

A Neighbourhood Economic Community - *finalité économique* for the ENP?

EU Diplomacy Papers

3 / 2008

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Views expressed in the *EU Diplomacy Papers* are those of the authors only and do not necessarily reflect positions of either the series editors or the College of Europe.

Abstract¹

Upon launching the European Neighbourhood Policy (ENP), the European Commission proclaimed that all the neighbouring countries should be offered the prospect of 'a stake in the internal market' with the free movement of persons, goods, services and capital. The long-term goal was to move towards an arrangement that would ultimately resemble the European Economic Area (EEA). However, within three years, any reference to both the four freedoms and the EEA have disappeared from the Union's discourse. Instead, the concept of a Neighbourhood Economic Community (NEC) was introduced in December 2006. This paper examines how this *finalité économique* is supposed to be achieved and what it might look like. It is argued that an NEC is likely to develop into a predominantly bilateral network of 'FTA plus' and 'internal market minus' associations and that the multilateral EEA may not serve as a model for this project.

¹ A longer and more detailed version of this paper will be published in Lannon, E. (ed.), *The European Neighbourhood Challenges*, Brussels, P.I.E. Peter Lang, forthcoming.

Introduction: from the 'Four Freedoms' to 'Enhanced Free Trade'

The elusive objective of the European Neighbourhood Policy launched in 2003 is "to expand the zone of prosperity, stability and security beyond [the EU's] borders".² In other words, its *finalité politique* has largely remained an open question. "The European Neighbourhood Policy's vision involves a ring of countries, sharing the EU's fundamental values and objectives, drawn into an increasingly close relationship, going beyond co-operation to involve a significant measure of economic and political integration."³ But what does a significant measure of integration imply for non-EU member states? Even though there are other important rewards on offer in the ENP, including foreign aid, technical assistance, improved infrastructure interconnections, participation in selected EU programmes and agencies, police missions and political dialogue, it is safe to argue that "the promise of greater participation in the internal market will be the catalyst for any reform momentum that develops within the ENP process".⁴

At the outset, the European Commission proclaimed that "all the neighbouring countries should be offered the prospect of a stake in the EU's Internal Market and further integration and liberalisation to promote the free movement of – persons, goods, services and capital (four freedoms)".⁵ The creation of such a market would involve both national liberalisation removing discrimination (negative integration) and (re-)regulation at the European level (positive integration). The Commission's long-term goal therefore was "to move towards an arrangement whereby the Union's

² Ferrero-Waldner, B., "The European Neighbourhood Policy: The EU's Newest Foreign Policy Instrument", *European Foreign Affairs Review*, 11(2), 2006, p. 139.

³ European Commission, *Communication from the Commission, European Neighbourhood Policy – Strategy Paper*, COM(2004) 373, Brussels, 12 May 2004, p. 5.

⁴ Vachudova, M.A., "Trade and the Internal Market", in Weber, K., Smith, M.E. and Baun, M. (eds.), *Governing Europe's Neighbourhood: Partners or Periphery?*, Manchester, Manchester University Press, 2007, p. 98.

⁵ European Commission, *Communication from the Commission to the Council and the European Parliament, Wider Europe – Neighbourhood: A New Framework for Relations with Our Eastern and Southern Neighbours*, COM(2003) 104, Brussels, 11 March 2003, p. 10. Article 14:2 of the Treaty establishing the European Community describes the internal market as "an area without internal frontiers in which the free movement of goods, services, persons and capital is ensured".

relations with the neighbouring countries ultimately resemble the close political and economic links currently enjoyed with the European Economic Area".⁶

However, these references to both the four freedoms and the EEA have soon been tacitly dropped from the Union's discourse on the Neighbourhood Policy. In 2004, the ENP offered "neighbouring countries the prospect of a stake in the EU Internal Market based on legislative and regulatory approximation, the participation in a number of EU programmes and improved interconnection and physical links with the EU".⁷ The same Strategy Paper considered that the next step in the development of bilateral relations could take the form of "European Neighbourhood Agreements".⁸

In its December 2006 Communication, the European Commission avoided any reference at all to a stake in the internal market. Instead, it introduced the concept of "a longer-term vision of an economic community emerging between the EU and its ENP partners", which "would include such points as the application of shared regulatory frameworks and improved market access for goods and services among ENP partners, and some appropriate institutional arrangement such as dispute settlement mechanisms".⁹ Hence, the ENP's *finalité économique* has now been defined in terms of a Neighbourhood Economic Community. The core of this community would be "deep and comprehensive free trade agreements" (FTAs), covering substantially all trade in goods and services as well as 'behind-the-border' issues such as "technical norms and standards, sanitary and phytosanitary rules, competition policy, enterprise competitiveness, innovation and industrial policy, research cooperation, intellectual property rights, trade facilitation customs measures and administrative capacity in the area of rules of origin, good governance in the tax area, company law, public procurement and financial services".¹⁰

