

**The reform of energy regulation in the EU:  
The market as a norm**

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***Abstract:*** This paper analyzes the impact of the EU liberalization process on the evolution of energy service provision in Europe. As a result of EU-level liberalization, energy provision became significantly more market-oriented. The paper demonstrates the usefulness of the market as a norm that as part of a Brussels-centered reformist political strategy through most of the 1990s. It refutes alternative explanations in terms of market forces, incremental bargaining, and paradigm change. Even after the completion of energy liberalization by 2007, politics and actors' evolving strategies will thus continue to play an important role in changing trends of energy regulation.

## **The reform of energy regulation in the EU:**

### **The market as a norm<sup>1</sup>**

In June 1996, the European Council of Ministers unanimously adopted a legislative text calling for a gradual liberalization of electricity supply in the European Union. Behind the façade of unanimity and the moderate tone of the intergovernmental compromise, the agreement represented a major step at the end of an overdrawn and rough negotiation process – almost four years after the “1992” inauguration of the Single European Market, and nine years after the original proposal of an Internal Energy Market for electricity. It set a mandatory timetable for the progressive entry of new competitors into a previously closed electricity supply industry and for an unprecedented availability of consumer choice for big (industrial) electricity consumers. Two years later, in 1998, a copycat text was passed in order to liberalize the European gas sector. And in June 2003, new legislations were adopted mandating a full liberalization of the energy sector by 2007 – for both gas and electricity and for all categories of consumers.

While the practical consequences of the 1996 electricity directive remained uncertain at the time, the passage of this legislation was a surprising reform and a watershed for public utility regulation in Europe. Until the 1990s, the electricity supply industry was highly entrenched in each country’s political economy. Since the early years of European integration, member states had been notoriously eager to preserve national autonomy in the energy sector, and had quietly filed away numerous proposals for a comprehensive European energy policy. The 1985 White Paper on the Internal Market

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<sup>1</sup> This paper will appear as chapter 6 of my forthcoming book: Market Ideas for Political Power: The European Union’s Quiet Revolution (Ithaca: Cornell University Press, 2006).

did not even mention energy. Typically, the early 1990s scholarship on the topic of the Internal Energy Market saw it as an illustration the “limits of 1992”.<sup>2</sup> Thus, the fact that the objective of an “Internal energy market” was progressively grafted on the Single Market agenda in the 1990s is remarkable. Why member states finally agreed to a gradual form of liberalization over electricity supply deserves a careful explanation.

This chapter argues that a key factor of change was the European Commission’s pursuit of its integrationist agenda through the means of the market as a norm. The advocates of European-level liberalization appealed to this norm by saying that energy supply was economically “inefficient”. As a normative model, the market is first and foremost a promise of superior efficiency. As defined by economists, efficiency (or, more specifically, Pareto efficiency) is reached when the individual welfare gains from trade are maximized. The appeal of this norm is not simply a matter of ideology by self-interested actors. In advanced industrial societies, it is hard to argue against the pursuit of efficiency. The market appears almost like a state of nature and is rarely recognized as an overtly normative vision. Yet it is possible, in a sense, to isolate the normative appeal of the market in sectors or policy areas where the market is *not* an overwhelming substantive force or constraint. The Internal Energy Market is especially illuminating as a control case against the utilitarian explanation of the European Union’s quiet revolution in terms of market and technological change.

Precisely because the functional rationale of energy liberalization was objectively not as obvious as in a sector like finance, the politics of institutional change can be highlighted very starkly. Significant change occurred in the highly entrenched

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<sup>2</sup> For earlier skeptical views about the prospects of electricity liberalization, and liberalization in general, see: Stephen Woolcock et al., Britain, Germany, and 1992: The Limits of Deregulation (New York: Council on Foreign Relations, 1991); Stephen Padgett, “The Single European Energy Market: The Politics of Realization,” Journal of Common Market Studies, vol. 30, no. 1 (March 1992): 53-75.

institutional framework within which the industry was embedded, i.e. precisely where it was to be least expected. The advocates of the Single Market in the 1980s and 1990s used this norm to draw up reform proposals for sectors where competitive forces were not initially present, like the electricity supply industry. They fought a long battle of ideas, but over time they managed to shift the normative underpinnings of sectoral organization. In strictly utilitarian terms, the economic rationale for market reform was weak. In institutionalist and constructivist terms as well, there was virtually no institutional development or learning process at work prior to the initiatives of liberalization advocates. Thus, the investigation of the driving forces of change in the electricity sector casts a very useful light on the causal dynamics of the European Union's quiet revolution. The market manifested itself not as a competitive pressure or as a best practice, but really as a normative weapon in a political battle of ideas.

The outcome of this battle was a process of controlled liberalization under EU oversight. Energy liberalization did occur *and* the process was gradual and carefully monitored by political actors. Depending on the perspective that we adopt, then, the cup can appear as half-empty or half-full. It would be rash to describe energy liberalization as an unstoppable tide, but it would be equally misleading to minimize its significance. It is therefore very important to explain both terms of this liberalization equation. The European Union, and especially the European Commission, stepped into energy politics and regulation by becoming the watchdog of liberalization. Since the new legislation basically mandated a radical re-organization of a highly institutionalized sector of the economy in many member states, there was no guarantee that the member states would fully live up to their commitments. Once the process was under way, however, many sectoral actors wanted to operate in a predictable environment and governments were

under increasing pressure to play by the new rules. Precisely because the process was slow and because good will could not be taken for granted, the oversight role of the European Union was solidly established in an area previously organized at the national level and beyond the scope of market competition.

Altogether, this chapter offers a strategic constructivist explanation as against alternative modes of explanation in terms of interests, ideas, and institutions. The argument proceeds in five steps. Section I presents the puzzle of electricity liberalization. Section II briefly summarizes the main events in the complicated and protracted history of electricity liberalization. Section III shows how the advocates of the Internal Energy Market were able to re-shape the institutional sphere of energy supply around the norm of the market. Section IV shows how this interpretation takes care of important shortcomings of alternative explanations couched in terms of economic interests, consensual knowledge, and institutional trajectory. Section V spells out some implications of the argument for the study of norms and of their effects in politics.

## **I. Reformist action in a static environment**

The “1992” process in the electricity sector took place against the background of a long period of sectoral stability across all the member states. Electricity supply was organized everywhere in Europe according to the public utility model. Since electricity

supply was network-bound and widely regarded as a natural monopoly, regionally- or nationally-based electricity companies usually enjoyed exclusive concessions on the public domain. They were taking care of the production, transportation, and distribution of electricity within their allotted areas of operation. Competition was absent and there was a preference for national autonomy in the supply of energy sources to the sector. Furthermore, the level of uncertainty in this sector was relatively low. Since electricity is a relatively simple and well-established basic commodity, the industry is not subject to erratic changes in demand or fast technological change. Its investments are highly capitalistic and carefully planned on a medium- to long-term basis. This is not to say that there were no important supply shocks and technological innovations in the 1980s and 1990s, especially with the considerable decrease in real-term oil prices and the advent of low-cost technology for gas-fired and combined cycle power generation. Yet these trends have been slowly progressing, and in terms of overall energy utility portfolios, their effects can only be felt over the long run. Thus, the sudden emergence of a legal-regulatory framework for sectoral competition at the European level represented a major departure from traditional ways of thinking and of doing business in this sector.

This chapter analyzes this new development as part of the European Union's quiet revolution. Actors pushed for the liberalization of electricity supply in the wake of the Single Market initiative. The market was branded as a normative ideal in a sphere where it was originally almost absent. Typically, electricity liberalization has been explained in terms of the evolution of actors' interests, historical trends, paradigmatic shifts, and institutional development.<sup>3</sup> By contrast, the explanation offered in this chapter grants pride of place to the pro-market militancy of political actors in and around the European Commission. Starting from an initially very static situation, these actors have managed to

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<sup>3</sup> Each mode of explanation will be more thoroughly examined in section IV below.

reshape the debate about and eventually the structure of European electricity supply. In this view, the process of liberalization followed a particular logic that resulted from the implementation of a particular strategy of action invented by the European Commission in the mid-1980s. The movement of economic liberalization in Europe needs to be understood as part of this innovative political movement, rather than exclusively in terms of external structuring factors – such as ideas about the economic efficiency and competitiveness, the interplay of national interests, or the weight of institutions.

There is an important sociological subplot underlying the story of electricity liberalization, namely of the construction of electricity policy as a “field” of European policy, with its own set of dominant actors, purposes, and practices. In this process, the negotiations and conflicts of interests took on important symbolic as well as material aspects. The role of Commission officials was central to the dynamics of field construction. As we shall see, Commission officials acted so as to crystallize the Internal Energy Market debate around a nexus of norms and practices. These institutional norms and practices are themselves in flux, however. Far from always shaping interests in a uniform manner, they acquire a multifarious dynamic of their own. These cognitive elements can be seen as complementing interest-driven behavior and orienting it, especially as they help to shape inherently fluid interests in a situation of uncertainty. But they are best understood as a set of cognitive elements that can be ordered and mobilized by political actors. Although the normative elements of field construction can be analytically isolated, strategic action gave a crucial purposive orientation to that sociological dynamic.

In the hands of actors within the European Commission, liberalization became not only a policy goal in itself but also a means to further regional institutional integration.

European Commission officials in Brussels tackled the task of reorganizing the field of electricity policy in Europe. They heavily relied on the acquired force of certain symbolic constructs, including the force of evolving legal norms. They compensated their obvious lack of material power and resources by developing a coherent panoply of normative arguments in favor of liberalization and by carefully constructing alliances within the domestic political arenas of the member states. Over time, they effectively eroded the dominance of well-entrenched domestic interests at the level of the member states. They made important allies at the national level and built political momentum that considerably enhanced the initially dim prospects of economic liberalization in the electricity sector and in the energy sector more generally.

