CHAPTER 2

FREE MOVEMENT OF GOODS

Common sense and mutual interests should induce nations to abate their natural envy and their distrust of each other. Common sense tells us that war between nations is so stupid and savage as duels between individuals. Mutual interests would suggest the establishment of perpetual peace as well as free trade between nations which would bring the greatest prosperity to us all. Nevertheless it is not yet safe for the lamb to lie down with the lion.¹

A Brief History

The only example in the nineteenth century of the formation of a customs union that involved the surrender by independent states of some of their sovereign rights was the establishment of the German Zollverein in 1834. The Zollverein was an economic union of the German States, wherein all trade restrictions within the union were removed and the entire territory was made a single tariff and trading area, subject to uniform laws regarding import, export and transit duties.² The Zollverein was established in the aftermath of the Napoleonic Wars, when the economies of the German States were desperately trying to overcome the devastation caused by these wars. On the one hand, they were faced with stiff competition from the English manufactures; and, on the other, their exports to the neighbouring countries were restricted by the protective practices of those countries. Furthermore, within the German Confederation, the States were hopelessly fragmented, both politically and economically. The German Confederation or Bund, formed in 1815, comprised of

thirty-nine member states, and, it is said that at the time of the French Revolution, around eighteen hundred customs check-points existed in Germany. As a result, they were deprived of markets within and outside of Germany. Prussia responded to the situation by abolishing sixty-seven different tariff schedules and replacing them with a uniform tariff. Thus, the entire state was made a single marketing unit. This Prussian tariff reform of 1818 put economic pressure on the country’s smaller neighbours to come to terms with it. In addition, Prussia started to absorb the numerous “enclaves” that existed within the Prussian kingdom into its own customs system. This expansionist and hegemonic character of Prussia paved the way for the establishment of the Zollverein. At the same time, in most cases, the initiative for the formation of customs union came from the smaller states. The first such union was established in 1830 with Hessen – Darmstadt. According to Murray Forsyth, this was because the smaller states felt that their independence and statehood stood threatened as much by the commercial and industrial power of larger states as by their military strength. In 1834, a fully-fledged Zollverein was established. Austria, one of the major powers, chose to stay out of the union and Prussia became the sole hegemonic power. Prussian rates of duty, customs laws and procedure became the Zollverein’s rates of duties, customs laws and procedure. Eventually, the Zollverein moved from common tariffs and common commercial policy to monetary unification also.

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6 The Dresden Monetary Convention of 1838 established a fixed rate of 14.24½ between the southern currency florin and the northern thaler. Further, a silver coin of the value of 2 thalers or 3½ florins was issued, which was to be the legal tender throughout the union. The common Zollverein currency existed alongside each state’s own currency.
The main advocate of the Zollverein, Friedrich List, considered the Zollverein a means to create a unified German economy. According to him removal of all barriers to trade within the customs union would ensure greater progress and lead to the unification of the economy. At the same time, a unified tariff schedule would allow infant German industries to compete evenly with British manufactures.

The German experience suggests that a customs union stimulates technical progress and promotes industrial expansion. It was no accident that the early railway age in Germany coincided with the formative years of the Zollverein. The Germans also discovered that with the development of the Zollverein further economic integration was inevitable. In transport, monetary affairs, commercial law and various other aspects of economic life the German states co-operated much more closely in the 1860s than they had in the 1830s. On the other hand the view that the economic integration of independent states eventually leads to political integration is also contestable, as twenty years of economic co-operation in Germany did not prevent the outbreak of civil war there in 1866.

The idea of the European Economic Community (EEC) also developed broadly under similar circumstances. At the end of the Second World War, the European nations found that the United States and the Soviet Union had consolidated markets in their own respective regions. They had their own trading areas, which the Europeans found hard to penetrate. At the same time, the erstwhile colonial powers were losing control

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over their colonies as the wave for self-rule spread across Africa and Asia. While some powers, like the Dutch, collapsed immediately, others, like the British, transformed more gradually. But, most importantly, Western Europe itself was dominated by protectionist tendencies. The United States championed the cause of trade liberalisation by pressurising West Europe, under the Marshall Plan, to adopt free trade. According to Bela Balassa, at the end of the War, when Britain had suggested political and economic arrangements among the non-Communist countries of Europe, the US had reacted negatively to it. The US regarded them as a “manifestation of the pursuance of selfish interest on the part of the UK.” But as the magnitude of the Soviet threat of expansion increased, the US reappraised its stance. It was felt that a united Europe would be able to counter the Soviet threat more effectively. As a result, the US pressed for institutional development in Europe, which paved the way for the establishment of the Organisation for European Economic Co-operation (1948), the Council of Europe (1949), and the European Payments Union (1950). These were followed by the more closely knit European Coal and Steel Community (1952), and also the European Defence Community (1954), which however, failed to see the light of day.

Once again, the main initiative came from the smaller states. Belgium and Luxembourg had already established an economic union between themselves in 1921. During the Second World War, the three governments-in-exile of Belgium, Luxembourg and the Netherlands had signed a monetary convention (1943), which fixed the parities of their two currencies. This progressed into the Benelux Customs

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Union in 1948 and subsequently into an economic union in 1960. The Netherlands, with this background, played a leading role in the establishment of the EEC. However, the Netherlands had not always been enthusiastic about a West European power bloc, sought especially by France, for fear of French domination. Subsequently, a redefinition of the concept of security occurred in the Netherlands, as in Belgium and in Luxembourg, to emphasise economic rather than military security. Johan Willem Beyen, the Foreign Minister of the Netherlands between 1948 and 1952, believed that the Netherlands should not join the federal constitution unless it received commercial recompense. According to Beyen, the recompense should be that the European Political Community (EPC) becomes a customs union. Furthermore, he proposed that the progressive elimination of tariffs must be written in detail into the draft EPC Treaty. Tariffs could not be lowered unless a supranational authority would be set up to enforce a "preordained, irrevocable course of action."

The European Defence Community (EDC) and the incumbent EPC were defeated as France failed to ratify the Treaty, and Jean Monnet and Paul Henri Spaak took up the customs union proposal only in 1955, which eventually led to the signing of the Treaty of Rome and the establishment of the European Economic Community.

Bela Balassa has defined five stages to economic integration. 1) Free Trade Area, where tariffs between participating countries are abolished, but each country retains its own tariffs against non-members. 2) Customs Union, where besides the

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11 In 1944 a convention for the establishment of a Customs Union was held. In 1947, the common external tariff was agreed and in 1948 the Benelux Customs Union was formed. In 1958 a Comprehensive Treaty of Economic Union was signed, and it came into force in 1960. See George J. Stein, Benelux Security Cooperation: A New European Defense Community? (Boulder: Westview Press, 1990), p.5.


13 Ibid., p.187.
suppression of discrimination in the field of commodity movement within the union, there is equalisation of tariffs in trade with non-member countries. 3) Common Market, where not only trade restrictions but also restrictions on factor movements are abolished. 4) Economic Union, which combines the suppression of restrictions on commodity and factor movements with some degree of harmonisation of national economic policies, in order to remove discrimination that was due to disparities in these policies. 5) Economic Integration, which presupposes the unification of monetary, fiscal, social and counter cyclical policies and requires the setting-up of a supra national authority whose decisions are binding on the member states.14

The Treaty of Rome clearly provides for the establishment of a Common Market. Article 3 of the Treaty provides for: a) “the elimination, as between Member States, of customs duties and of quantitative restrictions on the import and export of goods, and all other measures having equivalent effect;”15 b) “the establishment of a common customs tariff and a common commercial policy towards third countries;”16 and, c) “the abolition, as between Member States, of obstacles to freedom of movement for persons, services and capital.”17 Article 3 moves a step further and provides for (a) “the application of procedures by which the economic policies of Member States can be co-ordinated and disequilibria in their balance of payments remedied,”18 and, (b) “the approximation of the laws of Member States to the extent required for the proper

16 Article 3(b), EEC Treaty
17 Article 3(c), EEC Treaty
18 Article 3(g), EEC Treaty
functioning of the Common Market. Although paragraphs (g) and (h) of Article 3 do not presuppose anything, they do leave open the possibility of an eventual economic integration.

