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**REPORT FROM THE COMMISSION TO THE COUNCIL AND THE  
EUROPEAN PARLIAMENT ON**

**THE STATE OF THE INTERNAL MARKET FOR SERVICES**

**presented under the first stage of the Internal Market Strategy for Services**

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## NOTICE TO THE READER

This report is intended to present the difficulties affecting the provision of services between Member States as perceived by interested parties according to the consultations carried out by the Commission and Member States, or which arise from complaints, written and oral Parliamentary questions, petitions or studies and surveys. These consultations, accompanied by specific studies, will be continued in order to obtain further information, in particular on the situation of consumers in the Internal Market for services.

The report does not set out:

- to make a judgement on whether measures causing difficulties are compatible or not with Community law, and in particular with the principles of the freedom to provide services and/or the freedom of establishment, or with secondary Community law. Indeed, these measures could be justified by objectives of overriding public interest such as protection of health, consumers, workers or the environment. The report does not prejudice the position that the Commission may take with regard to current or future complaints. Certain difficulties listed may already have been pronounced as justified by the Court or, on the other hand, condemned by it. Others may be covered by existing Community instruments but arise from the unsatisfactory application of these, while other problems may be addressed by further Commission initiatives.
- to determine the type of measures necessary to resolve these difficulties, in particular the need for harmonisation or adaptation of existing rules or any infringement procedures which it might be necessary to begin against certain Member States

In the course of the second stage of the implementation of the Internal Market Strategy for Services, the Commission will undertake a legal and economic evaluation in order to determine what initiatives should be proposed at the Community level to resolve the problems encountered both by providers and recipients of services. This evaluation will be carried out in consultation with all interested parties, including consumer organisations.

## **EXECUTIVE SUMMARY**

The Lisbon European Council adopted an economic reform programme with the aim of making the EU the most competitive and dynamic knowledge-based economy in the world by 2010. A key part of this programme is to make the Internal Market work for services. With this aim the Commission adopted its two-stage Internal Market Strategy for Services. This report, which completes the first stage, attempts to draw up a comprehensive inventory of the Internal Market barriers that continue to inhibit services. This report analyses the common features of the barriers and makes a preliminary assessment of their economic impact.

The large-scale consultation which forms the basis of this report involved the European Parliament, the Economic and Social Committee, the Committee of Regions, Member States and interested parties, and was carried out throughout 2001 and early 2002. This report provides a basis for actions that will be launched as a second stage in 2003. Because of the interdependence of different service activities, this report, in line with the Internal Market Strategy for Services, is based on a horizontal rather than a sectoral approach. The report covers a large variety of activities, such as consultancy services, certification services, estate agents, engineering, construction, distribution, tourism, leisure and transport. Furthermore, since a barrier affecting a consumer or service provider at any one stage of the business process, may undermine the entire cross-border service, this report covers barriers encountered at each of the six stages of the business process ranging from establishment of the service provider, use of inputs necessary for the provision of the service, promotion, distribution and selling of services, to the after-sales phase. The report covers the whole range of difficulties perceived as obstacles by the providers and users of services, but does not at present seek to assess whether they are compatible with Community law; this question will form part of the second stage of the strategy which will propose solutions.

A key element of the state of the Internal Market for services is consumption. The report emphasises that the recipients of services, and particularly consumers, are the principal victims of the dysfunctioning of the Internal Market. Consumers can be prevented from having easy access to services from other Member States, or have to pay a high price, or lack the confidence to buy from other Member States. A more fundamental analysis of the nature and impact of these difficulties on consumers will be carried out during the second stage of the Internal Market Strategy for Services, with a view to bringing forward appropriate solutions.

### ***Services are the engine of economic growth***

Growth in the economy is essentially driven by services. They account for 70% of GDP and employment in the majority of Member States. Services are to be found in all areas of modern economies, including traditional manufacturing sectors, where, for instance, car manufacturers offer financial, consulting, training and rental services. A number of demand-based factors have contributed to an ever-growing number of different services, ranging from more traditional service sectors such as transport, retail distribution, telecommunications, tourism and the regulated professions, to more recently developed services such as waste management, energy conservation, business services (including management consulting), data processing and technical analysis and testing.

However, the potential for growth in services cannot be fully realised while expansion of services activities across national borders in Europe is hampered by a wide range of Internal Market barriers.

***Internal Market barriers hit services harder than goods...***

Services are much more prone to Internal Market barriers than goods and are harder hit. Because of the complex and intangible nature of services and the importance of the know-how and the qualifications of the service provider, the provision of services is often subject to much more complex rules covering the entire service activity than is the case for goods. Furthermore, while some services can be provided at a distance, many still require the permanent or temporary presence of the service provider in the Member State where the service is delivered. Whereas with goods only the goods themselves are exported, in the case of service provision it is often the provider himself, his staff, his equipment and material that cross national borders. As a result, some or all of the stages of the business process may take place in the Member State where the service is provided and be subject to requirements differing from those in the Member State of origin. This also means that barriers at a single stage of the business process cannot be looked at in isolation; their cumulative impact throughout the service activity must be considered.

***...and occur at every stage of the business process...***

Barriers to establishment in another Member State may result from, for example, requirements relating to authorisation or professional qualifications, restrictions on the use of a certain legal form for the service provider or on the partnerships between different professions. The number of authorisations required, the length and complexity of the procedures, discretionary powers of local authorities and duplication of conditions already fulfilled in the Member State of origin of the service provider have all emerged as key themes in the consultation. The next problem service providers meet when engaging in cross-border activities concerns the use of inputs necessary for the provision of the service. A variety of restrictions affect, for example, the posting of workers, the use of equipment or material by the service provider or the use of cross-border business services. The promotion of services is rendered particularly difficult because of very restrictive and detailed rules for commercial communications ranging from outright bans on advertising for certain professions to strict control on content in other cases. The large divergence of legislation between Member States impedes pan-European promotional activities for many services.

The distribution of services across borders is hampered by a variety of restrictions, including requirements for the service provider to be established or resident in the Member State where the service is provided, which precludes service provision from the provider's home base. In addition, there are authorisation, registration and declaration requirements which are combined with requirements concerning professional qualifications or other conditions for exercising an activity which differ significantly from those of the service provider's country of origin. Problems directly or indirectly linked to the selling of services across borders result from differences in contract law, fixed or recommended prices for certain services, requirements relating to payment and reimbursement of VAT subject in different Member States to different rates, classification systems and procedures. Finally, in the after-sales phase a service provider can also face particular difficulties resulting from divergences between Member States concerning professional liability and insurance, or financial guarantees, or problems with

repair or maintenance services if they involve the posting of workers across borders. At the very least, all service providers encounter barriers at one stage of the business process; often they encounter them at several or even at all stages. Since many barriers have been reported to exist in Candidate Countries, problems will multiply with enlargement.

*....as well as affecting consumers*

Lack of transparency, lack of confidence, divergent rules between various Member States: these factors prevent consumers, who account for a large part of the demand for services, from enjoying the full benefits of the Internal Market and from playing their full role in the market. From the perspective of consumers, the difficulty in obtaining information, problems of access to cross-border services and the weak protection against, for example, abusive behaviour, contribute to the fragmentation of the Internal Market for services.

*Lack of information as well as cultural and language barriers add to the burden*

Business and consumers have considerable difficulty in obtaining precise information on the regulatory framework, the competent authorities and the procedures in other Member States. Furthermore, companies and consumers are often not aware of the principles of the Internal Market which allow them to challenge unjustified or disproportionate measures or to enforce their right to supply or receive services. In addition, the question of cultural and language barriers, and the tendency of a large number of companies still to think only in terms of their domestic market, which can make life particularly difficult for consumers, were both raised in the consultation.

*Barriers have common features across service activities*

Although barriers are widespread, they have a number of common traits in both their origins and effects. It is apparent that while the previous Internal Market programmes were effective in removing physical and technical barriers, these have been replaced by “legal barriers” arising from national, regional and local regulation. In addition, new barriers arise from the behaviour of administrations, including the use of discretionary powers or heavy and non-transparent procedures, which favours domestic operators. A number of difficulties result from unsatisfactory application of certain EU instruments. It seems obvious that Member States lack the necessary confidence in the quality of each other’s legal regimes and are reluctant to adapt their own regimes where necessary to facilitate cross-border activities.

Many barriers are horizontal and affect a range of service activities. One common feature is that Member States apply a single regime both to service providers who want to establish themselves on their territory and to those who want to provide services from their home base. For the latter, which are already subject to legal requirements and control by national authorities in the country where they are established, this may result in duplication of requirements and disproportionate burdens. Another common trait is the legal uncertainty resulting from unclear requirements applied on a case-by-case basis by national authorities, the result of which is often unpredictable.

### ***The impact of barriers to services hits the entire economy ...***

The impact of the barriers identified in this report is on all sectors of the economy. Barriers to one service will trigger knock-on effects for other services and also for the wider industrial economy, given the integration of services into manufacturing. Services are intricately intertwined. They are often provided and used in combination and feature as inputs at each stage of the service provider's business process. For example, an operator of retail stores established in one Member State and wanting to establish in a number of other Member States might wish to use the services of the real estate agents, shop designers, architects, engineers, construction companies, banks and insurance companies with whom he works in his Member State of origin. In most cases this is impossible because of barriers affecting those service providers who may not have, say, the authorisations or qualifications required in the other Member States. As a result, the establishment of the retailer may be delayed or rendered more costly and difficult, which in turn affects the services he provides to manufacturers and consumers. This interdependence of services means that it will be necessary at the second stage of the strategy to develop further the economic assessment of the problems identified so that it covers the effects on the entire economy and is not limited to the impact on one service activity.

Barriers result in considerable costs for companies engaging in activities doing business between Member States. A service provider seeking to enter a market, whether through establishment or cross-border service provision, will have to bear the significant costs associated with complex legal assistance. Such assistance is required to examine whether he can export his business model or whether parts of it, such as his promotional strategy, will have to be altered. These costs are additional to costs resulting, in particular, from different languages or cultural differences in commercial and consumption habits. Since barriers may occur at each stage of the business process, these costs will multiply throughout the provision of the service. Furthermore, in addition to the legal assistance costs, a company bears significant further costs resulting from necessary changes to its business model. The impossibility of using the same business model throughout the Internal Market prevents companies from taking advantage of economies of scale. The consequence of these negative effects is a general misallocation of resources within the companies concerned, limiting investment in innovation and differentiation of services. Given the key role of services, this in turn affects the performance of the entire economy.

### ***... but SMEs and ultimately all consumers are particularly affected***

Small and medium-sized enterprises (SMEs) are prominent in the services industry, but their prospects for cross-border growth are severely hampered. They are hit much harder than their larger rivals, since the legal assistance costs are fixed and not proportionate to firm size. As a result, SMEs will either be dissuaded from cross-border activities altogether or will be put at a clear competitive disadvantage compared to domestic operators. SMEs in small and peripheral Member States seem to be particularly disadvantaged. Furthermore, SMEs may become an attractive target for acquisition by larger companies because of their significant local knowledge, experience and innovation potential.

However, it is the service users and in particular consumers who pay the price for these restrictions through not being able to benefit from a greater variety of better quality and



competitively priced services. Ultimately this affects their quality of life. They suffer directly when administrative and legal requirements prevent them from using services offered from other Member States, or they suffer indirectly when existing barriers dissuade companies from offering their services to customers in other Member States or result in higher prices, less differentiation and lower quality. Finally European citizens suffer from the lost job creation potential of the services industry as a whole.

***Barriers need to be removed urgently to meet the objective of economic reform***

A decade after the envisaged completion of the Internal Market, there is a still huge gap between the vision of an integrated EU economy and the reality as experienced by European citizens and European service providers. The range of barriers perceived as affecting service provision and use, which are far more wide-ranging than was expected, amounts to a considerable drag on the EU economy and its potential for growth, competitiveness and job creation.

It is clear that the goal set by the Lisbon Council to make the European economy the most competitive in the world cannot be met unless sweeping changes are made to remove barriers to cross-border services in the near future. The nature and the scope of the problems to be addressed require a major effort and a clear political commitment by all European institutions and Member States finally to make the Internal Market work for services. This report provides a framework for actions to be launched in 2003 as a second stage of the Services Strategy on the basis of further discussions with the European Parliament, Member States and interested parties.

This report, and the reactions to it, forms the basis of work for the next stage of the services strategy. It will involve both legislative and non-legislative actions whose scope and content require further analysis. In respect of possible legislative proposals, a careful balance has to be found between the need to avoid too detailed and wide-ranging regulation at Union level and the need to protect the general interest objectives concerned. In respect of non-regulatory initiatives, the Commission will in the first instance consider what measures could provide to consumers and business the information and assistance necessary to allow them to benefit fully from the EU's Internal Market.

## INTRODUCTION

Services are everywhere in the modern economy. In the EU they account for almost 70% of GDP and employment and offer prospects for further growth and more jobs. Realising this potential, and ensuring that services deliver better quality and value to European citizens and business, is a major aim of the EU's economic reform programme. Much more progress is required in order to make the Internal Market work for services.

This challenge has been recognised by European leaders. The Lisbon European Council in March 2000 asked the Commission and Member States to devise a strategy for the removal of barriers to services<sup>1</sup>. The need for further action was also highlighted by the Stockholm and Barcelona summits in 2001 and 2002, while the Internal Market, Tourism and Consumer Affairs Council, in reviewing the EU's priorities for economic reform, concluded that improving the Internal Market in services remained "*a crucial strategic challenge for the Community*"<sup>2</sup>.

In response to the call from the Lisbon summit, the Commission set out a broad-ranging strategy in December 2000<sup>3</sup>. The strategy recognises the impact of the information society on methods of supplying and using services. As more and more businesses use a mixture of techniques to meet customer needs and provide both on-line and off-line services, it is increasingly necessary to ensure that the Internal Market for off-line services can develop in a way which complements the Internal Market for services delivered on-line<sup>4</sup>.

The objective of the strategy is to allow services to move across national borders in the EU as easily as within a single Member State. It takes in the first instance a horizontal approach across all economic sectors involving services and proposes two stages. The first stage of the strategy, which is completed by this report, involves identification and analysis of existing barriers to the cross-border movement of services whilst at the same time accelerating a number of ongoing initiatives. Amongst these, flanking measures have been initiated with the aim of gaining a

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<sup>1</sup> Presidency conclusions, Lisbon European Council, 24.3.2000, § 17. More recently, the ECOFIN Council, in its recommendation 10093/02 of 21 June 2002 concerning the Broad Guidelines of the Economic Policy of the Member States and the Community, considered that it was necessary to re-launch structural reform, which should include creating "an effectively functioning Internal Market in services by the removal of barriers to cross-border trade and market entry".

<sup>2</sup> 2412th meeting of the Council (Internal Market/Consumer Protection/ Tourism), Brussels 1 March 2002, document 6496/02 MI 35.

<sup>3</sup> Communication from the Commission to the Council and the European Parliament, An Internal Market Strategy for Services, COM (2000) 888 final, 29.12.2000.

<sup>4</sup> It should be noted that in the context of the e-Europe 2005 action plan the Commission, in co-operation with the Member States, will re-examine applicable legislation in order to identify, and, as the case may be, to remove those problems which prevent business from taking up e-business and consumers from benefiting from the Internal Market. This examination will in particular consider how to ensure that the provision of goods and services off-line can, as with services provided on-line, benefit from a true internal market. An e-summit to be organised in 2003 will mark the launch of this examination involving all interested parties, and will provide high-level representatives of economic operators the opportunity to describe the difficulties encountered in the context of e-business.

comprehensive view of employment in, and the added-value created by, the sector. The gathering of data and economic analysis are being completed by studies on productivity in services and on the “virtual economy”. The second stage, based on this analysis, will bring forward appropriate solutions to the problems identified. This approach has been endorsed by the European Parliament<sup>5</sup>, the Economic and Social Committee<sup>6</sup> and the Committee of Regions<sup>7</sup>.

The Services Strategy is consistent with, and complements, a range of other initiatives designed to facilitate the operation of the Internal Market in services. The “2002 Review of the Internal Market Strategy”<sup>8</sup> provides an overview. It shows that progress has been made in many fields, for instance in implementing the Financial Services Action Plan, the adoption of the regulation on cross-border payments in euro, the adoption of the new regulatory package on electronic communication networks and services and the directive on postal services, the forthcoming adoption of the regulatory package for public procurement and the presentation of the Commission’s proposals to harmonise the legal regime for sales promotions and to provide a uniform, transparent and flexible regime for recognition of professional qualifications.

In the area of *consumer protection*, the development of consumer policy at the EU level has been the essential corollary of the progressive establishment of the Internal Market. The free circulation of goods and services has necessitated the adoption of Community rules aimed at providing sufficient protection for consumers while eliminating regulatory obstacles as well as distortions of competition. The strategy adopted by the Commission on 12 May 2002, and in particular the Community approach envisaging a high common level of consumer protection<sup>9</sup>, aims to remedy those aspects linked to consumers’ lack of confidence in cross-border transactions. Moreover, the consultation launched by the Green Paper on consumer protection<sup>10</sup> recognised that existing EU rules in the area of consumer protection did not match up to the challenges posed by a market in constant evolution and so had to be reformed. A number of responses indicated that the disparities between national rules, particularly in the area of commercial practices, led to significant distortions of competition. The majority of responses to the consultation expressing a preference wished for reform to proceed on the basis of a framework directive on fair commercial practices in relations between business and consumers. In order to reduce legal fragmentation as well as to improve consumer confidence, the framework directive should be accompanied by the revision in due course of consumer protection

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<sup>5</sup> European Parliament resolution on the Commission communication “An Internal Market Strategy for Services”, A5-0310/2001, 4.10.2001

<sup>6</sup> Opinion of the Economic and Social Committee on the Communication from the Commission “An Internal Market Strategy for Services” (Additional Opinion) CES 1472/2001, INT/105, 28.11.2001

<sup>7</sup> Opinion of the Committee of the Regions on the Communication from the Commission “An Internal Market Strategy for Services”, 134/2001 fin, 27.06.2001

<sup>8</sup> Communication from the Commission to the Council, the European Parliament, the Economic and Social Committee and the Committee of the Regions, 2002 Review of the Internal Market Strategy: Delivering the promise, COM (2002) 171 final, 11.4.2002.

<sup>9</sup> Consumer policy strategy COM (2002) 208. See also the Communication on the follow up to the Green Paper on consumer protection COM (2002) 289 and notably the proposal currently under consultation on a framework directive on commercial practices.

<sup>10</sup> COM(2001)531 final.

directives and by the replacing of minimum harmonisation clauses with maximum harmonisation rules.

It should be noted that consumer protection may involve obligations to services of general interest such as transport, energy (electricity and gas), telecommunications and postal services. In this respect, the Commission Communication “Services of General Interest in Europe” emphasises the importance of these services and the role of public service obligations or other obligations relating to consumer protection to which certain activities might be subject.

In the area of *contract law*, future initiatives<sup>11</sup> should be mentioned which follow up the consultation launched by the Communication on European contract law<sup>12</sup> in order to resolve legal problems affecting the functioning of the Internal Market.

In the context of the *European social dialogue*, initiatives in skills, qualifications and the promotion of quality have been launched or completed in several areas such as personal, cleaning, private security and construction services.

In the area of *the free circulation of persons*, the abolition of internal border controls, which has become a reality due to the Schengen acquis being integrated in the EU by the Treaty of Amsterdam<sup>13</sup>, will also facilitate contact between service providers and their potential clients<sup>14</sup>. This removal of controls will also gradually contribute to citizens and economic operators becoming more aware of all the dimensions of the internal space without frontiers.

As far as the *international dimension* is concerned, there is a synergy between internal market policy and external trade policy, including the services negotiations in the context of the GATS (General Agreement on Trade in Services). More specifically, it will be necessary to take account of the results of the current discussions on domestic regulation in the context of article VI:4 of GATS.

This report forms an important step in the process of creating a true Internal Market for services by presenting an overview of the reality of the Internal Market today. For the first time since the presentation of the “General Programmes” for the suppression of restrictions to the freedom of establishment and the free provision of services in 1962<sup>15</sup>, the Commission has undertaken a comprehensive analysis of the existing barriers in the Internal Market for services. Since then, progress has been limited. The

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<sup>11</sup> Following the request of the Council and the European Parliament, the Commission will present these initiatives by the end of 2002.

<sup>12</sup> Communication from the Commission to the Council and European Parliament on European Contract Law COM(2002) 398 final, 11 July 2001.

<sup>13</sup> OJ L 239, 22 September 2000

<sup>14</sup> The free movement of persons without controls at borders between Member States benefits EU citizens and members of their family, but it also allows foreigners holding a residence permit from a Member State to circulate freely without a visa on the territory of Member States for up to 3 months (article 21 of the Convention applying the Schengen agreement of 14 June 1985, signed at Schengen on 19 June 1990). However, this legal principle does not allow service providers who are third country nationals to supply their service in a Member States other than one in which they are established.

<sup>15</sup> Programmes généraux pour la suppression des restrictions à la liberté d'établissement et à la libre prestation des services, OJ C 2, 15.1.1962.

Commission's 1985 White Paper on completing the Internal Market<sup>16</sup> stated that "progress on the freedom to provide services has been much slower than the progress achieved on the free movement of goods". And the 1992 Cecchini report<sup>17</sup> concluded that the potential of services sectors "for much more significant growth is being artificially pinned back by regulations and practices which significantly inhibit the free flow of services and thus the free play of competition between companies supplying them".