This does not mean that Commission officials made no mistake or that they obtained everything they wanted. In their efforts to fundamentally change the norms of energy supply, Commission officials encountered important difficulties and opposition. Within the Commission itself, not everyone was equally convinced of the virtues of a more open and competitive electricity supply industry. The Commission's early proposals were not well received by most member states. There were long moments of inertia and stalemate in this process. As difficulties arose, the Commission was led to modify the content of its liberalization proposal. This explains why the eventual compromise solution, however significant, is not as "liberal" as some Commission officials would have liked (especially within the Competition Directorate DG Competition). Over time, however, the Commission's political strategy did alter the terms of the debate. The Council of Ministers never completely withdrew its support to the idea of "building an Internal Energy Market". In this context, the Commission was able to retain the initiative and to make sure that its proposal remained the only game in

town. Thus, the Brussels negotiation process continued and swayed the configuration of the field of electricity policy across Europe. Despite the important odds against electricity liberalization at the outset, this reconfiguration made it possible for the Commission's revised proposal to eventually gain the support of the Council and to prevail over an increasingly marginal opposition.

By tracing the various steps that led to the 1996 directive, this chapter demonstrates the importance of political strategy in driving institutional change. Market forces were not as omnipresent in the dynamics of reform as they were, for example, in the case of finance. While the advocates of electricity reform consistently appealed to market rationality, their success cannot be explained in terms of the sheer push of economic interests or the alleged diffusion of a free market consensus. Unlike the financial sector for which the arguments of market reformers were increasingly borne out by self-reinforcing market dynamics, the "objective" reasons for electricity liberalization were not nearly as pressing as in a case like finance. To identify economic interests as the key factor behind liberalization really makes no sense, since it ignores the important economic interests that were radically antagonistic to liberalization. Likewise, very few sectoral actors were convinced at the outset of the inherent superiority of the market as a norm of sectoral organization. In order to understand what caused electricity liberalization, we have to look at the nuts and bolts of the decision-making process that led to the adoption of the 1996 directive.

Electricity liberalization is not an isolated example, however. A number of collective services that used to be provided on an exclusive basis by public or semi-public corporations in each member state were de-monopolized and liberalized. A comprehensive examination of all these examples is obviously beyond the scope of this

chapter. Yet there appears to be striking similarities in the unfolding of European-level liberalization processes. Unlike financial reforms, European reforms of collective services largely preceded the evolution of national regulation.<sup>4</sup> Most evidently, the liberalization of the natural gas sector was directly modeled on the electricity directive. While objective reasons for introducing competition in sectors like telecommunications were more salient than in the case of electricity, there are reasons to believe that market pressures alone would not have been sufficient to warrant full-fledged liberalization. The reliance on a network infrastructure was a crucial and unavoidable aspect of service provision in telecommunications, railroad transportation, postal services. The market forces that pushed in the direction of liberalization were generally less powerful in these sectors than in a sector like finance – except maybe in some segments of the telecommunications sector. Thus, the case of electricity has a more general significance for understanding other processes of liberalization at the European level.

## II. The saga of electricity liberalization

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<sup>4</sup> There is a large volume of secondary literature and research on the liberalization of European collective services, including: Peter Cowhey, “Telecommunications,” Gary Clyde Hufbauer, ed., Europe 1992: An American Perspective (Washington: Brookings, 1990); Reinhard Ellger, “Telecommunications in Europe: Law and Policy of the European Community in a Key Industrial Sector,” in William James Adams, ed., Singular Europe (Ann Arbor: University of Michigan Press, 1993); Wayne Sandholtz, “Institutions and Collective Action: The New Telecommunications in Western Europe,” World Politics, no. 45 (January 1993); Hervé Dumez et Alain Jeunemaitre, “Political Intervention v. L’Etat de Droit Economique,” Essays in Regulation, no. 5 (Oxford: Regulatory Policy Institute, 1994); Volker Schneider, Godefroy Dang Nguyen and Raymund Werle, “Corporate Actor Networks in European Policy-Making: Harmonizing Telecommunications Policy,” Journal of Common Market Studies, vol. 32, no. 4 (December 1994): 473-498; Edith Brenac, “L’Exemple des télécommunications,” in Bruno Jobert, ed., Le Tournant néo-libéral en Europe (Paris: L’Harmattan, 1994); Susanne Schmidt, “Commission Activism: Subsuming Telecommunications and Electricity Policy Under European Competition Law,” Journal of European Public Policy vol. 5, no. 1 (March 1998); David Levi-Faur, “Governing Dutch Telecommunications Reform: State-Business Relations in the Transformation of National Policy Regime to (European) Embedded Policy Regimes,” Journal of European Public Policy vol. 6, no. 1 (March 1999).

In substance, the 1996 European directive mandating “gradual liberalization” laid the basis for an Internal Energy Market for electricity.<sup>5</sup> Until that directive, only the legally designated utilities in the member states had monopolistic rights to engage in the supply and commerce of electricity. Typically, third parties (i.e., non-chartered electricity producers, consumers or distributors) did not have direct access to the grid and were not allowed to contract with suppliers or customers of their choice. The directive changed the status quo not only by mandating a certain level of “third-party access” (TPA) to the electricity networks, but also by ending the monopoly rights for the construction of power lines and power stations.<sup>6</sup> In the first phases of market opening, only certain “eligible” customers will be concerned, and the task of defining criteria of eligibility is left to the discretion of national legislatures.<sup>7</sup> In order to diffuse and postpone possible disagreements in implementing the European legislation, the Council set the relatively remote date of 2006 for a review of progress toward the objective of an Internal Energy Market.

A first difficulty resides in assessing the significance of that text. In hindsight, it is clear that the 1996 electricity directive was not just an isolated attempt to marketize the energy sector. But only the future evolution of the European energy sector will tell us whether it was actually a landmark blueprint of change or a parenthesis between two periods of non-market sectoral organization. Some skeptical observers noted that the

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<sup>5</sup> Directive 96/92/CE of the European Parliament and of the Council concerning common rules for the Internal market in electricity, *Official Journal of the European Communities*, January 30, 1997.

<sup>6</sup> Third-party access (TPA) means that networks are open to third parties, with freer entry on the supply side and the possibility for customers to choose from a variety of electricity producers.

<sup>7</sup> Only big industrial customers consuming more than 100 GWh per year were initially to be considered as eligible. But the member states may also designate other consumers – even household customers – and electricity distributors as eligible. To provide for an equivalent degree of liberalization in all of the member states, the directive required the member states to conform to certain quotas at each stage of market opening. These quotas were based on the EU-wide annual consumption profile of various categories of industrial consumers (1999: >40 GWh, 2000:>30 GWh, 2003: >9 GWh). As a consequence of these incremental quotas, the member states had to gradually open their markets from around 25 percent of national consumption in 1999 to around 33 percent in 2003.

result of the 1996 compromise was to legitimate rather than remove the pre-existing obstacles to market competition in various countries. Advocates of liberalization within the European Commission and elsewhere believed nonetheless that, once the directive is implemented at the national level, market forces would be unleashed and would push electricity supply industry in the direction of greater openness. Several member states (Finland, Germany, Spain, the Netherlands, Sweden and the United Kingdom) quickly indicated that they would move far beyond the minimum thresholds and intended to fully open their markets. There is no doubt that the electricity directive contains a great degree of flexibility and has been described as “à la carte” when compared to other more sweeping examples of EU-level reforms. It delineated a careful and incremental schedule of market opening that was initially limited to particular segments of the market. Despite these limitations and in view of subsequent events, the directive now appears as a fundamental reform that hardly anybody expected in 1992 when the first Commission proposals were submitted.

In fact, the path to the final text of the directive in 1996 was neither straight nor uneventful. The directive proposal was introduced by the European Commission in 1992. This Commission initiative was in and of itself a rather surprising development and the result of a rather convoluted process. While liberalization in the electricity sector was only part of a broad movement of market-building encapsulated in the “1992” objective, the electricity sector was deliberately not mentioned in the White Paper on the Internal Market at the origin of the Single European Act. In the mid-1980s, the idea of a common energy market was not high on the agenda. On the contrary, there were bitter memories of failed attempts to build a common energy policy, since the early days of the European Community and through the oil shocks of the 1970s.<sup>8</sup> Under the goad of a 1986 Council

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<sup>8</sup> In particular, Euratom, which was originally designed as the spearhead of a European energy policy, did

resolution, however, a piecemeal approach to electricity liberalization began to emerge. In 1988, the European Commission introduced a green (working) paper about the Internal Energy Market, proposing price transparency and freer transit of electricity across borders.<sup>9</sup> Two directives were to be adopted, in 1990 and 1991, to fulfill these significant, yet relatively modest goals.<sup>10</sup> However vaguely defined at that stage, the Commission's objective to liberalize the electricity sector triggered already important reactions by both sectoral and state actors: In 1989, the member states' utilities and associations set up a trade association in Brussels – Eurelectric – with a mandate to defend their common interests. Also, the German and French governments passed a joint communiqué at their summit of November 1989 that included a protocol on energy policy, in which they tried to set strict boundaries for the liberalization dynamic – they accepted the principle of “free transit” of electricity across Europe, but only if mediated and controlled by the utilities; and they declared their opposition to the new concept of “third party access” as exemplified by the British electricity deregulation program.

In the early 1990s, it was far from clear that electricity liberalization would continue beyond the fairly limited steps which had already been agreed upon. Any attempt to further liberalize this sector was risky, if only because of the predictable political opposition to this process. After airing in 1991 a first concrete proposal for TPA and some internal hesitations about the best method to implement it, the Commission decided not to act under its discretionary competition law prerogatives (i.e., by way of an

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not live up to the expectations of its early supporters like Jean Monnet. One analyst concluded, at that time, that there was a “general agreement that energy policy must be ranked as one of the Community's major failures.” (See Padgett, “The Single European Energy Market,” p. 55). For a historical perspective on European electricity policy, see Janne H. Matlary, Energy Policy in the European Union (London: Macmillan Press, 1997).