Another improvement of the EEC over the Zollverein is its supranational character. The establishment of institutions such as the European Parliament, the European Commission, the Council of Ministers, the Court of Justice, and various consultative committees such as the Economic and Social Committee, implies the existence of a legislature, an executive, a judiciary and a new institution which brings in a confederal relation at the European level. But why economic integration and not just a free trade area? Why integration and not just inter-dependence? Why have supranational institutions and irreversibility? In the aftermath of the Second World War, the devastation and destruction of the economies of Western Europe was so complete that every economy was obsessed with economic recovery. Industrialisation and modernisation were the key words. The widespread belief was that economic recovery was possible only by means of industrialisation, which would lead to modernisation. But, the success of industrialisation required markets for the products as well as protection from competition. Hence the Common Market and the Customs Union were established, wherein the former would ensure the free movement of goods from the industrialised north to the more agrarian south and vice versa, and the latter would provide protection from outside Community competition. Furthermore, according to Stephen P. Magee and Hak-Loh Lee, there is a direct link between the degree of devastation of the economies due to war and their subsequent choice of

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19 Article 3(h), EEC Treaty

customs union or free trade area. France, Germany and Italy were among the most devastated countries and it was here that most rapid rebuilding happened and as a result they opted for a customs union. On the other hand, the principal members of EFTA, the UK, Austria, Norway, Denmark, Portugal, Sweden and Switzerland were somewhat less devastated by war and consequently they opted for a more protectionist EFTA.\textsuperscript{21} Integration also meant preservation of employment and welfare in the threatened industrial sectors, and, at the same time, income protection in the agricultural sector.\textsuperscript{22} Similarly, irreversibility was preferred as in intergovernmental arrangements, such as the OEEC, the tendency for member states to retreat from their commitments was more. But most importantly, it was crucial for the West European countries to bind West Germany in place, as it had proved to be the pivot of trade expansion in the region. In the 1950s, Germany was the dominating influence on the remarkable expansion of intra-Western European trade. Germany had become indispensable for the Benelux, Austria, Switzerland and Denmark in terms of both imports and exports. For Norway and Sweden trade with Germany was of major importance and for France and Italy it was by far the most rapidly growing market. As a result, Germany became “indispensable to the rescue of the European nation-state. This rescue had come to depend on a country that was not really yet a country, without full national sovereignty until 1955, an artificial creation whose future was highly uncertain, still the subject of a possible deal between America and Russia, and


still deeply distrusted." Thus, binding Germany was crucial, and there was nothing better than binding it in an irreversible economic community, which would ensure the "rescue" of the European nation-state. Since the choice of integration was worth its advantages, Member States were willing to give up sovereignty in the required policy areas. Having done that, the changes in the Member States' domestic policies have been "confined to limiting further integration rather than reversing existing bargains." In other words, in order to ensure the survival of the nation-state, integration was adopted. But, the Member States were willing to give up only as much as was absolutely essential. Anything more, or further integration, was faced with stiff opposition.

This pattern has been very obvious in the functioning of the Common Market. Though free movement of goods, persons, services and capital are integral to the functioning of the Common Market, this chapter will deal with free movement of goods alone. It is a vital tenet of the Community as well as of the Member States. The chapter includes one case study of broadcasting, which ideally falls under services but is included to emphasise the point that in spite of Community Directives being passed Member States invoke such sentiments as preservation of national cultures to protect their interests.

**The System of Free Movement of Goods**

The origins of the principle of free movement of goods are to be found in the Treaty of Rome, which attempted to integrate the economies of the Member States by removing barriers to trade. Though "an ever closer union" was mentioned, the

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23 Milward, n.12, p.67.
24 Milward and Sorensen, n.22, p.15.
provisions to attain this union were not spelled out in the Treaty. The thinking behind the Treaty implied that "all that was necessary to create a market would be removal of artificial barriers that impede natural markets"\(^{25}\), in the case of Europe, tariffs and quotas. Hence the approach was negative integration policies i.e. removal of barriers to trade to integrate the economies as opposed to positive integration policies, which would mean developing institutions to foster expanded and integrated markets. But, many integration theorists argue that even though a limited exercise in economic integration was adopted to start with, it would eventually have spill over effect, which would lead to greater and greater integration.\(^{26}\)

Article 3(a) and Articles 9–11 of the EEC Treaty form the general legal basis of free movement of goods. The principle of free movement of goods involves (a) the removal of fiscal barriers, and (b) the removal of physical and technical barriers.

**Fiscal Barriers**

"The Community shall be based upon a customs union which shall cover all trade in goods and which shall involve the prohibition between Member States of customs duties on imports and exports and of all charges having equivalent effect, and the adoption of a common customs tariff in their relations with third countries."\(^{27}\) As per Article 9 fiscal barriers include customs duties, measures having equivalent effect, fees, internal taxation and the common customs tariff. As per the Treaty, Member States were to refrain from introducing any new customs duties on imports or exports between themselves and from those which already applied in their trade with each

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\(^{27}\) Article 9, EEC Treaty
They were also to abolish all existing duties in accordance with a procedure laid down in Articles 13–16, by the end of the transitional period. For Article 12 to be operational, it is imperative that goods cross a frontier. If a tax is imposed on goods that cross an internal Community border then it impedes intra-Community trade and hence is prohibited. At the same time, charges having equivalent effect, which are "fiscal or parafiscal charges that are not customs duties in the classic sense but, like customs duties are levied on goods on the occasion of or in connection with the crossing of a frontier"; are also prohibited. This is so because the impact of charges having equivalent effect is to render those goods more expensive. As a result, they have a protectionist or discriminatory effect similar to that of customs duties.29 A judicial definition provided by the European Court of Justice (ECJ) states:

... the justification for the prohibition of charges having an effect equivalent to customs duties lies in the fact that any pecuniary charge, however small, imposed on goods by reason of the fact that they cross a frontier constitutes an obstacle to the movement of goods in that it artificially increases the price of imported or exported goods in relation to domestic goods. It follows that any pecuniary charge, whatever its designation and mode of application, which is imposed unilaterally on goods by reason of the fact that they cross a frontier constitutes a charge having an effect equivalent to a customs duty within the meaning of Articles 9, 12, 13 and 16 of the Treaty.30

Fees are charges levied in return for the performance of a specific service by the administration. The Treaty of Rome does not prohibit the collection of fees per se. As a result, Member States have attempted to use them as an effective barrier to free movement of goods i.e. charging fees on health and sanitation inspections, the collection of data for a statistical survey in aid of traders, quality control inspections,

28 Article 12, EEC Treaty
extended opening hours for customs posts beyond accepted national working hours, and the issue of import licences by a national agricultural intervention agency. These charges have a prohibitive effect as they are levied as payment for a service performed when goods cross a frontier.\textsuperscript{31} Similarly, discriminatory internal taxation as provided under Article 95 of the Treaty are also prohibited even though it does not fall under Article 9. According to the ECJ, Article 95 is calculated to close any loopholes which internal taxation might open in the prohibition on customs duties and charges having equivalent effect.\textsuperscript{32} The first paragraph of Article 95 states that: “...no Member State shall impose, directly or indirectly, on the products of other Member States any internal taxation of any kind in excess of that imposed directly or indirectly on similar domestic products.”\textsuperscript{33} The important point is that the goods need not be identical; they only need to be similar. Furthermore, Article 95(2) states: “... no Member State shall impose on the products of other Member States any internal taxation of such a nature as to afford indirect protection to other products.”\textsuperscript{34} In other words, even when goods are not identical or similar, if they provide competition to domestic products, then internal taxation is prohibited.\textsuperscript{35} Articles 18 - 29, govern the operation of the CCT. The main thrust of these articles is that if a good is imported

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\textsuperscript{31} Andrew Charlesworth and Holly Cullen, \textit{European Community Law} (London: Pitman Publishing, 1994), pp 211-12
\textsuperscript{33} Article 95(1), EEC Treaty
\textsuperscript{34} Article 95(2), EEC Treaty
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from a third country by any Member State then the free movement provisions are applicable on it. 36

**Physical and Technical Barriers**

The abolition of customs duties and charges of equivalent effect alone would not have been sufficient to guarantee the free movement of goods within the Common Market. Article 30, which eliminated quantitative restrictions and measures having equivalent effect, is therefore the central provision of the Treaty relating to the free movement of goods. "A quantitative restriction is a national measure which places physical/non-pecuniary restrictions on the amount of goods that may enter or leave the Member State. The most common example is a quota." 37 The Treaty prohibits Member States from resorting to such restrictions and from introducing new restrictions in trade among themselves. Being a direct prohibition, Member States more or less adhere to it. As a result, quantitative restrictions are not as prevalent as are measures having equivalent effect. The Commission interprets measures having equivalent effect in Directive 70/50 as:

... measures governing the marketing of products which deal, in particular, with shape, size, weight, composition, presentation, identification or putting up and which are equally applicable to domestic and imported products, where the restrictive effect of such measures on the free movement of goods exceeds the effects intrinsic to trade rules. 38

The ECJ defined measures having equivalent effect in the case *Procureur de Roi v Dassonville* (1974) as: "all trading rules enacted by Member States which are capable

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36 See Chapter 4
37 Owen, n.32, p.106
38 Cited in ibid., p.107
of hindering directly or indirectly, actually or potentially, intra-Community trade.\(^3\)

This landmark ruling led to the belief that all measures breaching the Dassonville formula would breach Article 30 unless justified by Article 36.\(^4\) However, this belief was clarified by the ECJ in another landmark ruling of the *Rewe-Zentrale AG v Bundesmonopolverwaltung für Branntwein* (1979) or Cassis de Dijon, where it introduced the “rule of reason” clause and the doctrine of “mutual recognition”.\(^4\)

Rule of reason implied that in the absence of common rules, it is for the Member States to regulate all matters relating to production and marketing on their own territory.