⁶ *Ibid.*, p. 15. This ambition stems from Commission President Prodi's earlier suggestion that it was "worth seeing what we could learn from the way the EEA was set up and then using this experience as a model for integrated relations with our neighbours". See Prodi, R., *A Wider Europe – A Proximity Policy as the Key to Stability*, Speech/02/619, Sixth ECSA-World Conference, Brussels, 5-6 December 2002, p. 7.

⁷ European Commission, *Communication from the Commission, European Neighbourhood Policy – Strategy Paper*, *op.cit.*, p. 14.

⁸ *Ibid.*, p. 5.

⁹ European Commission, *Communication from the Commission to the Council and the European Parliament on Strengthening the European Neighbourhood Policy*, COM(2006) 726 final, Brussels, 4 December 2006, p. 5.

¹⁰ *Ibid.*, p. 4.

Within a short time span, the stake in the internal market has thus gradually been narrowed down to improved market access for goods and services, which is now considered to "stand at the heart of the intensified ENP", and in return "partners must continue opening their economic systems and selectively adopt relevant parts of the EU acquis".¹¹ In view of this backtracking, this paper examines how the goal of a Neighbourhood Economic Community is supposed to be achieved and what shape it is likely to take. Even though the European Union still lacks clarity with regard to the substantive and institutional features of an NEC, I argue that this economic community is likely to develop into a bilateral network of 'FTA plus' and 'internal market minus' associations and that the multilateral EEA may, for various reasons set out below, not serve as a model for the future NEC.

The following section discusses the notion of an economic community, while the subsequent part identifies the steps that are envisaged to establish an NEC. The fourth part examines to what extent the EEA can be used as a signpost, and the conclusions raise some implications of the findings.

The Elusive Concept of an Economic Community

Whereas the 'neighbourhood' itself is defined in terms of the sixteen partner countries,¹² the notion of an 'economic community' escapes a concise meaning. There are, for example, several 'economic communities' on the African continent, such as the Economic Community of West African States, the East African Community or the Economic Community of Central African States, and the 1991 Abuja Treaty establishing the African Economic Community plans to build on these existing regional economic communities in order to gradually create a pan-African economic community by 2025.¹³ The steps towards such a community closely follow the European experience: from the formation of a free trade area to a customs union, followed by a common market and then economic and monetary union. However, even the European Economic Community is not based on a commonly agreed political, legal or economic definition.

¹¹ Council of the European Union, *Strengthening the European Neighbourhood Policy – Presidency Progress Report*, 10874/07, Brussels, 17 June 2007, p. 7.

¹² Algeria, Armenia, Azerbaijan, Belarus, Egypt, Georgia, Israel, Jordan, Lebanon, Libya, Moldova, Morocco, Palestinian Authority, Syria, Tunisia, and Ukraine.

¹³ www.uneca.org/itca/ariportal/abuja.htm (1.2.2008).

Economists distinguish five well-known forms of regional integration: (1) a free trade area abolishes the tariffs and quotas; (2) a customs union involves, in addition, common external tariffs against non-members; (3) a common market removes also restrictions on factor movements; and (4) an economic union harmonises certain economic policies, particularly macroeconomic and regulatory policies.¹⁴ The notion of an economic community seems sufficiently vague as to embrace elements of the first three steps. In 2003, ASEAN agreed to transform its ten member countries into an ASEAN Community, which would include an ASEAN Economic Community, defined as "a single market and production base with free flow of goods, services and skilled labour and freer flow of capital by 2020".¹⁵ The proposed ASEAN Economic Community has also been described as a 'free trade area plus' or a 'common market minus'.¹⁶

In political science, the concept of an economic community has not caught much scholarly attention. European integration has advanced via both strengthening the Union's decision-making authority and processes of market integration. However, it was observed that the collective policy-making capacity has, partly on purpose, not been strengthened to the same extent as the member governments' capabilities have declined since "building up an economic community is, above all, a matter of deregulation and strengthening the market as a central institution of allocation".¹⁷ Indeed, a trade agreement involves a commitment to remove trade obstacles, but in addition an "association, or 'economic community' [...] entails a deliberate banding together of actors to create a centralised political structure with genuine decisionmaking power".¹⁸

¹⁴ Balassa, B., *The Theory of Economic Integration*, Homewood, Richard D. Irwin, 1961, p. 2.

