

Polanyian Means to Hayekian Ends?

The ‘Ordo-liberalism on Steroids’ Economic Governance Philosophy of the EU

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Abstract

What sort of political-economic system has the European Union grown into over time? If one compares the EU to large Anglo-Saxon federations – Australia, Canada, and the United States – one quickly realizes that this remarkable international organization has developed much more muscular economic authority over its subunits than many national federal governments exercise. While the EU’s main goals fit well with Hayek’s conception of the ideal federation – a multi-level polity in which a central governing body guarantees openness across subunits, allows for competition among subunit policies, and promotes price stability – the EU’s institutional core, the single market and the Eurozone, seems more fundamentally Polanyian, with markets dependent on continual assertion of central institutional authority and rule enforcement. In this paper, we argue that these Polanyian muscles in Hayekian Brussels – “ordo-liberalism” on steroids – reflect a historical institutionalist story of evolving bargains and unintended consequences, stemming from the path dependent interaction of two dynamics in EU history. First, the EU bargaining space generally pitted Anglo-style neoliberal thinking against French-style *dirigisme*, with German *ordo-liberalism* somewhere in the middle, resulting in compromises and grand bargains. Second, the introduction of the euro and EU enlargement, which have substantially upgraded national demands and supranational opportunities to expand the restraining and supervisory role of the central institutions.

The robust and enduring authority of the supranational institutions of the European Union (EU) arguably represents the most remarkable change in international relations (IR) since World War II. Other developments may be more important – the collapse of the Soviet Union, the rapid pace of globalization, the rise of China, nuclear weapons proliferation, or climate change – but none of them challenges so directly our classic understanding of IR as framed mainly through a series of interactions between sovereign states. While experts continue to debate just how deeply Europe has moved “beyond the nation-state,” none would deny that the EU is far and away the leading example of such movement.

More specifically, the EU challenge to classic IR is most evident with respect to economic authority. Though the European project was sold first as a geopolitical attempt to bind war-prone Europeans together into peaceful cooperation, its framers chose economic integration as the means to that end. Today its “Single Market” and single currency hold broad and deep responsibility for the economic governance of the continent. This extensive transfer of authority seems to have achieved its core goal: war among EU member states continues to be hard to imagine. Despite this huge accomplishment, however, the EU faces many current challenges. Eurosceptic opposition has surged. Southern Europeans complain of structural economic disadvantages. Northern Europeans begrudge being asked to bail out the South and fear getting stuck in a transfer union. Central European proto despots are testing the limits of EU rules and democratic values. The British voted to leave the EU to “take back control.” Overall, not many Europeans seem that comfortable with the authority they have delegated to Brussels, even though both the COVID-19 pandemic that started in 2020 and Russian invasion of Ukraine in 2022 may force a more significant recalibration of EU authority in the popular imagination.

To clarify how much today’s EU challenges classic IR thinking and to better understand Europe’s current predicament, this article offers a new account of EU economic authority. Our first section makes a bold comparative claim: EU authority in the Single Market and Eurozone is now more extensive than analogous federal authority in nation-states like the United States, Canada, or Australia. The EU has surpassed all these polities in central constraints on state subunits’ economic policy choices. In some ways its central role is even more active than in the relatively centralized federation of Germany. In other words, practically all scholarship on the EU has substantially mischaracterized the outcome. It is not just the world’s most powerful international organization (IO). In important areas it is more powerful than many states. This

empirical claim gives new force to older arguments that the EU is best understood through direct comparison with other multi-level governments, and therefore ought to be studied from the analytical perspective of comparative political development rather than international relations.¹

Our second section positions this outcome in political-economic theory. What school of thought could see this EU as desirable or predictable? We review existing debates on the EU's relationship to the intellectual traditions of Friedrich von Hayek² or Karl Polanyi,³ and argue that it features a blend. The EU is a polity that pursues Hayekian normative goals – of cross-border openness and market discipline – in ways that fit Polanyian analytical expectations, which theorize that such openness requires strong central authority. We then note that the institutional result resembles the thinking of German ordo-liberals, who share Hayekian goals but envision stronger central authority to enforce it. We show, however, that today's EU displays even more extensive and active central authority than ordo-liberals have advised. The Polanyian muscles in this Hayekian Brussels amount to a kind of ordo-liberalism on steroids.

The third section considers how Europe's "ordoliberalism on steroids" could have arisen. While our dense descriptive work leaves insufficient space for a compelling account of why it *did* arise, with consideration of evidence against alternative explanations, we suggest key features of a plausible explanation. First, we suggest that this outcome seems to call for an explanation that treats interests as deeply contextual and endogenous. The striking variation we display in the policy autonomy that state-level actors defend, and thus the forms of central authority that they accept, hints that local institutions and ideas have channeled these arenas onto quite distinct paths. Second, we argue that Europe's distinctive path appears to reflect strong unintended consequences of sequenced inter-state bargaining rather than the intended outcome of Franco-German leadership. Europe's ordo-liberalism on steroids seems to have emerged because EU states first adopted deliberately supranational institutions; then upgraded commitments to market discipline within them; and then extended this framework across a much more diverse Europe, increasing supranational authority to enforce market discipline over heterogeneous units. Almost nobody intended this overall result — which helps us better understand the EU's current challenges.

¹ Hooghe & Marks 199x; Hix cite; McNamara 2018... and many more...

² Gill 1995; Harmes 2006; Höpner & Schäfer 2012.

³ Caporaso & Tarrow 2009; Van Apeldoorn 2009; Everson and Joerges 2012; Streeck 2016.

1. EU Economic Authority in Comparative Perspective

The EU is an international organization, founded in diplomatic treaties between states, but has gained so much authority that scholars have increasingly compared it to national federations.⁴ This literature presents the US, Canada, and Australia as the most plausible comparative cases, with some comparisons to the more centralized German federation. We survey how EU authority compares to these countries' federal authority over their subunits with respect to both market regulation and macro-economic policies.

1.1. Authority over “Single Markets”

Consider first the terrain of “single markets.” The original European Economic Community (EEC) centered on replicating a core element of American, Canadian, and Australian federalism: empowering central institutions to encourage open exchange across subunits. How does the authority exerted by these federal governments to require subunit openness compare to that of the EU? After these Anglo-Saxon comparisons we sketch the different German case, which becomes important later when we discuss ordo-liberalism.

1.1.1. Legal Foundations

The EU and the Anglo-Saxon federations have roughly comparable constitutional-level bases for federal authority to require openness. The language varies, but no one debates that the founders of all these polities sought to empower central institutions with this market responsibility.

The EEC treaty of 1957 features the most specific clauses to this effect. It committed member-states to eliminate quantitative restrictions on imports of goods “and all measures having equivalent effect,” as well as to “abolition... of the obstacles to free movement of persons, services and capital” (Article 3). Exceptions were possible for reasons of public policy, public security, or public health. It aimed to abolish restrictions on the freedom of establishment and “free supply of services” by 1969 (Arts. 52 and 59); to allow temporary provision of services

⁴ Sbragia 1992; Burgess & Gagnon 1993; Knop et al 1994; Nicolaidis and Howse 2001; Kelemen 2004, 2011; Fabbrini 2005, 2015; Parsons & Jabko 2005; Bartolini 2005; Menon & Schain 2006; Genschel & Jachtenfuchs 2014; Schakel, Hooghe & Marks 2015; Matthijs and Blyth 2015; McNamara 2015, 2018.

“under the same conditions as are imposed by that State on its own nationals” (Art. 60); and called for directives on the mutual recognition of professional qualifications (Art. 57).

The Commerce Clause of the US Constitution (Art. 1, section 8) is vaguer, simply authorizing Congress “to regulate commerce... among the several states.” The Privileges and Immunities Clause (Art. 4, section 2) added that “Citizens of each state shall be entitled to all Privileges and Immunities of Citizens in the several States.” But there is little debate about the founders’ intent on openness. Even conservative “originalists” like Kenneth Starr note, “The same concerns that prompted James Madison to insist on empowering the national government to regulate interstate commerce (the *only* substantive power not included in the Articles of Confederation) counsel in favor of displacing state common law, statutes, and regulatory standards that intrude on federal prerogatives or discriminate against out-of-state commerce.”⁵

The drafters of the Canadian and Australian constitutions were similarly concerned with interstate openness. In the 1860s Canada’s founders sought to upgrade central authority relative to the US, defining distinct federal/provincial competencies rather than making the latter the default.⁶ The federation received exclusive responsibility for “the regulation of trade and commerce” (section 91) and required that provincial goods “be admitted free into each of the other provinces” (section 121). Provinces were responsible for “local works” and other “merely local” matters (section 92). Australia’s drafters in the 1890s were less favorable to centralization, but even more so to openness.⁷ Not only did they copy the US Commerce Clause (Art. 51) and Privileges and Immunities Clause (Art. 117), they added an article (92) asserting that “trade, commerce and intercourse among the States... shall be absolutely free,” and authorized an Interstate Commission (Art. 101) for “execution and maintenance” of these provisions.

1.1.2. Judicial Interpretations

In all these polities powerful judiciaries have strongly shaped these legal commitments. But where the European Court of Justice (ECJ) has consistently maximized central requirements for openness, Anglo-Saxon courts have narrowed them. Relative to the EU, writes legal scholar

⁵ Starr 2007, xv, his emphasis.

⁶ Cites.

⁷ Cites.

Catherine Barnard, the US legal system (and by extension Canada and Australia) “allows a much greater degree of deference to state actors and to state regulation.”⁸

Such deference is strongest in Canadian and Australian jurisprudence. Early on, the Canadian Supreme Court limited federal authority to distinct problems of federal concern. Even federal laws aimed at inter-provincial commerce are unconstitutional if they tread on intra-provincial affairs, like in a 2012 case barring federal legislation to regulate securities.⁹ In the widely-followed “Free the Beer” case of 2018 – challenging New Brunswick’s limits on buying out-of-state beer – the Court confirmed previous rulings that constitutional “be admitted free” language only bars provincial laws whose “primary purpose” is protectionism.¹⁰ Australian law followed similar paths. In 1913, its High Court rendered the Interstate Commission stillborn by ruling that it lacked enforcement powers.¹¹ Like its Canadian counterpart it also found that federal legislation could not tread on intra-state regulatory issues, blocking federal internal-market action for most of the twentieth century. In 1988, the landmark case *Cole v. Whitfield* rediscovered some limits on state powers, but only to bar “discriminatory burdens of the protectionist kind.”¹² Explicitly discriminatory exceptions remain allowable if “appropriate and adapted to their purpose” for other goals.¹³ Other decisions uphold states’ rights to discriminate in public procurement and subsidies.¹⁴

US commerce powers have been interpreted more broadly, but not for the purpose of eliminating interstate barriers. In the 1940s, the New Deal Supreme Court diverged sharply from Canadian and Australian courts on the scope of commerce powers. Seeking to legitimate progressive federal legislation (not to require interstate openness), it found that almost any regulation affects interstate commerce – authorizing Congress to “preempt” many state policies. Later conservative courts narrowed this scope in *Lopez* (1995), *Morrison* (2000), and *NFIB v.*

⁸ Barnard 2009, 578.

⁹ Cite case; Hinajeros 2012. See also Dymond & Moreau 2012.

¹⁰ Cite.

¹¹ Gaegeler, Stephen. 2017. “The Inter-State Commission and the Regulation of Trade and Commerce under the Australian Constitution,” *Public Law Review* 28(3): 205-218.

¹² Cite to Zines, *The High Court and the Constitution* 5th edition, Sydney: Federation Press, 2008. p. 195; Gonzalo Villalta Puig, “The Boundaries of the Free Trade Jurisprudence of the High Court of Australia,” in Puig and Christian Twigg-Flesner, eds. *Boundaries of Commercial and Trade Law*, Munich: Sellier, 2011, pp. 76-101.

¹³ Walsh 2012, 14.

¹⁴ Cite.