Obstacles to movement within the Community resulting from the disparities between the national laws relating to the marketing of the products in question must be accepted in so far as those provisions may be recognised as being necessary in order to satisfy mandatory requirements relating in particular to the effectiveness of fiscal supervision, the protection of public health, the fairness of commercial transactions and the defence of the consumer.

The doctrine of mutual recognition meant that if a good has been lawfully produced and marketed in one Member State, then there is no valid reason why it should not be introduced into any other Member State. Nevertheless, Article 36 provided derogations from Articles 30-34.

The provisions of Articles 30 to 34 shall not preclude prohibitions or restrictions on imports, exports or goods in transit justified on grounds of public morality, public policy or public security; the protection of health and life of humans, animals or plants; the protection of national treasures possessing artistic, historic or archaeological value; or the protection of industrial and commercial property. Such prohibitions or restrictions shall not, however, constitute a means of arbitrary

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\(^4\) Article 36 provides derogations from the principle of free movement.

\(^4\) Chalmers, n.39, pp278-9
discrimination or a disguised restriction on trade between Member States.\textsuperscript{42}

National governments distort trade in the private sector by giving firms subsidies. In the EC, subsidies have been used by Member States to protect domestic firms from more competitive imports, even if imports are from other EC countries. Subsidies are also used to promote exports, which otherwise would not have been competitive.\textsuperscript{43} State aids also include tax breaks, low-interest loans, cheap public services and other ways of granting firms financial advantages. In the period 1986-96, state aid granted by the twelve Member States to industry alone (excluding agriculture, fisheries, coal and transport) amounted to an annual average of over ecu 45 billion (in 1996 prices). This is a significant level of support as it corresponds to about two-thirds of the total budget of the EC.\textsuperscript{44}

Similarly, discriminatory public purchasing has been traditionally one of the most powerful and frequently used instruments of industrial policy and an effective means of promoting national champions. Goods and services purchased by the public sector form a substantial part of the EC's economy, about 15 percent of GDP. The contractual part or the public procurement is estimated at 7-10 percent of GDP, but the amount that is actually bought from other Member States is only 0.14 percent of GDP.\textsuperscript{45}

\textsuperscript{42} Article 36, EEC Treaty
\textsuperscript{45} The Cecchini Report 1988, cited in Pinder, n.43, p.99
Intellectual property rights can form a potential barrier to the free movement of goods when Member States impose restrictions on imports if they infringe national industrial or commercial property rights. Similarly, different technical regulations, which are legally binding in each country, and standards, which are voluntarily agreed codifications written by national standardisation bodies and considered as an indicator of quality, also form a major factor behind the fragmentation of the EC market.

The Progress of the Common Market

The Common Market, established by the EEC Treaty, was based on the principles of free market and trade liberalisation, and the aim was economic growth. Though the Treaty does not contain any express provision for a specific economic system, the objectives stated and the means made available to achieve them have the essential characteristics of a free market. Similarly, the Treaty does not provide for developing institutions to foster expanded and integrated markets or trade liberalisation. It simply calls for removing all barriers to trade among the Member States. Such an approach should ideally restrict the latitude for national governments to adopt protectionist measures but in actual practise protection has been widespread.

1963 – 1985

A survey of statistics reveals that up till 1970 trade grew much faster than output. The European GDP grew on average at about 5.5 percent per annum and the per capita

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46 Charlesworth and Cullen, n.31, pp 310-30
income at 4.4 percent. Industrial production rose at 7.1 percent per annum.\(^{49}\) The fastest growing countries were West Germany, Italy, France and the Netherlands. The volume of commodity trade, at the same time, grew more rapidly than output, at a rate of 8 to 9 percent per annum.\(^{50}\) Till the Kennedy Round, trade liberalisation was limited to Europe and aimed at discriminating against the US.\(^{51}\) By the time the Kennedy Round lowered tariffs, the dollar was much overvalued, which meant no effective competition for West Europe. As far as the rest of the world was concerned, East Europe produced goods that could find no market, Japan produced goods that were almost wholly absorbed by the US, and the developing world was caught in the cycle of lack of capital, infrastructure, manpower skills and markets. As a result, Western Europe collectively enjoyed a "natural protection" against the outside world. It was able to sell to the rest of the world on a cost plus basis and also set these costs, allocate resources, and distribute factor payments in a way that suited its politics and changing values.\(^{52}\) Even though exports to the rest of the world grew, it was the intra-EC trade that was more significant. The dependence of the Six economies on each other grew steadily as compared to their dependence on the rest of the world.\(^{53}\) Intra-EC trade between 1963 and 1971 rose from $6790 million to $48117 million, a sevenfold rise. The individual members raised their proportion of trade with each other from 25 percent to 52 percent.\(^{54}\) This has been attributed to the rapid elimination of


\(^{52}\) Ibid.

\(^{53}\) Tsoukas, n.47, p.25

intra-EC tariffs and quantitative restrictions between 1958 and 1968. By 1968 the Six completed the abolition of all internal tariffs. At the same time, the general macroeconomic environment was quite favourable, with high rates of growth and low unemployment. As such liberalisation led to more trade, which in turn meant remarkable growth rates.

As mentioned earlier, the provisions of the Treaty were such that it left little room for national economic planning. But a major feature noticeable about the West European economies during this period was the increasing role of the state, at both macro and micro levels. Professor Tsoukalis cites three examples to prove the point. Firstly, the steep rise in the total outlay of the government as a percentage of GDP. From 1960 to 1985, it rose from 30.3 percent to 55.8 percent in the case of Belgium; in France it rose from 34.6 percent to 52.1 percent; Germany from 32.5 to 47.5 percent; Italy from 30.1 to 50.8 percent; Luxembourg from 30.5 to 51.1 percent and the Netherlands from 33.7 to 59.6 percent. In the case of Denmark, Ireland and the UK, from 1974 to 1985, the increase was from 45.9 to 59.3, 42.5 to 53.7 and 42.7 to 44.1 percent respectively.\(^{55}\) Secondly, the use of fiscal and monetary policy as a means of influencing aggregate demand. For example, Germany, Belgium and Italy placed great faith in monetary controls of one sort or another, whereas the UK resorted to fiscal regulators backed by credit and discount controls. France and the Netherlands depend on government planning with emphasis on government investment planning, sponsorship of investment projects by subsidies and licensing systems, and use of import controls and devaluations.\(^{56}\) And, lastly, the promotion of “national

\(^{55}\) Tsoukalis, n.47, p.28, Table 2.4

\(^{56}\) Aldcroft, n.50, p.190
champions”, which was a national means to counter the growing international competition.\textsuperscript{57}

All these factors are contrary to the principles of free market and liberalisation. Even in a period of high and steady growth, the Member States continued to strengthen the role of the national state. This is proof of the fact that Member States would not give away national control. National Interest was always the first concern. This feature became particularly pronounced in the post-1970 phase when the “golden period” came to an end.

