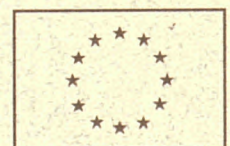


The 1996 single market review

**Background information for the report to
the Council and European Parliament**



EUROPEAN COMMISSION

The 1996 single market review

Brussels, 16.12.1996

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Background information for the report to the Council and European Parliament

This working document brings together the findings of the series of studies and surveys concluded as the background to the 1996 single market review and other factual material. It provides the basis for the Communication to the European Parliament and Council (COM(96)520 final of 30 October 1996) entitled 'Impact and effectiveness of the internal market'



European Commission

A great deal of additional information on the European Union is available on the Internet.
It can be accessed through the Europa server (<http://europa.eu.int>)

Cataloguing data can be found at the end of this publication

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1. Introduction

The single market (370 million inhabitants and a GDP of ECU 6 441 billion) is the backbone of economic integration within the Union and the principal achievement to date of the European Community. It was created to open up national markets to competition, thereby increasing European economic growth, improving overall competitiveness and raising standards of living. Through its development, the achievement of other important political and economic objectives of the Union will also be supported.

The completion of the single market during the period 1985-92 involved a major legislative programme (hereafter referred to as the single market programme, or 'SMP') aimed at the elimination of non-tariff barriers, particularly technical and administrative barriers, to trade and investment, and the free movement of persons. At the end of this process, in December 1992, the Council asked the Commission to report on the overall effectiveness and impact of this programme before the end of 1996. By Council Resolution 1218/92, the Commission was required 'to provide an overall analysis of the effectiveness of measures taken in creating the single market, taking particular account of promoting throughout the Community a harmonious and balanced development of economic activities, sustainable and non-inflationary growth respecting the environment, a high degree of convergence of economic performance, a high level of employment and of social protection, the raising of the standard of living and quality of life, economic and social cohesion and solidarity among Member States. This analysis could, in addition, consider the impact of improving the competitiveness of European business in world markets.'

This report is the Commission's response to that request.

1.1. The background to the review

The scope of this review has been broad, including not only the relevant directives but also the Treaty provisions which underpin them. Although the SMP strictly comprises the legislative measures which have been implemented over the period 1988 to 1994 as a follow up to the 1985 White Paper, for the purposes of this exercise it has been regarded as a more comprehensive policy package. The effectiveness of legislative measures relating to the 'four freedoms' (the free movement of goods, services, capital and people referred to in Article 7A of the Treaty) have also been examined in the context of other policies designed and implemented contemporaneously in order to help implement the single market measures, such as competition policy, social legislation, or measures to protect the environment.

Have the measures adopted to achieve the single market been effective? What are the strong and weak points of the legislative framework as it was implemented? How far have its original objectives been met? If not, what has been the cause? And what contribution has the SMP made to economic growth, employment, competitiveness and social welfare within the EU?

To answer these questions, the Commission has undertaken 38 studies and one extensive survey of business opinion, which are available from the Office for Official Publications of the European Communities and has examined data from other sources on the subject of the single market. The results of independent studies (listed in the table below) have been accompanied by qualitative assessments from available primary sources at a number of different levels in the world of business and commerce.

Table 1 — The 1996 single market review — Individual studies

Impact on manufacturing

Food, drink and tobacco processing machinery
 Pharmaceutical products
 Textiles and clothing
 Construction site equipment
 Chemicals
 Motor vehicles
 Processed foodstuffs
 Telecommunications equipment

Impact on services

Insurance
 Air transport
 Credit institutions and banking
 Distribution
 Road freight transport
 Telecommunications liberalized services
 Advertising
 Audio-visual services and production

 Single information market
 Single energy market
 Transport networks

Dismantling of barriers

Technical barriers to trade
 Public procurement
 Customs and fiscal formalities at frontiers
 Industrial property rights
 Capital market liberalization
 Currency management costs

Impact on trade and investment

Foreign direct investment
 Trade patterns inside the single market
 Trade creation and trade diversion
 External access to European markets

Impact on competition and scale effects

Price competition and price convergence
 Intangible investments
 Competition issues
 Economies of scale

Aggregate and regional impact

Regional growth and convergence
 The cases of Greece, Spain, Ireland and Portugal
 Trade labour and capital flows — The less-developed regions
 Employment, trade and labour costs in manufacturing
 Aggregate results of the single market (CGE modelling)
 Business survey

The main avenues of enquiry are described briefly below.

(i) First, 19 independent studies of manufacturing and services sectors were undertaken for the Commission. The sectors were selected on the basis of economic importance and relevance to the smooth functioning of the single market. Each study aimed to identify the single market measures under review, consider related aspects such as progress on European standardization and the application of Community law, determine whether the measures have led to the disappearance of barriers to free circulation, and identify any remaining obstacles to cross-border transactions.

(ii) Six independent 'barrier studies' were also undertaken. Dismantling non-tariff barriers lies at the heart of the single market programme. Each of these studies therefore aimed to assess progress in dismantling the most important non-tariff barriers, in terms of technical barriers, public procurement, customs and fiscal formalities, capital controls, and industrial property protection.

(iii) The economic impact of removing barriers was examined in a further 13 studies, which dealt with a wide variety of issues, including trade and investment flows, price convergence, competition and competitiveness, employment and labour markets, and economic cohesion.

(iv) A major survey of the awareness, attitudes and reactions to the SMP at company level was coordinated by the Statistical Office of the European Communities (Eurostat). The survey covered approximately 20 000 enterprises in 12 Member States; it asked all firms with more than five employees in the services sector and more than 20 employees in the manufacturing sector to rate the success of the SMP, and its impact on their strategies and operations. Over 13 000 replies were received (a 65% response rate). A separate survey of 200 European trade associations' perceptions of the effects of the single market, was coordinated in the context of the Commission's 1995/96 Panorama of European Industry, using 'face to face' interviews to seek views on the relevance of the legislative measures, their impact on industry, and an overall assessment of the operation of the single market (conducted by DRI consultants).

(v) A range of other sources of evidence about the effectiveness of single market legislative measures has also been considered. This includes additional independent studies or surveys, some of which were carried out in the Member States, related to sectors or issues not directly covered by analysis undertaken specifically for the Commission's 1996 review.

In the light of this analysis, the Commission has outlined in the concluding part of the communication to the Council and Parliament a 'new agenda' for the single market in order to improve its effectiveness. It is intended to serve as the basis for public and political debate in the coming months.¹ In the light of that debate the Commission intends to come forward in mid-1997 with an action plan presenting a detailed work programme for endorsement by the European Council in Amsterdam.

1.2. The difficulties of assessing the single market now

The timing of the review has posed three main problems.

First, it is too early. Some measures, in particular, technical legislation were not implemented until 1994 or 1995. Those involved have had only a very limited opportunity to adjust to the new freedoms and it is unlikely that for the purposes of this review they have been able to comment from experience. At the macro-economic level, there has been insufficient time for the effects of regulatory change to work through to any great extent.

Three examples underline the premature nature of the assessment:

- (i) eight 'new approach' Directives came into force between 1994 and June 1996;
- (ii) implementation delays, e.g. to public procurement, where the liberalization of purchases by public authorities and utility suppliers began after 1993;
- (iii) substantial delays in national level implementation of some directives, e.g. the Directive on liability for defective products was adopted in 1985 but experience of its application is still extremely limited (one Member State has still not implemented it).

Second, the timing of the studies undertaken for this review (most began in early 1995 and ended in mid-1996) meant that much of the data available referred, at best, to 1994. This meant a very short assessment 'window of opportunity' from the time when the measures were in place until the 'cut-off' point of the studies.

¹ A book on the impact and effectiveness of the single market is being published by the European Commission's Office for Official Publications of the European Communities (EUR-OP) with a number of different independent co-publishers in the Member States. Entitled *The single market and tomorrow's Europe*, the book draws on the extensive research undertaken for the Commission over the last two years and featured in its communication to the European Parliament and the Council of Ministers of 30 October. The first language version of the book, in English, was published in December 1996 with other language versions following in 1997. The book provides an overview of the communication and the 38 individual studies and the business survey conducted for the Commission and discusses the dismantling of barriers to free movement within specific industries. It also features a global assessment of the single market's effects on the EU's economy, considering macroeconomic aspects, such as trade and investment, competition, employment, consumer benefits, environmental issues and regional effects, as well as the role of taxation policy and economic and monetary union in the future.

Third, it is difficult to isolate economic effects solely due to the SMP. Other simultaneous developments such as globalization of the economy, cyclical effects, technological advances, political changes such as the demise of the former USSR and the reunification of Germany, and world trade liberalization through the GATT/WTO have complicated the analysis.

For all these reasons, the Commission expected that the review would not show very much change. The period effectively under review has been far too short for sufficient evidence to be gathered or for strongly positive or negative results to emerge. Nevertheless, the information yielded is valuable. It allows the Commission to target areas for further attention and it should help to raise general awareness of the benefits of the single market so far.

2. The effectiveness of the single market measures

2.1. Introduction

The removal of barriers to the free movement of goods, persons, services and capital within the single market is a means to an end, not an end in itself. The elimination of these barriers is a precondition for the achievement of other direct Community objectives: harmonious and balanced development of economic activities, sustainable and non-inflationary growth while respecting the environment, economic and social cohesion, high levels of employment and social protection, and better standards of living and quality of life.

Barriers will not be removed unless the legislation which aims to remove them is fully in place and really works. This chapter therefore assesses how effective the legislative measures taken to complete the single market have been, so far, in removing obstacles to free movement within it. Where barriers still exist, an attempt has been made to analyse the underlying causes and the relationship to single market legislation, if any. The aim has been to identify those areas where the measures themselves, rather than any other factor, require closer scrutiny.

2.2. Free movement of goods

2.2.1. Manufacturing sector surveys

The SMP aimed to provide for the removal of outstanding obstacles to the circulation of manufactured products within the Community. Cross-border shipments would no longer experience physical delays or supplementary costs related to burdensome fiscal declarations. Producers would no longer have to adapt their products before placing them on foreign markets. The liberalization of public procurement would ensure that providers could no longer be protected from cross-border competition. Businesses restructuring activities on a pan-European footing would have fewer legal or fiscal complications. Consumers would enjoy more choice and lower prices — without reduced safety.

Some trade obstacles were widespread; customs and fiscal formalities caused delays for all shipments crossing frontiers. Streamlining these formalities was expected to benefit all firms undertaking cross-border despatches or acquisitions. This expectation is borne out by the Eurostat business survey which finds that 60% of all firms surveyed benefited from the adaptation of customs documentation and 56% consider that the abolition of frontier delays has been of benefit. Only 35% of a broadly-drawn sample of manufacturing firms have been untouched ('no effect' and 'don't knows') by this part of the SMP.

However, most measures targeted products or services trade barriers due to national regulatory or administrative practices, which affected a narrower range of sectors. Within these sectors, benefits have been most keenly felt by companies actively trading with partner country markets. Although the survey clearly identifies a widespread lack of knowledge and awareness of the single market, this is partly explained by the fact that only those companies which were operating across national frontiers in 1985 have been able to comment from experience on the extent of any improvement over the period. Companies coming fresh to the business of cross-border trade have not experienced frustrations of the pre-SMP period.

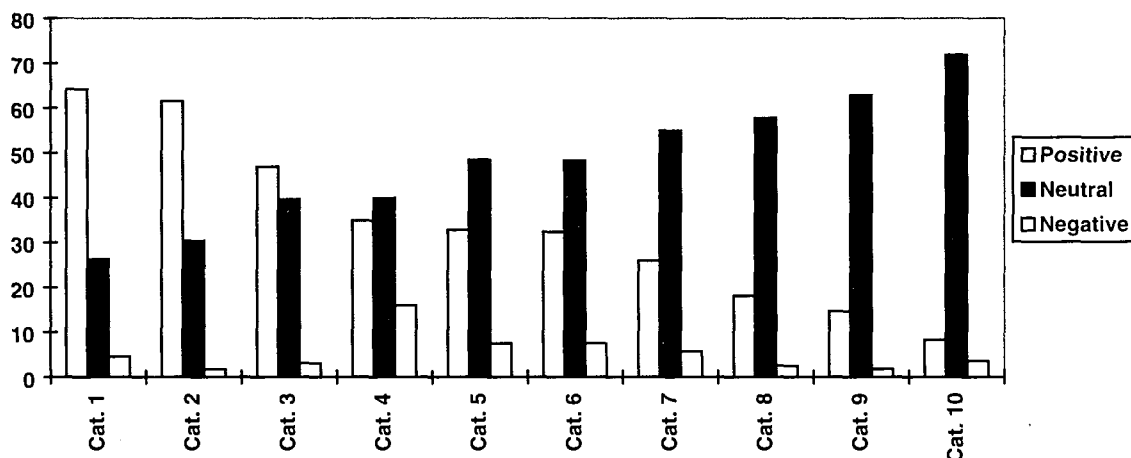
The survey, of some 100 European trade associations (in the context of preparing the Commission's Panorama of European Industry 1995 and 78% of total production in the 80 largest EU industrial sectors (and 80% of employment), reinforces the central importance of the SMP:

- (i) organizations representing 49.6% of the value of production and 48.4% of employment (of the top 80 sectors) saw the SMP as having a significant or strong positive impact on their sector;
- (ii) a large number of representative bodies thought that the single market (SM) framework was a safeguard against the introduction of new barriers and the refragmentation of the market. Many organizations thought that vetting national proposals for legisla-

tion, through such early warning systems as Directive 83/189, had helped to anchor the SMP and to encourage national regulatory authorities to take account of the implications of draft national rules on cross-border trade.

The majority of companies expressed a positive opinion on measures to abolish customs documentation and frontier controls and liberalize road freight haulage. They outnumbered respondents who considered that the single market had a nil or a negative effect.

Figure 1 — Manufacturing industries' assessment of the effectiveness of measures for free circulation of products, Eurostat survey (ranked by % of positive opinions)



Cat. 1 = Customs

Cat. 2 = Frontiers

Cat. 3 = Haulage

Cat. 4 = VAT

Cat. 5 = Technical harmonization

Cat. 6 = Mutual recognition

Cat. 7 = Conformity assessment

Cat. 8 = Company tax

Cat. 9 = Patents

Cat. 10 = Procurement

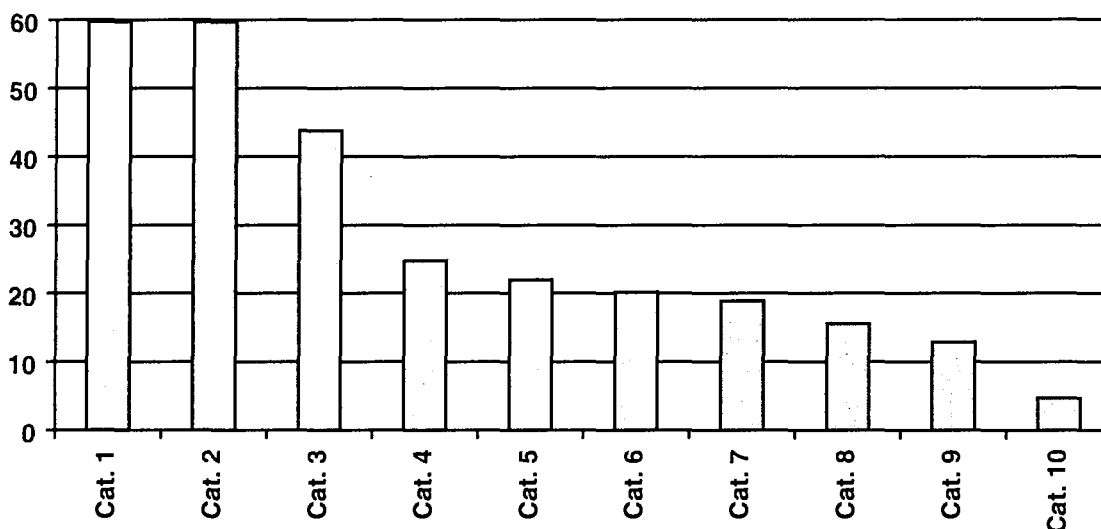
For all SMP measures there was a higher proportion of positive opinions than negative ones. The SMP elements seen as having had the most direct impact at this early stage are: the elimination of delays at frontiers; the elimination of customs documentation; and the liberalization of conditions under which road haulage services can be hired and used across borders.

A substantial majority had positive opinions about measures to eradicate technical barriers. Action to harmonize VAT was seen in a less favourable light, no doubt due to the cost of changing to the transitional system for VAT declaration and procedures which are more burdensome than domestic systems.

The smallest margins of positive over negative perceptions concern company taxation, simplification of procedures for obtaining and protecting patents, and public procurement. All three categories share certain features which might explain this comparatively modest scoring.

The legislative framework is either incomplete (company taxation, patents), or is not yet transposed and implemented (public procurement, trade mark protection). These SMP measures tend to concern fewer firms. In the case of company taxation, the measures concern primarily large multinationals operating plants or subsidiaries in more than one Member State. Only larger firms are concerned with EU-wide protection for patents and trade marks. The need to protect industrial property rights is of greatest strategic importance in a few sectors, such as pharmaceuticals, chemicals, and mechanical engineering components — which strongly favour EU intervention. Public purchasing also tends to focus on a few sectors (63% of total public purchasing of supplies, works and services is accounted for by 12 NACE 3-digit sectors).

Figure 2 — Perceptions of categories of measures, Eurostat survey (balance of positive over negative opinions)



Cat. 1 = Frontier abolition
 Cat. 2 = Customs
 Cat. 3 = Haulage
 Cat. 4 = Mutual recognition
 Cat. 5 = Technical harmonization

Cat. 6 = Conformity assessment
 Cat. 7 = VAT
 Cat. 8 = Company tax
 Cat. 9 = Patents
 Cat. 10 = Procurement

2.2.2. Abolition of customs and fiscal frontiers

2.2.2.1. Introduction

The abolition of physical frontier checks required the following actions:

- (i) the adoption of VAT legislation which retained the principle of taxing transactions at the point of origin while allowing VAT to continue to be levied in the Member State of destination on intra-Community trade between taxable persons. This VAT transitional regime proved necessary because it was impossible to achieve the harmonization necessary to move to a unified system of charging VAT in the Member State of origin before January 1993. For products subject to excise duty, a system allowing for duty-suspended movement of products between authorized warehouses was devised:

- (ii) changes to statistical reporting procedures (Intrastat) were also needed;
- (iii) the abolition of customs clearance procedures on intra-Community transactions removed 60 million customs forms and meant an 85% decrease in the number of Community transit movements;
- (iv) controls of veterinary and phytosanitary products and certain other sensitive products (e.g. drugs and drug precursors, national art treasures and dual-use goods) were also re-organized.

2.2.2.2. Switch-over to the transitional VAT system

The removal of checks at the Community's internal borders was achieved due to the transitional VAT system. A majority of firms now regard the transitional regime as an improvement on previous arrangements. However,

opinions vary as to how much traders have benefited. A detailed cost analysis of traders' in-house administration shows that the change to the current transitional procedures for VAT declarations on intra-EU transactions has reduced compliance costs by two-thirds. Aggregate savings are about ECU 5 billion per annum, or 0.7% of the total value of intra-EU trade. This cost-benefit analysis of changes introduced in 1993 suggests that there is an overall benefit to traders. However, these aggregate figures conceal a number of different effects, some of which act to lower costs and some to increase them. Unfortunately, it has proved impossible to distinguish fully between the following cost impacts:

- (i) Cost savings due to the abolition of customs formalities. The primary source of savings arises from the abolition of customs documentation and other formalities for shipments crossing the Community's internal borders.
- (ii) The cost of traders adapting accounting and tax systems to the new VAT rules (checking VAT ID numbers, drawing up recapitulative statements for intra-Community sales, checking intra-Community acquisitions, etc.). Unlike customs formalities which were contracted out to external agencies, these formalities are now carried out directly by firms themselves.
- (iii) The costs of carrying out transactions in Member States where the trader is not established. These operations are more expensive to traders than domestic transactions because they are required to use tax representatives, resulting in costs five or six times greater than those for a domestic transaction. The rules governing these types of transactions pre-date the introduction of the transitional system and reflect long-standing deficiencies in the Community VAT framework. Box 1 outlines some special trans-

Box 1 Special transactions giving rise to additional complexity

(a) The requirement to register for VAT, and submit Intrastat returns in Member States other than that of establishment

Such a requirement can be imposed in the following situations:

- distance selling (e.g. mail-order) where sales in another Member State exceed relatively low thresholds;
- installation of equipment: where a company provides for installation as part of its after-sales service, it may be required to register for VAT or be subject to the reverse charge mechanism;
- consignment stock: where centralized stock-holding takes place in a Member State other than that of establishment, the trader may be required to register for VAT purposes;
- chain transactions: where goods pass through several intermediaries in different Member States, one of these parties may be called upon to register in the country of origin;
- triangulation: initial confusion has largely been resolved for transactions between three parties within the EU.

The need for local registration requires submission of all relevant returns and payments to the VAT administration concerned, in accordance with its fiscal and legal provisions. This entails significant costs for the trader and may require recourse to a local VAT representative. In some Member States (e.g. France), traders must appoint a local VAT representative under appropriate circumstances. The latter will charge fees in respect of administrative and book-keeping services; it may also be necessary to place a bond/guarantee with the fiscal representative, and a charge reflecting the guarantee which the representative must furnish to the local administration. Local fiscal representation comes at a cost to the trader, and is a cause for much complaint in certain sectors (especially textiles and clothing, where chain and triangular transactions and mail-order sales are commonplace).

(b) The need to aggregate EC VAT and Intrastat data from more than one operating site or unit

The complications are particularly pronounced for statistical purposes.

(c) The requirement in some Member States for more complex EC VAT administration or more detailed statistical returns

For example, some Member States insist on submission of a periodic EC acquisitions list as well as an EC sales list, or impose data demands in respect of a larger number of data elements for statistical purposes.

actions which give rise to additional complexities and costs.²

The cost of switch-over to the new fiscal and statistical declarations procedures triggered much protest in the months following introduction of the system. According to a sample group of 230 companies, these costs amounted to less than ECU 15 000 for half of the sample and less than ECU 25 000 for 70% but were quickly amortized by companies regularly engaged in cross-border transactions. Companies accounting for one-third of total consignments should have repaid their set-up costs within the first three months, and those responsible for 50% would have recovered them within one year. Companies which undertake relatively few cross-border shipments have taken longer to reach the break-even point and for 20% this point will still not have been reached four years after the introduction of the new system. Despite this variation in the length of time taken to recover transitional costs, a large majority of companies now regard the transitional system as an improvement over previous arrangements.³

Compliance costs for cross-border transactions remain much higher than those for domestic transactions. Traders and operators wanted swift progress towards the definitive (origin-based) VAT system. Some 70% of companies wanted rapid progress to the origin-based system which will place intra-EU and domestic transactions on the same footing for the purposes of VAT.

This will also benefit national fiscal administrations by reducing scope for VAT evasion and simplification of administration, but is contingent upon the introduction of an agreed system for redistribution of indirect tax revenues between Member States.

2.2.2.3. Abolition of frontier controls

The elimination of border delays for hauliers resulted in additional savings of about ECU 400 million.⁴ (The total

cost of delays of about ECU 1 billion per annum has not been translated fully into increased vehicle use or savings because of other delays such as driver-stoppage or the collection of freight for return journeys).

Intra-EU shipments no longer entail additional complications when compared with domestic shipments. Reduced uncertainty about delivery times allowed the overhaul of distribution and logistics networks, and implementation of 'just-in-time' and quick replenishment strategies. It also stimulated pan-European logistics services and underpinned new sources of competitive advantage in the clothing sector. For fast moving consumer goods, commercial horizons widened as purchasers felt secure that foreign orders could be delivered on time. While it is difficult to quantify these improvements, they are probably a multiple of the direct cost benefits from the abolition of customs and fiscal formalities in the sectors concerned (Box 2).

2.2.2.4. Conclusions

The SMP means that the movement of products across borders is no longer subject to delays and uncertainties. Shipment is now as straightforward as within a Member State. These benefits can be important for specific sectors as illustrated by the case of the textiles and clothing sector.

Changes in fiscal and statistical compliance procedures have substantially reduced (although not entirely eliminated) the cost penalty which had previously been attached to cross-border shipments as a result of the abolition of customs documentation. Traders now perceive that the transition has been generally beneficial. However, it did involve related compliance costs. Furthermore, non-standard transactions frequently involve additional complexity and costs. In general, while traders regard the transitional system as a significant improvement, they see it as a stop on the way to an eagerly-awaited definitive (origin-based) system.

² Price Waterhouse study, *Customs and fiscal formalities at frontiers*.

³ Sitpro, United Kingdom 1995 and Price Waterhouse, 1996.

⁴ Price Waterhouse study.

2.2.3. Removal of technical barriers to trade

2.2.3.1. Introduction

Technical trade barriers were the most prevalent impediment to the free circulation of products in the EU market. Their very ubiquity added to the perception that the EU market was highly fragmented. It has been estimated that over 100 000 different national technical specifications co-existed in the EU in 1985, each of which was a potential impediment to trade. Whenever these specifications were laid down in national law, producers were confronted with the stark choice of adapting and retesting their product or forsaking export opportunities. This involved unnecessarily high production costs for imported products and reduced competition and market entry where these costs deterred producers.

Technical barriers were top of the list of obstacles to intra-Community trade in manufactured products (1987). Since then, national and European organizations (CEOC, CBI) have continued to emphasize the need for effective action to remove them.

Some 76% of the value of intra-EU trade is subject to mandatory technical specifications (including products covered by national regulations and those where Community harmonization measures have been adopted). If all of this economic activity were to be regulated solely at national level, it could be expected that much of it would be exposed to the risk of technical barriers. In fact, those sectors which are subject to regulatory specifications appear to be more heavily dependent on national markets. Sectors affected by regulatory trade barriers only account for 21% of trade as compared with 29% of industrial gross value added (GVA).⁵ This suggests that technical trade barriers are effectively discouraging cross-border trade and competition in some sectors.

Box 2 Impact of customs abolition on the textiles and clothing sector

Cross-border shipments in this sector were subject to all the customs and fiscal checks listed above. However, the incidence of customs checks on textiles and clothing shipments was particularly pronounced given that frontier controls were employed to administer national quotas on third country imports. These national quotas had persisted despite the establishment of the common commercial policy. Two-thirds of some 7 270 national quotas on imports of textiles and clothing from non-State trading countries which persisted in 1991 concerned textiles and clothing products. In order to prevent national restrictions on specific products from certain sources from being bypassed by indirect imports through Member States applying zero or limited restrictions to imports of the same product, special controls were enforced at intra-Community crossing points (on the basis of Article 115 of the EC Treaty). One half of all authorized restrictions on cross-border shipments in the period 1984-92 based on this provision related to textiles and clothing. As a result of these arrangements, cross-border shipments of textiles and clothing products were particularly hard hit by customs formalities and requirements in the pre-SMP period (IDS, 1996).

It is therefore unsurprising that operators in this sector have perceived large benefits as a result of the abolition of frontier formalities. Producers and distributors report reduced delivery times of 15-20% on average with some citing reductions from two to four weeks in the time taken from receipt of order to delivery. Cross-border shipments now involve no additional complications or costs when compared with shipments within Member States. When coupled with the reduction in cost of road haulage services (ascribed in part to SMP induced competition in this sector), the SMP is considered to permit rapid cross-border delivery. On the whole, these savings of a limited range of measures are thought to have allowed for a reduction in production costs of 0.2 to 0.5% of turnover (CEGOS, 1996).

Furthermore, it has become economical to ship small deliveries across frontiers, thereby expanding the range of clients and allowing overnight demands to be met. These developments are regarded as having facilitated the introduction of 'just in time' and rapid-response strategies. This is seen as increasingly important given the growing demands placed on producers by organized distributors who are anxious to source products on European level but require prompt deliveries and rapid turnover of product ranges. The study reports that, whereas previously products could only afford to exceed the price of third country imports by 15% (primarily as a result of tariff protection), it is now felt that this wedge has been increased to 20% given the enhanced service quality and rapid delivery times associated with SMP completion.

⁵ W. S. Atkins study, 'Technical barriers to trade'.

The trade-restricting impact of these national regulations barriers stems from the need to reconfigure products to comply with partner country specifications such as adjustments to packaging and labelling, registration or homologation procedures (cf. pharmaceuticals, motor vehicles, chemicals or foodstuffs) and the cost of obtaining proof, acceptable to product health and safety inspectors in the importing country, that the product actually complies with the specifications to which it is subjected (conformity assessment).

Technical trade barriers therefore strike at the heart of business operations, affecting pre-production, production, sales and marketing policies. The need to adapt product design, reorganize production systems, and repackage and re-test products entails costs, the magnitude of which differs across products and technologies. The costs of producing separate national variants of lifts to meet national specifications in each of the Member States can be significant and have been estimated to add 10% to average production costs. In the automotive sector, it has been estimated that the move from separate national systems for authorization of product models to European whole type approval can lead to savings of up to 10% of the cost of model development (ECU 30 million per model). This saving does not include the scope for additional improvements arising from enhanced efficiency of production of components and assembly.

While there is often a genuine need for product regulation and testing and industry itself recognizes the potential benefits of voluntary standards or marks, pursuit of these objectives at a national level may in some cases segment national markets to the detriment of producers and consumers. A central tenet of the SMP in this domain has been the need for greater coordination and collaboration to eliminate unnecessary costs. However, the EU approach has been to promote the fact that products manufactured and tested in accordance with partner country regulations could offer equivalent levels of protection to those provided by corresponding domestic rules and procedures (the principle of 'mutual recognition'). Harmonization of different national regulations should remain a last resort to be used in cases where Member States could not be brought to agree on the equivalence

of national rules. The table below provides an overview of the volume of trade and industrial added value covered by the different EU approaches for the removal of technical barriers to trade. Each approach will be discussed in turn.

2.2.3.2. Mutual recognition principle

Member States usually regulate for the same product risks in slightly different ways (or in the same way but requiring duplication of conformity assessment). In general, products manufactured in accordance with different national technical regulations dealing with the same product risks are effectively 'equivalent' in terms of the level of protection which they embody. Recognizing this, the Court of Justice ruled in the Cassis de Dijon case in 1979 that Member States must allow market access to products manufactured in accordance with partner country specifications embodying 'equivalent' levels of protection for prescribed objectives.⁶ Where regulations in force in the country of production offer 'equivalent' guarantees for the attainment of the regulatory objective in question in the Member State of destination, importing Member States may not require the product to be adapted to their own regulatory specifications.

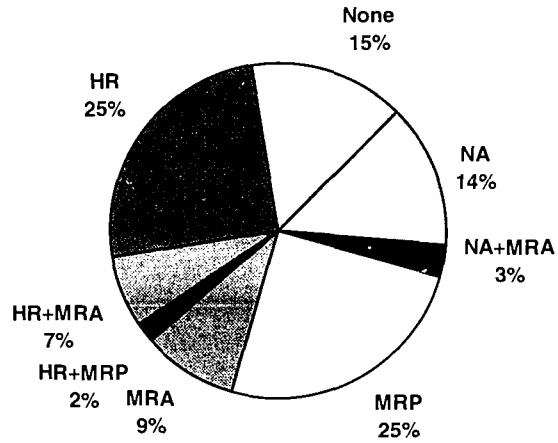
Mutual recognition has been central to EU efforts to eliminate regulatory technical barriers. In economic terms, the 'mutual recognition' principle is relied upon to overcome technical trade barriers affecting 25% of intra-EU trade. This statistic understates the importance of 'mutual recognition' which may come to play an increasing role in providing for free circulation of newly emerging products (particularly, national approaches for dealing with product risks converge). 'Mutual recognition' tends to apply where products are new, specialized, or fall outside the scope of EU harmonizing legislation.

Has this legal formula successfully removed technical trade barriers? 'Mutual recognition' can be relatively effective for equipment goods and consumer durables, but it encounters difficulties where the product risk is

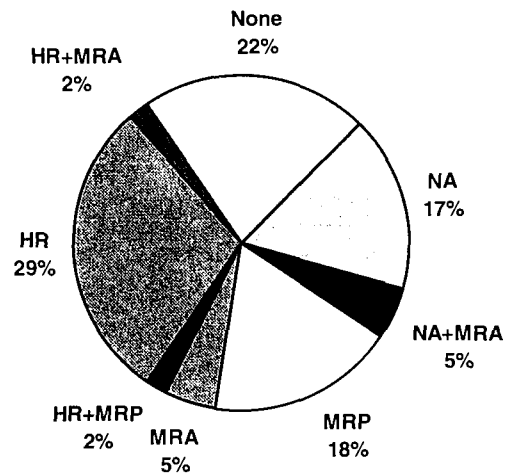
⁶ According to Article 36, these are public morality, public policy, public security, protection of health and life of humans, animals and plants, protection of national treasures, protection of industrial or commercial property. Account must also be taken of other 'mandatory requirements' which justify derogations for Article 30 (protection of the environment, working environment).

Figure 3 — Extent of application of approaches to removing technical barriers to trade

**Approaches to the removal of technical barriers to trade
(% of intra-EU trade)**



% of EUR 12 manufacturing value added



- NA = New approach
- NA+MRA = NA+mutual recognition agreement
- MRP = Mutual recognition principle
- MRA = Mutual recognition agreement
- HR+MRP = Detailed harmonization+MRP
- HR+MRA = Detailed harmonization+MRA
- HR = Harmonized requirements

high and consumers or users are directly exposed (e.g. pesticides and to a lesser extent, foodstuff products such as fortified products). In such cases, problems are often confined to individual Member States or a sub-group of Member States even in the highly sensitive foodstuffs area, the research documents numerous cases where Member States which enforce particular product requirements on domestic producers, accept products meeting partner country regulations. The German authorities have published a list of over 200 food products whose market access would be otherwise prohibited.

However, there are three outstanding concerns:

- (i) First, where national approaches to technical regulation are so divergent as to preclude smooth application of the principle, e.g. where consumers are directly exposed to the underlying risk, the 'mutual recognition' principle can play only a limited role in providing for free circulation. If free circulation throughout the EU is to become a reality for such products, some harmonization of permissible products and their composition and labelling may be needed.
- (ii) Second, where 'mutual recognition' is the chosen approach, health and safety inspectorates in the importing country may be unable to assess the reliability of proof of conformity of products with corresponding specifications of the exporting country where relevant. More exchange of information on national regulations and related conformity assessment procedures, including development of universally recognized accreditation systems for authorization of testing and certification bodies is needed.
- (iii) Third, even when regulatory obstacles to free movement have been overcome, customer preference in the importing Member State for products manufactured in accordance with local (voluntary) specifications may constitute an additional technical hurdle for imported products. This further layer of technical trade barriers has no legal force but derives primarily from the exercise of consumer or purchaser preference. Of the 76% of intra-EU trade potentially subject to regulatory technical barriers, approximately half is simultaneously affected by non-regulatory technical barriers. The 'mutual recognition' principle, by itself, does not provide any impetus

towards convergence of national standards, marks or conformity assessment arrangements, and these do not lend themselves to legislative remedy. Nevertheless, in the absence of appropriate structures for resolving these barriers, successful application of the 'mutual recognition' principle may still leave producers compelled to adapt their product to comply with non-mandatory but entrenched local specifications.

Currently, there is some dissatisfaction with the capacity of the mutual recognition principle to create the conditions for free circulation. Representative bodies have criticized the legal uncertainty and limited scope for taking action against apparent infringements.

However, persistent enforcement of the 'mutual recognition' doctrine by both the Commission (currently 1 230 cases) and national and EU judiciaries are proving effective, not only in resolving specific problems but also in increasing national authorities' awareness. 'Mutual recognition' is progressively taking hold. Its increasing effectiveness is largely due to the mechanisms and instruments which aim to prevent new technical trade barriers.