<sup>9</sup> Commission of the European Communities, The Internal Energy Market, reprinted in Energy in Europe, special issue (Luxembourg: Office for Official Publications of the European Communities, 1988): 17-18.

<sup>10</sup> Council Directive 90/377/EEC (June 29, 1990); Council Directive 90/547/EEC (October 29, 1990).

Article 90 directive). Instead, it submitted in 1992 a first directive proposal subject to the Council's and the European Parliament's approval (under the new co-decision procedure as defined by the Maastricht Treaty).<sup>11</sup> Yet, in the face of huge opposition on the part of important players, the proposal soon appeared moribund. Many observers interpreted the Maastricht treaty, which reasserted national prerogatives over energy policy, as an important setback for proponents of a European energy policy, including electricity.

As it turned out, however, the liberalization process in electricity did not stop there. The member states at the Council expressed their intention to proceed with liberalization and the relevant actors continued to negotiate actively on this issue. The Commission's proposal was the object of heated negotiations and numerous important amendments by the Council of Ministers from 1993 to 1996. The enlargement of the European Union to Sweden and Finland in 1994 gave a second wind to the idea of Third Party Access, while Germany and the Netherlands incrementally adopted official positions that were much more favorable to liberalization. The French government mandated the Ministry of Industry to set up an expert commission in order to draft a report with policy recommendations on the sectoral governance of electricity in France.<sup>12</sup> Following this report, France proposed its own brand of liberalization, the "single buyer" (SB) concept. While accepting the principle of market competition for electricity generation, the proposal reaffirmed the role of monopoly utilities as the sole operator of the technical networks for transportation and distribution of electricity. This new proposal did not satisfy the Commission, but the Council decided to fudge the issue and mandated that the SB proposal be drafted into the legislation in conjunction with TPA.

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<sup>11</sup> The Commission's directive proposal is reproduced in: Official Journal of the European Communities, March 14, 1992

<sup>12</sup> The report was drafted and published in January 1994 by the French Ministry of Industry as: Ministère de l'Industrie, Rapport du groupe de travail, La réforme de l'organisation électrique et gazière française. Paris: Ministère de l'Industrie, 1994. (Hereafter, we refer to this report as the Mandil Report.)

For a while, the anti-TPA stance was unexpectedly reinforced by two ECJ rulings that leaned in favor of the principle of public service, in the 1994 Corbeau and Almelo cases. In March 1995, the Commission issued a Council-mandated report comparing the TPA and SB systems, concluding that the two systems could be adopted in conjunction only if they guaranteed “equivalent results” in terms of market opening. But the question remained politically sensitive and negotiations kept stalling. The increased powers of the European Parliament under the co-decision procedure also created new hurdles in the policy-making process. At the Kohl-Chirac summit of December 1995, the French and German governments had agreed to maintain cohesion and not let each other be outvoted in the Council on the issue of electricity liberalization. Therefore the prospects of a denouement to the saga of electricity liberalization looked even bleaker, since the French and German governments held diametrically opposite positions on the most contentious aspects of the proposal. Until very late in the process, it was not clear that there would be any genuine liberalization of electricity supply, let alone one that was acceptable to all parties. Many had almost given up any hopes of ever reaching agreement on the Commission’s proposal.

The situation dramatically changed in the first half of 1996, when France and Germany came up with a compromise proposal that lifted the most important political obstacles to the directive. Based on the existing directive proposal, the governments of these two protagonist states in the debate on electricity liberalization had bilaterally negotiated a common solution to the remaining disagreements. The text of the directive was accepted and unanimously adopted by the Council of Ministers on June 21, 1996. The Council resolution was then sent to the European Parliament and definitively passed almost without any further amendments in December 1996. The dominant sentiment at

the time of the second reading at the European Parliament was that the carefully crafted compromise was the object of a fragile political balance; any further amendments would seriously thwart the chances of a directive ever seeing the light of day.

### **III. The re-shaping of an institutional sphere**

This section distinguishes four broad components in the strategy of electricity reform developed by its proponents, especially within the European Commission. First, they cautiously incorporated the energy sector into the “1992” reform agenda, thus opening an inroad in the forest of institutional obstacles that stood in the path of reform. Secondly, they undertook to re-shape the expectations of the main actors of European electricity supply in such a way as to present the process of liberalization as an inescapable movement. Thirdly, they resorted to a variety of more typical carrots and sticks tactics that were available to them. Fourth, they proved ready to sacrifice the purity of their liberalization objectives for the sake of reaching compromise. Altogether, the pragmatic development of this strategy explains both the extent and the limits of the electricity reform achieved by its proponents.

#### *Opening an inroad*

With the Single Market program, the European Commission was suddenly upgraded from a marginal to a potentially central role in determining the organizational characteristics of various sectors of the European economy. Yet the Commission faced a

series of difficulties, due to constraining institutional legacies and circumstances. First, the Single Market objective built on a series of technical proposals for market opening – the White Paper on the Internal Market – but did not specify the full range of economic activities to be covered by the Single Market. The Commission’s formal powers remained weak, except in certain domains such as competition policy.<sup>13</sup> There was also the fact that the Commission’s sectoral objectives were not always congruent with the new objectives expressed in the Single Market program. Adjustments had to be made on a sector-by-sector basis, and this was not necessarily easy.

On energy issues more specifically, the Commission’s thinking (as expressed by the Directorate General for Energy) was marked by a policy legacy that was more tainted by interventionism than by liberalism.<sup>14</sup> While the European Community had always been involved in energy policy since the early days of the European Coal and Steel Community in the 1950s, there was no exclusive Community competence in the area of energy policy. Historically, European policy objectives consisted of sheltering the energy sector from short-term market uncertainties and enhancing the general objective of security of supply. These goals had been promoted first through the European Coal and Steel Community for the provision of coal, and later through Euratom for the promotion of nuclear power. The Commission’s limited formal prerogatives had not been sufficient to formulate a comprehensive European energy policy, and Commission initiatives in this vein had been consistently thwarted by divergent national energy policies, especially in response to the 1970s oil shocks.

In the face of such obstacles, Commission officials’ attempts to capitalize on the

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<sup>13</sup> David Allen, “Competition Policy: Policing the Single Market,” in Helen Wallace and William Wallace, eds., Decision-Making in the European Union (Oxford: Oxford University Press, 1996).

<sup>14</sup> On the ambiguities of European energy policies, see: Francis McGowan, "Conflicting Objectives in European Energy Policy," in Colin Crouch & David Marquand, eds., The Politics of 1992: Beyond the Single European Market (Oxford: Basic Blackwell, 1990).

agenda of the SEM were not certain to succeed. The first step was to obtain a green light from the Council for the establishment of an Internal Energy Market, which came in 1988, in the form of a Council request to draft a proposal. While energy was not one of the areas covered by the White Paper, the Cecchini Report contained a section about the “costs of non-Europe” in the energy sector. As a matter of principle, a majority of member states were understandably in favor of reducing these costs. France, in particular, was eager to secure European export markets for its surplus nuclear power at that time. This was based not on a grand design of Europe-wide corporate expansion, but on the immediate and well-understood self-interest of its public utility Electricité de France (EDF), whose staff participated in the elaboration of the Cecchini Report.<sup>15</sup> Thus, by engaging the drive toward an Internal Energy Market at the Council of Ministers, France probably triggered, albeit involuntarily, a broader process of liberalization.

Following the Council’s request, the college of commissioners mandated DG Energy to draft a comprehensive working paper on energy liberalization.<sup>16</sup> That document reflected the ambivalence of many Commission officials in charge of energy toward the prospect of an Internal Energy Market. While the green paper did not close the door to the Internal Energy Market, it listed so many obstacles that it seemed unlikely that the Commission would proceed very far with market liberalization in this sector. DG Energy officials did not want to alienate their clients within the electricity supply industry. Opponents of large-scale structural change in the electricity sector felt generally comfortable in their claim that energy policy was a national prerogative, and this could

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<sup>15</sup>Later France turned against liberalization, when it became clear that electricity liberalization directly threatened its national monopoly and technical adjustment capacities. The EDF strategy was gradually clarified over time in the late 1980s, as it became apparent that the Internal Energy Market was not merely going to be about the interconnection of national electricity grids.

<sup>16</sup>Commission of the European Communities, *The Internal Energy Market*, reprinted in *Energy in Europe*, special issue (Luxembourg: Office for Official Publications of the European Communities, 1988)

only be reinforced by a 1992 provision of the Maastricht Treaty, requiring unanimous voting for issues of Europe-wide energy planning.

After the first and least contentious steps towards creating the Internal Energy Market (the transit directive and the price transparency directive), proponents of a more rapid and radical liberalization were gaining ground within the Commission. In particular, the position of Commissioner Leon Brittan and his Commission staff in charge of competition policy was boosted by the Court of Justice's early 1990s rulings in favor of the Commission's use of Article 90.3 to bring about competition in the area of telecommunications. DG Competition began attacking some special conditions awarded to certain interests, by stigmatizing the special electricity contracts granted to public sector or big firms in various countries. Some breaches of European competition law were relatively easy to point out, and this was the area in which the Commission's enforcement powers were most extensive. Meanwhile, the opponents of liberalization were slow to react to developments at the European level. For a long time, they did not have the mandate, the collective action capacity, nor the expertise to issue counterproposals at the European level.

In the long run, however, an agenda of electricity liberalization based only on the application of regular competition law was bound to reach certain limits. It is doubtful that liberalization could have been carried through in relatively short order simply by applying competition law formulas. Utilities were quick to redress the most glaring distortions of competitive pricing between their customers, and in many cases the discontentment of big electricity consumers in the face of high electricity prices could be appeased with the help of special discounts ("sweet-heart deals"). As for the possible use of Article 90, it was unclear that the European Court of Justice would support an

aggressive enforcement strategy on the part of DG Competition. The risk of alienating the member states on a politically sensitive issue such as energy policy was important, whereas the need for more competition was much less obvious, from a technological viewpoint, than in the area of telecommunications.

