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EC-92: CATALYST FOR CHANGE

BY

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The Single European Act of 1987, commonly referred to as EC-92, is a major European Community program to create a single, integrated European market by the end of 1992. The primary objective of EC-92 is to remove intra-Community barriers to free movement of trade. The program has been successful to an unprecedented degree in Community history. Its success has spawned renewed enthusiasm in the European Community to progress further in economic and political integration. Additionally, the economic success of EC-92 has attracted non-Community countries to seek closer affiliation or membership with the Community. The growing economic strength of the Economic Community has also put it in a leading role in world affairs. As Community influence grows, its institutions and processes are being challenged to adapt to the new role as a leading world economic power. This paper is an overview of the growth of the European Community, its emergence as an independent world power, the impact of recent major world events on the Community, the Community's progress towards Economic and Monetary Union, its progress towards Political Union and its prospects for the near term.

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EC-92: CATALYST FOR CHANGE

AN INDIVIDUAL STUDY PROJECT

by

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ABSTRACT

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The Single European Act of 1987, commonly referred to as EC-92, is a major European Community program to create a single, integrated European market by the end of 1992. The primary objective of EC-92 is to remove intra-Community barriers to free movement of trade. The program has been successful to an unprecedented degree in Community history. Its success has spawned renewed enthusiasm in the European Community to progress further in economic and political integration. Additionally, the economic success of EC-92 has attracted non-Community countries to seek closer affiliation or membership with the Community. The growing economic strength of the Economic Community has also put it in a leading role in world affairs. As Community influence grows, its institutions and processes are being challenged to adapt to the new role as a leading world economic power. This paper is an overview of the growth of the European Community, its emergence as an independent world power, the impact of recent major world events on the Community, the Community's progress towards Economic and Monetary Union, its progress towards Political Union and its prospects for the near term.

Introduction

The European Community is deeply embroiled in trying to integrate itself more closely as it continues to gain economic strength and political relevance. Increasingly, the Community is being treated as a major power in world affairs. Military power is becoming less important as a measure of influence, while the idea of great power is being redefined with a more economic content.[1] Jacques Attali says the old "Order of Force has been supplanted by the Order of Money, that is the reign of the market."[2]

The European Community has evolved from a customs union to a supranational institution whose stage of development is like an adolescent trying to know itself and understand its relationship to the rest of the world. It is just now realizing its impact on others and while anxious to take a place in the world, is seen as not yet totally prepared for its role and as a threat to existing structures. To complicate things, the world around it is dramatically changing and not quite in control of itself.

Community trade with the U.S. is illustrative of the European Community's growing influence. For the second straight year, exports to the European Community grew and totalled $98.1 billion for 1990 and resulted in an American trade surplus of $6.1 billion. This makes the Community the United State's largest single trading partner, and the most beneficial.

The single most important event leading to the economic success of the Community was its commitment to the Single European Act of 1987, also known as EC-92. It has been the catalyst to propel the Community into the forefront of European, as well as world, politics. The economic success of EC-92 amidst the changes in Eastern Europe, the unification of Germany and the Gulf crisis agitated debates over membership expansion, economic and monetary union and the need for deeper political cooperation and union. Central to the debate is how willing are Community members to pay a price for potential benefits by abrogating traditional sovereign functions to the European Community. The European Community has a spotty history of success in making fundamental change to its charter. However, the "failures were positive because they sensitized policy makers and the population to the risks of unbridled nationalism and unlimited sovereignty."[3] The member states generally perceive interdependence costs to be far less than benefits received.[4]

This paper will explore the current status of the major Community issues of expanding and/or deepening the European Community. Expansion is concerned with adding new members and deepening refers to achieving closer internal integration through economic and monetary union and closer political integration.

Background of the European Community

Following World War II, European leaders and intellectuals saw the need to unify Europe in some way in order to lessen the chance of war and to rebuild their economies. Germany was making substantial progress at reconstruction but presented itself as a potential problem, especially to French leaders. Jean Monnet saw his chance to subsume the German problem through a process of European economic and political integration. He proposed that French and German coal and steel production should be put under a common authority in an organization open to other European countries. In 1950 the French Foreign Minister, Robert Schuman, proposed the creation of the European Coal and Steel Community (ECSC) to establish a common basis for economic development and as a first step in uniting Europe. Germany was again being treated as an equal but by pooling basic resources the probability of war was lessened. The ECSC High Authority became a power independent of its member states in the responsibilities transferred to it. Accepting this principle of supranationality was a prerequisite for membership in the ECSC. Six nations, France, Germany, Italy, Belgium, Luxembourg and the Netherlands signed the ECSC Treaty. Britain declined to sign because it had just nationalized the coal industry and was unwilling to give up control over it to a supranational organization.