Some measures have already been adopted in order to suppress the most obvious difficulties which limit the development of the Internal Market in services. These measures are the result of the application by the Commission of its role as guardian of the Treaty and of exercising its power of initiative to bring forward harmonisation proposals aimed at making the Internal Market work. These measures have enabled the Internal Market to reach a higher level of economic integration than regional trading arrangements elsewhere in the world. Nevertheless, in spite of progress so far, contributors to the consultation were able to identify a wide range of difficulties which remain and which are the object of this report.

This report is based primarily on a large-scale consultation with interested parties, but also draws on information from other sources such as European Parliament petitions and questions, complaints to the Commission, economic and statistical studies and Member States' contributions. The consultation, which lasted throughout 2001 and early 2002, was launched in order to gather first-hand information on the barriers which hinder the development of cross-border services in the EU. It covered any and all problems encountered in the context of the provision and use of services, and of cross-border establishment in the EU. It is clear from the jurisprudence of the Court that any measure liable to prohibit, impede or render less advantageous the supply or use of cross-border services or cross-border establishment within the EU could constitute a barrier. This report therefore includes examples of barriers which are not simply prohibitions, discriminations or conditions which are impossible to meet, but various types of requirements which, if applied to companies from other Member States, would undermine the freedoms to establish or provide services. Some barriers are due to complex, burdensome or non-transparent regulation or practices; most are just due to the wide divergence of national rules.

The overall aim of the report is to describe the realities of the Internal Market as seen by providers and users of services. It does not at this stage seek to assess whether any individual barrier is justifiable or not.

The report covers areas which are subject to Community instruments or proposals. Furthermore, the report reflects comments made in the consultation on barriers faced by EU companies in the Candidate Countries. In these countries the companies are confronted with the same obstacles as in the Member States. However, additional barriers may result from nationality requirements, restrictions on ownership of companies in certain sectors by non-nationals or restrictions on access to real estate.

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<sup>16</sup> Completing the Internal Market : White Paper from the Commission to the European Council (Milan, 28-29 June 1985), COM (85) 310, 14.6.1985.

<sup>17</sup> "The European Challenge, 1992: The Benefits of a Single Market", Paolo Cecchini, Wildwood House, for the European Commission, 1988.

In line with the Services Strategy, this report covers barriers throughout the entire business process, starting from establishment and the use of inputs necessary for the service provision, to promotion, distribution, sales and after-sales activities. It is clear that service providers are far more exposed than producers of goods to barriers in each of these stages of their business activity. This is because the provision of services often requires the permanent or temporary presence of the service provider in the Member State where the service is delivered. As a result, some or all of the stages of the business process may take place in the Member State where the service is provided and be subject to requirements differing from those in the Member State of origin. For instance, a company wanting to establish in, or provide services to, another Member State might face obstacles in gaining authorisation, including mutual recognition of qualifications, posting its employees or using its equipment, promoting its services, distributing its services, concluding contracts with customers and providing guarantees or after-sales services. Obstacles at any of these stages may render the entire cross-border activity less attractive.

Furthermore, in accordance with the horizontal approach of the Services Strategy, this report covers barriers affecting a large variety of different economic activities. The reason is not only that a number of barriers, such as authorisation procedures, affect different sectors in a similar way, but that services are intricately intertwined and barriers affecting one service have knock-on effects on a number of different other services. A comprehensive approach is required to evaluate barriers to services in the Internal Market and their overall impact.

Services play a key role in the economy and in the life of every citizen. Barriers to services therefore not only affect the competitiveness of service providers themselves, they also deprive the recipients of services, which includes every business and every consumer in the EU, of the increase in innovation, price competition and quality, which greater access to services would bring.

## **I. BARRIERS TO THE INTERNAL MARKET FOR SERVICES**

With regard to the definition of the "Internal Market" in the EC Treaty ("*an area without internal frontiers*") and the objective, set out in the "Internal Market Strategy for Services", of making the provision of services between Member States as easy as within a Member State, it has to be said that the Internal Market for services is far from being a reality. Two broad categories of problems can be singled out: those deriving directly or indirectly from legal constraints and those deriving from non-legal factors.

### **A. Legal barriers**

The term "legal barriers" covers all obstacles to the development of service activities between Member States deriving directly or indirectly from a legal constraint and which are liable to prohibit, impede or otherwise render less advantageous such activities. Such barriers also stem from difficulties caused by divergent national regulations, as well as from problems relating to the behaviour of national authorities, or from the legal uncertainty caused by the complexity of some cross-border situations. In all cases, the result is the same: consumers and businesses alike are

discouraged from using services from other Member States, and service providers are discouraged from offering their services in other Member States<sup>18</sup>.

The inventory of barriers set out below highlights the difficulties which service providers are liable to encounter when seeking to exercise freedom of establishment or freedom to provide services in order to develop their activities in other Member States. These are difficulties which were identified by interested parties and Member States in the course of the consultation or which have emerged from complaints made to the Commission, from European Parliament petitions and written question, from recent cases filed with the European Court of Justice or from studies and surveys which have come to the notice of the Commission. This method, aimed at taking stock of how the Internal Market for services is operating in reality, has three major consequences

- *This report does not take a position on the compatibility* with Community law *of the barriers identified*, this question being the subject of the second phase of the Strategy, which will focus on solutions, particularly in terms of harmonisation needs. It is not the object of the inventory to call into question the need for, or content of, national rules as such, but merely to highlight problems to which they may have given rise when applied to cross-border activities;
- *The difficulties identified may already be the subject of ongoing Community initiatives*, existing Community instruments or measures, infringement proceedings or Court judgments;
- *Some difficulties may not have been identified*, even though this risk has been minimised by drawing on numerous sources of information.

In order to draw up as broad an inventory as possible of all difficulties hindering the development of service activities between Member States<sup>19</sup>, the method employed was to identify the problems which a service provider is liable to encounter at any stage in his activity, whether it be during the process of establishment in another Member State (stage 1), when posting staff to or using equipment in another Member State (stage 2), when promoting the particular service in another Member State (stage 4), when selling the service (stage 5) or, finally, after having provided the service in another Member State (stage 6). The inventory set out below presents all the difficulties identified as affecting cross-border activities in relation to each link in the business process.

## **1. Difficulties relating to the establishment of service providers**

The consultation showed that a national of a Member State, or a company already established in a Member State, wishing to become established in another Member

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<sup>18</sup> These "barrier effects" and the fact that they largely replace the technical, physical and tax barriers referred to in the 1985 White Paper on the completion of the Internal Market, already cited above, explains the use of the term "legal barriers".

<sup>19</sup> The inventory also includes difficulties identified in candidate countries. It should be borne in mind that very many of the difficulties cited in Member States are also encountered in candidate countries.

State in order to engage in a service activity there, may face a large number of difficulties. These have a particularly severe impact in the case of services: whereas goods can circulate among Member States (via distribution networks) without the manufacturer having to cross a border, the provision of services depends on know-how that requires a direct relationship between service provider and client. Even though the temporary relocation of the service provider or the provision of the service from a distance may enable such a relationship to come about (and is the preferred approach of SMEs) establishment in the target market remains a key commercial strategy<sup>20</sup>. This is particularly the case where the operator intends to maintain a long-term presence in the country concerned or where he wishes to adapt to the specific conditions of the market or boost customer confidence. Moreover, the complexity of regulating services, coupled with the fact that the quality of a service is directly dependent on the characteristics of the provider, engenders a number of requirements which are not to be found in regulations governing goods, e.g. specific rules on the legal form of the service provider and restrictions imposed on multidisciplinary activities.

(i) Monopolies and other quantitative restrictions on access to activities

**Monopolies** in some Member States were singled out, as they have the effect of preventing the establishment of service providers from other Member States in which no such monopoly exists. The monopoly concerned may be one that is entrusted to *a specific body*, such as those in partially liberalised sectors (such as postal services or energy utilities), a monopoly on the distribution of *certain products*<sup>21</sup>, which could affect distribution services in particular, or *activities reserved exclusively for certain operators*<sup>22</sup>.

**Quantitative restrictions** which some Member States impose on access to service activities, e.g. *quotas or numerus-clausus rules* governing the number of service providers<sup>23</sup>, rules on *maximum surface area*<sup>24</sup>, or on *geographical distance*<sup>25</sup> limit the number of service providers and could place established national operators at an advantage over new entrants.

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<sup>20</sup> See in particular a study entitled "Service internationalisation characteristics, Potential, Barriers", A. Henten, T. Vad, CRIC workshop, Manchester 1-3.10.2001, section 3, which stresses that the services sector is more dependent than manufacturing on cross-border establishment.

<sup>21</sup> For example, alcoholic beverages and tobacco products.

<sup>22</sup> For example, gambling activities or the distribution of pharmaceutical products. See also a OECD study entitled "Regulatory reform in road freight and retail distribution", Economic Department working papers No 255, 10.08.2000, section 39 et seq., and a study carried out for the Commission entitled "Barriers to Trade in Business Services", Centre for Strategy and Evaluation Services, January 2001, page 15.

<sup>23</sup> For example, national regulations stipulating there may be only one provider of chimney-sweeping services per district or per commune.

<sup>24</sup> For retail services, for example.

<sup>25</sup> For example, in one Member State medical laboratories may only analyse specimens collected at least 60 km away, while in another the minimum distance between opticians is fixed at 350 metres, and in another shopping centres must be in city-centre locations, which prevents the establishment of new entrants.



Difficulties identified include, for example, rules in one Member State imposing a limit of 1 optician per 10 000 inhabitants and one driving school per 15 000 inhabitants.

***Territorial restrictions*** applying in some Member States may confine authorisation to engage in service activities<sup>26</sup> to a specific region or locality, so that service providers wishing to cover the entire national territory are obliged to become established in several regions.

(ii) Nationality or residence requirements

***Nationality requirements*** exist in several Member States in respect of shareholders, management and staff of service enterprises<sup>27</sup> and in respect of some regulated professions<sup>28</sup>.

***Residence requirements***, particularly those relating to managers of service enterprises<sup>29</sup>, give rise to problems. For example, depending on the particular country, two thirds, one half or at least one of the members of the management board must be resident.

***A single-establishment requirement***, whereby a service provider wishing to become established in a particular Member State is directly or indirectly obliged to give up an establishment in another Member State, was pointed out by medical laboratories, for example. Such a requirement effectively prohibits the exportation of a business model by means of becoming established in several Member States.

(iii) Authorisation and registration procedures

Access to a large number of service activities<sup>30</sup> is subject to a prior authorisation requirement which often entails difficulties for operators from other Member States.

***The failure to take into account requirements already met by a service provider*** in a Member State in which he is established, e.g. securities or guarantees already deposited<sup>31</sup>, may have the effect of duplicating and compounding the constraints facing operators who are present in more than one Member State.

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<sup>26</sup> For example, private security services. Concerning the difficulties encountered in connection with services of this type, see a study conducted by CoESS/UNI-Europa and financed by the Commission entitled "A comparative overview of legislation concerning the private security industry in the European Union". ECOTEC, May 2002. In the context of the social dialogue, the European social partners in the private security sector (the CoESS for the employers and UNI-Europa for the unions) signed on 13 December 2001 a joint declaration on European harmonisation of legislation governing the private security sector.

<sup>27</sup> For example, engineering enterprises, aero-clubs and NGOs.

<sup>28</sup> For example, chartered surveyors.

<sup>29</sup> One such requirement may be that an applicant for a telecommunications service licence must be resident in the particular country (even before he or she has obtained the licence).

<sup>30</sup> For example, financial services, regulated professions, craftspersons, private security services, certification bodies, drinking water testing laboratories, trade fair organisers, telecommunications services providers, employment agencies and performers' agents, transport and processing of waste.

<sup>31</sup> For employment agencies or private security services, for example.

**The number of authorisations** required for some activities considerably amplifies the restrictive effects for an operator from another Member State, even if it just means having to contact more administrative bodies, fill in more forms and provide more certificates<sup>32</sup>.

For example, in one particular Member State, seven different local and national licences are needed in order to open a hotel or restaurant<sup>33</sup>; while in another a company wishing to open a retail outlet needs a building permit, an environmental permit and a socio-economic permit, as well as having to comply with zoning regulations which can sometimes be highly complex.

**The procedures and conditions associated with such regulations** may have restrictive or even discriminatory effects on operators from other Member States, particularly where the procedures involve bodies made up of competitors<sup>34</sup> or where the applicant has to prove that the application for authorisation is justified by a genuine need<sup>35</sup>.

**A registration requirement** applying to some service providers, whereby they are obliged to register with an administrative authority, a professional body, a chamber of craft trades or a trade association, is frequently encountered and could prove very expensive for operators who have a presence in several countries, particularly on account of the annual contributions to be paid, and where, moreover, membership of a specific sickness insurance scheme is involved.

**The bureaucratic nature of authorisation and registration procedures**, the long time they take to complete, the onus of proof, the certification of translations, the prices or fees to be paid, the less than constructive attitude taken by some authorities and the difficulties involved in lodging administrative appeals were very often singled out on account of their discouraging effect on service providers from other Member States<sup>36</sup>, particularly SMEs and start-ups<sup>37</sup>.

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<sup>32</sup> In one contribution it was even stated that one had to be a "collector of licences" in order to set up a bakery business in one particular country, as the requisite authorisations varied depending on the types of products and activities of one and the same bakery. Given these difficulties, the operator in question abandoned the plan of becoming established. The multiplicity and duplication of authorisations had also been identified as a problem in the "Report from the Commission to the Council, the European Parliament, the Economic and Social Committee and the Committee of the Regions on concerted action with the Member States in the field of enterprise policy" COM (1999) 569 final, section 2.1.1.

<sup>33</sup> See, for example, a study entitled "Tackling the impact of increasing regulation - A case study of hotels and restaurants". Better Regulation Task force (UK), June 2000.

<sup>34</sup> Those applicable to distribution services, for example.

<sup>35</sup> In one Member State, for example, this relates to a genuine need on the part of consumers with regard to existing shops; in another, the criterion is that there must be no negative impact on existing town-centre shops; and in another the granting of a licence is subject to a condition relating to the need for a performer's agent's activity "in terms for the demand for the placement of performance artists".

<sup>36</sup> For example, the difficulties encountered in opening retail outlets because of authorisation or registration requirements and the associated administrative formalities were identified in the OECD study cited above (section 39 et seq.) as being one of the chief restrictions on market access in the distributive trades sector. An Anglo-French study on the services sector in the United Kingdom and France underscores the negative effects on employment at the local level which are caused by licensing and *numerus clausus* systems applicable to some activities:

(iv) Restrictions on multi-disciplinary activities

A certain number of service activities are subject to rules designed to ensure independence and autonomy between different activities, preventing them from being exercised jointly. The disparity between national rules in this domain may have a particularly pronounced restrictive effect by preventing the exportation to another Member State of know-how consisting precisely of addressing in a multi-disciplinary, innovative and less expensive manner the different requirements of a customer. These restrictions may take several forms:

- **requirements concerning the structure or management of service enterprises**, preventing for example the formation of associations between different professions<sup>38</sup> ;
- **restrictions on the exercise** of multi-disciplinary activities - these lay down that the exercise of different activities *is incompatible*<sup>39</sup>, oblige a service provider to *exercise exclusively one particular activity*<sup>40</sup>, or stipulate that different activities may only be pursued in *different locations*<sup>41</sup>.

In one Member State, for example, estate agencies are prohibited from engaging in other professional activities such as property management, financial consultancy or cleaning.

(v) Legal form and internal structure of economic operators

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"The service sector in the UK and France. Addressing barriers to the Growth of Output and Employment. An Anglo-French Report.", Department of Trade and Industry and *Ministère de l'économie, des finances et de l'industrie* (Ministry of Economic Affairs, Finance and Industry), 2000, page 89.

<sup>37</sup> A business survey attached as an annex to the November 2000 Internal Market Scoreboard shows that 91% of the companies interviewed attached the highest priority to a simplification of administrative procedures [http://europa.eu.int/comm/internal\\_market/en/update/score/business.htm](http://europa.eu.int/comm/internal_market/en/update/score/business.htm). See also "Report on the implementation of the European Charter for small enterprises", COM (2002) 68 final, which stresses in particular that "the total number of procedures for starting a business could be an important target for simplification"(section 4: Conclusions); "Report of the Business Environment Simplification Task Force- Best" volume 1, OPOCE 1998 ; "*Etude comparative internationale des dispositions légales et administratives nécessaires pour la formation des PME dans six pays de l'Union européenne*" (comparative international study of the legal and administrative provisions governing the creation of SMEs in six countries of the European Union, Logotech, European Innovation Monitoring System, EIMS Publication No 27, March 1996.

<sup>38</sup> For example, in numerous Member States lawyers are not allowed to enter into partnerships with non-lawyers, e.g. accountants, tax consultants or patent agents. Other forms of restrictions may also exist. In one Member State, for example, only tax advisers, tax consultants or tax agents may be shareholders or executives of companies providing tax consultancy services. Concerning the rules applicable in the United Kingdom, see for example a report entitled "Competition in professions", Office of Fair Trading, March 2001, section 30.

<sup>39</sup> See, for example, studies on cases concerning incompatibilities between the activity of an auditor and that of an accountant in the above-cited survey carried out for the Commission entitled "Barriers to Trade in Business Services", appendices, case studies 6. See also the judgement of 9 February 2002 *Wouters C-309/99*, on the prohibition of multi-disciplinary partnerships between members of the Bar and accountants.

<sup>40</sup> In one Member State, for example, such a requirement applies to employment agencies.

<sup>41</sup> For example, in one Member State real estate services and insurance activities.

The obstacles concerned are particularly restrictive for operators who are already established in one Member State and are not subject to this type of requirement in their country of origin. The divergence between the rules in question means that operators may be obliged to create a legal entity that is "made to measure".

**Requirements regarding legal form** may impose a particular type of company on a service provider or, conversely, prohibit him from having such a legal form<sup>42</sup>. The situation can become highly complex for some activities for which different legal forms are mandatory in different Member States.

For example, a lawyer who wishes to become established in a different Member State must dissolve his or her one-person company in the Member State in which he or she is already established because in the other Member State lawyers are allowed to operate limited-liability companies only<sup>43</sup>.

In addition to the (above-mentioned) discriminatory rules affecting shareholders, **the capital of service enterprises** is subject in some Member States to restrictions such as a *minimum amount of capital* for companies providing private-security services and employment agencies<sup>44</sup>.

**A minimum number of employees** may be required for some service companies<sup>45</sup>.

(vi) Professional qualifications

Disparities between different countries' regulations governing professional qualifications may give rise to various kinds of difficulty for service providers wishing to become established in another Member State, particularly where qualifications for the profession concerned are not automatically recognised<sup>46</sup>.

**Differences between Member States regarding activities considered to be "regulated professions"** may cause difficulties, as there are many services<sup>47</sup> which are not regulated in all Member States, while some may be regulated in one Member State only<sup>48</sup>. For example, a service provider from a Member State with no requirement for

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<sup>42</sup> In one Member State, for example, trade fair organisers must be non-profit-making.

<sup>43</sup> Other activities are also affected by this type of problem, e.g. auditors.

<sup>44</sup> Restrictions may also include a maximum investment, as in the media sector, or an obligation to find other shareholders or co-investors for certain areas of activity. It should be noted that the Anglo-French report cited above also identified (page 36) minimum-capital requirements as being one of the main obstacles to service activities.

<sup>45</sup> In one Member State, for example, employment agencies must have at least 12 employees per 100 contracts concluded in the previous year. In other Member States, companies providing private security services must employ a minimum number of staff depending on the activities and territory covered.

<sup>46</sup> It should be noted that, quite apart from problems concerning the recognition of professional qualifications, differences in rules governing the professional training of employees may cause certain difficulties, as in the case of companies providing private-security services, which are subject to specific requirements in some Member States.

<sup>47</sup> For example, engineers and consulting engineers, tax advisers, estate agents, surveyors, landscape architects, managing agents of blocks of flats, consultants, craftspersons.

<sup>48</sup> For example, one Member State has established a specific vocational title for services consisting of drafting labour law documents which does not exist in any other Member State

a professional diploma wishing to become established in another Member State that does have such a requirement will not find it easy to have professional qualifications recognised.

*Aptitude tests* required by some Member States for activities not covered by arrangements for automatic recognition of qualifications could be a source of difficulties, particularly for SMEs<sup>49</sup> owing to a lack of transparency and predictability.

*Differences regarding the fields of activity covered by a particular professional qualification* may give rise to difficulties, and it may also happen that different professional qualifications are required for one and the same activity if different designations are used<sup>50</sup>.

For example, *chartered building surveyors* may be allowed to draw up plans for a building in one Member State, while only architects are allowed to do so in another.

(vii) Conditions governing the exercise of service activities

A decision as to whether or not to become established in a particular Member State may be influenced by differences not only between the respective conditions governing *access* to the service activities concerned but also between conditions relating to the way they are exercised, such as professional liability insurance regulations, rules on shop opening hours - which affect strategies for the establishment of retail outlets<sup>51</sup> - and rules on taxation and use of infrastructures, which may affect the establishment of telecommunications operators<sup>52</sup>.

