The Principle of Subsidiarity in the Treaty on European Union: A Critique from a Perspective of Constitutional Economics

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I. INTRODUCTION

In November 1994, George A. Bermann, in a lecture presented at the Eason-Weinmann Colloquium on International and Comparative Law at Tulane Law School, suggested that European Community law "fostered a remarkable renewal of interest in the problems of American federalism."[1] Professor Bermann has also presented the principle of subsidiarity, introduced to European Community law by the Treaty on European Union (commonly known as the Maastricht Treaty),[2] to an American audience.[3] The principle of subsidiarity[4] has been the subject of an ongoing discussion among American scholars. This principle has created

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1. George A. Bermann, *European Community Law from a U.S. Perspective*, 4 TUL. J. INT'L. & COMP. L. 1, 5 (1995).

2. *See* TREATY ON EUROPEAN UNION, Aug. 31, 1992, O.J. (C 224) 1, 5 (1992) [hereinafter MAASTRICHT TREATY].

3. *See generally* Bermann, *supra* note 1; George A. Bermann, *Taking Subsidiarity Seriously: Federalism in the European Community and the United States*, 94 COLUM. L. REV. 332 (1995).

4. *See* W. Gary Vause, *The Subsidiarity Principle in European Union Law—American Federalism Compared*, 27 CASE W. RES. J. INT'L L. 61 (1995).

an optimistic view of the "word that saves Maastricht"[5] to provide guidance in solving problems of federalism. In this Article, I will analyze the principle of subsidiarity by applying the tools of constitutional economics. The underlying hypothesis of this endeavor is that the principle of subsidiarity is valuable as a *general guide* on how to allocate powers in vertically structured political entities. However, there are certain shortcomings in using the principle of subsidiarity as a technical tool for effectively protecting the Member States of the European Union (EU) against a steady erosion of their sovereignty.

Section II of this Article begins with a brief overview of the present situation within the EU. The economic subdiscipline of constitutional economics is introduced in Section III, followed by legal analysis in Section IV. In Section V, I define the central problem at issue, and in Section VI, I apply the analytical instruments to the principle of subsidiarity. Finally, I will present conclusions of the analysis, and an outlook on this subject area in Section VII.

II. PRESENT SITUATION IN THE EUROPEAN UNION

When the Member States of the European Communities (i.e., the European Economic Community (EEC), the European Coal and Steel Community (ECSC), and the European Atomic Energy Community (EAEC))[6] decided to create a Political Union, they surpassed the original objective of an *Economic* Union. As a result, they were confronted with the problem of how to prevent excessive centralization of the new political entity. However, this was not a new problem posing a challenge to the European integration process. Prior to the Maastricht Treaty negotiations, the emphasis had been placed on overcoming difficulties arising from the ongoing integration process. The Single European Act of 1987 (SEA) attempted to accelerate the speed of integration by incorporating article 100(a) into the EEC Treaty,[7] which viewed integration as a means of creating the Internal Market, via legal approximation of its functions. This *functional approach*, linking Community competencies to their function for integration, remained in the Maastricht Treaty. However, the goal itself has expanded from the

5. Deborah Z. Cass, *The Word that Saves Maastricht? The Principle of Subsidiarity and the Division of Powers within the European Community*, 29 COMMON MKT. L. REV. 1107 (1992).

6. TREATY ESTABLISHING THE EUROPEAN COMMUNITY, Mar. 25, 1957, O.J. (C 191) 5 (1992) [hereinafter EC TREATY]; TREATY ESTABLISHING THE EUROPEAN COAL AND STEEL COMMUNITY, Apr. 18, 1951, O.J. (C 191) 44 (1992) [hereinafter ECSC TREATY]; TREATY ESTABLISHING THE EUROPEAN ATOMIC ENERGY COMMUNITY, March 25, 1957, O.J. (C 191) 50 (1992) [hereinafter EURATOM TREATY].

7. SINGLE EUROPEAN ACT, June 29, 1987, O.J. (L 169) 1, 8 (1987) [hereinafter SEA] (amending the Treaty establishing the European Economic Community).

creation of a Common Market to that of a Political Union. As the Member States realized the potential danger of the functional approach in defining competencies of the EU, they attempted to strike a balance between powers of the EU and powers of the Member States by introducing the principle of subsidiarity into article 3(b)(2) of the EC Treaty.

III. CONSTITUTIONAL ECONOMICS APPLIED TO A EUROPEAN CONSTITUTION

In a constitutional economics analysis,[8] the tools of modern economics are applied to constitutional problems. The *subject matter* of this type of analysis is the same as that of constitutional law. However, the methodological implications are quite different. The discipline of economics is no longer confined to the analysis of markets or the economy. Modern economics is applied to all fields where individual actors must choose between scarce resources. Beyond the market, institutions involved may include bureaucracies, political voting systems, the lawmaking process, and constitutional decisions.

