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Enlargement Ten Years on: New Europe's Contribution to Single Market

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Executive Summary

The mere prospect of the future membership of the Central and Eastern European countries in the EU internal market significantly increased the much-needed FDI inflow into this territory and this trend continued until the global recession of 2009. The EU internal market membership helped to reduce the risk premiums of investments in this region. The important condition for the enhanced FDI inflow consisted also in fact that the internal market rules on the prohibition of state aid did not prevent the governments in this region from further attracting the FDI inflow with generous incentives schemes even after the accession to the EU. This was due to the temporary derogations in the Accession Treaties and the subsequent lenient application of the exemptions from the state aid prohibition (the requests for incentives schemes exemption approval from this region were successful in 161 out of 180 cases).

The global recession of 2009 hit the Central and Eastern European countries particularly hard as their export-oriented economies become highly sensitive to external shocks. It resulted even in a temporary outflow of the FDI from the Central and Eastern European countries amounting to 1 % of the GDP. The membership in the EU internal market is however credited for preventing the global recession to have an even deeper impact, as most of the investments did not seek an early exit and stayed in the region.

The transitional restrictions on the access to the labour markets of the "old" EU15 member states in fact did not prevent significant migration inflows from the "new" EU member states. Their asymmetric application by certain "old" EU15 countries moreover resulted in artificial inputs to the migrants' decisions on where to move and thus prevented to reap the optimal results of human resources reallocation. The distorted migration inflows into the "old" EU15 countries resulted in case of the United Kingdom in an "enlargement fatigue" that nourish a spread of the current anti-immigration political sentiment.

The 2004 EU enlargement resulted in improved position in the wage level of the young workers (aged 35 and less) who stayed in their "new" EU home countries while their bargaining power rose with the rising possibility to migrate into the "old" EU15 countries. The biggest migration shock of young generation moving to the Western Europe, were witnessed in Lithuania (about 9% of the Lithuanian workforce) and Poland, Slovakia or Latvia (each about 6% of their respective workforce).

The studies show that migrants from the "new" EU member states were quite unlikely to represent a significant portion among welfare recipients in the "old" member states. The mostly young employment-seeking migrants from the East to the West thus was not as a threat to the existing welfare state systems of the "old" EU member states but a potential source for member states' welfare system sustainability.

The studies dealing with 10 years of the transitory provisions in Germany stress that immigrants on the German labour market and native Germans of the similar education and work experience are still largely non-substitutable. The incoming migrants compete primarily with the previous waves of immigration into Germany. The policy conclusion resulting from such studies is thus that the German transitory provisions did not help too much in protection of the German labour market but only diverted the needed young and well-educated portion of immigration from Germany to the United Kingdom; opening of the labour market from the beginning thus would have been a better policy choice.

The failure of the original Bolkestein's proposal for introduction of the country of origin principle into the EU service market can be connected with the fear in some of the "old" EU member states from the impact of the suspected increased heterogeneity of the level of service regulation within the EU after the 2004 enlargement. This was most likely further supported by the dislike of some of the "old" EU member states to open, through service liberalization, an alternative backdoor to their labour markets that were still protected during the post-enlargement transitional periods.

The adopted horizontally applicable directive on services in the internal market represent a set of "smart" tools to facilitate the free movement of services within the EU without the country of origin principle. Among those "smart" tools it is possible to include an approach of the directive that provides to the EU member states a possibility to introduce new regulatory provisions within the given flexibility discretion, which approach liberates them from the fear that an advanced liberalization in service sector would prevent them from reintroduction of regulation in case it is found necessary. It is suggested that a similar approach of flexibility may be used also in the other integration frozen areas that are claimed to enhance full operation of the EU internal market such as for instance the proposal of the Common Consolidated Corporate Tax Base.

1. Ten years of the New Europe in the Internal Market

The endeavour of the Western states that had been spurred by the Single European Act and resulted in a substantial move towards creation of the internal market culminated just at the time when the communist regimes in Central and Eastern Europe collapsed. The Maastricht Treaty shifted the European Union (EU) towards even higher levels of an economic integration including gradual introduction of the common currency. Given this increased speed of the European integration the invitation for the newly transforming countries of the Central and Eastern Europe was originally far from being certain.[1] Moreover, a recent study by Epstein & Jacoby (2014) claim that the decision to pursue the Eastern enlargement was not just about overcoming of four decades of different development under the communist regimes, but needed to face a deeper rooted East-West division dating to times when the geography destined the Eastern Europe to serve as a buffer zone from various invasions incoming from the further East. From this perspective the Eastern EU enlargement represents without hesitation an important historical break from the trends dating long into history. While authors as Epstein & Jacoby (2014) recognize that the membership in the EU and its internal market erased some of the previous asymmetries, they also recognize that certain new asymmetries have arisen including a deep economic dependence of the East on the West.[2]