*The different company tax regimes result in obstacles which penalise cross-border establishment of service providers*<sup>53</sup>. Although business would like to consider the Internal Market as just one market, numerous problems result from the fact that companies must conform with 15 different fiscal regimes. This situation undermines the economic efficiency of business strategies and structures. The multiplicity of fiscal laws, conventions and practices leads to significant compliance costs and constitutes a barrier to establishment which particularly affects SMEs.

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and which is subject to authorisation and an obligation to be entered in a national registry specific to this new profession.

<sup>49</sup> See the already cited "Report of the Business Environment Simplification Task Force", page 65, which states that, in some fields, the aptitude-test requirement "has tended to become the rule rather than the exception".

<sup>50</sup> For example, a carpentry diploma obtained in one Member State does not authorise the holder to exercise the profession of a "carpenter/joiner" in another.

<sup>51</sup> This type of restrictive effect was also identified in the OECD study already cited, sections 49-51.

<sup>52</sup> For example, taxation in respect of GSM transmission masts, or the setting of electromagnetic emission thresholds.

<sup>53</sup> See the study "Taxation of companies in the Internal Market" SEC(2001)1681, which, inter alia, examines in detail the principal fiscal provisions likely to constrain cross-border economic activity in the Internal Market. On the basis of this analysis the Commission presented a strategy to remove such obstacles. Communication from the Commission: "Towards an Internal Market without tax obstacles - a strategy for providing companies with a consolidated corporate tax base for their EU-wide activities" (COM(2001)582 final).

In particular, it seems that service providers are especially affected by problems linked to the fiscal treatment of intra-group transfer pricing, cross-border flows of income, cross-border loss relief and cross-border restructuring operations. These difficulties present a risk of double taxation and increased compliance costs.

## **2. Difficulties relating to the use of inputs necessary for the provision of services**

The cross-border use of inputs by service providers can take two forms. In order to offer its services, an enterprise already established in one Member State may have to move to another Member State and mobilise its own inputs there: i.e. its staff, equipment or the business services of which it usually avails itself on its domestic market. On the other hand, an enterprise may need inputs from other Member States. In both cases, the contributions to the consultation revealed difficulties. In particular, the cross-border recruitment or posting of staff could be problematical<sup>54</sup>, which runs counter to the aim of facilitating the mobility of workers<sup>55</sup>.

### **(i) Posting of workers (employees or temporary staff) to another Member State**

The provision of services between Member States often means that the service provider has to post staff temporarily to another Member State. Some difficulties may be encountered in this context. It should be noted that Directive 96/71/EC<sup>56</sup> sets out a common list of rules providing for minimum protection which must be observed in the country where the service is supplied by the employer which posts the worker in the framework of the provision of services.

***The requirement to make a prior declaration***, applying in several Member States to the cross-border posting of staff (permanent employees or temporary personnel), particularly in the construction sector<sup>57</sup>, may result in difficulties for operators from other Member States on account of the administrative burdens which they may impose<sup>58</sup>. Compounding these in some Member States is the obligation, on expiry of a

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<sup>54</sup> While human resources are one of the most important inputs for the provision of services, contributions also showed the cross-border deployment and posting of staff continue to cause service providers major difficulties which are hardly encountered at all by manufacturers of goods. Concerning the low level of worker mobility in border areas, see a study carried out for the Commission entitled "Scientific Report on the Mobility of Cross-border Workers within the EEA", MKW Wirtschaftsforschung GmbH, November 2001, section 1.3.

<sup>55</sup> Concerning this, see the Communication from the Commission to the Council, the European Parliament, the Economic and Social Council and the Committee of the Regions - Commission' Action Plan for skills and mobility, COM (2002) 72 of 13 February 2002.

<sup>56</sup> Directive 96/71/EC of the European Parliament and of the Council of 16 December 1996 concerning the posting of workers in the framework of the provision of services (OJ L 18, 21 January 1997 p1). This Directive aims to guarantee observance of the fundamental freedoms of the Treaty while at the same time protecting workers. The Directive also obliges Member States to establish co-operation between national administrations and to designate liaison offices.

<sup>57</sup> These formalities have to be completed for each individual site. A service provider who regularly posts personnel for short periods cannot obtain an authorisation valid, for example, for one year. In one Member State, the obligation to make a prior declaration has to be met, before work on each individual site commences, for each temporary worker provided by an employment agency established in another Member State.

<sup>58</sup> For example, the costs of translating certain employment documents into the language of the host country.

certain period (generally three months), to register posted workers with labour authorities, administrative bodies or the police<sup>59</sup>.

***The burden and complexity of administrative formalities***<sup>60</sup>, the stringent and quasi-systematic checks which some posted workers may have to undergo, excessive paperwork and the associated delays (stoppage of work), could result in difficulties in the case of regular and short-term postings.

For example it was indicated that, for the installation of a lift by two workers on a ten-day posting, a company had to complete a series of administrative formalities (in particular the submission to the labour inspectorate of data on the posted workers and safety measures, and an obligation to keep documentation in the language of the host country) although the company considered that it had already met similar requirements in its country of establishment.

***The application to posted workers***<sup>61</sup> ***of the host country's labour-law provisions***, without account being taken of the obligations and charges already met by the employer in the country of establishment, could lead to amounts being levied twice and to additional administrative costs and burdens having to be borne by service providers from other Member States. Such cases of duplication, notably as regards the minimum wage<sup>62</sup> or paid leave<sup>63</sup> could have particularly restrictive effects in the case of short-term service provision and with regard to SMEs and service providers established in border areas who would like to post workers to several Member States on a regular basis in order to provide their services there.

For example it was highlighted that it proved economically unattractive for a small craft enterprise to carry out work in another Member State on account of an obligation to make a quarterly provision for all social security contributions for its posted workers. Even though the amount would later have been reimbursed to the company concerned, this would have tied up too much cash<sup>64</sup>.

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<sup>59</sup> For example, the obligation to apply for a residence permit.

<sup>60</sup> For example, the obligation to draw up certain social and employment documents and make them available for the inspection authorities, or to keep such documents on file with a social representative in the host country for a certain period of time, and to translate these documents in their entirety into the language of the host country.

<sup>61</sup> Whether they are nationals of a Member State or a non-EU country.

<sup>62</sup> As regards wages in particular several contributions show that restrictions result from disparities in the methods of calculating wages. Some contributions, for example, highlight difficulties linked to a failure by the host country to take account of all the components making up remuneration in the country of establishment (e.g. 13<sup>th</sup> or 14<sup>th</sup> month's salary) which may mean that remuneration is higher than that imposed by law in the host country.

<sup>63</sup> For example, the obligation to contribute to a third party institution (such as a paid leave fund) despite the fact that the posted workers already enjoy a comparable benefit by virtue of national provisions guaranteeing holiday pay. In one such instance, payment for the contract was withheld until the matter had gone through the courts.

<sup>64</sup> See "Artisanat, Petites entreprises et zones frontalières – Analyse de cas particuliers d'entreprises travaillant en pays limitrophes (seconde action expérimentale)" (The crafts sector, small enterprises and border areas - Analyses of specific cases of enterprises working in neighbouring countries [second experimental scheme], Inter-regional Council of the Saar-Lor-Lux Chambers of Craft Trades, 1996.

*These restrictive effects are exacerbated by the existence of severe sanctions*<sup>65</sup>, including criminal penalties, the application of which is sometimes perceived as being discriminatory by service providers who do not meet obligations to make a prior declaration or fail to observe labour-law provisions.

*Procedures and conditions applying to the posting of third-country nationals* in several Member States are tantamount to authorisation requirements<sup>66</sup>. This fact and the slowness and cumbersome nature of the procedures concerned were also highlighted<sup>67</sup> as being liable to render the provision of services difficult or even impossible in some cases.<sup>68</sup> Such difficulties could primarily affect high-tech sectors in which operators seek the skills they need by using staff, e.g. software designers, from non-EU countries.

In several Member States, the posting of personnel from third countries is subject to the condition that the staff concerned have been employed by the posting enterprise for at least a year. In some cases they must even have a contract of indefinite duration. Moreover, it can take a long time for the document(s) required for a posting to be issued (up to six months in some cases).

(ii) Use of employment agencies or temporary workers from other Member States

Enterprises which may need to use an employment agency established in another Member State or to deploy temporary workers in another Member State<sup>69</sup>, could face a series of difficulties.

*Prior-authorisation rules*<sup>70</sup> *and establishment requirements*<sup>71</sup> applying to employment agencies could prevent operators from availing themselves of an agency

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<sup>65</sup> In one Member State, for example, the minimum fine is € 1,000, including for simple material errors, and can range up to € 26,000.

<sup>66</sup> These range from an obligation to obtain a work permit in the host country, the granting of which depends on an assessment of the labour market there, to a "work visa" or residence permit, without which no posting can take place.

<sup>67</sup> Concerning this, see in particular a study entitled "Managing mobility matters – a European perspective", PriceWaterhouseCoopers, 2002, section 2.5, as well as the "Report of the High Level Panel on free movement of persons" chaired by Mrs Simone Veil and presented to the Commission on 18 September 1997, "(the Veil Report), chapter 6.

<sup>68</sup> Moreover, the fact that third-country nationals who are insured in one Member State are not, in principle, covered by the provisions of Regulation (EEC) No 1408/71 of the Council of 14 June 1971 on the application of social security schemes to employed persons and their families moving within the Community, is also liable to make it more difficult and costly to post them to another Member State. A proposal from the Commission seeking to extend the field of application of regulation 1408/71 to third country nationals was agreed by Ministers at the Council of 3 June 2002.

<sup>69</sup> For example, in order to make up skills shortages, cope with a heavy workload, particularly on account of seasonal factors, or manage their resources with a degree of flexibility.

<sup>70</sup> The conditions and procedures for authorisation, the length of time they take, as well as the associated guarantees and deposits, can likewise exacerbate the restrictive effects of these authorisation rules. The granting of an authorisation may be linked to the quality or the structure of the service provider or to the agency having a minimum capital stock. It may also be conditional on guarantees or securities being deposited or on the payment of duties. In one Member State, a user enterprise that had to cope with a temporary rise in its workload was unable to use an agency established in a Member State on account of the time it would have



that is established in another Member State and does not have such authorisation. This has the effect of limiting operators' access to temporary workers from other Member States<sup>72</sup>. This could also prevent a company from calling on workers provided by an agency in its home state to supply a service in another Member State where such an authorisation is required. Such regulations could moreover delay the performance of a contract or make it impossible to meet a deadline<sup>73</sup>.

***The prohibitions imposed on certain sectors and restrictions on the use of temporary staff***<sup>74</sup> (such as the requirement to prove a specific need to use temporary workers) vary from one Member State to another. In the context of cross-border service provision, this is liable to hamper the posting of temporary staff employed by an enterprise<sup>75</sup>.

(iii) Other difficulties relating to the cross-border deployment of workers

Some contributions showed that operators encounter difficulties<sup>76</sup> when seeking to recruit or employ staff in one or more Member States particularly with a view to making up skills shortages<sup>77</sup>. This is especially the case for enterprises which are established in several Member States or which employ cross-border workers. These difficulties derive from obstacles to the cross-border mobility of workers within the Internal Market.

***Disparities between national regulations governing remuneration, taxation***<sup>78</sup> ***and social protection*** are perceived as a source of major difficulties<sup>79</sup> for enterprises

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taken for the requisite licence to be granted (four months). Moreover, the obligation imposed in some Member States to first consult trade union organisations, even in urgent cases, is also liable to slow down the procedure appreciably.

71 An agency may be required to have a local representative, or to be "active" in several regions of one and the same Member State.

72 Particular mention was made of "niche" sectors (such as high-tech activities and civil aviation), but also the building and construction sectors, as well as the tourism, hotels and health sectors.

73 For example, an air transport company was unable to use the services of an employment agency specialising in providing airline transport pilots because the agency in question was not established in the same Member State as the air transport company.

74 Such prohibitions affect several sectors (construction, the merchant navy, the public sector, removals and low-skill activities) but may also be limited by particular considerations (increased workload at an enterprise, performance of specific and exceptional tasks, replacement of seasonal employees or activities, launching of a new activity).

75 This is compounded by tax and social provisions specific to temporary employment which have the effect of making staff provided by an employment agency established in another Member State more expensive. For example, the user enterprise may be subject to double taxation from the first day of providing its service or to higher social security contributions. In some Member States, it may also be required to pay end-of-contract compensation.

76 It should be noted that the difficulties relating to nationality, residence and professional-qualification requirements which were raised in the section concerning the establishment of service providers are likewise a restriction on worker mobility.

77 Particularly in the information-technology, communications, construction, health and tourism sectors.

78 Disparities concerning taxation (level and structure of taxes) were cited in several contributions as being a major obstacle to the mobility of labour, as migrant and cross-border workers are often more heavily taxed in spite of bilateral agreements on double taxation (see the Veil Report as well as the study entitled "Managing mobility matters – a European perspective" both op cit.).

employing or seeking to recruit migrant or cross-border workers<sup>80</sup>, and could give rise to additional administrative costs and paperwork.

For example, pension contributions paid by migrant workers to pension schemes in the Member State of residence are not necessarily deductible from taxes payable in the Member State in which they exercise their activities.

***The complexity of social security regulations*** in all Member States may discourage enterprises from employing migrant or cross-border workers<sup>81</sup> and also cause additional administrative burdens.

***Diversities between pension schemes and obstacles to the transfer of supplementary pensions***<sup>82</sup>, may have a restrictive effect on the mobility of cross-border and migrant workers and give rise to high administrative and financial costs, preventing for example operators who are established in several Member States from centralising their pension management systems.

(iv) Cross-border use of business services

In order to engage in its particular activities, an enterprise normally requires the *input* not only of manpower but also of a variety of "business services". These may range from legal assistance and accounting services, through marketing services, website design, equipment leasing or hire, to transport and after-sales services.

***The use of cross-border business services*** may be affected by difficulties which can prevent an enterprise from using providers from other Member States whose services are more attractive in terms of quality or price. They may also prevent a company, when supplying services in another Member State, from using service providers with which it has long had dealings.

For example, a waste-transport enterprise may be prevented, in the context of its cross-border activities, from drawing on the assistance of its environmental consultant because the latter is not entitled to provide services in other Member States.

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<sup>79</sup> Disparities relating in particular to income tax and pension rights were identified in the above-cited studies entitled "Barriers to trade in Business services" (section 4) and "Managing mobility matters – a European perspective", as having a negative impact on an operator's ability to exercise its activities in several Member States and, in particular, to recruit personnel locally in another Member State.

<sup>80</sup> For example, an enterprise that wishes to recruit qualified personnel will not always be able to inform candidates of the exact amount of taxes and contributions which they will have to pay, even though matters have been simplified by the introduction of the euro.

<sup>81</sup> Contributions highlighted, above all, problems encountered in the application of the Regulation (EEC) No 1408/71 relating to the co-ordination of social security schemes (difficulties in determining the applicable scheme, in particular to border workers, non-application of the provisions of the regulation to benefits under collective agreements, e.g. in the case of occupational pensions. Moreover, some problems of double deduction of contributions have occurred in spite of the implementation of forms E101 and E128 used in case of a posting. The Commission has made a proposal to simplify this regulation.

<sup>82</sup> The difficulties concerning the transferability of supplementary pension rights acquired by migrant workers are highlighted in particular by the above-cited Commission Action Plan on Skills and Mobility.

Where such difficulties affect providers of business services, they will be dealt with from the perspective of the distribution of services.

- (v) Cross-border use of equipment and material

*Problems relating to the use of technical equipment in the cross-border provision of services* were highlighted by contributors to the consultation.<sup>83</sup> Service providers are liable to be seriously hindered, and their ability to benefit from the freedom of service provision compromised, by measures imposing restrictions on the use of equipment or material specifically required for the exercise of their particular activities. Such difficulties may relate in particular to the technical equipment of laboratories, the use of business vehicles, exhibition-stand materials, road-mending machinery, construction-site equipment, security vans or technical standards for electronic signatures. In some cases, Member States require the use of infrastructure and materials which cannot be transported into the country in which the service is provided<sup>84</sup>.

For example, the introduction of the euro has led to a sharp rise in demand for the cross-border transport of notes and coins, with central banks having an increasing proportion of their cash produced in other Member States in the euro-zone. Commercial banks as well as retailers may also find it worthwhile to have cash transported to and from other Member States. However, differences between national rules on the transport of cash, including technical requirements in relation to equipment and vehicles, are a hindrance to the provision of this type of service between Member States.

### **3. Difficulties relating to the promotion of services**

This is a key stage, particularly for the cross-border provision of services, it being imperative that operators promote their services if they are to penetrate a new market in another Member State. It is essential to advertise know-how and specialist capability, as these are the chief factors that differentiate operators in this field. However, communication of numerous service activities<sup>85</sup> is governed by strict and complex rules whose variations between Member States may make it difficult for service providers to promote their know-how across borders and virtually impossible for them to undertake a pan-European promotional campaign.

- (i) Authorisation, registration and declaration procedures

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<sup>83</sup> For example, equipment used by analysis laboratories, trade-fair exhibitors, certifying veterinary officers, opticians, chiropodists and construction enterprises (who have to cope with divergent legislation regarding construction equipment and undergo multiple inspections of hired cranes, with serious consequences in terms of additional costs and delays). Difficulties may also include the requirement for SMS companies to connect up with each operator involved in the cross-border transmission of messages.

<sup>84</sup> For example, requiring a chiropodist who is established in another Member State to have non-transportable equipment and a permanent infrastructure in the country of service provision is tantamount to imposing an establishment requirement in order for services to be provided.

<sup>85</sup> A wide range of sectors (the regulated professions, distribution, telecommunications, press, publishing, cinema and financial services) are affected by bans or limitations on the use of commercial communications.

**Prior authorisation** may be required for communications concerning certain services. Such authorisation mechanisms may cause delays and additional administrative burdens in the context of cross-border promotional efforts.

In the case of financial services, prior approval is required in some Member States for some or all forms of advertising of some or all types of financial services.

In the distribution sector, authorisation is required for the promotion of certain products<sup>86</sup>, for certain forms of promotion<sup>87</sup>, and for the use of certain media<sup>88</sup>.

A **declaration** may also have to be made to a specified body in respect of certain types of sales promotion or advertising for certain services<sup>89</sup>, which may cause delays and additional administrative burdens for cross-border activities.

(ii) Bans on commercial communications

**Bans on commercial communications** for certain types of services, certain categories of recipients or certain media affect service providers from other Member States as they, unlike national operators, have hardly any other means at their disposal for making their products and services known.

**Some regulated professions are subject to a total advertising ban**, imposed either by law or by codes of good conduct, limiting the opportunities for developing their client base beyond the borders of their Member State of residence.

Some Member States prohibit all forms of advertising for certain professions, such as physicians, accountants and engineers, preventing the communication even of factual information.

**With regard to other services, such bans may be imposed** in respect of specific communication media<sup>90</sup> and recipients<sup>91</sup>.

(iii) Content of commercial communications

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<sup>86</sup> For example, the advertising of medicines available without a medical prescription may require prior authorisation, and the advertising of fruit and vegetable prices outside the point of sale may be subject to the existence of a multi-sector agreement. See OECD study entitled “Assessing barriers to trade in services: retail trade services”, 2 October 2000.

<sup>87</sup> For example, some Member States stipulate that prior approval is required for promotional lotteries and games.

<sup>88</sup> For example, for mobile poster campaigns, particularly for the deployment of vehicles carrying commercial messages for each district of a city.

<sup>89</sup> In some Member States, for example, organisers of a promotional lottery or game have to make a declaration to the public authorities. In other Member States, any advertising on the part of a teaching establishment has to be notified in advance to the national ministry of education.

<sup>90</sup> For example, television advertising may be completely prohibited for certain sectors, as is the case in one particular Member State in respect of the distribution, press, publishing and cinema sectors.

<sup>91</sup> Some communication bans are often designed to protect minors. In some Member States, for example, television advertising aimed at children is completely banned at certain times. In other Member States, television advertising for toys is prohibited between 7 a.m. and 10 p.m.

*The type of message which operators are allowed to communicate* may also be subject to restrictions, causing difficulties in a cross-border context. In some Member States, not only are commercial communications by regulated professions limited to factual information, but this information itself is subject to restrictions<sup>92</sup>. For example, in some Member States, certain types of information, such as prices or a comparison between services rendered and their prices must not be the subject of a commercial communication.

In some Member States professionals such as lawyers are not allowed to mention their particular specialisation in their communications to the public, which limits their scope for attracting new custom from other Member States.

*Content restrictions in respect of the target audience*, which vary markedly from one Member State to another, may also exist for certain services, particularly for communications aimed at minors<sup>93</sup>.

*Restrictions in respect of the arguments used* may, in some Member States, prohibit for example the use of certain arguments, such as those of an "ecological" nature<sup>94</sup> or those extolling the virtues of a product or service in terms of its positive effects on health.

*Restrictions on the language used* in commercial communications exist in some Member States, e.g. in the form of an obligation to use the official language(s) of the Member State concerned<sup>95</sup>.

(iv) Form of commercial communications

Some regulations restricting scope for sending commercial communications without prior consent may make it difficult to canvass for business if they also apply to messages addressed to professionals<sup>96</sup>. Regulations may relate to specific forms of canvassing, such as telephone<sup>97</sup> postal or door-to-door canvassing.