¹⁵ ASEAN, *Recommendations of the High-Level Task Force on ASEAN Economic Integration*, www.aseansec.org/hlhf.htm, attached to *Declaration of ASEAN Concord II (Bali Concord II)*, Bali, Indonesia, 7 October 2003, www.aseansec.org/15159.htm (1.2.2008).

¹⁶ Soesastro, H., "ASEAN Economic Community: Concepts, Costs, and Benefits", in Hew, D. (ed.), *Roadmap to an ASEAN Economic Community*, Singapore, Institute of Southeast Asian Studies, 2005, p. 23.

¹⁷ Kohler-Koch, B., "Catching up with Change: The Transformation of Governance in the European Union", *Journal of European Public Policy*, 3(3), 1996, p. 364.

¹⁸ Smith, M.E. and Weber, K., "Governance Theories, Regional Integration and EU Foreign Policy", in Weber, K., Smith, M.E. and Baun, M. (eds.), *Governing Europe's Neighbourhood: Partners or Periphery?*, Manchester, Manchester University Press, 2007, p. 12.

Finally, European or international law does not offer an established definition of an economic community either. Article XXIV:5 GATT, which defines types of regional integration exempted from the most-favoured nation principle, refers only to free trade areas and customs unions. Moreover, many lawyers draw a distinction and view the concept of the internal market as being narrower than that of a common market. In particular, the internal market is said not to embrace "a completed external trade policy, a system of undistorted competition within the common market, and the harmonization or co-ordination of legislation for reasons other than the elimination of barriers between national markets".¹⁹ Even though the EU's internal market happens to be a common market with a customs union and a common commercial policy, this 'external dimension' is, from such a perspective, not a key element of a generic internal market. The EEA, for example, "is not to be classified as an improved free trade zone – it is to be classified as a less perfect internal market".²⁰ In sum, an economic community constitutes most likely a form of WTO-compatible regional integration, located somewhere between a classical free trade area and an internal market, and equipped with a certain, albeit low degree of collective decision-making capacity.

Establishing a Neighbourhood Economic Community

In a non-paper prepared for the European Council in June 2007, the European Commission presented some ideas on how the long-term vision of a Neighbourhood Economic Community could be developed:²¹

- the first phase would focus on the full implementation of the ENP Action Plans;
- in the medium term, the conclusion and implementation of deep and comprehensive free trade agreements would be aimed at;

¹⁹ Gormley, L.W., "Competition and Free Movement: Is the Internal Market the Same as a Common Market?", *European Business Law Review*, 13(6), 2002, p. 518. See also Bruha, T., "Is the EEA an Internal Market?", in Müller-Graff, P.-C. and Selvig, E. (eds.), *EEA-EU Relations*, Berlin, Arno Spitz, 1999, pp. 103-105.

²⁰ Bruha, *op.cit.*, p. 127. One should not forget that even the EU's internal market is not fully completed.

²¹ European Commission, *ENP – A Path towards Further Economic Integration, Non-paper Expanding on the Proposals Contained in the Communication to the European Parliament and the Council on "Strengthening the ENP" – COM(2006) 726 final of 4 December 2006*, Brussels, June 2007, p. 4. ec.europa.eu/world/enp/pdf/non-paper_economic-integration_en.pdf (1.2.2008).

- in addition, intra-regional integration between the ENP partners themselves should increase;
- and finally, in the long term, the EU member states and the ENP countries would build up a common NEC.

The implementation of the first three steps has already been tackled. The bilateral ENP Action Plans adopted since 2005 are country-specific political documents which define the reform priorities for the next three to five years.²² According to the principle of joint ownership, the Union does not seek to impose those priorities on its partners but they are set together. Each Action Plan contains, *inter alia*, chapters on trade-related issues, market and regulatory reform, on economic and social cooperation and development and on sectoral issues such as transport, energy and environment. The EU supports the implementation process with technical assistance, financial aid and policy dialogue. Monitoring is carried out in the relevant bodies and (sub)committees set up under the respective bilateral agreements as well as by the Commission's progress reports.