The edifice of the EU internal market had been already highly developed in the time of the 2004 enlargement, but it was still far from being complete. For instance the area of the free movement of services has been significantly less functioning than the area of the free movement of goods. Moreover, the 2004 EU enlargement and later the 2007 enlargement did not lead to an entirely full participation of the newly acceding EU member states on the EU internal market, but this was distorted by several transitional periods and temporary derogations in the Accession Treaties. The later accession of certain states form the 2004 enlargement wave to the Eurozone (Slovenia 2007, Cyprus and Malta 2008, Slovakia 2009, Estonia 2011 and Latvia 2014) and the fiscal crisis in some of the "old" EU15 member states made the situation on the internal market even more complex and the simple clustering into the Eastern and the Western camp has became less relevant. The Eurozone crisis and various contemplated forms of reactions to it at the one hand distracted the focus on the further internal market liberalization and at the same time also revealed that certain developments of the internal market cannot yet be taken for granted.[3]

[1] In this concern and for deeper analysis of the political impulses for the enlargement see for instance Schimmelfennig (2001).
[2] Epstein & Jacoby (2014) p. 2.
[3] For a detailed overview of the threats of the Eurozone crisis for the internal market see Dullien (2012).

This paper is going to explore the development during the last ten years in the following three important areas of the EU internal market a) the role that the internal market has played in the FDI inflows into the newly acceding EU member states; b) the way how the transitional periods influenced the free movement of workers, and c) how the EU enlargement has influenced the development of the internal market in the area of the free movement of services.

2. The internal market and the needed FDI inflows to the Central and Eastern European countries

The FDI inflows until the global economic recession of 2009

Securing of the inflow of Foreign Direct Investments (FDI) into the transforming economies of the Central and Eastern European was the primary factor in stimulating their much needed technological and productivity growth. As it is stressed in a study by Medve-Bálint (2014) the Central and Eastern European countries were not successful in attracting FDI through most of the 1990s; while during the last six years prior the EU enlargement in 2004 their stock FDI more than tripled and this trend continued well through the first decade of the new millennia until the global recession of 2009.[4] This success was admirable even in the global dimension as the per capita FDI annual inflow into the Central and Eastern European countries at that time surpassed all other emerging markets including Brazil, Mexico or China.[5]

There are various perspectives of how to look at the role of the EU and its internal market in stimulation of this immense FDI inflow. Breuss (2002) expected increase of the FDI inflow in the "new" EU member states after acceding to the EU internal market and connected it primarily with more security for foreign investors resulting in "a reduction of the risk premiums".[6] The principle requiring the new EU member states to adopt the whole *acquis communautaire* and thus guaranteeing an investment-friendly and internationally comprehensible regulation on the whole range of issues ranging from free movement of capital (including dividend payments), to free movement of workers (including managers overseeing the investment in the host country) and free movement of goods (including

[4] Medve-Bálint (2014) p. 38.
[5] Ibid. p. 37 and 38.
[6] Breuss (2002) p. 255.

shipment of semi-finished products and parts allowing cross-border collaboration in a product manufacturing process).

Besides this Bandelj (2010) sees the role of the EU also in political terms and underlines the influence of the EU elites over the political leadership in the Central and Eastern European countries and their decision to focus on the FDI attraction.[7] Medve-Bálint (2014) further distinguishes two alternative ways of FDI inflows into the new EU member states. The first is an investment entry through privatization of the previously state-owned companies that primarily aimed at expansion targeted inside the Central and Eastern European regional markets.[8] The second is investment on a green field aimed primarily on development of a manufacturing base for mostly export-oriented production, in which case the investment is freer in choosing its targeted location and may select the most generous FDI incentives schemes provided at that time by the mutually forcefully competing Central and Eastern European countries.[9] While these incentives schemes would have been in general prohibited under the EU internal market rules on prohibition of the state aid,[10] most of the pre-accession awarded tax allowances and fiscal subsidies had been covered by temporary derogations in the Accession Treaties, which certain authors see more as a victory of the lobby of a narrow group of big multinational companies than as a real concession to the Central and Eastern European countries.[11] Any further investment incentives schemes had to be justified under the pertinent EU rules.[12] According to observations by Medve-Bálint (2014) the European Commission has scrutinized under Article 88 of the EC Treaty (later Article 108 of the TFEU) almost 180 state aid cases involving targeted subsidies or tax allowances offered by the Central and Eastern European countries and only in 19 cases the result was not a provision of a state aid exception.[13] The author therefore suggests that the biggest contribution of the EU for the FDI inflows into the Central and Eastern European countries consisted in its lenient approach in application of the EU internal market competition policy in the area of exceptions from prohibition of state aid.