(v) Non-commercial communications

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<sup>92</sup> Numerous professions are affected by these kinds of restrictions: auditors, physicians, pharmacists, architects, accountants, notaries, lawyers.

<sup>93</sup> In one Member State, for example, a regulation on sales promotions provides that the value of prizes offered in promotional lotteries and games must not exceed €0.7.

<sup>94</sup> In one Member State, for example, it is prohibited to refer to a solarium as "biolarium".

<sup>95</sup> These restrictions may cover all advertising or just advertising messages relating to certain services (such as investment services) and may even apply in cases where the advertising concerned is aimed specifically at nationals of other Member States, such as foreign tourists.

<sup>96</sup> Where regulated professions such as auditors are concerned, for example, some Member States prohibit the unsolicited promotion of services, which may prevent such professionals from sending newsletters or brochures. For instance, a gravestone distributor was formally threatened with prosecution in another Member State for having faxed to undertakers in that country unsolicited (price) information about its activities.

<sup>97</sup> In some Member States, for example, the making of telephone calls to potential customers with a view to offering financial services is authorised only if the canvasser has obtained the prior consent of the client. In others, telephone canvassing is prohibited even if the persons targeted have been informed in advance in writing.

The compilation and circulation between Member States of independent information on the quality of services, based in particular on trials and comparative testing, are an essential means of enabling users of services to become aware of quality services in other Member States. In this regard, the application of certain rules relating to unfair competition<sup>98</sup>, parasitic behaviour, disparagement, counterfeiting, defamation, the right of reply and the citing of comparative tests<sup>99</sup> could give rise to legal uncertainty which may be detrimental to the cross-border dissemination of this type of information.

#### **4. Difficulties relating to the distribution of services**

The difficulties set out below are not those affecting the distributive trades sector proper but those encountered in the cross-border provision of all services. The distribution of services can come up against a much more complex set of barriers than does that of products. In contrast to products, the quality of a service is gauged not only by the inherent quality of the service itself but also by the provider, particularly the professional qualifications of staff, capacity, capital and the internal structure of the enterprise. Numerous requirements, varying considerably from one Member State to another, are therefore imposed on the cross-border provision of services.

More particularly, Member States tend to subject services supplied by providers established in other Member States to some or all of the requirements applicable to operators established on their territory. This explains why the inventory of difficulties affecting this stage often includes those identified as affecting the first stage, the establishment of the service provider.

- (i) Monopolies and other quantitative restrictions on access to activities

*The monopolies and other quantitative restrictions listed* in relation to the first stage (establishment of the provider) can represent an insurmountable barrier when applied to providers of cross-border services established in other Member States. The application of a monopoly system has the effect of depriving these providers of any opportunity to supply their particular service, even on a temporary or occasional basis. It is clear that the existence and application of monopolies can have severe effects on consumers.

- (ii) Nationality or establishment requirement

*In addition to instances of discrimination based on nationality<sup>100</sup>, the requirement that a provider be established<sup>101</sup>* in the Member State or region in which the service is delivered is one of the main difficulties faced in a large number of economic

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<sup>98</sup> For example, consumer associations have been taken to court for violation of honest trade practices following the publication of comparative tests.

<sup>99</sup> In one Member State, for example, it is forbidden to cite comparative tests in advertising.

<sup>100</sup> These still exist in some Member States for certain professions, such as notaries and surveyors.

<sup>101</sup> This requirements comes in various guises: an operator may be required to have its head office, a secondary establishment, a residence or a permanent presence etc. in a particular country.

activities<sup>102</sup> in several Member States. This type of requirement represents the very negation of the freedom of provision of services which enables operators to pursue their activities in a Member State other than the one in which they are established.

For example, in some Member States certification bodies for biological products are not allowed to provide their services unless they are established in the particular country concerned. This prevents the cross-border provision of a highly specialised service and also has the knock-on effect of hindering the sale of biological products.

***The obligation to have a local representative*** almost amounts to an establishment requirement<sup>103</sup>.

- (iii) Authorisation, registration and declaration procedures

Some Member States try to subject cross-border service providers who are established in other Member States to the authorisation, registration or declaration procedures applicable to operators established on their own territory (see stage 1).

***Prior authorisation*** in various forms (such as having to obtain a permit, licence, or other approval) is required<sup>104</sup> in numerous Member States, even in cases where a service is rendered on an occasional basis only. The application of such requirements to cross-border services can have particularly restrictive and discouraging effects, especially as severe sanctions, even criminal penalties, are frequently applied to those who do not have the requisite authorisation<sup>105</sup>.

***The failure of authorisation regimes to take account of requirements already met*** in the Member State of establishment can, moreover, exacerbate the restrictive effects and leads to a duplication of the rules to be complied with and of the burdens to be borne.

***Entry*** (or enrolment or accreditation) in a register (which might be kept by the national professional bodies or tax or social authorities) in the country in which the services are provided is also very often required and may cause not only a great deal of paperwork but also major costs<sup>106</sup>.

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<sup>102</sup> For example, wine transport and storage enterprises, building construction enterprises, patent agents, employment agencies, private security services, clinical analysis laboratories, boiler inspectors, enterprises handling the transport of deceased persons.

<sup>103</sup> A local representative is sometimes compulsory for the purpose of completing administrative formalities or for tax reasons.

<sup>104</sup> For regulated professions, for example, including tourist guides, mountain guides, craftspersons, trade-fair organisers, providers of telecommunications services, certification bodies, drinking water testing laboratories, patent agents, employment agencies, performers' agents, private security services, waste transport, importation and treatment companies, ambulance companies, leasing enterprises, enterprises providing cross-border electronic installation services. Several cases were also identified where national approval is regarded as being a *de facto* prerequisite for participation in public contracts. See study entitled "Barriers to Trade in Business Services" cited above.

<sup>105</sup> For example, this was identified by estate agents and by tourist guides of certain nationalities.

<sup>106</sup> In some Member States, for example, construction enterprises have to register with a professional body, landscape architects with that profession's national association; craftspersons have to be entered in the national register of artisans (including for activities of an exceptional nature and of limited duration), and numerous regulated professions are subject

For example, a general requirement for electricians in a particular Member State to register with a national trade association means that one particular professional who occasionally provides services there has to pay an annual contribution of around € 776 in that country (three times the contribution he pays in his country of establishment).

A *declaration* is sometimes required<sup>107</sup>. While imposing less of a constraint than the requirement to obtain an authorisation or to register with a chamber of trade, this obligation may nevertheless give rise to a considerable amount of paperwork and significant costs, given the difficulties involved in obtaining the requisite certification and the obligation to have documents translated and certified.

*Providers of cross-border services have to meet a whole series of requirements* associated with authorisation procedures: e.g. the obligation to register with a professional body, provide proof of a minimum amount of capital, deposit a guarantee<sup>108</sup> or to keep special accounts<sup>109</sup>. The overall result of these requirements and formalities may be to cause complications, delays and administrative costs, including in the case of occasional services of very short duration<sup>110</sup>.

(iv) Requirements regarding the internal structure and legal form of the service provider

*A specific legal form and specific internal structure* are often required not only for establishment in a particular country but also for the cross-border provision of services. Operators<sup>111</sup> from other Member States thus have to meet very different or even contradictory requirements.

In one Member State, surveying activities may be exercised only by public limited-liability companies which have a minimum amount of capital, provide a guarantee and have a minimum number of staff. This excludes any service providers who are established in other Member States where they are not subject to such requirements and pursue their activities as sole traders.

*Rules stating that various activities are incompatible with one another* are also sometimes applied not only to operators established in the country in question (see first stage) but also to cross-border service providers established in another Member State. The application of these incompatibility rules to cross-border services can have particularly severe restrictive effects, given that they often relate to the very structure of enterprises.

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to a requirement to register with a professional body or trade association. What is more, cross-sectoral obligations may exist, such as the regulation in one particular Member State which requires any foreign enterprise whose activity exceeds 30 working days to register with the chamber of commerce.

<sup>107</sup> In one Member State, for example, a separate declaration has to be made for every construction site.

<sup>108</sup> For example, for employment agencies, private security services or architects.

<sup>109</sup> For example, wine transport enterprises.

<sup>110</sup> For example, circus artists are sometimes confronted with long and complex procedures which are irreconcilable with the high level of mobility and frequency of travel which characterise this type of activity.

<sup>111</sup> For example, auditors, telecommunications operators, employment agencies, and private security services (which in one country are required to have legal personality).



- (v) Requirements in respect of professional qualifications and experience

***Disparities between national requirements concerning professional qualifications and experience*** (to which, moreover, the above-mentioned authorisation and registration procedures are often linked) are one of the problem areas often highlighted in the consultation<sup>112</sup>. Service providers experience difficulties in providing their services in another Member State on the basis of their original professional title. Generally speaking, they are treated in the same way as those wishing to be become established in the Member State concerned and are obliged to pursue no less arduous a procedure in seeking to have their professional qualifications recognised.

***Different professional titles*** are in some cases required for one and the same activity, where national designations do not tally<sup>113</sup>. Sometimes, a profession is regulated in some Member States only<sup>114</sup>, or even in just one Member State; in such cases, the country requiring a specific qualification for the exercise of a particular activity thus excludes the cross-border provision of the services in question by operators established in other Member States where no such qualification is required.

- (vi) Imposition on service providers of conditions governing the exercise of an activity

Differences between some rules laying down the conditions governing the exercise of service activities, in conjunction, as the case may be, with the problems just outlined, can cause numerous difficulties<sup>115</sup>. Differences between the conditions imposed by the Member State in which the services are provided and those imposed by the country of establishment may also cause serious problems for operators and sometimes prove to be discriminatory.

In one Member State, all performers' agents, including those from other Member States, are subject to a rule providing for a presumption of employed status for all

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<sup>112</sup> For example, for engineers, patent agents, electricians, and taxi drivers in some border regions. Difficulties in obtaining the qualification required in the country of destination were also highlighted by service providers carrying out electrical and sanitary installation work. Sport physiotherapists pointed out certain problems stemming from a lack of precise details as to the qualifications required by another Member State in which they were merely accompanying athletes visiting that country. See also studies entitled "Principen om ömsesidigt erkännande på tjänsteområdet" (The principle of mutual recognition in the services sector), Kommerskollegium, 26.October 2000; and "Rapport om barrierer for integration i Øresundsregionen" (Report on barriers to integration in the Öresund region) Öresund Chamber of Trade and Industry, December 2001.

<sup>113</sup> For example, equivalence problems may affect the activities of dentists or cardiologists.

<sup>114</sup> For example, craftspersons, estate agents, or labour consultants.

<sup>115</sup> This may concern, for example, rules governing a professional code of good conduct or the protection of a general interest, but also more specific rules, such as an obligation for private security services to ensure that their staff wear a different uniform from that worn in their country of establishment; an obligation for construction companies to pay 15% of the value of the work in question to the tax authorities before the work has been completed, the inability of designers of games of chance to offer their services in some Member States which impose restrictions in respects of games which can be played in casinos; the application to certain activities in candidate countries of strict language requirements, including for the conclusion of contracts.

performers with whom they conclude contracts and stipulating that they must keep a specific record of their activities in that country.

***Territorial limits applying to a licence may cause difficulties*** not only for establishment (see stage 1) but also for the provision of services by providers established in another Member State.<sup>116</sup>

#### **(vii) Transport and postal services**

***Transport services*** are subject to divergent requirements in the various Member States, particularly as regards the characteristics of the vehicles used<sup>117</sup>, such as lorries and tourist coaches. Differences also exist with regard to arrangements for the provision of transport services<sup>118</sup>, particularly in the case of the transport of deceased persons. Equally, the diversity of national rail systems (different gauge widths, different systems for supplying electricity or different maximum axle loads for wagons and locomotives) account for significant delays at border crossings and therefore extra costs<sup>119</sup>; moreover, national rules on access to networks vary and make it impossible to supply certain services<sup>120</sup>.

Some Member States prohibit, for example, the hiring of heavy goods vehicles (HGVs) registered in a Member State other than the one in which the transport operator is established, which hinders the use of hired HGVs transporting goods from one Member State to another.

***Air traffic*** suffers from the existence of several different and incompatible management systems, which is the source of congestion, extra expense and safety risks<sup>121</sup>.

For example, a flight from Rome to Brussels flies over nine different control centres.

Furthermore, the bilateral agreements between Member States and third countries may sometimes contain provisions incompatible with the Internal Market, which disadvantages Community airlines while profiting airlines from third countries operating in the EU.

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<sup>116</sup> For example, in relation to debt collection, transport and private security services.

<sup>117</sup> This relates to requirements (particularly as to weight and dimensions) concerning vehicles used for transporting certain types of goods, such as wine or chemical products, and vehicles which are leased or hired, as well as to restrictions on the use of tourist coaches in certain areas.

<sup>118</sup> For example, restrictions on driving on public holidays, obligations regarding specific documents/certificates relating to scheduled and actual driving times for a vehicle (and the translation of documents into the local language), VAT registration even where a vehicle is simply passing through the particular country, statistical declarations (which are a cause of delays at borders), the translation of documents into the local language, restrictions due to monopolies in port services, restrictions on cabotage concerning the islands of some Member States, airport taxes.

<sup>119</sup> The Commission presented several propositions to complete the legislative framework in January 2002.

<sup>120</sup> Some directives in this area are in the course of being transposed.

<sup>121</sup> The Commission launched an initiative at the end of 1999 to reform air traffic control in Europe. The European Council in Barcelona in March 2002 set 2004 as the date for the completion of the Single European Sky.

*Postal services* are also the subject of complaints, with regard for example to the slowness of deliveries, the knock-on effects of postage-rate differences on cross-border distribution activities, and the economic consequences of partial harmonisation. This is liable to make the development of pan-European express delivery services particularly difficult.

(viii) Restrictions on the receipt of services

*Service recipients*, and particularly consumers, as well as providers, are the direct victims of obstacles to the distribution of services, facing difficulties which may even make it impossible to receive certain services<sup>122</sup>.

*Preferential treatment for residents of a particular Member State or of a particular part of its national territory*, such as rules reserving the provision of services exclusively for nationals or residents of a particular Member State (or region or locality), may prevent recipients of services from other Member States from having the same access to services as nationals or residents of the Member State in which the services are provided. Such cases were highlighted in particular with regard to tourism, leisure activities, sport, distribution, transport and mobile telephony<sup>123</sup>.

For example, numerous consumers complain that they cannot have free-to-air access to both private and public-service television channels broadcast by satellite. Programmes on these channels are encrypted solely in order to prevent their reception outside the Member State in which the broadcaster is established.

## 5. Difficulties relating to the sale of services

The difficulties encountered at this stage are linked directly or indirectly to the transaction in question. They stem from rules or practices, differing markedly from one Member State to the other, relating to contracts, prices and payments, invoicing, accounting and VAT, but also to access to public contracts or to rules governing the reimbursement of costs to service recipients. These difficulties have a greater bearing

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<sup>122</sup> This relates, for example, to obstacles to receiving pay-TV channels broadcast from other Member States, to concluding a mobile telephone contract in another Member State, to benefiting from advantageous transport tariffs or from promotional offers by large-scale distributors which are sometimes restricted to the national territory of a particular country and are inaccessible for potential users from other Member States. Other barriers may affect users of equipment needed for the receipt of services from other Member States, e.g. parabolic dish antennas (the installation of which for individual or communal use may be subject to prior authorisation, monitoring costs, a fee or restrictive internal rules governing the building concerned) or winners of a contest/lottery who have to pay a tax both to the Member State in which they took part in the contest or lottery and in their Member State of origin when repatriating their winnings, and mobile telephone users who cannot receive calls in certain locations owing to the use of scrambling systems (prohibited in the majority of Member States).

<sup>123</sup> For example, cases were pointed out where service recipients are subject to additional conditions and guarantees when taking out a subscription with a mobile telephony operator, or are subject to higher charges in other Member States when taking part in a cultural or sporting event (such as a marathon), visiting a museum or tourist site, buying a ferry ticket, taking out an insurance contract, using sports facilities, hiring a car etc. Finally, there are also situations where, conversely, residents of another Member State enjoy preferential treatment, e.g. free parking at an airport.

on the sale of services than on that of products, especially as contracts play a more important role for services. This is because they determine the nature of the service concerned or because the drawing up of the contract is the service itself. Moreover, price calculation is often more complex in the case of services and may be subject to fixed or recommended prices varying from one Member State to the next.

(i) Formation and content of contracts

*The formation and content of contracts* can give rise to specific issues regarding services. The consultation launched by the “Commission Communication on European contract law”<sup>124</sup> has resulted in the identification of numerous problems with the functioning of the Internal Market, resulting from the legal regimes of Member States relating to contract law<sup>125</sup>. These difficulties also affect services and especially financial services (such as the insurance sector in particular). For example, the results of the consultation confirm that the existence of different national regimes of contract law results in additional transaction costs, in particular possible expense on information and litigation which weighs particularly heavily on SMEs and consumers. Moreover, the diversity of rules governing contract content, and the uncertainties surrounding the identification of mandatory or public policy rules from which the contracting parties may not derogate, make it impossible to use standard contracts throughout the Internal Market<sup>126</sup>. These problems make themselves particularly felt in the financial services sector.

Some Member States still require operators who are established in other Member States to give prior notification of the general and specific terms and conditions of insurance policies, in order to carry out checks and prohibit the use of certain clauses.

*Other specific issues* may affect certain cross-border services. For example, employment agencies may be confronted with rules which are specific to each Member State regarding the duration and renewal of contracts in the posting of workers. Even in domains for which minimum harmonisation has been introduced, such as doorstep sales, problems persist.

(ii) Price setting, payments, invoicing and accounting

*Price regulations* applicable to a certain number of services<sup>127</sup>, whether providing for maximum prices, minimum prices or prices set or recommended by Member States or professional bodies, can result in very different calculation methods and price levels for one and the same service, depending on the Member State in which it is rendered, and are liable to cause problems in the case of cross-border service provision.

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<sup>124</sup> COM(2001)398 final.

<sup>125</sup> See the summary by the Commission services of the results of the consultation at [http://europa.eu.int/comm/consumers/policy/developments/contract\\_law/index\\_en.html](http://europa.eu.int/comm/consumers/policy/developments/contract_law/index_en.html)

<sup>126</sup> For example, the impossibility of drawing up a standard contract of employment for an enterprise which is active in all Member States was underscored in the study entitled "Managing mobility matters – A European perspective" already cited above, section 4.3.1.

<sup>127</sup> For example, the regulated professions, private security services, debt recovery services, hotel services and road safety consultancy activities. Difficulties caused by regulations governing prices for tourism services were also identified as a problem by a report prepared for the Commission entitled: "Yield management in small and medium-sized enterprises in the tourism industry", Arthur Andersen, Frankfurt am Main, OPOCE, 1997.

**Rules and practices in relation to invoicing and payment** are perceived as being particularly complex in the various Member States and cause problems in cross-border transactions<sup>128</sup>. As far as invoicing is concerned, the rules relating to the law of VAT (notably obligatory indications, electronic invoicing and retention of invoices) have been recently harmonised<sup>129</sup> but other conditions (for example indications imposed by commercial law or linguistic rules) remains governed by national law. Means of payment do not have the same legal status in all Member States, and enterprises wishing to pay by credit card may have to establish contractual relations with the local bodies responsible for the administration of payments. Bank transfer costs are always too high, which affects both service providers and recipients<sup>130</sup>.

Opening a bank account in the Member State in which a particular service is provided is often necessary in order to facilitate payments, but is difficult as it involves making a declaration of residence or of non-residence, which in turn gives rise to tax declarations and causes administrative delays and costs.

**Accounting rules**<sup>131</sup> are designed amongst other things to meet tax inspection needs; for this reason in particular, they differ markedly from one Member State to another. For example, accounting documents have to be itemised in accordance with classifications drawn up by each of the Member States in which an enterprise files a VAT return. An enterprise which is active in several Member States is therefore obliged to maintain parallel accounting systems while at the same time ensuring consistency in the accounting of the enterprise as a whole.

(iii) Taxation

**The payment and reimbursement of VAT** is one of the problems most frequently cited in relation to the cross-border provision of services. Indeed, the rule according to which services are subject to VAT in the country of establishment of the provider is accompanied by numerous exceptions which give rise to complex situations in the context of cross-border sales. This results in numerous service providers being subject to VAT obligations in Member States other than the one in which they are established.

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<sup>128</sup> For example, in one Member State an invoice for professional services in the legal field must contain a specific reference to rules governing complaints.

<sup>129</sup> Council Directive 2001/115/EC of 20 December 2001 amending Directive 77/388/EEC with a view to simplifying, modernising and harmonising the conditions laid down for invoicing in respect of value added tax. *OJ L 015*, 17/01/2002 P. 0024 - 0028

<sup>130</sup> For example, in one Member States, banks make the recipient pay a fee even where the transferor has indicated that he wishes to bear all charges. In other cases, banks have refused to credit clients' accounts with amounts corresponding to winnings which the latter have lawfully gained in another Member State on the grounds that the bets concerned were not authorised in their own Member State. See also a report prepared for the Commission entitled: "Bank charges in Europe", IEIC, April 2000.

<sup>131</sup> In the insurance field, supervisory authorities impose different rules on accounting and statistics, which excludes the use of high-performance computerised accounting systems.