As a second step, a new generation of deep and comprehensive free trade agreements will be negotiated.²³ A 'comprehensive' free trade area encompasses both liberalisation of trade in goods "with respect to substantially all the trade" (Art. XXIV:8 GATT) and liberalisation of trade in services with "substantial sectoral coverage", eliminating "substantially all discrimination" (Art. V:1 GATS). A 'deep' FTA entails the reduction of non-tariff barriers to trade and regulatory approximation. Such enhanced agreements will be negotiated with the Eastern ENP partners following the expiry of their ten-year Partnership and Cooperation Agreements²⁴ and their accession to the WTO. The first negotiations have been launched with Ukraine in March 2007, and they will be expanded to deep and comprehensive free trade following the ratification of Ukraine's WTO membership.

²² Those Action Plans (Ukraine, Moldova, Israel) that reach the end of their term already in 2008 will be 'rolled over' for one year.

²³ In addition to the trade provisions of the Euro-Mediterranean Association Agreements (EMAAAs) and the Partnership and Cooperation Agreements (PCAs), the ENP countries currently benefit from unilateral EU trade preferences such as the Generalised System of Preferences 'GSP' (Armenia, Azerbaijan, Egypt, Jordan, Lebanon, Libya, Morocco, Moldova, Syria, Tunisia and Ukraine), the more beneficial special incentive arrangement for sustainable development and good governance 'GSP+' (Georgia) or additional autonomous trade preferences (Moldova).

²⁴ A PCA will be prolonged, however, if both parties do not request otherwise.

The Euro-Mediterranean Association Agreements are not yet 'deep and comprehensive' either, in spite of the current negotiations on the liberalisation of trade in services, the right of establishment, the liberalisation of agricultural and fisheries products and a dispute settlement mechanism for trade issues. They will need to be upgraded to include binding commitments on regulatory issues such as sanitary and phytosanitary standards, intellectual property rights, public procurement and competition.²⁵

The new FTAs will be tailor-made, taking into account each country's economic situation, cover selective alignment with the regulatory *acquis* and allow for a certain level of asymmetry.²⁶ They are likely to take the form of mixed association agreements.²⁷ Such agreements establish "an association involving reciprocal rights and obligations, common action and special procedure" (Art. 310 TEC) and create privileged links with non-member countries which allow them to a certain extent to take part in the Community system (e.g. Association Council, Association Committee, subcommittees).

As a third step, intra-regional integration is expected to contribute to the construction of a broader market. Since the mid-1990s the EU shows a "propensity to 'export' actively to partner countries its model of regional integration" as a complement to its own relations with a region.²⁸ The Union indeed encourages its neighbours to conclude bilateral or regional agreements in order to boost South-South or East-East trade and investment. However, progress has been slow in the ENP area. Intra-regional trade in the Southern Mediterranean is among the lowest in the world for any region of this size (less than 5 percent in 2006²⁹), even though the countries are part of various regional cooperation schemes (e.g. Arab Maghreb Union, Greater Arab Free Trade Area, Agadir Agreement).

The many bilateral or regional trade agreements among the Eastern ENP partners are essentially focused on trade in goods and contain major exceptions. The Western

²⁵ European Commission, *ENP – A Path towards Further Economic Integration*, *op.cit.*, p. 5.

²⁶ *Ibid.*, p. 6.

²⁷ See Hillion, C., "Mapping-Out the New Contractual Relations between the European Union and Its Neighbours: Learning from the EU-Ukraine 'Enhanced Agreement'", *European Foreign Affairs Review*, 12(2), 2007, pp. 169-182.

²⁸ Maur, J.-C., "Exporting Europe's Trade Policy", *World Economy*, 28(11), 2005, p. 1567.

²⁹ European Commission, *Mediterranean Countries: EU Bilateral Trade and Trade with the World*, DG Trade Statistics, Brussels, 7 August 2007, p. 4, trade.ec.europa.eu/doclib/docs/2006/september/tradoc_113485.pdf (1.2.2008).