[7] Bandelj (2010).
[8] Medve-Bálint (2014) p. 43.
[9] Ibid. p. 43 and 44.
[10] See Article 87 (1) of the Treaty establishing the European Community (**EC Treaty**), and currently Article 107 (1) of the Treaty on Functioning of the European Union (**TFEU**), which prohibits any state aid that may distort competition within the EU.
[11] Bohle & Husz (2005).
[12] In this case the justification under Article 87 (3) of the EC Treaty, and currently Article 107 (3) TFEU has to be mentioned, under which article aid to promote the economic development of areas where the standard of living is abnormally low or where there is serious underemployment may be compatible with the internal market.
[13] Medve-Bálint (2014) p. 45.

The FDI during the global economic recession of 2009

The global recession of 2009 stood for a severe stress test for the Central and Eastern European economies. At that time those economies had already become highly internationalized, extremely export oriented and dependent on foreign financing together with significant foreign ownership of banks operating within the region. This made them highly sensitive to external shocks and dependant on developments in Western European markets.[14]

1. The worst average capital outflow from the region presented itself in the last quarter of 2008 and the first quarter of 2009 but did not slump under 1 % of the GDP.[15]

2. As Epstein (2014) further indicated, Western banks who received assistance from their home governments during the financial crisis were under political pressure to reorient their lending activities on home markets to the detriment of their foreign involvement.[16] Notwithstanding to this pressure the pre-crisis levels of Western banks exposure have been maintained in most Central and Eastern European economies.[17] The rules of the EU internal market were important impediment to such bailout political pressures. Moreover, the Council of the EU in this context declared in March 2009 that "support for parent banks should not imply any restrictions on the activities of subsidiaries in EU host countries".[18]

3. Epstein (2014) concludes that the internal market rules and its impact on blurring of the distinction between home and foreign markets in the EU has prevented even deeper impact of the 2009 global recession on the countries of the Central and Eastern Europe.[19]

Therefore, while the dominant export orientation of the FDI inflows into the Central and Eastern Europe renders the region sensitive to global crises, the membership in the EU internal market cushion the tendency of the FDI to seek an early exit in reaction to an advancing economic crisis.

[14] Ibid. p. 47.
[15] European Bank for Reconstruction and Development (2009) p. 12.
[16] Epstein (2014) p. 29.
[17] Ibid.
[18] Council of the EU (2009) p. 2.
[19] Epstein (2014) p. 28-31.

3. Free movement of workers – the Internal Market half-opened

The transitional provisions

From the four basic freedoms of the EU internal market, the free movement of persons was the most severely affected by the transitional period restrictions applied on the side of the "old" EU member states. The Accession Treaties of the 2004 and 2007 enlargement allowed the pre-enlargement EU member states (the former EU15 in case of the 2004 enlargement and the former EU25 in case to the 2007 enlargement) to retain, for the specified time, restrictions on the access to their labour markets by migrants from the "new" member states.[20] The restrictions could have been applied only as the employment related requirements. The right to travel and reside has been guaranteed without any restriction. The duration of the transitory restriction provisions has been subjected to the so-called 2-3-2 formula. The first two years after the enlargement the "old" EU member states were allowed to apply labour market restrictions resulting from their national regulations and/or their bilateral treaties. After this, the application of the national work permit regulations could have been extended for the subsequent three years by a simple member state notification to the European Commission. The last possible extension by additional two years was made subject to a condition that the labour market of a particular "old" EU member state would be under danger of grave disturbances. The utmost transition period was thus seven years in total.

In the aftermath of the 2004 EU enlargement only the United Kingdom, Ireland and Sweden opened their labour markets without use of any transitional period. Within the second phase, these states were joined by eight more states of the former EU15, namely by France, Italy, Spain, the Netherlands, Finland, Greece, Portugal and Luxembourg. Only Germany and Austria retained the labour market restrictions for the whole transition period up until 2011. In Germany, any gainful employment by workers from the states of the 2004 EU enlargement wave was possible only under authorization granted in the form of a "work permit EU" (*Arbeitsgenehmigung-EU*), the exceptions being only workers from Malta and under certain circumstances also from Cyprus, in which cases the German labour market has been liberalized since their accession in the 2004.[21]

The fortunes of the transition restriction of the 2007 enlargement "new" EU member states (Romania and Bulgaria) were even worse than in case of the 2004 EU enlargement. It started on an optimistic note when ten EU member states of the EU25 agreed to liberalize their

[20] For individual Accession Treaties see http://ec.europa.eu/social/main.jsp?catId=474&langId=en.
[21] See e.g. Mävers, G. (2006).

labour markets from the onset of the Romanian and Bulgarian accession. A flaw on this positive beginning was that out of these ten countries eight belonged to the 2004 EU enlargement wave (only Hungary and Malta were absent) and from the "old" EU15 only Sweden and Finland joined this group. The global recession of 2009 did not help to fasten the labour market liberalization. At the end, nine EU member states utilized the full seven-years long transition period (ended by the end of 2013). Besides Germany and Austria, which used such an approach also in case of the post 2004 enlargement transition period, this was now true also for the United Kingdom, France, Spain, the Netherlands, Luxembourg and Malta. Ireland and Italy had liberalized their labour markets for workers from Romania and Bulgaria just at the end of the second phase (i.e. in 2012).

