce] Clause, Congress certainly has the power, at a minimum, to displace state laws that discriminate against interstate commerce, either explicitly or implicitly” (Bork and Troy 2002, 852).
In both the US and the EU courts have played a major role in interpreting these constitutional mandates. The US Supreme Court built up important federal powers through the Commerce Clause. Early on it recognized a “dormant Commerce Clause,” giving federal courts the ability to strike down barriers in state laws even without Congressional action. Later the mid-20th century Court broadened its interpretation of the Clause to authorize federal regulation on every conceivable aspect of the economy. Yet these moves did not tightly constrain state-level policies that might impede commerce while pursuing other goals. The dormant Clause has only been invoked consistently to bar purposeful interstate discrimination – like bans on out-of-state wine orders in *Granholm* (2005) – while allowing many other policies that obviously impede interstate commerce.\(^4\) The scope of the Clause was extended mainly to permit progressive federal policies, not to restrict a wider range of state policies. Another line of jurisprudence exempts public procurement entirely from the Commerce Clause, authorizing explicit protectionism in state purchasing (Julander, 2002).

In the EU, the ECJ has set limits on a far wider range of national laws. In goods, the 1974 *Dassonville* ruling found that the treaties forbade “[a]ll trading rules enacted by Member States which are capable of hindering, directly or indirectly, actually or potentially, intra-Community trade” (Weiler 2000). In services, cases from *Van Binsbergen* (1975) to *Säger* (1991) and *Gebhard* (1995) established similarly that member-states could not in any way “impede” or even “render less attractive” cross-border provision of services. Exceptions are allowed, but state policies that impede interstate mobility must be necessary for clear policy imperatives, non-discriminatory, suitable to obtain their goal, and proportional.\(^5\) Overall, the EU subjects its members to a
strong legal presumption of full and automatic openness to other member states’ citizens and firms, hemming in options in a huge range of policy areas.

These US-EU differences are even more striking when we move from law to policy. In the US, Congress has used its legislative authority to “preempt” state laws in many areas, but rarely in the name of reducing interstate barriers. Such concerns have been prominent in finance, like in the 1994 opening of retail banking, and partly relevant to federal laws in transport and telecommunications. But most modern preemptions relate to progressive concerns like food and drug safety, the environment, or labor conditions. They may harmonize diverse laws across the states, but their goal is not to facilitate interstate exchange (Buzbee, 2008; Epstein and Greve, 2007). For example, the current Republican-held Congress has pursued a wide-ranging agenda of loosening or removing federal regulations, with no attention to interstate barriers whatsoever.\(^6\) GOP leaders argue for “relief” from federal requirements rather than new federal rules to promote interstate openness.

By contrast, as any student of EU politics knows, the past thirty years have seen a flood of legislation to translate the ECJ’s legal parameters for the Single Market into active policy. Rulings like \textit{Dassonville}, \textit{Van Binsbergen}, and \textit{Cassis de Dijon} (1979) laid the foundations for the 1986 launch of a torrent of directives in the “Single Market 1992” program. The 1989 case \textit{Rush Portugesa} facilitated “posting” of workers to other states while regulating them under home-country rules, leading to a legislative attempt in the Posted Workers Directive of 1996 to limit circumvention of tougher labor regulation and costs in receiving countries. But since the directive was passed under treaty rules on “freedom of services,” the ECJ later interpreted it in ways that constrained receiving-
country options in the so-called “Laval quartet” of cases in 2007-8 (Davies, 1997; Barnard, 2008). Meanwhile a “big bang” in liberalizing services jurisprudence in the early 1990s (Säger, Gebhard, and other cases) set the stage for generalized services liberalization, which became the main Single Market legislative focus by the turn of the millennium (Hatzopoulous, 2012). The results were the Professional Qualifications Directive of 2005 and the Services Directive of 2006 (De Witte, 2007; Nicolaidis and Schmidt, 2007). Major legislative action in these directions continues today, despite the EU’s recent struggles. Active proposals seek to extend and enforce rules on services, procurement, company law, and digital markets.