*The burden of VAT obligations<sup>132</sup> as well as the very significant differences between Member States (for example in terms of rates, obligations, procedures or forms) result in considerable difficulties.* Furniture removers, for example, are obliged to deal with the competent authorities in each of the Member States in which they offer their taxable services, and ask for a VAT number<sup>133</sup> in each of these Member States and settle their affairs according to the different rules.

Where a travel agency sells hotel accommodation to other agencies in another Member State, it is subject to VAT obligations in that Member State, which is a significant source of practical difficulties.

Similar problems were also identified in relation to passenger transport, conference-organisation and business services<sup>134</sup>.

*An excessively pedantic approach* by tax administrations was underlined in numerous contributions as regards both the form and number of declarations<sup>135</sup> and the means of payment<sup>136</sup>.

*The reimbursement of VAT* is a particularly long and complex procedure in the case of cross-border transactions and is liable in some Member States to take several months or even years<sup>137</sup>.

(iv) Reimbursement, subsidy or aid to the service recipient

*Authorisation for the reimbursement of medical costs* incurred in another Member State is only granted by national authorities under certain conditions and this may therefore discourage persons insured under social security schemes from turning to service providers established in another Member State. Persons who decide for various reasons (waiting times, change of residence for private or professional reasons<sup>138</sup>) to travel to a Member State other than his or her country of social security affiliation in order to receive medical treatment there, will not often be reimbursed<sup>139</sup>.

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<sup>132</sup> These obligations are the subject of a study by the Commission in preparation for simplification and modernisation proposals. The study is due to be completed at the beginning of 2003.

<sup>133</sup> The time it takes to issue a VAT number ranges from one week to six months, depending on the Member State.

<sup>134</sup> For example, where a service enterprise charges management fees to an enterprise established in another Member State for services which it has rendered, according to the classification used for this type of service the Member State of taxation will be the country of establishment either of the provider or of the client, so that there is a risk of double taxation if both of these criteria are applied to the same provision of services.

<sup>135</sup> For example, some Member States do not allow periodic VAT declarations to be submitted electronically. As far as summary declarations are concerned, one Member State accepts only hard-copy declarations handed over personally.

<sup>136</sup> Payments are generally effected by means of bank transfer. Some Member States stipulate that an account must be held with a local bank.

<sup>137</sup> This problem could be addressed by the Commission's proposal aiming to allow cross-border deduction (COM(1998)377), but this has still not been agreed by the Member States in the Council.

<sup>138</sup> For example, two persons residing in another Member State returned to their Member State of origin in order to undergo a surgical operation there without having received the authorisation

A large number of patients face difficulties when they apply for the direct billing to national insurance schemes of medical costs incurred in another Member State, whether these relate to consultations with physicians, dental treatment, hospital treatment, detoxification treatment or thermal cures in another Member State.

**Reimbursement of costs below the level granted in the country of social insurance affiliation** for treatment in another Member State also represents an obstacle to freedom to provide and use services.

**More favourable tax treatment** for services received from local providers is a major, and indeed discriminatory, hindrance to the provision of services. In some Member States, for example, the costs of professional training are tax-deductible only if the courses take place in the particular country concerned. Similarly, life insurance and additional insurance policies, as well as pension fund and investment fund contracts can be offset against tax only if concluded with local insurance companies.

(v) Public contracts and concessions

The objective of most public contracts<sup>140</sup> is the performance of services, e.g. architectural services, construction work, waste management or public transport. In the context of the award and execution of public contracts and other forms of partnership, however, enterprises may face a whole series of obstacles.

**Restrictive practices** such as single-tendering or preferential treatment during a direct award, some approval procedures or qualification systems and negotiated procedures<sup>141</sup>, could lead to the reservation of certain contracts to enterprises established in the Member State of the purchaser.

For example, local authorities decide to outsource their domestic-refuse collection and treatment or waste-water treatment activities by contracting these services out to a third party in the private or public sector without a prior call for competition or by granting long-term concessions which are afterwards renewed.

**Procedures for the award of public contracts**, the complexity and the lack of transparency of certain national rules for the award of contracts below the thresholds at which Community directives would apply, and certain practices of public

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of the competent authorities in their Member State of residence, who refuse to reimburse the costs of the operations.

<sup>139</sup> See the analysis developed in this respect in a study prepared for the Commission entitled: "Implications of recent case law on the co-ordination of healthcare systems", International Association for Mutual Assistance, May 2000, and in the report by the High Level Committee on Health entitled: "The Internal Market and Health services", 17 December 2001.

<sup>140</sup> This term is understood to cover all contracts in the wider sense which may be concluded by a public sector purchaser (whether in the traditional form of a public contract or a works or services concession), by which the latter purchases a service or entrusts a third party with the overall or partial management of a service, for which the third party assumes the associated risks.

<sup>141</sup> For example, these may concern contracts awarded on the basis of mutual trust (intuitu personae) to a local partner.

authorities<sup>142</sup> were identified as hindering operators from other Member States wishing to tender for public contracts.

*Certain contractual clauses and conditions governing the performance of contracts* are prone to making the submission of tenders by foreign operators more difficult.<sup>143</sup>

## 6. Difficulties relating to after-sales aspects of services

The period after the sale of a service may give rise to difficulties both in the context of relations between the client and the service provider and vis-à-vis third parties. The distinctive characteristic of services compared with goods derives from their intangible and complex nature. This gives rise, for example, to specific professional liability insurance schemes and makes the provision of proof and expert evidence in legal disputes a complex affair. Another feature of this stage is the absence of retailers or resellers who could take care of after-sales services on behalf of the original service provider.

- (i) Liability and professional indemnity insurance of service providers

*Professional liability insurance schemes vary markedly between Member States* across a wide range of professions, such as auditors, tax advisers and architects<sup>144</sup>. Civil liability systems are often specific to certain activities and are sometimes combined with general systems, which may result in a high degree of legal complexity. Differences between Member States may relate in particular to the possibility of limiting liability or the maximum period of liability.

*Service activities are often subject to specific professional liability insurance schemes* laid down by legislation or governed by rules or recommendations issued by professional bodies, relating in particular to compulsory insurance, the field of activities to be insured, the minimum amount of coverage, including the basis on which it is calculated<sup>145</sup>, or the body with which the insurance must be taken out. These schemes may vary markedly between Member States.

For example, the minimum insurance coverage for auditors varies, depending on the Member State, between € 70,000 and € 4,090,385<sup>146</sup>.

*These disparities may cause difficulties in the cross-border provision of services*, as Member States have an incentive either to impose their own insurance schemes on

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<sup>142</sup> For example, a lack of information for tenderers on the criteria according to which their abilities and the quality of their tender will be evaluated and on purchasers' practices regarding price.

<sup>143</sup> For example, an execution clause imposing on a company an obligation to employ a certain number of people registered on national training programmes may make access more difficult for companies from other Member States which would not be able to employ persons benefiting from similar training in the Member State of their establishment.

<sup>144</sup> For example, the health profession, legal professions, auditors, consultants, property registrars, private security services, employment agencies, designers, estate agents, banking and insurance services, stock brokering companies, hauliers.

<sup>145</sup> For example, turnover or number of associates covered.

<sup>146</sup> See study carried out for the Commission entitled: "Systems of civil liability of statutory auditors in the context of a Single Market for auditing services in the European Union", Price Waterhouse Coopers, January 2001.



service providers from other Member States<sup>147</sup> or to require proof of equivalent insurance coverage in the country of origin, which is difficult if not impossible to provide.

***Specific financial guarantee schemes are mandatory for certain service activities*** such as those of property registrars and estate agents. There is a very great disparity between Member States, as a particular activity may be subject in some Member States to an obligation to put up a guarantee or have a minimum amount of stock capital, whereas in the other Member States no obligation of this type exists. What is more, the amount concerned and the methods of calculation may differ markedly.

***Reconciling these liability, professional-indemnity insurance and guarantee systems*** is a particularly complex matter, especially in the context of cross-border service provision, e.g. where coverage of a specific risk is provided in one Member State under a financial guarantee scheme and in another under a mandatory professional-indemnity insurance scheme.

(ii) Debt collection

***Difficulties encountered in the context of debt collection***<sup>148</sup> are a problem which was the subject of complaints in numerous contributions and which is exacerbated by excessive delays in cross-border payments<sup>149</sup>: a number of enterprises use the payment delay as a kind of credit facility, as the interest charged on late payments is low and redress procedures are slow. Also, some chambers of craft trades may offer to intervene in the event of late payment, but this avenue is not open to service providers established in other Member States. One particular difficulty relates to the use of debt collection agencies and the protection of creditors' rights in the event of bankruptcy in other Member States.

An enterprise cannot use its debt collection agency if the latter is not established in other Member States: approval formalities for debt collection agencies differ between Member States and sometimes even from one region to the next, the provision of legal assistance may be the preserve of the legal professions and the costs of debt collection are not always for the account of the debtor.

(iii) Provision of after-sales services

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<sup>147</sup> In one Member State, for example, all construction sites, including those operated by service providers from other Member States, must belong to an insurance scheme covering a specific guarantee which does not exist in the other Member States.

<sup>148</sup> In particular the essential need to take legal advice locally.

<sup>149</sup> See Communication from the Commission: "Report on late payments in commercial transactions", OJ C 216, 17.7.1997, and the Report from the Commission entitled "Creating an entrepreneurial Europe - The activities of the European Union for small and medium-sized enterprises (SMEs)", COM/2001/0098 final; the latter report states that: "Late payments are the cause of one in four bankruptcies [...]. Surveys show that over 20% of European businesses would export more if they could obtain shorter payment periods from their foreign customers. SMEs are particularly affected by late payments", section 3.7.

*The organisation of a cross-border after-sales service* could be more difficult as it is liable to come up against specific technical problems<sup>150</sup>, or legal ones, particularly as it often requires personal intervention on the part of the service provider and/or the posting of his workers. In this case, after-sales services are hampered by problems which mean that the service provider or his staff have to travel to another Member State. For example, a boiler fitter who has installed a boiler in another Member State and wishes to carry out a repair on it faces the posting difficulties already described above<sup>151</sup>.

*Disparities between rules on guarantees* are liable to constitute another barrier to the cross-border provision of certain services. Some contributions highlighted difficulties in the construction sector stemming from the application of a mandatory guarantee system in the Member State in which services were provided.

(iv) Legal redress

*Legal uncertainty, the costs and slowness of procedures*, and the difficulty of using services or experts from other Member States in the context of cross-border legal proceedings were highlighted. It emerged from contributions that enterprises which were a party to legal proceedings outside their Member State of origin felt they were placed at a disadvantage compared with the opposing party, whose case was viewed more favourably by the national courts.

## **B. Non-legal barriers**

### **1. Lack of information**

A strong theme of the responses to the consultation was the difficulty in accessing information about the regulatory framework in other Member States. This was a concern for both service providers and consumers and was considered a major disincentive to cross-border activities. A second issue that became apparent from the consultation is the low level of awareness of the opportunities of the Internal Market and the rights of citizens and business under the principles of the freedom of establishment and the free provision of services set out in the EC Treaty.

(i) Lack of regulatory information

*Lack of information about applicable national rules and their interpretation* takes various forms and occurs at all stages of the business process. Numerous examples of such problems were given in the contributions to the consultation including lack of information on necessary authorisations (including planning requirements), qualifications requirements and other conditions attached to them, employment law, technical standards for the equipment and material to be used by the service provider, rules on commercial communications, selling over the internet, taxation and contract law. Particular problems occur in areas where there are questions of interpretation of

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<sup>150</sup> For example, a toll-free after-sales service number is not accessible outside the country of origin.

<sup>151</sup> For example, for the maintenance servicing of a lift, a whole series of administrative formalities have to be completed in relation to the workers posted (data on the workers, working hours, proof of payment of wages, translations, membership of a sickness insurance scheme, site plan and safety register etc.).

national laws resulting from unclear, inconsistent or unpredictable national jurisprudence.<sup>152</sup>

***Lack of knowledge of competent authorities, procedures and formalities*** hinders the cross-border provision of services. Lack of information and transparency are a particular problem in relation to identifying the appropriate competent authorities in another Member State, obtaining all the necessary forms and understanding the procedures. Some respondents complained that on occasion public authorities provided contradictory information and it was suggested that there was little co-operation between government bodies in the various Member States. The lack of availability of necessary forms on-line was also emphasised.

(ii) Lack of awareness of the principles of the Internal Market

The replies to the consultation suggest that business and consumers are often unaware of their rights in relation to the provision and use of services and that more information is needed on the principles of the free provision of services and the freedom of establishment as well as on the Internal Market in general. This situation, at least for SMEs, is explained by a lack of available resource to monitor and interpret legal information. At the most basic level, this lack of awareness restricts the ambition of individuals and companies, especially SMEs, to take advantage of the opportunities which the Internal Market offers and “to think European”.

***The right to challenge non-discriminatory measures*** seems to be largely unknown and many service providers still believe that the Internal Market only prohibits discrimination (or applies so-called “national treatment”). They seem to be unaware of the jurisprudence of the Court of Justice, according to which free movement principles preclude not only discriminatory measures but also non-discriminatory measures which are liable to prohibit, impede or otherwise render less advantageous cross-border activities. Replies to the consultation indicated that while there were some areas where companies experienced inconvenience or complications, domestic and foreign companies were subject to the same rules. They therefore considered these as business-related conditions which applied in a given country and which had to be accepted.

***The right to question proportionality*** is also not well understood. Even where respondents identified barriers, they rarely questioned whether the relevant measure was proportionate. This suggests lack of awareness that, even where a measure is motivated by the protection of an overriding objective of general interest (for instance public security), it must not duplicate requirements already fulfilled in the Member State of origin, and must be proportionate, i.e. appropriate to achieve the relevant objective, and not go beyond what is strictly required to achieve it.

***The right to receive services*** seems to be virtually unknown as a principle and the recipients of services, in particular consumers (for instance, tourists or patients), are often unaware that the Treaty also gives them the right to receive services without restriction. This includes the right to go to another Member State and use services

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<sup>152</sup> It was also stated that it was often impossible to obtain any clarification from one’s own authorities regarding the application of legislation in the other Member States.

under the same conditions as nationals. The need for information for consumers was also brought up in the context of the consultation. It was suggested that consumers need to be informed about services in other Member States in terms of quality, conditions and prices to enable them to take an informed view of services on offer and their rights. This would increase their confidence to buy services across borders<sup>153</sup>.

## 2. Cultural/language barriers

The question of cultural barriers, particularly concerning language, arose frequently during the consultation. Numerous businesses, and particularly SMEs, see these as a major constraint on selling into different markets and some consider this to affect service providers much more heavily than manufacturers of goods. However, it is essential to distinguish between those barriers which are often described as cultural, but which in fact directly or indirectly result from different regulatory environments, and others which arise as a result of customer preference and market conditions.

### (i) Barriers related to different regulatory environments

*Language barriers in proceedings with authorities* are sometimes described as cultural although they also arise from legal and administrative requirements. A number of replies to the consultation highlighted the difficulties arising from the use of local language with the authorities and cited as a barrier the necessity to provide translations of documents, often to be carried out by an official translator and certified by a notary. It was perceived as especially frustrating when this procedure was instituted in order to carry out checks which had already been made in one or more of the other Member States.

*Cultural barriers related to different administrative practices* were highlighted in a number of contributions. SMEs consider it particularly difficult to understand how to deal with national authorities in other Member States and are often in the position of beginning an authorisation process without knowing how and when it will end or how much it will cost.

### (ii) Barriers related to different market conditions

*Commercial and consumer habits including language* cause difficulties which arise from the need to know the language, values and habits of a specific country or region. Although this type of difficulty was frequently mentioned in the contributions, respondents to the consultation seemed to accept that these were part of the reality of doing business, and that they would have to take into account such factors wherever they carried out their activities, even within their home market.<sup>154</sup> However, the costs involved in overcoming language barriers can make cross-border services less attractive.

*Companies still think national* and often do not consider growth across national borders, even if their services are not specifically designed for the domestic market

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<sup>153</sup> See «Rapport franco-anglais», op cit.

<sup>154</sup> Commercial habits vary within markets and consumers are rarely a homogeneous group within a country or even within a region, though they can be identified as specific groups, according to, for example, age, level of education or the language they speak.

and could potentially be exported. This applies especially to SMEs. A lack of trust and a natural resistance to deal with habits in other Member States was highlighted in some of the contributions as a cultural barrier. As some companies put it, there is still a lack of “awareness of Europeanness” or of “thinking European”.

## II. THE COMMON FEATURES OF THE LEGAL BARRIERS

Despite their apparent diversity, the difficulties affecting the operation of the internal market have many points in common.

### A. The changing nature of the barriers

The inventory of difficulties shows that the abolition of the discriminatory features referred to in the 1962 general programmes and the elimination of the physical, technical and fiscal barriers referred to in the White Paper of 1985 have, in the field of services, been partly offset by the erection of new legal barriers or by the increasing impact of those which were already there but whose effects became evident only gradually as trade between the Member States developed.

This changing nature of the barriers appears in terms of the *content* of the regulations, which has to adapt constantly to differentiation and innovation in service activities, as explained in greater detail in the third part of the report.

However, the changes in the legal barriers are also apparent in terms of the *form* which they may assume. One common feature of many of the difficulties reported is that they derive not from national legislation but from other forms of intervention and regulation whose impact on the internal market is becoming more and more evident.

#### 1. Administrative practice

A study of a large number of the difficulties reported shows that the restrictions are no longer to be found in the body of the legal texts, but rather in the behaviour of certain administrations or in the way in which the administrative procedures are perceived or implemented, including through circulars or practical guides. Nevertheless, two types of problem are worthy of particular emphasis.

*The authorities' discretionary power of appreciation* under the authorisation system is behind many difficulties, as it makes the decision finally reached by the authority concerned unpredictable and may make it possible, under a veneer of neutrality, to take decisions which place providers from other Member States at a disadvantage.

For example:

- Certain regulations on distributive services lay down that authorisation for establishment is granted on the basis of general socio-economic criteria such as the needs of the existing businesses. Moreover, the authorisation procedure may involve bodies made up of competing operators already present in the area concerned. Such criteria, which are to be found in other sectors such as hotels and employment agencies, give the competent authorities a wide margin of appreciation and have the effect of placing the

established operators at an advantage compared with newcomers, albeit in a way which is less visible than a provision which is openly discriminatory;

- Discriminatory legislation governing services organising fairs and exhibitions was replaced, following infringement proceedings by the Commission, by an authorisation system based on a set of general criteria and regional implementing measures which, in practice, leave it open to the authorities concerned to take decisions which discriminate against other Community operators.

*The excessive formalism, length, procedural costs and lack of transparency* were emphasised in a large number of contributions. The accumulation of formalities and procedures, combined with a lack of transparency and sometimes over-zealous implementation, could have a particularly dissuasive effect on service providers from other Member States, since they are not familiar with the administrative culture of the other countries.

For example:

- administrations sometimes demand certificates which do not exist in the provider's country of origin, or else certified translations by an authorised translator in the country where the service is to be provided; or else the head of a building undertaking is required to go personally to the Chamber of Trades of the country of provision to obtain a certificate. In practice, all these requirements are clearly easier to fulfil for a national provider than for one from another Member State;
- in the field of customs, contributions have shown that the benefits of abolishing customs duties appear to have been somewhat mitigated by the complexity of certain remaining customs formalities affecting transport services<sup>155</sup>.

As an indication of how widespread this type of problem is, the Court has had to pronounce several times in recent years on these new practices, as well as on the discretionary interpretation<sup>156</sup> and the extremely cumbersome and costly nature of certain authorisation procedures<sup>157</sup>. In addition, moves to simplify administrative procedures are under way at national and Community level, particularly subsequent to the report by the Mandelkern Group<sup>158</sup>.

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<sup>155</sup> In particular, for instance, the problems deriving from the differing interpretations of the Customs Code by the Member States, and even between the authorities of one and the same country, leading to additional procedures and costs for hauliers and their customers.

<sup>156</sup> Judgments of 20 February 2001, Analir, Case C-205/99; of 12 July 2001, Smits and Peerbooms, Case C-157/99; of 15 January 2002, Commission v. Italy, Case C-439/99; of 22 January 2002, Canal Satellite Digital SL, Case C-390/99.

<sup>157</sup> See, in particular, the judgment of 3 October 2000, Corsten, Case C-58/98.

<sup>158</sup> Final report of the high-level advisory group, chaired by Mr Mandelkern, presented on 13 November 2001.

## 2. Regionalisation of the barriers

The inventory of difficulties shows that the legal barriers tend to appear more frequently at the level of local or regional rules and practices. They may involve new barriers introduced under the decentralisation, federalisation or regionalisation measures taken in several Member States over the last few decades, or else restrictions which had already existed for a long time but whose impact became evident as and when the other barriers at national level (discriminatory measures, physical, technical and fiscal barriers) were abolished.

Local or regional authorities play an important role in regulating service activities either through legislative power of their own or through local implementation of national rules. The interest of the regions and their active role in developing the service economy is confirmed by the clear support given by the Committee of the Regions to the "Internal Market Strategy for Services", which emphasises in particular the need to allow regional SMEs to operate in the internal market using the new technologies to the maximum<sup>159</sup>. The inventory of difficulties showed, however, that in some cases the requirements of the operation of the internal market are not sufficiently well-known at regional level, and this can lead to difficulties for providers from other Member States. Moreover, when a provider from another Member State wishes to develop his activities not just in a given region but throughout the national territory, the multiplication of procedures, specific provisions and contacts with the regional or local authorities could make such an operation more complex and costly than for national operators, who can adapt to them more easily.