In 2014 the only existing transition period restrictions apply to the newly acceding Croatia. Thirteen EU member states of the EU27 employed the transition restrictions on access of Croatian workers to their labour markets.[22]

Change of the approach of the United Kingdom

The most striking change of its approach to the labour market restrictions could be seen in case of the United Kingdom. The United Kingdom moved from the application of the onset labour market liberalization for the workers of the new EU 2004 enlargement countries to holding of the full seven-years of transition period for workers from Romania and Bulgaria. Moreover, as Gower & Hawkins (2013) show, with the end of the transition period restrictions for workers from Romania and Bulgaria in 2013, the political scene in the United Kingdom has started to show increased desire for a possibility of a further prolongation of the transition period or even a change of the EU rules governing free movement of workers. The number of expected further migrants (despite acknowledgement that Germany, Spain or Italy may attract bigger share of migration from Romania and Bulgaria than the United Kingdom) and fear from abuse of the welfare benefits ranks among the highest incentives for such a political sentiment. It seems that the bold move of the British government with opening of the labour market in the 2004 and the subsequent accommodation of a large number of work migrants from the Central and Eastern European countries,[23] resulted in a British "enlargement fatigue" that at first led to a policy change towards the use of the labour market transition period in connection with the 2007 EU enlargement and is currently transformed into a growing political sentiment which may potentially influence the standpoint of the United Kingdom on the free movement of workers within the EU. A noteworthy contrast to the mentioned policy change on the side of the United Kingdom is the

[22] Namely: Austria, Belgium, Cyprus, France, Germany, Greece, Italy, Luxembourg, Malta, the Netherlands, Spain, Slovenia and the United Kingdom.
[23] For detailed numbers on migration into the United Kingdom and its composition see e.g. Gower & Hawkins (2013).

approach of Sweden, which remains the only country of the "old" EU15 that has never used transition period restrictions to protect its labour market.

Migration in the post 2004 enlargement EU

Kahanec & Zimmermann (2009) in their study focused on the effects of the migration flows on both the receiving and sending countries within the first and second phase after the 2004 EU enlargement emphasized the following findings:

1. utilization of the transitional protective measures by the "old" EU member states opting for this policy did not prevent significant migration inflows from the new EU member states;[24]

2. the policy choice of the opening of the national labour market for workers from the "new" EU member states resulted mainly in different composition of the inflow migration and the state with this policy attracted more educated and younger migrants than those with transitional protective measures;

3. together with findings of to Bonin et al. (2008) the study recognizes that most of the migration inflows from the "new" EU member states are primarily motivated by employment-related factors (better income, improved working conditions and suitable job finding opportunities) rather that attraction to welfare state benefits;[25]

4. Kahanec & Zimmermann (2009) even find enough evidence for suggesting that migrants from the "new" member states were quite unlikely to represent a significant portion among welfare recipients in the "old" member states.[26] The mostly young employment seeking migrants from the East to the West are thus seen not as a threat to the existing welfare state systems of the "old" EU member states but as a potential source for member states' welfare system sustainability and way to ease negative demographic patterns such as an aging population.

The impact of the gradual labour market liberalization on the wage level in the new EU member states in the Central and Eastern Europe is scrutinized by Elsner (2011) who indicates that the 2004 EU enlargement resulted in improved position in the wage level of the young workers (aged 35 and less) who stayed in their "new" EU home countries while their bargaining power rose with the rising possibility to migrate into the "old" EU15 countries. The study reveals that the lover substitutability of young workers by the older

[24] Similar arguments in connection with Germany are presented also in Elsner & Zimmermann (2013) p. 3 and 5.
[25] Kahanec & Zimmermann (2009) p. 13; Bonin et al. (2008) p. 8.
[26] Kahanec & Zimmermann (2009) p. 38.

generation (mainly as the members of the older generation acquired their education under the different economic regime) prevented the wage level improvement to spread through the whole labour market and limited the positive effect mostly to the staying young generation.[27] The trends mentioned in the study could be particularly seen in the "new" EU member states which experienced a bigger migration shock of young generation moving to the Western Europe, such as Lithuania (about 9% of the Lithuanian workforce) and Poland, Slovakia or Latvia (each about 6% of the their respective workforce).[28]