2.2.3.3. Preventing new generations of technical trade barriers

There is an ever-present tendency for regulatory authorities to adapt or expand the set of national technical regulations in the light of new technological and scientific advances, and the emergence of new products and related risks. Concerted action which does not provide for disciplines on adoption of new national regulations would be short-sighted. Any progress would be quickly undermined by the proliferation of new technical barriers to replace those which had just been dismantled. For example, Member States notified 430-470 proposals for new national regulations each year during the period 1992-94, a period when it might have been expected that the EU was progressing towards a common technical environment. Although the latitude for continued national regulation would seem to be greater in those areas where Community legislation does not exist, in practice Member States continue to concentrate much of their regulatory energy (90%) on precisely those sectors where EU legislation has been adopted (foodstuffs,

transport equipment, chemicals and pharmaceuticals, telecoms equipment, construction products and mechanical engineering).

In order to ensure that the propensity of national regulatory bodies to churn out large volumes of technical legislation does not undo efforts to roll back technical trade barriers, a mutual information procedure has been instituted (Directive 83/189, subsequently extended and amended). This procedure offers the Commission and other Member States the opportunity to consider any national regulatory proposals and to object to any potentially trade-restricting provisions before these become law. This screening process is used to great effect in securing respect for 'mutual recognition' where Member States are required to insert an undertaking to accord 'mutual recognition' to partner country products. While this step may seem of little immediate relevance to operators, it creates the conditions under which a successful challenge can be mounted against refusal to allow market access to partner country products.

The transparency and effectiveness of the 'mutual recognition' principle will be further enhanced by the entry into force (1.1.1997) of a requirement for Member States to notify all products where they withhold the benefits of 'mutual recognition'. In doing so, it paves the way for systematic analysis of all products where Member States consider that national rules embody qualitatively different levels of regulatory protection with a view to determining whether this assessment is objectively supported and whether appropriate action is required. Non-notification of refusal to allow 'mutual recognition' under this procedure will provide a clear signal that partner country products should be able to circulate freely without encountering any further technical barriers of regulatory nature.

2.2.3.4. EU technical harmonization

Where 'equivalence' between levels of regulatory protection embodied in national regulations cannot be assumed, the only viable way to remove the technical barrier in question is for the Member States to reach agreement (under qualified majority voting under Article 100a) on a common set of legally binding requirements. Once such agreement is reached, no further legal impediments can prevent the market access of complying prod-

ucts anywhere in the EU. The only possible derogation is where a Member State can be authorized to maintain pre-existing national requirements (Article 100a(4)). On the whole, there has been limited recourse to Article 100a(4), reflecting the high levels of regulatory protection embodied in EU legislation. In the chemicals sector this clause has only been evoked in one Directive. Even in this case they concern products of little commercial importance confined to just four Member States. In the foodstuffs sector, two Member States have submitted requests for application of this clause in respect of the colours and sweeteners Directive and miscellaneous additives Directive.

EU legislation harmonizing technical specifications has involved two distinct approaches, 'old approach' (detailed harmonization) and 'new approach'.

Detailed harmonization measures

For certain products, the nature of the risk requires extensive product-by-product or even component-by-component legislation. If EU measures are required to give effect to the free movement of such products, then these EU regulations must be sufficiently detailed to protect against this risk. Where registration with a national authority or formal authorizations are required before placing products on the market, a coordinated approach to product testing, a centralized approach (motor vehicles) towards procedures or a combination of both (pharmaceuticals) have been needed.

Research for this review provides insights into the effectiveness of measures in these areas. The adoption of programmes of detailed harmonizing legislation seems to have overcome deeply entrenched technical trade barriers affecting sectors accounting for over 30% of the value of intra-EU trade. The impetus generated by the SMP has allowed the most important pieces of legislation to be put in place in the motor vehicles, chemicals, pharmaceuticals and foodstuffs sectors. Although most of these measures have only recently entered into force, there is general satisfaction with their operation. Outstanding concerns relate to completion of detailed implementing regulations (as in the foodstuff sector), and the prevention of new forms of technical barrier (as in motor vehicles where some Member States are anxious to go beyond harmonized EU specifications relating to cars).

'New approach' legislation

A new approach to technical harmonization was introduced in 1985 based on a division of responsibility between public authorities on the one hand and producers, testing and certification bodies and standardizers on the other. To date, 17 national directives have been adopted.

The key components of the 'new approach' are:

- (i) new approach Community legislation confines itself to prescription of the requirements which are 'essential' for guaranteeing a high level of protection for the collective interest at issue. The detailed specifications for compliance are not prescribed;
- (ii) standardization bodies have the task of defining the detailed technical solutions which remain voluntary in character;
- (iii) however, application of these solutions (harmonized standards) endows presumption of conformity with the 'essential requirements', for example a producer who uses harmonized standards is no longer required to demonstrate how the essential requirements have been satisfied;
- (iv) producers are legally responsible for ensuring that all marketed products comply with the essential requirements;
- (v) conformity assessment is carried out by testing and certification bodies. These are designated by the Member State authorities and act under their responsibility. The Member States mutually recognize the certificates of conformity issued by bodies designated by the other Member States ('notified bodies');
- (vi) 'new approach' has been applied in a wide range of sectors, including both consumer products (e.g. toys) and equipment goods (e.g. machines). Some 17 new approach directives have been adopted to date (see table), covering products which account for 17% of the value of intra-Community trade in manufactured products. A number of these only became fully binding at the end of 1996, as a result of transitional periods during which national legislation continues to exist alongside the 'essential requirements'.

Given the limited time period for which this legislation has been in force, it is impossible to provide anything other than a preliminary judgement on this category of legislation. So far, the following observations can be made.

The transfer of responsibility from public authorities to private-sector activities has proceeded satisfactorily, despite the extent of the adjustments which this imposed on standardizers and conformity assessment bodies.

On the whole, the task of preparing European standards required for the effective functioning of the single market is well in hand. Completion of the current programme will provide the comprehensive set of technical specifications needed to underpin a technical barrier-free single market. European standardization has registered a dramatic expansion in its activity (5 000 European standards produced and 16 000 further work-items are foreseen). The 20-fold increase in annual output over 10 years was not achieved overnight. Capacity constraints and long preparation periods (on average five years for one European standard) for standards were the reasons behind accumulated delays in the finalization of harmonized standards needed to complement the 'new approach' legislation. These delays were most marked for Directives with a wide coverage such as the machines Directive, or where European standards would have a quasi-legislative function (as with the construction products Directive).

The absence of harmonized standards should not however be equated with the complete absence of technical benchmarks. In practice, producers apply the state-of-the-art or whatever (voluntary) technical specifications exist at national level as long as these comply with the essential requirements. The handful of safeguard actions launched to date, notably under the machines Directive, suggest that national technical solutions are mutually accepted.

More than 600 certification bodies, dispersed across the Community, have been notified to date by the Member States. For effective evaluation, a coordinated approach to the application of conformity assessment procedures is required. This coordination now operates for almost all 'new approach' directives. Despite some remaining difficulties in application, conformity assessment results issued by these notified bodies are rarely contested by other Member States.

The 'new approach' opened the way to a wider choice between conformity assessment procedures and, in particular, the option of quality-assurance. This development implies that producers do have to incur the costs of double-checks but also have access to cost-effective and internationally recognized quality assurance schemes. Industry strongly supports this approach and wants it extended to a wider range of products (see gas appliances). On the whole, the greater transparency and flexibility of new approach conformity assessment procedures and the benefits which accrue once testing and certification results are universally accepted draw most praise from operators.

The 'new approach' directives have contributed to enhanced safety and performance of products by allowing more rapid integration of innovation and quality improvements. The fact that pacemakers on the Community market are now two generations in advance of those available on the US market is attributed by industry experts to the implantable medical devices

Directive. Similar effects have been noted in respect of circular wood saws under the machines Directive.

Some teething problems have been encountered as 'new approach' legislation has come on stream. These difficulties are carefully monitored and addressed at Community level, drawing on the assistance of experts from the relevant national administrations. This continuous evaluation allows guidelines to be established to help national authorities to control and implement this legislation, to smooth out discrepancies between Member States.

Experience suggests that the new approach is effective. Products governed by this legislation can be marketed anywhere in the EU and circulate freely without further checks, or adaptation. Free circulation has been achieved without any compromise of the underlying collective interests which the legislation aims to uphold. Any outstanding difficulties, in the areas of standardization and conformity assessment, are primarily transitional.

Table 2 — New approach directives

Directive	Date of application	End of transition period
(Low voltage electrical equipment (73/23)	21.8.1974	1.1.1997 for CE marking)
Simple pressure vessels (87/404)	1.7.1990	1.7.1992
Toy safety (88/378)	1.1.1990	
Construction products (89/106)	27.6.1991	Open
Electro-magnetic compatibility — EMC (89/336)	1.1.1992	1.1.1996
Appliances burning gaseous fuels (90/396)	1.1.1992	31.12.1995
Personal protective equipment (89/686)	1.7.1992	30.6.1995
Telecommunications terminal equipment (91/263)	6.11.1992	
Machines directives (89/392, 91/368)	1.1.1993	1.1.1996
Non-automatic weighing instruments (90/384)	1.1.1993	1.1.2003
Active implantable medical devices (90/385)	1.1.1993	31.12.1994
Explosives for civil use (93/15)	1.1.1995	31.12.2002
New hot water boilers fired with liquid or gaseous fuels (92/42)	1.1.1994	31.12.1997
Medical devices (93/42)	1.1.1995	14.6.1998
Satellite earth station equipment (93/97)	1.5.1995	
Equipment and protective systems intended for use in potentially explosive atmosphere (94/09)	1.3.1996	30.6.2003
Recreational crafts (94/25)	16.6.1996	16.6.1998
Lifts (95/16)	1.7.1997	30.6.1999
Precious metals	Proposal to the Council and Parliament	
Pressure equipment	Proposal to the Council and Parliament	
Cable way installations	Proposal to the Council and Parliament	

2.2.3.5. Conclusions

Despite the fact that Community legislation to eliminate technical barriers is only now coming into force, it is generally seen as effective. Surveys of business operators and their representative bodies reveal a strong vote of confidence in efforts to eliminate technical trade barriers. In many product sectors (chemicals, mechanical engineering, office equipment, foodstuffs, motor vehicles), between 35 and 50% of respondents regard EU efforts as having generated benefits. The proportion of large firms having a positive opinion consistently exceeds 50% while smaller companies (<50 employees) reveal more negative assessment (29% positive and 9% negative). The higher proportion of smaller companies experiencing adverse consequences is probably due to the costs of switching over to new compliance procedures and/or specifications, but also increased competition from companies established in other Member States. This perception is supported by examination of specific product sectors which are subject to a combination of the various approaches for the removal of technical trade barriers (see Box 3 on experience of foodstuffs sector).

Endorsement of EU efforts to overcome technical barriers is particularly marked for products addressed by detailed harmonizing legislation and for those covered by 'new approach' directives which have been in force for some time. The 'new approach' is particularly applauded for focusing attention on conformity assessment arrangements. The elimination of repeated conformity assessment procedures is critical in convincing operators that technical barriers have been successfully suppressed.

On the other hand, the 'mutual recognition' principle is still proving difficult to enforce in a way which guarantees unimpeded access to all Member State markets. These difficulties are particularly pronounced for products for which the underlying risk to the consumer or user is intense. In the past, application of the principle was hampered by opacity about the number of cases where Member States refused to recognize 'equivalence' and the reasons for this refusal. This uncertainty will be largely resolved once pending notification procedures become effective. The mutual information Directive has also proved to be a valuable instrument for forcing increased awareness of and respect for mutual recognition on national authorities. However, even where acceptance of the equivalence of national regulatory specifica-

tions is achieved, further complications may arise related to non-acceptance of results of conformity assessment and discrepancies between voluntary national standards and marking requirements. The problem of diverging national voluntary standards may eventually diminish, as European standards replace national standards, but this will be a protracted process. Some technical barriers originate from non-regulatory features of the market, such as purchaser insistence on products complying with familiar national standards. These preferences can be devoid of any substantive or material justification — particularly where technical specifications are being increasingly aligned through the activity of the European standards bodies.

The EU cannot rely on heavy-handed legislative measures to break down residual technical barriers which are rooted in consumer choice. It can only encourage market-led initiatives aiming at mutual recognition and inter-changeability of local marks, or progress towards common marks. The EOTC (European Organization for Testing and Certification) was established for this purpose in 1991 but to date has made little headway. This limited progress is due to vested interests such as testing and certification bodies which prefer the status quo; for them increased inter-changeability or recognition of foreign national marks may mean the removal of monopoly rights and reduction in revenue. Only client pressure on testing and certification systems can overcome this situation.

This rather complex and mixed picture should not obscure the importance of recent accomplishments in defining ground-rules for the definition and implementation of technical specifications, and in creating an institutional infrastructure which is capable of delivering a technical barrier-free single market. Furthermore, these mechanisms and arrangements provide a crucial safeguard against the technical refragmentation of the single market. A recurrent theme from the survey of industry federations is that producers can now confidently conceive product specifications for a single market without having to worry about the spectre of technical barriers.

2.2.4. Conclusions (on the free movement of goods)

Markets for industrial products within the EU are now highly integrated. This reflects both a history of policy

Box 3

Functioning of approaches for the removal of technical trade barriers: foodstuffs

In respect of national quality requirements for food (compositional standards, recipe laws, etc.) the principle of mutual recognition is believed to be working satisfactorily. In comparison with the situation 10 years ago, the Commission receives few complaints under Article 30 concerning attempts by Member States to impose own national quality requirements on imported products.

The principle of mutual recognition does not work well in cases where Member States impose requirements for health or safety reasons. Specific problem areas at present include divergent national rules on the addition of vitamins and minerals to food (fortification), dietary supplements, processing aids and national limits on certain contaminants in foods (e.g. pesticide residues in baby foods).

For issues covered by harmonizing legislation, we observe a high level of compliance and implementation by Member States. For the whole sector, there are just 10 complaints pending regarding implementation of directives by Member States. One reason for this is that procedures for administrative cooperation and cooperation on enforcement issues are relatively well established in this sector. These arrangements allow for many problems to be resolved informally.

The dividing line between use of mutual recognition or harmonization reflects political decisions to avoid trying to harmonize all aspects of food legislation. The culinary diversity of the Community was to be regarded as an asset. The boundary between the two approaches must be kept under review. While the balance between the two currently seems appropriate, the issue will be examined in detail in a forthcoming Green Paper. Where it becomes clear that mutual recognition is not working, consideration must be given to harmonization.

The combination of mutual recognition and harmonization seems to be facilitating trade between the Member States. The level of increase in intra-Community trade varies across sectors. Non-regulatory factors seem to be a more important explanation than any outstanding technical barriers. Some large increases in intra-EU trade have been recorded in foods and beverages having a high value-to-bulk ratio such as spirits and chocolate, as well as heterogeneous products such as soup and coffee. By contrast, in products such as beer, soft drinks, and mineral water, local preferences and established brand names imply that markets are relatively impermeable.

intervention at EU level and the adjustment of commercial horizons and strategies on the part of business. Key areas of SMP legislation are only now becoming effective but initial indications are positive — there is substantial evidence that the measures in place can overcome the targeted barriers.

This positive assessment requires qualification to the extent that:

- (i) individual provisions of specific measures require clarification in some areas;
- (ii) complementary elements needed to make the measures fully operational are not always in place (e.g. the absence of some European standards complicates compliance with certain 'new approach' directives);
- (iii) operators must overhaul long-established practices or tendencies and adapt to new disciplines (procurement liberalization involves new thinking in this sector);

(iv) enforcement is sometimes perceived to be uneven or ineffective. One recurrent theme which may warrant attention is enforcement and guaranteed respect for rights and obligations. Effective redress, enforcement and post-market surveillance are critical if the 'mutual recognition' principle and technical harmonization legislation are to be effective.

These are transitional problems, which inevitably arise in an operation as vast and complex as completion of the single market. Significant effort will be required, particularly on the side of national authorities, to resolve the problems.

The achievement of free circulation has pushed a number of other distortions to the forefront, and renders market conditions more sensitive to distortions elsewhere in the regulatory and market environment. This review has highlighted three such instances. First, in pharmaceuticals markets, the administration of national reimbursement schemes and price controls has created substantial price disparities between Member States, and led to a limited (to date) amount of parallel trade. Second, in

motor vehicles, differences in tax treatment (including massive divergences in the level of purchase tax applying to new and second-hand vehicles) have distorted the pattern of pre-tax prices between Member States, which again artificially spurs cross-border purchasing and sourcing. However, consumer organizations have been vociferous in their allegations that attempts to take advantage of these differences have been unfairly impeded by refusal to sell or difficulties relating to registration of cars purchased abroad (now largely resolved). Third, exchange rates fluctuate: while the distortions mentioned above are sector-specific, abrupt currency realignments can result in overnight alterations in relative cost-competitiveness between producers located in different currency areas.

The completion of a single market therefore requires greater attention to the resolution of such problems, if trade and competition are not to be distorted by unidentified imperfections which could ultimately destabilize the markets concerned.

This review has not identified any substantial areas of trade in products which are affected by non-tariff barriers. Even in areas where non-tariff barriers are proving stubborn, instruments to overcome them have been put in place. A new regulatory infrastructure at European level, capable of effectively channelling national efforts in the regulatory sphere exists. This development provides operators with the necessary assurances that the single market is here to stay and will go from strength to strength.

The contrast with perceptions and conditions only a decade ago is striking; evidence suggests that the costs of doing business across borders are no longer a significant deterrent for manufacturing businesses. The benefits of integration have progressively become apparent and have influenced behaviour and activities. Recent progress is therefore not seen as a regime change, involving dramatic differences in competition conditions or radical re-formulation of company strategy. This perception, in combination with more pressing concerns relating to survival in economic recession, may explain why the SMP is generally seen as less important than other influences on business strategy or the operating environment.

2.3. Freedom to provide services

2.3.1. Introduction

European market integration in services aims to open markets, national and international, to free trade and competition in order to allow user access to services which are competitively priced, more efficient and better suited to their needs.

Trade takes place mainly through the consumption of international services such as road freight transport, telecommunications or consultancy services; the international movement of production factors (capital and labour) through the establishment of production units in a foreign country (for example banking or accountancy services); and finally through consumption of foreign non-traded services such as accommodation, catering or entertainment.

For some time, services were regarded as a 'non-traded' activity. As a result, a web of national regulatory restrictions developed that limited exchange and discriminated against foreign producers. Sector-specific regulatory restrictions not only affected the sectors directly concerned but also other industries upstream or downstream, for example advertising and broadcasting services or road freight transport and distributive trades. In addition, where access to the physical network was necessary to provide a service, disparities in national technical regulations fragmented the market.

The importance of regulatory restrictions depends on the sector. In some sectors, such as telecommunications, air transport, or audio-visual services, restrictions placed on access to the physical network, special or exclusive rights, restrictions on the use and/or ownership of radio frequencies, ownership rules and public service obligations have severely limited competition and denied access to new operators or service providers resulting in higher costs for business and consumers. In these sectors, the lack of interoperability between equipment and networks exacerbated the situation. In some sectors, such as road freight and air transport, quantitative restrictions limited the scope and volume of trade between Member States. In financial services, discriminatory conditions against other EU operators and administrative rules increased the cost of servicing foreign

markets, thereby limiting trading possibilities. In professional and business services, often regarded as the least regulated of market services, obstacles to market access stem from qualification requirements and other conditions for the professions and from a variety of sector-specific restrictions or standards for other business services (such as employment services, quality control and security services).

Other more general regulations affected the free flow of services even more severely, such as, for example, restrictions on capital movements in the financial services sector or fiscal barriers that distort competition and inhibit the flow of services between different markets.

These impediments to the free provision of services were further compounded by differences between Member States' legal systems. Economic operators in areas such as financial services and commerce refrain from supplying services to other markets if there is uncertainty about the legality of the transactions.

The SMP therefore proposed a package of measures aimed at:

- (i) opening up the market to new entrants on a non-discriminatory basis, by separating out far more clearly the issue of market access from technical rules on supervision, market stability, safety and consumer protection;
- (ii) eliminating quantitative restrictions on trade in services and barriers to the free flow of factors (capital and labour);
- (iii) cutting red tape, administrative burden and simplifying controls to reduce the cost of transactions;
- (iv) strengthening competition rules to ensure a level playing field in cases where 'market failure' is likely to endanger the market structure;
- (v) harmonizing indirect tax levy systems to avoid distortions in the market.

2.3.2. The dynamic of the SMP

The 1985 White Paper emphasized right from the start the need to liberalize services to provide for the freedom of establishment for service providers and freedom to

provide cross-border services enshrined in the Treaty of Rome. Although the initial scope of the programme was rather moderate and the details of the programme were missing, there was a clear orientation accompanied by a fixed timetable. Despite accumulated delays, most of the White Paper measures aimed at the elimination of barriers to trade in services had been transposed by 1993/94. More importantly, the original set of objectives in the services sector was significantly enlarged in subsequent years.

The initial SMP aimed principally at liberalizing cross-border trade in the so-called 'traditional services' (banking, insurance and transport). Services in 'new technologies' were included but without a detailed agenda except for audio-visual services where the Commission, as early as 1984 in the 'Television Without Frontiers' Green Paper, had recognized the importance of establishing a Community-wide broadcasting area for the free circulation of information and culture. As momentum picked up, the scope and the depth of the legislative programme was progressively extended as in telecommunication services or transport, while new areas were included in the utilities sectors such as electricity, gas, post and international railway transport. More recently the advent of the information society is exerting new pressure to create the appropriate legislative framework for the development of information services at Community level.

In transport, liberalization was split into two phases: first international transport and then national transport through cabotage (the supply of services by non-residents in national markets). In audio-visual services, liberalization was limited to opening up the international provision of broadcasting services. In the telecommunications sector the gradual process of liberalization started with the supply of terminal equipment in 1988, followed by the supply of value-added services and data services for corporate networks and closed groups of users in 1990, and the opening to competition of satellite services and equipment in 1994. This process of gradual liberalization was completed by setting the date of January 1998 for the full liberalization of voice telephony services for the public and of the network infrastructure in the EU, subject to derogations for some Member States.

The effectiveness of the SMP can only be measured by the degree to which this package of measures has successfully removed barriers to the free provision of services.

2.3.3. The effectiveness of the measures

2.3.3.1. Services sector survey

A first assessment of the effectiveness of the SMP for services is provided by the business survey coordinated by Eurostat in cooperation with the national statistical offices.

The following table presents service industries' assessment of the effectiveness of measures aimed at eliminating various barriers to the free movement of services.

The figures in Table 3 are weighted according to the number of employees in each firm, to reflect better the labour intensity of the industry and its polarization often between a limited number of big enterprises and a vast number of small players. These are average figures and provide a global assessment of the effectiveness of measures for a wide range of market services including hotels, catering, transport, financial services and business services.

The liberalization of cross-border operations and of capital movements score the highest positive opinions. Positive opinions on capital movements rise to 55% when the financial services sector is considered separately, while positive opinions for cross-border operations rise to 69% in air transport and 39% for land transport.

The breakdown by sector provides more insight on how economic operators view the success of the single market in eliminating obstacles to EU trade. In sectors such as land transport, air transport and financial services, positive opinions are high, ranging from 32 to 60%. But negative opinions are still relatively high, ranging from 11 to 19%, indicating that important barriers still persist. This is particularly the case with business services, where negative opinions outnumber positive ones (19% against 17%), and to a lesser extent with information services and related activities, where the single market scores a meagre 28% of positive opinions compared to 19% of negative opinions.

Table 3 — Service industries' assessment of the effectiveness of measures aimed at eliminating various barriers to the free movement of services (%)¹

Measures	Opinions		
	Positive	Neutral	Negative
Harmonization of licences	20	66	5
Recognition of licences	17	71	3
Facilitation of cross-border operations	30	60	4
Facilitation of physical establishment	17	74	1
Public procurement liberalization	16	68	6
Capital movements liberalization	25	66	1
Direct double taxation	18	67	1

¹ The sum is not equal to 100, the remaining percentage having no opinion on the issue.

Source: Eurostat survey, EU Member States excluding Germany.

Table 4 — Eurostat survey, EU Member States excluding Germany

Firm size	Opinions		
	Positive	Neutral	Negative
5-49	16	63	21
50-199	19	60	21
200-499	17	61	22
500-999	21	54	24
≥ 1 000	35	46	19
Total (EUR 11)	25	54	22

The survey confirms the view that while significant progress has been made in liberalization of some service sectors, especially the traditional services (transport and financial services), barriers are still high in other service sectors.

At the individual firm level, the SMP has been a success for bigger businesses employing more than 500 people (see table below). The majority of firms seem not to have been affected. This is understandable to the extent that services are often provided at local or regional level. However, for a large number of SMEs, despite their overall positive views on the SMP, the new competitive environment has failed to deliver a positive result. One possible explanation of this is that while SMEs recognize the opportunities created by the SMP they are unable to take advantage of the situation while having to bear the negative consequences of increased competition in their domestic markets. Meanwhile bigger businesses are more widely affected by the SMP (see the middle column) but seem to cope better with the opening up of the markets and benefit from the opportunities created.

2.3.3.2. Single market review studies

The sectoral studies in services provide more insight on the effectiveness of the mechanisms put in place to open up the market. The sectors studied can be grouped in three main categories according to the different typology of barriers to the free provision of services in each.

- (i) **Group 1** involves banking and credit institutions, insurance and road freight transport, where regulatory measures to ensure market stability, safety and consumer protection have traditionally played an important role in shaping the industry's structure at national level. These measures tend to create significant barriers to cross-border trade and discriminatory conditions for the establishment of new operators.
- (ii) **Group 2** involves sectors such as air transport, telecommunications services and TV broadcasting services; these are areas in which the regulatory framework has restricted or even forbidden market access through the award of special and exclusive rights and where regulation of companies' behav-

our is designed to balance 'market failures' or to promote the 'general good'.

- (iii) **Group 3** involves sectors such as distribution and advertising, where access to the market is not necessarily restricted by national regulations but where the costs of access are significantly increased by differences in market regulation. Although some specific sector measures were taken at Community level, the SMP has had an indirect impact through changes in the upstream or downstream markets, stimulated by EU liberalization in the trade of goods and services.

Table 5 gives an overall picture of the progress achieved in these three groups. It shows that Community measures have been effective in removing the most visible barriers that either restrict access to the market or the free flow of factors (columns 1, 2 and 3). Harmonization measures, however, through which minimum common requirements were set in order to create a level playing field between domestic and non-domestic competitors and to eliminate barriers that might increase the cost of supplying services internationally, have proved less effective.

The following section provides further analysis, by type of barrier and sector, of the effectiveness of single market measures concerning the sectors covered by the studies.

2.3.4. The liberalization effect

2.3.4.1. Free movement of goods and persons

Internal frontier controls for goods were one of the most visible barriers to the cross-border development of certain services, and their elimination on 1 January 1993 has clearly brought dividends to some service sectors. For transport services, for example, unnecessary border delays were cut, making delivery times more reliable and increasing vehicle use. For a typical 1 000 km road journey, savings for a haulier from the abolition of frontier controls were estimated at around 2% of total costs. In distribution, particularly in the fast moving goods business, the elimination of customs and fiscal formalities allowed distribution companies to improve their efficiency in sourcing and distributing goods.

Table 5 — Effectiveness of single market measures in removing barriers to the free provision of services (as perceived by economic operators)

	Barriers					
	Cross-border service restriction	Restrictions on establishment	Restrictions on factor flows	Regulatory/technical barriers ¹	Fiscal issues	Others
Banking	✓✓ Discriminatory conditions for cross-border sale of services ✓ Restrictions on marketing and service content	✓✓ Discriminatory conditions for licences	✓✓ Capital controls	✓✓ Prudential requirements ✓ Conditions for sales	Tax on savings Investment income tax Death duties	
Insurance	✓✓ Discriminatory conditions for cross-border sale of services ✓ Restrictions on marketing and service content	✓✓ Discriminatory conditions for licences	✓ Capital controls	✓ Consumer protection Conditions for sales	Taxation of reserves Taxation of premiums	Contract law
Road freight transport	✓✓ Bilateral quota restrictions on the access to other EC markets ✓✓ Price restrictions	✓✓ Discriminatory licensing conditions	✓ Cabotage restrictions ✓✓ Recognition of diplomas	✓✓ Weights and dimensions ✓ Road safety rules ✓ Speed limiters ✓ Resting hours	✓✓ Excise duties	✓✓ Border formalities for goods
Air transport	✓✓ Bilateral restrictions on free access to other EC markets ✓✓ Price restrictions Slots allocation	✓✓ Exclusive rights for licensing of air carriers Ownership rules in third country bilaterals	✓ Cabotage restrictions ✓✓ Designation and capacity restrictions	✓✓ Conditions for sales ✓✓ Security and safety rules Airports charges	✓ VAT	✓ Border formalities for passengers ✓✓ Access to computer reservation systems ✓ State aids, unfair practices
Telecoms liberalized services	✓ Discriminatory conditions for access to network	✓✓ Exclusive rights on mobile, data and satellite services	✓✓ Exclusive rights to sell equipment	✓ Technical conditions for use of networks		Fair access to networks
TV broadcasting services	✓ Restrictions on cross-frontier broadcasting ✓ Rental and lending rights ✓ Term of copyright protection ✓ Copyright applicable to satellite and cable	National licensing rules for broadcasters Media ownership restrictions		✓ Technical conditions for use networks		
Distribution (fast moving consumer goods)	No restrictions	No restrictions	✓✓ Restrictions on free movement of goods		✓ VAT	✓✓ Border formalities for goods ✓ Technical barriers on products
Advertising	Types of products and media Comparative advertising	No restrictions	✓ Restrictions on media	✓ Misleading advertising Content restrictions		

¹ These types of barriers tend to increase the cost of supplying services internationally and could be considered equivalent to technical barriers in manufacturing.
 ✓✓ Barrier effectively removed; ✓ Barrier partially removed; ◌ Remaining barrier; — Not relevant.

The effective removal of internal frontier controls, combined with the single market measures to facilitate the free movement of goods and transport liberalization, contributed to the appearance of new businesses and business concepts such as European distribution centres, pan-European logistics services, or express and timetabled light freight transport.

The reorganization of distribution generated substantial cost and productivity gains, such as lower cost, higher productivity and better service as a consequence of centralized distribution methods and more efficient logistics.⁵ Logistics cost reductions between 1987 and 1992 amounted to 29% from an average of 14.3 to 10.1% of total revenue. The largest cost reductions are in transport, where firms report up to a 50% cost reduction. The average number of days from order placement to reception of the shipment declined from 21 days in 1987 to 15 days in 1992. Furthermore, European companies reported service quality improvements in the form of reduced service failures realized in on-time delivery, order completeness and the fill rate.

For services even more than for manufacturers, progress in the free movement of persons is of the utmost importance because the actual supply of a service is often strictly related to the cross-border movement of the supplier of the service, in particular for business services and other professional services. Preliminary data indicate that demand for highly skilled specialists, managers, technicians and other highly qualified manpower is increasing, partly as a result of internationalization of businesses in the single market and the trend towards globalization of economic activity. However, gaps in the legal framework for the free movement of persons continue to hamper this process (for more detailed analysis see Section 2.5).

2.3.4.2. Quantitative restrictions and restrictions of the free flow of factors

Businesses in transport and distributive trades would not have been able to seize the opportunities resulting from the elimination of frontier controls if quantitative restrictions had not been removed at the same time. Capacity

restrictions in both road freight and air transport have been removed, allowing transport companies to extend their networks and improve the use of their assets. In road freight transport, the resulting savings for a typical 1 000 km journey from the abolition of quotas and gradual introduction of cabotage are between 3 and 4% of total costs. In passenger air transport, this has resulted in increased flexibility for airlines to adjust capacity (number of seats and frequencies) to meet passengers' demands and offer discounts to customers to improve traffic revenue.

In financial services, open competition has been the principal aim of the single market measures. The abolition of restrictions on the free movement of capital was an essential ingredient in this programme. Restrictions have been removed in most Member States since 1990 and in all Member States since 1994. But financial market integration has been a gradual process because the full effects of capital market liberalization are restricted by obstacles in the financial services market. Although banking services were liberalized at the beginning of 1993, the completion of the single market in this sector continues. The market for insurance services dates only from July 1994 and the liberalization of investment services from January 1996.

A more complex situation arises in television broadcasting services, where in order to promote European culture and harmonize the conditions in Member States, a quota system was introduced by the 'Television Without Frontiers' Directive by which a majority proportion of transmission time (excluding time for certain types of programmes) should be reserved for European works and 10% should be reserved for independent works. While these provisions have eliminated previous barriers to cross-frontier broadcasting, the flexibility allowed to Member States to introduce stricter rules has negatively affected the costs and conditions for the establishment of new broadcasters.

2.3.4.3. Freedom of establishment and access to the physical network

Ensuring freedom of establishment on a non-discriminatory basis and free provision of services is fundamental

⁵ Coopers & Lybrand, 'Distribution' study.

to achieving a single market. For utilities and network industries, it is essential to ensure fair and economically viable access to the physical network for all service operators and to promote network competition, where technically feasible and economically justifiable.

To achieve this objective, the concept of a single Community licence was developed and the 'home-country control' principle introduced. The new single market rules allow for air and road transport companies and financial and credit institutions from any Member State to trade freely in and with any other Member State, under home-country control, on the basis of a single Community licence. An operator can decide to incorporate his business in any Member State, out of which he can exercise his activities throughout the Community; other branches may be opened without first having to seek authorization in other Member States. To apply the rules effectively, the licensing conditions and the surveillance rules were harmonized. But it is the mutual recognition of the home-country controls that allows the whole system to work. National authorities must ensure that the licence conditions are respected and that their controls are sufficient to be recognized by the other Member States. However, some restrictions still exist in air and road transport as full cabotage will only be authorized as of 1.4.1997 for air and 1.7.1998 for road transport.

In the telecommunications sector, Community measures have recognized that licensing will continue to be predominantly a matter for each national regulatory authority, but in accordance with procedures and minimum conditions harmonized at an EC level. Much of the technical work relating to the harmonization of licence conditions is entrusted to expert bodies in the field of telecoms with a wider membership than the Community Member States.

The effectiveness of the new rules is difficult to measure because the decision of a firm to enter another part of the market depends not only on the underlying legal framework but also on prevailing market conditions. On paper, the new system seems to work well. Thus, in air transport, new companies have entered the market on both intra-Community and domestic routes,⁹ a prospect

unimaginable some years ago. Incumbent airlines too, such as British Airways, Lufthansa, Swissair and KLM, have taken advantage of the right to establish an airline based in another country and expanded their networks in other EU countries. In banking, cross-border branching by credit institutions has steadily increased over the last three years, albeit from a very low base, increasing by 58% the number of cross-border branches operating in the single market between 1993 and 1995.

Differences in market structure from country to country may deter new entry, even where this is legally feasible. However, the removal of legal barriers to entry and the easing of access conditions has had a psychological impact on service companies' perceptions of competition levels. Some 36% of land transport operators, for example, consider that competition from other EU operators has increased, with only 1% disagreeing.¹⁰ Figures for banking and credit institutions are similar; 31% think competition has increased and only 3% disagree; in insurance, the scores are even higher, 42 and 4% respectively. Competition from other domestic operators has also intensified. In air transport, 48% thought competition increased, with just 2% disagreeing; while in insurance the respective responses are 48 and 9%; in land transport, 30% of operators thought competition had increased, with 14% disagreeing. Only in banking and credit institutions did respondents think that competition from domestic operators had not risen substantially.

The elimination of trade barriers in the utility sectors, however, has met strong resistance from some incumbent operators and Member States, and liberalization in this area is consequently much less complete and much less effective.