The methodological toolbox of economics consists of three assumptions combined with methodological individualism. The three assumptions are: (1) the assumption of scarce resources; (2) the assumption of self-interested behavior; and (3) the assumption of rational decision-making. These assumptions are heuristic; they apply to groups of actors, rather than individual actors. Accordingly, the assumption of rational decision-making does not refer to well-informed choices of individuals who are optimizing their decisions. Instead, it applies to individuals with limited information about their situations, who tend to choose the option which according to their subjective assumptions are more useful (bounded rationality). Methodological individualism refers to the fact that decisions are made by individuals, not collectives. In addition, methodological individualism is unlike holistic or collectivist approaches that attribute decisions to collectives, such as states, parties and enterprises. In its normative version, constitutional economics adds normative individualism to methodological individualism,[9] such that any legitimization of constitutional or institutional choices must be based on the consent of individuals. Thus, the approach of constitutional

8. *See* HORST FELDMAN, EINE INSTITUTIONALISTISCHE REVOLUTION? ZUR DOGMENHISTORISCHEN BEDEUTUNG DER MODERNEN INSTITUTIONENÖKONOMIE, 53-6 (1995) (discussing constitutional economics in institutions); James M. Buchanan, *The Domain of Constitutional Economics*, 1 CONST. POL. ECON. 1 (1990) (explaining "constitutional economics" as a methodology for analyzing "choices among constraints").

9. *See* FELDMAN, *supra* note 8, at 54; Buchanan, *supra* note 8, at 7, 13.

economics is closely linked to democratic theories but is more general in its scope of application.

Application of this systematic analysis to issues of a European Constitution (as well as the set of existing treaties forming the three European Communities, the SEA, and the Maastricht Treaty,[10] which some regard as having formed a Constitution[11]) begins with the clear recognition of the fundamental importance of the value of *individual liberty* not conferred by Government, rather than a discussion of the desirability of European integration. The legitimacy of European institutions rests on the powers issued by the people. In a principal-agency model, citizens are the principals, whereas the members of the various national and European institutions are the agents.[12] Changing the allocation of powers to different levels of vertically structured political and legal systems means altering those principal-agent relations.[13] A constitutional economics analysis capable of producing workable proposals in the given political and legal context of Europe should be based on an analysis of the given legal situations of multiple jurisdictions in the EU. This legal analysis then must be translated into terms of constitutional economics in order to define the problem.

IV. LEGAL ANALYSIS

The original objectives of the Rome Treaty, to create a Common Market and a Customs Union based on the four freedoms (free circulation of goods, services, persons, and capital), have been changed and supplemented by the SEA and the Maastricht Treaty. The integration process shall now lead to an *internal European market*—an economic, monetary, and political union. To attain these goals, competencies have been increasingly transferred from the Member State level to the European level.[14] The treaties establishing the European Communities (now in the version of the Maastricht Treaty), the SEA, and the Maastricht Treaty function like a constitution[15] without having been

10. *See generally* EC TREATY, *supra* note 6; ECSC TREATY, *supra* note 6; EURATOM TREATY, *supra* note 6; SEA, *supra* note 7; MAASTRICHT TREATY, *supra* note 2.

11. *See* Case 294/83, "Les Verts" v. Parliament, 1986 E.C.R. 1339, 1365; Manfred Zuleeg, *Art. 1 EEC*, *in* KOMMENTAR ZUM EWG-VERTRAG 65-94 (H. von der Groeben, et al. eds., 4th ed. 1991); Ernst-Ulrich Petersmann, *Proposals for a New Constitution for the European Union: Building-Blocks for a Constitutional Theory and Constitutional Law of the EU*, 32 COMMON MKT. L. REV. 1123 (1995) (analyzing the constitutional functions of the EC Treaties).

12. *See* Christian Kirchner & A. Schwartze, *Legitimationsprobleme in einer Europäischen Verfassung*, 6 STAATSWISSENSCHAFT UND STAATSPRAXIS 183, 188 (1995).

13. *See id.*

14. *See* Petersmann, *supra* note 11, at 1125.

15. *See* Zuleeg, *supra* note 11, at art. 1 n.2; *Les Verts*, 1986 E.C.R. at 1365; Petersmann, *supra* note 11, at 1124.

adopted and legitimized by the "European citizen."[16] However, the Member States have agreed upon these international treaties. They create *international law* and bind the parties of the treaties, such as the Member States.[17] The European Community (EC) and the EU[18] are legitimized like international organizations by the consent of their members, who may ratify such treaties by parliamentary vote or referendum. Therefore, a problem of legitimization of European institutions exists only if they are outside the realm of international organizations (i.e., if Community law is different from ordinary international law).

The EC and the EU are not ordinary international organizations insofar as the *European Community* exerts its own *lawmaking power*. The EC Treaty provides for the legislative function of the Community. Community law either addresses the Member States or their citizens. Regulations (article 189(2) of the EC Treaty) are directly applicable. Even in the case of directives, which according to article 189(3) of the EC Treaty must be transformed into national law, the European Court of Justice has defined specific situations in which those directives are directly applicable.[19] Thus, the EC is more than an ordinary international organization; in some respects it resembles a nation-state, and in others it mirrors an international organization. The legislative functions are not in the hands of the European Parliament. Rather, this Parliament participates in the lawmaking process of the Community, while the real lawmaking power is vested in the Council (i.e., the governments of the Member States).

This feature can only be understood in light of the historic development of European integration, which originated with an international treaty by sovereign nation-states. Community law was legitimized indirectly insofar as the national parliaments and governments of the Member States were elected by the citizens of the Member States. As such, the European lawmaking system has no clear separation of powers, a feature that is one of the cornerstones of democracy. This deficiency has been called the democracy deficit of the EC.[20] When the

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16. *See* EC TREATY, *supra* note 6, art. 8(a)-(e) (introducing a Union citizenship; inserted by the Maastricht Treaty).

17. *See* Zuleeg, *supra* note 11, at art. 1 n.2.

18. The European Union consists of three components called "pillars": the European Community (first pillar), Common Foreign and Security Policy (second pillar), and Cooperation in the Fields of Justice and Home Affairs (third pillar). *See* MAASTRICHT TREATY, *supra* note 2, Title 1, art. B.