The 1970s opened with the oil crisis. The EC Member States soon found that nearly two percent of their GDP was going to the oil producing countries. The unexpected rise in prices caused havoc with their balance of payments. At the same time, President Nixon felt that it was not possible to continue with the dollar linked to gold at its then current valuation. Subsequently, in 1971 at the Smithsonian Conference the dollar was devalued, which led to the breakdown of the Bretton Woods arrangement. These developments prompted the EC Member States to lock their currencies together. The “Snake” and later the Exchange Rate Mechanism replaced the dollar with the D-Mark to provide stability as the D-Mark was the strongest currency in the EC. This had very adverse impact on economic growth. Germany traditionally followed a strict monetary policy, which stressed on keeping inflation levels and exchange rate fluctuations low. These strict conditions were to be followed by other Member States as well. Earlier, the other Member States dealt with Germany’s competitiveness by devaluing their currencies. This was how they kept their balance of payments under control without actually reducing demand. But, with the option of

\textsuperscript{57} Tsoukalis, n.47, p.27
devaluation no longer available, the Member States were forced to reduce demand in order to keep their balance of payments in line. This resulted in deflationary policies which slowed down the Community growth rate.58

At the same time, the “natural protection” enjoyed by the EC with respect to the rest of the world came to an end. The dollar was now realistically valued and the US started to export standard goods to Europe such as textiles. East Europe, with the help of transnational companies, equipped itself with modern plants and became a force in the world market. Japan too diversified its products and markets and gained inroads into the EC. Finally the developing world, especially the newly industrialised economies, started their stupendous rise in the exports market for manufactures.59

These developments exposed EC as a high cost area of production.60 In order to reduce costs, the only option the firms had was to postpone investments, and when they could no longer do that, they were either faced with bankruptcy or rescue by the state. Similarly, in order to combat the competition from outside EC and also inside EC, trade protectionism was seen as the answer. As a result, the role of the state in channelling investments into industry by tax concessions, preferential financing, subsidies, special depreciation allowances, bank-interest subsidies, etc., and as a last resort nationalisation became widespread. So also did protectionism, both direct and indirect, the powers of imagination of firms and national governments alike touching new heights. National products were protected from competition from products outside the EC by way of such measures as the Multifibre Agreements, or imposing

59 Hager, n.51, p.67
restrictions on Japanese cars, etc. But the measures taken by Member States to protect their products from products coming from other Member States of the EC is what interests us.

In 1965, the French government issued a decree, which forbade the sale of any refrigerator, French or foreign, in France that had not received the approval of the French Commissariat de Normalisation and that had not been registered as being in stock by 15 January 1966. This was a move designed to protect French refrigerator manufacturers from the imports flooding from Italy and Germany. Netherlands, a major producer of milk and dairy products, in an obvious bid to protect its industry, prohibited the sale of cheese in the Netherlands to which had been added the antibiotic nisin. Nisin occurs naturally in most varieties of cheese and has the property of retarding the process of deterioration of cheese. In other words, mostly cheese that was imported would have nisin, in order to preserve them from deterioration. The Netherlands government prohibited its use on public health grounds. But, the point is if nisin is alright for intake by the French or the Italians, why is it a health hazard only for the Dutch? Similarly, Ireland prohibited the sale or exposure for sale of imported articles of jewellery depicting motifs or possessing characteristics which suggest that they are souvenirs of Ireland, for example an Irish character, event or scene, wolfhound, round tower, shamrock, etc. The importation of such goods was prohibited unless it had an indication of the country of origin or the word "foreign". France had a system of preferential postal tariff for French newspaper and periodicals, which particularly excluded similar publications of other Member States posted and

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61 Financial Times, 5 January 1966, in PRO/TN (68) 3
63 Case 113/80, Commission of the European Communities v Ireland [1981] ECR1625
distributes in France. Similarly, all undertakings publishing a newspaper, a monthly or fortnightly journal devoted to political affairs was accorded certain tax advantages in France, which included a tax-free reserve for the purchase of assets or any expense incurred on purchase of assets be deducted from taxable profits, etc. In 1980, however, a rule was introduced whereby these tax advantages were not made available for newspaper publishers of publications printed abroad.

The European Court of Justice has been a major force behind disciplining Member States and forcing in a Community law regarding free movement of goods. But, there have been rulings which indirectly favoured the discriminatory practices of the Member States. For example, Keck and Mithouard, managers of two hypermarkets in France in the frontier zone with Germany were accused of reselling German coffee at a cheaper rate in France. The French Directorate for Competition and the Prevention of Fraud stated that there was a general prohibition on resale at a loss. The Court ruled that the provisions of the Treaty relating to free movement of persons, services, and capital within the Community have no bearing on a general prohibition of resale at a loss, which is concerned with the marketing of goods. As a result, the Court ruled in favour of France. The Treaty of Rome might not have any provisions regarding resale of goods at a loss but these are part of the marketing schemes of companies and retailers. The hypermarkets by reselling coffee at a cheaper rate might not actually be making a loss. In most cases, supermarkets work on the principle of selling products at lower rates along with attractive schemes. By prohibiting such sale effectively

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64 Case 269/83, Commission of the European Communities v French Republic [1985] ECR 837
65 Case 18/84, Commission of the European Communities v French Republic [1985] ECR 1339

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amounts to disruption of free movement of goods. In this case it obviously affected the local coffee producers, which prompted the ban on Keck and Mithouard.

**Actual Practise Among Member States**

The basic assumption in a common market is that under conditions of perfect competition, prices should reflect only production costs, which in turn depends only on the technical characteristics of the commodity. In other words, minus transport costs, a product must be priced the same anywhere in the common market. But, this is rarely so in the EC. Since conditions of perfect competition are rarely found, it is obvious that there will be product differentiation over and above the technical characteristics. Accordingly, the prices will vary across the common market. But the most important factor leading to price differences is the presence of market imperfections like oligopolistic practices and discrimination. Numerous tests conducted for various products reveal the widespread prevalence of discrimination. And, this is attributed to the fact that Member States have and do endeavour to protect the interests of domestic products, producers and industries. Direct prohibitions like customs duties and quotas, which have been strictly prohibited by the Treaty and which are too obvious, have been more or less given up by the Member States. However, numerous imaginative and innovative means are used to keep products from other Member States out. With the help of some examples we will try to elaborate the above argument.

**Cars**

The figures brought out by the Bureau Européen des Unions de Consommateurs for the consumer price differences for selected car models in 1989, net of taxes, for the model Fiat Typo 1400 was upto 69 percent, for Mercedes 190D upto 49 percent, Citroen AX11 upto 85 percent, Peugeot 405 1600 upto 72 percent and for Toyota
Corolla 1300 upto 93 percent. In other words, the same model, Toyota Corolla 1300 costs 93 percent more in the UK than in Denmark. This is mainly because the car producing countries – Germany, France, Italy and Britain – choose to subsidise production using very different instruments and non-producers like Denmark and Greece choose to tax cars heavily irrespective of the origin of the car. There had been considerable discussion in the UK on the fact that British cars are much cheaper in Belgium than at home. This was because of the decision of the UK government to encourage inward investment. It allowed manufacturers to collude to restrict imports, especially from Japan, and set prices high in the UK market, such that the consumers would subsidise the producers. Similarly, it was found that an Italian car was about 9 percent more expensive than an imported car in Italy. Was this because the Italian car was more technically superior to the imported one? When product differentiation, i.e. differences in technical characteristics, was removed by the hedonic regression technique, it was found that the domestic and imported car did not have very different images. In addition, when the model was tested for both differentiation and discrimination, it was found that discrimination was more significant. An example of such discrimination is: in 1956 a special French excise tax was introduced on passenger cars. Firstly, there was a registration tax, payable when a new car is

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70 Holmes and McGowan, n.68, p.162

purchased, which was charged at FF 13.2 per CV (fiscal horsepower) for cars upto 12 CV and at FF 20 Per CV for cars above 12 CV. In addition, there was an annual tax, which was for cars upto 16 CV and upto five years old between FF 60 and FF 150 per year. But for cars over 16 CV and less than two years old the rate was FF 1000. This was significant because at that time France did not produce passenger cars of over 12 CV. In other words, cars of over 12 CV were imported cars only and they would be subjected to a much higher registration and annual tax. This was amended in 1983 to the effect that for cars upto 16 CV the initial rate of special tax was FF 2400, whereas for cars rated over 16 CV it was FF 8100 and this special tax was no longer applicable for the first two years, but for the first five years of a cars life. In addition, for the next fifteen years the car would be liable to an annual tax of FF 4050. Again France did not manufacture passenger cars over 16 CV, so in effect the special tax was charged only on foreign cars. Furthermore, the cars liable to the special tax satisfied broadly similar consumer needs to those met by passenger cars bearing a lower tax burden, which were manufactured in France.