It is in the telecommunications sector, where the Commission has made use of its powers to introduce liberalizing legislation under Article 90(3) of the Treaty, that most substantial progress has been made in liberalizing a utility sector. This led to the progressive opening of the Community's telecoms markets, starting with equipment in 1988, value-added services and corporate services in 1990, data services in 1993, satellite services in 1994 and now in 1996 adoption of measures allowing early infrastructure competition, opening up mobile ser-

⁹ Restrictions on full cabotage remain until 1.4.1997.

¹⁰ Source: Eurostat business survey.

vices and setting the date of 1998 for full liberalization of all networks and public voice telephone services. The Commission's power to use Article 90 in this way, though controversial, has twice been confirmed by the European Court of Justice.

While in that case the aggressive policy of the Commission bore fruit, in television broadcasting services a more gradualist approach has been followed, with the result that important barriers to trade still persist, either because the legislation was narrowly defined — rules governing cross-ownership of the media, the licensing conditions of establishment in Member States and licensing of infrastructure were not harmonized, or because the application of the freedom of cross-frontier broadcasting has been restricted in practice. Member States have sought to prevent cross-frontier broadcasters from transmitting programmes into their territory which did not comply with local or national regulations or objectives. Differing views between Member States on how to define the place of jurisdiction of a broadcaster and the exercise of their right to apply stricter rules than required by the 'Television Without Frontiers' Directive, have limited the effectiveness of Community measures. As a result, broadcasters continue to encounter difficulties in entering markets without obtaining the explicit or implicit approval of the national authorities in the target State and therefore may prefer an establishment strategy rather than pursue a pan-European strategy. However, the current revision of the 'Television Without Frontiers' Directive as well as two recent European Court of Justice judgements will contribute to resolving these problems.

Harmonization of licensing rules and mutual recognition of surveillance rules are insufficient to open up the market in sectors where access to the physical network is a precondition for providing the service. In telecommunications, air transport and television broadcasting, specific provisions have been made to ensure access to the network but most of these measures are so far judged not to have produced the full benefits expected from liberalization. In television broadcasting services, for example, the cable and satellite Directive, which opens up access to

satellite services, has not yet been implemented in the majority of Member States. In liberalized telecommunications services, the application of the leased lines Directive has given rise to infringement procedures and has not yet achieved the full cost orientation of leased line tariffs, though important progress is being made now that clear dates for infrastructure competition have been set. As a result, prices for leased lines remain extremely high in Europe compared to other parts of the world. In air transport, the most important remaining barrier for the free provision of services, the lack of access to airport slots, still inhibits competition on existing routes and the development of new routes.

The Council Regulation on slot allocation, by accepting 'grandfather' rights, allows the incumbent carrier to continue to enjoy its privileged position resulting from these rights. As a result, the lack of peak hour slots at many major airports makes the entry of new carriers almost impossible on the densest routes, where competition would have been viable. It also inhibits niche carriers from serving regional routes.¹¹

2.3.5. The harmonization effect

Building on the Treaty rules and the principle of mutual recognition, secondary legislation has aimed at the necessary harmonization of national rules to provide a level playing field for business. This process is proving to be lengthy, however, and success so far has been uneven. Much depends on the attitude of Member States that decide on policies at national level and have the responsibility of transposing Commission Directives and guaranteeing their implementation.

With the removal of the more fundamental barriers, the relative importance of harmonization in areas, such as, the elimination of restrictions on the content or form of specific services; the conditions to ensure fair competition; and the elimination of fiscal distortions has significantly increased.

¹¹ The Commission will propose a new legislative framework, which if agreed could potentially resolve these problems.

2.3.5.1. Removal of service restrictions

Regulatory bans or limitations on particular types and forms of services applied at national level fragment the single market. Elimination of these barriers is important because legal certainty is an essential requirement for the provision of certain services, particularly where the service contractually binds the private parties.

In financial services where enough experience is available, there is clear evidence that product restrictions hamper the cross-border supply of services, in particular in retail banking. This is due to a marked tendency on the part of national authorities to:

- (i) restrict the free provision of services by invoking the 'general good' clause and reintroducing *a priori* controls (for example, mortgage credit law in Belgium and all consumer law in France have been classified as being part of the 'general good' and companies must therefore comply with this legislation);
- (ii) interpret in a restrictive way the notification requirements introduced by the second banking directive, thus creating uncertainty over the legality of certain transactions and the services to be provided.

Similarly, in the advertising sector, the muddle of disparate national rules creates obstacles for companies wanting to offer standardized services across national borders and also affects development in distributive trades that are the main end-users of such services.

2.3.5.2. Ensuring fair competition

Respect for competition rules is essential for ensuring the effectiveness of the single market measures. Responsibility is shared between the Community and Member States. Some current distortions are explained by historical reasons but new barriers to competition emerge either due to inadequate application of Community rules or because of the anti-competitive behaviour of some operators. Continual assessment of the market is necessary in order to ensure that competition policy is working.

The examples set out below illustrate some of the current problems:

In air transport, one of the most important problems with the liberalization of air transport services has been the very large sums of money going to some airlines in the form of State aids. The Commission's policy in this area is to limit the distorting effects of State aids to individual airlines by attaching increasingly stringent conditions to its decisions and, ultimately, phasing out such aids altogether.

However, despite these efforts the majority of airlines consider State aids as an important barrier to entry as unprofitable airlines may continue to operate on markets from which they might have otherwise withdrawn.

When faced with increased competition, companies may seek to strengthen their competitive position. Some consequent barriers have been effectively tackled in the air transport sector, for example, restrictions on access to computer reservation system (CRS) displays have been removed by a Commission Regulation. However, new practices can emerge which when combined can effectively deter competition by new airlines. A typical example is the use of frequent flyer programmes (FFPs) initiated by the larger carriers which offer them a major competitive advantage over small new entrants. The association of FFPs with alliances and code-sharing can cause a number of difficulties for the small operators who are not in a position to cope with such a dominant position. Similarly, the use of override commissions (high extra commission usually based on sales volumes) or other incentives by large carriers gives new entrants a competitive disadvantage in selling through agents.

In telecommunications, it is clear that the incumbent telecom operators (TOs) wield significant power. The UK example is illustrative; despite the early introduction of competition the former monopoly operator still has a dominant position in the market place. Ensuring the application in practice of the basic principles introduced by the open network provision Directive of fair, non-discriminatory and harmonized access to the dominant TOs network is key for the development of the single market in telecoms. If the power of dominant TOs is left unchecked, this could hinder competition and could be damaging to the expected benefits of liberalization in terms of price, choice and quality of services for business clients as well as households.

In road freight transport the even-handed enforcement of Community measures on resting hours, speed-limiters and road safety rules is essential in order to ensure fair competition between hauliers. There is some evidence that uneven enforcement is seen as a distorting factor of the market.¹²

In the financial services sector, respect for Community prudential rules is important in order to ensure market stability and avoid distortions in competition from under capitalized financial intermediaries.

2.3.5.3. Elimination of fiscal distortions

These barriers represent one of the principal obstacles for market integration in all sectors as well as a formidable disincentive to cross-border business. The sector in which the effects are most significant is the financial services sector. The persistence of certain discriminatory or distortionary tax rules in the EU is limiting the integration of the financial services sector and distorting flows of capital in the EU. These concern in particular:

- (i) differences in the taxation of savings, which also give rise to problems of cross-border tax avoidance and evasion;
- (ii) tax reliefs for certain financial transactions, such as mortgage interest payments, which may discriminate against non-domestic service providers or lenders;
- (iii) special taxation treatment for certain forms of savings or investment which are designed to promote selected schemes and which mould market activity and structure;
- (iv) double taxation in death duties or inheritance tax or the avoidance of death duties by non-residents.

In transport, the other major area of concern, problems relate to the future taxation of transport services in order to correct imbalances in the way the user charges and external costs are paid by the service providers. The

Commission has published a Green Paper on this issue to tackle the problem of taxation in the transport sector as a whole.

At present, problems are reported with the large variation in the application of VAT to air travel which is considered to affect competition in air transport services, in particular between interconnected flights combining an intra-Community leg with a domestic leg and direct intra-Community flights.

Although international passenger flights are exempt from VAT while rates on domestic flights range from 0 to 15%, depending on whether a passenger flies directly to his final destination or whether he uses the interconnected flight, he may be subject to VAT. Other such distortions concern the treatment of VAT on kerosene and excise duties.¹³

2.3.6. Issues of proportionality and transparency

A certain number of regulatory obstacles to the free movement of services could be solved by the direct application of the Treaty (Article 59). For instance, in the field of commercial communications, surveys have demonstrated that many companies face restrictions to cross-border activities. Some of these restrictions could be solved without new harmonization by applying the principle of mutual recognition. However, this leads to the need to assess the proportionality of the application of non-discriminatory restrictions to incoming services. This has led the Commission to propose a Green Paper in this area.

Given the expected growth in cross-border service provision with the advent of the information superhighways and the expected national adaptations and new regulations for on-line service provision, there is risk of increasing fragmentation of the single market in services. Rather than wait until these barriers come about and then contest or harmonize the law, it would be more suitable for the appropriate authorities to regulate to safeguard single market principles, thus avoiding new barriers to trade in services within the Union. With this

¹² NEA 'Road freight transport' study.

¹³ The Commission is currently studying this problem in order to make appropriate proposals to harmonize conditions in the single market.

in mind, the Commission has recently proposed an extension to the existing Directive 83/189 notification system for rules on goods and technical standards to include new information society service regulations.

2.3.7. Conclusions

The Community has established a basic legal framework in many services. The legislative changes introduced were more radical than in the manufacturing sector. As a result, the most obvious restrictions have been removed. However, full implementation of the new legislative framework has taken longer than expected, in particular in the utilities where the transitional period has been longer. Delays in transposing the new rules into national law have impeded progress (e.g. insurance). Further measures may be needed, particularly for financial services.

Nevertheless, the changes in place already appear to have increased competition in traditional services sectors. The separation of market access from other rules regulating market behaviour has proved successful in eliminating discriminatory rules based on nationality and helping to cut red tape. Non-discriminatory rules based on the protection of the 'general good', however, still hamper the cross-border supply of services, along with anti-competitive practices resulting from the ineffectiveness of Community rules or the behaviour of economic operators. Taxation issues are particularly important in financial services because lack of harmonization of taxation rules distorts capital flows and market structure.

The SMP in services is still incomplete. Business services, information services, and commercial communications are some examples of broad sectors where the single market impact has not yet been felt and where discriminatory and non-discriminatory barriers hinder EU integration.

2.4. Free movement of capital

The free movement of capital is now written into the Treaty of Rome and is one of the cornerstones of the single market. The first of the four fundamental freedoms for which a framework was realized, its benefits were enshrined in Directive 88/361/EEC adopted as long ago as 1988. From 1990, the Directive removed all capital controls and provided for the complete liberalization of all forms of capital movement between Community residents, whether natural or legal persons. From the beginning of 1994, new provisions, on the basis of directly effective Article 73b(1), have enshrined complete freedom of capital movements within the Treaty itself, rather than leaving it to the secondary legislation, thereby making it a 'building block' for EMU.¹⁴ The last of the derogations from the Directive expired in June 1994.

Apart from affording economic benefits, through a better allocation of capital among the Community, free movement of capital is also an essential condition for the free operation of financial services enterprises and their cross-border activities. The effectiveness of any Community harmonization measures in the financial services sector would be greatly reduced if corresponding capital movements were subject to restrictions. The free movement of capital is therefore a necessary condition for a single market in financial services and capital market liberalization.

Under Articles 73a to 73g of the Treaty of Rome (as amended by the Treaty on European Union), there are no longer any formal exchange controls, or other direct forms of restrictions to capital movements, in any Member State. Nevertheless, some administrative measures remain in force which still limit non-residents' freedom of access to domestic markets, customers, or financial instruments, or residents' freedom of access to foreign financial markets, institutions or instruments. Research¹⁵ for this review, attempting to capture the degree of capital market liberalization in the EU, included a survey of EU financial institutes on remaining barriers to the free movement of capital. Information on the latter was also obtained from the OECD Codes of liberalization. All Member States subscribe to two OECD

¹⁴ The second purpose of the Treaty provisions was to provide for freedom of capital movements, with some exceptions, for third countries.

¹⁵ Capital market liberalization study.

Codes of liberalization (one on capital movements and one on current invisible transactions). Adherence to the Code on capital movements involves an undertaking to remove restrictions from a specified list of cross-border capital transactions; this list (Annex A to the Code) closely resembles the nomenclature attached (as Annex I) to the 1988 Directive. By lodging a reservation against a specific item on the list, a member country retains the right to maintain restrictions on those operations, whilst still benefiting from liberalization undertaken by others.

The results of the survey suggest that a considerable degree of capital market liberalization has been achieved. Respondents judged the freedom of capital movement in the EU as a whole to score almost 8.5 out of 10 now, compared to less than 6.5 in 1990. Domestic requirements encourage residents to buy, sell and hold equities abroad, rather than at home, while to a lesser extent placing non-residents at an advantage over residents in the case of similar transactions on the home market. There may in fact be an artificial stimulus to capital movement in both directions which distorts the efficient allocation of capital. In general, non-residents are most free in their transactions on bond and money markets, while they are least free in respect of collective investment securities and in the field of investment services, especially management of privatization issues, lead management of bond issues, market-making and access to payment systems.

This perception of liberalization matches quite closely the results that emerged from the analysis of information on the OECD Codes. It appears that Member States generally have only very few, mostly quite specific, reservations¹⁶ registered under the Codes. The situation is not completely even across the Union: two Member States have no reservations, while seven Member States account for more than 80% of the EU total. There are also pronounced differences between the various categories of market activities, operations in collective investment securities and in money-market securities being relatively free of reservations while operations in securities on capital markets and the provision of banking and investment services together account for over

half the total number of reservations entered. In addition, 10 Member States have entered reservations against the freedom of establishment and operation of branches of foreign insurers, banks and other financial institutions. These reservations qualify the freedom of these operators to conduct capital market or money-market operations.

Of the various kinds of factors which were seen as inhibiting or distorting capital movements by the survey respondents, the most frequently cited were insufficient liquidity in local markets, non-residents' tax treatment, and exchange rate risk. Local prudential and incorporation requirements, as well as national differences in company law and accounting frameworks were also seen as significant constraints. Withholding taxes and the non-recoverability of tax credits were regarded as particular problems. In several countries, differential treatment of non-resident firms for corporate income tax purposes also causes distortions. Among regulatory obstacles, local restrictions on institutional investors' portfolios, generally in favour of domestic government bonds, were considered to reduce the liquidity of domestic equity and private sector bond markets, thereby raising the cost of capital to local firms and subjecting the institutions to lower returns and higher risk. A number of specific constraints arising from local market structures, customs in particular countries were also cited by respondents, notably in relation to government securities and membership of local stock markets and clearing systems.

There has been a substantial increase in the freedom of capital movement throughout the EU since 1990, with most change having been achieved in the most restricted markets. Significant minorities of businesses attributed this positive effect to the SMP and the liberalization of capital flows (some 23% of firms in manufacturing and 25% of firms in the financial intermediation business).¹⁷ However, the share of those perceiving no change at all remained relatively high, at 61% and 60% respectively.

Freedom of capital movements is judged to be 85% achieved by respondents to a further survey,¹⁸ compared with only 65% in 1990. Respondents assessed the impor-

¹⁶ In general, these reservations refer to both intra-EU capital flows and flows with the rest of the world. Overall, however, the number of reservations is higher from the latter.

¹⁷ Eurostat business survey.

¹⁸ Credit institutions and banking study survey.

tance of various single market measures on a scale of 1 to 100 and indicated that the liberalization of capital flows was 58 (quite important). On the same scale, the importance of barriers to capital requirements, in terms of the restrictions they place on enterprises' ability to operate in other EU countries, was seen only of low to medium importance by all of the EU.

In the manufacturing sector, the net balance of respondents weighted for size of company, reporting a positive impact of the SMP in terms of the free movement of capital was 30%. In the services sector, the net balance of respondents reporting a positive impact in distributive trades was 12.5%. The net balance of respondents reporting a positive impact on capital movements in other services was 11%. This evidence suggests that any malfunction of the free movement of capital may have been perceived more by manufacturing industries in relation to their cross-border activities than by operators of services.

However, insufficient liquidity of local markets, exchange rate risks, the tax treatment of non-residents, local prudential and incorporation requirements, and national differences in company law and accounting regimes were reported in the survey as still inhibiting or distorting capital movements. National prudential regulation has also been extensively used as a disguise for controls, with consequent effects on the structure of investment portfolios and therefore of returns.

Research for this report shows that the SMP has been effective in terms of the liberalization of capital flows.¹⁹ Improvements in the free movement of capital and lower costs of finance to industry suggest that, in general, the legislation is working.

The effectiveness of the single market is constrained, however, both by 'sluggishness' on the part of banks and credit institutions in responding to the SMP and by some remaining barriers which influence their behaviour.²⁰ In the field of mortgage credit, there is unequal access to capital markets for the purposes of refinancing. In France and Portugal, access to government debt markets

is limited to local or selected banks. There are problems too in some bond markets. In Greece, refinancing by foreign issuers is precluded by a domestic ban on the issue of certain types of bonds. Prior authorization for refinancing is required in Belgium, Spain, France and Italy, which effectively discourages foreign players. In Portugal, there is a ban on the issue of bonds payable in a foreign currency. In Britain, Germany and France, the issuing of mortgage bonds requires supervision by a domestic national (this is acceptable because it is a form of prudential regulation but nevertheless it causes delays and deters foreign transactors). Differences in taxation of investment income continue to perpetuate distortions in capital movements between Member States.²¹

The Commission's Green Paper on meeting consumers' expectations of financial services has also highlighted several important areas relevant to the free movement of capital, including the need to improve cross-border credit transfers. A Directive on cross-border transfers, designed to speed up and reduce the costs to consumers of small cross-border payments has now been adopted and is due to come into force no later than July 1999. And the question of the freedom of pension funds to invest across border continues to be debated. Some Member States still do not allow pension funds to be invested in foreign securities or restrict their scope for doing so, thereby impeding the free movement of capital.

Conclusions

The progressive liberalization of the rules has led on the whole to the progressive liberalization of markets. According to the survey of the EU financial institutes and the OECD Code information, the single market enjoys an enviable level of free capital movement. Businesses also rate this freedom 85% achieved and no study has revealed a lack of effectiveness in either the Treaty provisions or Directive 88/361/EEC.

But a few impediments remain and, with them, the continuing risk of new barriers to the free movement of capital. Pension funds, for example, are potential suppliers

¹⁹ Credit institutions and banking study.

²⁰ Credit institutions and banking study.

²¹ See paragraph 2.6.3.

of large and long-term funds which can augment the available pool of capital in the single market and contribute to long-term growth. In some cases, the remaining impediments are outright restrictions on foreign assets or currency matching rules; the third life insurance Directive even imposes a mandatory restriction. Large institutional investors who are restricted to small domestic markets are unable to provide the best return for their shareholders. Nor are they free to invest across the EU in small dynamic companies in the services sector where there is greatest potential for creating more jobs.

There is a need for closer examination of the regions and sectors where such practices impede or discourage the free movement of capital. It is evident from the levels of reservations under the OECD Codes and from the studies undertaken for the Commission that freedom to move capital varies as between Member States and that banking and investment services feature in over half of all reservation notifications. Access to certain markets is also effectively discouraged by the need to comply with domestic procedures which appear to go beyond prudential requirements. And, in spite of the generally positive mood of business, the list of remaining distortions to capital movements connected with exchange rate risks and taxation issues represents a tangible cost which may be measured in lost output, competitiveness and jobs.

From this review, therefore, it appears that the present legislation is well designed. Obstacles to the free movement of capital appear to be indirect. Remedies to these residual barriers to the free movement of capital may lie in closer examination of local practices and enforcement of rights under the Treaty.

2.5. Free movement of persons

The right of individuals to move freely between Member States is as much a part of the single market as the right to movement of goods, services and capital. In addition to its economic significance in terms of permitting the mobility of labour, this right is of considerable symbolic importance as a concrete expression of the concept of European citizenship.

On the basis of legislation which to a large extent predates the SMP, many citizens avail themselves of the right to free movement within the Union, whether for

short or long periods, and enjoy many advantages in the host Member State on the same basis as its own citizens. Workers and job-seekers can take up residence in another Member State, with equal right of access to all employment in both private and public sectors, with only a few exceptions (such as the judiciary or the police, diplomatic service). The coordination of social security arrangements ensures that migrant workers continue to be attached to a social security regime and maintain rights (particularly as regards retirement). They, and their families too in certain circumstances, are entitled to benefits such as sickness, maternity and invalidity allowances. They are also entitled to remain in the host country after retirement and to receive normal benefits.

Diplomas and professional qualifications obtained in another Member State must also be recognized, although in some cases conditions may be imposed to take account of differences in qualifications and training systems. Evidence on the operation of the Commission Directives on the mutual recognition of diplomas and professional qualifications shows that in the period 1991 to 1994 some 10 000 citizens availed themselves of recognition of their qualifications under the general system provided for in Directive 89/48/EEC. About 5 000 take advantage each year of recognition under the sectoral directives for doctors, dentists, veterinary surgeons, nurses responsible for general care, midwives, pharmacists and architects. These figures show a low level of mobility in the regulated professions (less than two per thousand of the total professional population). Although this may in part be ascribed to linguistic and cultural factors, it also suggests that there may be difficulties in understanding or making use of the relevant legislation.

Unemployed people, job-seekers, students and retired persons may also take up residence in another Member State provided they fulfil certain conditions regarding resources and health insurance.

However, there is evidence that in some cases citizens encounter difficulties in availing themselves of these rights, for example because of lack of familiarity with European law on the part of local officials or cumbersome and time-consuming administrative requirements. For this reason, in parallel with the present review, the Commission has established a High Level Panel under the chairmanship of Mrs Simone Veil to identify existing and potential obstacles to the free movement of people and to propose solutions. The remit of the Panel, which

began work in April 1996, covers both the way in which the existing measures are applied in practice and the identification of new measures which could complete the current body of legislation by removing obstacles or solving problems not yet addressed by the Community. The Panel's report will help the Commission to prepare an integrated strategy for free movement issues.

It has not been possible to reach agreement on the removal of border controls within the deadline originally envisaged. The Commission has, however, put forward proposals for three Directives designed to bring about their removal, while acknowledging that flanking measures must first be put in place to ensure the maintenance of a high level of safety in the area without frontiers. Furthermore, since 1 July 1995, seven Member States (Belgium, Germany, Spain, France, Luxembourg, the Netherlands and Portugal) have applied between them, in an irreversible way, the Schengen Convention abolishing all controls on persons crossing their common borders (although France has temporarily reinstated controls on its northern land border).

Conclusions

The legislative framework in place already largely ensures the right to free movement for European citizens throughout the Union. Practical problems in exercising those rights are now being examined. Meanwhile, removal of border controls between some Member States has been achieved, albeit outside the Community framework, and the Commission has tabled the necessary draft legislation to bring about their complete abolition.

2.6. Creation of a single business environment

In addition to legislation to remove specific barriers to free movement, action to complete the single market included steps in the following areas:

(i) measures to introduce competition into public procurement contracts. While similar in economic effect to many of the measures discussed above to liberalize trade and competition in manufacturing and service markets, these measures targeted public sector and utility purchasers of supplies, works and services. Public procurement liberalization therefore

extended the reach of single market integration into markets which had previously been sealed off from cross-border and often local competition;

- (ii) creation of new forms of industrial property protection (trade marks and patents), having wider geographical coverage. The goal was to offer economic operators the option of obtaining industrial protection covering all or a number of Member States as opposed to persisting with a 'bundle' of national rights;
- (iii) measures to facilitate the operation of subsidiaries, plants or branches in other Member States by eliminating double taxation of income generated by these operations (corporate taxation), and steps to harmonize national law concerning the setting-up of companies, the maintenance of their capital, their financial reporting, etc. and to reduce legal obstacles to restructuring and link-ups between companies in different Member States (company law).

Beyond contributing to the overall objective of removing impediments to cross-border transactions, those measures have little in common in terms of substantive content. They will therefore be considered separately.

2.6.1. Public procurement liberalization

EU public procurement legislation aims to break down discriminatory procurement practices which have restricted access to markets supplying the public sector or utilities to a limited number of national suppliers. In 1987, less than 2% of public purchasing was awarded to non-national suppliers, compared to levels of between 25% and 45% for private sector purchasing.

The potential benefit from open procurement is huge. Public procurement of works, supplies and services accounted for 11.5% of EUR 15 GDP in 1994 or ECU 721 billion (i.e. the combined size of the Belgian, Danish and Spanish economies or ECU 2 000 per EU citizen). A slight decrease in the relative size of public procurement since 1987 reflects increased pressure on public purchasers to pay lower prices. EU procurement legislation should make this goal achievable.

Protecting large areas of economic activity from competition involves large costs. Some sectors where there is

substantial scope for efficiencies of scale (for example railway rolling stock or boiler-making) are particularly sensitive to rules about public procurement. Procurement supply has traditionally been concentrated in a number of sectors: 12 fairly narrowly defined product and service sectors account for 62.8% of public sector purchasing. Public procurement is concentrated in a few service sectors, while public purchases of supplies are spread over a wider number of sectors.

EU efforts to open public procurement began with the adoption of two Directives in the 1970s. These measures were strengthened and extended under the SMP. One important extension was their application to purchases of services and to procurement by water and energy utilities, and the transport and telecommunications sectors.

This considerably widened the coverage of the regime; procurement of services now accounts for 30% of all procurement activity, while purchases by utilities make up a further 24%. The new legislative framework affects about 110 000 public authorities involved in awards of at least one contract in excess of the relevant thresholds.

This strengthened EU legislative framework for public procurement is underpinned by the following principles:

- transparency: contracting authorities must publish tender notices for contracts in the Official Journal;
- objectivity in award of contracts: contracting authorities must clearly announce the criteria upon which they will reach a judgement about the award of a contract and cannot modify these criteria in the course of the award process;
- the rapid review of any decisions taken by contracting authorities which infringe Community rules on public procurement.

Any judgement regarding the effectiveness of Community procurement legislation is constrained by the short time since the legislation came into force and the fact that in some cases Directives have not yet

entered into force.²² Only the rules relating to liberalization of supplies have been in force for sufficient time for the effects to take hold.

The slow pace of transposition of Directives into national law in the sector further complicates the analysis. Of 158 national transposing measures required by the various procurement Directives, 17 measures had not been notified to the Commission by July 1996. A lesser concern is the high proportion of deficient transposition measures; there are currently 39 cases of infringement proceedings in process for failure to transpose the legislation correctly or at all. These difficulties have robbed EU procurement legislation of some of its effectiveness since contracting authorities remain unaware of the procedures and rules and tenderers are faced with legal uncertainty and confusion when trying to take advantage of opportunities afforded by the legislation. As a result, only a minority of entities have reported real benefits.²³

Despite these imperfections, there are signs that the legislation is starting to bite. These changes are most evident in respect of obligations relating to transparency and openness.

- Publication of contracts: substantial increases in the level of publication of OJ tender notices have been recorded, from 12 000 in 1987 to 90 000 in 1995. Marked increases have coincided with the entry into force of the services and utilities Directives, suggesting that operators in these sectors take their obligations under the legislation seriously. But there is still an 86% shortfall between the number of authorities publishing and the estimated number covered by the legislation.
- Tenderers are beginning to perceive changes in market access: a wide-ranging survey of suppliers reveals that many have benefited from the new mechanisms for increased information and transparency (OJ, TED, etc.) to identify new opportunities in both partner country and domestic procurement markets. Companies identifying new opportunities also display high levels of responsiveness (90% rate

²² The codified excluded sectors Directive entered into force on 1 July 1994. Its entry into force is postponed for Spain until 1 January 1997, and for Greece and Portugal until 1 January 1998.

²³ Eurostrategy consultants 'Public procurement' study.

of response to domestic and 70% to cross-border opportunities). Of companies submitting tenders in response to newly-identified cross-border opportunities, 44% reported that they had won new business. Some 31% of companies reported that they were selling to partner country authorities, although much of this may be through local sales offices or as part of a local consortium. 36% of respondents also reported increased competition in their domestic markets, although this contrasts with perceptions of purchasing authorities that new tenderers have not increased since the introduction of the legislation.

Changes are also beginning to manifest themselves in the macroeconomic data. Combined direct and indirect import penetration from partner countries has increased between 1987 and 1994 (on average) from 6 to 10%. These developments are reflected in strong growth in the level of intra-EU trade in procurement-sensitive products. Changes are not limited to products or supplies; similar levels of import penetration, of up to 5%, are observed in the construction sector.²⁴

In spite of this encouraging evidence, a number of problems remain which have also been identified in the Commission Green Paper on public procurement.²⁵

- (i) Compliance with procedural requirements: in some cases, there is a marked tendency for utilities to make more use of negotiated procedures, but this is consistent with their demanding specifications. Under restricted and negotiated procedures, the use of pre-qualification stages may have the effect of unfairly limiting the number of potential tenderers.
- (ii) There may be insufficient guidelines on pre-qualification arrangements. The unjustified use of 'accelerated procedures' imposes severe restrictions on the scope for open tendering wherever it is used.

- (iii) Clarification of specific provisions of the legislation (for example, the boundaries between works, services and supplies contracts, and the 'aggregation' rules).

- (iv) Policing and enforcement: suppliers are entitled to seek redress before national courts, or other national review bodies, for injuries related to non-compliance. Research for this report²⁶ reveals that the threat of legal action has led to more conscientious adherence to the legislation.²⁷ However, this right to action before national courts may not be sufficient, due to the fear of jeopardizing future business by antagonizing purchasers, the difficulty of proving any breach of procedures (only the defendant will usually have all the relevant information) and the level of damages. The only watchdog is the Commission which is unable, given present resource constraints, to investigate all alleged infringements.

In conclusion, EU legislation on public procurement liberalization is already acting as an effective catalyst for increased competition in public procurement markets. The impact on cross-border competition has been lower, but non-negligible. The proportion of procurement purchases which are sourced directly from partner country markets has doubled from 1.4 to 3%. Procurement purchasing indirectly sourced from partner countries, through the intermediary of sales offices or subsidiaries, has expanded from 4 to 7%. Relatively high levels of import penetration are now recorded in many product markets typified by high levels of procurement. This is particularly true for complex products with standardized specifications such as office machinery, medical equipment and motor vehicles/buses (cf. table).

²⁴ Price competition and convergence study (case study on construction).

²⁵ *Public procurement in the European Union: Exploring the way forward*, 27 November 1996.

²⁶ Contracting authority survey.

²⁷ The public procurement study also shows that this threat can also lead entities to apply the rules too rigidly in some cases, thereby increasing administrative costs and deterring new suppliers.

Table 6 — Import penetration in public sector purchasing (%)

Sector	Direct	Indirect
Low-tech products:		
— office furniture	5	8
— uniforms	3	13
— printing and paper	<1	17-19
High-tech standardized products:		
— office machinery	4	22-29
— motor vehicles	3-4	16-19
— medical equipment	5-6	19-21
High-tech customized products:		
— boilers	4	9-10
— power generating equipment	6-7	11-14
— telecoms equipment	6-8	18-22
— railway rolling stock	10-11	19-21
Works:		
— construction/civil engineering	3	4-7
Services:		
— consulting engineering	1	5-6
EU average	2-4	5-9

While there seems to be increased competition and progressive integration of markets for procurement of products in particular, there is as yet little evidence of substantial savings to public purchasing authorities. There is anecdotal evidence of some significant price and technology improvements, particularly from entities which systematically apply the new procedures and those which use the threat of cross-border competition to force down established suppliers' prices. However, new entrants tend to price markets, and their market share is still small suggesting that expected savings have not yet been achieved.

Contracting entities and suppliers are only beginning to probe the new SMP opportunities. The fact that only 15% of purchasing entities thought to be subject to the legislation have published tenders suggests that entities have yet to come to grips with the new disciplines. The fact that the numbers publishing tenders and complying with the new procedural requirements are continually increasing, suggests that entities are still on a 'learning curve'.

Research identified a number of provisions in the legislation which might benefit from clarification (notably boundaries between works, services and supplies contracts and 'aggregation' rules). More monitoring of the economic realities of procurement markets in the

Member States will be necessary in order to judge the actual market-opening effects of the regime. Failure to detect and penalize non-compliance or infringement of procurement rules will lead to disillusionment on the part of potential suppliers, and reduce responsiveness to tenders. Low levels of responsiveness will discourage purchasing entities from respecting the procedures because of limited perceived pay-back in terms of greater competition or a wider choice of suppliers. The only way to prevent this vicious circle is effective surveillance and enforcement at national and EU level.

2.6.2. Industrial and intellectual property protection

The coexistence of separate national systems for protection of industrial property does not pose a threat to the free circulation of products or patented technologies. Interpretation of the Treaty (the 'doctrine of exhaustion') implies that Member States or holders of property rights cannot oppose parallel importation of those products or derived products once the goods have been marketed anywhere in the EU by the right holder or with his consent. This approach safeguards free circulation, but is less satisfactory in creating a legal framework which offers investors in proprietary technology and rights a secure return on their investment. At present, operators

who wish to defend themselves against imitation or infringement of property rights by partner country operators could be compelled to obtain parallel protection in all Member States. The pharmaceuticals sector is an

example where operators have to obtain a 'bundle' of national property rights. In other sectors, such as motor vehicles, the need for watertight protection is confined to a number of strategic markets.

Box 4 Importance of a single market for capitalizing on investment in IPR

(a) Pharmaceutical sector

More than any other industry, the European pharmaceutical industry needs a large internal market to recoup dramatically increasing investments in research and development. The R&D costs for a new active substance are estimated to amount to ECU 300 million. Efforts to harmonize European pharmaceutical legislation and the implementation of the Community marketing authorization system, contribute to the strengthening of the competitiveness of the pharmaceutical industry by providing a more unified market together with the means to bring products to market more effectively.

For the pharmaceutical industry, protection of new chemical entities is critical. To this end, patents are obtained in every Member State and they are used offensively to prevent infringement. Movement towards a unitary patent option would be of real interest but this would require the deficiencies of the Luxembourg Convention to be resolved.

Specific measures, such as the creation of a supplementary protection certificate (Council Regulation (EC) No 1768/92) restores the protection conferred by the patent, by extending the period of effective protection to 15 years after the first Community marketing. This measure is warmly welcomed by industry as standard patent duration is regarded as too short to allow investment in industrial property to be recouped.

(b) Motor vehicles

The Whole Vehicle Type Approval system with its single authorization procedure already constitutes an important step in helping operators to obtain a greater return on investment in industrial property. By substantially reducing the time to market (by up to three months), the single authorization procedure will reduce development costs and allow capitalization of investment from an earlier stage. The resultant savings are estimated to be ECU 30 million per model of 10% of costs of development (Ernst & Young).

The industry also has a strong interest in Community initiatives to create Community instruments for protection of investment in industrial property. This interest is particularly pronounced for trade marks, as the image of the producer is heavily bound up with the mark. Patents, on the other hand, are only secured for major manufacturing countries. They are increasingly used by manufacturers and their first and second tier suppliers in defining ownership and the framework for agreements. They are not used in adversarial fashion as the threat of infringements is relatively limited — high sunk costs prevent hit-and-run entry by pirates.

Pecuniary and time penalties implied by parallel registration of rights in different Member States require attention if the EU is to equip itself with a satisfactory framework for protection of industrial property rights. Substantial progress has been made to date under the aegis of the European Patent Convention in the area of patent protection. Further progress has been made in tandem with the SMP in respect of other issues and rights (trade marks, designs, anti-counterfeiting).