19. *See, e.g.*, Case 80/86, Kolpinghuis Nijmegen BV, 1987 E.C.R. 3969, 3985-87; Case 8/81, Becker v. Finanzamt Münster-Innenstadt, 1982 E.C.R. 53.

20. *See* Christian Kirchner & Joachim Haas, *Rechtliche Grenzen für Kompetenzübertragungen auf die Europäische Gemeinschaft*, 48 JURISTENZEITUNG 760, 764-67 (1993).

objectives of the Community were confined to the creation of a Customs Union and a Common Market, this lack of democratic legitimization was recognized. However, at the time, the competencies of the Community did not reach a level where this deficiency could endanger the democratic systems of the Member States. With only limited competencies, the conflict between Community law and national law of the Member States was minor.[21] This changed with the transfer of more competencies to the Community by the SEA.

Community competencies have been broadened, and the lawmaking power of the Community has been substantially strengthened by the inclusion of article 100(a) in the EEC Treaty.[22] On the basis of this new article, the Community was empowered to adopt measures for the harmonization of the law of Member States "which have as their object the establishment and functioning of the internal market."[23] This functional definition of community competencies is limited only by the objectives of the Community.

The potential conflict between Community law and the law of Member States was recognized by the parties of the SEA when they limited the scope of article 100(a)(1) of the EEC Treaty in section 2 of that article and pronounced certain safeguards for Member States in sections 4 and 5. On the other hand, it was clear by then that Community law preempted the law of Member States that did not fall under article 100(a)(4) of the EEC Treaty.[24] The conflicts between Community law and law of Member States are typical for a system of dual jurisdictions. There are various models regarding methods for coping with these problems.[25] The Treaties establishing the European Communities and the SEA, with the exception of article 100(a) and article 235 of the EEC Treaty, are silent on the issue.

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21. *See* BENGT BEUTLER ET AL., DIE EUROPÄISCHE UNION: RECHTSORDNUNG UND POLITIK, 294-98 (4th ed. 1994).

22. *See* Pierre Pescatore, *Some Critical Remarks on the "Single European Act"*, 24 COMMON MKT. L. REV. 9 (1987) (criticizing the SEA as a setback for the EC); Jürgen Schwarze, *The Reform of the European Community's Institutional System by the Single European Act, in* LEGISLATION FOR EUROPE 1992 (Jürgen Schwarze ed., 1989) (observing that the SEA's value derives from the commitment of Members, not from incoherent attempts at reform); *see generally* C.D. Ehlermann, *The Internal Market Following the Single European Act*, 24 COMMON MKT. L. REV. 361 (1987).

23. *See* EEC TREATY art. 100(a).

24. *See* Hans-W. Micklitz, *The Maastricht Treaty, the Principle of Subsidiarity and the Theory of Integration*, 4 LAKIMIES 508, 515 (1993) (discusing the doctrine of preemption).

25. *See, e.g.*, FRANK VIBERT, EUROPE: A CONSTITUTION FOR THE MILLENIUM 118-26 (Aldershot ed., 1995).

Article 235 of the EEC Treaty is a highly controversial provision.[26] Under this provision, the Council, by unanimous vote, may take the appropriate measures "if action by the Community should prove necessary to attain, in the course of operation of the common market, one of the objectives of the Community and this Treaty has not provided the necessary powers."[27] Whether or not this confers a competence-competence on the Community is still an open question, which under the present system, has to be answered by the European Court of Justice.[28] The granting of a competence-competence to the Community, and thus the application of an implied-powers doctrine, signals that the system of multiple jurisdictions is hierarchical, with Community law at the top of the pyramid. The functional definition of the powers of the Community in article 235 of the EEC Treaty could be utilized to draw more competencies to the Community level. However, this can only be successful if Community law is supreme vis-à-vis national law of the Member States. The Treaties establishing the Community are silent on this issue. One option is to start with the simple argument that the Common Market can only function if the four freedoms are working in all Member States in the same way, and if Community law is not distorted by national legal provisions. The next logical step would be to state the supremacy of Community law.[29]

Meanwhile, the doctrine of supremacy of Community law has become one of the cornerstones of Community law. In fact, the constitutional courts of the Member States have accepted that doctrine to a high degree. They have not, however, abandoned the doctrine of parallel jurisdictions under which certain fields of national jurisdiction cannot be invaded by Community law.[30] In addition, the positions of national constitutional courts have become more defensive. The line of defense for parallel jurisdictions is marked by the doctrine of enumerated powers,[31] which states that the Community has only those competencies that are explicitly conferred to it by the Treaties establishing the Communities and the SEA. The doctrine of enumerated powers may be traced in the text of those Treaties, where the competencies are not defined by certain fields of activities but by a mixture of fields of activities and objectives of the Treaties. Thus, the real problem is not the

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26. *See* BEUTLER, *supra* note 21, at 83-84; Ivo E. Schwartz, *Art. 235 EEC*, *in* KOMMENTAR ZUM EWG-VERTRAG (H. von der Groeben, et al. eds., 4th ed. 1991).

27. EEC TREATY art. 235.

28. *See* Micklitz, *supra* note 24, at 516.

29. *See* BEUTLER, *supra* note 21, at 96-97. *See also* Case 26/62, Van Gend en Loos v. Néderlandaise Administriatie der Belastingen, 1963 E.C.R. 1, 24.

30. *See* BEUTLER, *supra* note 21, at 98-109.