Similarly, in 1984 there was a sudden increase in the parallel import of cars into Italy. The Italian government responded to this development by introducing new administrative requirements for the registration of imported cars, which were very discriminatory. According to the new requirement, the registration of a new foreign vehicle was subject to the production of a certificate of origin of the vehicle issued by the manufacturer and a document indicating the technical specifications of the vehicle. For vehicles already registered in the exporting country, the importer had to

72 PRO/TN (68) 3, “Trade Negotiations Committee: General Agreement on Tariffs and Trade, Industrial Products Committee, Inventory of Non-Tariff Barriers”, 9 April 1968
73 Case 112/84, Michel Humbolt v Directeur des Services Fiscaux [1985] ECR 1367
provide, in addition to the above-mentioned two documents, a certificate of registration issued by the authorities of the exporting Member States. Further, the technical specifications were to be made by the legal representative established in Italy within a period of forty working days from the application. In addition, the manufacturers and the legal representatives were authorised to receive a reasonable fee for issuing those certificates.\textsuperscript{74}

In yet another instance, a Luxembourg national purchased two cars in Luxembourg, paid the value added tax there but used them in Belgium, where he was a student. The Belgian authorities, however, asked him to pay VAT on importation of both cars. Levying VAT on importation of a product purchased in another Member State, where VAT was already paid, was purely discriminatory.\textsuperscript{75}

The Cost of Non Europe\textsuperscript{76} identified the kind of barriers to free movement of cars that existed in the Community. 1) Fiscal barriers: variations in car sales taxes and VAT rates; variations in policies on VAT refunds for company cars; variations in state aid to "national champions"; non-uniform cross-border registration rules; variations in tax incentives for environmental improvements; and, variations in excise duty on fuel, both in terms of rates and the relative treatment of diesel and unleaded fuel. (2) Physical barriers: delays in import and export of vehicles; need for complex paperwork on temporary import and export of vehicles; and complex quota rules on Japanese imports. (3) Technical barriers: lack of uniform product testing and type-approval certification making personal imports difficult; differing standards on

\textsuperscript{74} Case 154/85R, Commission of the European Communities v Italian Republic [1985] ECR 1753
\textsuperscript{75} Case 249/84, Ministere Public and Ministry of Finance v Venceslas Profant [1985] ECR
exhaust emission; car equipment peculiarities which make model variations necessary, such as side repeater flasher lights in Italy, rear reflectors in Germany, dim-dip headlamps in the UK and yellow headlamps in France. Plus in the UK and Ireland they drive on the left; and, selective distribution systems whereby exclusive contracts are written by manufacturers which automatically segments markets and preserves producer control over selling prices.

According to Jean-Pierre Lehmann, “for the European car manufacturing countries, the automotive industry represents many things, both substantial and symbolic. The home-produced automobile is an institution, a tradition, a symbol of industrial strength and a source of considerable employment, both direct and indirect. It also plays a key role in European social developments, particularly in industrial relations.”77 This fairly explains the protective attitude of member governments. But, more significantly, by the late 1980s the European automotive market was saturated, with production capacity greater than current and forecast demand.78 Hence the need to keep imports out. Along with intra-EC competition, the European automotive industry was faced with competition from Japanese cars. The Japanese penetration into the EC was phenomenal. Its share in Ireland was 43 percent, Denmark 36 percent, the Netherlands 27 percent and Belgium 20 percent.79

By late 1970s the Japanese started to invest directly in regional sales and distribution offices. Subsequently, they started setting up their own motor vehicle assembly in Europe. It was the UK that first opened its frontiers to the Japanese. Nissan was the

78 Ibid., p.45
79 Ibid., p.44
first to establish a major production facility in England in 1984. Others like Honda, Isuzu and Toyota followed Nissan.\textsuperscript{80} The free movement criterion required that the Japanese cars, having entered the EC be allowed free movement through out the Community. However, this was not so easy. Italy invoked Article 115 of the EEC Treaty, which provides for a Member State to retain national controls on imports and thus restrict intra-EC flows of third country goods where the Member State has a valid derogation from the Common Commercial Policy (CCP). The Commission allowed Italy to invoke Article 115. France also attempted to invoke the same but was not allowed, which saw France resorting to aggressive protectionism without any legal foundation.\textsuperscript{81} The British automobile industry, faced with poor management, poor quality and poor labour-management relations, was faced with the threat of winding up the Rover group. As a result, Britain opted for collaboration with the Japanese. Germany, on the other hand, did not restrict the Japanese cars but allowed them to compete with the German cars. Germany could afford a more liberal attitude, as it was the only automobile producing country with an export market. The unification of Germany had further expanded its domestic market.

The 1992 Single Market Programme made the threat to national producers more real. Japanese cars – imported or produced in the transplant facilities in the UK – would have easy access into the hitherto protected markets, especially France, Italy and Spain. The Commission, realising the possibility of Member States not honouring their commitments, negotiated an agreement with the Japanese in 1991. They agreed


to prohibit the targeting of particular national markets and to retain country quotas. The agreement is an example of the power wielded by national governments. The very fact that the Commission negotiated such an agreement emphasises the fact that Member States endeavour in their domestic policies and practices to further their own interests while at the same time limit further integration.

**Broadcasting**

As per Articles 59 and 62 of the EEC Treaty, there should be no restrictions on the freedom to provide services within the Community and Member States should refrain from introducing any new restriction on this freedom. Accordingly, there should be no restrictions on the freedom to broadcast across the frontiers of Member States and Member States should not introduce any new restrictions. However, broadcasting has always been organised along essentially national lines with strong national focus and character, and each individual state has reserved the right to regulate broadcasting received on its territory.

By the early 1980s there were profound changes in the technology and economics of broadcasting. The new technologies of satellites and cable, and new terrestrial frequencies removed the constraint of “spectrum shortage”. It was now easy to reach new audiences and cover longer distances without much expense. As a result, broadcasting ceased to be simply within the territorial state. The territorial state was replaced with the “language area”. In the light of these developments, a need was felt, in several quarters, for an EC audio-visual and broadcasting policy. After taking

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82 Kenneth Dyson and Peter Humphreys, “The Context of New Media Politics in Western Europe”, in Kenneth Dyson and Peter Humphreys, with Ralph Negrine and Jean-Paul Simon, Broadcasting and New Media Policies in Western Europe (London: Routledge, 1988), pp 1-3
over as the President of the Commission of the EC, Jacques Delors, addressed the European Parliament at the opening of its 1985 session saying:

Do you know, ladies and gentlemen, that what we might call the culture industry will tomorrow be one of the biggest industries, a creator of wealth and jobs? Under the terms of the Treaty we do not have the resources to implement a cultural policy; but we are going to tackle it along economic lines. It is not simply a question of television programmes. We have to build a powerful European culture industry that will enable us to be in control of both the medium and its content, maintaining our standards of civilisation, and encouraging the creative people amongst us.\(^{83}\)

The general perception was that "... by enabling citizens in one Member State to receive directly or via cable ... unaltered broadcasts originating in others, a cultural inter-penetration can be achieved which will make a significant contribution to the European Community’s future development as a genuine Community.\(^{84}\) But, as the Treaty of Rome had no provisions for cultural aspects, broadcasting was to be undertaken as an economic measure. In other words, by virtue of being a service, broadcasting must be allowed to cross frontiers without any barriers. As a result, the 1980s saw the “Television Without Frontiers”, a Green Paper prepared by the Commission and the Community’s Directive on Broadcasting. Nevertheless, the fragmented and closed nature of the European markets continued to be a barrier to single market. In Procureur du Roi v Marc J.V.C. Debauve and Others (1980),\(^{85}\) Belgian law allowed cable operators to broadcast programmes from other Member States but did not allow the advertisements that accompanied the programmes. This was essentially a barrier as normally the programme is broadcast from a foreign


\(^{85}\) Case 52/79, Procureur du Roi v Marc J.V.C. Debauve and Others [1980] ECR 833
possible were eliminated from 1 January 1993 and those which remain
were removed to traders’ premises. This means there are no regulatory
takes at the internal frontiers, but trader-based controls provide
adequate safeguards in order to protect our high standards .... The UK
is committed to retaining controls to protect society subject to them
being justifiable, proportionate to the risk involved and involving
minimum burdens to business.127