For example:

- in one Member State, service activities such as debt collection are subject to an authorisation system for each province, which means that coverage of the entire national territory requires more than one hundred authorisations from different authorities;
- in some Member States, the lists of tourist sites which can be visited only if accompanied by a locally approved guide are drawn up by the local authorities according to differing criteria. In the absence of a list covering all the national territory, tourist guides and travel agencies in other Member States are confronted with a multitude of local lists which may cover specific museums or archaeological sites as well as entire cities or tourist zones;
- establishing distributive undertakings, hotels and restaurants is particularly affected by this regionalisation of the legal barriers, as in several Member States the authorisation criteria (including for town planning) are laid down and/or applied at local or regional level;
- in one Member State, many municipalities have introduced a tax on satellite aerials, which has had the effect of penalising consumers in particular as

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<sup>159</sup> Opinion of the Committee of the Regions already quoted, see in particular, § 10, 14, 16 and 27.

regards the reception of television channels from other Member States, and in particular by residents of foreign origin.

This trend towards the regionalisation of restrictions is illustrated by a recent judgment of the Court<sup>160</sup> in which it examined the compatibility with the principles of the free movement of services and the freedom of establishment of 14 different regional regulations in one Member State originating in six regions and dating mostly from the 1980s.

### **3. Implementation of Community instruments**

Because of the gradual development of secondary Community law over the last twenty years, a number of difficulties reported are directly related to the *acquis communautaire*.

*The problems of unsatisfactory application of the directives* lie behind a number of the difficulties reported. These problems may derive, in particular, from the presence in certain directives of provisions giving too much leeway to the Member States, or laying down derogations or optional requirements, or else minimum harmonisation clauses which allow stricter national rules to be adopted<sup>161</sup>. The Commission has already had occasion to note the negative effects of this latter type of clause<sup>162</sup>, and the Court has been obliged to limit its abuse by certain Member States<sup>163</sup>.

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<sup>160</sup> Judgment of 15 January 2002, Commission v. Italy, Case C-439/99.

<sup>161</sup> See also the "Report of the Business Environment Simplification task force Best", already quoted, page 61.

<sup>162</sup> Contained in certain directives on consumer protection; see the Green Paper on "European Union Consumer Protection", COM (2001) 531 final, paragraph 2.3.

<sup>163</sup> Judgment of 1 December 1998, Ambry, Case C-410/96.



The following were cited as examples in contributions:

- the directives on insurance, and in particular the widely differing application of the possibility given to the host Member States to take measures to protect the general good<sup>164</sup>;
- the directives on tax issues, and in particular the 6th Directive on VAT<sup>165</sup>;
- the directive on the transport of waste, for which the registration and authorisation system has been applied differently, making cross-border waste transport activities particularly complex in practice between four adjoining countries<sup>166</sup>.

*Issues relating to the implementation of the principle of the free movement of services* by means of instruments of secondary law were also sometimes reported<sup>167</sup>. It should be noted that, to tackle this kind of situation, the Court has in recent years, and notably in the field of health services, had to refer to the principle of the freedom to provide services laid down in the Treaty, rather than to an instrument of secondary law<sup>168</sup>.

For instance, interpretation of the conditions under which Member States apply Regulation 1408/71<sup>169</sup> caused problems for recipients of health services wishing to obtain reimbursement of treatment provided in another Member State<sup>170</sup>.

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<sup>164</sup> These difficulties are explained in the Commission Communication "Freedom to provide services and the general good in the insurance sector", C(1999)5046.

<sup>165</sup> See the "Communication from the Commission to the Council and the European Parliament - A Strategy to Improve the Operation of the VAT System Within the Context of the Internal Market", COM(2000)348 final.

<sup>166</sup> See the analysis of the Chamber of Commerce of the Grand Duchy of Luxembourg "Les autorisations de transport et de négoce de déchets en Saar-Lor-Lux", T. Theves.

<sup>167</sup> For example in the context of the implementation of Directive 96/71/EC of the European Parliament and of the Council of 16 December 1996 concerning the posting of workers in the framework of the provision of services (OJ L 18 of 21.1.1997, page 1), in particular in the case of postings of very short duration.

<sup>168</sup> In a series of judgments of principle (of 28 April 1998, *Kohll*, C-158/96, of 12 July 2001, *Smits and Peerbooms*, C-157/99, of the same day, *Vanbraekel*, C-368/98) the Court ensured, regardless of Regulation 1408/71 (already cited), the right of patients to obtain reimbursement of the cost of health services provided in another Member State. In the field of posting of workers, the Court was led, on the basis of application of Article 49 EC, to reiterate the need to assess to what extent the application of a national rule imposing a minimum wage on a service undertaking from another Member State employing cross-border workers is necessary and proportionate; judgments of 15 March 2001, *Mazzoleni*, Case C-165/98; see also judgments of 25 October 2001, *Finalarte*, Case C-49/98 and of 24 January 2002, *Portugaia Construções*, Case C-164/99.

<sup>169</sup> Regulation (EEC) No 1408/71 of the Council of 14 June 1971 on the application of social security schemes to employed persons and their families moving within the Community, already cited.

<sup>170</sup> See the study carried out for the Commission "Implications of recent case on the co-ordination of health care systems", already cited.

In the area of contract law, problems of coherence and of the uniform application of secondary Community law were emphasised by the Commission<sup>171</sup> and by those parties consulted<sup>172</sup>. Problems of coherence concern, for example, the different treatment of similar situations in several Community acts. The absence of coherence in the definitions used in secondary Community acts concerning such terms as "damages" or "contract", may create problems for the uniform application of such acts in Member States. Such problems may also result from transposition by Member States who make reference to different pre-existing rules of a general nature which form part of their legal systems.

Certain directives contain, for example, different definitions of the term "damages"; other directives use this term without defining it<sup>173</sup>.

#### 4. Collective non-government rules

A number of the difficulties reported come not from regulations issued by the public authorities, but from the disparity between standards adopted by non-public bodies in a Member State, such as professional associations, sports federations, the social partners drawing up collective agreements, or interested parties or groups drawing up codes of conduct or collective rules<sup>174</sup>.

Service activities are particularly affected by this kind of disparity, since the regulated professions are traditionally regulated by professional bodies at national level. The use of codes of conduct is tending to spread to other fields such as information society services, and the current debates on new forms of governance may lead to more frequent use of such codes, as well as co-regulation and other ways of putting economic regulation on a contractual basis.

– For example, codes of conduct adopted by certain professional bodies which prescribe quantitative limits on access to the profession or impose limitations on the types of services which can be offered, may cause difficulties for professionals of other Member States wishing to establish in the country in question or to offer their services there.

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<sup>171</sup> See Communication from the Commission to the Council and European Parliament on European contract law, COM (2001) 398 final, 11.7.2001, p11 and 12.

<sup>172</sup> See the summary by the Commission services of the results of the consultation on [http://europa.eu.int/comm/consumers/policy/developments/contract\\_law/index\\_en.html](http://europa.eu.int/comm/consumers/policy/developments/contract_law/index_en.html)

<sup>173</sup> For example, the concept of "damages" in the 'Package travel Directive', (which contains no definition of this term), has been interpreted by the Court of Justice in the light of this directive only, whereas, the Advocate General suggested interpreting it by taking into account other Community Acts.

<sup>174</sup> The Court has already had to pronounce on collective rules. The first judgment dates from 1974 (*Walrave*, Case 36-74, point 18), but the Court has been called upon to apply this case law in several cases in recent years: judgments of 15 December 1995, *Bosman*, Case C-415/93, point 83, and of 11 April 2000, *Deliège*, Case C-51/96 and C-191/97, point 47, including a regulation of a professional association of lawyers (judgment of 19 February 2002, *Wouters*, Case C-309/99).

## 5. The conduct of operators

This concerns the practices of individual operators which have the effect of making their activities or selling prices and conditions territorial. In particular, it may involve the refusal to sell to customers from other Member States for the sole reason that they are not resident in the country of the operator. Such practices penalise service users who wish to buy from providers in other Member States, and in particular consumers. Such behaviour can only be the result of legal barriers which make certain cross-border activities extremely risky. In certain cases, however, where such risks are fewer, it is more a reflection of a commercial resolve to break the internal market down into several national markets<sup>175</sup>.

One Member State, for instance, made a specific contribution stressing that it was impossible for its citizens to obtain access to encrypted television channels available in other Member States, because the channel operators refuse to sell or rent decoders to persons not resident in the countries where those channels are on offer.

### B. The horizontal nature of the barriers

An analysis of the wide range of legal barriers reported shows that many of them are common to a large number of widely varying sectors of activity. Three types of horizontal problems can be distinguished.

#### 1. Application of a single system to establishment and the provision of services

A large number of services encounter the same problem: the Member State of destination treats the service provider as if he were established on its territory, and hence subjects him fully to its legal system.

For example:

a patent agent who occasionally provides a service in another Member State is subject to an obligation to obtain authorisation from the latter, to meet the professional qualifications required there, and to enrol in a specific register; or a landscaping architect who is temporarily providing a service in another Member State is subject to the obligation to be a member of the national association and to comply with all the professional rules of that country.

The inventory of difficulties, in particular those relating to the distributive stage of services (stage 4 in the economic chain), shows that this kind of problem may assume various forms such as the following:

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<sup>175</sup> Although this kind of conduct must be examined in the light of the rules of competition, the Court has already opened up the possibility of examining the compatibility of such conduct with the freedoms of the internal market; judgment of 8 June 2000, *Angonese*, Case C-281/98, on Article 39 EC; see also the judgment of 13 December 1984, *Haug-Adrion*, Case C-251/83 on the compatibility with Article 59 of the EC Treaty of contractual clauses laid down in the general conditions of an insurance contract.

- an *obligation to become established* in the country in which the service is provided, whereby such establishment involves the operator becoming subject to all the rules of that country;
- a *system of authorisation* (or registration) by the authority in the country in which the service is provided, such authorisation being subject to compliance with all or some of the rules of that country;
- *systematic subjection of operators to the rules* of the country in which the service is provided (regardless of the existence of an establishment requirement or an authorisation system).

The objective is the same in all cases: to put the situation of a provider established in another Member State on the same footing as that of an operator in the Member State in question, so that he can be systematically made subject to the latter's regulations. Contrary to the case law of the Court<sup>176</sup>, this approach amounts to reducing the principle of the free movement of services to a simple obligation not to discriminate.

## 2. Legal uncertainty surrounding freedom of establishment and the free provision of services

A wide range of cross-border services are affected by a high degree of legal uncertainty as to their legality, since this will depend on a case-by-case assessment by the national authorities of the country in which the operator wishes to exercise his activity. This legal uncertainty becomes evident in two ways:

- national regulations are often *unclear or ambiguous* as to whether they might be applicable to providers established in another Member State. In many cases, the rules imposing obligations on service providers do not explicitly circumscribe their territorial scope, and in particular whether they apply only to providers established on the territory of the Member State in question. Such a situation leaves a margin of interpretation to the national authorities and will cause the provider to seek specific legal assistance or clarifications from the national authorities, or even their "green light";

For instance, a significant number of the draft national laws on information society services notified<sup>177</sup> to the Commission in 2001 revealed this type of problem.

- Certain national rules subject the provision of services or freedom of establishment to systematic compliance with a *criterion or test* to be assessed case by case by the authorities, with the outcome being difficult to predict.

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<sup>176</sup> "A Member State may not make the provision of services in its territory subject to compliance with all the conditions required for establishment and thereby deprive of all practical effectiveness the provisions of the Treaty whose object is, precisely, to guarantee the freedom to provide services", judgment of 25 July 1991, *Säger*, Case C-76/90, point 13.

<sup>177</sup> Pursuant to Directive 98/48/EC of the European Parliament and of the Council of 20 July 1998 amending Directive 98/34/EC laying down a procedure for the provision of information in the field of technical standards and regulations, OJ L 217 of 5.8.1998, page 18.

In one Member State, for instance, the use of an analytical laboratory in another Member State is possible only if that type of analysis *"cannot be carried out"* on its territory. It may involve criteria such as *"the impact on existing businesses"* (distributive services), *"the need for placement"* (agency services for the placing of artists), *"the general good"* (financial services), or *"aptitude"* or *"equivalence"* (regulated professions).

In practice, the effect of this legal uncertainty is to reverse the roles, since an operator who wishes to provide his services in another Member State finds himself in the paradoxical situation of having to invoke and justify the principles of the free movement of services and freedom of establishment, whereas normally, in line with the case law of the Court, it would in fact be for the national authority to justify any exceptions to those principles, whereby such exceptions may not at any event be applied in a general and systematic fashion<sup>178</sup>.

### **3. Application of the same type of requirements in different fields**

An analysis of the inventory reveals that certain types of restriction recur in a large number of sectors or service activities (even though the details may vary), and in particular the following: systems of authorisation, declaration, registration and inscription with a professional body or a chamber of trades, quantitative limits (numerus clausus, quotas, surface areas, etc.), territorial limits to the provision of services, rules applicable to the posting of workers in the framework of the provision of services in another Member State, the rules governing multidisciplinary activities, bans or limits to commercial communications, rules governing the fixing of prices, rules on professional liability, professional insurance and financial sureties or guarantees; certain aspects of the rules on contracts; the collection of debts; the rules on taxation.

#### **C. The common origin of barriers**

Despite the apparent variety of the legal barriers, the reasons behind them are very often the same and can be explained by three factors.

##### **1. Lack of mutual trust between Member States**

Many of the difficulties reported can be attributed primarily to a lack of trust of certain authorities in the quality of the legal systems of the other Member States.

Systematic application of the rules of the country in which the service is provided, the simple evocation of "general good" objectives to justify obstacles, without verifying the equivalence of the protection offered in the country of origin or the proportionality of the restriction, the subjection of operators from the EU to the same system as that

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<sup>178</sup> The consultation showed that this reversal of roles also appears in the application of the directives on insurance: whereas these provide the possibility, in certain cases, for the host Member State to apply its rules only when they are necessary for reasons of the general good, some Member States notify to the authorities of the country of origin an entire general list of rules which must be systematically complied with by a provider established on the territory of the latter. See the Communication "Freedom to provide services and the general good in the insurance sector" already cited.

applied to "foreign" undertakings from third countries, the presumption of circumvention of national rules by any cross-border service, more frequent checks on providers from other Member States - all these reveal a degree of automatic suspicion of services from other Member States and amount to considering that the protection of the general good and the regulation of service activities are not objectives shared by all the Member States of the European Union.

This lack of mutual trust may derive from ignorance of the implications of the principles of freedom of establishment and the free provision of services, but also from a lack of transparency and administrative co-operation between the Member States or, in certain fields, from a lack of harmonisation of the national rules, reflected in an excessive disparity between the levels of protection of the general good guaranteed by the national systems.

## 2. Resistance to modernisation of the national legal frameworks

A number of legal barriers can be attributed to the fact that the Member States have not really taken into account the requirements of the internal market in services. The fundamental principles of the Treaty, the importance attached to them by the Court, and the follow-up to the ambitious programmes of 1962 and 1985, have not always resulted in the adjustment of national legislation which might have been expected. On the contrary, as explained above, when the legal systems evolve it may be in the direction of confirming legal barriers or establishing new ones, rather than of abolishing them.

A survey<sup>179</sup> reveals that 42% of heads of undertakings active in the field of services consider that the regulations applicable to them are not in line with the facts on the market, or are slightly outdated, or even totally outdated<sup>180</sup>, with the rate being higher for the services sector than for all sectors of activity together (36.6%)<sup>181</sup>.

There may be several explanations for this reluctance to modernise:

- ***The weak monitoring of the judgments of the Court*** by the national authorities does not always allow them to identify the need to modify their national legislation. The existing mechanisms in the national administrations appear to concentrate on cases affecting their own country or, upstream, on the need to draw up written observations on a case concerning another Member State. Downstream, however, it seems that few Member States engage in any real active and systematic monitoring of all the judgments concerning other Member States in order to assess the needs in terms of adjusting their own legislation<sup>182</sup>. This explains why many of the problems

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<sup>179</sup> "Services Sector in Flash Eurobarometer 106", Flash Eurobarometer 106 (Special Targets), survey to monitor the single market, September 2001, conducted on behalf of the European Commission, attached to Scoreboard No 9, 19.11.2001,  
[http://europa.eu.int/comm/internal\\_market/en/update/score/busisum9.htm](http://europa.eu.int/comm/internal_market/en/update/score/busisum9.htm)

<sup>180</sup> The percentage being highest in France (60%) and lowest in Ireland (23%).

<sup>181</sup> Flash Eurobarometer 106 already cited.

<sup>182</sup> The monitoring is sometimes limited to informing the departments of the administration likely to be concerned.

reported have in fact already been the subject of judgments of the Court of Justice condemning similar measures or practices;

- *Treatment on a case-by-case basis and the relative effectiveness of penalties for infringements* of the law of the internal market help to give some national authorities the impression that an adjustment of their regulations is not indispensable as long as they are not directly and explicitly questioned by the Commission or the Court.

### **3. Protection of national economic interests**

Despite the established case law of the Court, according to which "*measures constituting a restriction of the free provision of services cannot be justified by objectives of an economic nature such as the protection of national undertakings*"<sup>183</sup>, it has to be pointed out that, notably with regard to certain preparatory Parliamentary work, a number of the difficulties reported show that the defence of purely national interests still remains fairly firmly anchored in certain Member States.

## **III. THE IMPACT OF THE BARRIERS**

### **A. The knock-on effects on the entire economy and on European competitiveness**

*Barriers will affect all services directly or indirectly.* Part 1 of this report has shown that Internal Market barriers impact on each of the six stages of a service providers' business process, which is also referred to as the "economic chain". Every service provider considering expansion into another Member State is likely to face one or several obstacles and will also be affected by barriers that his service suppliers encounter. This is because, in order to create, promote and distribute his service, the provider relies on a multitude of other services. This interdependence of services means that a comprehensive approach is necessary to evaluate the overall impact of barriers. This part of the report will examine the role of services in the economy, the interdependence of services, the potential for cross-border growth in services if barriers were removed and make a first evaluation of the impact on the economy as a whole that will be further developed during the course of the second phase of the strategy. The Commission will carry out work in 2002-2003 to develop the economic impact analysis with the aid of economic experts.

#### **1. The key role of services in the economy**

*Services play a key role in the EU economy*, accounting for almost 70% of jobs<sup>184</sup> and GDP in most EU countries<sup>185</sup>. The growth of services has exceeded overall

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<sup>183</sup> Portugaia Construções judgment already cited.

<sup>184</sup> This share is even higher if the number of employees in the manufacturing-industry engaged in services activities is taken into account. For example, a study from the Confederation of Swedish Enterprises indicates that estimates go up to 85% of persons employed. "Svensk Internationell Tjänstehandel – nuläge och möjligheter", Rapport inom projektet Internationaliseringen av Svenskt Tjänsteföretagande, Svenskt Näringsliv, O. Erixon, 2001. Another study carried out for the European Commission, indicates that this share is also increasing in privatised utilities (e.g. electricity companies) which are shifting from traditional industrial activities to being flexible

economic performance for decades, and so they account for an increasing share of the EU economy. It is clear that the major part of the potential for future job creation will come from the service sector as job creation in services is exceeding overall job growth<sup>186</sup>.

However, notwithstanding that manufacturing industry statistics are probably overestimated, due to the integration of services in manufacturing, the relative difficulty in classifying services, and practical difficulties in identifying basic flows in services, the importance of services in transactions does not bear relation to their importance in the economy. In 1999 services still only represented 21.6% of all commercial transactions in the EU, of which 11.9% was within the EU 15. Moreover, the statistical trend is towards a decrease in this share of services (they constituted 22.8% in 1992<sup>187</sup>). This gap can be partially explained by the existence of a functioning Internal Market in the field of goods but not in that of services. In the area of services, market participants have a tendency to rely on direct investment overseas and mergers, rather than cross-border trade; more than 40% of foreign direct investment derives from the area of services, of which 20.59% is intra-community, as opposed to 44% and 27.6% respectively for goods, with 15% unattributed<sup>188</sup>.

The potential for growth in services transactions is consequently significant. Even if the contribution of services to growth in productivity remains difficult to measure, it is probable that greater competition between operators from different Member States would lead to an increase in productivity.

***Services are to be found in all areas of the modern economy***, including in what might be regarded as “traditional” manufacturing sectors. For example, some car manufacturers now offer financial, leasing and rental services, consulting, training and fleet management services, or road assistance and recovery services<sup>189</sup>; and electronic hardware producers are increasingly offering custom-made software services<sup>190</sup> for their products<sup>191</sup>. At the production stage itself, the automobile

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service-oriented companies. “The Effects of the Liberalisation of the Electricity and Gas Sectors on Employment”, ECOTEC research and consulting, 2000.

<sup>185</sup> The proportion of services in the US economy is still higher, accounting for about 74% GDP, although the EU is catching up. See, for instance: Commission report of 2002 on competitiveness (SEC (2002) 528 of 21 May 2002); Communication from the Commission on Productivity: The Key to Competitiveness of European Economies and Enterprises (COM (2002) 262 final, 21 May 2002); “Dienstleistungsreport 2000”, Preussag AG, together with the Institut der Deutschen Wirtschaft, Köln, 2000, “Croissance et emploi dans le secteur des services, une analyse comparative”, Bureau Fédéral du Plan Belgique, working paper 6-00, 2000.