31. *See* Micklitz, *supra* note 24, at 517; BEUTLER, *supra* note 21, at 82.

decision for the implied-powers doctrine or the enumerated-powers doctrine, but how to confine the competencies of the Community in fields of activities where Member States are also active.

With the preemption doctrine being applicable, a functional definition of Community competencies according to the objectives of the Treaties would mean that, even in fields of mixed competencies, those competencies of the Member States could be eroded by interpreting Community competencies functionally. The interpretation lies in the hands of the European Court of Justice, which may or may not protect the existing competencies of Member States and which tends to favor a concept of dynamic integration, by applying the method of teleological interpretation (finality).[32] The functional concept is reinforced by the preamble of the SEA that states that the EU should be implemented and vested with the necessary means of action.[33]

The Treaties establishing the European Communities, the SEA, and the decisions of the European Court of Justice have created a *system of multiple jurisdictions* with many problems. This system, with its functional and "dynamic" interpretation of Community competencies, supremacy, and the preemption doctrine, was open to a process of European integration through continuous competence transfers to the Community level. It should be noted that legislation on the Community level does not conform to the principle of separation of powers which functions as a power-limiting device for government. In this phase, the system of multiple jurisdictions may be characterized by a hidden hierarchy with erosion of Member States' competencies and a lack of democratic legitimization.

The Maastricht Treaty has changed this system in two respects. First, the competencies conferred to the Community level[34] are substantially enlarged so that the objectives of the EU are more broadly defined than the Treaties that established the European Communities and

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32. *See* Van Gend en Loos, 1963 E.C.R. 1, 24; BEUTLER, *supra* note 21, at 246-47; *see* HJALTE RASMUSSEN, ON LAW AND POLICY IN THE EUROPEAN COURT OF JUSTICE (1986) (critically evaluating the role of the European Court of Justice); *see also* Roland Vaubel, *Die Politische Ökonomie der Wirtschaftspolitischen Zentralisierung in der Europäischen Gemeinschaft*, 11 JAHRBUCH FÜR NEUE POLITISCHE ÖKONOMIE 30 (1992); Roland Vaubel, *The Public Choice Analysis of European Integration: A Survey*, 10 EUR. J. POL. ECON. 227 (1994) (evaluating the institutional dynamics of integration).

33. The preamble of the SEA contains the following formulation: "Moved by the will to continue the work undertaken on the basis of the Treaties establishing the European Communities and to transform relations as a whole among their States into a European Union . . . ." SEA, June 27, 1987, O.J. (L 169) 1, 2 (1987).

34. The law-making power is vested in the so-called first pillar of the EU, the European Community. *See generally* EC TREATY, *supra* note 6; ECSC TREATY, *supra* note 6; EURATOM TREATY, *supra* note 6.

the SEA. The current goal is attainment of an economic, monetary, and political union. This redefinition of the objectives of the European integration process has a direct impact on the system of multiple jurisdictions insofar as the functional definition of competencies is being maintained. In fields of mixed competencies, the effect is that the new and broader objectives of the European Union erode the competencies of Member States more easily. The lawmaking power of the Member States can be preempted by Community law at each phase.

The second change refers to a new instrument of settling conflicts between Community and Member States' competencies—the principle of subsidiarity included in article 3(b)(2) of the EC Treaty by the Maastricht Treaty.[35] This subsidiarity principle has been praised as an instrument to stop further erosion of Member States' sovereignty, and it has been