Efforts to further integrate Europe continued. In 1957 the six ECSC members signed two additional treaties; the European Atomic Energy Community (EURATOM) treaty and the European Economic Community (EEC) treaty. The EURATOM Treaty was to further the use of atomic energy and the EEC's purpose was to form a common market by merging separate member markets into a single market with common economic policies. This became known as the Treaty of Rome from which the "Common Market" emerged.[5]

The EEC developed a customs union in addition to initiating agreements to dismantle quotas and barriers to trade and free movement of capital, people and services between member countries. Agricultural and fisheries policies were supranationalized under the authority of a commission and early steps were taken to harmonize tax policies.[6] Some policy decisions were subject to qualified majority voting but the largest part still required unanimous consent of member countries.

Britain had sent an observer to the conference but withdrew him when talks drifted to creating a customs union. Thus, Britain isolated itself from European economic strength and had to develop a new approach.

Britain formed the European Free Trade Area (EFTA) with six other non-EEC countries. Britain was not prepared to commit to a common agricultural policy or other supranational political and economic objectives of the EEC. However, Britain did want the benefits of free trade in industrial products. EFTA became a pure trade grouping with none of the attendant supranational features of the EEC. By 1961 Finland, Switzerland, Austria, Denmark, Norway, Sweden and Portugal had joined with Britain as members of the EFTA.[7] Hopes to merge the EEC and EFTA into an expanded free trade area did not materialize at that time because members of the EEC, under French leadership, were not going to dilute existing EEC arrangements.[8] Britain tried several times during subsequent years to join the EEC and was rebuffed each time, primarily through the efforts of the French under deGaulle.

In 1967 the executive bodies of ECSC, EURATOM, and EEC merged and formed the basic structure of the European Community (EC). The four executive institutions of the EC were the European Commission, the European Council, the European Parliament and the European Court of Justice. These remain the core EC structures today.

During the late 1960's and 1970's, proposals were put forth and accepted by the EC that called for developing into a more integrated monetary and economic union by 1980. However, international monetary and economic turmoil made progress to achieving these goals impossible.[9]

Other progress did, however, take place. In 1973 Britain successfully joined the Community along with Ireland and Denmark. In 1979 the first direct elections to the European Parliament took place. In 1981 Greece joined the EC and Portugal and Spain joined in 1986, bringing the total membership of the EC to 12 countries.

In 1984 the European Parliament drafted a treaty calling for a European Union. The allocation of responsibilities between member states and the Union would be based on the principle of subsidiarity which means the union would only be responsible for those tasks which would be more effectively carried out in common than by the individual states on their own. The areas of competence were divided into common action and cooperation between states. Common action would normally be taken by majority vote and cooperation would be by unanimous decision. French President Francois Mitterand, as president of the Council, persuaded his fellow Heads of Government to work out proposals for adapting the Draft Treaty. This was a key stimulus in the movement to the Single European Act (SEA).[10]

The Single European Act of 1986

The 1957 Treaty of Rome was aimed at a common market without barriers and should have resulted in mutual prosperity for the member states. Indeed, things went well at first. However, during the 1970's the pace of growth fell off and economic crises, especially the 1973 oil crisis, eroded community cohesion and moved governments into protectionist policies. Countries looked inward and tried to find national solutions to their economic problems. The goals of the EC were becoming impossible to achieve as protectionist measures fragmented the market and increased the cost of doing business.

In 1983 the European Parliament published the Albert - Ball Report, which showed how the EC was hurting itself by not working together to overcome crisis. Subsequently, in 1985 the EC Commission vice-president, Lord Cockfield, presented a White Paper entitled Completing the Internal Market. It outlined provisions and a timetable for further integration of the economies of the 12 member countries. It proposed the removal of all internal Community barriers to the free movement of goods, services, capital and people within the Community.

The White Paper proposals were approved by the EC Heads of Government in 1986 and came into force in 1987. It became known as the Single European Act (SEA).

The SEA established the objective of completing the EC internal market structure, through economic and monetary policies, by the end of 1992. It substituted weighted voting, or a qualified majority, for the Council in most areas relating to the internal market. Additionally, it established a political secretariat to assist in expanding the EC role in foreign policy development. European economies began to flourish.

The catalyst for EC invigoration was the projected economic benefit of a single internal market by the end of 1992. The first imperative was to begin removing some 282 identified barriers to trade. These barriers fall into three main categories of physical, technical and fiscal. Physical barriers include excessive paperwork, customs controls and border delays. Technical barriers relate to conflicting intra-EC standards, laws and regulations. Fiscal barriers primarily relate to taxes and excise duties. It was clear that these barriers were undermining EC prosperity. This was driven home when Paolo Cecchini published his study on the impact of breaking down protectionist policies and eliminating red tape in intra-EC commerce.