The novelty of the electricity liberalization project was that it potentially goes far beyond the concern of striking down trade barriers between the member states. The member states would have to agree upon common rules of electricity supply organization, which was virtually impossible – precisely because of the absence of a common structural framework of electricity supply (unlike the PTT model in telecommunications). In its endeavor to create a single market for electricity, the Commission had to depart dramatically from legal principles and rules of thumb such as “mutual recognition”, and was led to propose a coordinated cross-national reform of the organization of electricity supply.<sup>17</sup> Thus, the implementation of this agenda was bound to be challenged and possibly overturned, unless the Commission was able to build up support for its agenda and, crucially, to draw potential opposition to accept its terrain of battle. This would not have worked if the Commission’s agenda had not latched onto a broader strategy of changing the political-economic environment of electricity supply.

### *Re-shaping actors’ expectations*

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<sup>17</sup>Commission of the European Communities, Energy in the European Community (Luxembourg: Office for Official Publications of the European Communities, 1991). The Internal Energy Market objective was broken down into several sub-goals: getting rid of economically inefficient subsidies, especially those to non-competitive national coal industries; breaking the monopolistic structures that allow excessive slack in utilities and the extraction of rents on social welfare; promoting decentralized and market-driven technological innovation, especially technologies of energy efficiency, combined cycle and renewable energies.

In order to advance the Internal Energy Market, Commission officials started to fundamentally re-shape the context of expectations within which actors articulated their interests and strategies. The first step was to work out internally what strategy the Commission itself wanted to adopt. Traditionally, DG Energy was careful not to offend national utilities and governments and more reluctant to use competition law as basis for creating an internal market for electricity. But around 1990, the internal dynamics of the Commission changed somewhat. The new Portuguese Commissioner for energy, Antonio Cardoso e Cunha, moved strongly in favor of liberalizing the electricity sector. Perhaps fearing that Leon Brittan, his very active British colleague for competition, would capture the initiative on the Internal Energy Market, Commissioner Cardoso moved radically in favor of electricity liberalization and formed a special Internal Energy Market task force that reported directly to his cabinet – completely over the head of DG Energy’s staff, who should have normally been in charge of drafting the directive proposal.<sup>18</sup> Once the college of commissioners resolved the procedural issue by excluding the idea of an Article 90 directive, that task force was wholly in charge of drafting and amending the Commission’s proposal.

In order to induce state and sectoral actors to gradually accept the Commission’s proposal, it was necessary to make these actors believe that a preservation of the status quo was out of the question and to convince them that it was in their best interest to negotiate a compromise. In the European political climate of the mid-1980s, the idea of an Internal Energy Market acquired political momentum. The problem for Commission actors was to find the Achilles’ heel in the electricity sector’s institutional armor. The

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<sup>18</sup>Interview with Commission official. Cardoso’s activism did not fare very well among DG XVII bureaucrats and within the energy industry. See for example a very skeptical view on TPA originating from two Commission officials “expressing their own personal views”: Guy de Carmoy and Gerard Brondel, *L'Europe de l'énergie: objectif 1992 et perspective 2010* (Luxembourg: Office for Official Publications of the European Communities, 1991).

price differential problem was a good candidate. It figured prominently in the Commission's agenda for electricity liberalization.<sup>19</sup> This was a politically sensitive issue in the context of an emerging Single Market, especially in countries where electricity prices were high, whose governments were subject to pressure from big electricity-consuming industries and to the fear that these industries might relocate in low-price regions of Europe. The price of electricity varied within as well as across countries. In each national context, electricity supply has been subject to a number of economic, regulatory and political incentives and constraints.<sup>20</sup> Everywhere in Europe, electricity rate structures, somewhat like tax structures, had been the object of governmental intervention and in favor of certain categories of producers and consumers. Complex patterns of cross-subsidization prevailed, ranging from subsidies to favored domestic industries (e.g., regional and industrial development subsidies in France), or to "clean" or declining energy sources (e.g., environmental regulations and coal subsidies in Germany). Different national models of economic infrastructure and development across Europe, structured around different policy objectives, were largely responsible for the important price differentials that existed for any given category of consumers.

It is important to understand that technical methods to calculate prices and costs often incorporate what organizational sociologists call "ceremonial" elements.<sup>21</sup> Such

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<sup>19</sup>For an agenda of change set by the Commission, see Commission of the European Communities, Energy: A Challenge for Europe and the World (Brussels: Commission of the European Communities, 1992): 7-8.

<sup>20</sup>See the following passage from the French Mandil Report, which departs dramatically from the otherwise technocratic style of this document: "Electricity and gas systems are not only rational constructs, but are also the fruits of history, geography and geology. [...] There is no reason whatsoever for gas and electricity distribution to take the same forms in a country (Germany) that was built as a federation of towns, and in one (France) that owes its existence to the centralizing will of the *Capétien* kings."

<sup>21</sup> John W. Meyer and Brian Rowan, "Institutionalized Organizations: Formal Structure as Myth and Ceremony," in Powell and DiMaggio, The New Institutionalism in Organizational Analysis.

elements not only play the functional role of market signals, but also serve the purpose of enhancing the legitimacy of various energy-planning concepts. The apparently neutral cost-accounting and price-setting techniques used in the sector do not reflect only economic factors. Economic efficiency is obviously an important consideration, but there are also other concerns like security of supply, public service obligations, environmental concerns, etc. This explains in large part the conundrum of cost and price structures in the electricity sector. The fact that the Commission decided to examine these structures as a “test case” for the Internal Energy Market fits nicely with the sociologist’s notion that technical expertise is often used as a method to de-legitimize ceremonial elements. A harmonization of energy price structures, in effect, would involve a direct questioning of the cost-accounting elements which are not directly warranted by efficiency-based considerations.

The Commission’s choice to first investigate energy price structures was politically astute. While many pricing techniques could be criticized as incoherent or archaic, their underlying energy-planning concepts were so highly institutionalized that a frontal attack would have failed. From the beginning, therefore, the European Commission singled out price differentials as the single most important rationale for the enactment of liberalization reforms.<sup>22</sup> More surreptitiously, Commission officials often cast the utilities as monopolistic “rent-seekers,” whose cushy rents would be hurt by competitors in the supply of electric power.<sup>23</sup> The existence of monopolistic rents

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<sup>22</sup> Commission of the European Communities, The Internal Energy Market, reprinted in Energy in Europe, special issue (Luxembourg: Office for Official Publications of the European Communities, 1988): 17-18.

<sup>23</sup> See for example: Speech by Energy Commissioner Cardoso e Cunha, “The Unavoidable Future” (April 1992), in Commission of the European Communities, Energy in Europe 19, July 1992 (Luxembourg: Office for Official Publications of the European Communities, 1992). The Commissioner characterized the structures as monopolistic or oligopolistic and thus naturally bent on “protectionism;” “If I were in charge of one of the monopolistic undertakings in the energy sector I would very likely do exactly as they do.” (p. 5)

implies that the regulators are “captured” by the utilities and that the regulated prices are excessively favorable to the industry on a systematic basis. While this accusation was hard to prove, it made intuitive sense. The argument that utilities were protecting their cushy rents was not overly developed, but underlay pro-liberalization discourse as a politically useful characterization of the utilities and their behavior.

This pro-liberalization offensive also echoed timely concerns and broad political objectives, such as the necessity of liberating national economies from their “sclerosis” while preventing a race to the bottom and a relocation of national industries. Commission officials constantly referred to other models of liberalization as the vanguard of modernity – especially British precedents of liberalization in electricity and gas, as well as the precedent of European telecommunication – in order to justify electricity liberalization.<sup>24</sup> They also raised the specter of “regulatory competition” at the expense of high-price countries. It was argued that, in the absence of sectoral competition, prices would remain high, and this would provoke the relocation of energy-intensive industries and discourage their emergence. This argument was especially salient for Germany, especially after the publication of a much-discussed 1993 parliamentary report about the situation of Germany as a site of industrial production (*Standort Deutschland*) in the global economy.

The utilities’ first arguments were purely defensive. They warned against the disappearance of public service obligations in case of sectoral liberalization. They pointed out the failures of electricity liberalization in the UK, where a TPA formula had been pioneered rather unsuccessfully. They argued that the US, after contemplating liberalization in the 1970s and 1980s, had retreated from the idea and had decided to keep its regional monopoly structure. Yet the utilities were on shaky political grounds due to the highly technical and sometimes counterintuitive nature of their arguments. In the

1980s context of “market-oriented” reforms, the traditional electric utility structure of Europe appeared as particularly lackluster. Due to a variety of historical and technical as well as political legacies, the industry appeared as mired in antiquated and parochial patterns of strategic and technical thinking – to say nothing of its complex management structures. Defensive arguments were sailing against powerful political winds on many of these issues.

Much against their will, the utilities were drawn into an economic and political debate with the pro-liberalization advocates. They began to seriously consider the practicality of the TPA option. In 1989, they created Eurelectric, an industrial lobby based in Brussels, in charge of elaborating counterproposals. The lobby first came up with an alternative model to the TPA model of electricity liberalization. In defending the status quo, they called it the “industrial model” and presented it as the only “pragmatic” solution of “regulated competition” – implying that the other one remained utopian.<sup>25</sup> Whether this model was indeed “pragmatic” or not, it was not pushed by a coherent and stable coalition of interest groups. There was little in common between the different national utility structures which the anti-liberalization lobby coalesced to oppose. The “industrial model” was invented and put forward in the face of external pressure and, therefore, many actors’ reactions to this ad hoc model were negative.