35. *See* Karl Homann & Christian Kirchner, *Das Subsidiaritätsprinzip in der Katholischen Soziallehre und in der Ökonomie*, *in* EUROPA ZWISCHEN ORDNUNGSWETTBEWERB UND HARMONISIERUNG: EUROPÄISCHE ORDNUNGSPOLITIK IM ZEICHEN DER SUBSIDIARITÄT 45-69 (L. Gerkin ed., 1995); Cass, *supra* note 5 (analyzing the division of powers within the European Community); EC Commission, *The Subsidiarity Principle*, 10 BULL. EUR. COMMUNITIES 116 (1992); Von Dieter Grimm, *Subsidiarität ist nur ein Wort*, FRANKFURTER ALLGEMEINE ZEITUNG, Sept. 17, 1992, at 38; P. Haeberle, *Das Prinzip der Subsidiarität aus der Sicht der Vergleichenden Verfassungslehre*, *in* SUBSIDIARITÄTSPRINZIP: EIN INTERDISZIPLINÄRES SYMPOSIUM 167-310 (A. Riklin & G. Batlinger eds., 1994); R. HRBEK, DAS SUBSIDIARITÄTSPRINZIP IN DER EUROPÄISCHEN UNION. BEDEUTUNG UND WIRKUNG FÜR AUSGEWÄHLTE POLITIKBEREICHE (Baden-Baden ed., 1995); HELMUT LECHELER, DAS SUBSIDIARITÄTSPRINZIP: STRUKTURPRINZIP EINER EUROPÄISCHEN UNION (1993); DETLEF MERTEN, DIE SUBSIDIARITÄT EUROPAS (Duncker & Humblot eds., 1993); Micklitz, *supra* note 24 (discussing subsidiarity as a means to limit community competence to its enumerated powers); Wernhard Möschel, *Zum Subsidiaritätsprinzip im Vertrag von Maastricht*, 47 NEUE JURISTISCHE WOCHENSCHRIFT 3025 (1993); Oswald von Nell-Breuning, *Subsidiaritätsprinzip*, *in* STAATSLEXIKON 826-34 (H. von der Gorres Gesellschaft ed., 1962); Picot (1991); Jörn Pipkorn, *Das Subsidiaritätsprinzip im Vertrag über die Europäische Union—rechtliche Bedeutung undGerichtliche Überprüfbarkeit*, 22 EUROPÄISCHE ZEITSCHRIFT FÜR WIRTSCHAFTSRECHT 697 (1992); Wolfgang Renzsch, *Die Subsidiaritätsklausel des Maastrichter Vertrages: Keine Grundlage für die Kompetenzabgrenzung in einer Europäischen Politischen Union*, 1 ZEITSCHRIFT FÜR PARLAMENTSFRAGEN 104 (1993); Mathias Rohe, *Binnenmarkt oder Interessenverband? Zum Verhältnis von Binnenmarktziel und Subsidiaritätsprinzip nach dem Maastricht-Vertrag*, 61 RABELS ZEITSCHRIFT FÜR AUSLÄNDISCHES UND INTERNATIONALES PRIVATRECHT 1 (1997); Peter M. Schmidhuber, *Das Subsidiaritätsprinzip im Vertrag von Maastricht*, 108 DEUTSCHES VERWALTUNGSBLATT 417 (1993); Rupert Scholz, *Das Subsidiaritätsprinzip im europäischen Gemeinschaftsrecht—ein Tragfähiger Ma&stab zur Kompetenzabgrenzung?*, *in* FÜR RECHT UND STAAT: FESTSCHRIFT FÜR HERBERT HELMRICH ZUM GEBURTSTAG 60, 411-26 (K. Letzgus, et al. eds., 1994); Hans-Werner Sinn, *How Much Europe? Subsidiarity, Centralization and Fiscal Competition*, 41 SCOT. J. POL. ECON. 85 (1994) (comparing European subsidiarity with the centralization process that occurred within nation-states in the early part of the century); CLEMENS STEWING, SUBSIDIARITÄT UND FÖDERALISMUS IN DER EUROPÄISCHEN UNION (1992) (discussing subsidiarity and competing competences of community and Member States); A.G. Toth, *The Principle of Subsidiarity in the Maastricht Treaty*, 29 COMMON MKT. L. REV. 1079 (1992) (exploring the impact of the Maastricht Treaty and the principle of subsidiarity upon Member States).

criticized because of its impracticability for judicial review.[36] Its legal character can only be understood in the context of article 3(b) of the EC Treaty as a whole. Section 1 of the article states that "the community shall act within the limits of the powers conferred upon it by this treaty and of the objectives assigned to it therein."[37] The pending conflict between the implied-powers doctrine and the doctrine of enumerated powers is not resolved by this provision. The status quo has been cemented. On the one hand, the first part of the sentence clearly adopts the doctrine of separation of powers for the Maastricht Treaty. However, the recourse to the "objectives assigned to it therein" perpetuates the functional definition of Community competencies in terms of those objectives. The doctrine contained in article 3(b)(1) of the EC Treaty could be called the "qualified enumerative-powers doctrine." This increasingly broad functional definition of competencies easily can lead to a complete erosion of Member States' competencies. In fact, article 3(b)(2) of the EC Treaty states that for those areas that do not fall within its exclusive competence, the Community shall take action in accordance with the principle of subsidiarity, only if and insofar as the objectives of the proposed action cannot be sufficiently achieved by the Member States. Therefore, by reason of the scale or effects of the proposed action, these objectives would best be achieved by the Community. Article 3(b)(2) further states that any action by the Community shall not go beyond what is necessary to achieve the objectives of this treaty.

The principle of subsidiarity, as set forth in article 3(b)(2) of the EC Treaty, is not used to allocate powers to the Community or to the level of the Member States. The principle's function is limited to the application in mixed fields of competencies, which fits well into the development of a system of multiple jurisdictions in the European Communities. Yet, the hidden hierarchy as such has not been changed, except that the exercise of Community competencies in mixed fields of competencies could be limited to a certain extent.

In a legal analysis, the present situation may then be characterized by the following facts:

(1) Community competencies and Member States' competencies exist next to each other.

(2) The *doctrines of supremacy and preemption* are applicable according to the European Court of Justice where conflicts arise in fields of mixed competencies.

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36. *See* Möschel, *supra* note 35, at 3027-28; Scholz, *supra* note 35, at 416; *see also* Pipkorn, *supra* note 35.

37. MAASTRICHT TREATY, *supra* note 2, art. 3(b).

(3) The *doctrine of enumerated powers* has been explicitly incorporated into the EC Treaty but has been weakened by the functional definition of competencies.
(4) The exercise of community competencies in fields of mixed competencies is constricted by the principle of subsidiarity. The judicial review of that principle lies in the hands of the European Court of Justice.
(5) The lawmaking power of the Community is only indirectly legitimized by the citizens of the Member States; the doctrine of separation of powers is not working in that context (lack of democracy).

The system has no legal tool for repatriation of powers to Member States in fields of exclusive competencies of the Community. However, in fields of mixed competencies, the principle of subsidiarity may move in that direction.

