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ORIGINAL ARTICLE

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 USA. We then highlight how these tightly limiting principles of EU economic governance have shaped recent negotiations with Greece in the Eurozone and the UK 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.

Keywords Differentiation · European Union · Eurozone · Integration · Single market · United States

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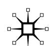


Introduction: toward a differentiated EU?

Differentiation is a hot topic in the European Union today. For good reason: Greek pain and temporary capital controls within 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.[1] 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.' Political calls for differentiation have been systematically 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 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. The EU maintains 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 USA. 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. This is not to say that the EU is more "integrated" than the US. To the contrary, economic and social flows are far smaller across Europe's interstate borders. Nor are EU rules even or pervasive: a broader picture of EU regulatory and fiscal authority would acknowledge significant variations across the "four freedoms" and its fiscal oversight. We simply argue that

[1] Montenegro and Kosovo use the euro; Iceland, Norway, and Liechtenstein are in the Single Market.

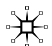
the core rules of the Single Market and Eurozone limit member states' room for maneuver significantly more than do equivalent federal rules in the USA.

After laying out this basic comparison, we show how these tight EU rules have consistently frustrated Greek and British demands for differentiation. Their demands confronted different technical challenges but ultimately encountered similar political problems. Technically, the single market creates much less of a "cliff edge" than the single currency: partial membership in the former is imaginable, but you are either in or out of the Eurozone. The UK faced constraints that were clearly political. London asked to reclaim control over free movement of people while maintaining trade access. The EU refused this demand based on political and legal arguments about the integrity of its rules. Greece's options of how to address its debt crisis faced sharper mechanical constraints, as it had no viable routes between meeting Eurozone conditions and opting for "Grexit." Yet, much of the conditionality and pushback against its attempts at differentiation also played out in ways that were politically motivated rather than technically necessary. Not wanting to leave the euro, Greece sought flexibility and support within the macroeconomic governance framework that accompanies membership in the common currency. Like the Brexit case, the Greek demands too were rejected essentially with political and legal arguments built into the Eurozone's rules, not because more flexible and supportive monetary integration was technically unimaginable.

Since we lack the space to look back and explain how this tight union emerged, our aspirations in this article are descriptive rather than explanatory. Still, our argument 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



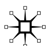
varies (Fabbrini 2019). Vivien Schmidt's image of a "soft core" Europe combines sectoral variations with more variation in national memberships (Schmidt 2019). Another scenario mentioned in Fabbrini's contribution extends the combined logic to an extreme vision of "institutional pluralism" akin to James 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." In political terms, the interaction of these kinds of differentiation is easy to see. 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] In Schmidt's terms, we suggest that the EU has a very hard core (Schmidt 2019). 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

[2] Fabbrini (2019). For a related discussion, see Schütze (2009).



the Single Market and Single Currency, with tighter rules than the more flexible arrangements of other regional organizations or even of Anglo-Saxon federations (Majone 2014). Yet Majone focuses on criticizing these rules rather than explaining how they could plausibly be altered. As Frank Schimmelfennig (2019) notes in this issue, 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.

A comparison of central constraints on the economic-policy discretion of member states between the European Union and the USA helps to convey concretely just how restrictive the EU is. We show that US states receive considerably more latitude from Washington, DC to differentiate their market regulations or fiscal policies than EU member states get from Brussels.

Single-market constraints on EU states in American perspective

Consider first a comparative US perspective on the extent to which the EU allows member states to maintain differentiated 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 underlying them. Even most EU experts do not seem to realize how much more the USA allows its states to choose to impede interstate exchange.

In *goods*, a variety of US federal agencies oversee sector-specific standards for products like toys, vehicles, food, alcohol, tobacco, many chemicals, and medical devices. Many goods have no federal standards, however, so states typically voluntarily adopt standards taken 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).

[3] See the website of the private American National Standards Institute. Its page on state variations (https://www.standardsportal.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."