But, the real barriers to trade were never really border controls and paperwork. The
real barriers are the numerous national regulations and standards. First and foremost,
what the Single Market programme did was to put harmonisation of technical
regulations on hold and replace it with mutual recognition. By concentrating on
deregulation, the 1992 programme carefully attempted to avoid having to make
detailed Community policy decisions in areas of “vital national interests.”128
However, mutual recognition by itself does not automatically lead to opening of
national markets. This is because access to national markets continues to be regulated
by national legal norms or product standards. The need, therefore, is to adjust national
provisions, which will still have to be imposed on the Member States on a case-by-

HM.S.O.: The Department of Enterprise, 1993), p.15
129 Jeanne-Mey Sun and Jacques Pelkmans, “Regulatory Competition in the Single Market”, Journal of
similar legislation. The two countries successfully kept other Member States’ products out on this ground. The other ten Member States wanted to take the UK and Ireland to Court but the Commission felt that UK and Ireland had a strong case under Article 36. Subsequently, UK managed to coax the others to adopt similar measures and have an EC Directive in this regard. By 1993 when the Commission was finally set to discuss a proposal for a Directive, Commission President, Jacques Delors, withdrew the proposal invoking subsidiarity as a justification. 130 This effectively meant that regulatory autonomy was transferred back to the Member States. The Maastricht Treaty introduced the principle of subsidiarity as one of the general principles with constitutional importance. 131 Further, the Edinburgh Summit of the European Council in December 1992 adopted a document that ensured that the principle of subsidiarity was observed in the everyday working of the Community institutions. 132 The essence of subsidiarity was that the Member States themselves may take all decisions and only if “the objectives of the proposed action cannot be sufficiently achieved by the Member States” may the Community take them. 133 Such a transfer of competence back to the Member States implies erosion of the achievements of the Single Market programme.

Secondly, mutual recognition replaced the principle of unanimity with qualified majority vote (QMV). However, QMV is not applicable in case of fiscal provisions, free movement of persons and rights and interests of employed persons. 134 Further,

130 Ibid., pp 79-80
131 Article B, Title I, Treaty on European Union
133 Article 3b, TEU
134 Article 18(2), SEA [Article 100A(2), EEC Treaty]
proposals concerning health, safety, environmental protection and consumer protection would entail "a high level of protection." This has enabled Member States to impose new and subtler barriers at the national level. These new obstacles are associated with public policy objectives and include environmental regulations or more sophisticated technical requirements.

Therefore, clearly Member States have gained regulatory autonomy and where they cannot exercise autonomy they continue to resort to non-tariff barriers that are subtler and more sophisticated.

Regarding fiscal measures, the Economic and Financial Affairs Council adopted on 19 October 1992 an agreement that a legally binding minimum standard rate of VAT of 15 percent would apply until the end of 1996 and would be subject to review at the end of 1995, which would require the unanimous agreement of all Member States. However, national resistance to change was strong with the UK refusing to give up its zero rates on food and children's clothing, and Denmark not agreeing to bring down the rates on alcohol and tobacco. Harmonisation had strong political overtones – politicians played these cards in their national politics, so also governments used fiscal policy for stabilisation purposes. As a result, slowly but steadily, Member States managed to erase "tax harmonisation" from Community jargon and instead introduced "tax co-ordination", which is less ambitious and implies a coming together of member states rather than a Directive from above. In the words of Heinz Jurgen Selling, the representative for the Government of Germany, "tax co-ordination is the procedure by which EU Member States co-operate in order to overcome tax obstacles for cross-

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135 Article 18(3), SEA [Article 100A (3), EEC Treaty]
136 UK, Department of Trade and Industry, n.127, p.14
country, which the cable operators simply receive on their dish and then redistribute among consumers. It is not in their hands to edit the advertisements. Another argument would be that when a common market already existed, where was the need to ban the advertisements of other Member States' products? The verdict of the Court, however, was that since Belgian law prohibited commercial advertisements for both national and non-national broadcasts, it did not constitute a barrier. Similarly, in *S.A. Compagnie Générale pour la Diffusion de la Télévision, Coditel, and Others v S.A. Ciné Vog Films and Others* (1980), the exclusive rights to distribute a French film in Belgium for seven years was granted to Ciné Vog. But, during that period, a German channel broadcast this film, which the Coditel companies relayed in Belgium over their cable diffusion networks, thus jeopardising the commercial future of that film in Belgium for Ciné Vog. Here again, the Court held when copyrights were involved then broadcasts of such programmes are not allowed. Thus the Court legitimised barriers such as advertisements and copyrights. Even the Council Directive concerning broadcasting activities (1986) clearly stated that “... the Member States shall ensure that broadcast advertising in internal broadcasts is checked prior to transmission and is broadcast only if it complies with the rules of this section.”

Further, “the Member States shall ensure that the retransmission by cable in their territory of internal broadcasts from other Member States may take place with respect for applicable copyright and related rights, in particular on the basis of contractual agreements between right owners and cable operators.”

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88 Article 17, ibid., p.28
One of the first steps taken to usher in the Single Market in broadcasting was the requirement that Member States ensure that internal broadcasters of television reserve at least 30 percent of their programming time other than news, sporting events and game shows, advertising or teletext services for broadcast of Community works. However, nothing much came of this requirement. In the words of Martin Bangemann, Vice-President of the European Commission and the Commissioner responsible for DG III, the quota provisions in the Directive were only "politically binding" and not "juridically binding". Almost all Member States were opposed to this idea. Belgium, Germany and Denmark questioned the Community's competence in this regard, while the UK dismissed it as saying "... we can't expect them to show Jacques Tate all the time to meet the quota." The governments tended to be more concerned to protect or promote their own "national champions"; they had different views on the appropriate forum to discuss European collaboration. For example, Germany preferred the Council of Europe to EC to discuss the issue as it included other German-speaking countries - Austria and Switzerland. Another feature of the endeavour was the rejection of "Community programmes" by the audiences. They preferred their national services. The major factor behind this was language. It would logically suggest that Europe not only needed a common culture but also a common language and it naturally pointed to English, but the idea itself was dynamite.

The result of such opposition and fragmentation of the market was that the tone of the Community approach has also changed from the idea of broadcasting fostering...
European unity to emphasis on preservation of the cultural diversity of the Community. In the words of Mariano Maggiore, former Deputy Head of DG X's Audio Visual Directorate, "we have no interest in promoting a melting pot. We want to preserve European identities ... we don't want to leave the audio visual to the English language media."93 The main thrust of the Community's recent policies is to strengthen pluralism by encouraging, in particular the diversity of the programmes offered to the public.

Alcoholic Beverages

Another interesting example is that of alcoholic beverages. Alcoholic beverages play an integral part in the social and private life in Europe. Beverages with varying degrees of alcohol content are produced by almost every Member State. Some like Champagne of France or Scotch whisky of the UK are world famous and are very peculiar to the region they come from. France is known for its variety of table wines and has had a surplus production right from the beginning. In fact, along with cereals and sugar, France had surplus production of wine as well and had insisted that price mechanism of the Common Agricultural Policy be extended to it. However, France faced cheap competition from Italy and Spain. Other Member States, be it Germany or Denmark, also have their own productions. Germany and the UK are known for their beer drinkers and production. Since all Member States produce some variety of alcohol beverages, which fall under the "similar" products category of Article 95, and since the consumption in almost all Member States is high, it becomes imperative for each Member State to protect its own products. This is one product for which there is

stiff competition and every Member State adopts some measure or the other to keep imports out.

As early as in 1968, the Trade Negotiations Committee for the GATT had identified France as resorting to non-tariff barriers such as a total ban on advertising of alcoholic beverages distilled from grain. This effectively discriminated against whisky and gin, which, though not produced in France, did compete with French beverages. There were also various taxes imposed on alcoholic beverages in France. VAT and alcohol consumption tax was uniform for all beverages but the grain alcohol tax was applicable only on gin, whisky and vodka; and the aperitifs surcharge, which was extended to cover these beverages. The overall impact of these taxes on gin, whisky and vodka was that their prices had increased by 73 percent overall. Germany, on the other hand, had a system whereby the duty on imported spirits had to be paid immediately while domestically produced spirits had a six months deferment which effectively meant that German producers did not pay duty until after the payment was received from customers to whom they could in turn offer deferred terms, while importers had to pay before distribution.