V. DEFINITION OF THE PROBLEM

This section defines the problem at hand as one of competing jurisdictions in a semi-hierarchical system of multiple jurisdictions. The principle of subsidiarity is just one part of the system; it functions as a guideline for settling competence conflicts in fields of mixed competencies. The question then is whether or not that principle can fulfill this function. A more radical legal approach would ask whether the existing system, as such, is functioning. Then, the objectives must be laid open. If progress in the European integration process is taken as the main objective, the functional definition of Community competencies proves to be an ideal tool for dynamic integration. If democratic legitimization of acts on the Community level is an important objective, the transfer of powers to the Community level must be constrained and can only be accepted with a simultaneous process of democratic legitimization on the Community level.[38]

The underlying problem is the democracy deficit. However, the situation is even more complex because the so-called democracy deficit cannot be cured simply by enlarging the powers of the European

38. *See* Matthias Herdegen, *Maastricht and the German Constitutional Court: Constitutional Restraints for an "Ever Closer Union,"* 31 COMMON MKT. L. REV. 235 (1994) (discussing the extent to which national powers can be given away such that the minimum requirements for democratic legitimization are no longer fulfilled); *see also* Kevin D. Makowski, *Solange III: The German Federal Constitutional Court's Decision on Accession to the Maastricht Treaty on European Union*, 16 U. PA. J. INT'L. BUS. L. 155 (1995) (analyzing the German Federal Constitutional Court's decision to ratify the Maastricht Treaty and noting the Court's reasoning creates uncertainty about the future effects of the decision); Manfred H. Wiegandt, *Germany's International Integration: The Rulings of the German Federal Constitutional Court on the Maastricht Treaty and the Out-of-Area Deployment of German Troops*, 10 AM. U. J. INT'L L. & POL'Y 889 (1995) (analyzing the German Federal Constitutional Court's ruling that the Maastricht Treaty did not violate the German Constitution).

Parliament.[39] Turning over the legislative function to the European Parliament would not automatically lead to a democratic legitimization of the law-making process because this Parliament has failed to fulfill the functions of an institution comparable to parliaments of Member States. The main deficits are the lack of a European public opinion, the lack of European parties, and the deficiencies of the rules under which members of the European Parliament are elected.

If *democratic legitimization* is the goal, the principle of subsidiarity would gain vital importance in protecting Member States' competencies. If the European Court of Justice were to interpret the principle of subsidiarity narrowly and continue with its broad interpretation of Community competencies, a conflict could erupt between Community jurisdiction and Member States' jurisdiction. The courts of law in the Member States could argue that the powers conferred upon the Community are limited and that an expansion of those powers by means of interpretation does not lead to preemption of national law of Member States.[40] The system of parallel jurisdiction again would come into play and, thereby, automatically confirm the doctrine of enumerated powers. In fields of national law of Member States, the doctrine of supremacy would not be applicable. The difficulty with such a concept is that a system of double control in fields of mixed competencies emerges. As a primary concern, the European Court of Justice has to define the range of Community competence in that field. If the Court construes the principle narrowly, a national constitutional court could oppose the decision of the European Court of Justice, arguing that the range of competencies being defined on the European level is not consistent with national law because such competencies have not been conferred upon the Community by that nation-state.

In order to present this legal problem in terms of a constitutional economics analysis, numerous assumptions and facts first need clarification.[41] An economic analysis, applying methodological and normative individualism, does not start with the interests of nation-states as collective actors. Rather, the question is how the interests of *individual actors* are affected by different constitutional arrangements, and how the decisions of *collective actors* may be legitimized by individual actors. In

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39. *See* Petersmann, *supra* note 11, at 1126.

40. This exemplifies the potential for conflict between the German Federal Constitutional Court and the European Court of Justice after the Maastricht decision. *See* Herdegen, *supra* note 38.

41. For a more in-depth discussion of the following issues, see Buchanan, *supra* note 8; *see also* VIBERT, *supra* note 25.

short, constitutional choice problems must be evaluated from the individual actor's point of view.

The issue of allocating competencies on the different levels of government affects the principal-agent relations between European citizens, lawmakers, and governments. Constitutional economics provides a different viewpoint where state activities are concerned, compared to the position of legal science. Whereas the latter focuses on institutions that legitimize such state activities and control mechanisms embedded in the court system, constitutional economics focuses on the role of states as suppliers of public goods. From a consumer's viewpoint of such goods (i.e., the European citizen), the question arises as to which level the production of these public goods is best allocated in order to serve the needs of the buyers. This calculus must take into account cost comparisons and differences in preference structures. In addition, a constitutional economics analysis must distinguish between the comparative static model and a dynamic analysis. Such analysis must consider institutional competition that may produce results superior to those of rational choice by the lawmaker.[42] These aspects of a constitutional economics analysis then have to be integrated into a consistent framework. The main problem from a theoretical point of view