An insights into the problem at the side of an "old" EU member states (Germany) and related policy suggestions are provided by Elsner & Zimmermann (2013). In line with the before mentioned general findings the study shows that despite application of the transitory provisions protecting the German labour market, enlargement years 2004 and 2007 represented a sharp increase of the inflow of migrants in the first instance mainly from Poland, and later also from Romania and Bulgaria.[29] Based on studies showing that immigrants on the German labour market and native Germans of the similar education and work experience are still largely non-substitutable,[30] Elsner & Zimmermann (2013) suggest that immigration has only a moderate effect on wages and employment of native Germans and the incoming migrants compete primarily with the previous waves of immigration into Germany.[31] The resulting policy conclusion by Elsner & Zimmermann (2013) is thus that the German transitory provisions did not help too much in protection of the German labour market but only diverted the needed young and well-educated portion of immigration from Germany to the United Kingdom; opening of the labour market from the beginning thus would have been a better policy choice.[32]

Germany is also well depicted as the current main target for the recent migration driven by the global economic recession and Elsner & Zimmermann (2013) observe that such migration in fact works as an adjustment mechanism that help to some extent absorb asymmetric shocks within the EU, but also remark that despite the surging recession the overall annual net migration into Germany from Southern Europe in 2011 was still "too small to substantially reduce the pressure on the labour markets in the source countries".[33]

In line with the economic theories, the mentioned studies provide arguments that the free movement of workers within the EU is essential for the improved allocation of the workforce, increased productivity and competitiveness, and mechanism to reduce

[27] Elsner (2011) p. 38-41.
[28] Ibid. p. 40, see also Elsner (2013): "Does Emigration Benefit the Stayers? Evidence from EU Enlargement." Journal of Population Economics, 26 (2).
[29] Elsner & Zimmermann (2013) p. 5.
[30] D'Amuri et al. (2010) and Brücker & Jahn (2011).
[31] Elsner & Zimmermann (2013) p. 13 and 14. See also Brenke et al. (2009).
[32] Ibid. p. 14.
[33] Ibid. p. 15.

asymmetries on the labour markets in the EU. The transitional restrictions on the access to the labour markets in fact did not make much difference in protection of the host country level of wages and employment. Their asymmetric application by the "old" EU15 countries moreover resulted in artificial inputs to the migrants' decisions on where to move and thus prevented to reap the optimal results of human resources reallocation. Last but not least, the distorted migration inflows into the countries that from the onset liberalized their labour markets to the workers from the 2004 EU enlargement countries, resulted in case of the United Kingdom in an "enlargement fatigue" that nourish a spread of the current anti-immigration political sentiment.

4. The persisting barriers for deepening the Internal Market in services

The failure of the Bolkestein Directive

While the internal market in the area of the free movement of goods was more or less achieved through the processes that started with the Single European Act, the free movement of services has been constantly lagging behind. The internal market with goods is constructed around the country of origin principle (*mutual recognition principle*) derived from the Court of Justice of the European Union (CJEU) case law started with the 120/78 *Rewe-Zentrale AG (Cassis de Dijion)* case under which a product legally manufactured or marketed in one EU member state should be accepted to markets in all remaining EU member states. Such principle has never been accepted for the free movement of services (or for the intertwined freedom of a service provider establishment). This area is still dominated by the regulations of the destination countries where the service is provided and service providers in cross-border situations thus often have to comply with regulatory provisions of their home country as well as with regulatory provisions of the country where the service is provided. Compliance with such regulatory burden and related cost on research into differing requirements is particularly burdensome for small and medium size enterprises which would like to engage in cross border operations.

This persisting multiple regulatory burden on the service market has also a lot in common with the negative political sentiment after the 2004 enlargement and the unfortunate timing of the European Commission's 2005 draft directive that aimed on introduction of the country of origin principle into the area of free movement of services, the so-called "*Bolkestein Directive*".[34] The proposal to introduce country of origin principle into the service sector

[34] The draft directive is connected with **Frits Bolkestein**, the Dutch Commissioner for Internal Market and Services in the time of the original proposition of the directive.

stirred in several "old" EU15 member states a severe opposition that reached its peak in mass protests in Brussels and Strasbourg.[35] The reasons for the opposition manifested in the allegory of a hypothetical "Polish plumber" that would have been allowed to provide services on a freelance basis freely in all EU member states and the only applicable regulation for him/her would be Polish law.[36] The feared accompanying consequence of this would be a general "race to the bottom" competition between national legislations reducing the service regulation potentially to almost zero.