Sebelius (2012), but it remains broad today.¹⁵ However, if Congress *could* invoke these powers against interstate barriers, it has hardly done so in living memory (see below). The main openness-related limits on states today reflect court decisions that invoke the so-called “dormant Commerce Clause” to invalidate the most protectionist state laws. It is now applied only against “purposeful discrimination,” like bans on out-of-state wine orders in *Granholm* (2005).¹⁶ Other rulings exempt procurement from commerce considerations – states can favor in-state firms as much as they wish – and exempt state actions like subsidies from antitrust scrutiny.

Meanwhile the ECJ interpreted its legal commitments to openness as far more restrictive for states. The 1974 *Dassonville* case found that the treaty forbade “[a]ll trading rules enacted by Member States which are capable of hindering, directly or indirectly, actually or potentially, intra-Community trade.” In 1979, the *Cassis de Dijon* ruling by the ECJ qualified *Dassonville* – allowing barriers that constitute proportional defense of “general interest” concerns – but clarified a principle of “mutual recognition:” states must accept all goods that meet any states’ rules, unless the receiving state shows they are harmful. Other 1970s cases outlined similar principles in services, though the “big bang” in this sensitive area came with cases in the 1990s.¹⁷ National rules may not “impede” or even “make less attractive” cross-border services provision unless they pass tests based on *Gebhard* (1995). They have to be necessary for imperatives of policy, security, health or the environment; apply equally to home providers (non-discriminatory); suitable to obtain their objective; and proportional (doing only what is necessary for the objective).¹⁸ Other rulings set similar principles for freedom of establishment across borders and somewhat broader limits on short-term “posting” of foreign workers.

1.1.3. Policy Action and State Authority Today

Important though legal principles may be, “judge-made law” is typically slow and passive.¹⁹ Requirements for openness matter most when enacted into legislation and administratively enforced. The most striking divergences in these cases arise at this level. The EU today continues

¹⁵ Quote from Halberstam 2004, 795, referring to the Roberts court, but it summarizes accounts of the Roberts court as well. See Tushnet 2005; Sullivan 2007; Banks & Blakeman 2012; Keck 2015; Bowling & Pickerill 2013; Tribe & Matz 2014.

¹⁶ See Regan 1986; Gardbaum; others...

¹⁷ Hatzopoulos 2012, 103; a key 1974 case was *Van Binsbergen*, and 1990s landmarks were *Dutch TV* and *Säger* (both 1991) and *Alpine Investments*, *Bosman* and *Gebhard* (all 1995).

¹⁸ Cites.

¹⁹ On this point in the EU context, see Nicolaïdis & Meunier (Cite).

to pass central legislation and tighten administrative enforcement to require interstate openness. The US Congress has hardly touched its commerce powers to promote openness in recent decades. Australia and more recently Canada have launched their own “single market” projects – both inspired explicitly by the EU. But unlike the EU, they have pursued voluntary, “inter-governmental” approaches that do not directly challenge state-level authority.

The EU’s single market legislative activity is well known. By the early 1980s, directives harmonized many areas of goods and some in services (like qualifications for doctors, lawyers, or pharmacists). Then came the “Single Market 1992” plan, which sought to implement *Cassis de Dijon* principles across the board. A torrent of legislation into the 1990s largely “completed” the single market for goods, established non-discriminatory public procurement, banned preferential subsidies, and removed some barriers in capital markets and services. Over time services became the main focus, as the “big bang” of services jurisprudence encouraged directives on “posted workers” and then general directives on Professional Qualifications and Services in the mid-2000s. These rules aimed to make the temporary provision of services (where someone based in one state sells services elsewhere) and establishment (where someone based in one state incorporates elsewhere) as automatic as possible. Receiving states face a burden of proof to justify remaining national conditions on such access, subject to Commission and ultimately ECJ review against *Gebhard* tests.

Less widely known is that this activity has continued in the past decade even as the EU struggled with multiple crises. Proposals for more effective enforcement of openness dominate the legislative agenda in the so-called “Services Package,” “Procurement Package,” “Company Law Package” and “Mobility Package.” Already states are required to publicize all remaining impediments to cross-border exchange and mobility, pre-notify the Commission of any changes, tender most contracts through an EU-wide e-Procurement system, and maintain online “Single Points of Contact” for authorization of incoming service providers. A core element of the new proposals would further integrate all remaining national impediments within “Single Digital Gateways” to make them transparently accessible to citizens and to EU reporting and oversight.

The US, meanwhile, has had no “single market project” at all, even though many barriers remain between states. Federal regulations set regulatory floors in several sectors – transport, telecommunications, food and drug safety, part of finance – but these are targeted preemptions in a fragmented landscape. In standards for goods, the US is “by far the most institutionally

heterogeneous and fragmented of all advanced industrial countries.”²⁰ No central standards exist for many goods. One example is elevators: manufacturers make different models for different jurisdictions.²¹ In sectors with federal “floors,” states often set additional requirements, like California’s chemical regulations.²² Professional qualifications are generally state-by-state: even experienced architects, lawyers, electricians, contractors, or hairdressers typically start from zero to qualify to practice in another state, just as they would if they had emigrated from abroad. The concept of temporary interstate provision of services does not exist: providers must be fully licensed in each state to practice for one day. In procurement, 47 states have in-state preferences, including outright bans: Pennsylvanian agencies may *only* buy coal in-state. States freely target subsidies to in-state firms.

Despite the dominance of pro-market rhetoric in the US since Ronald Reagan, Congress has not recently exerted its authority against interstate barriers except to liberalize interstate banking in the 1990s.²³ Reagan himself made “regulatory relief” a headline economic goal of his administration, but focused on weakening federal regulation, not using federal power against interstate barriers.²⁴ Subsequent pro-market Republicans maintained this focus on loosening federal rules, with no attention to requiring state-level openness. As Republican House Speaker Paul Ryan’s “Better Way” manifesto said in 2016, federal regulation should be “used sparingly,” because “States in many cases do a better job, and should be encouraged to take the lead.”²⁵ None of the deregulation under President Trump has related to interstate barriers.²⁶

Australia and Canada have undertaken more “single market” legislation, but without building up central legal authority. Until fairly recently, both countries had even more interstate barriers than the US.²⁷ In the 1980s, Australians became concerned about relative decline in wealth and productivity. In 1992, with constant references to Europe’s “Single Market 1992,” they created the “Council of Australian Governments” (COAG): an intergovernmental set of

²⁰ Jay Tate in *Varieties of Capitalism*, 463. See also Mattli and Büthe 2003.

²¹ Hoffmann 2011.

²² For an overview, see the American National Standards Institute site, https://www.standardsportal.org/usa_en/key_information/state_level.aspx.

²³ Cite on banking; Deroy Murdock, “Tear Down State Barriers to Health Insurance,” *National Review Online*, April 14, 2017.

²⁴ Prasad 2006; Viscusi 1994.

²⁵ Cite.

²⁶ See the Brookings Institution’s “tracker” of deregulation under Trump at <https://www.brookings.edu/interactives/tracking-deregulation-in-the-trump-era/>.

²⁷ Cites.

policy area councils of federal and state ministers. The federal budget incentivizes states to meet COAG goals, but their participation is voluntary.²⁸ Operating mainly by suggesting “model laws” that each state passes separately, the process has successfully ended discrimination in procurement, established some mutual recognition of qualifications, and adopted a stronger National Competition Policy. Preferential subsidies remain possible but must be justified in terms of “public benefits.” In 2007 it added a focus on reducing regulatory fragmentation in the “National Partnership Agreement to Deliver a Seamless National Economy.” Negotiations continue to move forward gradually today.²⁹

Canada’s more recent steps were even more directly spurred by the EU. In the 1990s, the North American Free Trade Agreement (NAFTA) and the EU’s “1992” model nudged federal and provincial governments into conversations on internal trade. They initially produced a non-binding, intergovernmental “Agreement on Internal Trade” (AIT) that delivered little change.³⁰ More significant steps reacted to the Canada-EU Comprehensive Economic and Trade Agreement (CETA) in 2014. It sparked objections that European companies would enjoy freer market access than Canadian firms did across provinces. This was indeed the case. Goods face different standards and requirements for interprovincial “imports;”³¹ professional qualifications are mostly exclusive; local preferences apply in subsidies and procurement. In 2016, the Senate published a report titled, “Tear Down these Walls: Dismantling Canada’s Internal Trade Barriers,”³² leading to the more robust Canadian Free Trade Agreement (CFTA) in 2017. The provinces agreed to pursue openness for goods and services (with a huge caveat for “protection... appropriate to achieve a legitimate objective”); non-discrimination in procurement and subsidies; and to reconcile provincial differences in regulation and licensing. Provincial participation remains voluntary, however, and results are modest to date. The 2018 “Free the Beer” case disappointed advocates who hoped for a new legal impetus. As one lawyer said after

²⁸ Walsh 2012, 37.

²⁹ See, for example, the Productivity Commission’s 2015 report on ongoing efforts in mutual recognition of qualifications. (ADD link).

³⁰ Brown 2001: 163.

³¹ See, ironically, European Commission, *The Food and Beverage Market Entry Handbook: Canada*. Brussels: European Commission, 2017.

³² See Canadian Senate report, “Tear Down These Walls: Dismantling Canada’s Internal Trade Barriers,” June 2016, <http://publications.gc.ca/site/eng/9.819431/publication.html>.

the decision, “This is going to have to be negotiated by the provinces rather than decreed by the Supreme Court.”³³

1.1.4. The Absence of Single-Market Issues in the Centralized German Federation

The EU’s Single Market authority is easiest to compare to that of Anglo-Saxon federations, which feature parallel debates about commerce powers and interstate barriers. To set up our discussion of ordo-liberalism below we quickly describe German federalism as well. The key point, though, is that it has few comparable debates. In this more centralized and homogeneous federation, “single market” fights have not come up.

Germany is often called a “unitary federal state.”³⁴ Its Basic Law assigns the federation responsibility for “legal and economic unity” and “the establishment of equivalent living conditions” (Art. 72), as well as sole authority for “unity of the customs and trading area” and “free movement of goods.” The *Länder* have little autonomy in taxation: strong revenue-sharing schemes equalize their budgets. They share “concurrent” authority with Berlin on most other “economic matters” – including major regulatory areas like labor, health and safety standards – but most regulation is passed at the federal level and implemented by the states. This logic of shared authority routinely involves the kind of federal “commandeering” that is fiercely resisted by Anglo states.³⁵ As one specialist summarizes, “...[T]o a far greater degree than... in Canada or the United States... the states carry out centrally-made decisions.”³⁶

The result is that the *Länder* exert influence over economic regulation mainly as partners in federal policymaking, not by resisting encroachment on their own distinct regulations. The Bundesrat (Senate), where *Länder* governments are represented directly, must pass roughly 60 per cent of federal legislation. Around this veto point extends “cooperative federalism,” with committees linking *Land* and federal departments and a Forum of Prime Ministers (including the German Chancellor). In some areas *Länder* defend more autonomy – education, culture, and police matters, with recent trends toward policy divergence³⁷ – but federal responsibility for “economic unity,” together with the longstanding dominance of national-level interest groups

³³ Litigator Andrew Bernstein, quoted by the BBC, 19 April 2018, <https://www.bbc.com/news/world-us-canada-43813125>.

³⁴ Kommers 1997, 68.

³⁵ Halberstam & Mills 2001.

³⁶ Taylor 2009, 153.

³⁷ Jeffrey et al 2016.

and standards associations, invites little conflict over interstate exchange. German jurisprudence has no parallels to commerce-clause fights, and the Federal Constitutional Court “has rarely had a role in judging conflicts about responsibilities between the federal government and the *Länder*.”³⁸ Thus German regulation is so nationalized, and German states participate so constantly in federal regulatory processes, that the German federation has not needed to actively develop or enforce requirements over state-level regulations. No hint of a “single market project” arose in modern Germany because it is a “federal state with a unitary political culture.”³⁹

In sum, if we compare the EU’s economic authority over its sub-units with other large Anglo-Saxon federations, we have to conclude that it possesses much more muscular central power from the point of view of its legal foundations, judicial interpretation, and policy action. As we will see later, the goals are Hayek’s – economic openness and free competition – but the means to get there are what Polanyi would have expected, i.e. centralizing governing institutions established by political power.