Lastly, it is crucial to note a level of prevailing discourse about internal-market constraints that supervenes on these regulations, legal rulings, and legislative acts. Thought the US federal government could plausibly justify a “Single Market project” on the basis of its Commerce Clause powers, no such concept is present in American discourse today. At most American elites see Commerce Clause considerations as one legal and political factor among many, to be considered as particular policy debates arise. In the EU, prevailing discourse portrays efforts to establish the “four freedoms” as the *raison d’être* of the institutional system. For example, the *Financial Times* ’ Wolfgang Münchau wrote recently (Münchau, 2017),

... the very essence of the EU are the four freedoms: of movement for goods, services, capital and people. The four freedoms are to the EU what golf is to a golf club. You can play golf, watch others play golf, talk about golf, or join me at the 19th hole. But you cannot turn the golf club into a bingo hall unless everybody else agrees with you.

Münchau’s language parallels EU leaders’ discourse about the Single Market’s “indivisibility.” This is not a legal concept; commitments to each of the “four freedoms”
are certainly well established, but arrangements across them have always varied, and no formal commitment requires otherwise. Nor does any economic logic dictate that aspects of market openness must go together (Sinn, 2017; Kohler and Müller, 2017). But the spirit of the treaties, as interpreted by the ECJ, enacted in legislation, and rehearsed in EU rhetoric, sets the political goal of automatic openness. Exchange and mobility within the Single Market should be fully automatic, with no controls whatsoever, except where the EU itself authorizes specific exceptions (Kelemen and Schmidt, 2011). This understanding of the goal of the Single Market steels EU leaders’ resolve – and, in more instrumental fashion, shields them rhetorically – to resist differentiation of Single Market constraints.

*Single-Currency Constraints on EU Member States in American Perspective*

Differentiated membership of the Eurozone is the single most salient and consequential sort of differentiation in the EU, as the existing literature emphasizes at great length (Dyson and Marcussen 2010; Schimmelfenig and Winzen, 2014; Winzen, 2016). When we focus on the policy differentiation available to Eurozone members in comparison to analogous economic autonomy for American states, however, the EU again looks remarkably constraining. This has especially been the case after the multiple institutional innovations introduced during the Eurozone’s sovereign debt crisis, not least the ratification of the Fiscal Compact (the “Treaty on the Stability, Coordination, and Governance in the Economic and Monetary Union”) in 2012. Furthermore, it is worth noting that the EU constraints on national fiscal policy exist without the American advantages of sovereign debt pooling, a central bank that can serve as a real lender of last
resort, and a powerful federal government’s fiscal policy that can act as a countercyclical force (Matthijs and Blyth, 2015: 252).

Under the American Constitution, the various states retain all sovereign powers that are not explicitly delegated to the federal government. States are barred from taxing foreign trade and interstate commerce, but otherwise retain sovereignty over taxes and spending. Both federal and state governments typically impose income and corporate taxes, though multiple states impose no income taxes. In the 1840s and 1850s, American States adopted “balanced budget rules” in response to multiple episodes of bond defaults and financial stress, but not as a disciplinary device from the center. The norm of balanced budgets is “neither a ‘clause’ in the US Constitution nor a provision of federal law” (Henning and Kessler, 2012: 12). As Federico Fabbrini notes, “each state opted for the “golden rule” through political debates that were largely autonomous” and it did not appear that these were even promoted by the federal government (Fabbrini, 2013: 30). As a result, the modus operandi and strictness of budgetary rules vary greatly across states. Today, Vermont is the only state without any kind of balanced budget rule. There is no such thing as federal oversight, let alone control, over state budgets.

At the beginning of the American Republic, the federal government mutualized all existing state debt incurred during the revolutionary wars with Britain in 1790, at the insistence of Treasury Secretary Alexander Hamilton (Matthijs and Blyth, 2015: 251). Later, a “no-bailout” norm was established in the 1840s when Congress rejected the assumption of debt for several years and, as a consequence, many states defaulted on their debt. Although there is still no formal ‘no-bailout clause’ in the US Constitution, there has been no federal bailout since the mid-19th century (Henning and Kessler 2012).
But states were always allowed to default on their debt while staying within the American currency union. While state spending typically ended up being pro-cyclical, the federal government provided macroeconomic stabilization during recessions. As Henning and Kessler note, this federal stabilization, along with direct federal subsidies to state programs, rendered pro-cyclical spending and balanced budget rules at the state level much more palatable. The fact that the federal government alone was responsible for stabilizing and bailing out banks also contributed to the feasibility of balanced state budgets (Henning and Kessler, 2012).