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42. *See generally* Ngo van Long & Horst Siebert, *Institutional Competition Versus ex-ante Harmonization: The Case of Environmental Policy*, 147 J. INST. & THEOR. ECON. 296 (1991) (comparing the benefits of centralized institutional arrangements with integrated national arrangements); Horst Siebert & Michael J. Koop, *Institutional Competition. A Concept for Europe?*, 4 SWISS R. INT'L ECON. REL. 439 (1990) (explaining the constitutional changes in the European Community that have created a more centralized governing system); Horst Siebet & Michael J. Koop, *Institutional Competition Versus Centralization: Quo Vadis Europe?*, 9 OXFORD REV. OF ECON. POL'Y 15 (1993) (comparing competition with harmonization as methods of achieving integration); Gerhard Prosi, *Europäische Integration durch Wettbewerb? Eine politisch-ökonomische Analyse*, *in* ORDNUNGSTHEORIE UND ORDNUNGSPOLITIK 119-35 (G. Radnitzky & A. Bouillion eds., 1991); Hans-Werner Sinn, *Tax Harmonization and Tax Competition in Europe*, 34 EUR. ECON. REV. 489 (1990) (arguing that tax competition may result in harmonization); Stefan Sinn, *The Taming of Leviathan: Competition among Governments*, 3 CONST. POL. ECON. 172 (1992) (assessing the consequences of a high degree of international capital mobility for the behavior of governments); Manfred E. Streit, *Dimensionen des Wettbewerbs: Systemwandel aus ördnungsokonomischer Sicht*, 44 ZEITSCHRIFT FÜR WIRTSCHAFTSPOLITIK 113 (1995); Manfred E. Streit & Werner Mussler, *The Economic Constitution of the European Community: From Rome to Maastricht*, 5 CONST. POL. ECON. 319 (1994) (discussing the introduction of social policies into the European integration process); Jeanne-Mey Sun & Jacques Pelkmans, *Regulatory Competition in the Single Market*, 33 J. COMMON MKT. STUD. 67 (1995) (analyzing elements of the regulatory strategy of the EC-1992 internal market programme); VIKTOR VANBERG, WETTBEWERB IN MARKT UND POLITIK—ANREGUNGEN FUR DIE VERFASSUNG EUROPAS (Friedrich-Naumann-Stiftung eds., 1994); Viktor Vanberg & Wolfgang Kerber, *Institutional Competition among Jurisdictions: An Evolutionary Approach*, 5 CONST. POL. ECON. 193 (1994) (outlining an evolutionary approach to the process of competition among institutions); Martti Vihanto, *Competition Between Local Governments as a Discovery Procedure*, 148 J. INST. & THEORETICAL ECON. 411 (1992) (analyzing the unforeseeable outcomes arising from competition).

is that vertically structured political and legal entities have not been a major field of research in the domain of constitutional economics.[43] Nevertheless, theories of fiscal federalism should be explored,[44] which range from simple models[45] to complex studies of institutional competition in the field of tax law.[46]

For a consistent framework, the analysis should begin with a comparative static analysis of different models allocating powers in a vertically structured political and legal entity. Dynamic aspects should also be included in the model. The following eight questions will be utilized:

(1) Do differences in preference structures exist and are those differences in line with existing nation-states?
(2) Can the activity in question be taken over by private enterprises?
(3) Are there economies of scale and/or of scope if the activity is being allocated on a higher level?
(4) Will allocation of competencies on the Community level lead to transaction cost savings?
(5) Are there positive or negative external effects if the activity is assigned to the lower level?
(6) If economies of scale and/or of scope exist, is it possible to find a solution outside the choice between community and nation-state levels?
(7) To which extent do agency costs rise in the case of allocating a competence on the higher level?
(8) What will be the effect of assigning a competence on a higher or lower level of institutional competition?

This set of questions refers to the allocation of competencies to the European or the Member State level. The problem of coping with a system of multiple jurisdictions is omitted. From a constitutional economics viewpoint, the solution for the conflict of laws has to be restated as follows: when an allocation of competencies between the European and the nation-state levels (or the international level and the

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43. *See* Homann & Kirchner, *supra* note 35, at 58-63.

44. *See* WALLACE E. OATES, FISCAL FEDERALISM 19 (1972) (defining fiscal federalism as "the determination of the optimal structure of the public sector in terms of the assignment of decision-making responsibility for specified functions to representatives of the interests of the proper geographical subsets of society"); Sinn, *supra* note 35 (explaining that centralization of economic decision-making is essential to Community development); Charles M. Tiebout, *A Pure Theory of Local Expenditures*, 65 J. POL. ECON. 416 (1956) (arguing that optimizing local government expenditures does not require a federal model); Gordon Tullock, *Federalism: Problems of Scale*, 6 PUB. CHOICE 19 (1969) (explaining democratic government through a theory of economic externalities).

45. *See* Tiebout, *supra* note 44.

46. *See generally* Charles McLure, *Tax Competition: Is What's Good for the Private Goose Also Good for the Public Gander?*, 39 NAT'L TAX J. 341 (1986); Sinn, *supra* note 35, at 97-100.

intergovernmental-cooperation levels) has been found that is optimal (at that particular time) in terms of the preferences of European citizens, this solution may become suboptimal if the given control mechanisms change over time (e.g., in terms of economies of scale, of differences in preference structures, of transaction costs savings, or of workability of institutional competition). The institutional task then is to create an adaptive mechanism for allocating competencies over time. Choices exist among various devices, ranging from constitutional changes to legislative and judicial decisions. Advantages can be gained by applying the chosen device for adapting the allocation of competencies to other purposes (which are similar to the adaptation problem but nevertheless distinct), such as the protection of the given allocation of competencies. The individual actor (i.e., the European citizen) is interested in adaptive mechanisms that ensure maintenance of the optimal allocation. However, this aspect alone is too static. Citizens may be interested in the results of a learning process that takes the shape of institutional competition. Thus, the problem is not simply to optimize allocation of competencies over time, but also to combine the advantages of that adaptation process with the positive results from institutional competition.

The framework for the constitutional economics analysis involves two levels: (1) on the first level, the issue of optimal allocation of competencies in vertically structured political and legal entities is at stake, and (2) on the second level, the adaptation processes of given competence allocations are scrutinized.

The connection between legal and economic analyses emerges when the legal analysis is founded on the goal of *democratic legitimization* of political and legal acts. Emphasizing the importance of democratic legitimization (as the German Federal Constitutional Court does), relates to the principal-agency problem in constitutional economics. However, the economic analysis does not function within the notion of given or absent democratic legitimization, but rather considers the changing cost situation in terms of agency costs.