There was however another important political aspect fuelling opposition to a prompt liberalization in the service sector. Immediate and full liberalization of cross-border provision of services and freedom of establishment for pursuit of self-employed activity would have weakened effectiveness of the post-enlargement transitional restrictions on the access to the "old" member states' labour markets as described in the previous section. The labour market restrictions did not apply to the free-lance workers and as Elsner & Zimmermann (2013) show even under the level of the free movement of services liberalization of that time the share of free-lancers among migrants coming to Germany soared after 2004 more than 5 times compared to the period before the EU enlargement.[37] The labour markets of economy sectors that allow for an easy substitution of a labour employment with freelancing could not be in fact protected with further service liberalization. The freedom to provide services served as a "backdoor" to otherwise protected labour markets of the "old" EU member states, which applied the transitional protective measures. The tendency of those "old" member states to postpone further liberalization of the free movement of services at least beyond the end of the possible duration of the labour market transition provisions was thus fully in line with the original rationale behind introduction of those transition provisions.

What really is the Service Directive?

The proposed directive was watered-down in response to the described opposition. The country of origin principle was utterly discarded and the implementation deadline was shifted to December 2009.[38] According to Bruijn et al. (2006) the original directive proposal could have led to a total increase in services trade by 30–62 % while the estimates for the directive without the country of origin principle went down to an increase only between 19 and 38 %.[39] At the time of the supposed implementation of the Service Directive the intra-

[35] See e.g. Lindstrom (2010); for a detailed analysis on the opposition to the Bolkenstain Directive in France see Grossman & Woll (2011).
[36] Lindstrom (2010) p. 1308 or Grossman & Woll (2011) p. 349-352.
[37] Elsner & Zimmermann (2013) p. 3.
[38] Article 44 (1) of the directive 2006/123/EC of the European Parliament and of the Council of 12 December 2006 on services in the internal market, OJ [2006] L 376/36 (**Service Directive**).
[39] Bruijn et al. (2006) p. 34.

EU trade in services amounted only to 5 % of the EU GDP which is in a sharp contrast to the overall role of the service sector in GDP and jobs creation in the economies of the EU member states and shows a large growth potential.[40]

The Service Directive, as it was adopted, is a set of rules horizontally applicable to all service sectors with exception of those sectors that are explicitly exempted either because they have a separate regulation on the EU level (e.g. audiovisual services) or that it was too far-reaching to include them.[41] Despite those exemptions the Service Directive still covers a wide area of differing service sectors, including for instance:
business services, office maintenance, advertising, recruitment services, legal or fiscal advisory, real estate services, construction, including the services of architects, services in tourism, travel agencies and car rental, sports centers and amusement parks.[42]
As Lenaerts (2011) observes this means that the Service Directive in principle covers all services that may be provided by self-employed persons from one EU member state in another member state.[43]

What the Service Directive actually brought new to the regulation of cross-border provision of services is however largely disputable. The two supposedly main Articles of the Service Directive[44] that substituted the former Article introducing the country of origin principle, are mostly considered as nothing more than mere repetitions of the case law of the CJEU that had been issued prior the time when the Service Directive was adopted.[45] The main positive contribution of these provisions is thus seen in their role as a catalogue of rights of service providers that may serve to improve their awareness of their rights derived from the EU primary law and the CJEU case law and enhance their position in dealing with public authorities of the EU member states.[46]

The biggest contribution of the Service Directive therefore does not lie in a further deepening of the free movement of services but in a series of "smart" instruments that the

[40] Organisation for Economic Co-operation and Development (2009) p. 21.
[41] See Article 2 of the Service Directive. The Service Directive covers the situation when the service providers want to provide services on temporary basis in other EU member states than where they are established (free movement of services in a narrow meaning, Chapter IV of the Service Directive) as well as to situations when service providers desire to move their practice to different EU member state on permanent basis (freedom of establishment, Chapter III of the Service Directive).
[42] For the whole demonstrative list of covered service sectors see Article (33) of the Service Directive Preamble.
[43] Lenaerts (2011) p. 35.
[44] I.e. Article 9 of the Service Directive addressing the authorisation schemes in connection to the freedom of establishment and Article 16 of the Service Directive that aims at member states' requirements that may be imposed on provision of services in the narrow sense.
[45] See e.g. Rentrop (2007) p. 17; for an overview of scholars supporting this position see Dashwood et al. (2011) p. 624.
[46] Barnard (2008) p. 393-394.

Service Directive introduces and that aim at administrative simplification of the process under which services may be provided in another EU member state. Those "smart" instruments include obligation of the member state to establish the so-called point of single contact – an authority through which service providers may, at a distance and by electronic means,[47] complete most of the administrative procedures and formalities necessary for provision of services in another EU member state.[48] In order to reduce mutual mistrust between administrative authorities of different EU member states the Service Directive also provides detailed rules facilitating mutual assistance between EU member states authorities that oversee provision of services.[49] The system of mutual assistance is decentralized and the EU is involved primarily in order to guarantee its smooth operation.[50] The Service Directive finally also demands from all EU member states to test their procedures and formalities applicable to provision of services and simplify them whenever they do not meet a criteria of sufficient simplicity.[51]

Which EU member states were behind time with the implementation of the Service Directive?