Recent efforts strike a balance between the advantages of streamlined procedures for obtaining EU-wide protection ('one-stop-shop') and offering economic operators sufficient flexibility in management of their industrial property portfolio. Management costs increase with the number of countries covered and many operators will

wish to choose the number of countries in which they enjoy protection. EU initiatives in this field have therefore left national systems of industrial property protection in place but have harmonized them considerably. Construction of this hybrid system — a working example of 'subsidiarity/proportionality' — has centred on the following.

- (i) Introduction of the possibility of obtaining a Community trade mark, through the Community Trade Mark Office which began work on 1 January 1996. The importance of this option to producers of branded products who wish to implement EU-wide sales and marketing strategies is reflected in 30 000 applications for Community trade marks in the first six months of the life of the Office. This option,

together with systems of national mechanisms for registering trade marks, is welcomed by industry.

- (ii) Patents: the European Patent Convention already provides an avenue for obtaining a 'bundle' of national rights through a single filing application. While the European Patent Office is well-regarded by users, they are concerned about the high costs of obtaining protection which is sometimes perceived as often unused translations. Property-right owners would be reluctant to use unitary EU patents, because of concerns about inconsistent quality of judicial rulings on the validity of patents. Unitary patent rights would carry the risk that patents struck down in one Member State would be void throughout the EU — creating potentially huge losses for the property holder. Industry has also pleaded for a reassessment of the structure of the patent system in Europe, in order to make it less complex and more cost-efficient. There is continued support for EU measures aimed at further convergence of national industrial property provisions protection, as in biotechnology for example.

Property owners support common approaches based on EU action, for example the supplementary protection certificate for pharmaceuticals or plant protection products, and existing Commission proposals in the field of protection of biotechnology inventions.

The Community has also been active in the field of intellectual property protection — primarily in dealing with copyright issues. Since 1991, five directives have been adopted in respect of copyright and related rights, aimed at smoothing out differences in Member States' protection levels. Previously, operators were reluctant to exploit protected rights in Member States offering low levels of protection. Measures adopted concern key issues linked to the protection of computer programs and databases, cable and satellite broadcasting, rental rights, lending rights, certain neighbouring rights as well as the duration of rights protection. However, the benefits of single market protection have so far been denied because of inadequate implementation and enforcement. Only one of the directives has been implemented by all Member States.

The EU has therefore an important role in the field of industrial and intellectual property protection. Appropriate EU action can contribute to a framework

which offers investors in innovation and quality sufficient assurances of a reasonable return on their investment. EU measures to date offer potential users flexibility as regards geographical coverage, and are highly regarded by property right owners.

2.6.3. Direct taxation

A number of obstacles to the smooth functioning of the single market remain in the field of direct taxation, particularly in relation to the freedom to provide cross-border services, the freedom to establish businesses in other Member States, and the free movement of persons and capital. Certain national measures which are designed to preserve revenues in the Member States concerned, or to prevent the loss of tax in an international context, can significantly impede the realization and development of the single market. This situation creates difficulties both for enterprises who do business in the single market and for national administrations, faced with problems of how best to operate an effective and non-discriminatory tax system within the EU which at the same time meets their national tax policy needs.

The central concern which underpins all these problem areas must be the elimination of double taxation on, and other possible tax obstacles to, cross-border income flows, while at the same time ensuring taxation at least once in the EU.

The taxation of branches of companies resident in other Member States continues to give rise to practical problems for the freedom of establishment. Although a branch is not in an identical situation to a resident company, its overall tax treatment must not be more onerous. Current barriers include imposing 'branch taxes' or taxes at a higher rate than on resident companies, not giving benefits (such as group reliefs), and not allowing branches to impute withholding taxes.

The cross-border provision of services, particularly financial services, also poses particular difficulties. The removal of regulatory barriers in this field has created the conditions for a true cross-border market but the continued existence of certain national laws restricting tax benefits to nationally-established providers undermines this objective. Current problems include limits on the tax deductibility of life insurance premiums; mortgage interest payments; and higher taxation of the proceeds of for-

eign life assurance policies. In addition, tax barriers (or differentials affecting savings income) distort the allocation of capital within the single market.

Although recent judgements in the European Court of Justice have decided that non-resident workers should not be taxed more heavily than a country's own residents, the principle of the free movement of persons is not yet wholly free from tax barriers. The mobility of workers within the EU is still trammelled by tax considerations, for example in the important area of pension provision for migrant or seconded workers and self-employed persons.

The Council's non-adoption of key legislative proposals in the direct tax field has contributed to the persistence of tax impediments, which increase the costs of doing business in the single market. Cross-border interest and royalty payments within groups of companies may still suffer withholding taxes, leading to cash flow losses and administrative costs. After long negotiations on the Commission's proposal to eliminate these withholding taxes, the Commission withdrew its proposal in November 1994. No progress has been made on the Commission proposal for taking account of the losses of subsidiaries and permanent establishments in other Member States for tax purposes.

In conclusion, there is evidence that taxation regimes can cause obstacles to and distortions in economic activity. In this way taxation problems are impeding the smooth functioning of the single market. This is particularly so in relation to the financial markets and financial services. In many Member States the taxation treatment of savings, insurance and pension products can lead to market inefficiencies rather than to an openness to market forces. Given the high degree of capital mobility which now exists this is also a particularly severe problem of tax avoidance and evasion in relation to derived investment income.

2.6.4. Company law

Nine Directives were adopted between 1968 and 1989 harmonizing 'to the necessary extent' (Article 54.3(g) of the Treaty) the safeguards which national law requires of companies for the protection of their members or third parties. These provide an adequate framework for the conduct of cross-border business by companies and for

their freedom of establishment. The Directives concern mainly the conditions for setting up companies, publicity, the maintenance of their capital, their financial reporting and mergers and de-mergers between companies. Transposition of the Directives is largely complete and non-compliance is not a general problem. (One major exception, involving the non-disclosure of accounts by SMEs in one large Member State, has provoked numerous complaints, implying that importance is attached to compliance with EU Directives in the marketplace. The case is currently before the Court.) The overall result is that companies set up subsidiaries and branches and conduct business with each other across internal borders under satisfactory conditions as regards legal security and transparency.

Nevertheless, it cannot be said that 'free movement' has been achieved for companies in the single market. The degree of harmonization achieved is limited, in view of deeply rooted differences between Member State systems which they have been understandably reluctant to change. The principles of subsidiarity and proportionality require that such differences be respected but some further modest degree of harmonization could be beneficial, for example in the laws concerning the structure of companies and the role of the various parties within them.

Differences between national approaches do not present insurmountable obstacles to companies wishing to operate at a single market level but they do involve costs. These would be diminished if 'bridges' could be established between the different jurisdictions. Such bridges could either be of an over-arching kind (European legal vehicles which would offer an alternative alongside national models, such as the European Company Statute) or of a linking kind (providing the necessary legal security for e.g. cross-border mergers or transfers of seat). Some proposals to create such bridges have been made, but remain unadopted (see Section 3.1.4.). Their absence is felt in terms of unnecessarily complex and cumbersome legal and organizational structures which impose costs on companies, limit their flexibility and damage competitiveness. The legal environment thus represents a brake on companies' efforts to exploit the full potential of the single market. It should on the contrary be designed to encourage such efforts. The Regulation on the European Economic Interest Grouping is an isolated legislative success in this respect.

2.6.5. Protection of fundamental rights and freedoms

The increasingly frequent recourse to the processing of personal data in every sphere of economic and social activity and the new data exchange requirements linked to single market integration have necessitated the introduction at Community level of measures to ensure the protection of personal data.

The Community has taken a first step to provide such protection, in the form of Directive 95/46/EC on the protection of individuals with regard to the processing of personal data and on the free movement of these data. The main purpose of the Directive is to remove obstacles to the free movement of data between Member States while at the same time ensuring a high level of protection for individuals.

The deadline for implementation of the Directive into national law is 24 October 1998. Leaving differences in the level of protection between Member States would continue to hurt both individuals and business. Incoherent and conflicting national rules make it very difficult for the same service, for example, to be provided across all 15 Member States and the result would be fragmentation of the single market.

Continued attention to the regulatory framework is therefore needed, in particular as far as new on-line telematic services are concerned.

3. Reasons for obstacles to free movement

As noted in the previous chapter, the Union's efforts to complete a single market have resulted in measures of varying effectiveness. This variation is caused by different factors which influence the quality of regulations and have to some extent been known from the start of the SMP.

- (i) Some proposals have not yet passed the Council. Most of the missing Directives represent complementary pieces to already existing legislation.
- (ii) Other proposals for single market legislation have been significantly altered in Council in the need to find a consensus. As a consequence, certain loopholes and limitations in the scope of single market measures were expected to result in reduced effectiveness from the outset.
- (iii) A few single market regulations contain very detailed provisions and the initial compliance costs may be high. In the long run, these should decrease and be more than compensated by their corresponding benefits.
- (iv) Deficiencies caused by unexpected difficulties stem from delays in the transposition of single market measures into national legislation, in standardization and in market surveillance and uneven enforcement.
- (v) Another unforeseen obstacle was the emergence and persistence of national regulatory and non-regulatory provisions, which in most cases cannot be overridden by EU legislation but which inhibit market access for companies and the establishment of pan-European strategies.
- (vi) Growing concerns have been expressed about the emergence of new trade barriers, particularly, but not exclusively, in the environmental field which business sees as seriously jeopardizing the functioning of the single market.
- (vii) Finally, a variety of non-regulatory obstacles (for example, access to justice, and administrative barriers and inefficiencies) become relatively more

important as threats to full realization of the single market.

Therefore, deficiencies in the single market still exist, although they are comparatively limited in scope compared to the achievements.

When examining the reasons for regulatory inefficiencies, we must therefore consider the different levels of legislative responsibility (for example, European, national, regional and local) and also take account of regulatory and non-regulatory developments at the international level. The main reasons behind the defects and inadequacies of the regulatory and enforcement mechanisms may well relate to complexities of the EU decision-making process, the persistence of national preferences, inadequate policy objectives or unexpected non-regulatory developments. It is also important to bear in mind two key issues:

- (i) the increasing concern expressed by business for regulatory reform and administrative simplification; solutions should primarily take the form of improvements of the existing regulatory framework rather than additional pieces of legislation;
- (ii) application of the subsidiarity principle: business has constantly repeated that, although full respect for the subsidiarity principle should be ensured, this should not lead to greater fragmentation of the single market.

3.1. Non-adoption of single market measures

Ten years after the White Paper programme was launched, a 'hard core' of proposals from the 1985 White Paper still remain to be adopted. In addition liberalization in sectors which were not covered by that programme has not been completed. The main stumbling blocks are in key areas affecting business management, such as company law and corporate taxation, the free movement of people, cross-border payments and full liberalization of the transport and energy markets.

European enterprises consider that the failure of the EU to put in place a consistent and simplified taxation system at EU level or to remove discriminatory provisions which create distortions between Member States' tax regimes prevents them from conducting operations as a single, integrated Union-wide business and from fully exploiting single market opportunities. This has been pointed out many times by business organizations who want an urgent breakthrough in taxation and company law.

3.1.1. Company taxation

The central objective must be to create a policy framework to eliminate all forms of double taxation on, and other possible obstacles to, cross-border income flows. The framework should also prevent tax losses within the single market as a result of cross-border arbitrage, avoidance or evasion.

Problems often referred to by business, which are only partly covered by current Commission proposals, include the persistence of withholding taxes on interest and royalty payments within groups of companies, the absence of a common system for EU-wide consolidation of losses within groups, the tax treatment of permanent establishments compared to domestic companies, as well as for inter-company dividends, and the uncompleted network of bilateral double taxation treaties to avoid double taxation.

Although tax harmonization is not an objective in itself, a better level of approximation and integration of direct taxation rules in the EU would enable companies to improve manufacturing, marketing and other functions on an EU-wide basis, with the necessary mergers, shift of business activities and changes in ownership structures not being hampered by tax impediments.

3.1.2. Approximation of taxation treatment of investment income

The current coexistence of different national taxation systems for investment income and differences between residents and non-residents distorts capital movements.²⁸

Differences in the structure and operations of national fiscal and taxation regimes are identified as resulting in distortions in banking and financial markets. Tax relief enjoyed by mortgage borrowers in the UK for example, distorts the housing finance market.²⁹

3.1.3. Transition towards an origin-based VAT system

Many concerns do not in fact stem from the transitional VAT regime but rather from difficulties with the nature of VAT itself. The present system is based on physical monitoring of movement of goods and is no longer suited to modern business practices. In addition using Directives to set up the system left Member States with options. As a result divergences have existed from the beginning. These divergences have now been exacerbated by the fact that traders are increasingly being affected by other Member States' legislation, and how it is applied. Divergences in the application of the common VAT system have a variety of origins: special arrangements, options and powers allowed by the directives, temporary or transitional derogations which have not been repealed, Council derogations and shortcomings in transposition or differences in implementation of common provisions.

The recently-proposed move to a definitive, origin-based system aims to move these problems by removing any distinction between domestic and intra-EU transactions and providing legislation which can be applied and enforced equitably throughout the EU. The Commission has set out a multi-annual programme of work³⁰ together with a timetable for putting forward proposals which, if agreed by the other institutions, should lead to the introduction of a real Community-wide VAT system, fully

²⁸ This may, at some stage, have a disruptive effect on EMU, especially in the transitional phase if all currencies are not part of EMU. Any EU level solution which appears particularly important for banking, should however, be part of a wider OECD-wide arrangement.

²⁹ Credit institutions and banking study.

³⁰ COM C(96) 328 final.

adapted to the requirements of the single market and enabling operators to fulfil their fiscal obligations in one place in the European Union.

3.1.4. Company law

Cross-border mergers are still hampered by legal problems. Two unadopted proposals — the 10th Directive and the European Company Statute — would provide the missing legal framework and allow companies to reap considerable cost savings through simplified organization and administration.

Companies urgently need an instrument such as the European Company Statute in order to adapt their corporate structure to exploit fully the benefits of the single market. This form of incorporation could generate considerable cost savings for companies, with direct benefits for competitiveness and knock-on advantages for growth and jobs. The Competitiveness Advisory Group, in its first report of June 1995, puts these potential cost savings at ECU 30 billion per annum.

The adoption of the proposed framework Directive on take-over bids would guarantee minimum standards of protection for shareholders in case of take-overs. This measure does not tackle structural barriers to take-overs (low dependence on public listings, various exceptions to the 'one share, one vote' principle, etc.) but could provide a framework of greater legal security which would make it easier to address these other obstacles later.

3.2. Inadequacies of the single market legislation

Research has revealed some qualitative problems with existing measures which, in a few instances, do not appear suited to the needs of economic operators wanting to engage in cross-border transactions. These design faults are due to:

- (i) lack of precision and clarity of the legislation, thereby opening the door to different interpretations and requirements;
- (ii) too limited scope, which has led to unresolved problems continuing to restrict free movement;

- (iii) over-complicated procedures, leading to excessive compliance costs.

Where this has occurred, the result has been market fragmentation, legal uncertainties for some operators, and reluctance to seek additional market opportunities.

3.2.1. Unclear legislation

Although the SMP aimed to create a level playing field by providing a set of rules to be applied evenly across Member States, some rules lacked clarity and precision. This resulted in divergent, occasionally even conflicting, interpretations in the Member States, leading to a situation whereby business had to face different requirements from different Member State trading partners and a fragmented, rather than unified, market.

Reasons behind this defect can be found in one or more of the following factors:

- (i) complex, EU decision-making processes, unanimity voting in Council, and last-minute compromise amendments to reach consensus, may have resulted in a dilution of the original proposal;
- (ii) Member States' insistence on preserving particular national rules and practices may have forced them to seek derogations from the common provisions, thereby creating distortions within the single market;
- (iii) the decision to use directives, which leaves Member States to decide how to achieve the enshrined objectives, rather than regulations, may have led to some loss of harmonization in the implementation phase.

A first example is the VAT transitional regime. Physical tax frontiers were removed in 1993, but this was achieved without any significant degree of harmonization or diminution in Member States' sovereignty. In addition to the complexities of the new arrangements — and in particular the fact that traders were obliged to create distinctions between domestic transactions and intra-Community supplies — the nature of Community VAT legislation has, as is explained in paragraph 3.1.3 above, always allowed Member States a wide variety of options and derogations from the common provisions. In total there are currently 66 special arrangements, options or powers granted by the Directive, some 130 temporary,

transitional or other derogations which have not been repealed as well as divergences in the way Member States have chosen to transpose or interpret common provisions.

This situation creates legal uncertainties and businesses cannot be sure that they are acting in accordance with the Member States' national legislation. Operators must invest time and money to be familiar with the details and practical effects of the legislation of up to 15 Member States. All these elements interfere with the smooth functioning of the single market and open the door to tax evasion and fraud.

Similar examples are found in areas like public procurement as well as in a few sector-specific measures.

- (i) Operators find procurement legislation unclear about the main requirements imposed on them.³¹ This includes in particular the boundaries between works and supply/services contracts, the use of 'framework agreements' in the public sector, and permissible criteria for shortlisting in the public sector. There are also a few inconsistencies and omissions in the Directives. One example cited is omissions in the supplier Directive of obligations found in the works and services Directive on how bids are invited in negotiated procedures and the information to be included in invitations.
- (ii) There is evidence that the Directive on noise emission from construction plants was too vague and led to different interpretation by Member States, notably in the way noise tests should be conducted.³² These differences are being addressed in an amended Directive.
- (iii) The construction products Directive adopted in 1988, has so far failed to ensure free movement because of the difficulty in negotiating the necessary complementary measures, first interpretative documents and then harmonized European standards.
- (iv) Some manufacturers also pointed out the unreasonable requirements of the machines Directive, which raised costs unnecessarily. In many cases, however,

these proved to be misinterpreted by manufacturers. This suggests that the Directive may be difficult to understand in places and that guidance documents are important.

3.2.2. Limited scope

In a few cases, single market legislation has not adequately encompassed new market and product developments or identified new needs or barriers. It has therefore failed to meet current business requirements. Economic operators were left with legislation of little relevance and the risk of facing a legal vacuum for some of their operations.

Some businesses have pointed to the need for a consistent, global policy framework for their sector, in order to ensure greater consistency between the different sector-specific measures and promote a more ambitious overall approach. They suggest that the framework could provide new provisions compatible with technological progress or international economic developments.

Several single market provisions were adopted with a limited scope, which was probably the price to be paid to secure agreement at Council level. In the audiovisual sector, the 'Television Without Frontiers' Directive, which was intended to provide broadcasters with a legal basis upon which to transmit services from one Member State to another, only sets minimum regulatory standards. Indeed, several articles in the Directives (Articles 3, 8, and 19) allow Member States to apply stricter rules in the context of cultural issues, advertising and sponsorship (although these articles are modified or deleted in the current revision of the Directive).

There continue to be significant variations in the rules relating to advertising and whilst the 'Television Without Frontiers' Directive enables broadcasters to ensure compliance only with rules of their place of establishment, the existence of stricter measures in other Member States may force advertisers to diversify their commercials in order to comply with national legislation.

In the pharmaceutical sector, the 1989 transparency Directive had limited effect in removing barriers to trade

³¹ Public procurement study.

³² Construction site equipment study.

and facilitating market access. The Directive aimed to make price determination and reimbursement processes more transparent. Attempts to extend its limited scope to bring the sector closer into line with normal single market conditions have been rebuffed by Member States, who retain control of public expenditure on medicines.

In the area of intermediation and distribution of financial services, in particular insurance, the absence of more binding legislation than the Recommendation of 1991, poses a problem for the completion of the single market, since insurance intermediaries who have no single licence effectively have to obtain authorization to operate, which is often time-consuming and costly, in 15 different markets. Similarly, in the area of contract law certain Member States' law requires foreign insurance providers to conform with the totality of their insurance legislation on the pretext that such measures are necessary and justified by 'general good' considerations.

The banking and credit sector also suffers from too many general opt-outs in the legislation, such as restricted access to certain activities and restrictions relating to banking staff qualifications. Some barriers relate to financial services marketing; for example, door-to-door selling and product prohibitions or restrictions persist in several countries. Although they may not necessarily discriminate against competitors, these barriers may discourage entry and are considered obstacles by potential entrants. In Greece, for instance, foreign banks are not allowed to lend for real estate transactions; in Italy, the provision of payment instrument services by non-residents is restricted.

The leased lines Directive states that tariffs must be based on the principles of cost orientation and transparency, and be independent of the application for which they are being used. Operators must implement cost accounting for these purposes. However, for many types of leased lines, tariffs do not respect this principle. This unsatisfactory situation is due, in part, to the absence of effective competition in leased lines, and reflects the fact that the ONP leased lines Directive is not adequately implemented in many Member States. However, important progress is being made now that clear dates for infrastructure competition have been set.

In this field of industrial products, harmonization does not cover installations rules. In some cases (for example gas appliances, electro-medical and telecommunications equipment) it might lead to difficulties in using products conforming with the Directives.

Some sectors also complain about substantial delays in adopting European standards and rigidities in product type approval measures, which are not reviewed frequently enough to keep pace with industrial innovation. Although the legislation itself is inadequate, business has often considered this an example of the deficiencies of the EU decision-making process. An example is the telecommunications equipment sector, where the backlog in implementing such action as type approvals and standards development is substantial and will take some years to work through, therefore delaying the benefits of reform.³³ Outstanding problems are concentrated in the area of terminal equipment, where the development of 'one-stop' approval based on common EU standards has been particularly problematic. However, the remedy consists more in continuing administrative attention than on legislative action. The automotive industry also advocates greater flexibility and frequent review of type approval measures to ensure that they keep up with innovation, for example in remote keyless entry.

3.2.3. Over-complicated procedures and high compliance costs

Companies sometimes complain about the costs of implementing the SMP, under two different headings:

- (i) the first is the short-term, transitional costs of change to harmonized systems and conformity with new technical requirements; these are inherent in any changeover and are offset by additional gains from improved market access and export opportunities, although for firms operating on local markets (particularly SMEs), compliance with new technical standards may be disproportionately costly;
- (ii) the second is an excessively complex and detailed regulation, which forces companies to invest substantially in order to comply; such regulations may

³³ Study on the impact on manufacturing telecommunications equipment.

have arisen from a combination of ambitious policy goals and the desire of Member States to maintain some of their prerogatives.

The equipment and machinery sector experienced short-term, transitional costs affecting SMEs in particular. Companies must manage some new documentation, in order to comply with the new conformity assessment procedure which replaced multiple national systems. In some cases, where existing products did not comply with the new essential safety requirements, they also had to adapt models to new specifications. Some products, which were previously only marketed in one Member State, also experienced increased costs for conformity assessment testing, although these costs will have been reduced for other products.

In other cases, the complex wording of directives imposed such a high burden of administrative requirement that they actually deterred businesses, especially small businesses, from seeking additional market opportunities. These measures have therefore been a major impediment to market diversification and full exploitation of SMP potential benefits. Companies were faced, for example, with a new intra-Community trade statistics collection system, Intrastat, which required a high level of detail in the statistical returns. The 'Combined Nomenclature', for example, is difficult to use to identify the correct commodity code; the required statistical value is difficult to assess, and the need to indicate net mass for certain products is irrelevant. In addition, most information providers complained about considerable delays in the availability of trade statistics and considered that the extra costs incurred by the changeover to the new system were not justified compared to the use being made of these statistics. Most of the abovementioned issues are being considered by the group set up under the SLIM (Simplification of the legislation of the internal market) initiative to review and simplify the Intrastat regime.

The new rules introduced under the VAT transitional regime were also seen as extremely complicated. They often depend on factors which cannot be determined objectively. This complexity tended to reinforce the divergences in applications by Member States of common provisions which have already existed since long

before the SMP by the fact that traders are now affected to a greater extent by the way legislation is applied by Member States other than the one in which they are established or pursue their usual activities. Rules determining the place of supply, the need for fiscal representatives and the introduction of special schemes for distance selling or new means of transport, substantially complicate the system. In some cases, the rules are a major disincentive for operators, particularly small ones, who experienced difficulty with the provisions requiring local VAT registration for work and spare parts related to equipment installation and repair, (regarded as locally supplied goods and services). This means that a non-domestic manufacturer must have a fiscal representative in order to sell and install a machine, even if he has no local facilities.

Associated costs were sometimes disproportionately high in relation to turnover and severely limited the ability to trade in other Member States and the scope for sound competition. These issues should however find a solution with the move to a definitive, origin-based regime as is currently being proposed by the Commission.

3.3. Ineffective implementation or enforcement

Whatever their shortcomings, agreed Community rules have to be put into law in every Member State and applied effectively and fairly. This review has shown that today this is still not the case.

3.3.1. Inadequate transposition

Although the transposition rate for single market measures is steadily improving, with an average rate of 92.9% for EUR 15,³⁴ inadequate transposition still emerges as a major concern in some sectors and areas. Substantial delays have been experienced in sectors such as chemicals (Directive on marketing of dangerous substances), public procurement and insurance. Poor quality transposition has also in some cases prevented business from fully exploiting the potential of the single market.

³⁴ Situation as at 8 July 1996.

It is difficult to assess the reasons for Member States' reluctance to transpose into their own legislation a text they have (most of the time) agreed in Council, but it may be partly due to the slowness and complexity of national parliamentary processes or political factors.

Slow transposition can seriously disrupt business. This is particularly true for public procurement, where some 10% of the measures already in force have not been implemented correctly. Contractors therefore do not know which rules and procedures apply to them, and all interested parties face legal uncertainty. However, delays in transposition can be seen as a transitional problem.

On the other hand, deficiencies in the quality of transposition may be more problematic. They are influenced by national sensitivities and policy priorities, and can be more difficult to resolve.

Member States also use different transposition 'techniques'. In the case of public procurement, some Member States have chosen to transpose 'by reference', i.e. by adopting legislation which simply provides that the rules in the EU Directive are applicable and enforceable under national law. Others have chosen to implement the rules largely by 'copying out', that is by repeating them verbatim in the national legislation. Others prefer to reorganize and rephrase the rules in their own legislation, with the risk, or even the aim, of elaborating on some of the requirements. This may result in legislation which, after transposition, leads to legal uncertainties and costly problems of interpretation. The overall effect of these differences is that operators may have to cope with different requirements, according to the Member States in which they want to tender, which leads to high compliance costs and ineffectiveness.

Another example of different transposition techniques which cause difficulties concerns the recognition of diplomas. The general system Directives cover a wide range of regulated professions; some Member States have chosen to adopt a general 'horizontal' measure which, in essence, transposes the general principles laid down in the Directives and appoints national competent authorities. Detailed rules applicable to individual professions must then be put in place by secondary legisla-

tion; this has frequently been delayed, rendering the primary legislation inoperable. Alternatively, Member States have chosen to transpose 'vertically', profession by profession, which has also produced delays, and sometimes reproduction of the same errors or omissions.

The number of derogations and the duration of transitional periods given to some Member States has also contributed to fragmentation of the single market in its early years. Transitional periods are by definition temporary and need not receive too much attention. Derogations, on the other hand, can be more problematic. For instance, the considerable freedom for national authorities to impose additional requirements in the financial services sector, by using the concept of the 'general good' opt-out, causes many uncertainties and inhibits freedom to provide cross-border services.

3.3.2. Ineffective enforcement

Uneven enforcement of EU legislation had already been identified in the Sutherland report⁸ as had the ensuing strategic programme for the internal market posing a major threat to the proper functioning of the single market. The various studies commissioned in the framework of this report confirm that uneven enforcement is still often regarded as being the barrier most difficult to identify clearly and to overcome because it entails close scrutiny of national, regional, or even local practices which cannot be supervised easily and a high level of accurate information exchange between private operators and between public administrations.

Enforcement problems can arise from different sources:

- (i) the way in which the high level of protection which is embodied in Directives governing the free movement of products will be achieved in practice.

The uneven way in which Member States apply the 'general good' clause in the financial services sphere is often referred to as a barrier to the free provision of financial services in the Community. Member States invoking this clause interpreted the new notification requirements introduced by the

⁸ *The internal market after 1992: Meeting the challenge*. Report to the European Commission by the High Level Group on the operation of the internal market, October 1992.

Examples of inadequate enforcement

In the air transport sector, the reluctance of some Member States to enforce the existing regulations, particularly in the early stages of the liberalization process, has hindered carriers taking advantage of opportunities that are intended to be available, for example, Italian resistance to Lufthansa consecutive cabotage operations, Greek delays in processing applications for licences and aircraft operators' certificates or France's limitation of access to Orly airport. Some of these problems have nevertheless been solved further to the Commission's effective intervention.

The telecommunication equipment sector also identified weak and slow implementation and enforcement of some national legislation as being a major source of cost. In particular, the backlog in standard development and the residual patchy approval procedures hinder business development, especially for smaller producers. However, good progress has been made in this area, in particular since the Community type approval mechanism is becoming effective and is now producing its first, positive results, in particular for the GSM and ISDN networks. This Directive is now being revised in order to facilitate the marketing of terminals, by proposing to move from the Community type approval system to a system of declaration of conformity to be made by the manufacturer.

The same problem exists in the chemical sector where Directive 94/27/EC, the 12th amendment to Directive 76/769/EEC, which aims to control the use of nickel in jewellery, so as to combat the problem of allergy to nickel, approximates the national law on this subject in Germany, Denmark and Sweden. However, the Directive cannot enter into force until CEN has published standards incorporating test methods to check the compliance. This work, which is effectively in the hands of the industries who want to stall entry into force, is unlikely to be complete before 1998. The result is that there is so far no single market in jewellery type products.

Cross-border supply of banking services, particularly in retail banking, has remained relatively low due to enforcement problems. There has been a very marked tendency on the part of the Member States' authorities to delineate freedom of services and freedom of establishment under the second banking Directive in such a way that, sooner or later, a bank providing cross-border services is obliged to have recourse to establishment (see below).

second banking Directive in such a restrictive way that it created uncertainty over the legality of certain transactions and the obligations to notify the competent authorities about the services to be provided. This situation is currently being addressed by the Commission to follow up the draft communication issued in October 1995. The mortgage sector suffered substantially from the 'general good' opt-out: cross-border mortgage loans have been void because it was considered that it would run counter to the general interest of Member States' institutions. In fact, mortgage credit law in Belgium and all consumer law in France have been classified as part of the 'general good';

- (ii) lack of, or delay in, adoption of other directives which are not necessarily implementing directives but which are seen as complementary.

This is for instance the case in telecommunications services, where services and ONP Directives required adoption of Directives on the mutual recognition of licences for the application of ONP to telephony. These texts are still blocked because of problems of competence between the institutions;

- (iii) the quality and availability of product testing and certification services and public controls;

- (iv) some sectors, in particular the processed foodstuff sector, complain about the discriminatory application of public controls, both between and within Member States. This occurs particularly where control is delegated to local and regional authorities. Considerable differences in the interpretation of levels of strictness can prevail between control bodies. In cases where mutual recognition applies, inspectorates in an importing country may also be unable to assess the conformity of the results carried out in another Member State, which suggests a need for more information about national regulations and related conformity assessment procedures. Evidence about low quality compliance controls was also found in the distribution sector.

Enforcement of the regulations on driving and resting time in road freight transport is seen as discriminatory. Because small companies are relatively hard to trace, Member States check larger operators more frequently. This implies a negative side-effect in terms of road safety and offers small companies the possibilities of unfair competition.

In general, enforcement of EU legislation by private parties is sought through the Court. The absence of effective judicial remedies or the existence of procedures blocking the enforcement of Community legislation may hinder this process. This is particularly evident in those single market matters where harmonization has taken place and where additional measures to guarantee proper enforcement of harmonized law before competent jurisdictions have often been introduced (e.g. for the Community Trade Mark, a system of judicial enforcement was required). But this is also the case in areas such as liability of the State derived from infringement of Community law. Enforcement of this liability by private parties in civil actions may also be limited by restrictive procedures, established by Member States. In relation to certain aspects, especially the free movement of persons, it is unrealistic to expect individuals with limited resources to take action before national courts; distance often increases the cost and limits access to legal advice or help. In addition, the degree of awareness of Community law among legal practitioners is still disappointingly low.

- There is no coordinated surveillance mechanisms or proper framework to ensure even-handed enforcement throughout the Community.

Article 100a provides for Community harmonizing legislation which embodies a high level of protection. Users, be they final consumers or business purchasers, legitimately expect that the application of these measures will deliver this high level of protection.

In order to operate effectively, producers need legal security and a legislative framework which provides for a level playing field. Producers require that there be reasonable equivalence in control of compliance with Community legislation. This concerns both divergences in the application of rules as well as intensity of controls and the severity of penalties in the event of infringement.

As regards public health, consumers expect that the competent authorities will be capable of implementing appropriate preventive actions (precautionary principle).

Specific considerations related to the new approach and the global approach

The 'new approach' to technical harmonization, by virtue of its characteristics, entails a heightened need for control compared to the methods of technical harmonization which were previously applied.

- On the one hand, they rely on the principle according to which the producer is solely responsible for the conformity of the product with the legislation. Certification bodies are responsible for those controls which they carry out prior to the placing of the product on the market, and for which they deliver a certificate of conformity. In no sense do they assume the responsibility of the producer. This situation represents a departure from previous practice where, at least in several sectors, public authorities authorized or approved products prior to their placing on the market. Consequently, they shouldered the responsibility for ensuring compliance of products with legislation. This new situation implies that Member States undertake substantial efforts to monitor producers who have declared the conformity of their products, with a view to guaranteeing simultaneously a high level of protection and equivalent competition conditions. This need is accentuated in directives for which products are placed on the market without the prior intervention of a third party, as illustrated by the case of the toy safety Directive.
- On the other hand, the flexibility offered by the legislation in terms of technical solutions coupled with the fact that, in principle, the solution which is applied is no longer indicated on the product in the form of a mark (of conformity to a standard, for example), require the organization of control systems. Services responsible for controls can no longer immediately distinguish those products carrying marks. In this respect, the introduction of CE marking and the fact that it substitutes, at least in part, for certain pre-existing marks, implies increased and widespread surveillance.
- The absence of effective remedies may hinder the correct enforcement of Community legislation. The provision of effective remedies requires a chain of mechanisms; from the capacity to identify a defective product to the willingness and ability to take measures to remove it from the market and, if appropriate, impose sanctions.

Redress can be sought by private parties through the national courts but here, too, there are barriers. The absence of effective judicial remedies to enforce Community legislation may hinder redress. Common measures to guarantee proper enforcement of harmonized law by the courts have sometimes been introduced (for example, for the Community Trade Mark), but elsewhere the enforcement of the liability of the State by private parties in civil actions may be limited. In some cases, it is unrealistic to expect individuals with limited resources to take action before national courts. Even when such action is taken, the degree of awareness of Community law among legal practitioners is sometimes very low.

Enforcement of public procurement Directives is problematic, for a number of reasons:

- (i) a dependence on the supply-side to police its customers. All current enforcement arrangements rely upon suppliers identifying an infringement, such as non-publication or incorrect application of procedures. This presupposes a high level of supplier awareness of complex and technical regulations which affect their customers;
- (ii) the lack of effective national systems of redress. The inability to obtain remedies sufficiently quickly and a lack of clarity with regard to damages are likely to be significant disincentives to firms considering pursuing a case;
- (iii) the lack of reliable and consistent market information on which the Commission, as principal enforcement body, could base decisions;
- (iv) the absence of an effective surveillance framework to reinforce national arrangements for monitoring compliance and the need to ensure that all the procedures have been correctly followed prior to the final award of contracts.

Various other sources confirm that a common framework to ensure even-handed enforcement of the single market legislation is still missing. Even-handed enforcement still suffers from the absence of general principles for

carrying out checks and coordinated control programmes and of quality standards to which official-control laboratories should be subject. The extent of enforcement cooperation varies considerably between the areas: there is strong cooperation between administrations in areas like customs, VAT, veterinary and plant health, banking and insurance; but cooperation still needs to be firmly established in areas like the new approach Directives, public procurement and the 'Television Without Frontiers' Directive.