When the euro was created in the early 1990s, the architects of the single currency gave it a strong independent central bank after the German model (the Bundesbank) and established an official ‘no bailout’ rule. The governing framework for fiscal policy – as agreed to in the Stability and Growth Pact (SGP) – put in place simple rules to avoid any active governance as much as possible. As is well known, the SGP included a 3 percent deficit floor and a 60 percent debt ceiling. However, this setup proved to be largely inadequate in governing euro members’ fiscal and financial imbalances, which resulted in the Eurozone debt crisis in 2010. While the crisis called for action – including bailouts of debtor member states in the ‘Southern’ periphery – creditor member states in the ‘Northern’ core only allowed this on the strict condition that financial assistance would be accompanied by much more intrusive and active oversight of all member states’ fiscal policies. The euro crisis hence saw a flurry of legislative activity on the fiscal side of Eurozone governance (Matthijs and Blyth, 2015; 2018).

The six-pack, two-pack, and Fiscal Compact were all introduced and served to further limit member states’ discretion over fiscal policy, introducing quasi-constitutional
balanced budget rules, and giving the European Commission additional powers in approving (and vetoing) national budgets before they were even voted on by national legislatures, through what is known as the “European Semester” (Matthijs, 2017b). As Fabbrini (2013: 32) observes, there is a “paradox in the new constitutional architecture of the EMU” in that “EU member states have willingly refused to embrace a U.S.-like federal model […] on the assumption that this was too restrictive of state sovereignty” while “they have established a regime that is much less respectful of state fiscal sovereignty than the U.S. one.” Additionally, unlike the hands off approach the US federal government has towards highly indebted states, the Eurogroup – led by Germany – would not allow a member state to fully default on its sovereign debt held by other EU member states or central EU bodies while still a member of the Eurozone, as in the case of Greece described below.

When it comes to structural reforms, especially in the countries that were bailed out but also in other highly indebted member states such as Italy, the euro’s central governing institutions – the European Commission and the European Central Bank (ECB) as members of the troika – were profoundly involved in making the reforms an implemented reality. Even Martin Sandbu (2015: 130) of the Financial Times, a staunch defender of the euro, refers to the troika’s policies in Greece as the “tyranny of technocracy” which served to “infantilize the Greek body politic” with its mandatory cuts in public services and reform measures in the labor market and sheltered services sectors. The ECB also largely overstepped its mandate when its president at the time, Jean-Claude Trichet, sent classified letters to Italian and Spanish Prime Ministers Berlusconi and Zapatero in the summer of 2011, asking for steps like large scale privatizations, the
liberalization of their countries’ labor markets and professional services sectors, pension cuts, and product market reforms. It was understood that these were strict conditions for the ECB’s intervention in those countries’ sovereign bond markets (Matthijs 2017b: 286).

To put today’s Eurozone reality in American perspective a bit more bluntly, it is simply unthinkable that California, Massachusetts or Texas would have to send in their annual state budgets for federal approval before having it debated and voted on in their own state legislatures. Furthermore, the idea that an unelected bureaucrat residing in Washington, DC could actually veto their budgets borders on the absurd. In similar fashion, the suggestion that the Chairman of the Federal Reserve Board could send secret letters to the governors of Wisconsin, Florida or Illinois, giving them a laundry list of structural reforms to enact in return for direct liquidity support, is as far removed from American political reality as one can possibly imagine.

Like the discourse on the ‘indivisibility’ of the single market’s four freedoms, the prevailing discourse on the Eurozone’s principles defines tight fiscal constraints as integral to the logic and the integrity of the single currency. From its origins Eurozone discourse has stressed that monetary integration across a heterogeneous continent must be exigent, not indulgent, to encourage increased competitiveness across the member-states. As German Chancellor Angela Merkel put it in the spring of 2010: “The rules must not be oriented toward the weak, but toward the strong. That is a hard message. But it is an economic necessity.”

It is no secret that this disciplining discourse reflects the preferences of Germany and other northern European governments, but in such a densely and explicitly institutionalized arena, it is not simply German power that preserves these constraints.
The understanding that participation in the euro means fiscal constraints – upgraded since 2010 to establish that oversight applies even more strictly to countries in trouble – is built into the rules and constantly rehearsed in the rhetoric of Eurozone officials. An institutional system that can only be changed by unanimity further empowers those who would defend this highly constraining status quo against differentiation.