The 1988 Cecchini Report showed the enormous costs associated with intra-EC trade. Just as important, it showed how opening the market would lead to strong economic growth and vigor. The study projected an overall 4.5% growth in the EC's gross domestic product (GDP), a 6% reduction in consumer price, a substantial increase in economic activity and a reduction in unemployment with the potential for six million new jobs.[11]

European businesses moved out as if EC-92 was going to happen and as a result, EC members economies have been expanding. The priv te sector, motivated by market success, has been maintaining pressure on EC governments to implement the White Paper recommendations.

The EC Commission has formally proposed all 282 regulations and directives to the EC Council. The Council has adopted two-thirds of the Commission proposals. However, implementation by member states is falling behind and is expected to take several years to complete.[12]

EC-92, the program of the SEA to complete the integration of the EC's internal market by the end of 1992, is well on its way. Additionally, the success of this process has stimulated activity to achieve other EC goals of developing greater economic and political union. European Federalists see the main goal of the EC as political union and the means to achieving that goal as economic. Certainly, that was Jean Monnet's intention as he set about inspiring the European community to come together in an economic union.[13]

Integration or Expansion

The momentum of EC-92 and the rapid changes brought on by world events since 1989 served to focus the nature of Community debate over the direction of the EC. The emergence of Central European democracies, the unification of Germany and the Gulf war had profound impact on the course of debate and agenda setting of the EC. Questions of deeper economic and political integration are competing with the issue of widening the EC by increasing its membership and expanding relationships with non-EC European Trading partners. "The EC can either evolve into an all European trade and monetary arrangement, or into a politically much more cohesive union of West European states."[14]

The question of expanding EC membership includes not only those Western European countries who have already asked for admission, and those likely to, but involves integrating the new Central European Democracies as they qualify for EC membership. "Democracy and market economy would be the only conditions for membership; the E.C's ambition would be limited to facilitating economic intercourse within the organization, and protecting the economic interests of its combined members without."[15]

Deepening the EC would involve strengthening political integration, so that the EC would speak and act as a stronger union in world affairs. This would include assuming more of the role currently played by nation-states. EC member states would have to cede more sovereignty to the EC. The dilemma facing the

EC is: if it wants to expand, political integration will be harder to achieve; if the EC wants to deepen its political integration then it will have to hold expansion in abeyance.

The Widening Agenda

The EC has decided to postpone any new membership negotiations, in order to deal with an overloaded agenda of completing EC-92. It is clear, however, that pressure will build to expand the EC as it gains institutional success and continued power. Potentially the EC could include every European country (Article 236 of the EEC Treaty). The new member must only be able to accept the EC rules of membership and meet the prevailing democratic and judicial standards of the other member states.[16] While only two years ago this possibility seemed to be a pipe dream, the unification of Germany and the radical changes in Central Europe have opened up speculation of a European Community stretching from the Atlantic to the Urals. Some European Federalists see this as the time to be forming a United States of Europe. Just as the United States of America started with a core of states and grew to today's fifty, so too would the EC form the nucleus of an expanding European Federation.[17]

Today the EC has applications, or is working with initial inquiries, for membership from EFTA countries, non-aligned countries, and several emerging Central European democracies. The success of the EC is a powerful inducement to join. It is argued that EC success "helped accelerate the fall of Communism in the East."[18]

Some countries are motivated simply by the costs of not being part of a growing economic power. The improved competitiveness of the EC is hurting non-member trade and welfare. EFTA countries are particularly pressed because the EC is EFTA's largest single trading partner. As the EC completes its single market, the effects could be significant if economic relationships with the Community continue to be determined simply by the free trade agreements with individual countries that date from the early 1970's.[19]

The history of EC-EFTA relations has been largely determined by the nature of the organizations. The EC is much more politically and institutionally integrated than EFTA. It has developed a number of common policies, while EFTA has not, because EFTA is much more reluctant to accept supranational institutions over sovereignty.[20] Nonetheless, the EC and EFTA have negotiated free trade agreements (FTA's) since 1973. They have also worked together to develop means to exchange information and form consultations to improve the general economic environment.[21] However, deeper relationships have always foundered on basic differences between the EC and EFTA. The differences, "comprehensive goals versus limited goals, supranationality versus intergovernmentalism, Community law versus international law, will continue to set limits for a new structured partnership."[22]

These differences are central to the difficulty being encountered in the negotiations to formulate a European Economic Space (EES), now being referred to as the European Economic Area (EEA), that will allow EFTA and other non-EC European countries access to the four freedoms of the EC's internal market - the freedom of movement of capital, goods, services and people.

The impetus for negotiating an EEA stems from two major factors. The first is non-EC businesses which feel the pressure of being in a poor competitive position in the EC markets. They are pushing their governments to formulate more favorable arrangements with the EC to avoid being locked out of an accelerating market process. In some cases, the pressure is directed at the government to abandon EFTA association in favor of full EC membership. The second impetus came from European Commission President Jacques Delors. In 1989 he proposed tightening the EC-EFTA bond through the EEA.