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 1 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% 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 a certain 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—simply authorizing the federal Congress "to regulate commerce… among the several states." Yet, 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-twentieth 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, nondiscriminatory, 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 Republican-held Congress pursued a wide-ranging agenda of loosening or removing federal regulations between 2010 and 2018, with no attention to interstate barriers whatsoever.[6] GOP leaders during that time argued 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 30 years have seen a flood of legislation to translate the ECJ's legal parameters for the Single Market into active policy.

Rulings like *Dassonville*, *Van Binsbergen*, and *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 *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

[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 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/.

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 2007–2008 (Davies 1997; Barnard 2008). Meanwhile a "big bang" in jurisprudence aimed at liberalizing services 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; Nicolaïdis 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. Though 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 pursuit of the "four freedoms" as the *raison d'être* of the institutional system. While commitments to each of those four freedoms are well established, arrangements across them have always varied. There is also no economic logic requiring all aspects of market openness to 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; Schimmelfennig and Winzen 2014; Winzen 2016). When we focus on the policy differentiation available to Eurozone members in comparison with 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 (or 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).

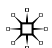
Under the American Constitution, the various states retain all sovereign powers that are not explicitly delegated to the federal government. States are barred from taxing foreign trade and interstate commerce, but otherwise retain sovereignty over taxes and spending. Both federal and state governments typically impose income and corporate taxes, though multiple states impose no income taxes.[7] In the 1840s and 1850s, American States adopted "balanced budget rules" in response to multiple episodes of bond defaults and financial stress, but never as a disciplinary device imposed 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 these were not 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-nineteenth 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 active governance as much as possible. As is well known, the SGP included a 3% deficit floor and a 60% 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'

[7] As of 2018, seven US states forego individual income taxes: Alaska, Florida, Nevada, South Dakota, Texas, Washington, and Wyoming. New Hampshire and Tennessee only tax income on capital investments, including dividends.



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 so-called "Six-pack," "Two-pack," and Fiscal Compact were all introduced and served to further limit member states' discretion over fiscal policy. They introduced quasi-constitutional balanced budget rules and gave 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." Unlike the US federal government's hands-off approach toward highly indebted states, the Eurogroup—led by Germany—refused to allow Greece 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 we recount 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)—were deeply involved in making the imposed reforms an implemented reality as members of the troika. 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. In one especially striking episode in the summer of 2011, the ECB's president at the time, Jean-Claude Trichet, sent classified letters to Italian and Spanish Prime Ministers Berlusconi and Zapatero 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 send in their state budgets for federal approval before debating and approving them in their own state legislatures. The idea that an unelected bureaucrat residing in Washington, DC could veto their budgets borders on the absurd. Similarly, the suggestion that the Chairman of the Federal Reserve Board could send secret letters to the governors of Wisconsin, Florida or Illinois with a list of structural reforms to enact in return for liquidity support is as far removed from American political reality as one can possibly imagine.

Like the discourse on '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 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 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."[8]

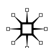
It is no secret that this disciplining discourse reflects the preferences of Germany and other northern European governments, but in such a densely and explicitly institutionalized arena, it is not simply German power that preserves these constraints. The understanding that participation in the euro 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 both 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. While in theory, any country can participate in the single market to a greater or lesser extent, there are legal norms, technological limitations, and political choices that can prevent differentiation. For the Eurozone, the basic choice is more mechanical: your exchange rate is either irrevocably fixed or not. You cannot be half-way in the euro area. The rules that govern that area, however, are there by political choice. The tight bounds on national fiscal policies that come with the euro are institutional requirements created and upheld by politics.

Despite explicit democratic support for national governments' demands in both cases, EU leaders have consistently and successfully defended 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 their commitments to one another. We show below how EU officials' bottom lines—non-negotiability of national fiscal constraints in the single currency and the strict 'indivisibility' of the single market—systematically frustrated Greek and British demands for differentiation.

[8] As quoted in Matthijs (2016: 375).