The process of implementation of the Service Directive was almost as troublesome as the process before its adoption. Twelve out of the EU27 member states did not implement the Service Directive within the December 2009 deadline, namely Austria, Belgium, Cyprus, France, Germany, Greece, Ireland, Luxemburg, Portugal, Romania, Slovenia and the United Kingdom. This means that among the twelve delaying states nine were the "old" EU15 member states and only three were from the group of the recently acceding states from both 2004 and 2007 enlargement. In June 2010 the European Commission issued a reasoned opinion (the second stage of the EU infringement procedure, the Article 258 (1) TFEU) to all the twelve delaying states.[52]

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[47] See Article 8 of the Service Directive.
[48] See Article 6 of the Service Directive.
[49] See Article 28-36 of the Service Directive. E.g. obligation of a member state where a service provider is established to undertake checks, inspections and investigations requested by another EU member state (Article 29 (2) of the Service Directive), or the alert mechanism obligation to inform the authorities of all other relevant EU member states in case that an EU member state becomes aware of an information that a service provision may cause damage to the health, personal safety or to the environment (See Article 32 of the Service Directive).
[50] The European Commission primarily plays a role of the arbiter for cases when one EU member state claims that its counterpart does not fulfil its mutual assistance obligation (Article 28 (8) of the Service Directive) and organizes the supporting systems such as the electronic system for the exchange of information between the EU member states, the **Internal Market Information System** (Article 34 (1) of the Service Directive).
[51] See Article 5 of the Service Directive.
[52] European Commission (2010).

In October 2011, i.e. almost two years past the implementation deadline, the European Commission referred three states, namely Germany, Austria and Greece, to the CJEU for the persisting incomplete implementation of the Service Directive.[53] All three remaining countries implemented the Service Directive in the course of the year 2012 (Germany in January 2012, Austria in April 2012 and Greece in May 2012) thus without necessity for the CJEU to adopt a decision penalizing the delayed states as was suggested by the European Commission.[54]

On the other hand, besides the issue of the deferred implementation, which in case of Austria and Germany coincided with the 2011 end of the possibility to maintain transitional labour market restrictions towards the 2004 EU enlargement wave, there is also a striking difference between number of national provisions implementing the Service Directive. In case of Germany and Hungary the implementation has taken to adopt 220 implementing measures, while Bulgaria and Estonia referred only the one horizontal transposition measure and in case of Ireland and Poland only two measures were referred.[55] This casts a shadow over the quality of the Service Directive implementation in the later mentioned states and in particular questions the proper reflection of the Service Directive in their sector-specific legislation.

What the Service Directive has achieved and can its flexibility clauses lure more?

The economic estimates by European Commission (2012b) on the already achieved contribution of the Service Directive show that the immediate impact of the adopted implementation measures brought an increase of 0.133% of GDP in the EU27 average.[56] The results of individual EU member states vary significantly. The range is from only 0.0042 % increase of GDP for Austria to 0.5209 % increase of GDP in case of Portugal.[57] The group of eight countries ranking with their individual increases above the EU average consist of a mixture of the "old" EU15 and recently acceding states, including Portugal, Spain, Slovakia, Slovenia, Hungary, Estonia, Latvia and Finland.[58]

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[53] European Commission (2011) where the incomplete implementation was specified as Austria delaying with passing of any horizontal transposition laws, Germany delaying with adoption of three measures (one at federal level and two at regional level) and Greece delaying with adoption of a whole series of measures, especially in economically important sectors such as tourism and personal and business services.
[54] European Commission (2012a).
[55] EUR-Lex.
[56] European Commission (2012b) p. 50-51 and 83. The estimates of the study are based on the procedural streamlining effort in simplification of variables derived from the World Bank's Doing Business 2012 Database.
[57] Ibid. p. 83.
[58] Ibid. p. 50 and 83.