At that point, the European debate on liberalization had acquired a dynamic of its own. The utilities probably contributed to this dynamic by engaging in the debate for fear of being left out of big decisions that affected them. The big German utilities, in

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<sup>25</sup> Eurelectric, “Quelle forme de concurrence pour le secteur électrique en Europe: position des membres continentaux d'Eurelectric,” March 21, 1991. The “continental members of Eurelectric” – i.e., everybody except the British – signed this position paper, in which the model of electricity deregulation is said to rest “on the ideology of ‘small is beautiful’” (p. 11). This exact same phrase can be found (p. 2) in conference paper delivered by two EDF executives in November 1990: Pierre Lederer and Jean-Paul Bouttes, “Electricity Monopoly vs. Competition?” paper presented at the Financial Times World Electricity Conference (London, November 12-13, 1990).

particular, were under considerable political pressure. By 1994, the German government had moved squarely in favor of electricity liberalization, with the Economics Minister Günther Rexrodt taking a vocal strong pro-liberalization stance both in the European and in the national spheres. Meanwhile, in the course of the first reading of its proposal by the European Parliament, the Commission had been induced to modify its proposal in a way which was deemed more acceptable by the German utilities.<sup>26</sup> In such circumstances, the big German utilities who belonged to Eurelectric calculated that, unless they took a more positive attitude towards liberalization, they would run the risk of being squeezed between the politically well-protected municipal distributors (*Stadtwerke*) and their would-be foreign competitors.<sup>27</sup>

Faced with the mitigated success of the notion of an “industrial model” and given the fragility of the supporting coalition behind it, Eurelectric decided to abandon its obstruction strategy in 1994. This was, as one analyst put it, a recognition that the “internal energy market debate was not going to go away.”<sup>28</sup> The report can also be seen as a tactical bargaining move on the part of the French, i.e. a way to regain some influence on the modalities of liberalization. After the breakdown of the Eurelectric compromise, the national opponents of TPA adopted diverging positions. The big German utilities called for all-out liberalization for everybody, including the dismantling of their potentially threatening rival EDF in France, whereas the French Ministry of Industry elaborated its so-called Single Buyer (SB) proposal as an explicit alternative to

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<sup>26</sup>The Commission adopted a modification originally sponsored by the association of big German electricity consumers (VIK) and relayed by members of the European Parliament, especially the Belgian *rapporteur* of the energy commission Claude Desama. The modification guaranteed that access to the network would be mandatory but subject to contractual agreement between the parties (i.e., “negotiated access” instead of “regulated access”). According to several interviews, the central purpose of this modification was to make TPA more palatable to German utilities. Subsequently, the Commission’s proposal was re-named “negotiated TPA”.

<sup>27</sup> Interviews with German utility executives.

<sup>28</sup> Janne H. Matlary, “Energy Policy,” in Wallace and Wallace, eds., Policy-Making in the European Union.

TPA under the subsidiarity principle. This proposal accepted the idea that some measure of liberalization was warranted, although not as mandated by the TPA proposal.<sup>29</sup>

In a spirit of compromise, the Council of Ministers mandated that the SB proposal be studied in conjunction with the TPA proposal.<sup>30</sup> For a while, confusion reached a climax, as the Commission and national officials in charge of negotiating the terms of the directive were asked to combine two abstractly defined models of market liberalization. From a technical viewpoint, combining the two proposals into a single liberalization project did not seem to make much sense.<sup>31</sup> This injunction, however, was a sure sign that the debate had moved completely into the political realm. As a result, electricity regulation moved into the purview of European decision-making. The reformers within and outside the European Commission had won the most difficult battle.

### *Carrots and sticks*

The re-shaping of the normative field of electricity regulation cannot be described as a smooth learning process orchestrated by enlightened reformist actors. Important political aspects of the directive emerged over time in the course of a bumpy bargaining process. Actors who were under political obligation to find some common room for an Internal Energy Market agreement continuously fought each other's arguments and episodically struck deals in order to avoid the morass of a collective loss of face. The

<sup>29</sup> The argument was that the utilities would lose the technical control of the network infrastructure, resulting in a loss of productive efficiency. The Single Buyer concept means that, while independent power production ceases to be a monopoly, the transport and distribution of electricity remain the responsibility of a single network operator. Thus, the operator continues to act as an intermediary between producers and customers.

<sup>30</sup> Meanwhile, the TPA proposal had been modified and renamed "negotiated TPA." The modification was that there was now some room for a negotiated, instead of mandatory, access of third parties to the network.

<sup>31</sup> The conjunction of the Single Buyer and TPA proposals would have meant that utilities retained responsibility for operating the network while losing their ability to fine-tune the generation of power with the capacities of the transportation network.

evolution of the Commission's Internal Energy Market initiatives provides a good illustration of this process. To some extent, Eurocrats discovered their preferences regarding the Internal Energy Market through pro-market action. Spurred by the success of the Single Market program, they used a relatively abstract cognitive and procedural framework, embodied in a competition law, in order to write the first electricity policy proposals.<sup>32</sup> The Commission first claimed that electricity was not a "special" commodity and that the internal market for electricity fit squarely within the Single Market agenda. In the face of political opposition to Commissioner Cardoso's 1992 proposal, the Commission's proposals seemed virtually stalled for several years. When a new energy commissioner, Christos Papoutsis, took office, he set aside the bad blood and rallied DG Energy officials to the job of designing an Internal Energy Market on the basis of a modified version of Cardoso's proposals. From that point on, the Commission as a whole could use its experience of Brussels politics, its unique albeit limited European energy policy mandate, and a combination of expertise both in energy policy (DG Energy) and competition law (DG Competition). The Commission's position evolved and left more room for compromise, as reflected in the final outcome.

With the benefit of hindsight, two well-trodden types of political tactics can be distinguished in the development of the Commission's strategy. First, the Commission used a variety of carrots and other positive inducements in order to find allies among key state actors, especially within the Council of Ministers. A majority within the Commission decided to pursue the Internal Energy Market through directives endorsed by the Council, rather than through generic competition law. That was a smart move because the member states felt that they retained the upper hand in the process of building

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<sup>32</sup> The draft directive on TPA unveiled in 1991 by the Commission is directly inspired by the principles of competition law, and few of its provisions appear to have been made on the basis of sector-specific considerations. Many observers report, sometimes critically, the legalistic bent of the Commission.

an Internal Energy Market. The Council began by passing two first directives mandating the free transit of electricity across borders and price transparency for industrial customers. For these directives, there was clear support coming from important constituents, especially among electricity-exporting countries (including France) and the majority of the electricity supply industry. The Council's direct involvement was important insofar as it opened the way toward more important developments. The Council took many years to reach a final compromise and along the way the debate often seemed completely bogged down. Yet each meeting of energy ministers invariably reiterated the Council's official support of the Internal Energy Market and thus comforted the Commission's position, even when its proposals did not go through.

Increasingly, the Commission was also able to rally the support of well-established actors at the sub-state level. While potential competitors to incumbent utilities did gain a certain measure of influence in the process of liberalization, their voice remained marginal, both because they had no foothold in the electricity supply industry and because they evaluated their prospects of entering this market with a fair degree of skepticism. By contrast, industrial consumer groups of electricity began to emerge and became politically active across Europe. This new interest group activity did not precede the directive proposal, however. They evolved largely in response to and in support of the directive proposal. Such groups existed both at the national level and at the European level, since they belonged to a federative entity called the International Federation of Energy Consumers (IFIEC) with its seat in Brussels. The most important group at the national level was probably the German Verband Industrielle Energie- und Kraftwirtschaft (VIK). VIK and other consumer groups were made up of German industrialists, often led by heavyweight corporate actors such as BASF, and united mostly

in reaction to the high levels of electricity prices in Germany.<sup>33</sup> Other groups were in countries where electricity prices were not as high, for example UNIDEN in France. In such cases, industrialists were looking for ways to increase their “bargaining room” for negotiating delivery contracts with the monopolistic utilities.<sup>34</sup> The impact of these groups was at first relatively weak, as they could hardly match the political clout of utilities such as EDF in France.<sup>35</sup> Yet these actors gained legitimacy over time and were increasingly able to convey their reformist message in support of the European liberalization process to politicians and government officials.

Secondly, the Commission made tactical use of the stick of competition policy. Commission officials, especially within DG Competition, periodically waved the threat of engineering a *fait accompli* by way of competition law or – even more threatening – through an Article 90 directive, over which the Council had virtually no control. One possibility was that the Court reach pro-competitive conclusions in the long-standing case brought by the Commission (under Article 169) against national import and export monopolies. Another possibility was for the Commission itself to use its exclusive prerogative under competition law, if all else failed, as a basis for creating the Internal Energy Market. The Commission never abandoned these threats, which proved to be a powerful goad during intergovernmental negotiations. Member state actors knew that, if no progress was made, there was a non-negligible risk that the Internal Energy Market would emerge anyhow, but as a result of a legal rather than a political process. Within the member states, an increasing number of people sided with the Commission’s proposals, especially within the closely connected social networks of national competition

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<sup>33</sup> Interview with VIK official.

<sup>34</sup> Interview with UNIDEN official.

<sup>35</sup> Interview with French government official.

authorities.<sup>36</sup> Despite a situation of apparent deadlock in 1992 and continuous difficulties in the bargaining process, there was progress, as reluctant member states reasoned that it was in their best interest to compromise.

Whether this was actually the case, however, is a moot point. The fact is that the agenda of economic liberalization was still relatively new and fragile. The treaties were notoriously ambivalent on the exact field of application of European competition law, especially concerning public undertakings.<sup>37</sup> Therefore the case law, which was relatively slim on issues concerning large-scale industrial organization and reform, took on an extraordinary importance. Existing case law, however slim, strongly suggested that the Luxembourg judges considered the Internal Energy Market central to the achievement of a legal framework for European integration. Judging from judicial precedents (especially in the telecommunication sector), it seemed that the Court was strongly inclined to help the Commission attain its market-building goals. The judicial uncertainty was therefore too high for member states to run the risk of clinging to the status quo.<sup>38</sup> State actors preferred to seize the initiative in the multilateral arena of the Council, where each member state could at least contribute some input, rather than leave the problem to a judicial arena over which they had no direct control.