VI. THE PRINCIPLE OF SUBSIDIARITY

When discussing the principle of subsidiarity as an instrument to prevent the uncontrolled transfer of competencies from the Member States to the Community, one should understand that the allocation of competencies is not at stake in article 3(b)(2) of the EC Treaty. Rather, it addresses the exercise of powers by the Community in fields of mixed competencies. The principle operates within a context defined by the doctrines of preemption, the supremacy of Community law, and the

qualified principle of enumerative powers. This context is important for the interpretation of article 3(b)(2) of the EC Treaty, because the test envisioned in that provision, namely whether or not the objectives of the proposed action can better be achieved by the Community, has to be conducted in light of the goal of the Treaties establishing the European Communities and the Maastricht Treaty. If the test concludes that the objectives of a proposed action can be better achieved by the Community, the national legal provisions are automatically preempted, with only the weak safeguards of sections 2 and 4 of article 100(a) of the EC Treaty at work. In terms of establishing a functioning control system, the first result of the analysis of the current multiple jurisdictions system under Community law is disappointing. The openness of the qualified doctrine of enumerative powers also intrudes on the application of the principle of subsidiarity. The objectives set by the Community provide the legal criteria used to decide whether a competence should be executed by the Community.

The second critical aspect of applying the principle of subsidiarity concerns the test itself, which refers to the question of whether the objectives of the proposed action can or cannot be achieved by the Member States. This part of the test may be related to the existence of economies of scale. Taking into consideration the variation in size of the Member States, the smaller Member States may not be in a position to reach the objectives of the proposed action if they act as individual nation-states. However, the text of article 3(b)(2) of the EC Treaty does not weigh the option that several small Member States could combine their efforts to reach the critical size for taking advantage of economies of scale and scope. If the provision is interpreted narrowly, the test leads to a negative result for those Member States that are not sufficiently endowed to achieve the objectives of the proposed action.

The third objection against the use of the principle of subsidiarity refers to the test component that compares economies of scale on the Community level and on the Member States' levels. The wording of the provision, "by reason of scale or effects of the proposed action," binds together the issue of economies of scale on the one hand and the issue of externalities on the other. The static scale-test provides that existing and predictable economies of scale are the measuring stick for deciding if the competence has to be executed on the Community level. The test, applied over time at different stages, may lead to different results so that changes in economies of scale allow for a repatriation of competencies to Member States. On the other hand, the test does not take into account dynamic aspects (i.e., it cannot weigh the potential effects of institutional competition).

The principle of subsidiarity channels and restricts the decision of whether the Community shall take action and thus execute a competence in an additional area. The choice is limited to activities either on the Member State level or the Community level. As a result, options to privatize certain activities fail to fall within these categories (question (2) above). Furthermore, models of cooperation of Member States on an intergovernmental basis also do not qualify (question (6) above).

The variation of preference structures between citizens of different Member States cannot be brought into play as an argument for assigning a competence on the Member States' level because it does not fit into the system of tests envisioned by article 3(b)(2) of the EC Treaty. However, this result could be cured by interpreting the externalities test in the following manner: The Community shall take action if, by reason of the effects of that action, the objectives of the proposed action can better be achieved by the Community.[47] The application of *argumentum e contrario* may offer the conclusion that in the case of differing preference structures between citizens of different Member States, the effects of actions taken by the Community are such that the objectives of the action cannot better be achieved by the Community. The effects of Community action would be to level the existing differences among preference structures.

The question of whether the principle of subsidiarity is a device that can be used to adapt a given allocation of competencies to changing conditions over time, and whether this principle can protect a given allocation of competencies, must be addressed separately. The *adaptive function* of the present provision of article 3(b)(2) of the EC Treaty depends on which changes are reflected by the principle of subsidiarity. The answer is mixed. The application of the tests leads to an adaptation in the allocation of competencies only if the changes have an impact on the tests to be applied under article 3(b)(2) of the EC Treaty. As mentioned above, article 3(b)(2) of the EC Treaty refers only to fields of mixed competencies, not to fields of exclusive competencies of the European Community. Thus, the adaptive function of the present use of the principle of subsidiarity is limited.

Whether the principle of subsidiarity can prevent an uncontrolled transfer of competencies to the Community level depends on: (1) the existing deficiencies of that principle, and (2) the application of the principle by the organs of the Community. First, the existing deficiencies should be examined. The tests envisioned in article 3(b)(2) of the EC Treaty do not conform with criteria that a constitutional economics

47. *See* EC TREATY, *supra* note 6, art. 3(b).

analysis would suggest. The tests are static; they do not take into account options outside the narrow set of options provided for in article 3(b)(2) of the EC Treaty. For example, the issue of institutional competition between the jurisdictions of Member States has no place if the principle of subsidiarity is applied as stated in article 3(b)(2) of the EC Treaty.

VII. CONCLUSION AND OUTLOOK

The analysis demonstrates that the principle of subsidiarity may be useful as a general guide in restricting the uncontrolled transfer of competencies from the Member States to the Community. If the principle of subsidiarity is applied in the American context, one can argue that it tends to prevent an undue transfer of powers from the state to the federal level. However, the application of constitutional economics as part of the analysis reveals numerous weaknesses of the principle. Rather than simply relying on the principle of subsidiarity, I suggest that the problem of vertical division of powers should be tackled in a more systematic manner, by utilizing the tools of modern constitutional economics.