Balkan states and Moldova have concluded a network of bilateral free trade agreements which in late 2006 was transformed into a single regional trade arrangement, the Central European Free Trade Agreement (CEFTA), supported by the EU's CARDS programme. The EU also encourages trade liberalisation in the Black Sea region. The European Commission's 'Black Sea Synergy' initiative aims at cooperation with the Organisation of the Black Sea Economic Cooperation (BSEC).³⁰

Growing intra-regional cooperation and the proliferation of deep and comprehensive FTAs would certainly constitute important building blocs for an NEC. The East-South dimension of economic liberalisation still needs to be explored, although the pattern of current trade and investment flows does not suggest that this may become an economic priority for the ENP countries.³¹ "With the EU's bilateral network of free trade agreements gradually extending to its entire neighbourhood, it is logical to envisage a multilateral 'basic free trade' area to include potentially all of Europe and the Mediterranean"- eventually not just the ENP partners, but also the EFTA states, the Western Balkans and Russia.³² This initiative would complement but not replace the present 'hub-and-spoke bilateralism' between the EU and each of its neighbours and help create connections 'between the spokes'. However, a multilateralisation of deep and comprehensive free trade would go "beyond trade policy issues into overlapping matters of domestic economic governance".³³ An internal market association such as the EEA would require certain 'quasi-supranational' features and institutions in view of the fact that a dynamic and homogeneous market calls not only for continuous far-reaching regulatory alignment but also for credible enforcement mechanisms. Consequently, in terms of substance, the NEC is likely to resemble a patchwork of 'FTA plus' or 'internal market minus' agreements (or a combination thereof, depending on the partner countries' ambition). In the first case, an extended market access will almost completely focus on the liberalization of trade and trade-related issues. The second case will go

³⁰ European Commission, *Communication from the Commission to the Council and the European Parliament, Black Sea Synergy – A New Regional Cooperation Initiative*, COM(2007) 160 final, Brussels, 11 April 2007. The BSEC comprises Albania, Armenia, Azerbaijan, Bulgaria, Georgia, Greece, Moldova, Romania, Russia, Serbia, Turkey and Ukraine.

³¹ European Commission, *ENP – A Path towards Further Economic Integration*, *op.cit.*, p. 4.

³² Emerson, M., Noutcheva, G. and Popescu, N., "European Neighbourhood Policy Two Years on: Time Indeed for an 'ENP plus'", *CEPS Policy Brief*, 126, Brussels, Centre for European Policy Studies, 2007, p. 3.

³³ *Ibid.*, p. 17.

beyond trade but not constitute "an area without internal frontiers" (Art. 14:2 TEC) nor cover all the internal policies which have an impact on free trade and competition. The free movement of persons, for instance, has largely been reduced to visa facilitation, migration management and increased people-to-people exchanges (e.g. educational and youth exchanges, mobility of researchers, civil society contacts), although labour migration would add flexibility to the labour market and relieve demographic pressures in light of the EU's aging population and the high population growth rates in the Mediterranean countries. In its Communication of December 2007, the European Commission cautiously "proposes facilitation of legitimate short-term travel as well as more ambitious – longer-term – developments in the area of managed migration, potentially involving the opening of Member States' labour markets where this is to the mutual advantage of the sending and receiving countries".³⁴ Furthermore, the Commission has suggested 'mobility partnerships'³⁵ for the ENP countries, including possibilities for visa facilitation, work permits and information related to seasonal labour market needs within the EU.³⁶

The integration of the two geographical dimensions of the ENP may in addition be intensified by a sectoral approach. Looking beyond South-South or East-East regional cooperation, the European Commission indeed points in a non-paper to the potential benefits of enhanced thematic cooperation across the entire ENP neighbourhood.³⁷ Among the cross-cutting sectors that could be addressed at an overarching ENP level are human rights and the rule of law, justice, freedom and security, trade and regulatory convergence, transport, energy, environment, maritime policy, social policy, education, information society or public health. This

³⁴ European Commission, *Communication from the Commission, A Strong European Neighbourhood Policy*, COM(2007) 774 final, Brussels, 5 December 2007, p. 5.

³⁵ 'Mobility partnerships' are to provide a framework for managing various forms of legal movement between the EU and third countries. They are to be agreed with those countries that are committed to fighting illegal immigration and have effective mechanisms for readmission.

³⁶ European Commission, *Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions, Applying the Global Approach to Migration to the Eastern and South-Eastern Regions Neighbouring the European Union*, COM(2007) 247 final, Brussels, 16 May 2007, p. 8. The 'Global Approach to Migration' brings together migration, external relations and development policy to address (legal and illegal) migration with third countries in a comprehensive way.

³⁷ European Commission, *ENP – Thematic Dimension, Non-paper Expanding on the Proposals Contained in the Communication to the European Parliament and the Council on "Strengthening the ENP" – COM(2006) 726 final of 4 December 2006*, Brussels, June 2007, ec.europa.eu/world/enp/pdf/non-paper_thematic-dimension_en.pdf (1.2.2008).

would contribute to striking a bilateral-multilateral balance in the Eastern dimension of the ENP, which in the South is already assured through the Euro-Mediterranean Partnership.³⁸ However, an institutionalisation of horizontal peer contacts and exchange of best practices is not very likely to constitute a political priority either for the ENP countries.