The Commission used the Internal Energy Market objective as a rallying call, but carried its proposal well beyond the strict least-common-denominator interest of the member states. It modified the original proposal to make it palatable to a maximum

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<sup>36</sup> Interview with DG Competition and French competition officials.

<sup>37</sup> This ambivalence reflects the compromise quality of many substantive provisions about the nature of the Common Market in the Rome Treaty, which were often – in those times just as much as today – the result of political compromises between national negotiators. For example, the very strong pro-competitive provisions of Article 90.3 are preceded by Article 90.2, which is, in essence, an escape clause from Article 90.1. On the political roots of the mix of liberal and not-so-liberal provisions in the Rome Treaty, see Ernst B. Haas, *The Uniting of Europe* (Stanford: Stanford, 1968), esp. pp. 19-31.

<sup>38</sup> See, for example: Mandil Report, p.21.

number of member states, while holding firm on the principle that some degree of competition must be forcefully introduced in the electricity sector. Once the debate was firmly set in Brussels, Commission officials invented a whole battery of technical arguments of a legalistic nature about how to introduce competition. The fact that they rarely asked the “why” question in a systematic way was virtually irrelevant. They had time on their side and the legal aspects already gave the negotiators plenty of work. The Commission’s arguments bode well with the legal procedures and negotiation context dominant in Brussels’ politics, including at the Council of Ministers. Thus, the Council’s decision to include both TPA and the SB system into the draft directive is not overly surprising. Although this political injunction was distressing to the drafters of the original directive within the Commission, it provided a way to defuse conflict and to make progress toward the final directive.

At the end of the day, a substantial measure of economic liberalization was achieved, despite all the odds against it. The national governments’ position papers evolved from a full-scope but abstract support for the SEM to a more limited and gradual but concrete and real version of economic liberalization. The realization of a market is the only objective which has remained endowed with the highest degree of legitimacy throughout the process. As the discussion became more concrete, the debate obviously became more technical, but remained loaded with political objectives and did not steer away from this course. The evolution of the French government was characteristic of such processes: it first advocated full liberalization, seeing the immediate benefits of freer transit for electricity exports; then it backed down and became much more circumspect, without however capsizing the negotiations. The initial binary choice set for structuring the electricity supply industry – i.e., the status quo ante vs. full-fledged liberalization –

disappeared along the way, as both alternatives became politically proscribed.

The Commission's success was to create a political momentum in favor of liberalization. First achieved in the name of the "1992" objective, it continued beyond that date. Periodically, the Council unanimously renewed its support of the Commission's plan to create an Internal Energy Market – even though there were intense disagreements between member states about the meaning and substance of the Internal Energy Market. The reasons for this unanimous support varied across member states. Some fully supported the Commission's approach (e.g., Britain), whereas others moved from reluctance to support (e.g., Germany). Yet the crucial point is that not a single member state was willing to take responsibility for obstructing the establishment of a much-heralded Internal Energy Market. Since the Commission retained the monopoly of initiative, those member states who opposed certain provisions of the directive proposal were progressively cornered into a defensive strategy (especially France). With the majority of the Council constantly supporting the Internal Energy Market, critics gradually lost political credibility.

#### *A compromise outcome*

In the end, while the two methods (TPA or SB) mandated to organize electricity supply were left optional, the 1996 directive specified that all member states must attain "equivalent results" – i.e., the presence of competition in electricity supply for eligible customers as defined by the directive. In the final text, the Commission was confirmed as the single agency in charge of monitoring the implementation of the directive, and was asked to report on its progress. A much fought-over article 3.3 states that "the interest of

the Community includes, *inter alia*, competition with regard to the eligible customers.” Most remarkably perhaps given the continuing feud over the directive, the member states voted unanimously in favor of the final draft directive. Of course, the game of face-saving required that everyone claim victory at the end. But national positions on the issue of liberalization have evolved considerably over time, largely as a result of the Commission’s action. However we define “liberalization,” the June 1996 directive clearly held the promise of a certain degree of genuine change in this direction and made a mere continuation of the status quo ante very unlikely. In this sense, some form of electricity liberalization – a very unlikely outcome at the outset – was now squarely on the European agenda.

The limits of the directive, however, were equally apparent. These limitations stem mostly from the compromised nature of the directive and the new political climate of the mid-1990s. The Commission was forced to water down its original proposal several times along the way. First, it backed down from its early preference for a “Big Bang” liberalization, envisioned by Leon Brittan during his tenure as competition commissioner, in favor of a more gradualist strategy. Then, in the process of building a coalition and assuaging potential adversaries, especially during the first reading of the proposal in 1994 at the European Parliament, the Commission had to accede to not-so-liberal demands for a more restricted and “negotiated” version of TPA. After a period of initial confusion, actors in the field found ways to lobby the relevant actors both at the national and the European level. The main outcome is that the Council systematically delayed its decision on TPA, and typically requested from the Commission some further elaboration of its proposals.<sup>39</sup> At various points during the negotiation process, member

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<sup>39</sup> Council of Ministers, Meetings of Energy Ministers: Nov. 30, 1992; June 25, 1993; Dec. 10, 1993.

state initiatives (e.g., the decision to go along with both the TPA and SB proposals, or the final bilateral negotiation between the French and the German government) took policy leadership away from the Commission.

As a result of this give-and-take process, the final directive was much less liberal and homogenous than DG Competition and some member states would have liked.<sup>40</sup> Due to the political bargaining between France and Germany, the proposed directive contained a reciprocity clause, which may actually slow down the development of a Europe-wide energy market since it could be used as a pretext for protecting national markets. Italy's long resistance to EDF's take-over of Montedison in 2001 only seemed to confirm this fear. Furthermore, eligibility criteria excluded entire categories of electricity consumers, who were to remain "captive" in the foreseeable future.<sup>41</sup> A lot of leeway remained for member states to decide who was eligible – at least until the rules were re-written in June 2003. In sum, the principle of liberalization was partially accepted, but the traditional utility structure for the management of the technical network was only gradually reformed. The 1996 directive itself was already clear on the member states' dual intent of re-regulating as well as liberalizing the sector, as indicated by its very title: "Directive concerning common rules for the Internal market in electricity."

Beyond the completion of energy liberalization in 2007, the normative trend of sectoral regulation remains sketchy. One likely scenario is the consolidation of connected but distinct national energy markets dominated by oligopolistic actors. But other scenarios are also possible. In 1996, the Commission issued a communication on "services of general interest in Europe", leaving much more room than in prior proposals

<sup>40</sup> Several interviewees have described the forthcoming process as "liberalization à la carte".

<sup>41</sup> Even at the last stage of implementation of the 1996 directive by 2006, only 40% of all consumers will be "eligible" to choose their electricity providers. The June 2003 directive later accelerated this schedule by mandating for an opening of the electricity market for all business consumers by July 2004 and for all individual consumers by July 2007.

for national definitions of “public service obligations”.<sup>42</sup> Subsequently, at the request of the French government, the Amsterdam Treaty of 1997 added a new provision to the list of general principles contained in the first part of the Rome Treaty, recognizing the “place occupied by services of general economic interest in the shared values of the Union as well as their role in promoting social and territorial cohesion”.<sup>43</sup> The 2004 Constitutional Treaty went even further in the same spirit, since it recognized the need to secure funding for these “services of general economic interest”.<sup>44</sup> As liberalization and changes in collective service provision begin to affect the lives of European citizens (including electricity consumers and utility employees) they may become more politicized. Future battles of European energy regulation will not simply reflect conflicting national interests *per se*, but will increasingly echo political struggles over the definition of the public interest. Disruptions or even reversals of liberalization remain possible, especially if sensitive issues such as job protection or the enforcement of public service obligations are involved.

#### **IV. A comparison of contending explanations**

While interests, ideas, or institutions certainly played a role at various points in the process of electricity liberalization, to focus on these variables misses what is arguably the main underlying dynamic of the story – i.e., the unfolding of a political strategy whose goal was precisely to short-circuit the normal interplay of interests, ideas,

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and institutions. The comparative advantage of a strategic constructivist approach is relatively obvious in this case, since the other causal dynamics do not strongly point in the direction of reform. Unlike the finance case, an interpretation of the case of electricity liberalization centered on the development of a political strategy does not require a counterfactual argument. A comparison of contending explanatory perspectives is sufficient to highlight the crucial importance of political strategy.

### *Interests*

A first and most traditional type of explanation would emphasize the causal impact of *interests* – either sectoral or national. Explanations in terms of sectoral interests have a distinguished pedigree in regional integration studies, going all the way back to neofunctionalist theory. They stress the impact of particular interest groups on pluralistic decision-making processes. In the case of electricity liberalization, such an explanation would seem particularly appropriate, since certain well-identifiable economic interests appear to be in a position to benefit from liberalization. While all big industrial buyers of electricity now face the prospect of a choice of suppliers, some electricity producers who harbor ambitions to increase their market share may also benefit from liberalization. On the face of it, it would seem that some big industrial players, including big industrial customers but also the biggest and most powerful utilities in Europe, would be in good position to benefit from liberalization. In the advent of full-fledged liberalization, the big industrial customers would be in a stronger bargaining position vis-à-vis the utilities to obtain electricity at cheaper rates, while the most efficient and/or biggest utilities would likely retain good chances to compete successfully against

potential new entrants and even to capture new market shares. And indeed, at various moments since the beginning of the negotiations, big customers have generally been in favor of introducing more competition, and big utilities have declared themselves in favor of a certain degree of liberalization.