Because apparent obstacles and over-complicated procedures encountered by those exercising their rights to the freedoms of the single market are often due to limited knowledge and the incorrect application of Community law by national civil servants, specific measures for further cooperation and improved information have also been identified through various contacts made, in particular with national administrations:³⁶

- common interpretations of the terms used in directives and common application (particularly relevant for the new approach Directives);
- information exchange in the field of compliance surveillance and the way in which complaints are dealt with at national level (laboratory test, public procurement);
- guidance for systematic inventory of material difficulties;
- detailed information on technical criteria and administrative procedures for national approvals (for example, for pharmaceutical products); the need for exchange of information on testing techniques and products/services characteristics;
- better information on contact points in national administration in order to provide sufficient information on the enforcement structures and procedures. Member States' notification still needs to be completed. Contact points should also be established for the public, especially SMEs, to facilitate the exercise of the rights conferred on them by single market rules so that the system can yield its full benefits;

³⁶ See in particular the Commission report on 'Cooperation between administrations for enforcement of internal market law — A progress report', COM (96) 20 final, 29.1.1996.

- improved mutual confidence which could be brought about by improved cooperation backed up by little specific legislation (pharmaceutical);
- increase in resources and communications infrastructure (technical harmonization, general product safety).

3.4. Regulatory barriers

The abolition of physical, technical and fiscal barriers to trade under the SMP did not override other national rules governing economic activity as a whole.

These can be justified by Member States' desire to control public expenditure, in particular social security expenditures, and by the full respect of the subsidiarity principle. However, they influence economic operators'

choice of destination once they decide to expand, and may deter their entry into national markets.

Illustrations of such regulations can be found in the pharmaceutical and distributive sectors.

New barriers to trade, particularly those resulting from legislation aimed at protecting the environment and consumers, are frequently identified by operators as backward steps for the completion of the single market. In some cases, the problem is linked to shortcomings in EU legislation as, for example, in waste recovery, where there is little restriction on the measures that Member States can adopt with a view to achieving the objective laid down. In other cases, Community rules may have been undermined by additional, more stringent specifications at national level. Differing national provisions on labelling and packaging, marketing, or use of chemical products, for example, which require regionally

Box 5 Examples of differences in national practices

Despite substantial progress achieved towards completing a single market for pharmaceutical products, national regulations in respect of price and reimbursement schemes hamper the free movement of these products. National price controls are considered by business to have the following effects:

- access to national markets may be delayed while admission to reimbursement or permitted price systems are agreed;
- prices may be fixed at relatively low levels;
- price controls may be used to encourage or reward local products.

Despite Commission efforts to press for freer pricing, higher patient contributions and a more restrictive approach to State contributions, price controls and reimbursement systems remain firmly in the hands of Member States and still constitute potential barriers to the free movement of pharmaceutical products. Nevertheless, the response of the pharmaceutical industry has been to seek to preserve separate markets with prices, by using different brands, different packaging and different appearance for the same product in different countries, in order to build up customer loyalty and restrict parallel trade.

Similarly, national measures hamper the market entry of distributive companies in several countries. In particular, the retail business has to face many restrictions imposed by national legislation which although non-discriminatory, are considered as barriers to market penetration by potential entrants.

- Restrictions on retail development, imposed by national, regional or even local authorities. This limits the expansion of larger outlets such as hypermarkets, or restricts them to unattractive locations.
- Restrictions on opening hours, which differ very much from one country to another. Although substantial changes are taking place in countries where restrictions have been tightest, short opening hours still obstruct larger retailer expansion because they are seen as increasing the proportion of their overhead fixed costs. They can also create disincentives to more product diversification.
- Restrictions on promotional techniques, which prohibit the use of specific techniques in several Member States. They impede economies of scale for larger retailers and limit the potential returns from a streamlined national and international promotion campaign.

All these measures make access to the retail end of the market more difficult and prevent full exploitation of the single market's potential.

differentiated product presentation, were seen as dividing the single market. Such differentiation has a significant impact as barriers, particularly against smaller or nationally oriented companies seeking to enter new markets. Although some of these measures can be justified by Treaty provisions or Court rulings, they are sometimes disproportionate to their objectives. Business continues to complain about the lack of a clear environment policy, consistent with a level playing field, and the need not to jeopardize the smooth functioning of the single market.

Recourse to Article 100a (4) to justify national measures aiming at environmental protection also worries some sectors, particularly chemicals. Key areas include national regulations on the movement of waste, packaging, waste packaging and eco-labelling. In the automotive sector, national policy initiatives in the field of the environment and safety also risk undermining the single market. For example, national initiatives which create *de facto* additional safety or emission norms for new cars (e.g. through ranking the performance of vehicles measured against tests which are not anchored in Community law) can impose a further level of regulation above and beyond the EC whole vehicle type approval system, thus defeating the objective of EU-wide vehicle certification, one of the major achievements of the SMP.

3.5. Business behaviour

Even in cases of full liberalization, appropriate transposition and enforcement, and the abolition of all regulatory barriers, market penetration may still be constrained by the behaviour of local economic agents. Despite open markets, they may prefer national suppliers or favour local standards and conformance testing. Market penetration may also be restricted by more use of commercial products which, by tying customers to particular products, reduces the chances for potential market entrants, such as lower insurance premiums, for products carrying local trade marks.

Consumer preference for domestic products is often not easy to overcome quickly even when trade barriers have been removed. It is therefore not surprising that local tastes have often been referred to as a major barrier to trade. It is not however the responsibility of public authorities to act against such barriers although they must refrain from reinforcing them (by, for example, referring excessively to national standards or certification systems for regulatory or procurement purposes). It is up to economic operators in the market to overcome these commercial barriers.

Box 6 Behavioural obstacles to the functioning of the single market

Despite the existence of CE marks, some customers still insist on conformity with national standards to ensure approval by national inspection bodies, particularly in the machinery and construction site equipment sectors. As a commercial rather than legal requirement, it does not constitute a regulatory barrier to trade *per se*. However, such a distortion may be reinforced by the provision of more advantageous conditions, such as lower insurance premiums for products carrying national trade marks or conforming with national standards. Complaints about this type of barrier are frequently levelled at the construction site equipment sector, where German (and to a lesser extent French) purchasers often insist that products be adapted to local voluntary specifications. This clearly represents a barrier to trade, entailing additional costs for foreign manufacturers.

In the telecommunications equipment market, some PTOs look for a greater diversification within sourcing, as part of a global strategy to reduce costs. However, the continuing propensity for others to buy a significant proportion of their switching and transmission equipment from their traditional suppliers is another example of behaviour that is hard to change quickly. This phenomenon, which will take some years to disappear, is influenced by cultural and political factors as well as technical and operational constraints.

In air transport services, smaller operators also regard major operators' marketing promotion techniques as anti-competitive instruments. Frequent flyer programmes (FFPs) have a tendency to give large carriers a major competitive advantage over small new entrants. The association of FFPs with alliances and code-sharing can cause a number of difficulties for the small operators who are not in a position to cope with such a challenge. Similarly, large carriers use override commissions, or other incentives, which disadvantage new entrants competing to sell through travel agents.

In the financial intermediation sector, consumer preference for familiar domestic products and institutions prevents many firms from offering new services and leads them to opt for acquisitions or cross-border alliances offering reciprocal access to each party's customer base.

3.6. Remaining cultural differences

Some barriers to market integration will continue to exist within the EU because of differences in language, culture and history. However, their impact on the free movement of products and services must be taken into account when assessing reasons for the ineffectiveness of the SMP.

Most of the advertisers, and media operators, identified cultural differences among EU countries as the main obstacle towards a greater standardization of their advertising strategies. Some degree of social and cultural convergence across Europe and the development of niche (cross-cultural) driven media have already had a notable impact on the relationship between pan-European media and the degree of standardization of cross-border campaigns. However, the persistence of cultural divergence together with regulatory hurdles, caused by the non-application of mutual recognition, inhibits the development of pan-European media.

Historical differences will also continue to require products which are tailored to individual markets. The need to manufacture right-hand vehicles for a few national markets affects market access for some low volume European producers, where the variant costs are higher than the benefits of selling the models in the non-domestic markets. Consequently, some producers pulled out of the UK market because of the costs of developing such variants. Changes required to engineer a car to right-hand drive can effect up to 15% of the total car, by value.

3.7. 'Gaps' in the harmonization programme

Several gaps in the harmonization programme have been identified by this review.

Further progress will also be needed to keep pace with recent global developments in the information society. A Directive concerning a regulatory transparency mechanism

to cover information services, recently proposed by the Commission, aims to counter any threat from national measures aiming to update the legislative framework and undermine single market integrity.³⁷

The automotive industry has indicated that differences in tax structures impose large costs on producers. The fact that some Member States based their ownership on the cubic capacity of the engine, weight, horsepower levels or fuel type can have major R&D and production implications. One manufacturer estimated these could add up to 20% of variant costs. This can also affect the distribution of certain specialist marks. Such differences, which should in themselves be progressively reduced, may be exacerbated by the introduction of fiscal instruments in various Member States as a means of achieving environmental and other policy objectives. In order to minimize the disruption to the single market to which such national fiscal initiatives can lead, the Commission has always favoured the establishment of a framework for fiscal incentives to promote the early marketing and registration of clean vehicles. This policy has been pursued further in the Commission's latest proposals to reduce emissions from cars resulting from the auto oil programme (COM (96) 248 of 18 June 1996), albeit with additional elements of flexibility introduced (notably the establishment of a second stage for incentives in 2005). Different registration procedures for new cars also cause increased costs. Even though a Directive has been put in place, each Member State requires a different selection and presentation of data from this set, imposing an extra administrative burden on producers.

The lack of harmonization of requirements for the use of off-highway vehicles on public roads often has serious cost implications for construction site equipment manufacturers. Member States' requirements for maximum permissible speeds, lighting, steering and braking sometimes widely differ and represent real barriers to trade.

Several gaps still remain to be addressed in the banking sector, together with barriers to the marketing of financial services (for example, door-to-door selling). Product restrictions also persist in several countries. The system of mortgage credit guarantees differs across Member States, making cross-border activity difficult.

³⁷ It might also be necessary to regulate at EU level to ensure that information society products and services benefit fully from single market advantages, such as a regulatory framework which would also protect and stimulate creativity and innovation.

In the insurance sector, intermediaries cannot benefit from the different provisions adopted so far (single licence, right of establishment). This prevents insurance companies from using their own distribution channels for marketing their products.

More progress is also needed in the foodstuffs legislative programme under Article 100 of the Treaty. Further implementing measures and supplementary legislation in the fields of hygiene, new foods, additives, flavours, processing aids, labelling, materials, articles in contact with food and nutritional food are expected.

Other harmonization gaps identified concern pressure equipment, which is still subject to extensive national regulation, but for which a directive based on the new approach is under discussion in the legislative process.

According to business, a genuine single market also requires greater harmonization of external trade policy. For example, there is no Community transit agreement with each third country.³⁸ The number and cost of transit licences for crossing third countries seem to depend on bilateral agreements between individual Member States and third countries. There have also been complaints about the diversity of external border controls for vehicles registered in non-EU States.

3.8. Additional supporting measures

It is widely agreed that the effectiveness of the legislative changes introduced by the SMP will be limited if they are not accompanied by increased competition in other key sectors, particularly the utilities (telecommunications, energy and transport). As part of its research the Commission conducted forward-looking studies to explore the potential benefits of further market integration in these areas. Further progress is needed, especially in the following areas.

3.8.1. Telecommunications

In telecommunications, the liberalization of telecommunications equipment, data and value-added telecoms services, satellite services and from 1996 mobile communications and the use of utility-owned networks and cable TV networks has removed barriers to investment in each of these segments, led to lower prices (particularly for telephone calls between Member States) and improved service quality. These measures have opened the way to new entrants and prompted strategic alliances by telecoms operators both in response to the changes in the telecoms market and in anticipation of the full liberalization of telecoms networks and services from 1998.

Political decisions in favour of full liberalization have been accompanied by proposals for a detailed framework to assist the take-off of effective competition. Article 90 Directives which set the date for liberalization have been completed with proposals for a common framework on interconnection, licensing and universal services (under Article 100a). Despite the early stage in the adoption of these measures the intention is clear. New entrants will be encouraged into the market in order to foster competition.

Many Member States have already made considerable progress towards liberalizing their national telecom markets by establishing an independent national regulatory authority, privatizing the national operator and implementing a regime to ensure interconnection between operators and service providers on fair and reasonable terms.

However, substantial additional benefits are expected from the full liberalization of telecommunications in 1998. Over a 10-year period, up to the year 2005, it is expected that full telecoms liberalization could add cumulatively up to 1.2% to EU GDP generating some 640 000 net new jobs.³⁹ Revenues in the telecoms sector could grow up to 75% over the same period generating a cumulative ECU 225 billion of extra revenue for the sector, leading to a more than twofold increase in capital expenditure up to 6.7% per annum. This should reverse the decline in employment in the telecoms sector which

³⁸ Road freight transport study.

³⁹ Single information market study.

is expected to grow up to 1.1 million by 2005 compared to 985 000 today (in the definition used systems integrators and cable TV industry are included).

3.8.2. Energy

Although important steps were made in the early 1990s, in the form of the European Union Directives on transit and price transparency, efforts at market liberalization are only now coming to fruition. A common position for a Directive concerning common rules for the single market in electricity was agreed on 25 July 1996 and the draft Directive is now in the European Parliament for its second reading. This Directive introduces mechanisms for the gradual and progressive opening of the electricity market over a period of six years, beginning in 1997. Market opening will begin at approximately 22%, calculated on the basis of a common European average (40 GWh) which is obligatory for all Member States and which continues up to 33% (9 GWh) after six years. This leaves Member States the possibility of defining customers eligible to participate in the opening of the market. The composition of this market share must include all final customers consuming more than 100 GWh per annum and distribution companies for the volume of electricity consumed by their customers designated as eligible, to supply those customers. Beyond these requirements Member States are free to define those customers eligible to participate in the opening-up of the market.

Substantial benefits can be expected from full liberalization of the electricity market.⁴⁰ Additional gains for consumers would amount up to ECU 10 to 12 billion per annum, an equivalent of ECU 30 per inhabitant. This is twice as much as gains anticipated from an increased competition scenario, based on an opening rate of approximately 30%.

The introduction of TPA in gas is also likely to lead to benefits for consumers, particularly large consumers. The main impact of completing the single market for the gas sector would be to redistribute economic rents between producers, transportation companies and consumers. Total gains could amount to some ECU 900 mil-

lion per annum, and substantial additional gains (billions of ecus per annum) could emerge if increased gas-to-gas competition was to emerge.

3.8.3. Transport services

The basic framework of the single transport market is in place but further measures are still necessary.

Regarding air transport, access to airport slots should improve as the shortage of slot slack is presently inhibiting competition on existing routes and the development of new routes. The lack of peak hours slots makes the entry of new carriers on the densest routes almost impossible. It also prevents niche carriers from serving regional routes. The Commission has tabled a proposal to reform the present system of allocating slots and reduce market rigidities at congested airports.

Regarding railways, this sector developed along national lines based on monopolistic structures that resulted in management inefficiencies, cross-border operating difficulties, inadequate planning of interstate infrastructures and fragmentation of the supply industry. The first steps have been taken at Community level with Directive 91/440/EEC on development of the Community's railways to introducing limited access rights for international traffic. The Commission has submitted a new proposal to provide complete access open to all freight transport as well as international passenger transport, but this proposal has not yet been adopted by the Council. The Council, however, adopted in 1995 two Directives establishing common rules and criteria for the licensing of railway undertakings (Directive 95/18/EC) as well as for the allocation and charging of railway infrastructure (Directive 95/19/EC).

In order to reverse the declining trend in railway transport and restore its competitiveness which has been undermined by increased liberalization in competing modes (e.g. road and air transport) the Commission put forward in July 1996 a White Paper on revitalizing the Community's railways. Building on existing Community legislation, the White Paper outlines the action needed in a number of different areas:

⁴⁰ Single energy market study.

- the clarification of financial relations between the State and the railways;
- further exposure to market forces, notably through the creation of 'rail freeways' for freight transport;
- improvement of the quality and efficiency in the provision of public services;
- increased efforts to improve infrastructures, enhance R&D and harmonize technical standards to ensure further integration of national systems.

Regarding the road haulage sector, driving bans on goods vehicles, in particular areas and at particular times is, under subsidiarity, a national or even local problem. However, if these bans should be extended it might affect reasonable free access to the networks especially for long distance transport.

For road passenger transport, Regulation (EEC) No 684/92 on common rules for the international carriage of passengers by coach and bus and Regulation (EEC) No 2454/92 laying down the conditions under which non-resident carriers may operate national road passenger transport services within a Member State, have introduced the principle of freedom to provide services in this sector. In practice, this means that international transport and cabotage services between Member States are permitted without discrimination on grounds of nationality

or place of establishment. The Commission has submitted new proposals to be adopted by the Council in order to liberalize this sector further.

While considerable progress has been made in removing regulatory barriers to the cross-border provision of services, physical barriers, either natural such as geography or artificial due to costly interfaces and poor connections between countries, are limiting competition and continue to impede the free flow of goods, services and people in Europe. The new responsibilities for trans-European networks conferred to the Community by the EU Treaty have created the conditions for further developing the missing trans-European infrastructures.

In order to assess the benefits to the single market from increased integration of the transport networks and services, one of the studies carried out in the single market review focused on this issue.⁴¹ The study attempts to separate the impacts of infrastructure investment from the impact of policy actions on the performance of transport systems in the single market. The results are positive and confirm the long held view that infrastructure development should go in pairs with the reform of the regulatory framework. The table below summarizes the results. The full integration scenario reveals the importance of successfully implementing the regulatory reforms and of completing all the 14 TENs priority projects to enhance competition and achieve cost reductions and larger scale integrated transport operations in the Union by 2005.

Table 7 — Annual savings against 2005 base scenario (ECU 91 million)

	Cost savings	Time savings	Total cost and time savings	Total savings (including other indirect costs)
Partial integration (PI) annual savings	2 089	1 546	3 635	10 268
Full integration (FI) annual savings	53 407	13 118	66 525	92 467
Congestion charging (CC) (based on FI) annual savings	60 812	24 738	85 550	119 321
Rail service quality (RQI) (based on FI +CC) annual savings	66 893	27 674	94 567	128 965

⁴¹ Transport network study.

3.8.4. Single currency

The currency turmoil experienced over the last four years has created some problems in respect of the functioning of the single market in some sectors. The speed and scale of the changes which occurred since September 1992 have posed adjustment problems for certain sectors and regions, which had so far enjoyed cost-competitiveness advantages. Furthermore, the uncertainty arising from these changes may have led to some mis-allocation of resources in terms of the location of production activities and investment decisions. Economic agents have also displayed an uncertainty and 'wait-and-see' attitude which have had a negative impact on investment and growth. All these problems affecting the functioning of the single market have been made more difficult by the fact that the Community was experiencing cyclical recession over the same period.

The temptation for firms to react to these barriers by introducing trading restrictions to protect their margins, and the pressure on public authorities to intervene to help sectors or regions particularly affected, has complicated efforts to complete the single market. They have also clearly demonstrated the need to progress to economic and monetary union.

3.8.4.1. Impact of a multi-currency system on the single market

As noted in the Commission's communication of October 1995,⁴² the impact of currency fluctuations, as they took place in the 1992-95 period, has been more visible at sectoral and regional levels than on Member States' trade balance. At the aggregate level, trade balances appear to have been influenced primarily by changes in relative demand, the role of exchange rate fluctuations having been largely overshadowed by evolution of the profit margins.

The effect of currency and cost fluctuations on export prices depends on the phase of the business cycle: in 1992-93, export profitability declined, causing it to fall below that of the domestic sector in appreciating countries, while in depreciating countries export profitability

rose in the aftermath of the crisis as their exporters preferred to increase profits instead of reducing their export prices. Price setting has therefore been quite heavily dependent on 'profit margin' behaviour. Consequences of these developments are difficult to predict: firms in depreciating countries could be tempted in the future to pursue more aggressive commercial policies, while these variations in profitability may also have an impact on corporate investments.

Some sectors reported having been more strongly affected by currency fluctuations and concerns were expressed about the falls in business export margins and the contraction in market shares for some of them. Overall conclusions which can be drawn from the studies undertaken so far indicate the following:

- firms from countries whose currency has appreciated have encountered problems in penetrating the markets of countries whose currencies have depreciated;
- firms from countries whose currencies have depreciated have not improved their positions on other EU markets;
- but some of them improved their positions on non-EU markets.

Currency fluctuations nevertheless affected some of the main business strategic operations, especially pricing and sourcing strategies. Some car manufacturers reportedly wanted to maintain a relatively clear price structure across Europe to help dealers near the border and avoid the possibility of parallel exports. Some of them were forced to increase their prices in the devaluing country, thereby reducing the possibility of growth in that Member State (Nissan in Italy). Companies were also forced to seek greater diversification, by trying to balance the proportion of supplies sourced in individual countries to the levels of demand across the countries.

In the construction site equipment sector, exchange rate fluctuations also made it difficult for companies to maintain a single pricing strategy. Fluctuations also very much influenced their decisions to source in other parts of the EU, in particular for those companies based in countries with relatively strong currencies which sought

⁴² COM(95) 503 final.

Box 7 Sectoral impact of currency fluctuations between 1992 and 1995

Motor vehicles: Improved export performance by the devaluing countries is explained by better export performance to non-EU countries. This is particularly true for Italy and Spain which did not perform much better in countries whose currencies appreciated but substantially improved their export performance to non-EU countries. This poor performance on the EU market is explained by higher unit price increase (in national currency and ecus) for intra-EU markets than for non-EU markets. On the other hand, countries whose currencies appreciated experienced more difficulties in penetrating other EU markets, while their performance on non-EU markets slightly improved.

Textiles: There has not been any such clear-cut differentiation. German reunification and EU enlargement to Spain and Portugal seem to have played a more important role. French manufacturers experienced some difficulties in penetrating the Italian market, while Italian, Spanish and Portuguese manufacturers improved their export performance to countries whose currencies appreciated. Some trade diversion from depreciating countries to appreciating countries has also been noticed.

Clothing: No clear trade diversion has been experienced. Operators in weak countries have increased profit margins, by raising exports prices in ecus while decreasing production prices in ecus.

Footwear — shoes: This is another example of discriminatory pricing policies where operators from depreciating countries have been reluctant to reduce prices in foreign currency with a view to increasing profit margins in national currencies. German exports grew above the average in all weak markets while Italian firms experienced some recovery in their exports to both EU and non-EU markets. Italian, Spanish and Portuguese producers increased their profit margins.

lower material and component costs by sourcing in countries which have devalued. Firms from appreciating countries also sought to increase their subcontracting activities in East European companies.

3.8.4.2. The costs of foreign exchange transactions

Costs of foreign exchange transactions include costs induced by interbank trade (due to the spread between buy and sell rates), non-bank cross-border transactions, costs of foreign exchange trade in coins and notes, hedging costs for intra-EU exchange transactions and company internal costs for managing multiple currencies in the EU.

Despite sinking unit costs over the last 10 years, total costs for interbank trade (based on 'autonomous' interbank deals, deals not done on behalf of non-banks) increased from ECU 8.7 billion in 1986 to ECU 12.4 billion in 1995. This increase is mainly due to the strong increase in autonomous transactions (ECU 27.6 trillion in 1995 against ECU 8.7 trillion in 1986).

Transaction costs for non-bank business (except for cash trade) cover both current account transactions and capital account transactions.

- Current account transaction costs were estimated at ECU 11.6 billion in 1995 (compared to ECU 9 bil-

lion for 1996). Additional costs for payment made by credit cards, cash, Eurocheques or traveller cheques, which are more cost-intensive (total commission fees of around 2.5% were charged for these payments in 1995) led to an additional ECU 1 billion.

- Capital account transactions represent a higher volume on average but are subject to lower average foreign exchange unit costs. Transaction costs for 1995 amounted to ECU 6.9 billion for ECU 5.1 billion for 1986.

For payments made in the forward market, additional hedging costs apply. They were estimated at ECU 5.9 billion for intra-EU current account transactions, and ECU 2.6 billion for capital transactions, due to the fact that unit costs for hedging operations are lower for capital account transactions than for current account transactions.

Cash transactions are subject to particularly high commission rates. Over recent years, there has been a noticeable increase in spreads between buy and sell rates for foreign coins and notes. For a total volume of cash transactions of around ECU 150 billion in 1995, transactions costs amounted to ECU 7.95 billion in 1995, compared with ECU 3.5 billion and 2.7 billion in 1989 and 1986 respectively.

Finally, companies also experienced extra internal costs in dealing with the management of foreign exchange.

These internal costs were estimated at ECU 7.8 billion for personnel and equipment costs and around ECU 1 billion for costs accruing through longer transmission periods for intra-EU payments than for payments within national borders.

The overall result shows that total foreign exchange transaction costs due to multiple currencies in the European Union amount to roughly 1% of GDP of the EU. This is more than double the level found in the 'One market, one money' Commission study in 1990.

Table 8 — Costs of foreign transactions

	1986	1989	1995
I. Interbank business	8.7	11.6	12.4
II. Non-banks (except cash) — current account transactions	8.9	10.0	11.6
Supplement for:			
— hedging costs	3.9	5.0	5.9
— checks and credit cards	0.2	0.4	1.0
III. Non-banks (except cash) — capital account transactions	5.1	11.1	6.9
Supplement for:			
— hedging costs	1.0	3.0	2.6
IV. Non-banks — cash trade	2.7	3.5	8.0
V. Company internal costs	5.3	7.4	8.8
Total costs (% of GDP)	35.8 (1.00)	52.0 (1.17)	57.2 (0.95)

Source: Study on intra-EU multi-currency management costs, by IFO Institute for Economic Research.

3.8.4.3. One money for a single market

The single currency is the most frequently cited measure which economic operators and business organizations view as missing for the single market. It aims to help European enterprises to reap the full benefits of the opening up of markets to competition.

Single currency benefits for the market are well known.

- (i) The single currency is the 'guarantor' of the single market; it will make monetary integration irreversible and restrict Member States' ability to resort to some form of renewed protectionism and increased use of subsidies or safeguard measures.
- (ii) It will reduce transaction costs, which as noted above amount to roughly 1% of GDP of the EU.

- (iii) It will remove the exchange risks that now characterize cross-border trade, investment and competition, thereby ensuring optimal resource allocation in the European economy, reducing production costs and making European industry more competitive.
- (iv) Increased price transparency will enhance competition and whet consumer appetites for foreign goods; price discrimination between different national markets will be reduced.
- (v) It will contribute to a microeconomic climate conducive to the smooth functioning of the single market.
- (vi) It will contribute to the equalization of interest rates, thereby stimulating investment and growth.

Not all Member States will be part of EMU as early as 1999. The proper functioning of the single market must

therefore not be endangered by real exchange-rate misalignments, and excessive nominal exchange-rate fluctuations which could lead to disruption of trade flows between Member States. Lasting convergence of economic fundamentals, as well as sound fiscal and structural policies in all Member States, are prerequisites for sustainable exchange-rate stability. In accordance with Treaty provisions, non-participating Member States should therefore treat their exchange-rate policies as a matter of common interest, monitoring and assessing them at Community level in order to avoid any distortion of the single market.

4. The economic impact of the SMP

4.1. Introduction⁴³

In the early 1980s, the European Community (EC) was suffering severe economic problems, including rising unemployment and poor competitiveness in high-tech activities. Diagnosis of the European malaise pointed to a central cause: market rigidities, responsible for the sluggish response of European economies in the 1970s and 1980s to rises in the oil price, globalization of the world economy and the information technology revolution. Rigidities pervaded all European markets, whether for products or production factors. Curing such 'Euro-sclerosis' required structural reforms aimed at enhancing market flexibility and reducing barriers to mobility within the EC.

Discussion within the Community on these problems culminated in the 1985 White Paper on completing the internal market, which spelled out a programme and a timetable for unifying European markets. It proposed that Member States abolish, by end-1992, all remaining barriers to the free circulation of goods, services, persons and capital (the four freedoms). Previous chapters of this document have analysed the extent to which implementation of the 1985 White Paper and related actions has been successful in eliminating obstacles to cross-border transactions. Progress towards completion of the single market was seen as one contribution to restoring the capacity of the EC to generate growth and employment.

However, the scope of the SMP extends beyond the nearly 300 specific measures listed in the White Paper for removing physical, technical and fiscal barriers hindering trade and factor movements within the EC. It covers two additional areas, because the Community has always taken the view that the abolition of obstacles to the freedom of movement of goods, services, capital and persons is a necessary, but not sufficient, condition for a truly single market. The first of these two areas are the two particularly important Community flanking policies of competition policy and regional policy. There was a danger that completion of the single market would be accompanied by private or public measures aimed at

reducing competition, such as cartels and State aids. This led to a strengthening of Community competition policy, especially in the domain of merger concentration with the adoption of the Merger Regulation in 1989. Similarly, the combination of the single market and the enlargement to Spain and Portugal in 1986 created the risk of reduced cohesion within the EC. To counter this possibility, an extension of Community regional policy, involving the doubling of Structural Funds, was enacted in 1989. The second area concerns a number of sectors (such as energy) which were not covered by the White Paper but have since become the target of liberalizing measures.

How much economic activity is affected by the SMP?

Taking the narrow single market blue-print laid down in the White Paper programme, it has been estimated (Buigues *et al*, 1990) that 40 out of 120 manufacturing sectors listed in the NACE-3 digit classification were likely to be directly affected by these measures. Intra-EU trade in these sectors was substantially impeded by non-tariff barriers. These 40 sectors represented somewhere between 12 and 18% of EU GDP (around 40-60% of value added in manufacturing). However, the SMP was perhaps even more important for the integration of market services as it marked the first real attempt to overcome obstacles to cross-border provision of services and establishment-based trade in many key services such as financial services, road and air transport and telecommunications. Services had traditionally been subject to relatively intensive regulation at national level which either prevented operators from offering services on a cross-border basis or deterred them from establishing in partner country markets. These regulatory obstacles are however compounded by entrenched structural obstacles which will have a profound bearing on the degree and speed of market integration. The SMP has been seen as the 'beginning of the last step to freedom' for these market services, in contrast to the situation for manufactured goods where the SMP can be regarded as adding the finishing touches to the process of integration. While only 50 of the White Paper measures concerned services,

⁴³ A more detailed analysis of the economic impact will be published in *European Economy*.

there have been several substantial extensions of this agenda in subsequent years (e.g. energy, voice telephony).

In combination with technological progress and globalization, the SMP has created the potential for substantial restructuring and growth of market services. Given the importance of market services to the Community economy — in 1990 they accounted for 48.2% of GDP and 42% of employment — the cumulative effect of such restructuring and growth could be very significant.

The competition and other SMP induced changes are not confined to those sectors which are directly targeted by the SMP, but will be transmitted to other upstream or downstream sectors. Through market interactions and strategic reactions by firms, changes in competitive conditions in one sector have spilt over to related sectors, which serve as either customers or suppliers to the market concerned. For example, SMP-driven changes in the glass sector have led to upstream restructuring in the soda ash industry; similarly, the liberalization of telecom services has had a profound impact on the telecommunications equipment market. Likewise, attempts by producers of SMP-sensitive manufactured products to obtain a gateway to partner country markets have added momentum to the Europeanization of distribution and logistics systems. At a more general level, the freeing up of resources and previous expenditure on SMP-sensitive sectors may be reflected in changes in demand for even non-related products. Thus, once account is taken of knock-on effects, the creation of a single market is bound to affect virtually all parts of the European economy.

The mechanisms which produce the economic effects

In economic terms, the SMP can be expected to produce three types of economic effects: allocation effects, accumulation effects and location effects. The first consists of the impact of integration on the static, short-run allocation of resources, i.e. on economic efficiency. The second effect encompasses the impact on the accumulation of productive factors and covers both medium- and long-run growth effects. The third effect refers to the geographical allocation of resources across Member States and/or regions of the EC.

Previous analyses of the SMP focused entirely on allocation effects, adding to classical analysis on compara-

tive advantage an innovative approach that highlighted economies of scale and increased competition. The removal of barriers implied by the SMP was expected to produce an improved allocation of resources through the fuller exploitation of comparative advantage and specialization. In addition, in many sectors of the European economy the SMP was expected to improve efficiency via rationalization of production associated with a fuller exploitation of scale economies. Great emphasis was laid on efficiency gains from economies of scale at the plant or firm level associated with the size of the EC market. However, as economies of scale inevitably lead to concentration in production, the potential impact of the SMP on competition was also emphasized. It indicated that the removal of barriers was likely to produce strong 'pro-competitive' effects, although it recognized also the need for a strong Community competition policy. Provided greater competition was obtained, the lower production costs associated with the efficiency gains from the SMP were to translate into lower consumption prices.

Clearly, the potential efficiency gains from the SMP require reallocation of resources within the EC: reallocation within and across firms, reallocation within and across sectors, and reallocation within and across regions or even Member States. Such reallocation may imply more or less adjustment costs depending on its nature and on the functioning of factor markets. It was recognized from the outset that the effects of the SMP on employment were bound to be weaker than the effects on GDP due to an increase in productivity. Thus, in the short term, the SMP may create unemployment. As the report indicated: 'let there be no mistake, the [SMP] is a medium-term therapy; it will take time for its benefits to become apparent, and patience and political determination will be required if we are not to change course' (European Commission, 1988).

Accumulation and location effects are likely to require a longer time span to materialize than allocation effects. The SMP can boost accumulation, and thereby contribute to higher growth rates in the EC, in two ways. On the one hand, the static, efficiency gains of the SMP translate into higher incomes, which may generate higher investment and raise growth in the medium term. On the other hand, the SMP could improve the benefits and reduce the costs of producing new innovations in the EC, which would boost growth in the long run. The SMP is also likely to affect the geographical distribution of production within the EC. The economic literature has noted

that the degree of specialization in Europe is far below what is observed in the United States. Some ascribe this situation to the existence of trade barriers in Europe and predict, therefore, that the SMP could increase geographical specialization in the EC.

Related to the issues of growth and location is the question of the impact of the SMP on real convergence between the Member States and the regions of the EC. The expected effect of the SMP on convergence is ambiguous. On the one hand, the SMP should favour convergence of per capita income levels across Member States via greater mobility of goods, services, capital and labour. On the other hand, increased geographical specialization could lead to increased polarization between richer and poorer countries or regions. Obviously, the purpose of the enhanced Community regional policy is to tilt the balance in favour of the former outcome.

Earlier studies attempted to estimate the *ex ante*, potential economic effects of the SMP. The purpose of the present exercise is to provide an evaluation of the *ex post*, actual effects. In many ways, this is a very difficult mission. Firstly, the period which has elapsed since the beginning of the SMP is extremely short. It is unreasonable to assume that economic operators integrated the SMP into their decisions before 1987 or even 1988. Furthermore, many of the measures were not adopted until recently. At the same time, much of the required statistical information stops in 1994 or even 1993. Accordingly, the period of analysis is in many instances very short — too short to evaluate properly a structural transformation on the scale of the SMP. Secondly, the SMP is an extremely complex process: it has been implemented at varying speed and intensity in different sectors and different Member States; it potentially affects the entire value chain of most economic activities; and it purports to remove some barriers, while leaving others untouched. Lastly, the period of investigation has been an extremely eventful one from the viewpoint of economics. Within Europe itself, it has witnessed not only the implementation of the SMP, but also the enlargement of the EC to Spain and Portugal, German re-unification, and the economic transformation in Central and Eastern Europe. All this has been against the background of a globalizing world economy and the information technology revolution. For all these reasons, the *ex post* economic evaluation of the SMP should be viewed as an highly tentative exercise.