1.2. Authority over Fiscal Policy & Debt Management

Now we turn from market regulation to macro-economic policy. Here it seems like international authority should be even harder to establish. The EU’s authority over market access is an extreme case of a phenomenon that is nonetheless common: states routinely negotiate trade treaties that legally constrain their policies. In fiscal policy, by contrast, formal international constraints are extremely rare. Normally they arise only around poor states in severe crises that cannot finance themselves. In democracies, moreover, budgetary control is frequently seen as a fundamental responsibility of domestic elected officials.⁴⁰ For an international organization to gain authority in this realm is thus especially striking. In this section, we show that even though the EU lacks national federations’ resources as a fiscal *actor*, it greatly exceeds their authority in fiscal *oversight*.

1.2.1 Central Institutions as Fiscal Actors

³⁸ Schneider 2006, 143.

³⁹ Scharpf 2008, 510.

⁴⁰ Genschel and Jachtenfuchs 2014.

One channel of fiscal authority by which central institutions influence subunits in multi-level polities is their own ability to tax, spend, borrow, and redistribute. In this respect the EU has nothing like the powers of federal governments. This relates to the EU oversight powers noted below: with few fiscal resources of its own, EU authority necessarily operates through oversight rather than action. It also makes that authority more remarkable. An IO with modest resources to offer – unlike, say, the International Monetary Fund (IMF) – has acquired substantial control over national budgets.

The American, Canadian, Australian and German federations are all substantial entities that spend a great deal of money. They have broad authority to levy taxes and borrow money and then spend in many areas and may also influence their sub-units through conditional grants. They also confront various limits on their fiscal action, however, which all have stronger parallels in the EU.

One simple sort of limit is decentralization. States that spend more money generally have more autonomy. Canada is the most decentralized OECD member, with direct federal spending (after transfers to provinces) at roughly a third of overall expenditure (see Table 1). The American federation is a bigger spender, at over 50 per cent. Australia's federal spending share is close to America's, but stronger federal domination of tax collection makes its states more dependent on transfers and centralizes power overall. Germany falls in the middle of the pack. Its more unitary principles allow much freer federal "commandeering" of states to administer federal policies, so direct spending understates federal influence, but the Länder's strong role in federal policymaking through the Bundesrat means that such influence is usually meticulously negotiated.⁴¹

Other limits come in requirements for equalization of revenues across sub-units. Such rules make most federal transfers quasi-automatic in Canada (such that federal conditionality is very modest), Germany (where the constitution specifies extensive tax-sharing and equalization, plus other transfers are effectively negotiated between the Bund and the Länder rather than simply offered conditionally) and Australia (where equalization rules are especially redistributive, though a larger federal budget makes unconditional transfers only about half of all

⁴¹Cite Halberstam.

transfers).⁴² By contrast the US federal government attaches conditions to almost all grants and faces no equalization rules.

Some federations face limits on areas where they can spend. The German federation requires Bundesrat authorization to spend in areas of Länder responsibilities. Australian federal spending is mostly free, though recent jurisprudence raises questions about possible limits.⁴³ Again the US is unconstrained: its Supreme Court holds that federal spending can freely incentivize state action even in areas beyond federal legislative authority. Canada’s federation enjoys the same authorization, though decentralization and equalization leave much less room to use it.

Table 1. The EU and national federations as fiscal actors

	Initial central share of total revenue ^α	Central share of total spending ^α	Share of state revenue from central transfers ^β	Fiscal equalization across states?	Conditional transfers share of all transfers ^ζ	Central share of all public debt ^δ
AUS	69%	55%	45%	Yes	≈50%	71%
US	58%	52%	26%	No	>80%	72%
DEU	64%	47%	15%	Yes	<10%	64%
CAN	46%	32%	19%	Yes	<5%	42%
EU[‡]	0%	1.9%	1.8%	No	Most	.004%

^α2014 figures from Blöchliger and Kim 2016, 16; Australian figures from 2011, in *OECD Economic Surveys: Australia 2014*.

^βParker 2015, 192. Figures are from 2007.

^ζWatts 2005, 55; updated support for these rough estimates from Hueglin and Fenna 2015, 166-204.

^δ2016 figures from IMF Government Finance Statistics.

[‡]EU figures are authors’ calculations based on EU data, http://ec.europa.eu/budget/figures/interactive/index_en.cfm.

[Needs to be updated to take into account “next generation EU” response to the Covid-19 pandemic & “re-Power EU” response to the Russian invasion of Ukraine]

⁴²See Watts 2005; Hueglin and Fenna 2015; Parker 2015; Béland and Lecours 2018.

⁴³See Chordia and Lynch 20xx.

How does the EU compare as a fiscal actor? Among IOs, it has no peers. Its budget is roughly fifteen times that of the United Nations (including peacekeeping operations), and larger than the national budgets of all but eight EU member-states.⁴⁴ But if EU spending is substantial enough to affect targeted policy areas and regions, it is not in the same category as national federations. Many limits make its fiscal role look much more like an overgrown IO than a national government.

No national federation has ever approached EU levels of fiscal decentralization. The EU collects none of its own revenue. It all comes as upward transfers from the states through negotiated formulae for sharing customs duties, VAT, and direct budgetary contributions. Then almost all effectively gets transferred back to be spent by the member-states. Of the 1.9 per cent of overall EU-28 revenue that was transferred into EU “own resources” in 2018, over 75 per cent of that revenue was doled back out to member-states to spend in programs for farmers, fishermen, and regional development. The EU can only borrow to make loans to member-states under specific conditions, not to finance operations.

“Equalization” of various sorts dominates the distribution of downward EU transfers. Transfers to support farmers, fishermen, or poorer regions are declining, but are still roughly 70 per cent of the 2018 budget. Only about 20 per cent of the budget targets items that are arguably distinctive EU-level priorities—research, educational programs like the Erasmus exchange framework, trans-European infrastructure, foreign and security policy, migrant integration—and these too bear a heavy mark of interstate distributive bargains. Significant EU oversight and conditionality shape precisely how all these monies are spent, but “precisely” is the key word: EU priorities exert influence within the main lines set by multi-annual redistributive deals.⁴⁵

Overall, the EU’s budgetary limits are so severe that its fiscal role “bears little resemblance to that in central government of nation-states, whether federal or unitary...”⁴⁶ Its revenues are capped at 1.2 per cent of EU gross national income (GNI). Budget frameworks are haggled out in seven-year “multi-year financial frameworks” (MFF) that require member-state unanimity, underscoring a disconnect from macro-economic management that could respond to

⁴⁴ EU Budget Factsheet, http://ec.europa.eu/budget/library/biblio/publications/2017/EUbudget-factsheet-2018_en.pdf; United Nations: <https://www.un.org/en/ga/fifth/72/ppb1819sg.shtml>

⁴⁵ CITE someone on EU budgetary politics here.

⁴⁶ Begg 2009

evolving conditions. The current MFF (for 2014-20) also saw the first-ever real decline in EU spending, at the insistence of richer member-states.

A greater fiscal role may be in the EU's future. As a first step into counter-cyclical action, in 2014 Commission President Jean-Claude Juncker cleverly repurposed €20 billion to back €60 billion in borrowing by the European Investment Bank, which then had some success in leveraging private investment in projects too risky to undertake otherwise.⁴⁷ In June 2018 the Commission proposed to render permanent this mechanism as a new "InvestEU" fund. French President Emmanuel Macron has recently floated ideas for a more serious Eurozone budget.⁴⁸ Next Generation EU – the EU's "Recovery and Resilience Facility" set up in response to the COVID-19 pandemic – added up to 800 billion euro over 7 years, with roughly half of it to be disbursed as grants and the other half as loans, the equivalent of an extra 0.5% of the EU's annual GDP. While this constitutes a significant step towards a closer EU fiscal union, for the moment, the EU's fiscal action continues to pale in comparison to its oversight powers.

1.2.2 Central Fiscal Oversight

Besides using their own fiscal resources, central actors in multi-tier systems may exert authority over subunits' resources. In principle such arrangements could range from fully autonomous subunit spending and borrowing to hierarchical relations where the center can steer or veto subunit choices. The latter might or might not come with central responsibility to support or bail out subunits in fiscal difficulties.

At one end of this spectrum today is the US, which sets no demands or supports around state fiscal autonomy. Its states define their budgets and borrow "essentially as sovereigns."⁴⁹ State budgets face no federal monitoring or expectations for bailouts in crisis. At the republic's origin this separation was uncertain: the federal government initially assumed state debts. The key step toward today's arrangements came in 1843, when better-off states blocked bailout requests from nine insolvent states. International money markets reacted to the multi-state default by shutting the whole US out from finance into the late 1840s, extending an already-severe depression. Yet this painful episode consolidated "no bailout" expectations that have

⁴⁷Sarah Gordon, "Juncker's Investment Plan: Rhetoric versus Reality," *Financial Times*, March 28, 2017.

⁴⁸ Beatriz Rios, "Goodbye Juncker Plan, Hello InvestEU," *Euroactiv.com*, June 6, 2018.

⁴⁹ Rodden 2006, 142.

endured ever since.⁵⁰ It also convinced states to limit themselves fiscally, launching a wave of balanced-budget rules. States did so voluntarily, without any federal role in this movement.⁵¹

Canadian provinces enjoy similar autonomy. In Jonathan Rodden’s phrase, “each Canadian government often proceeds as if the other did not exist.”⁵² Canadian observers perceive more uncertainty, however, about the potential for bailouts.⁵³ Canada never explicitly rejected bailouts like the US did in the 1840s; to the contrary, federal funds rescued insolvent Alberta and Saskatchewan in the 1930s. Moreover, greater decentralization means that provinces hold a majority of public debt, hinting at pressure for bailouts because state-level defaults would be more likely to taint all national credit.⁵⁴ Still, the status quo is that the provinces tax, spend and borrow as they please without oversight. Like US states, their only strict limits are the balanced-budget rules that eight of the ten provinces adopted themselves (in this case, since 1990).⁵⁵

Australia has long occupied the other end of the spectrum. Not only are its states especially dependent on federal fiscal resources, they must submit annual plans for borrowing to the national Australian Loan Council. This body dates from the 1920s, when the Commonwealth absorbed state debts and created the Council to approve all future state borrowing. But if Australian fiscal federalism overall has centralized even more since then—with the federation gathering more taxes and using its resources to influence state fiscal action⁵⁶—direct fiscal oversight actually lessened considerably in the 1990s. Federal and state leaders agreed to replace the effective Commonwealth veto with market discipline, and states became free to borrow. They still report annual financing needs, and the Council may request an explanation, but cannot alter their choices. Its goal now is just to attract market scrutiny if borrowing seems excessive.⁵⁷

Germany has moved in the other direction, putting new legal limits on state fiscality. Its postwar regime is closer to the Australian end of our spectrum, with “fiscal semi-sovereignty”

⁵⁰ Rodden 2006, PAGE (ch. 3). But the constitution assigns federal responsibility for the District of Columbia, which was bailed out the 1990s. Puerto Rico’s budget has also been under federal oversight since 2016.

⁵¹ Fabbrini, 2013: 30

⁵² Rodden 2006, PAGES (ch. 10).

⁵³ Jacques Poitras, “What happens if New Brunswick defaults on its debt?” CBC News, March 1, 2018. <https://www.cbc.ca/news/canada/new-brunswick/nb-what-happens-default-debt-1.4555976>.

⁵⁴ Joffe, Marc. 2012. “Provincial Solvency and Federal Obligations.” Ottawa: MacDonald-Laurier Institute.

⁵⁵ Mou, Haizen, Michael Atkinson and Stephen Tapp 2017. “Do Balanced Budget Laws Matter in Recessions?” *Public Budgeting & Finance* 38(1): 28-46.

⁵⁶ Fenna 2018.