As it turns out, however, most utilities opposed rather than favored liberalization during the 1990s. They saw it as a risk to their adjustment capacity, and potentially to their market position and notoriously high profit margins.<sup>45</sup> All in all, vested interests in the status quo, traversing the whole electricity supply industry, have pushed strongly in favor of existing equilibria and against the idea of liberalization. When the incumbent utilities – through the mediation of their Brussels lobby Eurelectric – officially declared themselves in favor of liberalization, this was more the result of tactical opportunism than because they wanted it to occur.<sup>46</sup> Likewise, on the consumer side, while some industrial consumers pay very high electricity rates in certain countries (especially in Germany), this was nothing new. Until the mid-1980s, the industrial consumers' long-standing desire for cheaper rates had never threatened to upset the very structure of the electricity supply industry. An explanation in terms of interest group politics begs the question of why these interests were suddenly able to prevail at the European level. Furthermore, the big consumers' desire for cheap electricity could be satisfied in many ways other than liberalization, e.g. tougher price regulation on the utilities. Their support of the liberalization process was instrumental yet not crucial to the eventual success of the Commission's directive proposal. Thus, it is doubtful that the big consumers' interests were of such a pressing nature as to "explain" the drive towards liberalization.

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<sup>45</sup> Some European Commission officials, including Energy Commissioner Cardoso, have accused the utilities of oligopolistic rent-seeking behavior. Although it remains to be proved that rent-seeking is the sole rationale of industry lobbying, these statements do reflect the fact that the utilities have a vested interest in the present status quo.

<sup>46</sup> Interviews.

One potential way out of this explanatory conundrum is to point to a potential shift in national interests in favor of liberalization. Germany, with its notoriously high electricity prices, is the obvious candidate here. Past a certain point, one could argue, expensive electricity undermined German competitiveness and the German state was bound to take up this problem and drive the process of electricity liberalization. By the same token, France would be the main obstacle to liberalization and would side in favor of the status quo for reasons of national interest, due to the fact that its electricity was cheaper and that the country exported electricity under the existing system. Yet it is once again unclear whether the dynamics of national interests was really tilted in favor of liberalization. In the absence of an intergovernmental consensus on how to reform electricity supply, a status quo was perhaps the most likely outcome. From the perspective of national interests, it is not at all clear that liberalization was a priori more likely than a continuation of the status quo. Besides, it took several years before most governments, including Germany, changed their positions on electricity liberalization. All other things being equal, electricity liberalization was not clearly in the cards by the mid-1980s.

On the whole, interest-based explanations do not seem to withstand the test of time very well, and their conclusions must be periodically re-evaluated as new events occur and they become obsolete. This is all the more surprising given that the electricity sector is relatively static over time. One would assume that that this would be an ideal case for entrenched interests to constitute more powerful magnets or constraints. Yet this relative entrenchment of interests is precisely the problem. Insofar as powerful interest groups and potentially powerful national actors were going to be hurt, the pure dynamic of finding a least common denominator between objective national interests would have

probably led to a stalemate.<sup>47</sup> It is difficult to single out any hard-and-fast “interests” that can be identified as the independent variable driving liberalization from the beginning to the end. In the face of relatively stable sectoral characteristics (e.g., slow-moving technology, small number of actors), a constant need to re-evaluate the explanation is troublesome. The point is not to say that objective interests did not matter in the process. Yet an analysis of electricity liberalization that mainly tries to identify such interests runs the risk of being wrong-headed. Material interests were not absent, but they were not the key driving variable behind liberalization.

In the case in question, the Commission acted as the main engine of political change, fostering and leading, rather than bandwagoning behind, an interest group coalition of favor of its liberalization agenda. The Commission’s supply of a new policy perspective counted more in driving the process of liberalization than the interest-driven demands of its natural constituents, which remained quite static. The Commission’s political strategy induced the relevant actors (the big industrial consumers, and later the big electric utilities) to re-articulate their interests around the ever-more concrete prospects of actual liberalization. In explaining liberalization, therefore, the political strategy that consisted in actively channeling interests into a pro-liberalization process deserves pride of place.

### *Institutions*

Another category of explanation in political science foregrounds the institutional factors that shape actors’ interests and thus structure the range of possible outcomes.

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<sup>47</sup> Indeed, an analysis of the process of electricity liberalization plausibly concluded that the process was going to fail due to a divergence of national interests. See Padgett, "The Single European Energy Market".

Here the approach would identify the institutional determinants of the process of liberalization. The presence of certain institutionalized procedures or expectations may have channeled actors' interactions, thus yielding identifiable patterns of reforms. For example, the evolution of the intergovernmental negotiation away from systematic anti-TPA obstruction could be the result of a convergence of actors' expectations and beliefs on some institutional method for building an Internal Energy Market. Candidate institutional determinants include the organizational characteristics of electricity supply (e.g., whether the former system rests on a centralized or a decentralized organization of electricity supply), or the set of institutional procedures or legal norms that underpinned European negotiations (e.g., the development of competition law subject to the principle of mutual recognition, or the dynamic of qualified-majority voting at the Council).<sup>48</sup>

To be sure, institutionalist explanations illuminate certain aspects of the electricity liberalization process. In particular, international and domestic institutional structures help to explain the moderation of the 1996 directive and some patterns of cross-national differences in its subsequent implementation. At the European level, the institutional dynamics of the negotiations also heavily impinged on the substance of the 1996 directive. In particular, the incremental bargaining dynamics at the Council and more generally the historical and institutional environment of EU-level negotiations help explain the open-endedness (some would say the vagueness) of the electricity directive. In turn, institutional inertia at the domestic level and cross-national differences are quite persistent, despite the enactment of a common electricity directive. In fact, the open-

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<sup>48</sup> For an explanation of the mitigated results of electricity liberalization in terms of Community case law, see Piet Jan Slot, "Energy and Competition," *Common Market Law Review* vol. 31: 511-547 (1994). For a similar argument cast in terms of an institutionally-induced principal-agent logic, see Schmidt, "Commission Activism". For an argument about the embeddedness of electricity liberalization in domestic and European institutional frameworks, see Rainer Eising and Nicolas Jabko, "Moving Targets: National Interests and Electricity Liberalization in the European Union," *Comparative Political Studies*, v. 34, no. 7 (September 2001): 742-767.

endedness of the directive makes it potentially problematic to speak uniformly of a “European” process of electricity liberalization, when some national electricity markets are being opened much more widely and rapidly than others. Institutional determinants, in turn, are helpful to explain cross-national variation in liberalization outcomes.

Yet institutional determinants largely fail to explain the prior and main puzzle, namely the occurrence of electricity reform at the level of the European legislative framework. The problem with this type of explanation is that there were also important institutional dynamics that played in favor of a complete status quo. At the industry level, utility-centered social and institutional networks and practices had been established over the years at the national level in each member state. Indeed, the developmental function of electricity supply, in addition to its territorially defined sphere of activity, had brought electric utilities into a close, sometimes symbiotic relationship with the political and administrative elite. In many instances, this was reinforced by the public or semi-public ownership or management structures. Internationally, the belief that cooperation, rather than competition, was the normal business practice in electricity supply, was partly a result of cross-national network socialization. The task of interconnecting national electricity grids had fostered social interactions within well-established international technical organizations, such as UCPTTE (created in 1925) and UNIPEDDE (created in 1951). The utilities conducted various forms of cross-national coordinated energy planning, including joint R&D projects. Finally, the latest addition to these network structures was the lobbying organization Eurelectric (created in 1989).

While the shift to qualified majority voting did somewhat change the rules of the game, this institutional factor was not sufficient in itself to generate a departure from the status quo and an agreed-upon idea of what the Internal Energy Market should mean in

concrete terms. There was no least-common-denominator, well-delineated and agreed-upon rule or model available for electricity liberalization. Competition law was of little help in this area, since almost everybody recognized that it would be difficult to apply off-hand. No actor alone was powerful enough to impose any particular institutionally solution. This state of affairs did not fundamentally change after the adoption of new voting rules and other institutional reforms contained within the Single Act. Any agenda of institutional change had to proceed by iteration – and this could not be done without sacrificing legal and institutional purity. In and of themselves, the institutional characteristics and legacies of competition law tell us little about the broader significance of liberalization in the electricity sector. Unless an attempt is made to explain why a particular institutional formula suddenly carried *more* political weight than others, it is impossible to understand the dynamics of the liberalization process. Objectively, there was no preset institutional basis for agreement on any particular formula of reform.

The strength of the Commission was its ability to use the informal institution of the market, in combination with legal arguments and threats of legal action, as a weapon in the political battle. This resulted much less from any secular evolution of European law than from a particular political strategy developed in the “thick” context of the 1992 project. For this reason, a strictly institutional perspective misses much of what is most interesting about electricity liberalization. The process of electricity liberalization epitomizes the importance of market rationality and the Commission’s newly-acquired aggressiveness on competition issues – not the institutional dynamic of competition law alone. In fact, the record shows that the Commission displayed considerable restraint in its judicial initiatives before the European Court of Justice. Since the member states were unwilling to isolate each other – especially France and Germany – the risk of a backlash

from the member states was ever present, even after the shift over to qualified majority voting. In the search for a compromise solution, DG Energy officials did not particularly care about preserving the legal purity of their arguments as long as they managed to advance the cause of their directive proposal. In the end, the Commission agreed to restrictive eligibility conditions in order to obtain French assent to its directive proposal. It even put up with a “reciprocity” clause that flew in the face of competition law principles, so as to consolidate German support. In both cases, the Commission did not hesitate to jockey its way toward a directive, even if that implied major distortions of its original proposal and of its policy principles.

*Ideas and paradigms shifts*

The last hypothesis that we will examine focuses on the role of ideas and paradigm shifts in technological evolution. In the case of electricity liberalization, it has been argued that, due to technological and market evolution, there has occurred a change in actors' thinking, or "paradigm shift," about optimal ways of organizing electricity markets.<sup>49</sup> This type of explanations stresses the causal role of "learning" and the evolution of dominant thinking about technological and market evolution. In constructivist scholarship, ideational factors are rarely erected into mono-causal factors of change. Usually, they are singled out as key factors of institutional change, but acting alongside the evolution of interests or the developmental trajectory of institutions. Insofar as historically prevalent sets of ideas – alias paradigms – can be distinguished from actors' interests and from the institutional context within which these actors interact, however, they represent a different type of variable whose explanatory power can be assessed separately.