**Frustrated Demands for Differentiation from the EU’s Core Commitments**

What does it look like when the EU’s tight constraints in its core economic areas generate and thwart strong national demands for differentiation? This is the core storyline of two of the EU’s biggest internal conflicts of the past decade: Greek attempts to survive a sovereign debt crisis in the Eurozone, and British attempts to renegotiate its participation in the Single Market. Despite explicit democratic support for national governments’ demands in both cases, EU leaders have consistently and successfully defended extremely sharp, “cliff-edge”-style lines between in/out scenarios for these uncomfortable members. EU leaders insisted almost ad nauseam that doing otherwise would eviscerate the founding principles of the EU’s commitments. We show below how EU officials’ bottom lines – non-negotiability of national fiscal constraints in the single currency and ‘indivisibility’ of the single market – systemically frustrated Greek and British demands for differentiation.

**Differentiation Frustrated in the Eurozone: The Case of Greece**

Much of the literature on the Greek debt crisis focuses on Germany’s role in making an example of Greece by strictly enforcing the single currency’s rules (see, for example,
Newman, 2015; Jacoby, 2015; Matthijs 2016). German power is indeed critical to the story, but Berlin was also on very strong institutional ground in insisting that EU rules allowed little room for discretionary policies in Greece. Furthermore, the real consequence of the crisis has been to greatly extend fiscal and structural constraints on public policy to every Eurozone member state, not just Greece. The EU would follow the German line and make it clear that the only way member states in trouble could remain in the Eurozone was by accepting harsh fiscal constraints and intrusive oversight in return for a financial rescue.

As is well known, Greece faced vastly increased European central powers in the form of “troika” supervision and draconian bailout terms starting in 2010. When the Greek economy continued to nosedive over the following years,9 Greek citizens increasingly demanded more democratic input into their own economic policies. Calls to negotiate better terms with creditors eventually found a voice in the program of the new hard-left Syriza movement led by firebrand Alexis Tsipras. Syriza then swept the January 2015 parliamentary elections.

Room for maneuver within EU rules – differentiation – was the core of Syriza’s program. In its Thessaloniki Program, the party had promised voters a clear choice between “European negotiation by a Syriza government, or acceptance of the creditor’s terms […] by the [previous] Samaras government” (Syriza, 2014). Published in September 2014, the program demanded significant debt relief, in the form of a debt write-off similar to the one Germany received in 1953, a “growth clause” for debt refinancing, a grace period for debt servicing and much more flexibility of the SGP. Syriza’s manifesto also pledged to replace the Memorandum agreed between the previous
government and Greece’s creditors with a new “National Reconstruction Plan.” Some of the measures proposed in this plan, such as the reinstatement of the minimum wage and the country’s collective bargaining framework, were designed to explicitly reverse Memorandum policies.

At first, the Greek reform proposals put forward in the spring of 2015 remained within the spirit of the Thessaloniki program, even though there were already some notable deviations. Without suggesting a debt write-off, two proposals written in May and June 2015 asked for other debt relief measures as well as demanding an end to the IMF’s involvement. Red lines were drawn at further pension cuts and the proposals insisted on collective bargaining and higher minimum wages. To still meet the creditors’ demands for prudent economic and fiscal policy, the Syriza government proposed economic measures such as limits on early retirement, further deregulation of product markets, conditional privatization, and the creation of an independent tax authority. With the June proposal, Finance Minister Yanis Varoufakis hoped to achieve a compromise by suggesting stricter measures such as higher health care contributions for pensioners, as well as primary surpluses much closer to the creditors’ demands.

Instead, the European Commission, IMF and ECB presented their own demands for extending the bailout deal and freeing up €15.5bn of fresh liquidity to avoid a Greek default. They pushed for further spending cuts, lower pensions and a wider VAT base and outright refused any debt relief measures (European Commission et al, 2015). Unwilling to accept these conditions, the Greek government rejected the creditors’ June offer. In the resulting absence of emergency financing, Athens had to introduce capital controls on June 29 and defaulted on an IMF loan the following day (European Commission 2015a;
On July 5, a referendum was held on whether Greece should accept the creditors’ bailout conditions. It resulted in a resounding oxi (or no) – 61% of votes were cast in opposition to the bailout conditions and not a single Greek region voted in favor (Arnett and Galatsidas, 2015). Clearly, the Greek public still held on to its demand for temporary deviation from the Eurozone’s governing rules that had paved Syriza’s path to power half a year earlier.