As mentioned earlier, Dassonville and Cassis de Dijon were two trend setting and law making cases in the history of the ECJ. In the former, Belgian authorities required that a certificate of origin accompany all Scotch whisky coming from the UK. The Belgian claim was that this measure would ensure the originality and quality of Scotch whisky. In the latter, Germany did not allow the sale of a French beverage Cassis de Dijon, a liqueur spirit, made from blackcurrants, on the ground that it had too low

94 PRO/TN (68) 3, n.72
95 Ibid.
alcohol content to be labelled spirits and too high to be classified as wine. The German argument was that Cassis, with low alcohol content, could more easily induce a tolerance towards alcohol than more highly alcoholic beverages. Moreover, by lowering the alcohol content the product secures a competitive advantage in relation to beverages with higher alcohol content, as alcohol is the most expensive beverage by virtue of the taxes imposed on them.97

Germany later used the health card to assert the traditional Reinheitsgebot of 1516 as a reason for excluding imported beer. According to the Reinheitsgebot, beer must contain only barley, hops and water and no chemical additives. This requirement meant that all non-German beer would be excluded from being sold in Germany as beer.98

The UK had a rate of excise duty on still wine produced in other Member States at UKL 2.955 per gallon till 1976. From 1 January 1977 it was raised to UKL 3.250 per gallon. At the same time, the rate of excise duty on locally produced beer was only UKL 0.557 per gallon till 1976, which was raised to UKL 0.613 per gallon from 1977. This amounted to a discrimination against wines produced in other Member States. UK argued that there was no comparison between wine and beer but as mentioned earlier, there is a degree of substitution for one another as to a certain extent at least the two beverages were capable of meeting identical needs.99

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96 Ibid.
97 Rudden and Phelan, n.66, p.117
98 Vickerman, n.76, p.87
Similarly, Italian legislation imposed a manufacturing tax on nationally produced wine alcohol and an import tax on imported wine alcohol. Both taxes amounted to the same. But, an exception was granted in favour of wine alcohol used in the production of the home liqueur Marsala. The reduction amounted to 60 percent of the basic amount.100

Denmark produces wine mostly made of fruit and not grape. The taxation system in Denmark discriminates against table wine and wine liqueur made of grapes. Bulk of the domestic products fall within the favourable tax category. The ECJ ruled fruit wines and grape wines display similar characteristics, meet the same needs, are obtained by fermentation, have a similar alcohol content and are consumed in the same quantities.101 The bottom line is that the tax systems tended to have a bias built into them that favoured home products.

Another means used by Member States is to lay down national rules regarding description of the product, labelling, bottling, and other standards, which in effect do not allow products from other Member States enter their markets. For example, in Fietje, a product Berentzen Appel made from apples and spirit distilled from wheat, imported from Germany was not allowed sale in the Netherlands, as it did not have the description “likeur” on it. Having to add such a description adds to the cost of the supplier and hence prohibits him from importing the product.102 In Gilli and Andres,103 Italian authorities prohibited the import of apple vinegar from Germany on the ground that Italian law was clear that vinegar could only be produced from wine.

100 Case 277/83, Commission of the European Communities v Italian Republic [1985] ECR 2049
101 Case 106/84, Commission of the European Communities v Kingdom of Denmark [1986] ECR 833
102 Case 27/80, Criminal Proceedings Against Anton Adriaan Fietje [1980] ECR 3839
103 Case 788/79, Gilli and Andres [1980] in Charlesworth and Cullen, n.30, p.228
In case of Danish regulations, all beer must be sold in returnable bottles with refundable deposits. This meant foreign producers face higher costs and hence almost all beer consumed in Denmark is locally produced.\textsuperscript{104}

**White Paper on Completing the Internal Market**

The ultimate aim of the European Community was never specified, either in the Treaties or in the subsequent dealings. “An ever closer union among the peoples of Europe” did nothing but hide the likely implications of the creation of the Common Market. Occasionally, Member States would voice their concerns about the measures taken to strengthen the competence and authority of the EC institutions. Such protests “seemed to reflect anxiety over an inability to make others in the EC follow a line prescribed by one states national interest.”\textsuperscript{105} At the same time, the EC was an arrangement that was beneficial to all Member States in some way or the other and it offered them a forum to pursue national interests. Exclusion from the EC would be expensive as the non-member has to forfeit input into further decision-making in the EC and also it would have to forgo whatever benefits result from them.\textsuperscript{106} As a result, either because Member States wanted the EC to continue to be a forum for pursuing their national interests or because the European politicians never anticipated the magnitude of what they were agreeing to,\textsuperscript{107} when in 1985 Jacques Delors, the Commission President and Lord Cockfield, Vice-President and Commissioner

\textsuperscript{104} Vickerman, n.76, p.87
responsible for internal market, brought out the White Paper on completing the internal market.

The White Paper exposed the failure of the EC as it prescribed exactly what the EC had set out to do in 1957 i.e. create a Common Market with free flow of goods, services, capital and persons. Lord Cockfield identified 300 measures required to establish a Single Market. These were subsequently reduced to 282 measures. The intellectual foundation was provided by the Cecchini Report, a sixteen-volume report on the cost of non Europe. Besides an introduction, the White Paper consists of a description of each measure required to eliminate a barrier, and a timetable for each measure to complete the internal market by the end of 1992.

The White Paper classified all measures under three heads:

**Physical Barriers**

The most obvious example of this category are customs posts at frontiers. According to Professor Tsoukalis, some of these frontier controls were the result of gaping holes in the common commercial policy, examples being quantitative restrictions on imports from Japan, and multi-fibre arrangements for textiles and clothing imports from third countries.\(^{108}\) However, frontier controls are not merely because of gaps in the CCP. It is mainly because of gaps existing in the common market. In agricultural trade among Member States, there exists tax and subsidies in the form of monetary compensatory amounts, which calls for checks and paper work at the frontier.\(^{109}\)

Similarly, because different standards exist in different Member States regarding health, specifications, packaging, etc., there is need for checks on the border. In

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\(^{108}\) Tsoukalis, n.47, p.68

\(^{109}\) See Chapter 3
addition, different rates of indirect taxation also call for fiscal controls at the frontier. Lastly, factors that touch the core of national security and sovereignty like public security, immigration and drug controls call for physical barriers.\textsuperscript{110}

**Technical Barriers**
These barriers cover a host of trade barriers such as different technical regulations and standards. This category also includes recognition of workers' qualifications in different Member States and the different regulatory systems for services, especially financial services. Other aspects include legal differences such as on company law and Community wide competition in public procurement. Public purchasing is particularly concentrated on building and civil engineering, energy products (for example, electricity generation, oil), telecommunications, transport equipment and business services. Only a small proportion of these public sector contracts are awarded to companies from other EC Member States. Protectionism and discrimination is practised by national governments by not publicising information on their buying requirements, as such keeping firms of other Member States from bidding.\textsuperscript{111}

**Fiscal Barriers**
When the EC was formed the Member States had very different systems of taxation. In most countries the system of indirect taxation was based on the cascade system, in which a full ad valorem tax was levied at each stage of the production process. Under such a system while remitting turnover taxes on exports if it was too little then it meant that exports were artificially disadvantaged, but if it was too much then it

implied an artificial export aid. This worked as a non-tariff barrier to trade.\textsuperscript{112} The main achievement of the Community has been the adoption of a uniform system of turnover taxes based on French system of value added tax. This is a system where tax is paid at each stage of production on the value added at each stage in the production process. But, even under VAT, if a product faced a turnover tax of 10 percent in one Member State, and the same product faced a 20 percent tax in another Member State; and if the product from the first state is exported to the second then it has an artificial competitive advantage in the country of destination. Hence there was the need to adopt the destination principle wherein the VAT rate of the country of destination is applicable and not that of the country of origin. In 1987, the Commission called for a shift from the destination principle to the common market principle that simply meant extending the national regime to cross-frontier transactions. The importer would be able to deduct the VAT payment. The Commission proposed that there be a standard VAT band of 14-20 percent and a reduced VAT rate of 4-9 percent.\textsuperscript{113}

The Commission also proposed the harmonisation of excise duties. The main thrust in this case also being, as in VAT, to move towards tax minima.\textsuperscript{114} In the long run, the Member States were to converge on target rates or narrow (2 percent) target bands. Lastly, the White Paper stressed the need for harmonisation of corporate tax. This is because tax competitions, wherein Member States tend to lower taxes, create

\textsuperscript{112} Swann, n.26, pp 156-7
\textsuperscript{113} \textit{Bulletin of the European Communities}, 1985, Vol.18, No.5, p.8
loopholes against other Member States so that they attract business activities, leads to distortion of trade.