This chapter will present the main findings from *ex post* analysis of the impact of the SMP. It will turn first to the implications of the SMP in deepening the channels of integration between the Member State economies through trade and investment. The analysis will then seek to determine whether this reinforcement of integration channels has been associated with the restructuring of manufacturing and service sectors and changes in market structure and performance of operators. In a final section, the chapter will present the results of simulations which attempt to determine whether observed changes in market functioning and structure can be expected to translate into changes in indicators of macroeconomic performance (GDP, employment).

4.2. Impact on trade, cross-border investment, and specialization

The SMP builds on the well-grounded belief that the removal of artificial constraints to economic activity between Member States will serve to boost economic prosperity. The analysis of the economic impact of the SMP must therefore start by determining whether measures taken to date have strengthened trade and investment flows between the Member States.

4.2.1. Trade

Trade expansion is believed to allow for increased economic welfare because less efficient domestic production is replaced by imports produced more efficiently. The SMP, by removing trade barriers between countries, was expected to expand trade among EU Member States and thereby improve welfare.

For the period between 1985 and 1995, the share of intra-EU imports in total manufacturing import increased on average by 6.7 percentage points from 61.2% in 1985 to 67.9% in 1995. For services during the same period 1985-95, the share of intra-EU export in total services export increased on average by 3.1 percentage points from 46.9% in 1985 to 50.0% in 1995.

Intra-EU import penetration also increased significantly in the EU for manufacturing as a whole. However, there

Figure 4 — Share of intra-EU trade in total trade



are significant differences amongst sectors within manufacturing. Intra-EU penetration ratios increased much more in the 15 manufacturing industries particularly sensitive to the SMP than in the rest of the manufacturing sectors. Econometric assessment provides clear evidence on the direct effect of the SMP on intra-EU trade flows. It shows that the SMP has created trade within the EU. Direct and pro-competitive effects of the SMP on trade explain 80% of the change in the market share of total imports. Such effects are also higher the higher the sensitivity of the sectors to the SMP. Alternative analysis estimates that the long-run impact of the SMP on manufacturing trade could be a 20 to 30% increase in the volume of intra-EU exports and imports (Gasiorek, Allen & Smith, 1996).

The SMP has also led to external liberalization towards non-EU countries, because market access is easier with a single system. There was a possibility that increased trade amongst the Member States could be at the expense of trade with third countries. On the other hand, the SMP could have had the effect of improving market access for third country imports into the EU market, thus to some extent reducing the welfare gains just discussed. The latter effect seems to have predominated and there is no evidence at all in the studies that increased intra-EU trade has been at the expense of trade with non-EU countries. Extra-EU import market shares increased by 2.5 percentage points between 1991 and 1994 in total manufacturing and by 2.9 percentage points in the 15 manufacturing industries particularly sensitive to the SMP. The overall estimated impact of the SMP accounts for the largest proportion of the observed changes.

4.2.2. Cross-border investment

Cross-border or foreign direct investment (FDI) can take the form of 'greenfield' investment (establishing a new company from scratch) and cross-border mergers and acquisitions (M&A) of existing firms. Trade and FDI are different ways of supplying international markets. Multinational companies are the main source of FDI flows, and the sales of multinational foreign affiliates are now by some estimates worth double the value of world exports.

The expected impact of the SMP on foreign direct investment is ambiguous. On one hand, because the single market lowers cross-border trade costs, it could increase trade relative to FDI. Conversely, for Member States whose locational advantages are significantly improved by the SMP (because of market integration and the dynamic impact on economic growth), FDI will increase relative to trade.

In fact, the SMP impact on FDI seems to have been even more positive than its impact on trade. The European Union absorbed 44.4% of FDI inflows from all countries in the world at the beginning of the 1990s, compared to 28.2% in the period 1982-87. Moreover, intra-EU FDI increased four times faster than intra-EU trade in the period 1984-92.

Examination of the geographic distribution of FDI outflows from the largest EU Member States suggests that the SMP has had very substantial positive effects on their FDI flows to the rest of the EU. Between 1984-85 and 1992-93, EU FDI inflows from all sources increased five times (seven times for intra-EU inflows, for example, flows between Member States).

4.2.3. Trade, specialization and adjustment costs

Originally, the common market consisted of six Member States with roughly comparable industrial structures, productivity or capital/labour ratios. Entry of the southern European countries to the EU brought partners for integration in intra-Community trade with quite different industrial structures and productivity levels. These southern Member States, with low labour costs and relatively high capital costs, were specialized in industries with a commensurably high labour content but low technology and skill content. The northern Member States, with high labour costs and relatively low capital costs, specialized in industries with a high technology, capital and skilled labour content.

The effects of the SMP and economic integration on trade are complex. In the traditional analysis of international trade, the SMP should lead to greater specialization by countries on the basis of their respective comparative advantages. The SMP would, in that case, favour an increase of inter-industrial trade, each Member State specializing primarily in the sectors where it is relatively efficient. However, if we take into account economies of scale, imperfect competition and product differentiation, the SMP could increase intra-industry trade, the simultaneous import and export of similar product lines between Member States (e.g. cars for cars).

The gain from economic integration differs between these two modalities (inter-industry trade and intra-industry trade). Inter-industry trade between different countries carries efficiency gains, with each country specializing in those activities in which it is relatively more efficient, whilst consumers gain lower prices as a consequence. However, this implies a deeper specialization between the less developed Member States and the more advanced, each country experiencing a contraction of some of its sectors and expansion of others (for example, clothing vanishing in high labour cost countries, and high technology in low skill ones). The redistributive implications of this are considerable and the adjustment process costly.

By contrast, intra-industry trade benefits the consumer by leading to a much wider variety of products, whilst producers face lower adjustment costs. Here, adjustments would take place amongst firms inside industries rather than among industries. As Member States' industrial structures remain roughly similar, the EU becomes more diversified and is therefore less vulnerable to sector specific shocks (e.g. increases in the price of oil etc.). A shock has no very different effects depending on the Member State (no asymmetric shocks). This is particularly important, of course, within a monetary union.

At the beginning of the 1980s, most trade within the Community could be classified as inter-industry⁴⁴ corresponding to specialization based on comparative advantages (around 45%), but this started to decline in the mid-1980s. The preparation phase of the single market was accompanied by a decrease in the share of inter-industry trade in Europe and a rise in intra-industry trade. However, intra-industry trade could be further sub-differentiated: either intra-industry trade in similar products in terms of prices and quality or intra-industry trade in products differentiated by price and quality (for example, one country exporting expensive brand-name shirts and the other inexpensive low-quality shirts). The rise in intra-industry trade has predominantly been the latter type (from less than 35% in 1985 to more than 42% in 1994), whilst intra-industry trade in similar products⁴⁵ remained rather stable (around 20% of total intra-EU trade). The SMP has therefore increased the range of products available to consumers in terms of prices and quality and encouraged differing business strategies: either emphasizing design, research and development (R&D), and advertising in some cases (high-price quality) or production cost-minimizing in others.

The increase of intra-industry trade in price differentiated products implies larger adjustment costs than intra-industry trade in similar products, but still much lower adjustment costs than an increase in inter-industry trade would have produced. Its benefits are a much wider range of products in terms of prices and quality for consumers, as well as efficiency gains due to specialization on the basis of relative comparative advantages within sectors (innovation, design, distribution).

⁴⁴ We have inter-industry trade between two countries when one country's trade flow (import or export) with the other in a sector represents less than 10% of the other country's trade flow (import or export) with it in the same sector.

⁴⁵ We have intra-industry trade in similar products when export and import unit values differ by less than 15% and we have intra-industry trade in differentiated products when unit values differ by more than 15%.

4.2.3.1. The country dimension

In the period 1985-94, all EU countries experienced a decrease in inter-industry trade, but especially Spain, the UK, France and Germany. Nevertheless, in 1994, inter-industry trade corresponding to specialization based on comparative advantages still accounted for over 58% of Greece, Portugal, Ireland and Denmark's total manufacturing trade. At the same time, conversely, intra-industry trade in price quality differentiated products represented over 42% of total trade for the UK, Germany, France, Belgium, Luxembourg and the Netherlands, a share which grew between 1987 and 1994 for all this group of countries plus Spain and Portugal.

Analysis of price quality differentiated intra-industry trade shows a striking difference between northern and southern countries. Scrutiny of the contribution to the trade balance of low, medium and high-price quality product ranges spotlights different country groupings. Germany has a comparative advantage in high-price quality product ranges, France in medium to high-price quality ranges, the United Kingdom, the Netherlands, Belgium, Luxembourg and Denmark only in medium-price quality ranges, Spain in medium to low-price quality ranges, and Greece and Portugal only in low price quality ranges. These specializations have been unaffected by monetary fluctuations.

In the period 1985-94, the share of medium price quality products in overall intra-EU trade declined (by some 10 points) to the benefit of high price quality products (plus 7 points) and low-price quality products. This is especially so for the most advanced European economies. However, also for southern Member States, specialization has changed and the share of low-price quality products generally fallen whilst the share of high-price quality products has increased.

The SMP has therefore contributed directly, via the removal of border formalities and reduction of cross border transportation costs, and indirectly, via growing income convergence between EU Member States, to a growing share of intra-industry trade.

Growing intra-industry trade with price differentiation implies that Member States are more and more specialized inside industries on products with differing price level ranges, importing low-price quality ranges and exporting high ones, or vice versa. Of course, the situa-

tion could differ for different sectors: one country could import high-quality clothing and export high-quality cars. For most advanced countries such an evolution implies growing intangible investment in R&D, training, innovations to compete in traditional mature industries, and for less advanced countries, the possibility of entering high-tech and high value-added sectors and competing on price.

4.2.3.2. The sectoral dimension

However, manufacturing sectors are not all comparable in terms of the nature of trade (intra- versus inter-industry trade) and therefore in terms of adjustment costs and efficiency gains resulting from the SMP.

In terms of inter- versus intra-industry trade, manufacturing sectors can be broadly divided into two groups: firstly, in food and beverages, mining, textiles and non-metallic minerals, trade is mainly inter-industrial. These sectors represent about one third of total manufacturing value added. Secondly, in non-electrical machinery, professional goods, electrical machinery, motor vehicles, chemicals, wood and paper, trade is mainly intra-industry differentiated by price and quality. These sectors represent about two thirds of total manufacturing value added.

In general, for all sectors between 1985 and 1994 intra-industry trade in price quality differentiated products increased whilst inter-industry trade decreased. In particular, for sectors traditionally characterized by high inter-industry trade, the implementation of the single market is characterized by a steady increase of intra-industry trade, notably due to an increase of trade in price quality differentiated products (food and textiles).

4.2.4. FDI, specialization and adjustment costs

FDI (whether 'greenfield' or M&A) raises welfare in aggregate terms, the main issue being whether FDI is welfare improving for both the source and the destination country. For the destination country, the foreign affiliates may provide new products and processes, methods of superior management and so on. For the source country, domestic multinationals will only invest abroad rather than supplying overseas markets from

local plants via exports if the decision is expected to be beneficial to profits and efficiency-enhancing.

With the removal of market fragmentation and the dynamic impact on economic growth of the SMP, FDI will increase relative to trade to Member States whose relative locational advantages are significantly improved by the SMP.

4.2.4.1. The country dimension

The impact on the domestic economy of FDI (FDI inflows to GDP) differs widely amongst Member States. At the beginning of the 1990s, annual Irish FDI inflows were worth over 9% of GDP. In Belgium and Luxembourg, the ratio was 4.7% a year. The Netherlands (2.7%) came third, then Portugal (2.6%), the UK (1.8%) and Spain (nearly 1.8%). By contrast, in Germany (less than 0.4%), Italy (0.4%) and Greece (0.6%) these figures were very low. Over the period 1986-93, two Member States (Belgium and Ireland) gained considerable ground in terms of attractiveness as locations for FDI. Taxation also plays an important role in this. In general, catching-up countries (Ireland, Portugal and Spain) and small core countries (Benelux countries) are among the ones which have benefited most from the single market in terms of FDI.

As hosts for FDI from other EU countries, Belgium, Luxembourg and France have become increasingly important since 1986, so that each absorbed some 18% of total intra-EU FDI in the period 1992-93. Meanwhile the UK (9% of total intra-EU FDI in 1991-93) became significantly less important over the period 1986-93. As hosts for extra-EU FDI, however, the UK dominates (37% of total extra-EU FDI), with France second, receiving 16% over the period 1990-93.

The extent and direction of the SMP impact on FDI in the EU Member States has been estimated using different approaches (a 'gravity' model and an econometric assessment). The results of the studies are consistent. For example, the results suggest that the SMP may have raised the constant price stock of UK investment in the EU by some USD 15 billion as of 1992, around 31% of the UK's aggregate stock at that time.

4.2.4.2. The sectoral dimension

For sectors subject to technical economies of scale, the SMP will lead to relatively more trade than FDI, because economies of scale due to concentrating production at a single plant tend to discourage dispersed production. However, for sectors characterized by knowledge-based assets, FDI will increase relative to trade (better approach and access to consumers in particular, importance of after-sale services, and to facilitate the deployment of technological assets).

The ratio of intra-EU trade to FDI fell substantially during the period of the SMP, from 240% in 1984-86 to 61% in 1990-92 for manufacturing industries. This decline, corresponding to an increased importance of FDI relative to trade flows, was most marked in the food sector, a sector where knowledge-based assets are typically important (differences in tastes, importance of advertising). The food sector is also the one which has increased most in terms of the share of total manufacturing intra-EU FDI (from around 10% in 1984-86 to 22% in 1990-92).

The sectoral breakdown of inward FDI flows may be reflecting the comparative advantages of different Member States. In northern Member States, cross-border manufacturing M&A activity is mainly in technology intensive sectors (engineering, transport equipment, machinery) whilst in southern Member States, cross-border M&A activity is mainly in relatively basic products (textiles, clothing, timber and wooden furniture).

However, the bulk of FDI to the EU as a whole is targeted at the services sectors. In the 1980s, 63% of FDI cumulative inflows went to service sectors, whilst only 31% went to manufacturing sectors. This partially reflects the fact that the services sectors are the largest and fastest growing part of advanced economies, but also that service sectors are generally less tradable than manufacturing sectors (FDI tends to be the only way to supply foreign markets), so that they are characterized by significant firm specific assets and by the importance of proximity with consumers. Of the estimated increase of UK and German FDI stocks in other EU Member States due to the SMP, the largest gains have been in financial services. Of course, services may also have been the most affected by the SMP because of the hitherto high level of barriers which the SMP has been systematically removing.

4.2.5. The location issue

One question is whether the SMP has induced more concentration of EU industry around an industrial core (which can be central or peripheral in terms of geography) or a more even dispersion amongst the Member States. Such evolution is not expected to affect all industrial sectors in the same way. Economic integration entails, in principle, a concentration of industries characterized by economies of scale in the economic core region and therefore, for those sectors, a decline in intra-industry trade. As has already been said, however, manufacturing as a whole inside the Community has actually experienced an increase in intra-industry trade, with Member States trading in products from the same industries differentiated by price and quality. This implies that countries are broadly producing the same type of goods, but with different price-quality characteristics. In other words, a process of specialization is occurring, but within industries. Nevertheless, for a limited number of sectors with large potential scale economies, a certain concentration may still develop in the future.

The process of industrial specialization inside the EU on the basis of price and quality differences has certain consequences for the cohesion and convergence of richer and poorer Member States, an issue which is dealt with in point 5 below.

4.3. Impact on market structure, competition and efficiency

Many of the beneficial effects of the SMP for the European economy were supposed to result from competitive forces unleashed by integration. The *ex ante* analysis of the impact of the SMP forecast substantial gains for the European economy from increased efficiency, with lower costs and prices, and increased product variety. The main channels through which these benefits were to be reaped throughout the economy were the exploitation of scale economies by firms, and increased competition, which would eliminate inefficient firms and lead to a restructuring of European industries.

4.3.1. Changes in the structure of European industries

Barrier removal due to the SMP has affected the structure of both trade and production. The previous section highlighted important changes in trade and investment flows between Member States. In this section, we look at the shifts in domestic production and market structure that accompany such changes.

4.3.1.1. Mergers and acquisitions

In recent years, the EU has witnessed rapid growth in mergers and acquisitions (M&As) activity. This growth has been particularly strong in cross-border activity, which is one of the main components of the wave of FDI analysed above. However, the bulk of M&A operations is still overwhelmingly domestic, indicating that the restructuring has taken place, at least initially, through changes to domestic market structures. For the EUR 15 over the period 1990-95, more than 70% of all operations were domestic, a proportion which was roughly the same over the period 1986-90.

The domestic nature of the restructuring process is especially significant in countries such as Germany, Spain and Italy and, in general, it is a feature of the largest economies in the Union. Small open economies in the Union tend to have a larger share of cross-border M&As. This is particularly true for Austria and Ireland. As mentioned before, cross-border M&As are increasingly Community M&As (18.7% between 1990 and 1995). Operations involving firms from the rest of the world continue, however, to be important for countries such as the UK, Ireland, Sweden and Austria.

The extent of industry restructuring that has taken place over the SMP implementation period varies by Member State. This may be due to differential effects of the SMP, but to a large extent it is related to national differences in financial and regulatory systems. Amongst the largest economies in the Union, restructuring via M&As has been especially important in the UK, whilst Italy and Spain have registered rather low levels of operations when compared with the importance of their economies.

Interestingly, companies from the Nordic countries, the Netherlands, France and the UK, have predominantly taken the bidding role in the M&A process. Conversely,

companies in countries such as Italy, Spain and Germany have usually been the targets of acquisitions.

At the sectoral level, restructuring has taken place both in manufacturing and in services. Manufacturing was the more active target over the period 1988-92, possibly even in anticipation of the removal of barriers by the SMP; in the latter period (1993-95), services took the lead, in accordance with the delayed introduction of SMP measures in these sectors. Between 1986 and 1995, the number of operations grew from 720 to 2 296 in manufacturing, and from 783 to 2 602 in services.

The importance of domestic operations in the M&A process is particularly significant in the case of services, where institutional restrictions may have prevented the extent of intra-European cross-border operations which has been observed in manufacturing. In 1995, 70% of all deals were domestic in services, and the figure was 63.5% in manufacturing. Incomplete adoption of SMP regulations in services could therefore prevent some beneficial cross-border restructuring (for example, in the banking and transportation sectors).

M&As have allowed both external firm growth and internal restructuring as demanded by the new post-SMP scenario. Next, we review how this has translated into changes in market structure and efficiency.

4.3.1.2. Concentration

In manufacturing, restructuring has led to substantial increases in the concentration of European industry. For industry on average, the share of total sales by the four leading firms increased from 20.5 to 22.8% between 1987 and 1993, although in France, Belgium and the UK, domestic concentration actually decreased. Only Germany over this period experienced a tendency towards increasingly concentrated industries. Such a tendency is at the root of the increasing gap between the average size of manufacturing firms in Germany and the size of firms elsewhere in the EU.

Many industries have experienced increases in concentration exceeding five percentage points. The most significant increases have taken place in industries related to public procurement, (in telecommunications: wires and cables, transmission equipment; or transportation: aerospace, rail stock), in food sectors sensitive to the

SMP (pasta, starch, oils and fats) and in other sectors such as electrical machinery, domestic electrical appliances and measurement equipment.

Overall, the trend towards increasing concentration at the EU level is especially significant in technologically intensive industries (see Table 1). These are industries which were particularly sensitive to the SMP, and where the efficiency gains from an enlargement of market size and an increase in scale are both particularly important and seem to have been reaped by the sectors' leading firms.

In industries where advertising, brand name and marketing are important (such as mass consumer goods like food products, consumer chemicals, consumer electronics and motor vehicles), the increase in EU-wide concentration is more moderate, and fundamentally at the national level, suggesting the predominance of domestic restructuring. This is consistent with the industries' characteristics where the diversity of preferences and distribution channels across the EU might still be partially segmenting national markets. Leading firms do deploy their marketing skills Europe wide, but most of the increased concentration is the result of increasingly concentrated domestic markets. In this type of industry, the average share of the four leading firms went up on average between 1986 and 1992 by 2.9 percentage points in Germany, 1.3 points in France and 3.2 points in the UK.

The impact of the SMP on concentration in market services has been very much affected by the nature of each service. Sectors such as distribution and road freight transport — which were very sensitive to the SMP (by virtue of direct regulations or indirectly as in the case of distribution) but now face relatively light regulations — have registered substantial restructuring, involving both domestic and EU increases in concentration. The improved efficiency of these sectors has had a significant upstream effect on manufacturing industries and downstream on final consumers, to the extent that significant cost reductions in distribution have been achieved (see below).

In road freight transport, the industry has segmented with an increase in both large and small specialized competitors, but a declining share for intermediate firms. In distribution, increased EU-wide concentration by manufacturers and retailers has reduced wholesalers' market share. New firms providing logistic services throughout

the distribution chain have gained substantial ground in the industry.

Highly regulated services, with large potential gains from scope and network economies (economies tied to the simultaneous exploitation of several businesses or a distribution network) such as telecommunications, airlines or retail banking, have observed smaller increases in EU-wide concentration. Quite often, due to institutional constraints, the benefits that can be derived from a wider EU market have been exploited by alliances and not M&As. Increased concentration has been observed only at the domestic level, selectively and very much depending on the extent to which some of these sectors had restrictions on entry before the implementation of the SMP. For example, the market share of the leading firms has increased slightly in banking, but declined in airlines and telecommunication services, where entry regulations had artificially kept concentration ratios high.

4.3.2. Efficiency and competitiveness

The SMP is expected to boost productive efficiency through a number of channels. These include the elimination of technical inefficiencies arising from low competitive pressure which results in the under-utilization or misapplication of productive, managerial and human

resources. Cost reductions may also be realized through more effective exploitation of economies of scale and scope either at plant or firm (R&D, advertising) level. Other efficiency gains may spring from economies which are external to the firm, as when firms within a given region enjoy technological spillovers or share access to specialized inputs. Finally, the SMP may have a dynamic efficiency effect, changing the incentives to undertake R&D, the rate of adoption of new technologies or increasing the benefits of learning-by-doing processes by EU firms.

4.3.2.1. Direct savings resulting from SMP integration

That the SMP has been a source of direct savings to firms, particularly manufacturing firms, is confirmed by responses to the Eurostat business survey (see Tables 2 and 3). Overall, the survey records more positive than negative responses about cost reductions, especially when stratified by enterprise size. Large firms appear to have benefited most from unit cost reductions associated with the SMP. According to the survey, the gains in terms of lower unit costs were mostly due to reductions in raw materials costs (new sourcing opportunities), the costs of operations and distribution costs. These perceptions concern only the first-order effects related to barrier removal.

Table 9 — Perceived importance of unit cost changes in manufacturing by cost category

(% of firms expressing an opinion)

Category	Important	Not important	Don't know
Production process	22	33	44
Testing and certification	19	37	44
Distribution costs	21	35	44
Marketing costs	15	41	44
Cost of raw materials	30	26	44
Banking costs	17	40	44
Insurance costs	14	42	44
Other costs sources	4	24	71

Source: Eurostat, 1996.

4.3.2.2. Scale economies

According to previous analyses, the SMP was greatly expected to improve efficiency by making it possible and worthwhile to exploit previously unexploited economies of scale, thereby producing an increase in plant size. There is no empirical evidence so far in support of this view. The available empirical evidence indicates that firm size has increased however not in sectors sensitive to SMP.

However, data on the distribution of firms by size is not gathered on a consistent and timely basis, and even simple information on average firm size is only available after a considerable delay. In any case, average firm size is an indicator to be interpreted with great caution.

One of the remarkable facts of the European manufacturing sector is the significant difference between average firm size in the leading industrial Member State, Germany, and other major industrial countries such as France or the UK. In 1985, gross value added per firm in Germany was ECU 7.4 million (1990 prices), a third higher than in the other two countries. The data show that manufacturing firm size in the largest EU countries increased between 1985 and 1992 by between 8% in France and 15% in Germany and Italy. Of the main EU economies only the UK did not experience an increase in firm size. The overall period increase was 11% for the four economies.

This means that after the implementation of the SMP, this structural characteristic of the European manufacturing sector has remained unaltered. If anything it has been reinforced given the comparatively weak growth of firm size in France and, in particular, the UK, compared to Germany.

At the sectoral level, the large size of German firms is particularly significant in motor vehicles, chemicals and engineering industries, but also in more traditional industries such as textiles and timber. Over the SMP's implementation period, the size gap between Germany and the other countries has increased in sectors such as office machinery, measurement equipment and transportation equipment; but also in the food, textile and clothing industries.

However, the SMP does not seem to have had a differential effect in terms of its impact on firm size across

sectors. The strongest growth in firm size has actually been in the set of industries which were not SMP-sensitive. Sectors where the SMP was supposed to have a stronger impact already had a larger firm size on average, and growth has lagged behind.

Changes in firm size have therefore not been fundamentally linked to the impact of the SMP, but rather to the nature of competition in each industry. Strong growth of the average size of firms has been detected in advertising-intensive industries in all four main EU countries. This trend is consistent with the data on national concentration and confirms that in these industries firms are increasing their size, so as to reap dynamic scale economies linked to the creation of strong brand names, new product development and heavy up-front advertising investments.

The performance of sectors where R&D is important has not been as impressive in terms of the size of the average firm but nevertheless, as argued above, the data on concentration do indicate that R&D intensive industries have taken advantage of an EU-wide market and spread across the Community their large up-front fixed costs. Moreover, the firm size indicator is particularly inappropriate in this kind of sector, which is subject to entry by new innovative firms and which tends to diminish the observed average firm size.

In sectors where scale economies are linked to establishment size (technical or engineering economies), we also observe an increase in the average size of firms. However, there is no systematic evidence yet that firms have indeed profited from the SMP by reorganizing production across Europe and increasing the size of their establishments.

Efficiency gains in service sectors associated with the SMP have been harder to detect due to the nature of service activities and the problem of measuring outputs and inputs in these sectors.

In sectors such as distribution and road freight transport, some indicators show remarkable productivity gains. For example, improvements in the distribution sector over the period 1987-93 led to logistic costs declining as a proportion of total revenue for a large sample of 1 000 large European firms by 30%. Other gains have been a reduction in the number of days between order placement and shipment receipt (from 21 to 15 days) and an

increased quality of service (a decline of 31% in the service failure rate). In road freight transport, the SMP has reduced the cost of cross-border transport by an estimated 6%. However, the harmonization requirements imposed on this sector by the SMP have also led to cost increases for international transport ranging between 1 and 2.5%.

Productivity and efficiency gains in the more regulated sectors (telecommunications, banking, airlines) have been less pronounced and, in general, it is uncertain whether the observed changes can be linked to the SMP. Large gains have been observed only in liberalized telecommunication services. In this case, the SMP has indeed promoted rapid technological change (for example, in cellular telephony through the adoption of the GSM standard) which is the main source of efficiency gains in such a dynamic sector. In airlines and banking the evidence is less comforting.

For airlines, labour productivity has increased ahead of labour costs, although this is basically due to the reduction of the labour force directly employed by airlines. In banking, no significant improvements in productivity or efficiency are reported. Staff costs in banking have declined but these reductions may have been compensated by increases in non-staff costs related to investments in information technology. These trends, however, do not appear to be the direct result of the SMP measures adopted in the area of banking.

The SMP has also boosted Community firms' relative performance by forcing them to compete more aggressively. Detailed econometric analysis of trade flows in different manufacturing sectors suggest that reductions in price-cost margins in response to the SMP have helped producers in SMP-sensitive sectors to win increased market share. This analysis takes as its starting point that price-cost margins in SMP-sensitive sectors have decreased by 3.9%. This has allowed these companies to expand domestic production at the expense of both intra- and extra-EU imports, enabling them to hold on to an estimated 1.2% of domestic markets which would otherwise have been lost to partner country and third country competitors. More successful defence of domestic markets through this price-reduction has denied partner country producers a 0.8% increase and third country producers a 0.4% increase in share of the national market in question. This outcome compares with other manufacturing sectors, where sectors have not encountered the

SMP stimulus to reduce price-cost margins. As a result, domestic producers in these sectors have lost 0.8% of national market share, with other EU and third country producers benefiting to an equal degree.

4.3.3. Competitive conditions in European markets

The promotion of active competition is particularly important because, as described above, the European economy has undergone a process of increased industrial concentration as a result of the SMP. Such an increase in concentration and firm size could result in reduced economic welfare were it to stifle competition. However, evidence on price cost margins and business perceptions seems to indicate that the efficiency gains associated with large size have been passed on to consumers and users thanks to increased competition associated with the SMP.

Implementation of the SMP has had a significant positive effect on the degree of competition in manufacturing sectors. Over the period 1980-92, European manufacturing industry registered a trend recovery of price-cost margins, at a yearly rate of about 2%, controlling for the evolution of the economic cycle and the diverging industrial structures of the EU Member States. Within this overall trend, the statistical analysis of price cost margins confirms that implementation of the SMP imposed increasing pressure on price-cost margins, thus ensuring that cost reductions have been passed on to consumers and downstream users. The data indicate that the SMP has led to a significant reduction of price-cost margins, with a yearly 1% reduction in margins as of 1986/87. That is, in the absence of the SMP, margins would have grown faster over the period. The relative decline in margins triggered by the SMP has been particularly important in some of the manufacturing sectors most sensitive to the SMP, namely, industries in high-tech public procurement sectors (i.e. office machinery) and sectors which had moderate non-tariff barriers before the SMP (consumer electronics, motor vehicles, textiles and clothing). The effect on other SMP-sensitive sectors (traditional or regulated public procurement markets such as pharmaceutical products, electrical equipment, etc.) does not appear to have been significant.

The increased competitive pressure revealed by margins data is confirmed by the perceptions of firms reflected in

the Eurostat business survey. The pro-competitive impact of the SMP has expanded beyond the sectors which were targeted by SMP measures. Through market interactions and strategic reactions by firms, changes in competitive conditions in one sector have spilt over to related sectors, such as clients or suppliers. For example, SMP-driven changes in the glass sector have led to upstream restructuring in the soda ash industry; similarly, the liberalization of telecom services has had a profound impact on the telecommunications equipment market. This spreading of the SMP effect means that the linkage between SMP sectoral sensitivity and changes in performance — for example, prices — is not simple, since many non-sensitive sectors end up being affected by the SMP.

Competitive conditions in services have also been significantly altered by the SMP. A significant increase in competition is noticeable in sectors such as telecommunication services or retail banking, but also in airlines, where implementation of the SMP has only been partial so far. Overall, however, the increase in competition seems to be less strong than in manufacturing sectors, reflecting that many regulations are still maintained on services and that the SMP has not been fully implemented in several domains. This difference in the reaction of manufacturing and services is also consistent with the results obtained by the business survey. Business perceptions also indicate that the increased competitive pressures in services are mostly due to the behaviour of domestic competitors, which is in tune with the predominantly domestic nature of restructuring due to the SMP (highlighted above in the analysis of M&As).

The change in the degree of competition in services has been prompted by new entry in certain markets (telecommunications, airlines) but also by the elimination of conduct regulations which restricted firms' marketing strategies (airlines, banking).

Increased competition has resulted in substantial and quite general reductions in prices in sectors such as telecommunications, and a more selective decline of prices in segments of the airline and banking industries. In airlines, margins in real terms declined by almost 20% between 1986 and 1994. In banking, intermediation margins have also declined, reflecting increased competition in some segments of conventional retail banking markets (i.e. high-yield checking accounts etc.). Prices have declined for selected products such as credit cards, cor-

porate loans and some deposit products in most EU countries.

In road freight transport, the margins for cross-border traffic declined sharply over the period 1986-94. The result has been a reduction in real transportation prices which, together with efficiency gains in the distribution sectors, have led to substantial changes in the sourcing patterns of manufacturing and retailing firms. A wider range of sourcing possibilities explains the decline in input costs, one of the key components of costs reduction due to the SMP as reported in the business survey results.

Finally, competition in some service sectors has been distorted by the existence of restrictions which have prevented market adjustment. State aids and other government interventions or regulations have prevented the complete restructuring of some industries — such as airlines or banking — to face the new competitive environment created by the SMP.

The pro-competitive impact of the SMP may have been dampened by the behaviour of firms and/or governments. In the case of firms, it could help explain the *de facto* limited changes following the liberalization of public procurement markets. In the case of governments, State aids still play a role in certain sectors. Note also that these markets have registered remarkable increases in concentration and firm size through a process of mergers and acquisitions, and only limited declines in price-cost margins.

4.3.4. Price convergence across the European Union

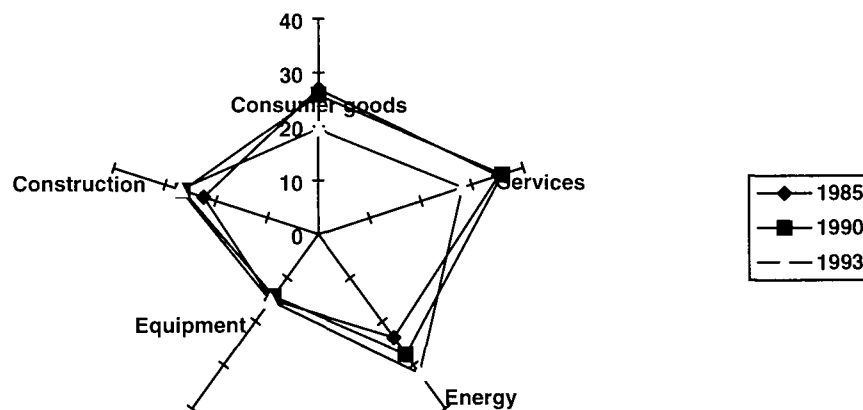
The changes in structures and the degree of competition of European markets prompted by the implementation of the SMP have also resulted in increased price convergence across the EU between 1985 and 1995. For certain goods, no additional convergence of prices is expected as existing levels of price dispersion are the result of structural sectoral characteristics fully compatible with the achievement of an integrated pan-European market, such as differences in taste and culture, in income levels, etc.

Most price convergence is observed in consumer and equipment goods, particularly those that are highly

traded within the EU and with the rest of the world. Convergence in consumer goods has been accelerated by the SMP. In 1993, within the EUR 12, the price variations⁴⁶ of identical products and services in different Member States were including taxes: 19.6% for con-

sumer goods, 28.6% for services, respectively down from 22.5% and 33.7% in 1995. However, energy and construction price variations increased respectively from 21.1% and 22.1% in 1985 to 31.7% and 27.4% in 1993 (see Figure 3).

Figure 5 — Price variations for different products/services, EUR 15



Source: DRI Europe (1996).

In services, price convergence is also observed and has been accelerated by the SMP, although less convergence is to be expected in non-tradable services as the degree of price dispersion is basically correlated with the dispersion of incomes per capita. No convergence is observed, however, for energy and construction.

Taxation (in particular, excise duties) and regulatory intervention are significant determinants of exceptionally high levels of price dispersion. This can be observed in the energy sector, and to a lesser extent for manufactured goods, for example, for health care related products, where regulatory intervention helps price dispersion to take place. These sectors have not been affected by implementation of the SMP.

Finally, price convergence has been faster in the Member States which joined the Community after 1980, especially the countries from southern Europe.

The increased convergence of prices for many products and services across the EU corresponds, at the detailed microeconomic level, to the process of convergence in inflation (disinflation) achieved in the EU over the last

few years. The SMP effect on prices has facilitated the conduct of a stability-oriented macroeconomic policy in making adjustments less painful in terms of less employment than could otherwise have been created.