The formal phase of the Service Directive implementation that ended with Greek implementation in May 2012 is however only the beginning. The articles of the Service Directive that codify the previous CJEU case-law and require member states to refrain from restrictive regulation unless it is non-discriminatory, justifiable and proportional to its goals, provide a significant flexibility to the EU member states on to the extent of ambition with which they pursue the implementation.[59] The European Commission (2012c) in this case recognizes that some of the less ambitious implementations may not constitute a violation of the Service Directive and be also fully in line with the EU law, this however does not preclude the European Commission from stressing the economic advantages of the more ambitious implementation.[60] In this connection the biggest stimulus for an adoption of the more ambitious implementation lies in the clauses of the Service Directive that allow to reintroduce the regulatory provisions that would fall within the discretion provided by the Service Directive.[61] Although the procedure of introduction of new regulatory provisions is partly made more difficult by the Service Directive's requirement to notify to the European Commission (and through it to other EU member states) any new regulatory measures that fall within the discretion, this notification requirement however does not prevent the adoption of the new regulation unless it is found to be outside the scope of the discretion and thus against the EU law.[62] This is a very progressive way how the EU may encourage its member states to be more courageous in their service liberalization endeavour and free them from the fear that a bold move in reduction of the regulatory burden would close a door for an adoption of a similar regulation in the future in case that they realize some adverse effects caused by the liberalization. Such a flexible approach also helps to fend off most of the possible claims that the EU legislation is far-reaching and in breach of subsidiarity or proportionality principle.

The story of the Service Directive reveals that the failure of the original Bolkestein's proposal for introduction of the country of origin principle into the EU service market can be connected with the fear in some of the "old" EU member states from the impact of the suspected increased heterogeneity of the level of service regulation within the EU after the 2004 enlargement and most likely also with the dislike of some of the "old" EU member states to open, through service liberalization, an alternative backdoor to their labour markets that were still protected during the post-enlargement transitional periods.

The resulting Service Directive represent a set of "smart" tools to facilitate the free movement of services within the EU without the country of origin principle and at the same

[59] European Commission (2012c) p. 5 in this concern expressly mention Article 15 of the Service Directive (aiming on member state regulation requesting from a service provider to have e.g. a specific legal form) and Article 16 of the Service Directive (aiming in general on regulations limiting access to or exercise of a service activity).
[60] European Commission (2012c) p. 4 and 5.
[61] See Article 17 (6) and (7) of the Service Directive.
[62] Ibid.

time without introduction of any horizontally applied positive integration of the service sectors at the EU level. These "smart" tools include for instance the points of single contact allowing an access of the service providers to the administrative authorities form one unified place and the Internal Market Information System that facilitates administrative cooperation between the relevant authorities of the EU member states. Finally, a further "smart" approach of the Service Directive lies also in the possibility of the EU member states to introduce new regulatory provisions within the given flexibility which release them from the fear that an advanced liberalization in service sector would prevent them from reintroduction of regulation in case it is found necessary.

The flexibility maneuver of the Service Directive shows a possible way of how to proceed in some of the other frozen areas that might enhance the full functioning of the EU internal market such as for instance the European Commission's proposal for the Common Consolidated Corporate Tax Base where the possibility of any EU member state to feely join and leave such an arrangement (with the end of any annual tax period) could possibly work as a catalyst for its very adoption.[63]

5. Conclusion and implications

For the evaluation of the 10 years of the Central and Eastern European countries participation on the EU internal market it is useful to understand the EU integration as proceeding on two axes. The first vertical axis represents the level of integration and its deepening. In the area of the internal market this includes primarily the extent of the real undisturbed functioning of the four basic freedoms. The horizontal axis then shows the territorial extent encompassed by the integration and the moves on this axis proceed mostly through the process of the enlargement.

In area of the FDI inflows into the newly acceding EU member states the internal market has played the role of a guarantee of the application of the EU wide regulatory standards and enhanced the attractiveness of the Central and Eastern European countries for investments. This area moreover shows that the vertical axis represented in this case by the strictness in application of the state aid prohibition had been moderated in order to allow the new member state governments to attract FDI with the widespread practice of the incentive schemes.

The case of the transitional periods revealed that the internal market was not fully opened to the newly acceding EU member states from the onset. The vertical axis represented by the

[63] In this connection see for instance position of the government of the Netherlands stating that the Common Consolidated Corporate Tax Base proposal has not pass its subsidiarity test; Netherlands Government (2013) p. 8.

free movement of workers in this area spread in the horizontal dimension only in gradual steps as the "old" EU15 states successively opened their labour markets to the migrants from the "new" EU member states. This at the one hand most likely helped to spread the shock of the migration waves in the sending countries into several stages, on the other hand resulted in an artificial motivation for migration and an increased impact of the migration inflows on the "old" EU15 countries that opened their labour markets in the earlier stages.

Finally, the issue over further liberalization of the free movement of services shows that the newly acceding EU member states were not those who would on their own hamper further development of the internal market. The horizontal spread of the internal market and the resulting decrease in mutual trust and the fear from an increased heterogeneity of the service regulation however prevented the proposed move onto the vertical axes consisting in introduction of the country of origin principle in the area of free movement of services. The need to overcome this display of the "enlargement fatigue" resulted in lesser ambitious move on the vertical axis by adoption of the Service Directive. The methods used by this directive in substitution of the country of origin principle represent a creative endeavour to facilitate the liberalization of the cross-border provision of services within the club of 27(28) member states.

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