Ultimately, in the fourth phase, the Neighbourhood Economic Community would further eliminate obstacles to trade among ENP partners and create a common regulatory space.³⁹ Flanking policies to support the effective functioning of an NEC would need to be developed, including in key sectors such as energy, environment, transport and human capital. Besides these substantial issues, an institutional framework would have to be explored, including political, legal and budgetary questions. "Any change from the bilateral/regional 'hub-and-spokes' approach to a broader regional approach would need to be supported with appropriate structures, including the possibility to let partners have a voice in policy-shaping."⁴⁰ Hence, indirectly the Commission still refers to the EEA: the EFTA countries do have such a limited voice in the EEA's decision-making process.

The EEA as a Blueprint for an NEC?

The differences between the ENP and the EEA are manifold, in particular with regard to the partners, the policies, and the institutions (polities and processes). First, the EFTA states are small, rich and highly industrialised democracies with a common intergovernmental organisation. They are all eligible for EU membership. The ENP countries, however, are politically and economically very heterogeneous and (with the exception of Israel) noticeably below the EU average in terms of GDP per capita or the degree of democratisation.⁴¹ They have lower-quality infrastructure and greater political risk and lack the necessary institutional and administrative capacities for an EEA-like internal market association, even in the more distant future.

Second, the EEA is the most advanced arrangement that the EU has with any group of countries, reflecting the longstanding relations between very similar countries. It covers the free movement of goods, services, capital and persons, competition rules

³⁸ *Ibid.*, p. 1.

³⁹ European Commission, *ENP – A Path towards Further Economic Integration*, *op.cit.*, p. 7.

⁴⁰ *Ibid.*, p. 8.

⁴¹ See Gstöhl, "Blurring Economic Boundaries?", *op.cit.*

as well as horizontal policies (e.g. environment, social policies, consumer protection, statistics and company law) and flanking policies (e.g. cooperation in research and development or education). Excluded are the EU's external relations,⁴² the common agricultural, fisheries and transport policies,⁴³ budget contributions and regional policy,⁴⁴ justice and home affairs, taxation as well as economic and monetary policy. However, many of these excluded areas are of vital interest for the ENP countries. An EEA-like ENP area would thus partly cover other policies, not the least since the ENP states benefit from extensive EU funds.

Third, the structure of the EEA Agreement is multilateral, whereas the legal bases of the ENP are bilateral. An EEA-like set-up for the ENP neighbours (respectively their participation in the EEA) would raise many institutional questions. The EEA Agreement is a dynamic agreement which foresees the continuous adoption of new *acquis* in the relevant fields based on an elaborate two-pillar system. The enhanced FTAs, however, will be of a more static nature, and substantial changes will require new negotiations. The EFTA states are obliged to take on new *acquis*, but enjoy only limited means of influence in the decision-making process. Full participation in the internal market also requires the application of EU regulatory and competition rules and an arbitrator that enforces compliance. By comparison, the former Commission President Prodi clearly spoke of a framework for the ENP "in which we could ultimately share everything but institutions".⁴⁵

While the EEA attempts to ensure a homogenous market and uniform application of the *acquis*, the ENP aims at differentiation and tailor-made solutions. In order to preserve the homogeneity of the European Economic Area, relevant new 'mirror' legislation is continuously being added. The Commission retains the exclusive right to initiative, whereas the EFTA countries have the right to raise a matter of concern at the EEA level at any time. In the so-called 'decision-shaping phase', EFTA experts are consulted by the Commission in the preparatory stage of new measures (expert

⁴² Nevertheless, the EFTA states follow a policy of 'shadowing' the EU in concluding trade agreements and are associated with the Schengen and Dublin agreements. Norway and Iceland are also closely linked with the EU on foreign, security and defence policies.

⁴³ The sensitive issues of Alpine transit and Nordic fisheries, like trade in agricultural products, were dealt with separately in bilateral agreements with the EFTA states concerned.

⁴⁴ However, the EFTA countries had to establish financial mechanisms to contribute to the reduction of social and economic disparities in the EU (EEA Financial Mechanism, Norwegian Financial Mechanism).