⁵⁷ Koutsogeorgopoulou and Tuske 2015.

for the Länder.⁵⁸ Almost all Länder revenue comes from “shared” taxes (which both levels must approve) distributed through elaborate fiscal equalization, and since 1969 budgeting has been partly coordinated in a federal Financial Planning Council. This cumbersome co-dependence long left borrowing as the one area where Länder were fairly free. Here they faced no oversight—besides an ineffective constitutional injunction against borrowing in excess of “investment purposes”—and their influence in the Bundesrat protected them from central sanction. They also enjoyed federal support: in 1992 two insolvent Länder argued successfully in court that the federation’s responsibility for “equality of living conditions” made it liable for bailouts. Constitutional reforms in 2009 altered this permissive regime. As Abraham Newman has argued, “solidarity exhaustion” hit much of Germany after the expensive reconstruction of Eastern Germany.⁵⁹ The richer Länder led a push to impose a “debt brake” (*Schuldenbremse*) on both levels of government.⁶⁰ Länder budgets must now be kept close to balance. They must report on debt twice a year to a Stability Council (the upgraded Financial Planning Council), and they cannot incur new net debt after 2020. The Stability Council itself cannot impose sanctions, so doubts remain about enforcement, but the legal expectations are clear.⁶¹

How does EU fiscal oversight compare? Like with fiscal action, it is in another category from national federations—but in the other direction. In principle EU member-states accepted fiscal limits when they agreed to create the euro in the Maastricht Treaty of 1991: its “convergence criteria” limited deficits to 3 per cent of GDP and national debt to 60 per cent. Concerns about loose application of these criteria, especially from Germany, led to the Stability and Growth Pact (SGP) in 1997, which aimed for permanent scrutiny along these lines.⁶² Initially it arrangements proved ineffective, and an ailing Germany itself supported loosening SGP rules in 2005. But with the onset of the sovereign debt crisis in 2009, a slew of new regulations and

⁵⁸ Rodden 2006, page (start ch. 7). He echoes Katzenstein CITE.

⁵⁹ Newman in Future of Euro, 128.

⁶⁰ Feld and Baskaran 2010.

⁶¹ Kirchgässner 2017. The Council was, however, able to impose special conditions on five shaky Länder who received special support during the transition period to 2020.

⁶² Cite Heipertz and Verdun (2004)

treaties upgraded EU oversight.⁶³ The result is the “European Semester,” “an annual cycle of coordination and surveillance of EU economic policies” (as the Commission puts it⁶⁴):

- First comes a process of goal-setting. Each November the Commission publishes an Annual Growth Survey, launching a discussion of economic priorities to be approved by the European Council (the heads of government) in March. In parallel, the Commission publishes reports in February on each state’s economic situation and progress on previously-agreed reforms.
- As mid-year approaches more specific parameters are set. In April states must present three-year budget plans to the Commission, including plans to address previous EU recommendations. In May the Commission produces country-specific recommendations. These address not only fiscal rectitude but also countries’ efforts to meet EU policy goals. They are discussed in the Council and adopted in July by “reverse qualified majority voting” (RQMV): accepted unless a super-majority opposes them.
- Autumn is final budgeting season. By October 15 states must submit full draft budgets to the Commission, prior to passage through national parliaments. In November the Commission assesses plans against the SGP and its recommendations and issues an Opinion. Countries that are not currently meeting the SGP’s debt or debt rules are evaluated against the “adjustment path” to which they have previously committed. The Commission can reject a state’s budget and require specific amendments, as it did to Italy in November 2018. States must adopt their budgets by the end of December.

The “Semester” also feeds into the Macroeconomic Imbalance Procedure (MIP). Each November, past reviews can trigger an early-warning “Alert Mechanism Procedure” for special scrutiny going forward.⁶⁵ The Commission can eventually take punitive steps against states failing to address debt problems or serious imbalances. For Eurozone states it can issue a warning (with Council approval by RQMV) and require the state to set aside an interest-bearing deposit of up to 0.2 per cent of GDP. Past the warning stage it can seek Council approval to

⁶³ Matthijs and Blyth (2018)

⁶⁴ European Commission (2019) https://ec.europa.eu/info/business-economy-euro/economic-and-fiscal-policy-coordination/eu-economic-governance-monitoring-prevention-correction/european-semester/framework/eu-economic-governance-explained_en

⁶⁵ Thirteen states were flagged in 2018 (Bulgaria, Croatia, Cyprus, France, Germany, Greece, Ireland, Italy, Netherlands, Portugal, Romania, Slovenia, Spain, Sweden).

initiate either the “Excessive Debt Procedure” (EDP, by RQMV) or the “Excessive Imbalance Procedure” (EIP, by normal QMV). It can require specific reforms, suspension of some EU funding, and large fines (up to 0.2 per cent of GDP for the EDP; 0.5 per cent given statistical fraud; or 0.1 per cent for the EIP). The power of these tools has recently been tested: after the Commission threatened to launch the EDP for Italy, Rome’s populist government backed down and revised its budget.

All this oversight comes with some potential for central support, though not much. Eurozone countries are eligible for bailouts from the European Stability Mechanism (ESM). Funded by national contributions—almost half from Germany and France—it can offer up to €700 billion for countries at risk of losing access to market financing. Over the past decade the ESM and its temporary predecessor (the European Financial Stability Facility, EFSF) distributed €254.5 billion for broad bailouts of three small economies (Greece, Ireland, Portugal) and more targeted banking rescues for one large and one tiny one (Spain and Cyprus). Even the lion’s share of these funds could not restore faith in Greek debt, however. Greek bond yields only retreated from crisis levels in 2012 after ECB President Mario Draghi announced the “Outright Monetary Transactions” (OMT) program to purchase debt of distressed states— after saying he would do “whatever it takes to preserve the euro.”⁶⁶ This pledge of ECB resources to salvage national debt was so effective that OMT was never used. Yet it is unclear today that even the ESM and OMT together could bail out an economy like Italy’s (ten times bigger than Greece’s). Moreover, states may only receive OMT support after seeking an ESM bailout, which means accepting reform plans and far *more intrusive* oversight. Thus even the populist Italian government that recently picked a fight with the EU eventually opted to follow the Commission’s fiscal guidance.

As EU specialist Ben Crum summarizes, “the experience of the Euro crisis has led national economic policies to become incorporated in a dense web of European surveillance.”⁶⁷ Not even the centralized federations of Australia or Germany subject states to such extensive fiscal oversight. Like in the Single Market, EU authority in the Eurozone has surpassed that of national federations in important ways.

⁶⁶ Cite Draghi July 2012 London speech

⁶⁷ Crum 2018, 281.

2. EU Economic Authority in Theoretical Terms

Having described the EU's economic authority in comparative perspective, we now consider what sort of political-economic thinking could have inspired such a model. What theoretical perspective on economic governance might endorse such authority normatively, or help us to understand analytically why it arose? Three notable political-economic labels that have been prominently applied to the EU in recent years are "Hayekian," "Polanyian," and "ordo-liberal."⁶⁸ Positioning the EU outcome relative to these theoretical schools allows us to describe it as a Polanyi-esque pursuit of Hayekian goals, or a bulked-up form of "ordo-liberalism on steroids."

2.1. A Hayekian EU?

When political economists seek labels for binding frameworks of openness and market discipline, they are likely to think of "Hayekian." Friedrich von Hayek's famous 1939 essay on "The Economic Conditions of Interstate Federalism" argued that a certain form of multi-level government would best deliver economic liberty and its wealth-generating effects. Markets flourish where central authority ensures that "goods, men and money can move freely over [subunit] frontiers" – but does little else.⁶⁹ If the center is limited to this function (plus defense), and mobility and competition across subunits deters their interventionism, the desirable result will be "less government all round."⁷⁰

These ideas later developed into "constitutional economics" in the hands of American economists like Milton Friedman (and the "Chicago School") and James Buchanan (and the "Virginia School").⁷¹ In the US context Hayek's model became known as "competitive federalism:" tight constitutional limits restrain federal power, and interstate openness disciplines states through competition over mobile factors of production.⁷² The same ideas are known to many political scientists through Barry Weingast's concept of "market-preserving federalism." Weingast argued that multi-jurisdictional markets thrive if "subnational authorities have primary authority over regulating the economy," but central authorities are tasked with "preventing the

⁶⁸ See Caporaso and Tarrow 2009, Höpner and Schäfer 2012, Young 2014, Matthijs 2016.

⁶⁹ Hayek 1939, 258.

⁷⁰ Ibid, 266.

⁷¹ Boettke & Candela 2016.

⁷² Buchanan 1975, 1989; Brennan & Buchanan 1980.

lower governments from using their regulatory authority to erect trade barriers against the goods and services from other units.”⁷³

This image sounds much like the EU, especially when we add Hayek’s musing that central enforcement of openness might need to be extensive:

... all the effects of protection can be achieved by means of such provisions as sanitary regulations, requirements of inspection, and the charging of fees for these and other administrative controls. In view of the inventiveness shown by state legislators in this respect, it seems clear that no specific prohibitions in the constitution of the federation would suffice to prevent such developments; the federal government would probably have to be given general restraining powers to this end. This means that the federation will have to possess the negative power of preventing individual states from interfering with economic activity in certain ways, although it may not have the positive power of acting in their stead.⁷⁴

Also evocative of the EU was Hayek’s inclusion in his 1939 essay on interstate federalism of a “common monetary unit” under which “the latitude given to the national central banks will be restricted as much as it was under a rigid gold standard...”⁷⁵

It is tempting, then – though ultimately problematic – to join the scholars who argue that the EU has come “to resemble Hayek’s blueprint of ‘interstate federalism.’”⁷⁶ With its active central enforcement of openness and macro-economic discipline, the EU certainly features a neoliberal “new constitutionalism”⁷⁷ that imposes “constraints on government intervention by locking-in inter-jurisdictional competition.”⁷⁸ But this characterization is problematic for a simple reason: Hayekians dislike the EU’s economic authority. Not only do they voice unsurprising criticisms of the EU’s market-mitigating features – the Common Agricultural Policy, regional development funds, social policy rules – but they object that the Single Market and Eurozone are *too* restrictive. Buchanan lamented Jacques Delors’ vision of a Union in which “the whole economy is subject to uniform regulation,” belying a “basic failure to understand the nature of competitive federalism.”⁷⁹ Hayekian historian John Gillingham describes the EU’s

⁷³ Weingast 1995, 4.

⁷⁴ Hayek 1939, 267.

⁷⁵ Hayek 1939, 259.

⁷⁶ Höpner & Schäfer 2012, 431.

⁷⁷ Gill 1995.

⁷⁸ Harmes 2006, 727.

⁷⁹ Buchanan 1995, 25; Buchanan 1996, 255.

regulatory harmonization as derailing a promising “new market economy” into an ominous “superstate.”⁸⁰ The related “Bocconi School” economists Alberto Alesina and Enrico Spolaore object to the EU’s “excessive centralization,” since “fiscal policy and taxation, regulation of markets, education, and social protection and welfare... are best left in the hands of national governments.”⁸¹ Hayekian monetary theorists like Roland Vaubel or Milton Friedman have been vitriolic critics of the Euro from its origins.⁸² Experts at the Hayek Institute in Vienna, the Mont Pelerin Society Hayek founded, or the Cato Institute in Washington, DC today display a “wholesale rejection of the European project,” seeing the EU as a centralized monstrosity.⁸³

These criticisms reflect a downgrading of the role for central authority in Hayek’s later work and others’ – especially Americans’ – elaborations of his themes. The early Hayek displayed clearer support for central authority to establish market conditions, more like German *ordo-liberals* (of which more below).⁸⁴ During his later career in the UK and then the US, he placed increasing emphasis on “competition as a discovery procedure.”⁸⁵ Wherever possible the best policies should be “discovered” in evolutionary processes of decentralized competition, not bindingly imposed. This thrust was at the heart of the work of Milton Friedman, James Buchanan, and others, who identified central authority as the main threat to markets, not states’ protectionist temptations. The bigger the government, the more regulatory capture and inefficient abstract rules would produce bad outcomes. “If government is to exercise power,” Friedman argued, “better in the county than in the state, better in the state than in Washington.”⁸⁶ Buchanan developed public choice theories to argue that given basic interstate “exit” possibilities for capital or labor, states will compete to attract them. Charles Tiebout theorized that “sorting” will then enhance welfare even if states are not disciplined into market-friendly policies, since remaining differences in state policies allows mobile citizens to choose among packages of public goods.⁸⁷ Even on single market issues concerning interstate barriers – e.g. occupational

⁸⁰ Gillingham 2003.