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<td><strong>Primary Surpluses</strong></td>
<td>2015: 0.8 / 0.6% 2016: 1.3% 2017: 3.9% From 2018: 2.3.5%</td>
<td>2015: 1% 2016: 2% 2017: 3% From 2018: 3.5%</td>
<td>2015: -0.25% 2016: 0.5% 2017: 1.75% From 2018: 3.3%</td>
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<td><strong>Debt Repayment</strong></td>
<td>-“European Debt Conference”; -Growth indexation &amp; Grace period; -QE: direct sovereign bond purchases.</td>
<td>-Schemes to swap ECB held debt with EFSF/ESM loans; -Further debt extension and GDP growth-index debt owed to GLF &amp; EFSF; -End IMF lending</td>
<td>-Three year ESM loan program; -No concrete commitments to longer grace or payment periods; -No nominal haircuts; -Continued IMF assistance.</td>
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<td><strong>Economic Reforms</strong></td>
<td>-Humanitarian measures; -More progressive income and property taxes; -Raising higher minimum wage, employment rights &amp; collective bargaining.</td>
<td>-Conditional privatization; -Collective bargaining &amp; gradually restoring minimum wage; -Limit early retirement, recapitalization of social security and pensions, no cuts; -Liberalizing product markets; -Fiscal Council.</td>
<td>-Coal’d extensive privatization with independent fund; -Tax reform including VAT &amp; reversal of prior income tax reform; -2010-2012 pension reforms back + compensate for 2012 court ruling against pension cuts; -Review and reversal of prior labor market reforms &amp; product market liberalization; -Long-term comprehensive Social Welfare Reform; -Fiscal Council + quasi-automatic spending cuts.</td>
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Despite the public’s clear-cut rejection of the creditors’ proposal, Greece had little room to implement different policies. With the EFSF program having expired on June 30, the Greek government was forced to request stability support from the ESM before a longer term agreement could be reached. In its formal request of July 8, followed by a more detailed list of policies submitted on July 9, Tsipras’ government begrudgingly pledged to accept the surplus targets demanded by its creditors and implement far-reaching tax and pension reform, much of which crossed its previous red lines.
Yet, even these new proposals did not go far enough for some members of the Eurogroup, notably Germany. On July 10, the possibility of Greece leaving the Eurozone – “Grexit” – was first seriously proposed in a German government non-paper. Complaining that the reform concessions made by Greece were insufficient, Wolfgang Schäuble’s Finance Ministry listed two conceivable options: Greece could present “radically improved proposals” or it could take a “time-out” from the Eurozone with possible debt-restructuring. Debt-restructuring, the paper argued, was not compatible with Eurozone rules. In other words, Germany insisted that Eurozone rules defined a “cliff-edge” separation: either submit to strong constraints or leave the euro.

Two days later, eleventh hour negotiations at a summit of Eurozone leaders in Brussels were to decide about Greece’s Eurozone future. The Schäuble proposal made it into the Eurogroup’s position paper and Greece was asked to implement more draconian reforms before negotiations for a new ESM loan could even begin. Absent an agreement, the option of an at-least temporary “Grexit” was now on the table (Kwasniewski, 2015). By the end of two high-stakes days of uncertainty, a preliminary agreement emerged: Greece would receive a bridge loan and negotiations for an ESM loan could begin. In return, Tsipras’ government would have to reverse or compensate for much of Syriza’s labor market and pension reforms, introduce quasi-automatic spending cuts to make sure it met its primary surplus targets, and accept continued IMF assistance. A debt haircut was ruled out and no concrete commitment to debt relief was made (Euro Summit, 2015).

With the threat of Grexit looming, the Tsipras government had accepted even more punitive reform measures than those rejected by the Greek citizenry only eight days prior. The eventual new Memorandum of Understanding for the ESM loan, which was
finalized on August 19, came with further strict conditions, such as the reversal of Syriza’s previous tax reforms, and failed to provide the debt relief Syriza had fought so hard to get. Only the primary surpluses for 2015, 2016 and 2017 were brought back to more realistic levels, after the troika took into account the fact that the Greek economy was projected to shrink by another 3 percent in 2015, instead of growing by 2.5 percent as projected back in the Autumn of 2014 (Merler, 2015).