⁴⁵ Prodi, *op.cit.*, p. 6.

committees and comitology committees). During the 'decision-taking phase', once the Commission transmitted its proposals to the EU Council and the European Parliament as well as to the EFTA states, discussions take place in the EEA Joint Committee (preceded by negotiations between subcommittees of the EFTA Standing Committee and DG External Relations).⁴⁶ The EEA Joint Committee decides by consensus as closely as possible in time to the adoption of the same rules by the EU Council in order to allow for a simultaneous application. Hence, EFTA representatives participate in the work of the Commission, but not in the work of the Council, the European Parliament or the EU's advisory bodies. However, they take part in the EEA Joint Parliamentary Committee and the EEA Consultative Committee for the social partners which act as joint advisory bodies. EFTA may also send its comments to all the EU institutions or lobby through its Secretariat and national missions in Brussels or via EU member states. In addition, the EEA Council meets at ministerial level twice a year to give political impetus.

In contrast to the ENP Action Plans, the EEA is predominantly based on legally binding acts. The 'sticks' are similar to those faced by EU members since infringement procedures (and preliminary rulings) are part of the EEA surveillance mechanisms. On the EFTA side, surveillance and enforcement are carried out by the EFTA Surveillance Authority and the EFTA Court of Justice. In order to secure a uniform interpretation of EEA rules, the EEA Joint Committee reviews the development of the case law of the European Court of Justice (ECJ) and the EFTA Court.⁴⁷ Adoption of any EU legislation or other provision into the EEA requires agreement in the EEA Joint Committee. In case of an opt-out from new *acquis*, the EFTA countries, which need to 'speak with one voice', face the threat of a provisional suspension of related parts of the Agreement if all other solutions (e.g. transitional periods, equivalence of legislation, safeguard measures) fail. Unlike the PCAs and EMAAs, the EEA Agreement does not contain a human rights clause and there is no political conditionality in EU-EFTA relations.

⁴⁶ Norberg, S. *et al.*, *EEA Law: A Commentary on the EEA Agreement*, Stockholm, Fritzes, 1993, pp. 129-148. The EFTA Standing Committee, which constitutes the EFTA part of the EEA Joint Committee, is supported by five subcommittees: free movement of goods, free movement of capital and services, free movement of persons, flanking and horizontal policies, and legal and institutional matters. These subcommittees are in turn supported by various EFTA working groups.

⁴⁷ *Ibid.*, pp. 188-196, 213-272.

During the EEA negotiations the EFTA countries had to learn very quickly that real joint institutions and decision-making procedures with the EU were not possible.⁴⁸ In this context it is interesting to note that even before the launch of the EEA initiative in 1989, the Commission had, at a joint ministerial meeting in May 1987, made clear that EU-EFTA relations should be governed by three basic principles: the priority of the Community's internal integration, the preservation of the Community's decision-making autonomy, and the maintenance of a balance of benefits and obligations.⁴⁹ In other words, cooperation with EFTA must be in conformity with EC rules and not interfere with EU decision-making procedures. These 'Interlaken principles' were subsequently enforced in the EEA negotiations. Likewise, the European Court of Justice had in its *Opinion 1/91* objected to the structure and competences of a joint EEA Court of Justice, composed of EFTA and ECJ judges, on the ground that its legally binding interpretations could adversely affect the autonomy and exclusive jurisdiction of the ECJ. This Opinion may play a role whenever the ECJ assesses the need to safeguard the autonomy of the Community legal order with regard to international agreements.⁵⁰

As a result, the construction of an EEA-like Neighbourhood Economic Community looks rather unlikely.⁵¹ The community will essentially cover the free movement of goods, services and (partly) capital, yet only marginally tackle the free movement of persons. Its institutional framework will be based on bilateral associations, without direct participation in the EU institutions, and with a mere thematic multilateral dimension at best. Over time, differentiation between the ENP countries will increase as some are more able and willing to proceed than others. Given the ENP countries' reluctance to further integrate in their own region – and even more so across the Eastern and Southern dimensions – the NEC might thus result in a two-fold 'hub-and-spoke' system centered around the EU, that is, a patchwork of 'FTA plus' for some ENP partners and 'internal market minus' for others.

⁴⁸ Gstöhl, S., "EFTA and the European Economic Area or the Politics of Frustration", *Cooperation and Conflict*, 29(4), 1994, pp. 333-366.

⁴⁹ De Clercq, W., Speech at the EC-EFTA Ministerial Meeting, Interlaken, 20 May 1987.