Differentiation frustrated in the Eurozone: the case of Greece

Much of the literature on the Greek debt crisis focuses on Germany's role in 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 (Matthijs and Blyth 2018).

As is well known, Greece faced severe European constraints 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 more favorable terms with creditors eventually found a voice in the program of the new hard-left Syriza movement and its firebrand leader Alexis Tsipras. Syriza subsequently swept the January 2015 parliamentary elections.

Room for maneuver within EU rules—differentiation—was the core of Syriza's manifesto. 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 of Understanding (MoU) 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 in the spring of 2015 remained within the spirit of the Thessaloniki program, though already with some notable deviations. Without suggesting a debt write-off, two proposals written in May and June 2015 asked for other debt relief measures and demanded 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 creditors' demands for prudent economic and fiscal policy, the Syriza government proposed limits on early retirement, further deregulation of product markets, conditional privatization, and the creation of an independent tax authority. Greek leaders hoped that these stricter measures and a promise to achieve primary surpluses would allow for a compromise.

[9] Greece's gross GDP at market prices decreased by 27% between 2008 and 2015: http://appsso.eurostat.ec.europa.eu/nui/show.do?dataset=nama_10_gdpandlang=en.

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 refused any debt relief outright (European Commission et al. 2015a, b). 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 then defaulted on an IMF loan (European Commission 2015a; IMF 2015). On July 5, a referendum was held on whether Greece should accept the creditors' bailout conditions. It resulted in a resounding *oxi* (no): 61% of votes opposed the bailout conditions, without a single Greek region in favor (Arnett and Galatsidas 2015). Clearly, the Greek public still held on to its demand for temporary deviation from Eurozone rules that had paved Syriza's path to power half a year earlier (Table 1).

Despite domestic support, the Greek government had little room to implement different policies. Expiration of the bailout program on June 30 forced it to request stability support from the European Stability Mechanism (ESM) before a longer-term agreement could be reached.

Around this point Greek Finance Minister Yanis Varoufakis proposed measures to push back against creditors, but Tsipras' inner cabinet voted him down, causing his resignation on July 6 (Lambert 2015). Then on July 8–9 the government begrudgingly crossed its previous red lines to accept the surplus targets demanded by its creditors and far-reaching tax and pension reform.

Yet, even these new proposals did not go far enough for some Eurogroup members, 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 Greece's concessions were insufficient, Wolfgang Schäuble's Finance Ministry listed two options: Greece could present "radically improved proposals" or take a "time-out" from the Eurozone with possible debt-restructuring. The proposals rested on the argument that debt-restructuring was incompatible with Eurozone rules. Thus, Germany insisted that Eurozone rules defined a "cliff edge": either submit to strong constraints or leave the euro.

Two days later, 11th hour negotiations at a summit in Brussels decided 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 Grexit option was now on the table (Kwasniewski 2015). After two high-stakes days of uncertainty, a preliminary agreement emerged: in return for a bridge loan and opening negotiations for an ESM loan, Tsipras' government would reverse or compensate for much of Syriza's labor market and pension reforms, introduce quasi-automatic spending cuts to meet primary surplus targets, and accept continued IMF assistance. There would be no debt haircut or concrete commitment to debt relief (Euro Summit 2015).

With the threat of Grexit looming, the Tsipras government had accepted reform measures even more punitive than those rejected by its citizenry only 8 days prior. The eventual new Memorandum of Understanding for the ESM loan again failed to provide debt relief and came with further strict conditions, like the reversal of Syriza's previous tax reforms. Only the primary surpluses for 2015, 2016 and 2017 were