**Progress to the Single Market**

The implementation of the White Paper was not possible under the existing Treaty provisions. Accordingly, the European Council meeting in Milan on 28 and 29 June 1985 decided to convene a conference of representatives of the Governments of the Member States "to draft the provisions needed to achieve concrete progress on European Union with regard to ... changes to be made to the decision-making process and the inclusion of new policies of activity in Community competence."\(^{115}\) The Inter-Governmental Conference (IGC) held on 16 and 17 December 1985, under the chairmanship of Jacques F. Poos, the Foreign Minister of Luxembourg, finalised all the texts in a "Single European Act".\(^{116}\) The SEA was clearly a very watered down version of Alterio Spinelli's proposal for a federal Europe, "Draft Treaty Establishing the European Union" (1984). Spinelli had suggested regarding internal market that the union should have exclusive competence to complete, safeguard and develop the free movement and also free trade between Member States.\(^{117}\) Further, the liberalisation process should take place on the basis of detailed and binding programmes and timetables laid down by the legislative authority. Accordingly, within two years of adopting the Treaty, the Community should achieve free movement of goods and persons.\(^{118}\)

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\(^{115}\) Bulletin of the European Communities, 1985, Vol.18, No. 7/8, p.9

\(^{116}\) Bulletin of the European Communities, 1985, Vol.18, No.12, p.9


\(^{118}\) Article 45(2) and (3), ibid.
What the SEA did was lay a time frame for establishing the internal market i.e., by 31 December 1992. Whereas decisions regarding services, movement of capital and transport were to be taken by qualified majority vote, any changes in the common customs tariff, mutual recognition of degrees and fiscal measures continued to require the unanimity principle.119 Further, the continued existence of the Luxembourg compromise negated this shift to qualified majority vote.120 Geoffrey Howe, Foreign Secretary of the UK, announced in April 1986: “As a last resort, the Luxembourg Compromise remains in place untouched and unaffected .... [It] is not a provision of the Treaty; it is a component of political reality in the Community ... [and] is in no way affected one way or the other by the Single European Act.”121 Besides, regarding the Single Market, most measures have the status of Directives or Decisions, as opposed to Regulations that pass directly into national legislation; they have to be enacted by each member government. Therefore, the SEA’s provisions are a far cry from Spinelli’s call for exclusive Community competence regarding free movement.

The share of measures actually transposed into national legal systems gives a first rough indicator of the degree of implementation of the overall programme. By mid-1991, the Commission reported that all 282 measures of the 1985 White Paper had been presented to the decision-making bodies but 89 of them were yet to be agreed.122 By mid-September 1996, however, Member States had transposed on average 92.9

120 According to the Luxembourg compromise if the vital interests of any Member State is involved then it has the right to veto a proposal.
122 Vickerman, n.76, p.107
percent of the measures. The fact that most of the Single Market programme legislation has been transposed into domestic legislation is a necessary but not a sufficient condition for the Single Market to actually work. According to Vickerman, an analysis of the measures actually transposed into national legislation showed varying degree of enactment by Member States. Besides, it is not the number of measures enacted (or not enacted) that are crucial but specific measures that matter. For instance, by retaining duty-free allowances until 1999 and not agreeing on the harmonisation of the VAT regime, Member States have ensured that crucial specific measures are either delayed or not enacted. Hence, instead of a genuine Single Market we have a watered down version.

The main symbols of the Single Market were, as explained earlier, removing frontier controls, technical regulations and standards, and, the harmonisation of fiscal regimes. All evidence seems to suggest that these main objectives have not been fulfilled entirely. Customs formalities at the frontiers in most cases have been removed but instead of abolishing them they have been simply shifted from the frontiers inland, in part to businesses themselves. Also, additional administrative costs on cross border deliveries of goods and services still remains. For instance, the Department of Trade and Industry, UK, reported that:

Many of the controls operated up to 1 January 1993 by UK customs at the frontier in respect of restricted and prohibited goods were based on the requirement to produce documentation. As many of the controls as

123 Ibid.
125 Vickerman, n.76, p.108

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border activities without giving away sovereignty ... By contrast tax harmonisation has some common rules for the tax structure.  

In the final analysis, it is beyond the scope of the chapter to examine the degree of adoption of all the 282 measures suggested by the 1985 White Paper. But, a close look at the main symbols of the White Paper reveals that none of them have been adopted in the spirit suggested by the White Paper. While frontier controls simply moved inland, national regulations and standards continue in newer forms, and fiscal measures have also been diluted in order to suit the member countries. In none of these areas have they surrendered sovereignty completely to the EU. While the Member States still need the EU for their survival, they continue to ensure that it does not mean the end of the nation state. The nation state continues to be all-powerful in the EU. And, this is where the EU differs from its precursor, the Zollverein.

Conclusion

The Zollverein also followed the negative approach to integration, emphasising the removal of barriers to trade among the numerous German states and establishing a common external tariff. The approach worked well for Germany as it soon transformed from a backward society to one of the leading industrial states of Europe. The Zollverein was instrumental in bringing about the economic integration of the German States and when they were finally politically unified under Bismarck's Second German Empire in 1871, the Zollverein was easily absorbed.

The similarity between the Zollverein and the Common Market are many. Both were established broadly under similar circumstances; both brought hitherto warring and

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divided entities together, where both big powers and small states co-existed; and, both were instrumental in removing a major chunk of the barriers to trade among members with the result that trade increased and that there was economic growth and modernisation. However, whereas the German States were ultimately politically unified to form the State of Germany, it is not clear if the Member States of the EC expect such an end result. Though the Treaties talk about an “ever closer union among the peoples of Europe”, a political union seems as remote as ever.

The EC was established as an antidote to the aggressive nationalism. Continuous wars had completely devastated each and every country of Western Europe. Peace, economic recovery and modernisation were the sought after mantras in Europe. These were absolutely essential for the survival of the nation state. And by providing these, the EC “rescued” the nation states of Europe. Throughout the 1960s the countries of Western Europe experienced remarkable growth and modernisation. Unemployment levels were low, balance of payments was stable and the currency markets were also stable. But, when conditions changed in the 1970s, the cracks in the picture-perfect EC started to appear. Yes, the EC had rescued the nation state, they now were able to survive, but when the oil crisis hit their expenditure levels and balance of payments, when the dollar ceased to provide the much needed stability to their currencies and when aggregate demand started to fall leading to unemployment and instability, the nation state sought its own rescue. Protection of national interest became first priority. Domestic markets were protected by means of numerous frontier controls, non-tariff barriers and fiscal measures. The state came to replace free market conditions. The state promoted national champions, diverted trade by means of public procurement,

(London: The Stationary Office, 20 July 1999), para 54, p.16

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imposed numerous regulations and standards preventing access to products from other Member States, and so on. For all practical purposes instead of a Common Market, twelve individual markets were in action with twelve different national monetary and fiscal policies.

The 1985 White Paper on Completing the Internal Market identified and acknowledged these ills and provided ways and means to attain the goal of Single Market by 1992. All of a sudden 1992 became a much-hyped year, when suddenly the Community was expected to transform itself. The White Paper identified 300 measures for achieving this goal. But, because of disagreement among Member States, finally they were brought down to 282. Broadly, the White Paper attacked fiscal measures, technical regulations and standards, and frontier controls for hampering free movement. The SEA made the relevant amendments to the Treaty in order to put to practise these measures. But, the magic date came and went and the Single Market continued to elude the Community.

Yes, by mid-1996 almost 93 percent of the measures had been transposed into national legislation. But is that really the yardstick to measure the success of the Single Market? While the degree of enactment of the measures varied among the Member States, even the ones enacted were simply done in the literal sense. Frontier barriers were removed from the borders but simply shifted inland. Regarding technical regulations, harmonisation gave way to mutual recognition but this only gave the national governments more regulatory autonomy. If the 1992 programme failed in terms of being completed by the end of 1992, then it is mainly because businesses could easily coax national governments to enact new technical regulations to protect national interest. Now, the common non-tariff barriers have disappeared but new sophisticated ones are adopted by Member States, notable among them being
environmental standards. Similarly, there is no difference in the sphere of public procurement. It continues to be a national business. Governments adamantly refuse to advertise on a Community wide basis. At the same time, the principle of subsidiarity, which has been institutionalised by the Maastricht Treaty, passes the competence right back to the nation state. The White Paper had sought the harmonisation of fiscal measures but lack of agreement among Member States has watered it down to coordination of taxes. The emphasis is surely being shifted from binding rules to voluntary cooperation.