<sup>186</sup> “The rise of the knowledge-based society will shift employment demand towards higher skill levels”. Quote from “Innovation in the Service Sector – Selected Facts and Some Policy Conclusions”, Zentrum für Europäische Wirtschaftsforschung, G. Licht, G. Ebling, N. Janz, H. Niggemann, 1999, p. 5.

<sup>187</sup> Source: “EU international transactions”, Eurostat edition 2001.

<sup>188</sup> Source: “EU Foreign Direct Investment”, Eurostat 2000.

<sup>189</sup> See “Job Revolution, Wie wir neue Arbeitsplätze gewinnen können”, P. Hartz, 2001 and “Grundlagen der Automobilwirtschaft”, W. Diez, 2001

<sup>190</sup> For example, consumer electronics companies are offering an increasing range of video-game software or are investing in the entertainment (notably film) industries.

<sup>191</sup> Further examples are manufacturers of health care products who are increasingly offering consulting services to hospitals, producers of foodstuffs providing consulting on food safety and telecommunications operators who are generating considerable revenue from offering telephone assistance to software users.



industry uses IT, design services or quality control services, for instance. Industry is thus very dependent on services and their quality. Many of these services are hidden in the official statistics for manufacturing companies<sup>192</sup>. This “bundling” of goods and services and efficient integration of service inputs allows business to provide differentiated products more adapted to customers’ needs<sup>193</sup>. This in turn improves the productivity, competitiveness, sales and, ultimately, the profitability of firms.<sup>194</sup>

A recently published U.S. study illustrates the increasing importance of services for the value-added of major corporations:

*“What company is the world’s largest service business? Disney? Citibank? American Express? Based on several measures the answer is actually IBM or General Electric – two corporations far better known for their products than their services.”*<sup>195</sup>

For example, manufacturers of quality goods have always attached great importance to the issue of client service. This is particularly true in the case of sophisticated engineering products, where extensive consultation is often needed at the design stage, in order to meet the exact customer requirements. Customer service continues in the form of training, maintenance, “teleservice” via the internet, hotline support, and may extend to financing and “build and operate” models for large infrastructure projects.

Surveys undertaken in Germany in the engineering sector show that revenue derived from service functions is growing. About 10% of engineering companies derive more than 50% of their income from service activities. In the past these services were usually included in the final price of the product, but there is an increasing tendency to charge for them separately.

Leading edge goods manufacturers frequently derive their competitive advantage from buying in advanced information technology services. Sometimes the know-how for developing products with embedded intelligence is available in-house, but frequently it is provided by specialist providers of computer related and communications services. Examples can be found in the automotive sector, where engine management systems, automatic braking systems and navigation systems are increasingly common. Other traditional engineering products, like cranes and machine tools, are also frequently equipped with systems for remote monitoring and diagnostics, in order to provide maximum availability, and reduce the cost of maintenance.

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<sup>192</sup> For example, an OECD report concluded that the distinction between manufacturers and service providers is no longer feasible. Likewise a Danish study noted that 31% of those Danish companies interviewed and officially listed as manufacturers considered themselves to be service providers. “The service economy”, OECD, Science Technology Industry Forum, Paris, 2000; “Svensk Internationell Tjänstehandel – nuläge och möjligheter”, op cit.

<sup>193</sup> See “Dienstleistungsreport 2000” op cit; “Marktpotentiale für Unternehmensbezogene Dienstleistungen im Globalen Wettbewerb”, Institut für Wirtschaftsforschung, 1998.

<sup>194</sup> See “Stratégies tertiaires des exportateurs industriels. Économies et sociétés. Les services de l’an 2000”, Tome XXXIII N°5, mai 1999: p. 17-43; “Trading Services in the Global Economy”, L. Rubalcaba-Bermejo, J. Bryson, 2002.

<sup>195</sup> “S-Business: Defining the services industry”, Association for Services Management, S.W. Brown, B.A van Bennekom, K. Goffin, J.A. Alexander, 2001, p.4.

At the same time, manufacturers have been outsourcing the service functions which they do not regard as part of their core activities to service providers who can provide them more efficiently. There is a close inter-dependency between goods manufacturers and the companies that supply services to them. This has not only had consequences for the structure of the industrial sectors, but has also changed the way in which manufacturing companies organise themselves internally.

The extent to which service functions are provided by manufacturing companies is often obscured by published statistics. Even though their primary business is manufacturing, several leading companies in Europe employ tens of thousands of people in their services divisions.

***Demand-based factors contribute to the growing role of services in EU economy.***<sup>196</sup>

There is increasing demand: for specialist business services due to outsourcing; for services combined with goods; for knowledge-based and leisure-related services; and for a variety of services as a consequence of demographic changes<sup>197</sup> such as health and personal support services<sup>198</sup>. This has resulted in an ever growing number of different services ranging from more traditional service sectors such as transport, retail distribution, telecommunications, tourism, health and financial services to more recently developed services such as business services in the areas of environmental/waste management, energy conservation, management consulting, data processing and technical analysis and testing, to name but a few.

## **2. The interdependence of services**

*Services are intricately intertwined* since they are used often in combination in each stage of the economic chain of a service provider's business activity. For example, a retailer provides services to manufacturers and a bundle of services to the final consumer including in-store catering and after-sales services. The retailer relies in turn on numerous other services at each stage of the business process ranging from establishment, via the use of inputs, promotion, distribution and sales to the after-sales stage. This is illustrated below.

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<sup>196</sup> See "Innovation and Productivity in Services: State of the Art, OECD, D. Pilat, 2001; "The Service Sector in the UK and France: Addressing Barriers to the Growth of Output and Employment" op cit.

<sup>197</sup> Such as an ageing population and higher participation of women in the labour force.

<sup>198</sup> See for example a report carried out for the European Commission "Services for Individuals and Households in the European Union", Institute for Employment and Research, 2001.

### Economic chain for a retailing service

<u>Establishment</u>	<u>Use of inputs</u>	<u>Promotional activities</u>	<u>Distribution activities</u>	<u>Sales activities</u>	<u>After sales activities</u>
<b><u>Services used</u></b>					
Legal	Legal	Legal	Legal	Legal	Legal
Management consulting	Insurance	Advertising	Transport/Delivery	Tax advising	Returns management
Tax advising	Banking	Media sales	Leasing	Price management	Guarantees management
Real-estate brokering	Management consulting	Sales promotion	Rental	Customer Database-management	Customer relations
Shop designing	Purchasing	Sponsorship	Logistics	Payment	Debt recovery
Construction Architectural	Logistics	Printing	Environmental/waste management	Credit	Environmental/waste management
Engineering	Wholesaling	Web design	Customer base management	Invoicing/Accounting	
Environmental and planning	Transport	Market research	Franchise planning	Auditing	
	Leasing			Rental and leasing	
	Labour				
	Recruitment				
	Data processing				
	Inventory management				
	Yield management				
	Security				
	Pricing management				
	Invoicing/Accountancy				

***Barriers to one service will trigger knock-on effects on other services*** because of this interdependence. For example, as has been highlighted in the consultation, a retailer established in one Member State and wanting to establish in a number of other Member States would normally wish to use in those other countries the services of the real estate agents, shop designers, architects, engineers, construction companies, banking and insurance companies with whom he works in his Member State of origin. This would enable him to gain from the long-standing co-operation with his existing service suppliers as well as to exploit efficiency gains and economies of scale. However, there are numerous barriers to the provision of these services in other Member States, which will in turn make the establishment of the retailer more costly and onerous<sup>199</sup>.

***Barriers will multiply throughout the economic chain.*** To take the same example of a retailer, he may discover that he cannot use as an input the temporary employment agency he used to work with, his promotions can no longer be provided for by his usual sales promotion agency, his road haulage company cannot provide him distribution services and his accountant cannot design and verify his sales activities. All these services either cannot be offered across borders easily (or at all) because of problems at one or several stages of their own economic chains<sup>200</sup>. As a result the

<sup>199</sup> For example, architects and engineers might face problems concerning professional qualifications; construction companies concerning posting of their workers; insurance companies concerning different contract and taxation legislation.

<sup>200</sup> See the description of barriers in part 1. The temporary employment agency may not be able to provide services without being established in the countries concerned, the sales promotion agency may not be familiar with the detailed legal requirements for sales promotions, the road haulage

retailer will at each stage of his economic chain be obliged to use different services in other Member States and will suffer significant efficiency losses as well as higher costs.

***Barriers to services in the Internal Market require a horizontal impact assessment*** in order to take into account all the knock-on effects which they produce on a multitude of activities, in line with the Commission Communication on impact analysis<sup>201</sup> which foresees an integrated method of analysis of economic, environmental and social consequences. The latter includes, amongst other things, the impact on public health and safety and consumer rights<sup>202</sup>. As regards economic consequences, an analysis which only deal with effects on one particular activity or a given sector would be one-sided and misleading. It is necessary to use an evaluation methodology which includes not only the impact of a difficulty listed in the economic chain in relation to a particular service up to the final consumer, but also includes the impact of that problem on the economic chain of other linked activities. Such a dynamic and qualitative evaluation will be undertaken by the Commission services, with the assistance of specialist economists, during the second phase of the Internal Market Strategy for Services<sup>203</sup>.

### **3. The demand for cross-border services**

***Demand for cross-border services is steadily increasing***<sup>204</sup>. Demand for services is not limited to national markets. However, despite the predominant role of services in the economy, the absolute level of cross-border service provision is less than trade in goods. Since, over the past decade, real (i.e. adjusted for inflation) turnover growth of European enterprises has been export-led<sup>205</sup>, this suggests that there is considerable potential for further economic growth driven by exports of services.

***Globalisation and the linkage between service firms and their multinational clients*** is one well-documented reason for such growing demand in the field of business services. Multi-national service providers, as well as manufacturers which have increased their international operations, have encouraged the service providers they use to support these operations either by export or secondary establishment.<sup>206</sup>

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firm may have difficulties using his vehicles, the accountant's firm may not have the required legal form etc.

<sup>201</sup> COM(2002)276 final

<sup>202</sup> COM(2002)276 final

<sup>203</sup> It should be noted that the utility of such a horizontal and dynamic evaluation is also recognised by the OECD: see "Quantification of Costs to National Welfare from Barriers to Services Trade, a literature overview" OECD 2001

<sup>204</sup> Service exports from EU countries increased by 7.3% between 1990 and 1999 although this was not as rapid as the increase from the US and especially China and Japan. Since 1990 Western Europe has lost some 8.6 percentage points of its world market share. See for example recent Swedish and Danish studies: "Svensk Internationell Tjänstehandel – nuläge och möjligheter", op cit and "Internationalisering af Service – Potentialer og Barriere, Erhvervsministeriet, 2001.

<sup>205</sup> See "SMEs in Europe", Observatory of European SMEs, European Communities, No2 2002; "Service Internationalisation – Characteristics, Potentials and Barriers" op cit.

<sup>206</sup> A German study on technical services highlights that the increase in cross-border trade of services is closely related to the emergence of multinational firms, which choose those service providers with the best price/quality, offer, independent of nationality. "Marktzugangsregelungen/Berufszugangsregelungen für Technische Dienstleistungen und deren Auswirkungen auf die Internationale Wettbewerbsfähigkeit", Institut für

***Specialisation and differentiation in business services*** that may be scarce in certain Member States is also contributing to cross-border demand. The increasing need to look beyond national markets to recruit specialist and skilled labour, in particular in hi-tech and knowledge-based services, is well documented<sup>207</sup>.

***New information and communications technologies*** will further enhance the trend towards internationalisation of services. New technologies allow knowledge-based services to be provided at a distance and facilitate the import and export of services without the need for foreign direct investment.<sup>208</sup>

***Increased mobility and the higher disposable income of consumers*** combined with more information, thanks to new information technologies, have all resulted in increasing cross-border demand for a range of consumer services including tourism, health and leisure services.

***The resulting potential for cross-border services*** cannot, however, be fully realised because of Internal Market barriers<sup>209</sup> and resulting costs and their chain effects throughout the economy.

***The liberalisation of electricity and gas markets*** is likely to result in an increase in cross-border demand, not only in relation to energy, but also as regards ancillary services, such as lighting, heating, cooling and energy-efficient power generating systems. These services will be closely linked to the actual delivery of gas and electricity and thus provide a further example of the complex interaction between services. However, this potential will not be capable of full exploitation unless barriers to the provision of the whole range of services are removed.

#### **4. The costs of barriers to services**

***Barriers result in ex-ante compliance costs*** on cross-border service use and provision. The barriers identified in Part I of this report give rise to a series of compliance costs. A company seeking to enter a market, either through establishment or via cross-border service provision, will have to rely on complex legal assistance to examine whether it can roll out its operations into the new market or whether and how parts of its business model will have to be altered.

***Ex-ante compliance costs multiply throughout the economic chain.*** The examples in the field of retailing below show that ex-ante compliance costs are considerable even when they concern only one or two stages of a service provider's economic chain.

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Wirtschaftspolitik an der Universität zu Köln, M. Fredebeul-Krein, A. Schürfeld, Oktober 1998.

See also "Trading Services in the Global Economy", op cit.

<sup>207</sup> See for example "Employment in Europe 2001: Recent Trends and Prospects", DG Employment and Social Affairs, European Communities, 2001

<sup>208</sup> According to the British Government, the increasing range of services that can be provided at a distance is also bringing to light new barriers which potentially limit trade and competition in the EU. See "Realising Europe's Potential, Economic Reform in Europe", HM Treasury, 2002.

<sup>209</sup> An example of the lost potential can be found in a survey amongst business services providers that was conducted on behalf of the European Commission, the majority of the respondents replied that they would be likely to increase their sales of business services in other EU Member States, if regulatory barriers were removed. "Barriers to Trade in Business Services"; op cit.

However, since barriers normally affect each of the stages of the business activity, the overall level of ex-ante compliance costs is much higher.

#### **Examples of ex-ante compliance costs**<sup>210</sup>

A major fixed-store retailer had to allocate a senior manager full time for 8 months (costing €200,000) to research necessary adjustments to the selling strategy (stage 5 of the economic chain) of the group to comply with legislation in another Member State, whose market it wished to enter.

Prior to the adoption and transposition of the e-commerce directive a mail-order company, considering marketing and selling via a web-site, was charged €25,000 by a law-firm for advice on how to comply with the different rules throughout the EU relating to advertising, including product specific rules (stage 3) and contracting (stage 5).

A retail bank paid a law firm €19,500 to assess how it would need to alter its advertising (stage 3) of a particular investment service in two other Member States.

A cosmetics distance-selling company had to place one of their full-time legal staff for six months in another Member State to assess how the company's retailing model would need to be modified to comply with that Member State's rules. The company finally decided not to enter the market given the radical alteration to their business model that would have been required.

***Ex-ante compliance costs are not linked to the size of the enterprise:*** examining national legal requirements and administrative practices and assessing the possibility of offering or using a service normally requires almost the same up-front investment in legal advice whether the company is large or small<sup>211</sup>. Moreover, ex-ante compliance costs are sunk costs which have to be paid before a company can even decide whether or not to enter another Member State's market.

***Small firms will find ex-ante compliance costs prohibitive*** yet micro- or small enterprises play a key role in the service sectors<sup>212</sup>. Average firm sizes in the European retail sector suggest that ex-ante compliance costs are disproportionately high compared to turnover and would, in all likelihood, dissuade an average sized European retailer from even considering an Internal Market strategy.

#### **Average firm size in the retail sector (EUR 13, 1998)**<sup>213</sup>

<sup>210</sup> Examples were provided in the context of the consultation for the Services Strategy by service providers and law firms advising them.

<sup>211</sup> For example, a German study indicates that external costs of legislation hit SMEs disproportionately. "Externe Kosten von Rechtsvorschriften, Möglichkeiten und Grenzen der Ökonomischen Gesetzesanalyse, Institut für Weltwirtschaft an der Universität Kiel, H. Dicke, H. Hartung, 1986. See also "Regulation and Small Firms", progress report from the Better Regulation Task Force, 1999.

<sup>212</sup> This is common to all service sectors. See "Major Trends and Issues", OECD, M. Edwards, M.Crocker, 2002.

<sup>213</sup> The averages are based on information in 13 Member States. Germany and Greece are excluded because relevant data was not available. "Distributive Trade Statistics: Retail Trade in Europe", Statistics in Focus: Industry, Trade and Services., Eurostat, J. Hubertus, Theme 4-40, 2001.

average number of employees: 3.2

average annual turnover: €582,207

In 1998, for those Member States providing data, around 90% of retailing firms employed fewer than five people. This size class covered 73% of retail businesses in Ireland (the lowest percentage) and as many as 94% of companies in Italy.

**Organisational compliance costs are an additional burden** over and above the ex-ante compliance costs, that arises when a company is obliged to change its optimal strategy in each stage of its economic chain. There are both static costs in each stage of the economic chain and dynamic costs which result from the knock-on effects throughout the economic chain as the company redesigns a new business model for each market it enters. Organisational compliance costs are very broad ranging and can be considerable as the following examples suggest.

#### **Examples of organisational compliance costs**

A major fixed-store retailer had an in-house architectural team. However, in order to get approval for this team's store design plans in certain Member States, the company had to hire nationally registered architects, leading to considerable extra costs (stage 1 of the economic chain).

A clothes retailer explained that, unlike its home Member State where sales could be organised according to fashion seasons<sup>214</sup>, regulations limiting sales to twice a year required a major change in their operations. The store's promotional campaigns had to be totally readjusted (stage 3). Moreover, this also had further organisational effects on other stages of the firm's economic chain, such as changes to purchasing contracts with suppliers - as fewer seasonal lines could be offered in such Member States (stage 2) - inventory management (stage 2) and pricing strategy (stage 5).

A retailer that was used to Sunday opening in its home Member State was not allowed to do this in another Member State. Since 60% of its sales were achieved at weekends this meant that sales were concentrated on Saturdays. This required the building of much larger stores, bigger aisles, reduced stock on display and larger car parks (stages 1 and 4). These higher costs had to be borne even though lower levels of sales were achieved compared with the home country.

## **5. The lost growth and performance of the European economy**

**Compliance costs have implications for the entire economy.** Examining compliance costs for individual service providers gives only a partial assessment of the impact of barriers identified in part 1, since they do not take account of the consequences of these costs for the wider economy over time<sup>215</sup>. In particular, due account has to be taken of the following:

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<sup>214</sup> For certain product lines there are eight fashion seasons per year which mean that the remaining stocks for each line will need to be cleared through sales.

<sup>215</sup> It is important to note that even the Cecchini report (op cit) took a "static" view of the EU economy. To quote the HM Treasury paper "Realising Europe's Potential: Economic Reform in Europe" op cit p.16: "Cecchini himself was aware of this limitation, recognising that dynamic,

**Reduced investment in research and development, innovation and training** will result as available resources are diverted to meet the ex-ante and organisational compliance costs and as there will be lower levels of revenue growth. Since service growth depends on innovation, further specialisation and training of specialised staff it follows that the service provider's competitiveness and performance will suffer<sup>216</sup>.

**Reduced investment in information gathering, differentiation and customisation of services** for clients will also result as a consequence of this misallocation of resources within service companies. Given that services are heavily knowledge-intensive and that they require detailed information to be tailored to their clients' specific needs, such reductions will be particularly harmful to the performance of service firms as well as their clients.

**Reduced economies of scale and scope** result from the fact that a successful business model cannot be exported because several or all of the stages of the business process need to be changed to comply with differing legal and administrative requirements in other Member States. Although services are differentiated or even personalised, certain upstream or back-office tasks can be standardised or can benefit from technology if sufficient demand levels are achieved.

**Over-reliance on merger and acquisition strategies will increase costs of expansion.** Organisational compliance costs may persuade service providers to rely more on cross-border growth by acquisition than by green-field investment<sup>217</sup>. Growth by acquisition is generally considered to be more rapid to execute but also more costly to organise in that two firms with two business models have to be combined and managed.

**Anti-competitive defensive strategies** also arise from regulatory fragmentation. Given the constraints on cross-border green-field investment and the risk of becoming acquisition targets for larger suppliers, service firms seek to grow through acquisition or agreements at national level to defend their markets<sup>218</sup> rather than grow through innovation or differentiation.<sup>219</sup>

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non-price factors stemming from the removal of trade barriers and accompanying reforms, would, over the longer term, have far greater consequences than any 'static' step change for EU productivity, employment, growth, and economic and social stability."

<sup>216</sup> The fact that innovation is expected to be largest in those sectors which are most open to international competition has been acknowledged in: "Innovation in the Service Sector – Selected Facts and Some Policy Conclusions", op cit, p. 5.

<sup>217</sup> For example, according to the study on Trading Services in the Global Economy op cit international growth in Europe by mergers and acquisitions has been increasing more rapidly than growth by greenfield foreign direct investment. Regarding the retail sector, it was stated at a seminar that: "...acquisitions have become the main means of growth to gain access to countries with restrictive legislation – in particular, France, Italy and Germany." Quote from E. Colla "Commerce 99 – Proceedings of the Seminar on Distributive Trades in Europe", Eurostat, Brussels, 22–23 November 1999.