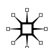


Table 1 Consecutive Greek proposals and eventual agreement

	Syriza's Thessaloniki Program (13 September 2014)	Greek proposals to Creditors (11 May 2015/11 June 2015)	Greek formal request for ESM support/reform proposal (July 8–9 2015)	Euro summit statement/ESM MOU (July 12 2015/August 14 2015)
Primary surpluses		2015: 0.8/0.6% 2016: 1.5% 2017: 1.5/2.5% From 2018: 2/3.5%	2015: 1% 2016: 2% 2017: 3% From 2018: 3.5%	2015: −0.25% 2016: 0.5% 2017: 1.75% From 2018: 3.5%
Debt repayment	"European Debt Conference" Growth indexation and Grace period QE: direct sovereign bond purchases	Schemes to swap ECB held debt with EFSF/ESM loans Further debt extension and GDP growth-index debt owed to GLF and EFSF End IMF lending	No debt relief measures mentioned	Three year ESM loan program No concrete commitments to longer grace or payment periods No nominal haircuts Continued IMF assistance
Economic reforms	Humanitarian measures More progressive income and property taxes Restoring higher minimum wage, employment rights and collective bargaining	Conditional privatization Collective bargaining and gradually restoring minimum wage Limit early retirement, recapitalization of social security and pensions, no cuts Liberalizing product markets Fiscal Council	Extensive privatization, transferring assets to independent fund Adjust income and property tax rates and raise corporate tax rate, raising VAT Limit early retirement, increase retirement age, phase out solidarity grant for pensioners Liberalizing product markets Fiscal Council	Cont'd extensive privatization with independent fund Tax reform including VAT and 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 and product market liberalization Long-term comprehensive Social Welfare Reform Fiscal Council + quasi-automatic spending cuts

Source: Authors

brought back to more realistic levels, after the troika acknowledged that Greece's economy was projected to shrink by another 3% in 2015, instead of growing by 2.5% as projected back in fall 2014 (Merler 2015).

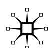
The negotiation outcome revealed the striking power imbalance at play. While the other Eurozone countries seemed no longer afraid of Greece exiting the single currency, Greece saw its future firmly within the Eurozone. Not only would introducing a new currency be devastating for Greece's economy, Greek public opinion remained strongly in favor of keeping the euro.[10] 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 UK

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). Hoping to appease Eurosceptic backbenchers while staving off the electoral threat from the far-right UK Independence Party (UKIP), Cameron said a Conservative government after 2015 would first attempt to renegotiate the terms of EU membership and would then ask citizens to vote on staying or leaving. The Conservatives' victory in May 2015 appeared to validate Cameron's electoral strategy—but the promised renegotiation would prove difficult to deliver. Like Greek demands in the Eurozone crisis, 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.

Even before the Tories formulated their plans for renegotiation, the EU was signaling that there was little room for change. 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 the possibility of 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). Cameron was committed to his course, however, and set out several demands first in his 2015 election manifesto and then in a letter to the EU requesting the renegotiation. He sought 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. Clawing back powers from the EU proved much more difficult than Cameron probably expected. Doubt about the feasibility of treaty change that might meaningfully limit the EU's central authority emerged immediately. 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

[10] From May 2015 to November 2015, the Eurobarometer measured an *increase* in support for membership in the Economic and Monetary Union.



achieve in its negotiations was a red-card mechanism in which 55% 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, then 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 negotiations, 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 4 years rather than withheld for a full 4 years after arrival. Even this could only occur under a 7-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 4 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 2 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 2 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."[11] At the time of writing, it remains unclear what the future relationship between the UK and the EU will be.

Conclusion

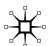
We want to be clear that we do not mean to dismiss the notion that the EU's future will likely include more differentiation. Our point is simply that useful analysis of such options must begin by understanding what variation is permissible within current EU rules, and thus what exactly would need to 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 Tsipras or Britain's brash band of Brexiteers, neither of whom understood what they were dealing with.

We can have some sympathy for their mistakes, since it is easy to exaggerate the degree to which the EU is a smorgasbord of flexible policy collaborations. Holdouts, 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 hodgepodge of acronymed arrangements 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 as they please in diplomatic relations.

Prominent academics have worked 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 2013). 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.

[11] As reported in the Financial Times: https://www.ft.com/content/9099a1a8-bcda-11e8-8274-55b72926558f.



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.

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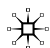

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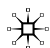

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