Delors' rationale was that EC-92 precluded the possibility of entertaining any new EC membership. He proposed instead a concept of a Europe of concentric circles - The European Economic Space. By creating an economic halfway house with EFTA, "the EC could forge greater economic links with its neighbors, while excusing them both from the benefits and obligations of political participation."[23] The proposal has raised a storm of debate in both the EFTA and EC camps.

The fundamental issues remain EFTA's desire to influence EC decisions and process without relinquishing sovereignty. EFTA presses the argument that since EES/EEA rules affect everyone, not just the EC, then all participants require a role in formulating and accepting the rules. The EC counters that sharing decision making would water down the EC's autonomy. In the end, however, it is EFTA which will probably concede the most.

Internal national pressure for greater participation in the EC internal market is rising in EFTA countries. The cost of non-participation is just too high. So as EFTA continues to seek accommodation with the EC, its member states will likely continue to lean toward full EC membership in the post 1993 years.[24]

The success of EC-92 has made EC membership appealing to the countries of Central Europe as well, but they find themselves poorly prepared to participate. The fundamental problems are uncertain democratic governments, the poor economic condition of the emerging democracies and the high costs associated with bringing them to competitive and contributory standards of the EC countries. Even hard line EC Federalists concede the need to develop the economies, as well as politics, of the central states, as a pre-condition of EC association and membership. To do otherwise, would entail too large an economic drain on the EC and a loss of momentum in the core membership to develop it's competitive economic power base.

The EC is moving to assist Central Europe develop itself by a network of trade and cooperation agreements which may serve as a bridge to normalizing relationships. The EC has also established financial networks to assist in economic development in addition to providing direct EC loans to Central Europe. At the 1989 Strasbourg meeting of the European Community Council, the Community affirmed its intention to "continue its examination of the appropriate forms of association with the countries which are pursuing the path of economic and political reform." Future association agreements will be of special value in themselves and should be distinguished from any commitment concerning the question of accession.[25]

The previous paragraph shows the direction the EC has taken in its treatment of Central European States. Its approach has been measured in increments designed to prepare the states before committing either party to closer association. The principle of solid democratic and market based societies as a prerequisite for closer EC association is being firmly adhered to.[26]

Time is a relevant issue when looking at Central European development. The costs of economic and political development will not be quickly absorbed and the harsh reality of a long and tough transition period cannot be ignored. Likewise, the EC recognizes the developmental disparity between individual states and will tailor its relations based on individual progress in economic and political development.[27]

The EC has assumed a central role in reconstructing Europe. As the European Council stated on 9 December 1989 in Strasbourg, "In this time of profound and swift change, the Community is - and must also be in the future - a firm point of reference with a strong power of attraction. It remains the cornerstone of a new European architecture and in its desire for openness - the stabilizing influence in a future European balance."[28]

One of the rising issues of expanding the EC has been what institutional framework should be in place to manage the process. The current proposal under debate centers on Delors' proposition of an EES/EEA that would provide not only an arena for trade but a staged structure for EC membership accession. In this regard, EFTA may be a key element in the process of gaining full EC membership.

"The EC and EFTA could pool resources and offer, in the EES framework, new, flexible forms of cooperation and association to their Eastern neighbors."[29] The EEA would give non EC European states access to the market and allow them to trade, while they work internally to prepare and qualify for full EC membership - if they so desire. EFTA would function as a waiting room for countries desiring EC membership but not ready politically or economically to enter. This transition mechanism would be useful in bringing the Central European states into the western market. The concept has not received universal acclaim but has focused debate on the process in both the EC and EFTA.[30] Milan Cernohuby, commercial counselor at the Czechoslovakian mission to the EC, stated "the EC may have to create a new category - below membership but above mere associate status - to accommodate East European nations. Eastern Europeans won't be satisfied with some associate status designed for the EC's Third World trade partners."31

As the EC continues to reach out to its European neighbors through trade and association agreements, the scope of the Community will expand. The very vitality of the EC that is drawing attention to its widening agenda has highlighted its weaknesses in internal structure. The EC's priorities were clearly indicated with the convening, in December 1990, of two Intergovernmental Conferences (IGC). The first is on economic and monetary union (EMU) and the second is on deepening the political union. In essence, the EC has set its priority to getting its house in order before bringing in new members.

The Deepening Agenda

Economic and Monetary Union

As the EC consolidates its program to complete EC-92, it is confirming the need to deepen EC economic and monetary union. Community leaders hold that without stronger economic and monetary policies and programs, the full potential of EC economic power cannot be harnessed and would fall short in the face of U.S. and Japanese economic mobilization. Although the Community has pursued economic and monetary union for many years, it has been frustrated in gaining unanimous member participation in previous programs.