<sup>218</sup> At the seminar on Distributive Trades in Europe op cit, it was stated that "The globalisation of companies also encourages concentration at national level. Wal-Mart and Promodes-Carrefour are examples: the acquisitions of Wal-Mart in Europe in 1998-1999 triggered a competitive reaction, of which the merger between the two French giants only constitutes the most impressive event".

<sup>219</sup> See also "Cross-border acquisitions and Greenfield entry", the Research Institute of Industrial Economics, P-J. Norbäck, L. Persson, Working paper No 570, 2002.



***High levels of inflation of service prices result*** from this unrealised potential for cross-border growth in services in the Internal Market and the lack of cross-border competition. Consumers in particular suffer from the negative impact of fragmented markets, since they are denied the benefits of price competition<sup>220</sup>. Given the interdependence of services, it is evident that this price inflation will further erode the competitiveness of companies using services. That will in turn have a negative impact on growth and employment in the European economy as a whole.

## **B. The principal victims**

### **1. Small and medium-sized companies**

***SMEs' may find the cost of cross-border expansion to be prohibitive.*** SMEs are predominant in the services industry, accounting for a far greater proportion of total output than in manufacturing<sup>221</sup>. However, they are more severely affected by compliance costs than larger companies. In addition, for those that nevertheless do enter new markets, the significant organisational compliance costs that result undermine the success of their cross-border strategies or put them at a clear competitive disadvantage compared with incumbents.<sup>222</sup> And since their scale of operations does not justify the recruitment of specialist compliance staff, their skills and capacity to work with different sets of regulations are very limited.<sup>223</sup>

***SMEs are exposed to mergers and acquisitions.*** Medium-sized firms constrained from expanding abroad but often with significant local knowledge, experience and innovation potential, will be attractive targets for larger companies. The latter may be non-domestic entrants seeking to enter by acquisition or incumbents that wish to undertake pre-emptive acquisitions to dissuade entry by non-domestic rivals<sup>224</sup>.

***SMEs in small and peripheral Member States are particularly disadvantaged.*** On the one hand, SMEs in such Member States need to grow across borders because their home market has insufficient demand. On the other, they cannot benefit from the cross-border use of attractive business services. This is because their relatively low levels of potential demand make them the least attractive markets for providers of

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<sup>220</sup> “Realising Europe’s Potential, Economic Reform in Europe” op cit.

<sup>221</sup> See “Innovation in Services and the Knowledge Economy; the Interface between Policy Makers and Enterprise: a Business Perspective”, Irish Coalition of services industries, 2002 and “Major trends and issues” op cit.

<sup>222</sup> The dissuasive effects of compliance costs should not be underestimated and experience of regulation at national level also deters companies from entering new markets. For example, a recent UK report notes that in order to comply with national provisions small owner-managers spend three to five working days per month dealing with government administration and that this has increased by 35% over the past four years. This rise is partly due to complexity of regulation resulting from increasing service differentiation. “Local shops: a Progress Report on Small Firms Regulation” Better Regulation Taskforce (UK), July 2001.

<sup>223</sup> See for example, “The Services Sector in the UK and France: Addressing Barriers to the Growth of Output and Employment” op cit.

<sup>224</sup> At the seminar on Distributive Trades in Europe (op cit) it was said that “The commercial fabric of these countries [France, Italy and Germany] has always been made of a number of small and medium-sized family-run or independent businesses, or those belonging to purchasing groups or voluntary chains. These companies are the preferred targets of the large chains, which try to buy them out...].”

business services since expected returns on investment are not sufficient to cover high compliance costs.

## 2. The users of services, in particular consumers

*Service users, and in particular consumers, ultimately pay the price* for the existence of Internal Market barriers in the services field. Citizens suffer directly when they are prevented from using services offered by suppliers in other Member States, or when regulatory and administrative fragmentation dissuades companies from offering their services to customers residing in other Member States. This situation also contributes to the lack of consumer confidence in services from other Member State. Moreover, companies are at times advised against selling to other Member States by their own government authorities while, equally, citizens are cautioned by their representative bodies not to risk buying from abroad.<sup>225</sup> In the same way as for SMEs, this particularly affects citizens in small Member States. Thus consumers generally cannot benefit from a wide variety of competitively priced services and thus the better quality of life that they might expect from a fully integrated Internal Market.

The Commission's "Cardiff report" on the functioning of the Internal Market<sup>226</sup> has revealed that significant price differences remain within the Internal Market. The report has shown that certain retail prices can be up to 40% higher or lower compared with the European average and that the average price difference is 30%. The report concludes that these differences are due to "economic" rather than "geographic" factors and that "economic reform and competition measures seem best to eliminate residual price dispersion in these markets"<sup>227</sup>.

*European employees do not benefit from the job creation potential of the services industry.* All businesses are affected by these barriers, since services are relied on by every single enterprise in the European Union. It follows that the higher costs, lost productivity gains and thus lower employment levels extend throughout the European Union. Given that services account for the major part of employment across the Union it is this lost potential that is the most concerning of all.

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<sup>225</sup> For example, in guidelines on the application a rule relating to civil jurisdiction, a national authority explicitly advises e-commerce companies not to sell to consumers in other EU Member States in order to avoid the risk of being sued for breach of contract in all these countries.

<sup>226</sup> COM(2001)736 of 7 December 2001

<sup>227</sup> The European Round Table on Financial Services has produced a report on "The benefits of a working European retail market for Financial Services" F. Heinemann, M. Jopp 2002. It estimates that the potential cost savings could amount to €5bn and that the benefits could result in increased economic growth of between 0.5 and 0.7%. The report identifies the divergence between national rules in the area of consumer protection as a significant obstacle which "makes a pan-European marketing strategy and product standardisation impossible". Moreover, a Eurobarometer study carried out for the Commission (FLASH BE 117 "consumer study", January 2002) has shown that consumers have less confidence in purchases made in a Member State other than their own. 32% of European consumers feel well protected in a dispute with a company established in another Member State, compared with 56 % o, the case of a dispute with a domestic company.

## C. The weak credibility of the internal market in services

The multiplication of legal barriers may lead European citizens and operators to consider that the internal market is a danger zone. For those who are not put off providing services across internal frontiers and who cannot afford to pay the costs generated by the latter<sup>228</sup>, there are two possible ways of tackling those risks: either to come to an arrangement with the authorities or local partners, or else to conduct their activity "on the sly".

### 1. Perception of the internal market as a danger zone

As a consequence of the large number of difficulties reported, contacts with interested parties show that the recipients and providers of services often consider cross-border activities to be much more risky and costly than purely national activities. This is why businesses often choose to pursue their activities in a national or local context and, when they wish to extend their field of activity, they seem to favour direct investment abroad, mergers or acquisitions, rather than providing cross-border services.

In the same way, consumers feel less confident about undertaking transactions in another Member State. Indeed, the development of such transactions depends also on consumers' confidence and their perception of the market.

This perception that the internal market in services is more of a risk than an opportunity might partly explain why only 29% of undertakings have made use of cross-border professional services<sup>229</sup>, or why operators consider that they risk not being treated equitably by the courts in another Member State which might find out about a dispute involving them.

The credibility of the internal market in services thus depends largely on the effectiveness of the appeals and sanctions against a national authority which does not comply with the law of the internal market. In this respect, a survey reveals a degree of scepticism on the part of heads of undertakings: *"Where they do try to solve problems, businesses tend to use trade associations, chambers of commerce or their own networks. Use of administrations, national or at European level, as a form of recourse is not popular with most firms regardless of size. However, it is a means which larger companies will use more often than smaller ones. The findings underline the importance of making means of redress more accessible and effective, notably at the national level"*<sup>230</sup>. The European Parliament<sup>231</sup> and the Economic and Social Committee<sup>232</sup>, in their opinions on "An Internal Market Strategy for Services" placed

<sup>228</sup> Analysed above in Part III, §A.

<sup>229</sup> "Barriers to Trade in Business Services", already cited, page ii.

<sup>230</sup> Study attached to Single Market Scoreboard No 3, 3.11.1998.

[http://europa.eu.int/comm/internal\\_market/en/update/score/busien.htm](http://europa.eu.int/comm/internal_market/en/update/score/busien.htm)

<sup>231</sup> "a rigorous infringement policy vis-à-vis Member States which take measures incompatible with Articles 43 and 49 of the Treaty", European Parliament Resolution on the Commission Communication: "An Internal Market Strategy for Services", already cited, § 27.

<sup>232</sup> The opinion states that "The Commission should perform in a more determined and effective way its role as guardian of the Treaty, particularly by speeding up the procedures for dealing with breaches of the principles of free movement of services and freedom of establishment, and by examining carefully the question of the proportionality of the national measures underlying these restrictions. At a time when an exceptional effort is required of the applicant countries in order to

particular emphasis on improving the effectiveness of infringement procedures in the field of services.

## 2. "Arrangement" strategies

The absence of legal certainty in the exercise of the freedoms, and the lack of effective redress in the event of obstacles force providers to enter into negotiations with the national authorities or local operators in order to arrive at an "arrangement". Even if the obstacles are not legally justified and could be contested before a court or the Commission, the need to find a pragmatic and rapid solution in order not to delay access to the market in question leads many operators to embark on this type of strategy.

Contacts with interested circles confirm these arrangement practices, and in particular those involving the establishment of partnerships with local operators in order to "re-nationalise" the situation and thereby circumvent the reluctance of certain authorities to grant access to their national market<sup>233</sup>.

There are many drawbacks to this strategy:

- It tends to enshrine the legal barriers because it prevents legal action to abolish them and because the operator, once he has arrived at an arrangement, has no further interest in seeing the barriers in question disappear, since they are a barrier to the entry of competitors into the market (anti-competition effects);
- It involves additional costs for negotiations with the local authorities or for the partnership with a local operator (for example, the costs for using the services of local consultants or interpreters or counterparts, etc.).

## 3. "Black market" strategies

An alternative to arrangement strategies is to provide a service without bothering about its legality, i.e. to start thinking in terms of the black market or the parallel economy. These terms must be understood in the broad sense, i.e. as covering not just activities which are illicit as regards the tax systems, but also those which are illegal as regards any other legal requirement whatsoever, or any activity whose legality the operator cannot ensure and deliberately does not bother about.

In the case of cross-border services, following the "black market" strategy may be less the result of fraudulent intent than a consequence of the multiplication of legal barriers which make it particularly complex to assess the legality of cross-border services. As the Court recognised in a recent case<sup>234</sup>, a situation which a national

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adopt the entire Community *acquis*, the Member States should feel obliged to set a good example", Opinion of the Economic and Social Committee on the Commission Communication: "An Internal Market Strategy for Services", already cited, §7.5.

<sup>233</sup> This strategy was also noted in the field of public contracts; see "Selling to the public sector in Europe. A practical guide for small and medium-sized companies". OPOCE, 2000, page 17.

<sup>234</sup> Corsten judgment already cited; this case concerned a German architect who had entrusted a Dutch undertaking with floor tiling work on a building in Germany. As the Dutch undertaking was not

authority might consider clandestine working might in fact be no more than the legitimate exercise of the freedoms of the internal market.

Pursuing black market strategies is a lose-lose situation for all parties:

- The recipient and the provider of the service expose themselves to the risk of heavy penalties and deprive themselves of the means of defence and official appeal in the event of a dispute;
- The provider must keep a low profile, will lose opportunities because he can never openly promote his services and, in the long term, will not be able to ensure the competitiveness of his undertaking. Moreover, a black market strategy may serve as an alibi for certain national authorities to strengthen the legal barriers in the name of combating the black market, instead of abolishing them so as to promote the lawful exercise of cross-border services<sup>235</sup>;
- The public authorities are deprived of tax revenue and faced with the complexity and cost of the fight against the black market because they are not sufficiently able to distinguish between cases of legitimate activities under Community law and cases of deliberate fraud.

In line with the Commission Communication "New European Labour Markets, Open to All, with Access for All"<sup>236</sup>, the abolition of the legal barriers so as to promote the assessment and monitoring of the legality of cross-border activities thus appears to be one of the key instruments in combating the black market.

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entered in the register of trades in Germany, the German administration of the labour inspectorate imposed a fine for infringement of the German legislation on combating clandestine working. Such behaviour was challenged by the Court in the light of the principle of the free provision of services.

<sup>235</sup> In this context, a number of contributions from the building sector which stress the multiplication of labour inspectorate checks when the site is occupied by providers established in other Member States.

<sup>236</sup> Commission Communication "New European Labour Markets, Open to All, with Access for All", COM (2001)116 final of 28.02.2001 "The Internal Market in services is still fragmented. Yet it accounts for two-thirds of total employment, and for all new employment growth. Since, with technological advances, many services can now be provided at a distance, this fragmentation is causing distortions and may, indirectly, encourage movements of jobs outside the Union, or the development of irregular work within."

## CONCLUSIONS

A decade after the envisaged completion of the Internal Market, there is a huge gap between the vision of an integrated EU economy and the reality as experienced by European citizens and European service providers. The complexity and severity of legal barriers, which have replaced physical and technical ones for a large variety of services, is far more wide-ranging than was expected when the new Strategy for Services was launched.

The loss to the competitiveness of European economy as a whole cannot be underestimated. At this point it is already obvious that the goal set by the Lisbon Council to make the European economy the most competitive in the world cannot be met unless sweeping changes are made to the functioning of the Internal Market for services in the near future.

The nature and scope of the problems to be addressed require a major effort and a clear political commitment by all European institutions and the Member States to give high priority both to the removal of existing barriers and to the avoidance of new ones, while taking care to maintain a high level of protection of objectives of general interest. Candidate countries should as far as possible be involved in this process.

As already explained, this report does not seek to take a position either on the compatibility with Community law of national measures which are at the root of the difficulties described here, or on possible proposals to improve the functioning of the Internal Market for services. This report will serve as the basis of work for actions to be launched as a second stage of the Services Strategy in 2003 following discussions with the European Parliament, Member States and interested parties. These discussions need to cover the barriers to the cross-border provision and consumption of services, as well as obstacles to cross-border establishment, encountered in a wide variety of service activities.

Cross-border establishment, which plays an important role for service providers, needs to be facilitated by removing unnecessary administrative burdens and reducing red tape. However, SMEs are predominant in the services industry and for them cross-border service provision, rather than establishment, remains the principal way to exploit new markets, thanks in particular to the information technologies which overcome many of the reasons for permanent physical presence. It is therefore important to encourage cross-border service provision and make this as easy as it would be to provide services within a single Member State.

To achieve these objectives the Commission will, as outlined as part of the second stage of the Internal Market Strategy for Services, propose the necessary legislative actions, the scope and content of which require further analysis. In this respect a careful balance will have to be found between the need to avoid too detailed and wide-ranging regulation at the EU level and the need to protect the general interest objectives concerned. This requires more detailed analysis of areas for additional harmonisation that will be carried out in close co-operation with the European Parliament, Member States and other stakeholders. Particular attention will be given to barriers directly affecting the freedom to receive services by European citizens. In this context there will be close examination of demand-side issues, particularly the

situation of consumers in the Internal Market for services. Work in progress aiming to ensure a high level of consumer protection<sup>237</sup> will serve to reinforce the conditions necessary for consumer confidence in cross-border transactions.

To address non-regulatory barriers, the Commission will, as outlined in the Strategy, propose appropriate measures of a non-legislative nature. In this respect, the Commission will in the first instance tackle the need for information and assistance for citizens and companies wanting to use or provide cross-border services.

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<sup>237</sup> See the consultation in progress on a proposal for a framework directive on commercial practice; Commission Communication on the follow up to the Green Paper on consumer protection COM(2002)289.

## ANNEX

### **METHOD USED FOR THE CONSULTATION**

#### Background

The Commission's Communication on an Internal Market Strategy for Services was issued in December 2000 and Member States, other Community Institutions and interested parties were asked for their views. Given the complexity and the extremely wide scope of the issue, it was decided to extend the consultation and run it throughout 2001 and early 2002 in order to give sufficient time for all the parties concerned to provide their contributions.

#### Purpose of the consultation

The consultation was launched in order to gather first-hand information on the barriers which may hinder the development of the Internal Market in services in the EU. The existence of barriers to free movement of services and freedom of establishment was already recognised, but the precise nature and scope of those barriers was not well understood. For this reason, and for the first time since the presentation of the "General Programmes" for the suppression of restrictions to the freedom of establishment and the free provision of services in 1962<sup>238</sup>, the Commission has compiled an inventory of the existing barriers in the Internal Market for services based largely on the contributions of providers and users of the services, although information was also drawn from other sources, as is explained below.

#### What kind of services were covered?

The objective of the consultation was to collect information on problems encountered by providers and users engaged in **any sort of economic services activity** in the EU. The services did not need to be recognised in statistical terms or defined by any type of regulation. For example, many services are provided by manufacturers of goods (e.g. a furniture-maker might also carry out design, installation and maintenance services). All different forms of cross-border services were covered as well as establishment.

The consultation covered difficulties which service providers encounter throughout the entire business process – establishment, use of inputs (factors of production) necessary for the service provision, promotion, distribution, sales and after sales services. At each stage obstacles might be encountered. It is clear that an obstacle in one of the stages of the process might have an impact on the entire business process and force the service provider to change its business model.

#### What kind of barriers were covered?

The starting point for the identification of the barriers was the jurisprudence of the Court, from which it is clear that any measure which is liable to prohibit, impede or otherwise render less advantageous service provision between Member States

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<sup>238</sup> Op cit.



constitutes a barrier. Barriers are thus not only discriminatory measures, i.e. where an incoming service provider faces restrictions on the grounds of nationality or residence. Non-discriminatory measures, i.e. those which apply equally to service providers established in the country of the service provision and those established in other Member States, can also be barriers to trade.

Barriers arising from regulatory or administrative action i.e. those which are due to requirements in legislation, self-regulation systems, or to the practices of public authorities (administration or courts) and other regulatory bodies (such as professional bodies or, regional chambers) were covered. This included, for example, rules or procedures relating to authorisation, advertising, taxation and employment law in the case of the posting of workers. It also included circumstances where delays, fees or other problems made service provision unattractive or impossible. Some barriers might be due to complex, burdensome or non-transparent regulation or practices; most are just due to the wide divergence of national rules.

The Court has also made clear that there are circumstances where, subject to certain conditions, it is possible to justify restrictions, for instance to protect public health or consumers. However, the aim of the first stage of the strategy was to find out from the viewpoint of business and citizens what barriers were faced, rather than to make a judgement as to the whether or not they were justified. Therefore, areas which are subject to Community instruments or proposals were covered. Furthermore, barriers faced by EU service providers in the Candidate Countries were also taken into account.

#### How was the consultation carried out?

First, an independent survey of over 6000 companies of all sizes in 14 EU Member States was carried out on behalf of the Commission by a market research company<sup>239</sup>. This survey provided a valuable overview of the scope of the problem as it confirmed that **more than one in three** of the companies interviewed had direct experience of problems in relation to the free provision of services or freedom of establishment. The problems encountered were spread across all industry sectors, affected all sizes and types of companies and occurred at all stages of the business process (from establishment, use of inputs via promotion, distribution and sale of services, to after-sales activities).

Second, an open consultation was carried out through a number of mechanisms and channels in order to maximise participation. Several separate mailings were carried out to European and national level associations. Individual service providers and users were contacted either directly or through national associations. Bilateral meetings were organised in order to follow up issues and participation in conferences and workshops was ensured in order to raise awareness of the consultation process. Where necessary, the Commission developed more detailed informal questionnaires aimed at particular audiences (for instance, SMEs). All this resulted in responses from more than 668 different sources, who provided a total of 698 separate contributions.

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<sup>239</sup> Germany was excluded because of complications arising from rules relating to market research, but the Commission services gathered comparable information through a separate exercise.

### Other sources used

In order to complement the open consultation and the survey and provide as full a picture as possible of the reality of the Internal Market in services today, information was also drawn from other sources.

First, the Commission examined the questions and petitions put to the Commission by the European Parliament. The Commission has received a significant number since the launch of the strategy and they provide a very useful source of information about the preoccupations of European businesses and consumers. Second, formal complaints to the Commission and infringement cases, of which a significant number has also been received since the launch of the strategy, have provided an important source of information. These sources were particularly helpful in identifying cases where individual citizens were finding it difficult to use services because of Member States practices.

Third, information received from consultation and problem solving mechanisms, such as the Commission's Dialogue with Citizens and Business and the Member States' internal market co-ordination centres and contact points for citizens and business, was examined.

Finally, the Commission used economic and statistical studies from established sources and its own services, from Member States and other bodies.

### Member State contributions

In addition to the call for contributions made in the Communication of December 2000 on the Internal Market Strategy for Services, the Commission wrote to Member States in September 2001 with a more detailed request for responses, including any economic or statistical data on national and European services markets. A further request was addressed to Member States in the first quarter of 2002 concerning the organisation at the national level of the follow-up to the Court judgements. Most Member States have replied to these requests and their contributions also reflect consultations which they have held at national level with interested parties.

In November 2001, the Commission established an expert group of Member States to advise it on the strategy. The group has met twice so far and it is anticipated that the group will meet 3-4 times per year. A number of Member States organised workshops on the strategy and the Commission services participated in some of these. The workshops were particularly helpful in explaining the aims of the strategy, establishing a dialogue with service providers and users, and in comparing and refining information already received on types of barriers.