⁸¹ Alesina & Spolaore 2003, 206.

⁸² Cite Vaubel.

⁸³ Rohac 2016, 10.

⁸⁴ Kolev 2010; Jackson 2010.

⁸⁵ For one of many statements, Hayek 2002(1968).

⁸⁶ Friedman 1962, 3.

⁸⁷ There is, however, little empirical evidence either that American states change their policies or that citizens move for these reasons. Tiebout 1956; Musgrave 1959; Oates 1972; Oates & Schwab 1988; McKinnon 1997; Banzhaf & Walsh 2008.

licensing – these theorists tend to see state “competition” over such rules as preferable to “uniform regulation.” These are the arguments that conservatives in the UK offer to insist that “Hayek would have been a Brexiteer.”⁸⁸

In monetary affairs, Hayekians tend to praise the EU’s macro-economic disciplining of Eurozone members while remaining skeptical of its strong central authority to do so. At the end of Hayek’s career, he called for privatizing money, criticizing government currencies as money “monopolies” and envisioning a competitive “discovery process” among specie. At this point he specifically rejected a European currency.⁸⁹ Some note that he took this stance because he thought it impossible politically to do what the Eurozone later did: establish an independent European Central Bank (ECB) with a sole mandate for price stability and (initial) guarantees against monetary financing.⁹⁰ If Hayek might have conceded some merit in the euro’s framework, however, Hayekian economists have generally attacked it with themes that parallel their opposition to regulatory harmonization: such high-level authority is vulnerable to “capture,” delivers crude one-size-fits-all policies, and will tend to expand its interventionism.⁹¹ They feel vindicated by the ECB’s shift to quantitative easing and the EU’s expansion of fiscal oversight and banking regulation, showing that such centralized institutions could never resist political pressures to meddle further.⁹²

If the EU’s economic model shares Hayekian normative goals of openness and market discipline, then, it does not reflect Hayekian advice about how to pursue them. Hayekians expect that their goals are best delivered by institutional arrangements with much less central authority.

2.2. A Polanyian EU?

Perhaps, then, other political economists are right to perceive “Polanyian” dynamics at work in the EU? Polanyi saw a “double movement” in the spread of “market society” in nineteenth century Europe.⁹³ The first movement was a state-driven ideological project of market building. Polanyi judged the drive to marketization to be profoundly harmful and unnatural, and observed

⁸⁸ As one example among many, Ryan Bourne, “Hayek Would Have Been a Brexiteer,” *Institute of Economic Affairs (IEA)*, London, blog entry March 16, 2016, at <https://iea.org.uk/blog/hayek-would-have-been-a-brexiteer>.

⁸⁹ Hayek 1978.

⁹⁰ Issing 1999, 56.

⁹¹ Vaubel 1999; others?

⁹² Need citations.

⁹³ Polanyi 1944.

a destructive process of “dis-embedding” economic exchange from other social relationships. Analytically he argued that it thus depended heavily on central state authority to advance and maintain itself. He also theorized that the first movement would naturally provoke a “second movement,” as people fought to “re-embed” markets in social norms.

Polanyi-inspired scholars usually criticize the EU even more sharply than Hayekians in normative terms, but their analytic understanding of market-building makes better sense of EU authority. Many Polanyians interpret EU history to this point as a “first movement” process in which an especially wide and deep market project is predictably accompanied by increasingly powerful central institutions. Indeed, some of the critics cited above who denounce the EU as Hayekian – but ignore that Hayekians dislike strong central institutions – are really offering Polanyian analyses. Adam Harmes draws on Polanyi to explain why Hayekian goals require “more deliberate and specific institutional mechanisms to separate economics from politics.”⁹⁴ Stephen Gill stresses that the EU’s “new constitutionalism” uses institutions to prevent a second-movement reaction.⁹⁵ Many other scholars invoke Polanyi in similar veins. Michelle Everson and Christian Joerges argue that in a Europe where ECJ decisions undercut national labor laws and the constraints of monetary union operate without democratic input, “... Polanyi’s insights have gained a depressing degree of topicality.”⁹⁶ Wolfgang Streeck writes of his conversion to Polanyian thinking to understand Europe’s challenges and answer the dramatic question, *How Will Capitalism End?*⁹⁷ Matthias Goldman sees the EU reproducing Polanyi’s 19th-century story, such that “... we might sleepwalk into another human, political, economic and social catastrophe.”⁹⁸

Less clear, and contested among Polanyian thinkers, is whether the EU outcome today also displays the second prong of Polanyian expectations. The scholars cited above are rather pessimistic Polanyians, emphasizing that central institutions and business power still stifle any significant “second movement.” More optimistic Polanyians read aspects of the EU as maintaining or developing “embedded” limits on markets. Economic sociologist Fred Block’s “neo-Polanyian” analysis of American neoliberal deregulation – which he attributes to an

⁹⁴ Harmes 2006, 730.

⁹⁵ Gill 1998, 23.

⁹⁶ Everson and Joerges 2012, 646.

⁹⁷ Streeck 2016.

⁹⁸ Goldman 2017, 273.

alliance of American business with the religious right – refers to the EU as better balanced between Polanyi’s two forces: “Without the prospect of a dramatically different set of political allies, business in Europe has generally kept its distance from the most aggressive versions of market fundamentalism. At both the European Community level and within member states, businesses generally lobby for their preferred policies within a framework that acknowledges the necessity and legitimacy of a governmental role in shaping the economy.”⁹⁹ Bastiaan Van Apeldoorn, while more critical of the EU order, also describes it as “embedded neoliberalism” that mixes markets and social protections.¹⁰⁰ James Caporaso and Sidney Tarrow build on Block to emphasize an even more optimistically embedded image of “Polanyi in Brussels.” They see in ECJ jurisprudence an “attempt to shape market-making through regulations that aim to embed the market within its understanding of legitimate social purposes.” In ensuring the portability of social benefits, for example, they argue that “the ECJ has intervened between the European free-market regime and domestic structures to begin to create what we regard as a structure of *supranational embedded liberal compromises*.”¹⁰¹

Our preceding description of the EU economic order in comparative perspective better supports the pessimistic Polanyians. More than any other current polity, the EU institutionalizes a central prioritization of unfettered economic flows and macro-economic discipline over other considerations. Its authority is uniquely active: no other polity has comparable ongoing processes in which well-resourced agencies systematically target internal obstacles to cross-jurisdictional flows, nor does any other multi-tiered polity have comparable central processes to surveil and pressure units toward fiscal balance and structural reform. We are somewhat skeptical of Caporaso and Tarrow’s view that ECJ social policy jurisprudence runs against these priorities. As other scholars have argued, decisions like the portability of pensions have the intention and effect of preventing national social policies from disrupting interstate mobility, not of empowering governments to “embed” those flows.¹⁰² The social rights clauses of the EU treaties might yet provide bases for other developments, but in Höpner and Schäfer’s aptly phrased title, the substance of European rules is still “waiting for Polanyi in a Hayekian setting.”¹⁰³ Together

⁹⁹ Block 2008, 26.

¹⁰⁰ Van Apeldoorn 2009.

¹⁰¹ Caporaso and Tarrow 2009, at 598, 594; emphasis in original.

¹⁰² Höpner & Schäfer 2012; Mabbett 2014.

¹⁰³ Höpner & Schäfer 2012. More plausible, perhaps, is to see a Polanyian “second movement” in the rise of Eurosceptical nationalism (Hopkin 2017, 476). But this second movement too has yet to alter the EU order.

with our previous point that Höpner and Schäfer miss how much that Hayekian setting relies on un-Hayekian central authority, we conclude that the EU today is best characterized by a mix of these labels. There are Polanyian muscles behind Hayekian Brussels.¹⁰⁴

2.3. *An Ordo-Liberal EU?*

The notion that the EU order combines muscular central authority with Hayekian goals will evoke another label for political economists: “ordo-liberal.” This German tradition, defined by “Freiburg School” economists like Walter Eucken and legal scholars like Franz Böhm (with overlapping “Austrian School” economists like Wilhelm Röpke), differs from Hayekian-American neoliberalism in advocating a stronger state framework around markets. Especially since the Eurozone’s debt crisis, a wave of scholarship describes the EU as ordo-liberal.¹⁰⁵

Ordo-liberalism’s principles certainly seem to fit EU authority. Ordo-liberal theory departed from concerns in Weimar Germany that markets are most threatened by cartels, monopolies, and “rent-seeking capitalists.”¹⁰⁶ This focus made early ordo-liberals less worried about central state power than Hayek and his descendants. As one German economist summarizes: “Hayek... emphasized the threat to the free market system emanating above all from the state’s attempt to steer a purpose-free, self-organizing, and complex order of actions, whereas ordo-liberals stressed that economic freedom is mainly endangered from within, by economic power groups facing a ‘weak’ state that is unable to protect and enforce the competitive order.”¹⁰⁷ Eucken’s “first principle” was, “The policy of the state should be directed at the dissolution of economic power groups or at limiting their functions.”¹⁰⁸ Indeed, early ordo-liberals championed state action to foster markets so strongly that they sometimes equated their own interventionism to socialism, just with different goals.¹⁰⁹ They favored “market-conforming” intervention to set background conditions for private exchange, opposing “non-conform” actions to steer or cushion market mechanisms. In market regulation, ordo-liberals focused above all on robust competition policy, while also recommending that all regulations and taxes be

¹⁰⁴ For related general discussions of Polanyi and Hayek that suggest that Hayekian orders could only come about through Polanyian dynamics, see Cahill 2018 and Mirowski 2018.

¹⁰⁵ Moss 2000; Dullien & Guérot 2012; Dale & El-Enany 2013; Somma 2013; Biebricher 2014; Jacoby 2014; Young 2014; Siems & Schnyder 2014; Matthijs & McNamara 2015; Matthijs 2016; Schäfer 2016.

¹⁰⁶ Dyson 2017, Kindle location 2897.

¹⁰⁷ Wolgemuth 2013, 160.

¹⁰⁸ Eucken 1952, 334; see Streit & Wolgemuth 2000, 254.

¹⁰⁹ Siems & Schnyder 2014, 380, in particular citing Miksch 1949, 327. See also Bilger 1964.

“systematically checked as to whether they tend to promote or to inhibit a well-functioning competitive order.”¹¹⁰ In macro-economic terms, Eucken called for an “economic constitution” with the first goal of upholding “the functioning of the price system,” a second goal of assuring price stability, and an emphasis on clear (never joint) liability.¹¹¹ Monetary policy should aspire to “rational automatism,” with minimal policy discretion within a framework of explicit rules.¹¹²

Many scholars perceive this doctrine at work in the EU today. Pierre Dardot and Christian Laval find ordo-liberalism in the EEC treaty, arguing that “Ordo-liberalism provided the basics of the doctrinal foundation of current European construction...”¹¹³ Some specialists on EU competition policy stress ordo-liberal inspirations.¹¹⁴ Christopher Allen traces the EMU deal to ordo-liberal principles, and Sebastien Dullien and Ulrike Guérot describe a “long shadow of ordo-liberalism” over European (and especially German) responses to the debt crisis.¹¹⁵ Most famously, Mark Blyth sees an “ordoliberalization of Europe” in the past decade as a German-dominated EU imposed austerity and oversight on its southern members.¹¹⁶

We agree with a core thrust of this scholarship: the outcome of EU economic authority today better matches the principles of ordo-liberalism than any other school of political economy. Like with our previous discussion of Hayekians, however, this observation confronts a simple problem: ordo-liberals today are not happy with the EU. Though their emphasis on central authority places them closer to the EU outcome than Hayekians, many ordo-liberals have been uncomfortable with the EU since its origins, and their discomfort seems only to have grown. At the beginnings, Röpcke and many figures in the German Economics Ministry opposed the EEC as likely to be overly interventionist.¹¹⁷ For similar reasons German Economics Minister and ordo-liberal “fellow traveler” Ludwig Erhard was publicly opposed to the early EEC negotiations.¹¹⁸ Later ordo-liberals approved of the “Single Market 1992” program, but the Maastricht deal on a single currency was “highly controversial” among German economists.¹¹⁹

¹¹⁰ Vanberg 1988, 20.