4.4. Income, employment and convergence

4.4.1. Income and employment

The previous sections supplied an analysis of the main channels through which the SMP impacted on different segments of the European economy. This mostly microeconomic analysis produced many interesting pieces which provide evidence about the changes to the EU economy set in motion by the SMP. In the present section, we attempt to put together these different pieces so as to furnish a coherent *ex post* quantitative macroeconomic assessment of the SMP.

Providing this assessment is a perilous task due to methodological difficulties. Quantification of the SMP effect raises the anti-monde problem, e.g. estimating

⁴⁶ In fact, the measure used is the coefficient of price variation (including taxes), but the point is still the same.

what the world would have looked like in the absence of the SMP. Two types of models can be used for simulating the anti-monde, each with its own advantages and disadvantages: macro models and computable general equilibrium (CGE) models. Another methodological problem relates to the fact that the use of simulated models (regardless of whether they belong to the macro or CGE variety) to assess a regime change such as the SMP suffers from the inherent difficulty of incorporating such change in the model. Two models were used for the *ex post* quantitative macroeconomic assessment of the SMP: GEM-E3-IM, a multi-country, multi-sectoral dynamic CGE model;⁴⁷ and QUEST II, a multi-country dynamic macro model.

Based on these assumptions, GEM-E3-IM estimates that the EU GDP growth in 1994 was 1.1% above the level that would have prevailed without the SMP. The similar estimate based on QUEST II is 1.4%. Given that in 1994 the level of GDP for EUR 12 was around ECU 5 500 billion, these estimates imply that the SMP produced, in 1994, a gain of GDP in the range of ECU 60 billion to ECU 80 billion.

Where do the gains come from? The two main components are the increase in competition/efficiency and the rise in total factor productivity, each accounting for about half of the total effect. The elimination of trade barriers reduces the degree of segmentation of national markets, thereby increasing the degree of competition, which leads firms to increase their level of output. The result is also a decrease in costs and in prices, with a decrease in price-cost margins. This is the allocation or efficiency gain that puts the economy on a higher trajectory, albeit at the same growth rate as in the absence of the SMP. On the other hand, the rise in TFP, associated with a decline of X-inefficiency prompted by greater competition, induces a higher growth rate of GDP (the increment being of 0.1%).

Both GEM-E3-IM and QUEST II also compute the impact of the SMP on employment. GEM-E3-IM estimates that the EU employment level in 1994 was about 300 000 units above the level that would have prevailed

without the SMP. The similar estimate based on QUEST II is 900 000 additional jobs. Further analysis of the impact of the SMP on employment was undertaken with the help of E3ME,⁴⁸ a multi-region, multi-sectoral econometric input-output model of EUR 12. This model assesses the impact of the SMP on manufacturing trade and ultimately on employment. The anti-monde simulation produced by E3ME is based on trade equations reflecting the absence of the SMP. The model estimates that the level of employment in 1993 was 600 000 units above the level that would have prevailed in the absence of the SMP.

Although, as pointed out above, the single market impact on overall employment is positive, it is negative for the manufacturing sector alone by around -5.3%. These results suggest that the single market has had the effect of accelerating structural change towards services. Within manufacturing, strong rationalization has taken place in rubber and plastic products and agricultural and industrial machinery. These sectors' job losses are offset by gains in ferrous and non-ferrous metals, metal products and textiles, clothing and footwear.

In conclusion, the impact of the SMP on income and employment obtained up to now is far from being negligible. There is little doubt that the effects will continue to grow as the SMP is further implemented and economic agents adjust to the new competitive environment of the European economy.

4.4.2. Convergence

Ensuring a high degree of convergence of economic performance and promoting economic cohesion are fundamental objectives of the European Union.⁴⁹ This section will also assess to what extent the single market has succeeded in spreading growth increases across all EU Member States and regions, focusing particularly on the less developed ones. Issues such as specialization patterns in trade and production are relevant to this discussion.

⁴⁷ See National Technical University of Athens study, *Computable general equilibrium modelling for the ex post effects of the EU internal market programme*, November 1996.

⁴⁸ See Cambridge Econometrics study, *Employment, trade and labour costs*, November 1996.

⁴⁹ Article 2 of the EC Treaty as amended by Article G(2) of the EU Treaty.

The expected effect of the SMP on convergence within the EU is ambiguous. On the one hand, the SMP should favour convergence of per capita income levels across Member States through greater goods, services, capital and labour mobility. On the other hand, increased geographical specialization could lead to increased polarization between richer and poorer countries or regions.

Within EUR 12, analysis of the performance of Member States grouped by their date of entry into the EU provides useful insights. In terms of gross value added (GVA), the EUR 6 and EUR 9 performed much the same as the EUR 12 as a whole, but the new entrants, Spain, Portugal and Greece, saw a larger relative improvement, their overall GVA in 1993 being nearly 7% higher than it would have been had pre-1987 growth trends continued. These three countries plus Ireland form the group of the so-called cohesion countries.

This group's performance is even more striking, with a nearly 9.5% improvement in 1993 relative to an extrapolation of pre-1987 trends. This reflects the rapid growth of the Irish economy since 1987. With an average growth rate of about 8.5% per annum post-1987, compared with 2.7% per annum in the period up to 1987, Ireland's GVA in 1993 was about 40% higher than it would have been if its economy had continued to grow at the pre-1987 rate. Examining GVA per capita, the comparison of actual and extrapolated levels ceases to be positive for the original EUR 6 and EUR 9, but the improved performance of the new entrants and the cohesion countries is even higher.

Statistical analysis confirms that Ireland, Portugal and Spain have had above average growth, and have therefore converged, after 1987. Among the poorer parts of the Community, only southern Italy and Greece have performed relatively worse after the SMP than before. The analysis gives some support for the fact that the SMP, in general, has contributed to these trends. However, in the case of Spain and Portugal, accession to the EU may have played an even larger role.

On a regional level, there are some indications that the convergence process has been Community-wide rather than concentrated in a few Member States. Country-specific influences remain important but, taking into account differences between Member States, the speed of convergence of the regions is broadly similar. The question here is to what extent convergence is due to the

SMP or to Structural Funds support (including the capacity of each Member State to manage these efficiently). However, given that the launch of the SMP was accompanied by a significant Community regional policy package that ensured large flows of Structural Funds to the less-developed regions, it is difficult to distinguish with accuracy the effects of Structural Funds spending on the favourable growth performance post-1987 from the SMP effects.

5. The single market and other policies

5.1. Introduction

The previous chapter considered the economic impact of the SMP on the European Union economy as a whole, on industrial structures, trade and investment, prices, competition and competitiveness, growth and employment.

This chapter examines the impact of the single market measures on the achievement of other Community policies and, where appropriate, the implications and challenges which the single market represents for the further development of these policies.

The chapter addresses the following areas:

- The single market and social policy
- Enterprise policy: the single market and SMEs
- Environmental policy
- Consumer policy
- Competition policy
- The single market and third countries.

5.2. The single market and social policy

There are significant interactions between the single market and social policy. Accompanying measures in the social field have often been accompanying measures necessary to achieve single market completion. Most social policy measures were designed either to guarantee one of the four freedoms — namely free movement of workers — or to ensure that the single market would translate into real improvements for workers. Since

economic integration is not possible without adequate social provisions, social policy measures based on safeguarding free movement and support for vulnerable groups are also required for the success of the single market. Examples of social policy initiatives which have been taken in anticipation of changes brought in by the single market are the Directive on a European Works Council⁵⁰ and the Directive on detached workers at present under discussion. These two pieces of legislation aim to respond to a new economic reality that has developed since the implementation of the single market: the importance of the trans-European company or problems that might arise due to increasing workforce mobility. Other pre-existing social measures, such as recognition of social security rights, have also provided a supporting framework for single market measures related to the free movement of people or freedom to provide services.

5.2.1. The SMP's impact on the social environment

5.2.1.1. Social dumping

Fears that investments would flow to those countries within the EU with lower levels of social protection and lower labour costs, seem to have been unfounded. There are only isolated examples of competitive undercutting of pay and conditions by firms exploiting differences in labour costs or labour regulations between Member States. Most EU and non-EU multinationals admit that except for very specific sectors and functions (centralized management for airlines) other factors have played a more important role in location decisions. This is even more true for the manufacturing sector where transport facilities or logistics are more important. However, this factor has played the same role for Japanese and Korean companies, starting greenfield investments in Europe.

⁵⁰ Council Directive 94/45/EC of 22.9.1994 on the establishment of a European Works Council or a procedure in Community-scale undertakings and Community-scale groups of undertakings for the purposes of informing and consulting employees (OJ L 254, 30.9.1994).

5.2.1.2. Changes in industrial relations: collective bargaining and social dialogue

The new challenges and changes introduced by the single market have led to a certain consensus, across Member States and economic agents, on whether employers or trade unions, that labour markets had to become more flexible and new dialogue channels had to be developed and adapted to the new reality. How to achieve this goal is an open debate in most Member States and also at the EU level, related to the specific needs of each country or economic sector.

Some major changes occurred between 1985 and 1995 in pay determination and the pattern of collective bargaining. These reflect a variety of international and domestic pressures rather than an identifiable general single market effect. However, it is possible to relate some of these changes to the indirect effects of the single market. Changes in four areas have been assessed: corporate personnel and pay policies, wage setting and inflation, decentralization of collective bargaining and the relationship between pay and performance at individual level.

- The single market impact on corporate personnel and pay policies has generally been limited. The number of staff being transferred between countries has increased but these are still largely confined to managers and highly specialized workers. Company remuneration systems for these categories are therefore tending slowly to converge. At company level, more indirect effects of the single market have been an increased concern to control labour costs, changes to grading or classification of employees, and improved links between pay and performance.
- Increasing concern has spread among policy-makers and social partners about the need for more credible national economic policies, due to the new economic environment created by the single market and the EMU convergence criteria. As a result, a significant change in attitudes towards the relation between pay and inflation has been seen in a number of countries. Inflation forecasts have become more important as a point of reference in pay negotiations than backward-looking informal indexing. Italy is a good example of a country where a major reform of collective bargaining — featuring in particular the abo-

lition of indexing — was strongly influenced by the European integration process.

- A major change in collective bargaining across Europe, due to heightened international competition, has been a clear tendency towards greater decentralization. Despite great diversity, there has been a broad convergence towards greater scope for local negotiations and a greater degree of subsidiarity at company level. The single market influenced this, to the extent that it increased awareness among the social partners of the need to make pay correspond better to productivity at company level in order to sustain increasing competition. However, decentralization of bargaining began several years before the 1992 programme and was by no means an 'EC phenomenon'. Spain and Italy are examples of countries where in-depth reforms have taken place with the aim of liberalizing industrial relations in a number of ways, including the allocation of separate roles for industry-wide and company bargaining (Italy) and the promotion of collective bargaining as a replacement for the courts and labour ordinances (Spain).
- Variable pay (productivity bonuses etc.) as well as payment systems related to company performance (profit-sharing arrangements etc.) are increasingly widespread in Europe. Although, neither seems to be a direct effect of the single market, they have certainly been spurred by the SMP, among other international factors. To the extent that they motivate employees and/or relate pay more closely to productivity or profitability, these systems reflect the general drive for greater competitiveness.

5.2.2. Geographical labour mobility

Free movement of workers has been a reality for the six founding members of the European Community since 1968 (Regulation 1612/68 and Directive 68/360). Free movement is defined as the 'abolition of any discrimination based on nationality between workers of the Member States regarding employment, remuneration and other conditions of work and employment.' It now applies to all the Member States and three of the EFTA countries (Norway, Iceland and Liechtenstein). Free movement of workers has been facilitated by supporting measures such as mutual recognition of diplomas or the right to transfer social security entitlements to other Member States.

To a large extent this legislation has succeeded in abolishing all obstacles to free movement of workers. Increased use of these instruments would therefore have been expected. However, available empirical evidence does not support the claim that the single market has promoted geographical labour mobility within the Union. The influx of unskilled and semi-skilled workers from within the Union 25 years ago, which balanced labour shortages in the high income countries, does not seem likely to recur.

Several factors have contributed to the absence of a visible single market impact on intra-EU migration flows.

- (i) Trade relations between Member States have intensified as a consequence of the single market. Furthermore, trade and competition have happened more because of product differentiation than because of inter-industry division of labour which has reduced the potential for job displacement. Unemployment would have been a potential incentive to migrate, but did not materialize significantly in the run-up to 1992.
- (ii) Incomes across the Member States (for per capita national product) are tending to converge. Pressure to migrate for economic reasons is low between countries with similar levels of development. Hence, if improvement of the standards of living in the home country can be expected, incentives to move abroad diminish. If during the integration process an alignment of economic development and therefore of pay levels occurs, then the income differential factor for migration will tend to disappear. This has been the case in those countries which had served in the 1960s and 1970s as manpower providers (Spain, Italy, Greece and Portugal), whose rapidly improving economies will not favour an excess supply of labour there over the long run.

Although, considerable differences between low-income and high-income regions within Member States still remain, they tend to contain migration flows within individual States and not to induce workers to migrate across national borders.

- (iii) Modest overall employment growth did not increase employment opportunities for potential migrants.

- (iv) Capital has proved more mobile than labour and has substituted for migration. Available evidence suggests that, partly as a result of the SMP, intra-EU trade and investment flows have been boosted to such an extent that they have actually substituted for migration.

- (v) Cultural and social barriers: language problems, difficulties in assessing foreign qualifications, differences in social and cultural background, and family situations are all major factors impairing workers' mobility.

There is evidence, however, that the positive impact of actions to improve the free flow of labour (for example the mutual recognition of educational and training certificates) has promoted a new type of labour mobility between Member States. Labour force survey figures suggest a slow but constant increase in EU nationals working in other Member States. Rather than generalized and substantial migration of labour, we are likely to see more specific patterns of geographical mobility, circumscribed to well-defined regions and occupations.

- (i) Labour demand has concentrated in the high-skilled qualified workforce. Either the single market, increasing qualification requirements, an ageing workforce or the pressure of globalization, has intensified competition within the EU for scarce qualified personnel, particularly managers, professionals or highly specialized technicians. These constitute an increasingly flexible, mobile and internationalized workforce, as opposed to other labour categories that remain confined to their national labour markets. As a result, changes brought in by the single market, by improving the free movement of workers and the recognition of diplomas, have opened up new opportunities for business to fill available posts, with more choice, and in a more flexible manner. For example, data from Germany indicate that more migration of the highly qualified workforce will take place. In this country, whereas overall employment of EU nationals has gone down, employment of graduates from EU countries has risen, although the level is still quite low.

- (ii) More migration has taken place in regional economic areas near the borders. This has resulted in commuting between a place of residence and a place of work in different countries, particularly in certain

regions, such as the Franco-German or the Franco-Luxembourg borders. Intra-EC frontier migration, which has increased by 18% between 1987 and 1994, is encouraged by differences in pay, as well as differences in taxation, social security and housing costs.

(iii) Another type of temporary migration of labour is that of so-called contracted workers from EU countries. Even if local wages are being paid, as provided for in an EC Directive currently under discussion between the European Parliament and the Council, cost advantages may be gained by posting large groups of workers from Member States with low social security contributions to Member States with high contributions. Most posted workers go to Belgium and Germany, whereas the majority of posted workers originate from France, the Netherlands and the United Kingdom. From statistics made available by Member States, most postings on the basis of Article 14(1)(a) of Regulation (EEC) No 1408/71 take place in the field of construction.⁵¹

5.2.3. The effects of social policy

Outright harmonization of social policies has not been an objective of the Union. However the implementation of the single market led, through the realization of the Commission's 1989 social action programme, to the establishment of a framework of basic minimum standards, providing a bulwark against using low social standards as an instrument of unfair economic competition.

Some Community social initiatives, such as those related to protection of health and safety at work, are also relevant to the smooth functioning of the single market, since a consistent level of protective measures across the European Union ensures fair competition for businesses. Consistent working conditions for employees stimulate and facilitate their mobility. According to Article 118A of the Treaty, the EU is to encourage such improvements.

The Treaty (Article 129) stipulates that health protection requirements shall form a constituent part of the

Community's other policies. Some single market measures have numerous interactions and consequences for health. Health requirements are of particular importance and relevance for citizens. Examples of legislation with health implications include regulations on specific products, for example, pharmaceuticals/medical devices and cosmetics, on the tar content of cigarettes and the labelling of tobacco products, and on the quality of food and foodstuffs. Similarly, health protection requirements play a role in other areas where single market regulations have been developed, for example, free movement of people (such as health professionals), environmental policy, energy policy or transport policy.

Current EU policies and programmes (mutual recognition of diplomas, freedom of residence, exchanges of students) implemented to support and overcome remaining obstacles to free movement of workers have facilitated the development of new patterns of labour mobility, such as the rise of a new international highly qualified labour force, an increase of labour flows in cross-border regions or increasing flows of contracted workers. However, the positive role of these policies has been much more relevant to the highly qualified workforce, strengthening the current trend for a more international labour supply in this segment of the labour market.

Adequate protection by Community legislation in the field of social security is also a precondition for the effective use of the right to move within the Union. Without such protection, existing disparities between the social security schemes of the different Member States would adversely affect people moving across frontiers. Regulations (EEC) Nos 1408/71 and 574/72, coordinating the social security schemes of Member States, guarantee that rights to social security benefits acquired or in the process of being acquired under national legislation (for example for pensions, health insurance, family benefits), will not be lost when people leave their country to work, to look for a job, to reside or to stay elsewhere in the Union. As an example of the extent that these instruments have been used, the total number of E101 forms issued for postings within the Union rose from 356 000 in 1991 to 535 000 in 1994.⁵²

⁵¹ Donders, Peter. *Applications of the provisions of Regulation 1408/71 and the issue of posting: facts and problems*, 1995.

⁵² Data excludes Luxembourg, Germany, Italy and Belgium.

Another example of social Community action to promote the free movement of workers, is the EURES network created in 1989. EURES aims to provide services and information concerning job vacancies, and living and working conditions, throughout the Member States, Iceland and Norway; it therefore contributes to the transparency of the single market and facilitates mobility in an open European job market. Furthermore, the work of the EURES network helps to identify and throw light on obstacles to mobility, especially at the practical level.

5.3. Enterprise policy: the single market and SMEs

Research for this review⁵³ suggests that, overall, the single market has benefited large companies more than SMEs. They perceive the positive consequences of the SMP more keenly than smaller firms. For example, for the manufacturing sector, 47% of companies with more than 1 000 employees consider that the SMP has successfully eliminated obstacles to EU trade in their sector, as opposed to 38% of smaller firms (between 20 and 49 employees).⁵⁴ Results for the intervening size categories occupy intermediate positions but show little variability.⁵⁵

This pattern is systematically repeated when companies are questioned about specific categories of measures. The discrepancy between small and large firms is not so important when changes in customs procedures and abolition of frontier controls are considered (54% positive impact for small firms opposed to 72% for large firms in respect of customs documentation); but in other fields, the gap between small and large firms is more pronounced (e.g. protection of patents 9% vs. 36%, or public procurement, 8% vs. 20%). This may, in part, reflect intrinsic market distortions (information asymmetries, entry barriers arising from high-fixed costs of entry for small companies, lack of access to financing, or the dominance of procurement by larger firms).

The more positive assessment by larger companies of measures taken to complete the SMP may be attributable to two factors:

- (i) the fact that SMEs operate only at local or regional level makes them believe that access to new markets is not a priority for them, and that most measures related to free movement of goods or services are therefore irrelevant to their activity. This would explain the low level of awareness of the SMP among smaller firms. The higher propensity of larger firms engaging in cross-border transactions makes these companies more aware of changes in the trading environment;
- (ii) many of the sectors most sensitive to single market measures tend to be characterized by higher average firm sizes (telecoms equipment, electrical machinery, chemicals and man-made fibres, pharmaceuticals, motor vehicles, machine tools and basic chemicals). Firms from these sectors have a more positive perception of the impact of various categories of SMP legislation than those in other sectors which were less directly targeted (and which are also smaller in size).

For most SMEs, whether they operate at international level or not, their biggest problem is the cost of complying with new technical, administrative and fiscal regulations. Large companies report that they have been able to reallocate a member of staff to deal exclusively with the paperwork needed in order to comply with the new legislation. Smaller companies state, however, that this poses a serious cost to their business. These represent once-off fixed costs that tend to be a higher proportion of an SME's total turnover than that of a larger company. Also, small manufacturers in some sectors, such as machinery manufacturing, tend to produce bespoke equipment so the costs of conformity for each new model are high. For example, smaller machinery manufacturers view the CE marking as a necessary marketing tool. However, the cost of complying with it is a fixed

⁵³ In particular, the DRI trade associations and Eurostat business surveys.

⁵⁴ The size classification of companies used by Eurostat in the business survey, does not correspond with that adopted by the Commission on 3.4.1996.

⁵⁵ Source: Eurostat survey.

cost, which inevitably raises the break-even point: this is negligible for large manufacturers producing in series, but can be important for manufacturers of specialized one-off or short runs of machinery.

Nevertheless, SMEs from some sectors have expressed more positive views about the impact of the single market on their activity. This is the case, for example, in the detergent and cosmetics sector, where SMEs have experienced an improvement in access to European markets. In the construction site equipment sector too, 29% of SMEs as opposed to 7% of large companies feel that single market legislation has encouraged them to sell in other markets.⁵⁶ Small companies already operating at international level, in sectors such as machinery, considered that the system of self-certification for affixing CE marking greatly supports SMEs, by helping them to raise the technical standard of their products and compete more effectively against larger companies. Other surveys confirm that since the implementation of the single market 37% of SMEs surveyed claimed to have significantly improved their European distribution and marketing, 27% claimed to have improved products or production processes and a further 12% had taken on staff with new skills to adjust to the European market needs.⁵⁷ Also, in relation to VAT procedures for intra-EU sales, 32% of SMEs considered that the new system has had a positive impact in their activity as opposed to only 30% of large companies.

Conclusions

At first sight, the impact of the single market on SMEs reveals a mixed picture. However, on closer examination it may not be quite so ambivalent. Although it is true that larger companies have benefited the most from the new opportunities opened by the single market, this is due to the fact that smaller companies are less involved in cross-border operations, since they have oriented themselves towards their traditional local and regional markets. This may also explain why small and medium-sized companies are less aware of changes in legislation which occurred after the implementation of the single market, and are less motivated to exploit its benefits.

However, SMEs operating internationally prior to the implementation to the single market, such as those located in cross-border regions, feel that single market measures have improved their performance by encouraging them to raise quality or adapt themselves to stronger competition, or by reducing paperwork and delays in custom procedures. The most striking problem faced by SMEs is the one-off costs of compliance with new single market legislation. An important number of SMEs has also felt that the single market has brought new incentives to get involved in cross-border operations.

Among the measures that SMEs consider would help them to take advantage of the new opportunities afforded by the single market are the following:

- (i) improvement of mechanisms for consulting SMEs prior to implementing new single market initiatives in order to take better account of implementation costs. Efforts in this direction have already been made at Community and national level, so far with limited impact due to the difficulty of the task as recognized in a recent report evaluating the Commission's SMEs policy;⁵⁸
- (ii) improvement of collective R&D programmes for SMEs (such as CRAFT) and simpler access to these programmes: today, participation in these projects can even translate into greater costs (packaging machinery). However, some industrial sectors assessed the impact of these initiatives as having been very useful and beneficial for SMEs (this is the case for mechanical engineering sectors such as pumps and woodworking machinery);
- (iii) reduction of financial burdens related to cross-border operations such as costs of international banking transactions;
- (iv) reduction of regulatory constraints.

⁵⁶ Atkins, *Impact and effectiveness of the internal market programme in the construction site equipment sector*, May 1996.

⁵⁷ *EU initiatives for SMEs — are the policies appropriate?* Deloitte Touche Tohmatsu International, 1995.

⁵⁸ See *Evaluation of the second multiannual programme for SMEs (1993-96)* by Arthur Andersen.

5.4. Environmental policy

Environmental policy cannot be dissociated from the single market. An integrated approach of both policies, that would enable a sustainable path of social and economic development, is not only vital for the environment itself but also for the long-term success of the single market. This success depends heavily on the sustainability of the objectives pursued by the abolition of barriers to trade. Moreover, effective environmental protection, which goes beyond national borders, can only be achieved in the framework of a properly functioning single market and harmonized environmental rules.

5.4.1. The impact of the single market on the environment

Prior to the implementation of the single market, expectations about the potential environmental impact of the single market were quite pessimistic. Increased movements of nuclear and hazardous waste in a Europe without borders, increased road-haulage and air transport as well as environmental degradation due to economic growth are just a few examples of the anticipated strains on the environment.⁵⁹ It is still too early to make a definitive assessment and to quantify the environmental — static or dynamic — impact of the single market in order to validate or disqualify those estimations.

Actually, the studies carried out for this exercise do shed some light on the extent to which the single market has affected the environment. In most cases, as for sectors such as transport,⁶⁰ chemicals⁶¹ or energy,⁶² existing research focuses on the expected impact of fully implementing single market legislation that might result in environmental benefits for the future.

When asked whether the single market had influenced their environmental policies, 26% of companies from the chemical sector said that the SMP had a very significant impact and 35% companies said it was significant.

The main environmental effect of the completion of the single energy market is likely to be the increased use of gas, which should reduce CO₂ emissions as opposed to more polluting fuels. This reduction of CO₂ emissions is estimated at 105 million tonnes per annum. Decreased capacity requirements should also lead to a reduction of local environmental disruption.

As regards transport, it is difficult to assess the contribution which the single market has made to traffic growth in the first half of this decade. However, growth in road freight transport in EUR 15 was around 15% between 1990 and 1994, and average annual growth rates in road freight traffic were slightly higher between 1990 and 1994 than during the 1980s. The environmental concern associated with those trends, in the absence of major improvements in vehicle fuel economy, is the increase in CO₂ emissions which makes it difficult for the Community to achieve its CO₂ stabilization and reduction objectives. In addition, increasing traffic puts additional pressures on the environment in transit regions (e.g. the Alps). At the same time, technological improvements made to motor vehicles under Community legislation, for example in harmonized technical specifications introducing stricter emission standards, will at least in the near future lead to reductions in air polluting emissions from road transport. Early estimations foresee considerable emission reductions in the field of regional transport of goods where between 1986 and 2010 emissions of CO₂ and hydrocarbons would decrease by 47% and 38% respectively.⁶³ It is also hoped that the liberalization policy pursued by the Community within the single market framework for railways will, in the longer term, strengthen the competitive position of this environmentally more benign form of transport. For example, the total share of combined barge-road transport grew from 1.2% (9 million tonnes) in 1985 to 2.0% in 1990 (19 million tonnes). These numbers are still low but reflect the still existing barriers to developing combined transport.

⁵⁹ 1992, *The Environmental Dimension*, Task Force report on the environment and the internal market, 1990.

⁶⁰ NEA, *The internal market impact on road freight transport*, August 1996.

⁶¹ KPMG, *Single market review 1996 — Chemicals*, August 1996.

⁶² London Economics, *Effects of completing the single energy market*, August 1996.

⁶³ NEA, *The transport of goods by road and its environment in the Europe of tomorrow*, Rijswijk 1992.

5.4.2. Environmental policy and the single market

There is widespread recognition among business of the need for environmental legislation. For some sectors, such as natural gas, mechanical engineering or packaging products, environmental requirements have been an incentive to R&D in new environmental-friendly technologies, more environmental machinery or cleaner production processes. The compatibility between environmental legislation and a competitive industry is highlighted by the fact that the highest benefits from compliance with environmental requirements are reaped by firms that adopt a pro-active attitude and integrate environmental concerns into their overall business policy.

However, fears remain, especially among businessmen, about the way environmental protection measures are implemented. Non-harmonized legislation or different environmental protection systems for each Member State are perceived to affect businesses' economic performance or to reduce the benefits they draw from a single market. Therefore, the choice of environmental measure will have to be done on a case by case basis, taking into account the environmental considerations at hand as well as the repercussions for the single market.

Yet, fears that environmental legislation would lead to new market fragmentation by indiscriminate use of Article 100A paragraph 4, which allows an 'opt-out' clause to Member States, have not been confirmed. First, because the Community has been able to take into account environmental objectives, and therefore, increase environmental protection according to the objectives of Article 100A, and second because the application of Article 100A paragraph 4 has been very limited and the few cases concerned have not had any major effects on trade and functioning of the single market. For example, Member States have used this article only eight times to apply national provisions for the production of three chemical products.⁶⁴ However, it concerns only one Directive and products of relative little commercial importance confined to four Member States (Netherlands, Denmark, Germany and Sweden).

The successful integration of Community environmental and single market policies is revealed by the perception within industry that in some specific sectors, such as chemicals, Community environmental legislation has made significant progress towards establishing a level playing field. Over 70% of surveyed chemical companies found that EC environmental legislation has had a positive or neutral effect on overcoming barriers and obstacles to trade.⁶⁵ It has to be noted though, that 28% of the companies still consider that the introduction or the maintenance of national measures which are stricter than those adopted by the Community was leading to losses of competitiveness versus the rest of the EC Member States (e.g. Germany and the Netherlands).

In relation to compatibility between environmental legislation and the proper functioning of the single market, the following have been identified as the most important concerns for businesses.

- (i) Short-term costs associated with compliance with environmental regulations: some industries are concerned with the perceived short-run increase in their production costs due to compliance with environmental legislation.
- (ii) Analysis of the costs and benefits of environmental regulation: this is a mutual concern for both businesses and Community legislators, in order to make sure that environmental regulations are cost-effective. It is a principle recognized in the Treaty that has been applied to the Commission's assessment of Community policy.⁶⁶
- (iii) Degree of harmonization of environmental regulations: the establishment of common environmental standards and the avoidance as far as possible of differences between Member States' legislation is regarded by industry as essential to avoid distortions in competition. An example of problem areas is the national regulation of emissions and hazards which, though partially regulated at EU level (for example, use of titanium), is mostly covered by national legislation (emissions of solvents).

⁶⁴ Directive 76/769/EEC on PCP, creosote and cadmium.

⁶⁵ KPMG, *Single market review 1996 — Chemicals*, August 1996.

⁶⁶ See Declaration No 20 of the Treaty on European Union.

⁶⁷ Regulation (EEC) No 880/92, 23.3.1992, OJ L 99, 11.4.1992.

Community environmental legislation insufficiently enforced or inadequately implemented in some Member States has also resulted in different requirements for producers at national and EU level. Some industry sectors have reported that although the Community eco-labelling scheme has been in force since 1993,⁶⁷ and common sets of criteria for the award of the label have been established for a number of products, few applications for use of the label have been made. At least, for the time being, national schemes are very well established and have been regarded as imposing *de facto* standards for entry to certain markets.⁶⁸ Another example of incomplete implementation of the Community's legislation would be the waste management regulations.⁶⁹

- (iv) Waste trade: The EU Regulation on the shipment of waste, providing *inter alia* common rules for the application of the Basel Convention on the control of transboundary movements of hazardous wastes and their disposal, endeavours to strike a balance between trade interests and environmental concerns. According to industry, however, it imposes certain unnecessary restraints on the waste trade. For example, in some cases industry considers that the definition and classification of waste as stated in this Regulation is too wide. Thus, the trade with recycl-

able non-ferrous metals or ferro-alloys is submitted to supervision and control. In addition, industry has expressed its concern that restrictions in scrap trade, extensively used as a raw material in steel production, have increased costs considerably.

5.5. Single market and consumers

European consumers, as well as businesses, were meant to benefit from the advantages of greater competition, a wider variety of products and services, new channels of delivery and lower prices. Greater product differentiation, which, in some cases, also reflects businesses' reactions to increased competition and better information about products and services, emerges as having been generally beneficial to consumers.

The SMP has offered retailers, and in some cases consumers, improved access to the best products at lower prices. There is some evidence of a switch to EU sourcing, particularly in products such as electrical household appliances, food and furniture. However, entrenched consumer preferences as well as a preference for retailers to purchase from local small-scale suppliers still predominate in other sectors.

Box 8 Telecommunication equipment and services

Equipment prices were estimated 7% lower than would have been the case without the SMP, equivalent to total benefits for consumers of between ECU 1.5 and 2 billion per annum. As far as tariff adjustments by telecom operators are concerned, the Commission has actively promoted a rebalancing of tariffs, so that they are oriented towards costs. This has led to considerable reductions in regional, long distance and international call prices. For example, there has been an average reduction of 42% for phone calls towards the US between 1990 and 1995. This has been accompanied by some increases in real terms of the prices of local calls during business hours, and in installation and line rental charges to reduce the loss made on the provision of the connection and local call service. This is generally being accompanied by the introduction of special and flexible tariff schemes for business and residential users.

Air transport

The impact of growing competition was observed in lower economy fares, with deeper discounts and special offers pitched below the lowest available published fare. By contrast, fully flexible and club class fares have increased. This mainly indicates that airlines have pursued strategies of price discrimination: competition has been vigorous for leisure passengers, while competition for full fare passengers has been more through the level of service and product innovation, rather than price. Significant variations still exist on a directional basis, and between intra-EU and domestic fares. However, there is substantial evidence to suggest that users appear to have benefited from the strategic responses of incumbent carriers and from market entry which have resulted in greater variety and choice.

⁶⁷ KPMG, *Single market review 1996 — Chemicals*, August 1996.

⁶⁸ EC provisions of waste (Directive 91/156/EEC) and the shipment of waste (Regulation (EEC) No 259/93).

5.5.1. The SMP impact on prices for final consumers

There is no strong evidence that the SMP has triggered price reductions for the benefit of final consumers. Evidence in important manufacturing sectors like food-stuff and textiles is inconclusive; however, in some services sectors such as air transport and telecommunications, price reductions have been experienced, although it is doubtful that liberalization is the only factor behind them.

Progress towards uniform or lower prices in the EU has been inhibited by different factors.

(i) Currency fluctuations, as they prevailed over the last four years, had an impact on pricing strategy for some sectors in some countries. This is particularly the case of the motor vehicles industry where large manufacturers have revised their pricing policy to avoid consumers benefiting from currency fluctuations and to preserve the margins of dealers near the border with a devaluing country.

(ii) The persistence of some forms of price controls, often linked to differences in national per capita income, have also impeded price convergence. In the pharmaceuticals industry, and despite the Transparency Directive, which only had modest effects, the single market did not lead to significant price convergence, as Member States wanted to keep control of public expenditures for medicines subject to reimbursement.

(iii) Consumer preference for national, regional or local products also prevented improved market access opportunities from delivering its full effects through lower prices. This was particularly the case in the foodstuffs industry, where branded products were the only ones to benefit from improved market access (with the consequence of price increases in some cases). High transport costs relative to products' unit values also restricted product tradeability over long distances.

Box 9 Examples of quality enhancement

In the automobile sector, increased consistency in type approval measures across all Member States brought about a small but positive benefit in terms of reduced costs and prices and a much greater choice of models and variants within each Member State. The SMP also forced car manufacturers to create pan-European sales and distribution systems under which consumers can be more readily assured of consistent sales and service support wherever they may be located in the EU.

Consumers may also gain from increased choice of pharmaceutical products, especially in the self-medication field. They should also have benefited in the prescription area in that they have more rapid access to new medicines, thanks to the reduction in admission procedures.

In the processed foodstuffs sector, the SMP has also resulted in greater ranges of products being made more quickly available to consumers thanks to more sophisticated delivery systems. Moreover, the increase in competition has also encouraged the development of high quality own-label products at competitive prices which contributed to further reduction in retail price spreads and greater choice for the consumer.