The success of EC-92 has refocused the attention of the EC on the economic benefits of a single currency and common banking system. The EC report "One Market, One Money" says up to $25 billion in annual savings would be realized by converting to a single European currency. It also proposed that reducing exchange rate fluctuations would stimulate economic growth by as much as 5 percent.[32] Clearly, a new approach to economic and monetary programs needed to be taken.

The European Monetary System (EMS) was set up in 1979, primarily to counter the effects of the U.S. dollar on European currencies and exchange rates. It established the European Currency Unit (ECU) as a common unit of currency for the exchange rate mechanism (ERM). The ERM establishes a central rate for the ECU against each participating state currency and those currencies are allowed to fluctuate only within a narrow band. If a currency exceeds the limit of that band, national banks must intervene to maintain equilibrium. Changes in valuation of individual currencies must be made jointly by all participants.[33]

The ECU is used primarily as a means of settling debts among EC members and institutions and as a Community credit reserve. However, the ECU may take on a new role as the EC implements its new program for economic and monetary union and establishes a single European currency.

The main shortfall of EMS was that not all EC states participated or participated under arrangements tailored to address disparate economic environments. The U.K. did not participate in the exchange rate mechanism until October 1990 because of long-standing reluctance to relinquish sovereignty to the EC. Spain and Italy's exchange rates are allowed to fluctuate +/- 6 percent, rather than the 2.5 percent fluctuation limit established for the other EC states. The EC needed to find a way to improve its monetary system.

In 1989 Jacques Delors presented a proposal to the EC Economic and Finance Council urging a three stage program for economic and monetary union (EMU).

Stage I, which began on July 1, 1990, called for closer coordination of national monetary policies and inclusion of all currencies in the European Exchange Rate Mechanism. After initially holding out, the U.K. joined the Stage I program but maintained serious reservations about participating in further implementation of EMU.

Stage II is seen as a transition period when EC countries would begin collective decision making on Community monetary policy, but with the ultimate responsibility for policy remaining with national members. Stage II calls for the creation of a central bank along the lines of the U.S. Federal Reserve. This system is often referred to as the Eurofed. Stage II is scheduled to start at the beginning of 1994.

During Stage II the following preconditions to monetary union must be met: internal free trade, i.e. EC-92, must be essentially completed; there must be convergence of EC members' economic performance and policies; exchange rates must be stabilized; members must accept binding rules for the transfer of monetary policy to the new bank.[34]

The most probable shape of the Eurofed, as described in current literature, is that it will be modelled after the German Bundesbank and U.S. Federal Reserve System. Three basic concepts of operation are emerging: it will be independent; it will be committed to price stability; it will be subject to democratic accountability.[35]

Delors' report did not specifically lay out the organizational structure of the Eurofed. A subsequent report, issued in April 1989 by the Committee for the Study of EMU, did outline four characteristics of the institution's structure and organization. First, the institution should be federative to account for the EC's political diversity. Second, a Eurofed Council should be established, made up of the governors of existing EC central banks and members of a Eurofed Board. This body would be similar to a corporate Board of Directors and responsible for formulating and deciding on broad issues of monetary policy. Third, the European Council would appoint a Eurofed Board, somewhat like senior corporate officers, to oversee implementation of common monetary policies. Fourth, the policies and decisions of the Eurofed Council would be executed through the national central banks.[36]

Stage III is the final stage and will introduce a single European currency, but only when EC member states have significantly satisfied the preconditions of Stage II. The EC institutions will have the authority to constrain national budgets and determine monetary policies.

The authority to be vested in the EC to implement EMU goes beyond the scope of the Treaty of Rome. The program to move towards a centralized banking system and a common currency requires agreement on common policy and practice and a transfer of authority to the EC.[37] The extent of the power to be vested in new EC institutions and the impact on individual states is no small matter of concern to the EC member states. It is these issues that are the subject of debate at the Intergovernmental Conference on EMU that started in December 1990.

Prior to the start of the IGC on EMU, the U.K. found itself once again at odds with the majority of EC members over the basic issue of ceding sovereignty to a supranational institution. The debate over integrating the U.K. further into the EC and the ramifications of future European political integration contributed to the change of Conservative Party leadership and John Major became Prime Minister. Margaret Thatcher's hard line on the principle of British sovereignty, and attendant role within the EC, had run head on against the increasingly poor economic condition of the U.K. and internal political pressure for a more accommodating European posture.

As John Major takes political control, he is attempting to end British isolationism. Going into the December IGC on EMU, he proposed a plan, first offered when he was Chancellor of the Exchequer, to moderate EC momentum toward a European single currency. He proposed a "hard ECU" that would be a 13th currency along side of other national currencies. Member states would use this common currency in addition to their national currencies. The "hard ECU" could evolve into Delors' single currency, if and when Europe's economy was ready for it.