¹¹¹ Eucken, Grundsätze, p. 14. The second goal was called “the primary of currency policy,” but he meant price stability. See Feld et al, 2015, 58.

¹¹² For a discussion, see White 2017.

¹¹³ Dardot and Laval 2013, 194.

¹¹⁴ Gerber 1998; Buxbaum 2006; Ryner 2015.

¹¹⁵ Allen 2000; Dullien and Guérot 2012.

¹¹⁶ Blyth 2013, 142.

¹¹⁷ Van der Groeben 1988, 48; Abelshauser 2016.

¹¹⁸ Lee 1995.

¹¹⁹ Hein & Joerges 2018, 15; see also Majone 2014, 151.

During EU responses to the euro crisis, prominent figures associated with ordo-liberalism resigned from the Bundesbank and the ECB, while an economics professor founded the anti-euro political party *Alternative für Deutschland*.¹²⁰ Overall, writes one specialist, ordo-liberalism has become “increasingly unrecognizable” in the EU.¹²¹

Two points about ordo-liberalism square these observations and further specify our description of the EU outcome. First, ordo-liberalism itself evolved over time to be more critical of central authority. Eucken, its central figure, died unexpectedly in 1950. In 1962, Hayek moved from Chicago to Freiburg, and his developing ideas on “discovery procedures” mixed into ordo-liberal thinking through economists like Erich Hoppmann and Ernst-Joachim Mestmäcker.¹²² In the 1980s and 1990s Viktor Vanberg led an importation of Buchanan’s constitutional economics into Germany, effectively arguing that American “competitive federalism” was what ordo-liberalism’s founders meant all along.¹²³ The turn of the millennium confirmed “the disintegration of ordo-liberalism in economic science,” as American-style formal theorists won an explicit battle with the vestiges of *Ordnungsökonomik* in German universities.¹²⁴ In parallel to this mixing of German economists’ views with Hayekian themes, German economic policies also became less distinctive. Kenneth Dyson and Brigitte Young argue that German monetary policy from the 1970s onwards was more Chicago-School than ordo-liberal (“Milton Friedman trumped Eucken”¹²⁵), and that neither the logic of the EMU deal nor many German economists’ concerns about it were distinctively ordo-liberal. They “owed more to the New Institutional Economics taught at virtually all Anglo-Saxon economic departments as well as prominent economics and business school studies curricula in Europe.”¹²⁶ In sum, some of ordo-liberals’ recent discomfort with the EU traces back to their Hayekian turn.

The deeper reason behind ordo-liberals’ unease with the EU is that their founders never clearly intended their ideas to apply far beyond their German context. They formulated their model of background economic rules within a centralized federation with a unitary political culture and routine federal commandeering of the states. The *Länder* had limited fiscal autonomy

¹²⁰ Jacoby 2014; Grimm 2015;

¹²¹ Biebricher 2017 (Kindle location 3187).

¹²² Dyson 2017.

¹²³ Ibid; Vanberg 1988, 1994; see also Grosskettler 1994; Streit & Wolgemuth 2000, 258.

¹²⁴ Hien and Joerges 2018, 17.

¹²⁵ Dyson 2017, Kindle location 3009.

¹²⁶ Young 2017, Kindle location 3836.

and decreasing inclination since the 19th century to develop distinct regulations. Low state-level variation made it relatively easy to imagine an automatic role for federal rules that required little active management or discretion. Thus ordo-liberals never developed clear views about what exactly the federation would need to do to discipline heterogeneous units. There are no real parallels in German jurisprudence to American fights over the Commerce Clause or ECJ decisions on the Single Market, and no perceived need in the 20th century for anything like a German “Single Market project.”¹²⁷ Nor has Vanberg’s introduction of “competitive federalism” in economic discussions had much impact on discussions of German federalism, because there simply is not enough policy variation among the *Länder* for this model to resonate strongly. Furthermore, the German experience with reunification underlined the incompatibility of a pure ordo-liberalism in an economy not already long attuned to these practices.¹²⁸

The main source of ordo-liberal unhappiness with the EU is that extending their model even further, i.e. across a heterogeneous continent, predictably creates opportunities or pressures for the active governance that they aspire to eliminate. One ordo-liberal concern has been the political problem that European institutions could offer opportunities to non-Germans to pull Europe away from pro-market commitments. This was Röpcke and Erhard’s worry about the EEC: even if the treaty enshrined pro-market principles, the French in particular might steer it in market-mitigating directions.¹²⁹ But the deeper conundrum for ordo-liberals, in our view, has been that extending ordo-liberal goals across Europe constantly raised complex questions about what the EU should require of its increasingly heterogeneous membership. In the Single Market, strong legal commitments to openness produced a far more active and ongoing regulatory project to root out barriers and harmonize differences than ordo-liberal theories ever pictured. It also invited calls for market-mitigating side payments that ordo-liberals disliked, like in the EU’s regional development funds. In the Eurozone, advocates of market discipline hoped to force member states to align on background rules with the Maastricht convergence criteria, ban on bailouts, and Stability Pact. Instead EMU actually worsened certain national divergences and eventually produced a crisis that opened the door to more active European governance in the

¹²⁷ For an English-language overview, consider Kommers 1997, 61-96.

¹²⁸ Jeffrey et al 2016, 171.

¹²⁹ The French indeed attempted this across EU history, though the outcome makes clear that they had little success altering the EU’s core commitments.

form of bailouts, monetary financing, and fiscal and regulatory oversight. As Hien and Joerges put it, “Not only von Hayek, but also Walter Eucken would be horrified.”¹³⁰

In sum, recent EU changes indeed make sense as an “ordoliberalization of Europe,” but not as an intentional plan orchestrated by ordo-liberals from the very beginning. These Polanyian muscles in Hayekian Brussels can also be described as “ordo-liberalism on steroids.” Healthy, disciplined ordo-liberals would never advocate taking steroids, of course, and they never envisioned the bulking-up of central economic authority that the EU has developed in extending ordo-liberal-style goals across 28 countries. These descriptive points hint that we must look beyond German hegemony, and beyond the intentionality of any configuration of powerful actors, to explain this EU outcome.

3. Implications for Explanatory Debates

We have argued descriptively that EU authority over state-level market regulation and state-level fiscal policies exceeds that of many national federations, but also the recommendations of pro-market Hayekian or ordo-liberal theorists. What scholars care about most, though, is how such a description influences theoretical explanations of these outcomes.

Should we question whether these rules really matter on the ground? We see little room to debate their basic importance. That is not to say that they are seamlessly applied and enforced.¹³¹ Far from it: the EU certainly applies its rules in selective ways that reflect variations in state-level support or resistance. It probably does so more than national federations, given its very limited fiscal resources and personnel for direct enforcement. In the Single Market, both legislation and administrative action have focused the principles of *Dassonville* or *Gebhard* on certain national regulations while leaving others partly or fully untouched.¹³² The same is true of fiscal enforcement in the Eurozone. For example, tough treatment of Greece and even Italy seems to contrast to careful recent handling of France. The Commission’s November 2018 assessment already found the French budget “at risk of non-compliance,” before the “Yellow Jacket” uprising extracted promises from Macron that swelled projected deficits from 2.8 to 3.4

¹³⁰ Hien & Joerges 2018, 99.

¹³¹ See Kelemen 2006, Börzel 2001

¹³² Cites on enforcement.

per cent of GDP. The Commission has muted its criticism, saying these developments would be evaluated in the normal process in May 2019. Still, some variation in the application of EU rules does not plausibly imply that the core principles in the Single Market and Eurozone do not matter. Just as American actors would be puzzled at questions about whether interpretations of the Commerce Clause are important, or as Canadian actors saw high stakes in the “Free the Beer” case, so it is in the EU. Anyone who suggested to businesses or national courts that the *Dassonville* or *Gebhard* jurisprudence can be ignored, or to Macron’s team that Eurozone rules pose them no problems, would be laughed out of the room.

Thus IR theory must come to grips with explaining these EU rules. This last section considers explanatory implications of our redescription. Debates about explaining the EU comprise one of the best-developed areas in IO scholarship. Rich variants of broader IR theoretical approaches compete to explain the same empirics. Our dense descriptive work leaves insufficient space to fully engage these debates, but we suggest elements of a theoretical approach that seems like it *could* explain why Europe’s remarkable authority arose. We briefly highlight that our redescription seems to pose challenges to leading IR theories, and then note that this outcome seems to hint at an explanation involving deeply contextual and endogenous political dynamics and a sequence of powerful unintended consequences. Again, these are just apparent hints from the outcome about what *could* have led to it. We look forward to concrete debates about what actually *did*.

3.1 Classic IR Theories and the EU Outcome

Why would European states build such strong EU economic authority? Two schools have long dominated theories of international regimes and are prominent in recent scholarship on the EU. Liberal theories, represented in EU debates by “liberal intergovernmentalist” theory (LI), explain international rules as tools to capture policy gains under conditions of interdependence.¹³³ Realist approaches, which gained new prominence as reunified Germany occupied Europe’s center stage, explain them as tools of regional hegemony.¹³⁴ At first glance, at least, both struggle with the EU outcome.

¹³³Keohane, Young, Milner, Martin, Simmons, Moravcsik 1998.

¹³⁴Cites.

The dominant strand of regime theory since the 1970s is liberal. LI's creator, Andrew Moravcsik, has been very influential in EU studies, and recently defended LI as the “essential baseline” for explaining the EU. He theorizes it as a normal regime that states constructed to capture policy gains for their dominant interest groups. European states saw interests in unusually strong central institutions because they experience unusual levels of economic interdependence. Thus the EU showcases “the only sensible way to manage concrete interdependence.”¹³⁵ Moravcsik also holds that the EU outcome is “carefully calibrated in its authority” to achieve concrete, issue-specific policy goals.¹³⁶

When we compare EU Single Market authority to that of Anglo-Saxon federations, however, this explanation looks unpromising. “Concrete interdependence” is far higher in national federations, especially the United States. Interstate trade is roughly 40% of US GDP, versus about 20% of EU GDP.¹³⁷ US interstate mobility is roughly *twenty times* that in the EU.¹³⁸ Large-scale businesses dominate the US economy far more than the EU.¹³⁹ US states have more specialized (and thus more interdependent) economies than EU member-states.¹⁴⁰ If Americans exchange and move far more across their states, this theory seems to predict that the US should see far more mobilization than the EU to demand credible institutional commitments—delegations of authority—to facilitate such exchange, like empowering central action against interstate barriers or reducing regulatory fragmentation. That is not the case.

As for Eurozone rules, Moravcsik allows that LI cannot explain them. In the 1990s he argued that the “issue-specific” payoffs that European business and governments sought in creating the euro were lower interest rates for weaker-currency countries (led by France) and a lower exchange rate for stronger ones (led by Germany).¹⁴¹ Questions surrounded this explanation from the start,¹⁴² but even Moravcsik does not extend it to the later development of Eurozone rules. He recently characterized the Eurozone's evolution as an exception to LI that

¹³⁵ Moravcsik 2018, 23.

¹³⁶ Moravcsik 2018, 7, 23.

¹³⁷ Pacchioli 2011.

¹³⁸ Bonin et al 2008; Kaplan & Woll 2015.

¹³⁹ European Commission 2016.

¹⁴⁰ ECB 2004.

¹⁴¹ Moravcsik 1998, 379-471.