The negotiation outcome revealed the striking power imbalance at play. While the other Eurozone countries seemed no longer afraid of Greece exiting the single currency, Greece itself saw its future firmly within the Eurozone. Not only would introducing a new currency be devastating for Greece’s economy, Greek public opinion remained strongly in favor of keeping the euro. According to Yanis Varoufakis, he indeed proposed measures that might have triggered Grexit the day after the Greek referendum to put pressure on its creditors. However, Tsipras’ inner cabinet voted him down, causing his resignation on July 6 (Lambert, 2015). Overall, Syriza’s attempt at achieving meaningful differentiation within the single currency had been systematically thwarted by EU central constraints. Unwilling to take the exit option, Greece was forced to comply.

_Differentiation Frustrated in the Single Market: The Case of the United Kingdom_

With the euro crisis smoldering in the background, David Cameron announced in January 2013 that he would hold a referendum on the UK’s EU membership if his party won a majority at the next general election (Matthijs, 2013). He hoped to appease Eurosceptic backbenchers while staving off the electoral threat from the far-right UK Independence Party (UKIP). The Conservative’s victory in May 2015, set in motion a series of events
that eventually resulted in a two-year process to negotiate a British EU exit (‘Brexit’).

Prior to holding the referendum in June 2016, the Conservative Prime Minister attempted to renegotiate the United Kingdom’s existing terms of membership in the European Union – in keeping with the promises laid out in the Conservative Party manifesto that laid the foundations for victory in the 2015 UK general election.

One of the main worries the Cameron government addressed during the renegotiation was the economic governance of the Eurozone and its impact on non-Eurozone members. In this area, it was able to achieve a symbolic compromise. Even that was too much when it came to other key concerns – renationalizing EU competencies and restricting free movement of labor. The deal David Cameron finally negotiated fell well short of the stated aims of powers flowing back to national governments and radically reduced migration inflows. Like with the Greeks in the Eurozone, the EU pushed British demands to a cliff edge: only by leaving the Union could the UK regain control over free movement and increase its national sovereignty.

Over the two years prior to the official renegotiation of the UK’s membership terms, the Tories’ demands on economic governance took shape, first in their 2015 election manifesto and then in David Cameron’s letter to the EU requesting the renegotiation. HM government asked for safeguarded access to the single market, no financial liability of non-Eurozone countries for measures to support the single currency, changes such as the introduction of a banking union remaining voluntary for non-Euro countries, as well as a formal recognition of multiple currencies within the EU. The one point of contention was France’s worry that Britain was trying to win exceptions to EU
rules for the City of London. This resulted in a line emphasizing the “level-playing field” for financial institutions within the internal market in the final agreement.

Clawing back powers from the EU proved much more difficult. Doubt about the feasibility of treaty change that might meaningfully limit the EU’s central authority emerged immediately. In December 2012, President of the European Council Herman Van Rompuy warned that “cherry picking” could “cause the EU to fall apart” and voiced doubts over treaty change after years of crisis (Traynor, 2012). In 2013, President of the European Commission José Manuel Barroso declared that renationalizing competences of the EU was “doomed to failure” (Waterfield, 2013). By June 2015, even David Cameron had to admit that treaty change would be unlikely prior to the EU referendum (Cameron, 2015a). In the absence of such change, all the UK could achieve in its negotiations was a red-card mechanism in which 55 percent of national parliaments could jointly block commission proposals. It also gained symbolic recognition that the UK did not have to strive for an “ever closer union.”

For those who wanted to see the UK remain in the European Union, the country’s inability to limit immigration under the rules of free movement was even more damaging than the lack of competencies flowing back. Since 2013, migration and free movement had become increasingly toxic in the British political debate. Against the repeated promise of the Tory government to limit migration to “tens of thousands,” net migration rose to over 300,000 in the years of 2014 and 2015 (ONS, 2018). The prospect of Romanian and Bulgarian citizens receiving unlimited access to free movement in 2014 sparked calls to delay their ‘right to work’ by Tory MPs and led David Cameron to rush in measures that would limit migrants’ immediate access to benefits (Grice, 2013).
Former Prime Minister Sir John Major openly floated the idea of a short-term cap on the freedom of movement – one of many demands for caps and emergency breaks on migration put forward during that period (BBC, 2014).