Greater competition on the markets for residential telecommunication equipment has contributed to a significant improvement in the range of products available and the range of retail outlets through which they can be purchased or leased. The single market's valuable contribution to the success of GSM standards has also benefited consumers, from both a qualitative and price point of view. The almost universal deployment of the GSM system in Europe has made high functionality mobile services widely available to business users and the success of the system is now leading to affordable services for consumers. The growth of GSM usage has also contributed to the falling cost of analogue mobile telephony, which is now affordable for a large segment of the consumer market. The quality and level of telecommunication services have shown a steady and significant improvement in the last five years. The digitization of the telephone networks combined with improved signalling means that a range of supplementary services is now being offered on the basic telephone (touch-tone dialling, call waiting, call forwarding, calling line identification and call barring) as well as soft-disconnection schemes which reduce cut-off pressure for users.

Liberalization in the audiovisual sector, in particular the TV Without Frontiers Directive, had a significant impact on the range of products and channels available to European consumers. It facilitated the entry of a number of pan-European channels by easing licensing procedures. It also had some, although limited, impact on the expansion of terrestrial broadcasters and enabled a small number of broadcasters to transmit programmes primarily targeted at one Member State from outside that Member State.

In financial services, the most common strategic response to increased competition was the introduction of new products and services and diversification of the products range into areas such as insurance and investment management, sometimes through alliances and acquisitions of other financial organizations. Banks and other financial organizations have also become far more aggressive in developing, designing and promoting a wide array of savings and loan products with different income/capital appreciation/risk trade-off characteristics. This trend was observed in a number of EU countries and, as a consequence, there has been some emerging convergence in consumer tastes across the EU. Pensions and insurances have grown as a share of personal sector financial assets in a number of countries. One of the negative aspects attached to that new range of products on offer is their lack of transparency and the concomitant need to increase consumers' understanding of what services or benefits the products provide and the relevant risk/reward characteristics (see below).

In air transport, passengers clearly benefited from access to a larger number of destinations by scheduled non-stop flights, thanks to more flights between regional cities, and a change of destination to the schedules of a number of charters. Quality improvement and greater flexibility have also compensated for the absence of any significant price-effect in the case of fully-flexible and business class fares.

5.5.2. Product diversification — Better quality

While the SMP impact on prices is rather inconclusive, consumers benefited from improved access to a wider range of products, both in consumer goods and services.

These benefits of increased product diversity and keener price or quality competition have been achieved without compromising the safety and welfare of consumers. At the outset, it was feared that the opening of markets would expose consumers to additional risks, particularly as regards products imported under mutual recognition as a result of variations in the stringency of standards and their enforcement in the different Member States. To counter this threat, the SMP has been complemented by increased convergence of conformity assessment systems, tougher penalties against producers placing defective products on the market and early-warning and rapid withdrawal systems to allow speedy detection and suppression of unsafe products. The SMP has not placed the interests of free circulation before those of consumers. This is, for example, the case in the processed foodstuff sector where the single market and consumer protection objectives have become inextricably linked. Experience has shown that the Council and the Parliament will only accept proposals if they are satisfied that an appropriate level of protection is maintained. Moreover, the very existence of the possibility of Member States maintaining stricter legislation provided for by Article 100(a)4 and the existence in all public health legislation of safeguard clauses which allow Member States to take unilateral action to counter serious risks to public health, mean

that the choice of a high level of protection is essential if the single market is to function properly.

5.5.3. Consumer policy

The Treaty clearly requires the European Union to deal with a broad range of consumer issues, some of which relate to the SMP. Discharging this obligation involves careful consideration of the subsidiarity principle. Since the early 1990s, consumer policy has aimed to support the successful completion of the single market. Industry generally welcomed the basic aim of EU regulations; but inadequate transposition and stringent requirements by Member States were seen by European companies as clear attempts to fragment the market and protect national producers from foreign competition (particularly in the case of product liability and labelling provisions).

In the field of financial services, as mentioned above, the creation of the single market has provided for increased competition, choice and innovation which benefit consumers. However, it is also generally agreed that, since so much is at stake (mortgage, life insurance facilities, savings, etc.), a high level of consumer protection is necessary to allow consumers to shop around in the different Member States for the cheapest deals.

Consumers are faced with more and more diversified and complex financial services offered by financial institutions and often lack knowledge about the main characteristics of these services. They also sometimes find it difficult to get independent advice.

³⁰ COM(96) 209 final.

Box 10 Problems encountered by consumers in financial services

- One aspect of major concern from the consumer point of view refers to cross-border payment systems. The main problems reported by consumers concern the lack of full written information on conditions, double charging, excessive execution time and lack of adequate redress procedures. As regards payment cards, researches and studies have showed that in most Member States, the 1988 Commission Recommendation on payment systems is not fully implemented. Various other aspects of payment cards (condition of use, prices) also need to be taken into account. Consumer groups request that an assessment of the need for and contents of a global initiative in this domain be undertaken, with a view to giving full effect to the single market.
- Significant barriers still exist in the field of mortgage credit where consumers have little choice and are not able to take full advantage of the single market in buying mortgage credit. Although it is theoretically possible, it rarely happens. Consumers are faced with many disincentives, such as domestic tax regimes and interest rates. Consumers' organizations claim that a significant gap in the single market is effective EU legislation on mortgage credit and provisions for cross-border debt recovery. It emerged however that, in areas relating to housing mortgages, access to capital markets, differences in the treatment of withholding tax and varying subsidy arrangements are the main obstacles which continue to hinder the creation of a true single market.
- In the insurance sector, the various Directives aimed to increase transparency in insurance contracts and to help consumers to understand insurance contracts. However, despite the fact that the third life insurance Directive removed all restrictions on advertising, consumers apparently are not making much use of the possibility of purchasing insurance services across frontiers. In most cases, this results from national provisions applied by Member States to prevent the proper functioning of the single market more than from financial techniques inherent in insurance activities. In particular, fears over how to handle legal disputes deter consumers from buying foreign policies and lead them to seek efficient, rapid and independent redress mechanisms for handling complaints. Consumer organizations also claim that further legislation is necessary, in particular to set common minimum requirements in the field of insurance contracts, introduce common rules on information to be provided to consumers and clearly define compulsory insurance.

The Commission has therefore recently adopted a Green Paper on 'Financial services: meeting consumers' expectations',⁷⁰ which discusses the problems still facing consumers and the particular protection which individual consumers should enjoy in regard to financial services.

Advertising is also an area of particular significance for consumers. The misleading advertising Directive which is aimed at protecting consumers in a similar way throughout the EU against misleading advertising and at removing barriers to advertising across EU borders, is based on a minimal harmonization level and a generic definition of 'misleading'. Its implementation has not led to any significant changes because of too great flexibility and has had no significant impact on the costs of pan-European campaigns. In July 1991, the Commission published a proposal for a Directive on comparative advertising, under the form of an amendment to the 1984 Directive. This aimed to improve consumer information, increase competition and ensure a coherent legal framework throughout the EU, the lack of which is still recognized by consumers and industry as an important obstacle to the development of cross-border advertising.⁷¹

Despite the progress made towards greater consistency between single market and consumer protection objectives, the food sector experienced many problems in labelling as Member States continued to impose provisions over and above Directive requirements. Excessive labelling requirements not only increase the costs of marketing products, but can also lead to ineffective warnings for consumers. Moreover, it is not clear that all information provided on food labels is really helpful to consumers. Some of this is unusable by consumers because of its complexity and there are indications that other key information needs are not met at all. For the minority of consumers for whom food selection is critical because of health reasons, complex information may be helpful because their medical advisors at least can comprehend such information.

The time may be approaching when it will be possible to review and simplify this legislation so that the benefits of the single market together with the need for improved consumer protection can be maximized.

⁷¹ Study on the effectiveness and impact of internal market integration on the organization and performance of the advertising services sector, Università Commerciale Luigi Bocconi.

Access to justice and guarantees also represents an important element of the single market from a consumer point of view. It is important for consumers to have confidence in cross-border shopping. According to consumer organizations, conditions for access to justice in cross-border situations should therefore be improved. However, consumer litigation is typically in respect of low amounts; this makes the prospect of cross-border litigation very unattractive. Moreover, national legal systems reflect national needs and tradition and are not designed solely for consumers' disputes. The Commission therefore recently proposed a Directive on the coordination of the laws, regulations and administrative provisions of Member States relating to injunctions for the protection of consumers' interests and a communication setting up an action plan for consumer access to justice and the settlement of consumer disputes in the single market.

Finally, a major area where progress is needed concerns the information and education of consumers about the single market opportunities. Unless consumers are sufficiently aware of the changes in market conditions further to the development of the single market, they will be disadvantaged. However, information supply will not suffice. Unless serious efforts are made through targeted consumer education, to develop understanding of a wide range of subjects, many consumers will not be able to navigate with confidence through markets. This is one of the objectives behind the launch of the major information campaign called 'Citizens First', which will embrace several topics, including financial services, travel and cross-border purchase of goods and services especially targeting citizen consumers.

5.6. Implications for third countries: the external dimension

The launch of the SMP initially provoked some apprehension on the part of the EU's trading partners. Some third country observers were concerned that liberalization of intra-EU trading conditions would be accompanied by tighter restrictions on third country trade. In fact, the SMP has not entailed any heightening of trade barriers with the rest of the world — on the contrary, almost all changes in conditions of access for third countries have amounted to unequivocal reductions in the level of

absolute trade barriers to the Community market. The SMP has made it easier for third countries to do business in the Community.

5.6.1. Single market makes it easier for third countries to do business in EU

SMP benefits are also reaped by third country operators. They and EU operators benefit from measures aimed at eliminating obstacles to intra-Community trade. Three examples illustrate some of the benefits for third country manufacturers.

- Abolition of customs and fiscal frontier formalities facilitates the circulation of third country products in the same way as products of EU-origin. In fact, third country operators may have reacted more quickly than domestic companies, by adapting their distribution networks (for example, US and Japanese companies make greater use of Euro-Distribution Centres) as compared to EU companies which have displayed some inertia in overhauling distribution systems.
- Abolition of technical trade barriers to intra-Community trade facilitates the intra-EU marketing of non-EU products. Henceforth, third country producers need only comply with a single set of specifications and conformance testing. The fear that EU technical specifications would be sufficiently stringent to deter third country imports fundamentally misunderstood EU regulatory processes and the consensus-based nature of EU harmonization, which precludes extreme solutions. The bulk of European Standards ensuring compliance with 'new approach' Directives are largely identical to internationally agreed standards (ISO, IEC). Over 90% of European electro-technical Standards derive directly from international standardization. Wherever the 'mutual recognition' principle applies, there is no technical harmonization in the first place. To date, there have been no substantiated cases of product regulation being used for protectionist purposes. Given the trade-facilitating impact of internal EU action, third country producers express frustration similar to that voiced by EU firms about the slow removal of some technical barriers. The EU has been willing to build on these benefits through bilateral mutual recognition agreements to alleviate costs associated with

obtaining conformity assessments from EU-notified bodies. This step further enhances the market-opening effects of EU efforts to overcome technical barriers. As of July 1996 mutual recognition agreements between the Community and Australia and New Zealand have been initialled. Negotiations were opened with the US, Canada, Switzerland and Japan. The scope for these agreements is conditional on conformity assessment bodies in the trading partner complying with certain technical and scientific criteria.

- Third country operators established in the EU benefit without distinction from SMP cross-border provision of services and action to develop a business framework consistent with a single market (e.g. industrial property measures, company law, and corporate taxation). With the enlargement of the Community to 15 Member States, the advantages of the SMP are accentuated. Market opportunities for trading partners of third countries have been expanded, given that subsidiaries of third country parent companies are treated as Community companies once the subsidiary is established under the laws of one Member State. Building on this liberal stance towards establishment-based trade, the Community and Member States have made a substantial contribution to the Uruguay Round negotiations on trade in services, as demonstrated in the level of binding to which the Community has pledged itself in the schedule of specific commitments. Community trade policy aims to obtain comparable market access commitments from trading partners.

5.6.2. SMP resulted in completion of a liberal common commercial policy

The EU fully subscribes to multilateral trading arrangements governing most of its international trade. These impose constraints on how much the EU can operate a restrictive common commercial policy or target certain trading partners with selective actions. Furthermore, the single market required completion of the common commercial policy, such as anomalies like outstanding national quotas in textiles and clothing, consumer elec-

tronics, and footwear. Under the provisions of GATT/WTO agreements, any common solution could not impose tighter restrictions on trade than the combination of pre-existing national arrangements.

The need to replace remaining national quotas with common EU measures stemmed from the abolition of customs controls at intra-EU frontiers meaning that autonomous national restrictions could be circumvented by trade deflection. In 1991, 7 629 national quotas governed imports from non-State trading countries and another 4 800 applied to imports from State-trading countries.⁷² Member States' capacity to enforce these restrictions relied on preventing indirect imports via other Member States. Article 115 authorized restrictions and intra-Community trade surveillance to curb any trade deflection. The system relied on extensive documentation controls on all intra-EU shipments and was at odds with a single market. The abolition of customs formalities removed the infrastructure for enforcement of Article 115 restrictions and surveillance measures. As a result, the number of restrictions and surveillance measures fell from 1 500 in 1988 to zero by July 1993.

The only cases in which 'communitized' quotas replaced a web of pre-existing national restrictions involve textiles and clothing products (for the transitional period until the phasing out of MFA) and selected measures on certain imports from a single State-trading country. While EU Regulations governing the import regime allow regional application of safeguard measures, this has only been invoked twice. The SMP and completion of the common commercial policy have benefited third country products previously targeted by national restrictions, including textiles and clothing, footwear, transport equipment, agricultural products and sundry manufactured items (e.g. sewing machines, car radios, televisions). Imports from State-trading countries, as well as restricted imports from some market economies such as Japan and South-East Asia, were previously the most frequently targeted by national restrictions. Producers in these countries have therefore benefited most from liberalization dependent on completion of the single market.

In services, the division of responsibility between Member States and the Commission for international

⁷² The products most frequently affected included cotton, articles of clothing and accessories (knitted and non-knitted), man-made staple fibres, electrical machinery and equipment, man-made filaments, transport equipment (excluding rail rolling stock), wool and animal hair, and coffee, tea and spices (under the International Coffee Agreement quotas).

representation and negotiation has been less clear. However, single market completion means that policy negotiation between individual Member States and selected trade partners is no longer in the collective interest. 'Go-it-alone' policies offer third countries the possibility of securing a gateway to the entire single market while offering reciprocal access to only one Member State. Single market completion has therefore increased awareness of the need for a common Community negotiating stance in international and bilateral trading agreements (see GATS and recent granting of mandates to the Commission to negotiate 'open sky' agreements with US and CEECs).

In conclusion, the single market has spurred the EU to remove remaining problems in the common commercial policy. Previously restricted third country suppliers have benefited most from these adjustments. Improved third country producer access as a result of the SMP has been amplified through adoption of the Uruguay Round. Following adoption of this package, average duty rates for non-agricultural imports will decrease from 5.7 to 3.6%. In addition, the Community subscribed to the complete elimination of duties (zero for zero) in the sectors of construction, medical equipment, furniture, steel, agricultural equipment, paper, beer and spirits. Following these concessions, 40% of all Community imports will be free of duty.

5.6.3. Single market provisions relating to third country treatment

In international trade areas governed by multilateral disciplines, the EU is required to apply the Most-Favoured-Nation and 'national treatment' principles to third country operators. Member States may not therefore impose additional or discriminatory provisions on them. The principle of 'national treatment' has also been extended to third countries through a series of bilateral agreements. However, in a limited number of fields, international trading rules have yet to be agreed on a multilateral basis. In a handful of cases, single market legislation contains provisions which offer Member States the option of taking restrictive action against trading partners who do not offer 'reciprocal treatment'. Four provisions have been at the forefront of discussion:

- A 'reciprocal treatment' clause in EU financial services legislation foresaw Member States' denial of authorization to subsidiaries or branches of companies from third countries which did not provide national treatment or effective market access to EU financial service operators. This provision does not apply, and as of 1 July 1996, it has been revoked in respect of the other 28 countries which have signed the Marrakech Agreement.
- Article 36 of the Directive liberalizing public procurement purchasing by utility operators in the water, energy, telecommunications and transport sectors: in the absence of rules binding all WTO Members, EU legislation allows contracting entities to reject third country offers and requires rejection where the price advantage is less than 3%. However, this clause is waived where the trading partner in question has subscribed to the WTO Agreement on Government Procurement (EU Member States plus seven and expanding). The single market therefore improved market access conditions as compared to the pre-existing situation where there were no rules prohibiting discriminatory treatment of other EU or non-EU suppliers. Under EU public procurement legislation, contract awards must now take place in accordance with open and transparent procedures and objective criteria. Nationality (EU or non-EU) cannot be a criterion for award of a contract. The only discriminatory element is Article 36 of the utilities Directive which, as seen above, is withdrawn when the EU's counterparts offer reciprocal access to their procurement markets.
- Media: the 'Television Without Frontiers' Directive (89/552) requires that 'wherever practicable' a majority of broadcasting time be reserved for 'European works'.⁷³ This provision has attracted adverse comment from US producers, who consider that their high share of EU television programming would otherwise be even greater.
- The data protection Directive (95/46) will, once it enters into force, require that Member States do not allow flows of personal information towards third countries which do not provide for adequate protection in this field.

⁷³ 'European' includes all works created by persons located in a Member State of the Council of Europe.

The above provisions are an attempt to retain some means of redressing disparities in market access in areas not fully covered by WTO disciplines. The waiver where trading partners agree to a system of rules which provide for a level playing field is an inducement to other countries to follow the EU lead in liberalizing these areas.

5.6.4. Trade data

An examination of trade data gives the lie to fears that the SMP would result in substantial trade diversion away from third country imports. Extra-EU imports increased their share of Community apparent consumption from 12 to 14% over the period 1980-93. Extra-EU imports continue to account for a steady 40% of total (extra- and intra-) Community imports. Detailed simulations have been undertaken to establish the implications of completing the common commercial policy through the 'communitization' of national quotas. Two scenarios were examined: in the first, national quotas are allowed to lapse without being replaced by Community level measures as in the footwear sector: the second case examined involved situations where national quotas are replaced by a Community level quota without any regional/national subdivisions as with the textiles and clothing sector. In the first case, both previously restricted third country producers and consumers in the Member States applying quotas enjoy strong benefits. In many cases, third country producers benefit at the expense of other third country suppliers which had not been targeted by national quotas. In the case of 'communitization' of quotas, previously restricted third country producers benefit. Within the EU, there is a net benefit as savings to consumers outweigh any loss of share experienced by domestic suppliers. The lion's share of the benefits is reaped by consumers in Member States which previously enforced a restrictive regime.

5.6.5. Conclusions

Single market measures have helped non-EU operators to do business in the EU. In this sense the EU is a building-block, and not a stumbling-block, for an open inter-

national trading order. This point is acknowledged in periodic reports on Community trade policy carried out by the WTO, as well as analysis commissioned by the UN and key trading partners.⁷⁴ It is perhaps instructive to quote the former US representative to the EU on this point:

'This [the completion of the single market] is a great boon to companies, European and American, doing business in Europe and is one of the most creative economic innovations of the post WWII world. Importantly, it has been done without creating a Fortress Europe mentality, free on the inside, protectionist on the outside. The EU is far more open to US and foreign business today than a decade ago and more supportive of the multilateral trading system. Today it is virtually as easy to ship products from Germany to Italy, as it is from New York to California — a remarkable achievement of great benefit to Europeans and Americans.'⁷⁵

⁷⁴ The reader is referred to the fifth annual report prepared by the US IRC on the SMP programme (1993) or, more recently, the UNECE study on the implications of the single European market for Asia and the South Pacific (1996).

⁷⁵ Farewell remarks by Ambassador S. E. Eizenstat (US Representative to the EU) Committee of the American Chamber of Commerce, Brussels 8.2.1996.

6. Appendix: The structure of the research

In response to the Council Resolution to report in 1996 on the effectiveness and impact of the SMP, the Commission launched a series of independent research studies to assess its impact on both specific business sectors and across the economy as a whole. To ensure the independence and objectivity of the work, the background research was carried out by contracted parties, operating only subject to quality control by Commission services. In addition, a panel of independent academic experts was appointed to ensure that sound methods of analysis were employed. The structure of the study programme is outlined below.

The research programme was designed to elicit information on what in fact had happened in the market place as a result of the implementation of the SMP rather than to validate previous research into the effects of the single market. It should therefore not be seen as a 'Cecchini Mark 2' report.

The research consists of 38 studies, accompanied by a wide-ranging business survey.

To measure the effectiveness of the SMP a common methodological approach was established. A 'bottom-up' approach was followed to assess the difference that the single market legislation has made to specific chosen economic sectors covering both manufacturing and service industries. This was complemented by a cross-sectoral analysis at the macro level in order to measure the single market impact on trade, investment, competition, and aggregate and regional levels and to assess the effectiveness of the dismantling of barriers to the free movement of capital, goods and services.

Half of these 38 studies are sectoral while the rest adopt a 'horizontal' approach to the measurement of the impact of the single market. It would have been impossible to carry out individual studies on all sectors of the economy and choices had to be made on the basis of the economic significance of the sector and relevance to the operation of the single market. The combination of examination at both the sectoral and horizontal level should mean that no aspect of the single market impact has been overlooked.

From the information gathered at the micro and macro levels, a picture emerges of how the SMP has translated into broader effects in the Community and national economies, shedding light on the mechanisms through which SMP effects have permeated economic activity. The research does not simply focus on the consequences of liberalization and harmonization measures, but inevitably throws the spotlight onto other Community and national policies which influence the business dynamics and adjustment mechanisms liberalized by the single market. Foremost amongst these policies are monetary integration, the regional impact of the single market, competitiveness and employment, competition, the environment and the promotion of consumer interests.

However, the results derived from the research undertaken in the framework of this exercise need to be qualified. Measuring what in effect is the impact of the legislative programme on the basis of economic criteria is not as straightforward as it might appear. Assumptions had to be made regarding:

- what the economy would really look like in the absence of the single market in order to draw meaningful comparisons;
- how the late transposition or implementation of single market measures may have affected the response economic operators;
- how the interaction of the SMP with other factors that have influenced the economy in the same period may have amplified or dampened the single market effect.

The research amounts to the first extensive *ex post* analysis of what has been happening to the European economy as a result of the SMP. In terms of economic impact the conclusion is positive and encouraging. The Community needs to build on its success and iron out the remaining practical difficulties that inhibit the full potential of the single market from being exploited. The debate that will ensue from this research programme and the accompanying Commission report are timely and should inform the debate about priorities for the future development of the single market.

The research was funded by the European Commission under the direction of Mario Monti with the following Steering Committee:

Directorate-General XV — Internal Market and Financial Services

John Mogg, Thierry Stoll, John Farnell, Alexandros Spachis

Directorate-General II — Economic and Financial Affairs

Giovanni Ravasio, Jan Schmidt, Pierre Buigues

Directorate-General III — Industry

Stefano Micossi, Michel Ayrat, Peter Smith

The project coordinators were Alexandros Spachis and Pierre Buigues.

The project team comprised, Niall Bohan, Ana Gallo, Byron Kabarakis, Jean-Yves Muylle, Patrick Roe, Lorna Windmill, Maria Jesus Ruiz, Liana Cafolla and Jill Hughes from Directorate-General 'Internal Market and Financial Services'.

The studies were conducted by independent consultants and evaluated by Commission staff and the members of an independent 'Academic Panel' comprising the following professors:

PROF. E. BERGLÖF	ECARE Université libre de Bruxelles
PROF. G. BERTOLA	Università di Torino, Istituto di Economia politica
PROF. F. BOURGUIGNON	DELTA/ENS, Paris
PROF. D. GROS	CEPS, Brussels
PROF. P. HOLMES	School of European Studies, University of Sussex

PROF. G. KLEPPER	Institut für Weltwirtschaft, Kiel
PROF. D. LUCENA	Faculdade de Economia, Universidade Nova de Lisboa
PROF. F. MALERBA	Università Luigi Bocconi, Milano
PROF. P. MESSERLIN	Institut d'Études Politiques, Paris
PROF. D. NEVEN	Université de Lausanne
PROF. E. O'MALLEY	ESRI, The Economic and Social Research Institute, Dublin
PROF. P. SEABRIGHT	Churchill College, University of Cambridge
PROF. N. THYGESEN	University of Copenhagen
PROF. L. TSOUKALIS	University of Athens and Collège d'Europe Bruges
PROF. VAN WIJNBERGEN	University of Amsterdam
PROF. J. VIÑALS	Servicio de Estudios, Banco de España, Madrid
PROF. A. WÖRGÖTTER	Institut für Höhere Studien, Wien

The 38 background studies and the business survey will be published by the Office for Official Publications of the European Communities. The list of studies, the consultants involved and the members of the evaluation committees are given below.

Study Subseries 1 — Impact on manufacturing	Consultant	Evaluation Committee
Food, drink and tobacco processing machinery	DRI/Mc Graw Hill	C. Martinez, DG II/B.3 N. Bohan, DG XV/A.1 J. Hatwell, DG III/D.1 P. Ayalla DG III/D.1
Pharmaceutical products	REMIT	B. Kabarakis, DG XV/A.1 J. Sheehy, DG II/B.3 J. Winawer, DG III/E.3 H. Sundblad, DG III/D.1 M. Franca, DG XXIV.2
Textiles and clothing	CEGOS	J. Sheehy, DG II/B.3 N. Bohan, DG XV/A.1 C. Livas DG III/E.4 M. Franca DG XXIV.2
Construction site equipment	WS Atkins	A. B. Gallo Alvarez DG XV/A.1 J. Sheehy DG II/B.3 G. Mattino DG III/D.1 J. Hatwell DG III/D.1
Chemicals	KPMG	B. Kabarakis DG XV/A.1 C. Martinez DG II/B.3 P. Glynn DG III/C.4 A-L. Sundquist DG III/C.4 O. Lluansi DG XI/E.2 J. Madeira DG XI/B.1
Motor vehicles	ERNST & YOUNG	A. B. Gallo Alvarez DG XV/A.1 C. Martinez DG II/B.3 C. Kendall DG III/E.5 M. Franca DG XXIV.2 H. Arp XI/D.3
Processed foodstuffs	BER	C. Martinez DG II/B.3 A. B. Gallo Alvarez DG XV/A.1 D. Seite DG III/E.1 R. Hankin DG III/E.1 A. Anzalone DG III/E.2 M. Franca DG XXIV.2
Telecommunications equipment	Analysys	J. Gual DG II/B B. Kabarakis DG XV/A.1 P. Johnston DG XIII/B.1 A. Jaime DG XIII/A.2 M. Franca DG XXIV.2

Study Subseries 2 — Impact on services	Consultant	Evaluation Committee
Insurance	CEGOS	L. Windmill DG XV/A.1 P. Roe DG XV/A.1 C. Ohly DG II/B.1 S. Skovmand DG XV/C.2 J. Allix DG XXIV
Air transport	Cranfield University	B. Kabarakis DG XV/A.1 J. Sheehy DG II/B.3 A. Colucci DG VII/C.1 C. Berrozpe Garcia DG VII/C.2 A. Calvia DG III/A.3
Credit institutions and banking	Economic Research Europe Ltd	L. Windmill DG XV/A.1 P. Roe DG XV/A.1 J. Gual DG II/B M. Becht DG III/A P. Clarotti DG XV/C.1 L.G. Collados DG XV/C.1 U. Bader DG XV/C.1 J. Allix DG XXIV
Distribution	Coopers & Lybrand	N. Bohan DG XV/A.1 C. Martinez DG II/B.3 R. Ratchford DG XXIII/A.2 A. Filopoulos DG XXIII/A.2
Road freight transport	NEA	B. Kabarakis DG XV/A.1 C. Martinez DG II/B.3 K. Crawford DG VII/B.1 A. Rainaldi DG VII/B.1 A. Calvia DG III/A.3 H. Arp DG XI/D.3
Telecommunications liberalized services	Bossard	J. Gual DG II/B B. Kabarakis DG XV/A.1 J-L. Ferrero DG XIII.A A. Calvia DG III/A.3
Advertising services	University Bocconi	B. Kabarakis DG XV/A.1 J. Sheehy DG II/B.3 J. Bergevin DG XV/E.5 M. Paemen DG XV/E.5
Audiovisual services and production	KPMG	B. Kabarakis DG XV/A.1 A. Kosmopoulos DG X/D.3 J. Sheehy DG II/B.3 J. Bergevin DG XV/E.5

Study Subseries 2 — Impact on services	Consultant	Evaluation Committee
Single information market	Analysys Ltd	B. Kabarakis DG XV/A.1 J. Sheehy DG II/B.3 A. Calvia DG III/A.3 H. MacDermot DG V/B.5 S. Conti DG XIII/A.3
Single energy market	London Economics	J-Y. Muylle DG XV/A.1 J. Sheehy DG II/B.3 N. Doherty DG XVII/A.3 M. Benville DG XVII/A.2 I. Gowans DG XVII/A.5 A. Calvia DG III/A.3
Transport networks	Trasporti e Territorio, AT Kearney, ME & P	B. Kabarakis DG XV/A.1 J. Sheehy DG II/B.3 A. Baron DG VII/A.3 J. Elias DG VII/E.2
Subseries 3 — Dismantling of barriers		
Technical barriers to trade	WS Atkins Ltd	N. Bohan DG XV/A.1 C. Ohly DG II/B.1 F. Dintilhac DG XV/B.2 S. Lebrun DG III/B.1 M. Da Molo DG III/D.2 D. Hanekuyk DG III/B.1 N. Premoli DG III/B.1
Public procurement	Eurostrategy	J. Sheehy DG II/B.3 N. Bohan DG XV/A.1 D. Redonnet DG XV/B.4 W. O'Brien DG XV/B.3 P. Willingham DG XV/B.4 T. Westphal DG XV/B.4
Customs and fiscal formalities at frontiers	Price Waterhouse	N. Bohan DG XV/A.1 C. Ohly DG II/B.1 J. Carriat DG XXI/C.4 M. Staedtgen DG XXI/C.2 U. Trautmann DG XXI/C.1
Industrial property rights	CJA Ltd	N. Bohan DG XV/A.1 J. Sheehy DG II/B.3 P. Leardini DG XV/E.3 B. Posner DG XV/E S. Lebrun DG III/B.1

Study	Consultant	Evaluation Committee
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Currency management costs	Ifo-Institut	C. Ohly DG II/B.1 L. Windmill DG XV/A.1 P. Roe DG XV/A.1 P. Shanley DG XV/C.4 O. Koumartsioti DG III/A.3
Subseries 4 — Impact on trade and investment		
Foreign direct investment	EAG	J. Sheehy DG II/B.3 A. B. Gallo Alvarez DG XV/A.1 L. Windmill DG XV/A.1 M. Messmer DG III/A.3
Trade patterns inside the single market	CEPII and CIREM	C. Martinez, DG II.B.3 A. B. Gallo Alvarez DG XV/A.1 L. Windmill DG XV/A.1 P. Roe DG XV/A.1 M. Buti DG II/B.1 M. Messmer DG III/A.3 J-F Lebrun DG V/A.2 W. Floyd F.S.U. R. Hall DG XVI/A.4 L. Rassmussen V/F.5
Trade creation and trade diversion	CEPR	N. Bohan DG XV/A.1 W. Noë DG I.1 M. Messmer DG III/A.3 W. Floyd F.S.U. C. Martinez DG II/B.3
External access to European market (Lot 1)	University of Sussex	G. Davila Muro DG II/B.1 N. Bohan DG XV/A.1 B. Brunet DG I/AD.1 A. Sapir DG II/B C. Martinez DG II/B.3 L. Windmill DG XV/A.1

Study	Consultant	Evaluation Committee
Subseries 4 — Impact on trade and investment		
External access to European market (Lot 2)	Southbank University	G. Davila Muro DG II/B.1 N. Bohan DG XV/A.1 L. Windmill DG XV/A.1 B. Brunet DG I/AD.1 A. Sapir DG II/B C. Martinez DG II/B.3
Subseries 5 — Impact on competition and scale effects		
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Study Subseries 6 — Aggregate and regional impact	Consultant	Evaluation Committee
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Results of the business survey	Eurostat and national statistical offices	J-Y. Muylle DG XV/A.1 J. Sheehy DG II/B.3 R. Depoutot Eurostat

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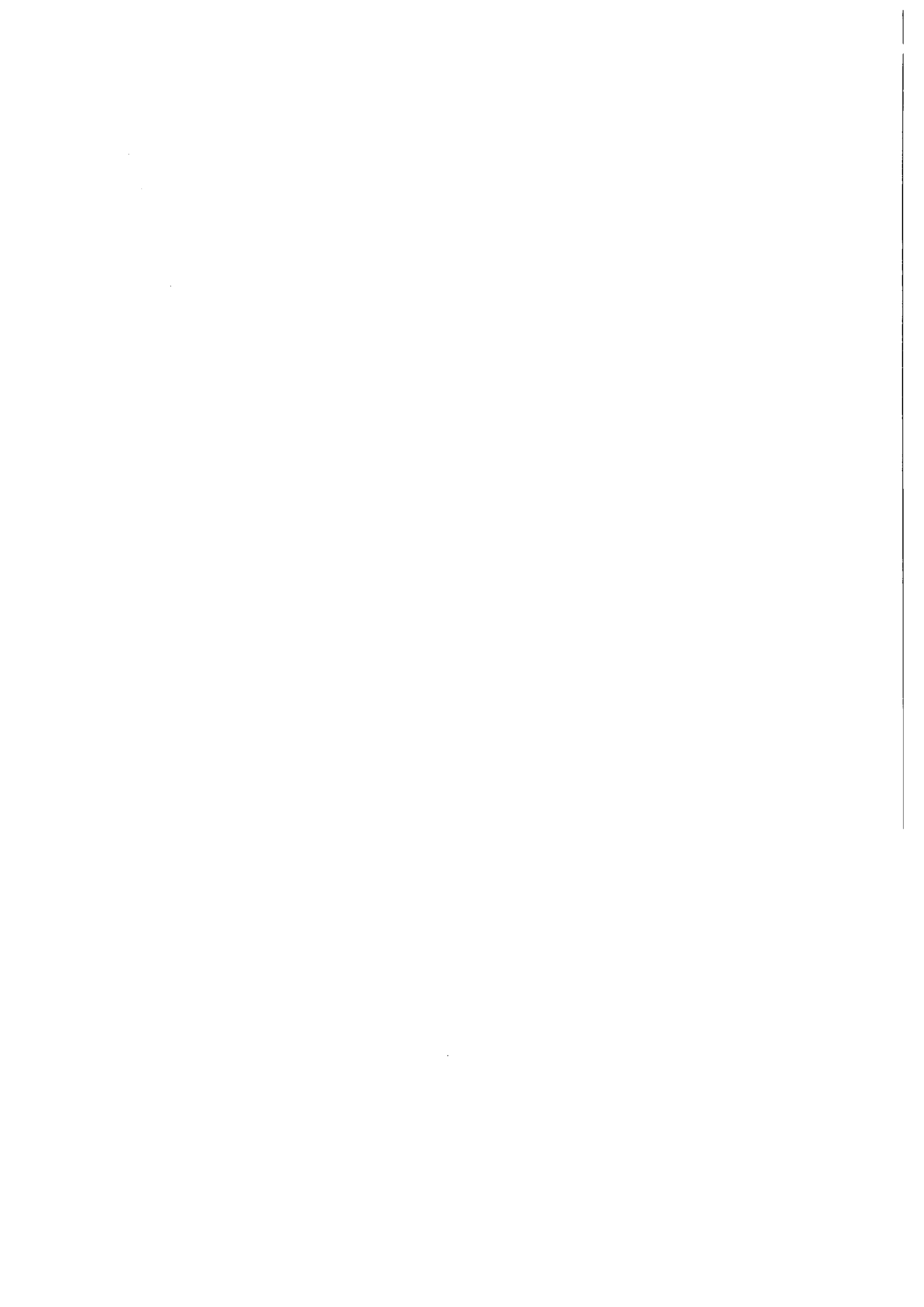
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