¹⁴² For example, if a “decisive majority” of business groups in France and Germany wanted these policy goals (Moravcsik 1998, 381), why could the French not discipline their own monetary policy, or the Germans weaken their own currency, without subjecting themselves to binding new European institutions?

reflects institutional path dependence: “Today it is hard to find a state that would enter EMU again if it had a time machine and could relive the choice...”¹⁴³ We can only concur. It is difficult to even brainstorm an account that would begin from the pursuit of French and German business interests and predict, without major unintended consequences, the emergence of European rules wherein both France and Germany abjure national monetary flexibility, subject their own budgets to permanent oversight, and take responsibility for bailouts of other countries.

The other classic approach to international regimes and organizations is realist. International rules reflect the interests of regional hegemon. They design rules to pursue their national goals and capture broad gains from regional stability. Since the mid-2000s, when Germany emerged from challenges partly related to its reunification, most observers see it as clear *prima inter pares* in the EU. As we have seen, the “ordoliberalization of Europe” has tempted scholars to describe EU developments as Germany-driven.

As we have also already seen, a German-hegemony explanation stumbles over German doubts about EU deals. German leaders only grudgingly accepted Eurozone bailouts and ECB actions. They succeeded more at setting conditions on Eurozone crisis response than at defining its direction. Backing up to earlier steps, all accounts of the Maastricht deal on EMU agree that it was extracted from (not demanded by) Germany.¹⁴⁴ All accounts of the Single European Act (SEA) agree that Germans largely welcomed it but were relatively passive in its negotiation.¹⁴⁵ In the run-up to the SEA, though, German officials led the opposition to its expansion of “mutual recognition” principles, which they feared would undercut German standards.¹⁴⁶ (Germany still has such concerns: in 2018 it was the target of more EU infringement proceedings than any other country.¹⁴⁷) All accounts of the EEC agree that German positions favored a less supranational, geographically broader free trade area.¹⁴⁸ At each step the German government has been central and powerful, setting conditions on deals, but at no major stage in the EU’s construction has it played the role of lead proposer or *demandeur*. This does not look much like hegemony.

Once again, these are broad initial observations, not serious tests of these rich theories.

¹⁴³ Ibid, 20. This is similar to Jones, Kelemen & Meunier 2015.

¹⁴⁴ Cites.

¹⁴⁵ Cites.

¹⁴⁶ Alter & Meunier-Altsahalia 1998.

¹⁴⁷ <https://www.handelsblatt.com/today/politics/papa-dont-preach-germany-is-the-leading-breaker-of-eu-rules/23581000.html?ticket=ST-1165161-sPMcfgXabNp9HT9ycTfv-ap4>.

¹⁴⁸ Cites.

Careful theorizing and closer empirical investigation might support counterintuitive accounts rooted in these traditions. We simply mean to suggest that in light of our description, they definitely look counterintuitive. It seems like other theoretical explanations might make better sense of the outcome.

3.2 Turning to More Contextual and Endogenous Interests

When we set the EU alongside national federations, we see striking variation in the kinds of policy autonomy that state-level actors think they can or should defend. Behavior from one arena seems hard to imagine elsewhere: consider the American “feds” vetoing Florida’s budget, compelling New York to admit New Jersey lawyers, or requiring US states to tender public contracts through a central procurement system. In principle such variation may just reflect complex differences in which underlying interests are present or dominant in these arenas, but again, that looks counterintuitive as a point of departure. These cases look more like contexts in which interests are differently understood, or at least very differently prioritized.

Such variation seems to favor theories that portray interests as substantially endogenous to context. This is the realm of institutionalist and ideational theorizing. Rather than tracing interests to an exogenously-given landscape—as liberal theorizing does to economic conditions or societal pluralism, and realist theories does to a distribution of power—institutionalist and ideational theories hypothesize that people develop their interests as they build political contexts around themselves. Institutional theories emphasize that as people craft certain rules and organizations to solve certain problems, they generate constraints and capabilities that feed back on their possibilities and priorities for action down the line. Ideational theories emphasize that people construct context-specific interpretations of their interests in the form of norms, ideas, identities, practices, and discourse.¹⁴⁹

These theoretical traditions have become increasingly prominent in EU debates and IR more generally as alternatives to classic exogenous-interest theories. At the origins of the EU project, Ernst Haas’s “neofunctionalist” theory suggested an endogenous institutionalist logic of “political spillover”: initial delegations of authority to Europe’s supranational agents would allow them to build support for more delegations of power later on. This dynamic was often

¹⁴⁹ Note on use of ‘institutionalist.’

subordinated to neofunctionalism's other emphases on technocratic functionalism and liberal interest-group pluralism,¹⁵⁰ but more coherently endogenous theorizing of European integration arose as neofunctionalism merged into the "new institutionalism" of the 1990s. Scholars like Wayne Sandholtz, Alec Stone-Sweet, Liesbet Hooghe, Gary Marks, and Paul Pierson drew on institutionalist concepts from comparative politics to reconceive political spillover as an instance of the institutional path dependence that they saw as common in domestic arenas. Within heavily institutionalized polities, complex policy problems and conflicts among boundedly-rational actors lead rules and organizations to evolve with many unforeseen consequences over time. Actors' concerns, priorities and strategies co-evolve with the institutional game around them. These theorists saw similar things happening in the EC (as it was called then). Drawing parallels to unintended trajectories of American and Canadian federalism, Pierson called for "...thinking of the EC, not as an international organization, but as the central level—albeit still a weak one—of an emergent multitiered system of governance."¹⁵¹

Attention to endogeneity and contextualized interests has strengthened in EU scholarship since then. After the SEA and Maastricht, scholars began describing the EU as a "multi-level government,"¹⁵² comparing it to national federations,¹⁵³ studying its feedback into national politics under the rubric of "Europeanization,"¹⁵⁴ and debating the quality of its democratic legitimacy relative to national models.¹⁵⁵ Most of this literature was couched in institutionalist concepts from comparative politics, but ideational approaches developed too. They portrayed the euro deal as rooted in a context of monetarist ideas,¹⁵⁶ national bargaining within EU institutions as channeled endogenously by socialization,¹⁵⁷ support for the Single Market and monetary integration as assembled by Commission discourse,¹⁵⁸ and even the whole EU story as a process by which institutional rules "bound all Europeans into a certain ideological agenda."¹⁵⁹

¹⁵⁰ See Burley & Mattli; Parsons 2000.

¹⁵¹ Pierson 1996, 158.

¹⁵² Cite

¹⁵³ Most importantly, Kelemen...

¹⁵⁴ Cite

¹⁵⁵ Cite

¹⁵⁶ McNamara 1998.

¹⁵⁷ Lewis 2005.

¹⁵⁸ Jabko 2006.

¹⁵⁹ Parsons 2003, 7.

One school occupies the center of such endogenous-interest theorizing and has attracted broad attention in IR recently: historical institutionalism (HI). As scholars like Henry Farrell, Abraham Newman, Orfeo Fioretos, Tim Büthe, and Thomas Rixen have introduced in general IR-focused statements, historical institutionalism explores how “state institutions and social preferences are implicated in each other, and how feedbacks from the state shape the preferences of social actors.”¹⁶⁰ Such feedback can be profound, writes Büthe, such that it “might over time not only change how actors pursue their goals but also might change their interests or even constitute new actors.”¹⁶¹ The core of most HI theorizing is organizational, not ideational—positing that rules and organizations built to solve certain problems at time t alter the costs and benefits of strategic choices at time $t+1$. It tends to feature rules and organizations that channel mostly-rational actors in certain directions, rather than directly altering how actors interpret things ideationally. Yet as Büthe’s phrasing suggests, HI posits that over time, organizational channeling can shape action profoundly enough to affect basic interests and the configuration of actors. This hypothesis of deep endogeneity is why many HI theorists are also open to combining organizational path dependence with attention to ideas. They do not expect actors’ expressed interests to map closely onto general exogenous conditions (like economic interdependence or a geopolitical distribution of power), nor do they think it promising to bypass theorizing interests with an agnostic societal pluralism. They advise us to provide direct empirical accounts of how interests came to be expressed as they are, and generally expect that evolving organizational constraints and possibly contextual ideas will be necessary to such accounts.

Our redescription of the EU outcome seems to call for such an analysis. It displays institutional outcomes that look counterintuitive relative to common theories of exogenous interests. That so many actors are uncomfortable with the outcome—including central and powerful ones—seems to hint at substantial unintended consequences. Our final section sketches a stylized explanation of Europe’s “ordoliberalism on steroids” that might fit the bill.

3.3. A Stylized Explanation of Europe’s Economic Authority

¹⁶⁰ Farrell & Newman 2010, 619; Fioretos 2011, 2017; Büthe 2016; Rixen, Viola & Zürn 2016; Fioretos, Falletti & Sheingate 2016. For key statements outside IR, Pierson 2004, Streeck and Thelen 2005; Capoccia & Kelemen 2007; Thelen & Mahoney 2010.

¹⁶¹ Büthe 2016, 41.

Beyond the broad notion that Europe's overall outcome of "ordo-liberalism on steroids" seems to call for some sort of endogenous-interest explanation, three aspects of our description suggest elements of a plausible explanation. First, while Europe's Single Market authority has taken decades to reach its current levels of specification and enforcement, its strong principles were partly present in the original EEC text. That fact, we think, hints at ideational dynamics at the system's origins. Second, both the Single Market and Eurozone ended up with an ordo-liberal-like combination of market discipline and strong central authority despite long-running ordo-liberal doubts about this project. That fact, we think, hints that Europe's marriage of markets and authority reflects bargaining between diverse agendas more than coherent intentionality. Third, the greatest expansions of EU authority and most expression of discomfort with it occurred as the EU enlarged to more diverse membership. That fact, we think, hints at unintended consequences across a sequence of EU bargains. EU principles defined mainly among early members brought new demands and opportunities for expanded authority when extended across the continent. Together these points sketch an HI-style account in which actors with a variety of agendas struck a series of institutional bargains, each of which affected subsequent interaction in unintended ways.

Future versions of this paper will flesh out this account, but for now a stylized version will have to do. Its first element is to posit that national governments' positions across the construction of the EU have at least been heavily tinged by ideational commitments, not just interest-group demands or jockeying for regional influence. Two kinds of ideas seem critical to the story:

- **Europeanism.** Our comparison highlights that the original EEC treaty had extraordinarily strong principles written into it regarding openness and free movement—but mainly as a vehicle for Europeanist goals of "integration," not as a conscious tool for Hayekian elimination of lower-level regulation. Though the treaty's key clauses on the "four freedoms" were indeed drafted by German ordo-liberals—Hans von der Groeben and Alfred Müller-Armack—most of the treaty's key supporters at the time stood out for Europeanist commitments rather than their ordo-liberal ones. Indeed, most early neoliberals opposed the EEC, interpreting its supranational institutions as compromises

with French *dirigisme*.¹⁶² They implicitly agreed with its many socialist supporters, who hoped it would support regulatory coordination.¹⁶³ Thus the EEC member-states endorsed legal foundations that could later become ordo-liberal without most actors desiring or expecting that outcome.

- **Distinctive ‘Nationally Embedded’ Traditions of Political Economy.** A massive literature characterizes the French as enduringly leaning toward forms of statist dirigisme and more voluntaristic, pro-growth economic policy; the British leaning toward classic liberalism, and later Hayekian thinking; and the Germans approaching most economic questions through the frame of ordo-liberalism, which can be roughly understood as combining elements of the other two positions. This basic configuration of national economic traditions put German-style positions in the middle of the European economic bargaining space: more sympathetic to liberalization than the French but less than the British, and inclined to make the case for explicit centralized rules and “market-making” efforts that the British were (sometimes) willing to accept as tolerably pro-market and the French were (sometimes) willing to accept as tolerably amenable to central steering.¹⁶⁴

With these ideational commitments informing what the most powerful governments understood as their interests in European economic integration, a sequence of interstate bargains translated these national positions into the EU outcome over time. After the founding moment of the EEC deal, we see two bargaining threads intertwining into that path-dependent sequence.

The first thread consists of bargains between the earlier EU members in northwestern Europe to define the core nature and scope of European economic authority. It featured two key steps, centering on the “Single Market 1992” deal in the Single European Act and the single-currency deal in the Maastricht Treaty. Prior to the mid-1980s, the potentially ordo-liberal principles of the EEC treaty had been robustly elaborated in the jurisprudence of the European Court of Justice, but political support for legislating, implementing, and enforcing those

¹⁶² Slobodian, 2018, 184-202.