At the European level, such proposals met heavy resistance. Martin Schulz, the President of the European Parliament, proclaimed that the principle of free movement was “not up for negotiation” (Withnall, 2014). Meanwhile, Barroso entered into a war of words with Tory MP Grant Shapps and David Cameron after telling the BBC that there was “no possibility of the UK reducing the number of immigrants from EU to UK” (McSmith, 2014). Restricting free movement was a red line the EU and its member states were unwilling to cross, even if that meant risking Brexit: A report in 2014 suggested that the German Federal Government had started considering Brexit a real possibility and regarded a quota on EU migrants as a “point of no return” (Spiegel, 2014).

While the UK government wanted to radically reduce immigration, it was also one of the staunchest proponents of an integrated single market. In light of EU opposition, David Cameron decided against proposing a cap on migrants. Instead, he focused on restricting migrants’ access to the UK’s social security system, fighting abuse of the system such as sham-marriages and restricting access to free movement in future rounds of accession (Cameron, 2014).

The latter two measures were already available to the UK before renegotiation took place. The most significant changes proposed were therefore to limit EU-migrants’ access to in-work benefits and to prohibit sending child benefits abroad. Although this was already a far cry from introducing caps or emergency breaks, it still proved to be the main stumbling block in the renegotiation, as the Visegrad countries were weary of any
form of discrimination against their citizens (Visegrad Group, 2015). After two long days of negotiation, the eventual compromise that emerged from the EU summit was much weaker than David Cameron’s proposals. Child benefits could still be sent abroad, but may be indexed by the receiving country’s living standards. In-work benefits would be phased in over four years rather than withheld for a full four years after arrival. Even this could only occur under a seven-year “emergency break.” To add insult to injury, the existence of an actual emergency had to be determined at the EU level. This deal was unlikely to deliver the reduction in immigration that the Conservatives had promised.

Since the UK voted to leave the European Union four months later, the agreement Cameron renegotiated never came into force. After ‘leave’ narrowly won the referendum, Cameron resigned and Theresa May was left to pick up the pieces as the new Prime Minister. The next two years would display even more starkly how difficult it is to achieve differentiation within the single market, even for a major EU member willing to contemplate a “cliff edge” withdrawal.

Boris Johnson’s initial proposal to have “access to the single market with limited migration” in June 2016 was quickly rebuffed by Angela Merkel who said in the Bundestag two days later that the Brexit negotiations would not be a “cherry-picking exercise” and that the UK could only enjoy access to the single market if it accepted “the four basic European freedoms – that of people, goods, services and capital” (Johnson, 2016; Merkel, 2016). In her Lancaster speech in January 2017, May suggested that the future UK-EU relationship would be shaped by an agreement that could take some elements of current single market arrangements, like on the export of cars, or the freedom to provide financial services across borders (May, 2017). Michel Barnier quickly
responded that there could be “no cherry-picking” from the single market by the UK in the upcoming talks (Barnier, 2017).

A month after the UK triggered Article 50 of the Lisbon Treaty on March 30, 2017, which formally notified Brussels of its desire to leave the EU, the European Council responded with its official negotiation stance in which it stated that “preserving the integrity of the Single Market excludes participation based on a sector-by-sector approach.” It went on to say that it “welcomes the recognition by the British government that the four freedoms of the Single Market are indivisible and that there can be no “cherry picking”” (European Council, 2017). A year later, in her Mansion House speech on the future of UK-EU relations in March 2018, Theresa May once again repeated that the UK would be leaving the single market, wanted freedom to negotiate trade agreements with the rest of the world, but would also like to continue its frictionless border with the EU (May, 2018). One senior EU official commented in the Financial Times shortly after the speech: “Cake, more cake and buckets of cherries. Nothing concrete on how leaving the customs union and single market would attain the goals she wants” (Parker and Barker, 2018).