Major's proposal served to bring the U.K. back into the integration process as a participant in EMU. In contrast, Thatcher's stand had been that Britain would remain uncommitted to EMU beyond Stage I. When the agreements for Stage II and III became fully spelled out, Britain would then exercise the right to participate or not. Mr. Major has softened this position and has been seeking common ground for agreement on how to proceed towards monetary union with other EC heads of state.

The "hard ECU" originally had a following among some economists who viewed it as a way to temper the rush to a single currency before achieving greater economic convergence among member states. However, the "hard ECU" has lost much of its original appeal because it allows for the possibility of a multi-tiered financial system, and precisely because it delays arriving at a single European currency.

Within Britain, as well as the other EC member states, business leaders are increasing the pressure to move towards a single currency. Intra-EC trade is expanding at such a rate that the cost of transactions associated with multiple currencies cannot be ignored. "Companies may care little about the statutory framework of a Eurofed, but they are sold on its ultimate mission - the minting of a single currency."38 However, before the single currency can be arrived at, the Eurofed and Stage II of EMU must be up and running.

Increasingly, the eyes of the Community are on Germany. German unification has been a key player in the acceleration towards EMU because of the perception that an already economically dominant Germany would only become stronger with unification. The French have long acknowledged the strength of the German economy and have sought to moderate that strength through the EC. The French see EMU as a way to tie the power of the German economy to the EC. This will both dampen the tendency of Germany to de-facto determine the EC economic condition and tie other EC members' economies to German strength.

However, Germany is not united on its own position towards EMU. Foreign Minister Hans-Dietrich Genscher favored an early date for Stage II of EMU. But, he has been opposed by Finance Minister Theo Waigel and Bundesbank President Karl Otto Pohl, who strongly favor delaying Stage II. Chancellor Kohl is playing somewhere between the two. He favors a one year delay, engineered just prior to the October summit, but states he will support a Eurofed only if it was truly independent and focused on monetary stability.39

Pohl is understandably worried about a central European bank controlling the deutche mark. The strong suit of German monetary stability has been controlling inflation and maintaining independence from government influence on monetary policy. Pohl is also concerned about the effect association with other currencies will have on the strength of the deutche mark. The existence of a two track exchange rate mechanism in the European Monetary System shows the disparity between member states' economies. Pohl argues that there must be a greater economic convergence before the sought after discipline of a central bank system can be put in place.

The "Economist" February 23, 1991, reports that both Mr. Major and Chancellor Kohl agree in principle with Pohl's concern and on his position to slow the pace of Stage II until there is greater economic convergence within the Community.[40] Policy conflicts, arising from national objectives, are bound to happen and can be seen in today's situation where Germany, concerned about inflation triggered by the mounting cost of unification, is raising interest rates. Meanwhile, Britain and France are concerned about recession and want to cut interest rates to stimulate their economies and increase employment.

Except for the Bundesbank, EC national banks are directly influenced by their national governments in determining monetary policy. Politicians use the banks to achieve political aims by manipulating inflation and interest rates. A Eurofed would prohibit such actions, if it is modelled on the Bundesbank. This is an essential trade-off if the EC is to gain the advantage of a unified, strong centralized system whose objective is to dampen fluctuations and put a premium on price stability.

Budget policy may also cause a problem if a member state cannot increase its money supply to cover deficits. The Germans worry that the Italians, Greeks, Spanish and Portuguese will continue to overspend and need the Germans to cover their deficits. The Italians, Greeks, Spanish and Portuguese worry that restrictive budgetary controls will not allow them the flexibility to lower costs through devaluation of their currencies. They then would not be as competitive in the market. The Germans recognize this and see it as an additional financial drain because, under the Eurofed, stronger members will have to cover the poor members of the Community. The disparity has led to discussions on a possible two tier system that would not force a country to participate fully in EMU until its economy develops to a point of convergence with core EMU members. However, Greece and Spain are on record as opposing any system that would differentiate between member states. They would prefer to wait to implement EMU as a unified community, rather than rush in with a multi tier system.41

Since the start of the IGC on EMU in December 1990, there has been little substantive agreement between the Community members. Just recently, Kohl has stepped up his opposition to moving rapidly to EMU by stating that German economic union has been a disaster that should be avoided by the Community. In a March 21st Wall Street Journal article, Kohl is reported to believe that German monetary union should have waited until the two economies were brought into closer alignment. Chancellor

Kohl countered by saying that "the very special issues of the German to German monetary union have nothing to do with discussions on the concepts for European monetary union."[42] Pohl later said that his comments were meant to be constructive and not meant to reopen debate over monetary union. Audry Choi reports that the exchange is indicative of the push to unify European currencies for political reasons and could be a liability to those currencies whose economies are not ready for unification.[43]