¹⁶³ Shaev, 2018.

¹⁶⁴ In our view French leaders have repeatedly overestimated their own ability to then steer the resultant central economic authority, which helps explain why they agreed to such strong rules for openness and discipline, but that is another story.

principles was ambiguous. As many accounts narrate, the 1980s then saw a new European bargain come together to endorse deeper liberalization and European authority to enact it.¹⁶⁵ All accounts agree that the British under Prime Minister Margaret Thatcher were most enthusiastic about liberalization, that the French under President François Mitterrand were most enthusiastic about empowering the EEC institutions but lukewarm about liberalization, and that the Germans under Helmut Kohl were less aggressively interested in either theme but open to both. As one of us has argued,¹⁶⁶ most existing accounts exaggerate the extent to which the bargain came together because the British or the French altered their initial positions, being ostensibly persuaded either by structural imperatives or by Commission persuasion that both strong liberalization and more EEC authority (most notably the effective endorsement and extension of majority voting on internal-market issues). Instead, the French and British positions remained quite divergent, but they struck a bargain. Thatcher agreed to accept institutional reforms she was never persuaded were desirable. She said so consistently before, during, and after the SEA negotiations, with the exception of some light rhetorical adjustment in her published memoirs.¹⁶⁷ Mitterrand and his Socialist government agreed to accept more liberalization than they thought was desirable in order to achieve institutional reform.¹⁶⁸ The Germans (like the Dutch) had long been broadly supportive of both further steps on the internal market and more robust EEC authority, and went along with this deal relatively comfortably. Therefore, the ordo-liberal-style leanings of the EEC treaty and jurisprudence were strongly upgraded in the “Single Market 1992” plan, *without* German ordo-liberal-style actors doing much to push that development.

The second major intra-northwestern-European bargain that defined today’s European economic authority came with the deal for a single currency. Here the initial positions of the three most powerful governments related to their positions in the SEA negotiations. Even though the French had substantially converged on monetarist, neoliberal-style policies by the late 1980s,¹⁶⁹ their main concerns in the process leading to the EMU bargain were again relatively dirigiste: they wanted to regain a directive voice over monetary policy that they felt they had lost due to the logic of asymmetric adjustments to currency fluctuations in the European Monetary

¹⁶⁵ Sandholtz and Zysman 1989; Moravcsik 1991; add others.

¹⁶⁶ Parsons 2010.

¹⁶⁷ Parsons 2022.

¹⁶⁸ Parsons 2010.

¹⁶⁹ McNamara, 1998.

System, and if possible to set up a more voluntaristic “economic government” alongside a single currency.¹⁷⁰ The British, meanwhile, were again skeptical of any centralization of authority and argued halfheartedly for the Hayekian regulatory-competition option of issuing a “common currency” alongside national ones (before they eventually decided to opt out of the deal). The dominant German position on the monetary-policy issues was also decidedly skeptical about the economic value of a single currency and clearly opposed to French hopes for an “economic government,” which makes sense especially given what we noted earlier: the main strands of German monetary thought had moved by this point away from distinctive ordo-liberalism toward a more Chicago-school neoliberalism.¹⁷¹ Still, German economic views remained more ordo-leaning and favorable to centralized options than those of the British, as we can see in the fact that German officials broadly dismissed the decentralized “common currency” as unworkable.

Relatively concrete discussions on the road to EMU began in 1987 when the French proposed to discuss new monetary steps in a committee of national economic advisors under the chairmanship of Commission President Delors. While Kohl supported Delors’ chairmanship, over Thatcher’s protests, the Germans allied with the British to insist that the committee be composed of central bankers, who were generally opposed to single-currency plans. Cleverly, however, Delors steered the committee to consider under what conditions and arrangements a monetary union might be feasible, not whether they actually recommended a single currency. Within this framework, the British and German central bankers ended up supporting Delors’ proposals for a three-stage process to full EMU for tactical reasons. They believed that they could parry French suggestions for moving first toward broad economic coordination by endorsing gradual steps, conditional on national-level economic convergence, toward an ultra-independent, inflation-fighting European bank. There is no question that most German policymakers still saw the resultant basic plan as economically undesirable, mainly because they feared that even the most independent, disciplining European system would fall prey to the French government’s unmistakable hopes to steer it in more pro-growth directions and to political pressures to let in non-convergent southern Europeans and bail them out down the line. But to make a long story short, Helmut Kohl eventually overruled his economic policymakers to make the political choice in favor of Delors’ EMU plan, apparently mainly out of his personal

¹⁷⁰ Sandholtz, 1993; Jabko, 1999.

¹⁷¹ Dyson 2017, Young 2017.

Europeanist commitments.¹⁷² Mitterrand did the same on the French side, overruling bitter opposition from some of his closest allies (most notably his Socialist Finance Minister and then Prime Minister Pierre Bérégovoy) who argued that this deal left no real prospects for pro-growth policies or an economic government. Thus the Europeanist commitments of top leaders bridged a gap between different national political-economic traditions. The bargain pulled the French into a more disciplining arrangement than they generally preferred, but also effectively pulled the Germans away from their increasingly Anglicized neoliberalism toward a more centralized ordo-liberal-style framework.

This thread of intra-northern-European bargaining over economic authority continued after Maastricht, spinning out its logic in tussles over the Stability and Growth Pact in the 1990s and thereafter, but at this point the nature and scope of today's EU economic authority was clearly visible. It was tasked with a never-ending effort to implement stronger requirements for single-market openness than exist within any national federation, and with monetary authority explicitly designed to be highly autonomous and disciplinary.

Crucially for our analysis, this bargaining thread then increasingly interacted with another: bargains to extend membership in the EU project across a much more diverse set of countries. The intersection of these threads greatly ramped up the central authority already built into the EU's rules in ways that seemed quite ordo-liberal and felt increasingly uncomfortable to actors with ordo-liberal-style ideological sympathies. The conscious ideological ordo-liberalism of mid-20th century Germans had been conceived within the homogeneous context of German federalism, where pro-market, non-discretionary, non-interventionist governance could plausibly be achieved mainly just by tying the polity to a central mast of background commitments. The unintended, bargained-out, institutional ordo-liberalism of the EU arena attempted to apply similar market-building goals across a radically more heterogeneous space. The attempt to extend roughly ordo-liberal principles across a diverse Europe generated national demands and supranational opportunities for a much more active central role, drawing the EU into projects of remaking national political economies in a far more interventionist way than actual ordo-liberals had ever envisioned. The more diverse and less liberal polities are included in a space governed by ordo-liberal-style principles, the more it can be argued that central authority must identify and

¹⁷² Heisenberg 1999.

address subunit features that impede market principles—and the more that process elicits political compromises and opportunities to develop decidedly non-ordo-style support rather than discipline.

One realm in which these dynamics have been visible since the Greek and Iberian enlargement is the expansion of the Structural Funds. The original European Regional Development Fund emerged in the 1970s mainly as a side payment to the newly entered UK, which objected that it benefited little from an EEC budget centered on agricultural subsidies and asked for a new funding stream that could be steered at least partly toward redevelopment in deindustrialized cities. After the enlargements of the 1980s, and especially after the push to the “Single Market 1992” program, the new southern entrants insisted that they needed more development-style funding support to handle a deepening level of openness to richer-country competition. The richer members agreed roughly to a doubling of the Structural Funds in the late 1980s and another doubling in the early 1990s—but on condition that oversight of these funds also be ramped up, with the richer members effectively arguing that the Commission had to be empowered to track how their money was spent in southern Europe. This had a side effect of increasing Commission oversight of Structural Fund spending in the rich countries as well, whether in northern England or eastern Germany.¹⁷³ These same dynamics continued to play out through the long-developing eastern enlargement.

Far more important are the broadly similar dynamics showcased in the development of the Eurozone. Again, the Germans did not actually want the euro for economic goals, but given a political decision to achieve it, they could only accept the euro while demanding fiscal discipline from other countries. Though able to stipulate these conditions in the EMU deal, later flanked by the SGP, political pressure began right away for the exceptions to these arrangements that ordo-liberals feared. While enormous disciplinary fiscal pressure was indeed exerted on Italy and Greece as conditions for joining the launch of the euro, political compromises were also made on the convergence criteria (as well as for some states further north like Belgium). As a by-product of these interactions, Germany itself was subjected to fiscal oversight that became uncomfortable in the wake of the massive costs of German reunification, leading to the watering-down of the SGP in 2005.¹⁷⁴ Meanwhile, after what seemed like a mostly-successful launch of the euro in the

¹⁷³ Ansell, Darden and Parsons 1997.

¹⁷⁴ Matthijs and Blyth 2018.

early 2000s, ongoing asymmetries in member-state economies were exacerbated rather than mitigated by consequences of the new monetary regime—most notably the convergence of national borrowing costs despite enduringly different national conditions—such that the financial crisis of 2008-9 hit European states in hugely different ways. Germany and other rich northern member-states sought to defend the disciplinary regime in response, but eventually came to conclude that steps to bypass EMU’s “no bailout” logic were necessary to avoid an economic and political cataclysm. They could only extend such support if it came with a new regime for overseeing fiscality and structural reform in the receiving countries, however, generating a host of new arrangements including the “European Semester.” The receiving countries largely experienced this deal as leaning in ordo-liberal directions, with what they perceived as strict conditions and miserly support, and at the same time Germany and other richer members subjected their own budgets to annual approval by the European Commission.¹⁷⁵

There is much to add to this stylized account, but this is basically why the EU ended up with much more explicit and active economic authority than we see in German federalism itself. Ordo-liberalism on steroids arose without ordo-liberals strongly pushing for that outcome due to a sequence of interstate bargains that reshaped Europeans’ interests over time. Awkward deals between pro-market and institution-building agendas generated strong commitments to supranational economic authority, which the dominant members then found themselves enforcing across a far more diverse membership.

4. Conclusion: Europe’s Difficulties on the Hobbesian Frontier

Why has the European Union’s remarkable economic authority been so widely overlooked? Partly it is because these data points are simply difficult to put together. Descriptions and analyses of EU politics and law appear almost entirely in separate venues from discussions of American, Canadian, Australian, or even German federalism. Literatures on comparative federalism and law that unite them are still in relative infancy within small specialist circles.

There are reasons, however, why these data points are separated. The subfield of IR is premised on the notion that international relations is a distinct political space, deserving of its

¹⁷⁵ Matthijs 2016

own questions and theories. Its intellectual space is defined by the Hobbesian line between domestic order and international anarchy. This distinction made considerable sense in 1651 and still does today in many ways: it is a descriptive fact that modern IR generally lacks the claims to authority that frame domestic politics. Fortunately, the Hobbesian frontier has not always been an insuperable barrier to scholarly debates that range across it, especially in recent decades as theoretical approaches have followed the explosion of cross-border flows and international institutions. Nevertheless, it has clearly made it difficult for scholars to even characterize the EU outcome. Even though scholarship on European integration centered on questions about the extent of delegations of authority from states to central institutions—and even though the EU project, alone in modern history, loudly advertised an attempt to cross the Hobbesian frontier!—subfield divides have impeded comparison of the EU to national federations.

More importantly, the Hobbesian distinction shapes not just scholarship on the EU but politics around it. Citizens too learn the modern narratives that national governance is legitimate but international authority is suspect. Moreover, European citizens were not asked about most of the choices that carried their governance across this frontier. Even among elites, only a minority of Europhiles advocated that goal. And even within that elite subset, our observations here imply that even fewer (if any) would have consciously advocated a Europe with the kind of economic authority the EU developed. In other words, almost nobody clearly wanted this Europe. That is not necessarily analytically surprising or normatively damning in itself: American, Canadian, and Australian federalism all originated in complex compromises and have all evolved in ways unintended by their founders, without many clear moments where their citizens could check their trajectories. But the EU is the only polity that has followed such compromises and evolutions across the normative line of the Hobbesian frontier.

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