In the UK government’s so-called Chequers Plan in early July 2018, the May government agreed to a free trade area for goods, de facto committing to staying in the Single Market for goods only, but expressing its desire to have different arrangements for services and also to control immigration (HM Government, 2018). Michel Barnier, speaking at the US Council on Foreign Relations in New York once again responded in kind: “Everybody will understand that we will protect the single market which is based on the indivisibility of what we call the four freedoms, of movement for people, goods,
services and capital. […] They know the rules. They know the indivisibility of the four freedoms” (Barnier, 2018). By September 2018, during an informal EU summit in Salzburg, Theresa May was surprised to find her effort to pick apart the four freedoms rebuffed by a united front of 27 EU leaders. Donald Tusk restated the basic dynamic of the past several years to sum up the general consensus: “There are some areas where we are not ready to compromise, on our four fundamental freedoms, the single market, and this is why we remain skeptical about the Chequers proposals.”

Conclusion

We want to be clear that we do not mean to dismiss the notion that the EU’s future will likely include more differentiation. Our point is simply that useful analysis of such options must begin by understanding what variation is permissible within current EU rules, and thus what exactly would need to change to open new room for more variation in national policies. Differentiation in the Single Market and the Eurozone may be possible – there is nothing immutable about the existing rules – but pursuing it in ill-informed ways is a recipe for disaster. Just ask Greece’s Alexis Tsipras or Britain’s brash band of Brexiteers, neither of whom understood exactly what they were dealing with.

We can have some sympathy for their mistakes, since it is easy to exaggerate how much the EU is a smorgasbord of flexible policy collaborations. Hold-outs, opt-outs and exclusions from the Eurozone and Schengen, together with the transitional statuses of newer and prospective members, can make the EU seem like a bewildering mix of ‘acronymed’ memberships that states mix and match at will. More generally, the fact that the EU is legally an international organization still places it in a conceptual category that
even well-informed elites assume to be defined by its flexibility: ultimately nation-states will do what they will and as they please in diplomatic relations. Prominent academics have worked very hard to encourage this view of the EU (e.g. Moravcsik, 1998, 1999, 2002).

But this has not been an accurate picture of the EU for a long time (if ever). It was explicitly created to be different from international organizations, with unprecedented emphases on supranational authority and automatic interstate openness. A ratcheting construction process built a remarkably tight and binding framework on these foundations, with a series of boosts from pro-integration leadership (Parsons, 2003) and an entrepreneurial Commission (Jabko, 2006), together with crucial legal dynamics of “integration through law” (Cappelletti et al, 1986; Augenstein, 2012). Membership expanded as this process developed, such that growing authority was extended over a far more heterogeneous space. In both southern and eastern Europe, this extension was often portrayed as desirable in itself, with EU accession pursued explicitly to leverage a wide range of economic and political reforms. The original members also often found themselves supporting more EU authority, despite their own misgivings, because enlargement to more diverse members implied more oversight and more support.

Together these dynamics produced the core EU features we have described: an international organization that sets tighter constraints on states’ economic policies than does the federal government of a nation-state like the US. They also provoked the widespread calls for differentiation that we hear today. In order to find negotiated paths to workable and legitimate responses, Europeans must start by acknowledging more
clearly the distinctively integrated institutions that they have built. Rather than ‘unity in
diversity’ they have ended up with an ‘ever tighter’ union.
Notes

1 Montenegro and Kosovo use the euro; Iceland, Norway, and Liechtenstein are in the Single Market.
2 For a related discussion, see Schütze, 2009.
3 See the website of the private American National Standards Institute. Its page on state variations (https://www.standardsporal.org/usa_en/key_information/state_level.aspx.) explains, “The hallmark of the United States standardization and conformity assessment systems is its decentralized nature. In large part, this defining characteristic is a product of the United States’ decentralized federal governmental structure organized to balance power with individual U.S. state governments.”
4 The Court has often suggested that it also employs a “balancing” logic to evaluate whether a restriction on commerce is justified by its local benefits, but Donald Regan (1986) argues compellingly that this is so inconsistently applied that the effective logic focuses on purposeful protectionism.
5 These criteria are known as a “Gebhard test” in services, and are similar in goods.
6 See the Brookings Institution’s “tracker” of deregulation under Trump at https://www.brookings.edu/interactives/tracking-deregulation-in-the-trump-era/.
8 As quoted in Mathijs 2016: 375
10 From May 2015 to November 2015, the Eurobarometer measured an increase in support for membership in the Economic and Monetary Union.
11 As reported in the Financial Times: https://www.ft.com/content/9099a1a8-bcda-11e8-8274-55b72926558f
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