As the IGC on EMU continues, it becomes increasingly apparent that politics is an overriding concern within the EC. In economic terms, EMU has been amply justified: It is the timing, mechanisms and structures that are confounding the member states, and this has everything to do with political implications, as well as the issue of sovereignty. However, the EC seems willing enough to cede sovereignty if the benefits of EMU can be realized. The experience of German unification, the slip in Stage II implementation, the Gulf war and the change in U.K. leadership have tended to keep progress towards EMU in the discussion stage. If the EC is going to achieve real economic union and economic power through common monetary policy, it must progress beyond non-committal talks and commit to implementing a common central bank and eventually, a common currency. In this way, the EC will increase its role in world affairs and reflect its influence as a major economic power. If progress towards economic and monetary union seems halting, progress on the EC political agenda is even more tenuous.

The Deepening Agenda

Political Union

The evolution of EC political cooperation has been slow. Ironically, it is political unification that was the ultimate goal of the EC's founding fathers. They understood that a unified Europe was going to be a long process and that there had to be a binding mechanism, more tangible than philosophical or ideological agreement among intellectuals, to guide states along the road to unity. The EC provided the mechanism, because there is a necessary sharing of sovereignty entailed in economic integration. This requires some degree of political integration.

Supporters of deeper political integration have seized on the momentum generated by the success of EC-92 and issues surrounding the debate on EMU to incorporate European Political Union (EPU) in the Community agenda.

The latest political push is "happening in classic EC fashion, in which grand designs are aired, expectations raised and are then brought down to earth."[44] In April, 1990, Kohl and Mitterand proposed to the European Council that the EC should commit itself to political union by 1993. They called for an IGC on the matter, to run concurrent with the IGC on EMU.

The IGC has convened but there is no consensus on how to proceed towards EPU. The main issues are beginning to focus on how to achieve more democratic decision-making; how to make the decision process more effective; and how to address common foreign and security policy. "The implicit consensus is to concentrate on making the Community work better and not go for radical overhaul. Usable propositions...... look more attractive than grand designs which may not be negotiable."[45]

Since the start of the IGC on EPU, it has become clear that 1993 will remain significant for the degree of economic integration through EC-92. EPU will be a longer range objective. Even Chancellor Kohl and EC Commission president Delors see EPU as a long term objective, to be reached by the end of the century.[46]

The movement towards EPU received impetus from three major events which are helping to shape the debate: first, the issues surrounding the emerging Central European democracies; second, the Gulf crisis; and third, the unification of Germany. These events acted to highlight the political weaknesses of the EC when the EC had to function as an independent body outside the realm of its expertise - economic cooperation. EC response was slow, fragmented and in the view of critics, impotent.

When the extent of reconstruction necessary in Central Europe became apparent, President Mitterand proposed, and had accepted, that the EC become the executive agent for the Bank for European Reconstruction and Development. The bank brings together 34 countries to help finance building the economies of emerging democracies. This put the EC in a policy role, where it is forced to make decisions on the distribution of over 10 billion ECU's to governments that must meet as yet undefined lending principles. The EC has moved into the leading role of coordinating the West's "Marshall Plan" for central Europe.[47] The process of formulating policy to execute this program is drawing attention to the weakness of the EC to effectively and efficiently function as an institution outside of it's community.

The nature of EC response to the Gulf crisis was even more indicative of why EC members are supporting EC political reform. Throughout the crisis, member states acted unilaterally in response to the U.N. resolutions. There was little "European" response. John Major, commenting on EC actions, said: "political union and a common foreign and security policy in Europe would have to go beyond statements and extend to action. Clearly, Europe is not ready for that."[48] Jacques Delors concurred and added: "To be brutally honest, public opinion sensed that Europe was rather ineffectual."[49]

In the January 1991 issue of Europe, Sir Leon Brittan, EC Commission Vice President in charge of competition, sums up the task confronting the EC as assessing how the EC can better respond to such events, and influence them. "The EC must develop a common foreign policy as opposed simply to trade and economic policies. We are still essentially coordinating 12 national policies and reacting to international developments, rather than seeking to shape them."[50]

The EC included a legal framework for European Political Cooperation (EPC) in the Single European Act. It committed members to endeavor jointly to formulate and implement European foreign policy. However, the EC's EPC secretariat is overcome by recent events and unable to cope with rising demands for the EC to function as an independent power. This not only includes issues of foreign economic policy but also includes emerging security issues.

Current events have raised questions, but not consensus, on how to tailor European security structures in the face of: a perceived reduction in the Eastern threat; ways and means to conduct common European "out of area" security coordination; and how to deal with pan-European security issues, such as, terrorism, drug traffic, migration and environmental deterioration. EPC shortcomings are apparent. "It depends on consensus: No supranational authority constrains any nation's sovereignty."[51] Proposals for changing the EC political process are far apart. The U.K. represents an end of the spectrum. Its views are reflected in Margaret Thatcher's statement that, "We have not successfully rolled back the frontiers of the state in Britain only to see them reimposed at a European level, with a European superstate exercising a new dominance from Brussels."[52] Prime Minister Major seems to be softening this hard line anti-federalist position and is trying to forge friendlier relations with other EC governments. This is in part due to the desire of the U.K. to avoid being shut out of European political evolution, as well as a recognition that change will happen and Britain can best serve its own ends by working within the system.