⁵⁰ See Baudenbacher, C., "Was ist aus dem Gutachten des EuGH 1/91 geworden?", in Baur, G. (ed.), *Europäer – Botschafter – Mensch: Liber Amicorum für Prinz Nikolaus von Liechtenstein*, Schaan, Liechtenstein Verlag, 2007, pp. 79-107.

⁵¹ See also Gould, T., The European Economic Area: A Model for the EU's Neighbourhood Policy?", *Perspectives on European Politics and Society*, 5(2), 2004, pp. 171-202.

Conclusion: Implications of an NEC

It is still an open question how strongly the ENP countries will be motivated to carry out reforms by prospects of an eventual 'stake in the internal market' or of some easing of visa restrictions but not an EU membership perspective. If the *finalité économique* is to serve as a useful incentive for the Eastern and Mediterranean countries, the EU must clarify the substantive and institutional features of an NEC. The ENP has so far largely been a Commission-driven policy project, yet the more the policy progresses into politically sensitive or cross-pillar areas, the more important the member states' support. In order to deliver genuine incentives for the ENP countries to carry on with the necessary reforms, "the Commission, Council, European Parliament and EU Member States must cooperate even more closely to strengthen the ENP".⁵² The EU's credibility will also depend on a consistent and coherent application of the two core principles of conditionality and differentiation. This requires appropriate 'carrots and sticks' with clear benchmarking as well as close monitoring. Another crucial factor is the political will for reforms of the ruling elites in the ENP countries. Domestic adaptation costs, above all in authoritarian regimes with strong vested interests, may hamper reforms, in particular since the benefits will materialise only in the longer term. The less inclined the ENP elites toward domestic reforms, the less likely an accession to the EU, or the less asymmetric the economic relationship between the EU and a neighbour, the less political leverage for the Union. Hence, there are many potential obstacles ahead of the ENP that could make an NEC founder.

Assuming that the ENP will be successful, how will it affect the EU's other neighbourhood initiatives such as the multilateral Euro-Mediterranean Partnership, the EEA or the Strategic Partnership with the Russian Federation? It could be envisaged to include the EFTA countries and Russia – as well as, if necessary, Turkey and the Western Balkans – in a broader Neighbourhood Economic Community.⁵³ Such a grand strategy would, however, have significant implications for the multilateral trading system. Besides, the more successful the ENP and the NEC, the greater without doubt the pressure for a further Eastern enlargement of the Union.

⁵² European Commission, *Communication from the Commission, A Strong European Neighbourhood Policy*, *op.cit.*, p. 11.

⁵³ The EFTA countries have already concluded bilateral free trade agreements with most ENP and Western Balkans countries, and Turkey is part of the Euro-Mediterranean Partnership.

Lastly, can and should the European Union 'export' its economic model to its near abroad? As argued elsewhere, a deep, comprehensive and *acquis*-based form of cooperation, covering many behind-the-border issues and closely following the evolution of the *acquis*, may raise legitimacy concerns in third countries that are affected by internal market decisions but not represented in their making.⁵⁴ The ENP relies closely on the enlargement toolbox which the Union had successfully developed for Central and Eastern Europe. "EU demands for pre-accession legal and institutional alignment – however onerous, one-sided, and asymmetrical they may be – are legitimized by the prospect of full inclusion and the promise of future equality of participation."⁵⁵ However, a membership perspective is officially absent in the European Neighbourhood Policy.

⁵⁴ Gstöhl, S., "The Internal Market's External Dimension: Political Aspects", in Pelkmans, J., Chang, M. and Hanf, D. (eds.), *The Internal Market in Comparative Perspective: Economic, Political and Legal Analyses*, Brussels, P.I.E. Peter Lang, forthcoming.

⁵⁵ Magen, A., "The Shadow of Enlargement: Can the European Neighbourhood Policy Achieve Compliance?", *Columbia Journal of European Law*, 12(2), 2006, p. 422.

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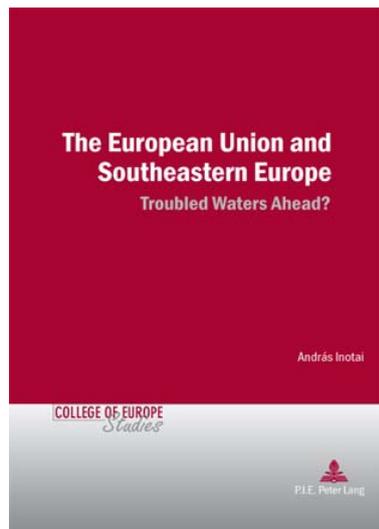
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