A certain "shadow of the future" certainly became more widespread in the 1990s amongst many actors in the electricity supply industry, which could superficially appear as an example of dominant paradigm. In particular, the combination of low gas prices and gradual technological progress (improvements in the technology of co-generation) prompted a dash for small-scale decentralized power stations, such as gas-fired or combined cycle power stations. This seemed to raise the prospects of a different energy portfolio in the future, and a greater recourse to market mechanisms in order to fine-tune supply and demand. Some also argued that, in the post-oil shock context of abundant energy resources, the specter of energy dependence had receded so far that the premium placed on energy independence as well as the preference for certain technologies (e.g.,

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<sup>49</sup> Matlary, "Energy Policy," in Wallace and Wallace, eds., Policy-Making in the European Union. Padgett's article implicitly makes a similar assumption, by equating the common interest with the proposed liberalization.

nuclear) should be considerably lower. Yet in order for the paradigm-shift story to hold as a valid explanation of energy liberalization, the view that liberalization would entail clear benefits must first be consensual among a majority of concerned actors. This is the point where a technology-based line of explanation encounters important difficulties. While proponents of liberalization have typically – and not very surprisingly – adopted this view, it was hardly shared by all actors.

First, the economic foundations of the pro-liberalization argument appear to be somewhat fragile in the eyes of many observers. A number of economists, in view of the nature of electricity supply industry, tend to agree with the traditional view that important segments of the electricity supply constitute “natural monopolies.” In the presence of market imperfection, it is generally recognized that the social benefits of certain monopolistic structures may outweigh their costs. An important body of literature on the topic of transaction costs in electricity markets suggests that there is a good case for maintaining a classic public utility structure, at least in certain crucial segments of the electricity sector.<sup>50</sup> In other words, there may be some elements of economic truth in the utilities’ self-interested claim that they operate in a “special” economic sector. A second and perhaps more immediate concern is that power generation entails huge sunk costs, which cannot be easily recouped in a context of liberalization given the fact that

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<sup>50</sup>This is due, in particular, to high degrees of asset specificity of high-cost investments; the market uncertainty stemming from the absence of stocks (since electricity cannot be stored); the pervasive situations of small-number bargaining and possibilities for opportunistic behavior, since electricity must be supplied in a coordinated manner to all customers on a continuous basis (this is a special problem if nuclear reactors represent a large part of the supply system, since they are economically profitable only in continuous “baseline” operation). See Paul Joscow and Richard Schmalensee, Markets for Power: An Analysis of Electric Utility Deregulation (Cambridge: MIT Press, 1985); Paul Joscow, “The Role of Transaction Cost Economics in Antitrust and Public Utility Regulatory Policies,” Journal of Law, Economics and Organization, vol. 7, special issue (1991). The underlying transaction cost approach is explained in Oliver Williamson, The Economic Institutions of Capitalism (New York: Free Press, 1985), especially chapter 13.

European markets are quasi-saturated.<sup>51</sup> It is useful to remember that liberalization is about the Europe-wide creation of a competitive market. A full-fledged market is not simply waiting in the wings to be unleashed. It seems certain that a large-scale transition to gas on a European scale would entail hefty adjustment costs – not to mention the industrial restructuring costs and the political costs of hurting certain well-entrenched constituencies.

Furthermore, the presence of important market uncertainties makes it difficult to speak of a strongly dominant paradigm of electricity supply. Despite the “dash for gas” in certain countries, like Britain – a country that also happens to have important gas resources – representatives of the electricity supply industry remained generally cautious. Nobody really knew, given the obstacles (both political and technical) to cross-border electricity traffic, what the abolition of all trade barriers will really mean – no more today than in 1986 or even in 1992. Nobody knew how the general political context would evolve. The hot issues in the European energy policy debate, after “deregulation,” could easily become “sustainable energy”, or “employment”, or “public service”. Other major uncertainties included the evolution of energy portfolios after Chernobyl, the threat of global warming, and the level of oil reserves and prices. Nobody knew how these issues would affect the future organization of the electricity market – e.g., what the future of nuclear energy and fossil fuels, including natural gas, would look like. Thus, on the whole, the assertion that there was an emerging consensus, or paradigmatic shift, in favor of decentralized fast-moving production technologies, seems premature. Energy analysts and policy-makers continued to strongly disagree on the “shadow of the future.” It was not clear, even to the actors involved, that liberalization would necessarily increase

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<sup>51</sup> This is very different from the situation in other sectors, e.g. telecommunications, where analysts recognize that the prospects of rapid demand expansion are high.

economic efficiency and therefore lead to a paradigm shift in electricity supply.

*The comparative advantage of strategic constructivism*

The above critique of alternative lines of explanation does not mean that interests, institutions, or historical trends and ideas, did not matter. Neither does it constitute a systematic refutation of all potential explanations based on one or a combination of these core concepts, potentially supplemented by other factors. Yet it suggests that a number of potential outcomes – and perhaps the most likely in terms of interests, institutions, and ideas – simply did not materialize. It claims that electricity liberalization is hard to understand if we simply assume that interests, institutions, or historically salient ideas “matter” in the simple sense of independent variables that are able to single-handedly explain a particular trajectory of institutional reform.

A potential eclectic solution to the puzzle of electricity liberalization would be to describe a path-dependent series of outcomes resulting from loosely combined interests, institutions, and ideas. There is clearly a possibility that liberalization was simply the result of day-to-day political expediency and muddling through. Yet the fact that each of these concepts – interests, institutions, and ideas – could have just as easily explained the (counterfactual) occurrence of inertia as the (averred) occurrence of change means that such a muddling-through explanation is neither particularly elegant nor convincing. If electricity liberalization was a case of muddling through, then the force of institutional routines would have prevailed over the wind of change. Muddling through still implies that there is a problem to be solved and some kind of necessity to implement reform – a very dubious contention in this case. In any institutional sphere, reforms are always

possible and in some cases even desirable, but that does not mean that they are politically easy to implement. Therefore, the analytical challenge when it comes to explaining the occurrence of institutional reform is to identify specific combination of causal factors in a systematic rather than ad hoc fashion.

In this respect, the comparative advantage of taking political strategy as a core concept for explaining institutional change is that it helps understand the compromised nature of the outcome. Electricity liberalization is best understood as a re-shaping of the field of European energy policy-making. There was no fixed ex ante predictable definition of the “Internal Energy Market” as mandated by the Council in 1986. The configuration of the field of electricity policy became the object of political struggles between various actors. Contrary to many expectations, a small number of comparatively weak “Eurocrats” were able to considerable reshape the field of European electricity policy and thus enable a significant, albeit gradual, form of electricity liberalization. By appealing to the political legitimacy of Europe’s Single Market program, Commission officials led other actors to change the ways in which they articulated their own interests and strategies. In this endeavor, market ideas were central to the Commission’s success, but they do not fully explain that success. Commission officials were able to gain a political high ground not despite, but because of the fact that they eventually sacrificed the purity of the original liberalization objective.

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This chapter has demonstrated the political usefulness of the market as a norm. Throughout the process of energy liberalization, the Commission’s political strategy was

a central driver in the utilization and implementation of this norm. The Commission's political activism fundamentally re-shaped the field of electricity policy, thus short-circuiting the deeper but slower evolution of material interests, economic and legal-political institutions, and historically dominant ideas. While each of these three factors was obviously important in the sequential unfolding of events, none of them can be crisply identified as an independent driving factor behind the reform process. By contrast, the political strategy of pursuing European integration through marketization reoriented and re-shaped the field of electricity supply on the European continent with the help of an umbrella policy objective, namely the Internal Energy Market.

This political strategy relied on the market taken as a norm, in two main respects. First, the proponents of a European directive on third-party access to the electricity grid invoked the efficiency gains of the market. They pointed to the monopolistic structure of the electricity supply industry as an obstacle to the "normal" operation of a market – by which they meant a competitive situation in which a relatively large number of suppliers and distributors offer different electricity supply and delivery conditions, including price conditions, to the general pool of electricity customers. They argued that existing regulations did not offer a sufficient guarantee against inefficiencies and rent-seeking behavior on the part of the regulated utilities. They progressively tipped the debate in the direction of a technical discussion on *how* to open the market that largely eluded the more fundamental question of whether such change was needed. The political objective of the Internal Energy Market guided the re-shaping of the field of electricity supply in terms of market rationality.

Secondly, the proponents of a liberal electricity directive, while arguing in the name of the market as a norm, also made sure that their proposals were compatible with

the interests expressed by powerful actors. As it happens, the norm of the market appealed to existing industrial interests, especially big electricity consumers, potential new entrants into the supply industry, and state actors who were engaged in the general endeavor of de-monopolization (like the German Economics Ministry or the French Competition directorate within the Ministry of Finance). Once liberalization was on tracks, incumbent utilities understood that they were shooting themselves in the foot by resisting change. At that point, they often decided to join the chorus of market advocates. These preferences, however, were expressed relatively late in the process of liberalization. They did not pre-exist the drive for liberalization and only contributed to its success on the margin. For the main part, the proponents of liberalization relied on the threat of litigation before the European Court of Justice and on the power of judicial precedents, especially in the area of telecommunications liberalization.

These findings suggest a much more intimate connection than is generally recognized between the liberalization agenda and the progress of Europe's integration in the 1990s. Electricity liberalization is but one of several examples of collective service liberalization that occurred at the European level. Similar processes took place for gas, telecommunications, transportation, postal services, and other sectors. Yet the case of electricity starkly reveals the power of the political strategy of market-building. Electricity was an area where the Commission's liberalization initiatives were originally unwelcome in many member states. Within the Commission itself, the desirability of a marketization of energy supply was far from consensual. Even at the most controversial stages of the debate, however, the member states never withdrew their collective support nor reneged on their fundamental commitment to the realization of an Internal Energy Market. The liberalization of energy carried the day because it proved to be a viable path,

perhaps the only one realistically available at the time, to ensure some convergence in the evolution of domestic energy politics and policies in Europe.