The EC acknowledges that there is an accountability problem in the decision process of the Community. A great deal of law is being shaped in Brussels but the Community is divided on how the relationships with individual states should be defined and how the EC citizens, 320 million strong, will be assured a say in EC decisions. Institutional reforms to solve the "democratic deficit" are reflected in opinions of those who favor a more federal Europe and those who favor a looser confederation of highly independent nation states.

The federalists, led by Germany and the Netherlands, favor increasing the role and responsibility of the European Parliament. Jacques Delors proposes that the European Parliament should elect the members, or least the president, of the European Commission. "This would make the Commission directly answerable to the Parliament, which itself, is elected by voters in the member states."[53] The U.K. and France, proponents of a looser confederation, favor preserving the authority of national governments and parliaments by giving greater power to the Council, at the expense of the Commission and Parliament. The Council is made up of the foreign ministers of member governments. The Commission is the EC's independent governing body and has 17 members, who are appointed by their national governments. Britain, France, Germany, Spain and Italy have two members each. The other countries have one member. In addition to the traditional national arguments over a federative Europe there is increasing recognition and concern over regional input to the EC process.

Lothar Spath is the Prime Minister of Baden-Wurttemberg Lander and a strong advocate of a federal Europe. He bases his argument for rapid progression to federation on the premise that Europe's nation states have become obsolete.[54] This makes European political union imperative, so that a democratic process will establish the rules of the new order. "If we have only an economic Europe, without a political Europe, the rules will no longer be dictated by those who have the democratic legitimacy to do so."[55] He says that although "European" problems are macro issues, the micro-problems are regional and best solved at the regional level. This argues for greater regional input in the EC. Among other things, it would dampen fears of an all powerful German state that results from unification. "The Alsatians and people of my Land have a lot more in common with one another than with the inhabitants of Schleswig-Holstein, who in turn have a lot more in common with the Danish."[56]

As the IGC on EPU progresses, two key areas that will draw attention are: "the checks and balances between the branches of EC government; and the changes to the structure and powers of each branch."[57] Any proposals for structural or procedural changes require amendments to the Treaty of Rome. EC consensus will probably gravitate to the least contentious and threatening solutions. Most likely, the outcome of the IGC on political cooperation and union will be a road map for future EC political integration, rather than any radical changes that will challenge state sovereignty or Community equilibrium. Certainly, the process is refining the way the EC surfaces and deals with its shortfalls.

Conclusions

"The European Community is a major geopolitical development. Except for the United States, it already is the only European political entity, west of the river Bug, able to act effectively across a broad range of interests."[58] The Single European Act, EC-92, was a key to bringing this about. It energized the Community to move further and faster along the road to economic integration more than any single event in EC history. But, conditions were right.

European business was hurting under fractured national economic policies and barriers to commerce that severely crippled EC members' intra-Community and extra-Community competitive posture. The strong support that business gave EC-92 and the proven success of economic growth, maintained pressure on national governments to press ahead with the EC-92 program.

The world experienced dramatic change as the emerging democracies of the Central Europe began to assert themselves on the West and the issue of reconstituting their economies was taken up by the EC. The unification of Germany posed a different problem to the EC. The EC has set out to seek ways to harness the economic might of Germany, enhanced by the addition of the eastern half, without allowing Germany to totally dominate the Community. Then the Gulf crisis arose and showed the ability of the Community to act in a "European" way. But, not without severe difficulties, which highlighted the need to examine the basic constitution of the Community with a view to strengthening the political architecture and process.

The EC is being transformed by the events around it. However, the rush to seize the opportunity afforded by world events is being tempered by widely divergent opinions on what changes Europe and the EC will have to make.

The EC has limited and prioritized its agenda. Its first priority is to achieve the objectives of EC-92. Widening EC membership has been postponed until the issues involved in the deeper EMU and EPU agenda are more fully addressed. The IGCs on EMU and EPU will continue, but expectations for dramatic moves forward are waning. Instead, the IGCs will probably provide a road map for future EC integration, at a measured pace. The priority IGC is EMU because of tangible economic benefits. However, progress on EMU will necessitate some political reform, as well as require changes to the Treaty of Rome. European federalists take some comfort in this, since they see it as a forward step in the direction of an eventual Federal Europe.

In the meantime, the rest of the world will carefully monitor the evolution of the European power and adapt itself to an EC that is increasingly assuming an independent role.

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