

# **REVISED PARTIAL REGULATORY IMPACT ASSESSMENT**

**(on the draft “Services Directive”)**

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## **1. TITLE OF PROPOSAL**

**Amended Proposal for a Directive of the European Parliament and of the Council on Services in the Internal Market (hereafter referred to as the “Services Directive”)**

### **Amended Proposal:**

Brussels, 04.04.06  
COM (2006) 160 final  
2004/0001 (COD)

### **Original Proposal:**

Brussels, 13.01.2004  
COM (2004) 2 final  
2004/0001 (COD)

## 2. SUMMARY

### Background

The Commission submitted its original proposal in January 2004. Following the European Parliament's first reading on 16 February 2006, the Commission issued a revised proposal on 4 April 2006, incorporating most of Parliament's amendments. The revised proposal covers all economic service activities, except those for which specific exclusions or derogations are provided. Activities excluded are: all financial services; electronic communications and networks (to the extent that they are covered by the European Community telecoms legislation package); all transport services and transport-related services falling under TEC Title V and port services; healthcare services; services of temporary work agencies; audiovisual services; gambling activities; activities connected with the exercise of official authority; social services relating to social housing, childcare and support of families and persons in need; private security services; and all taxation. Labour law and criminal law are also excluded.

### Rationale for Government Intervention

The UK government attaches particular importance to the creation of a better functioning internal market for services in the EU because it recognises that it can be a powerful spur to productivity, employment and prosperity not just in the UK but also in all Member States. Services form the backbone of the modern economy and are the engine of productivity growth, yet they account for only a small proportion of total cross-border trade. The barriers to trade can be broken down into three broad categories: administrative burdens, efficiency losses at the firm level, and efficiency losses at the economy-wide level. Without action specifically targeted at removing unjustified barriers, services are likely to continue to be traded at a level far below their potential. The UK and EU Member States would continue to miss out on the significant potential benefits of increased trade and better regulation in services, including higher productivity, employment, investment and a wider choice of better quality services at lower prices.

### Options

#### Option 1 – No Directive

While the UK could in principle vote to reject the amended Services Directive, the most likely outcome is that this would still result in the UK having to implement the Directive, or face infraction proceedings, since it is a co-decision dossier decided under Qualified Majority Voting in the Council of Ministers,. Given the commitment of all Member States (including the UK) to both the freedoms of the Treaty and the Lisbon Agenda, it is extremely unlikely that a blocking minority could be found to reject the proposal out of hand.

#### Option 2 – Accept the Revised Proposal entirely in its current form

The main differences between the current version and the original are that:

- The country of origin principle has been replaced by a different mechanism for the free movement of services

- There are more exclusions from the scope of the Directive, for service activities such as healthcare, social services, gambling, temporary work agencies and audio-visual services.

Whilst a great many of the UK's negotiating objectives (agreed by EP Cabinet committee EP(C) in late 2004) have been met by the revised proposal, there are some further changes that the UK needs to see to meet our policy objectives, notably in order to ensure that we can uphold UK standards in health and safety and sensitive policy areas.

### Option 3 – UK to broadly accept the Revised Proposal while seeking further amendments

The UK would seek to negotiate amendments to the present text in line with the UK's negotiating objectives. The main changes would be to ensure that:

- Single points of contact are points of information<sup>1</sup>, not points of completion: the costs-benefit analysis of these two alternatives strongly favours the former. (*Economic implication.*)
- The Directive does not prevent the UK upholding standards on health and safety and sensitive policy areas. (*Social and Environmental implications.*)

### **Costs and Benefits**

In terms of net economic benefits, the present version of the Services Directive will be massively positive for the UK (over £5 billion) whether or not there are further minor changes affecting administrative costs. It will also be massively beneficial for other EU Member States, although those impacts are not included in the UK perspective used for this assessment.

### **Social and Environmental Effects**

As services are more important for employment in London and the South East of England than elsewhere in the UK, a slightly larger proportion of the benefits might be expected to go to London and the South East. We do not expect the Directive to have any significant effect on the environment. There may however, be some unquantifiable social effects if the UK were unable to uphold standards in health and safety and sensitive policy areas under option 2.

### **Small Firms Impact Test**

SMEs are disproportionately affected by barriers to establishment and cross-border trade in services, because the costs of overcoming them are often independent of firm size. The proposed Directive, which aims to reduce the administrative burden through the creation of single points of contact and other simplification measures, should therefore benefit UK SMEs significantly. This view is supported by initial feedback from the Small Business Service and small business organisations.

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<sup>1</sup> Gateways through which providers can access and complete all necessary procedures at the relevant authority websites – see page 35 in Section 5.3

## **Competition Assessment**

The Directive should have a pro-competitive effect on the affected markets. In reducing the national rules and regulations that foreign service providers must comply with to enter the market of another Member State, it is reducing the barriers to entry that they face. The Directive is likely to have the greatest impact in the regulated professions sectors, where the barriers to entry are greatest.

## **Recommendation**

Option 3, which is for the UK to broadly accept the amended proposal while seeking further amendments, is recommended. The economic benefit is by far the most significant of the impacts to the UK of the Services Directive and will be in the region of £5 to 5.6 billion annually. The total net benefit of the Directive depends on other factors in addition to the economic benefit e.g. the social and environmental impacts and the administrative costs of the single point of contact. These impacts, whilst having only a minor effect on the total net benefit of the Services Directive, are nevertheless important in informing the final recommendation. The precise figure for the total net benefit depends on whether option 2 or 3 is implemented. The quantifiable difference in net benefit between option 2 and option 3 can be considered to be negligible (£120 million compared with overall benefits of around £5 billion). However, taking the social and environmental impacts into account as well, Option 3 is clearly preferable, as it allows for amendments in line with agreed EP(C) policy objectives to meet any UK concerns in sensitive areas, as well as delivering a higher benefit-cost ratio due to its reduced implementation costs.

### 3. PURPOSE AND INTENDED EFFECT

#### 3.1 History of the Proposal

The Commission drafted its original Proposal for Services in the Internal Market in January 2004, intended to tackle barriers to establishment of service providers in, and free movement of services between, EU Member States. The Proposal was controversial for many Member States and has therefore taken a long time to reach its first reading in the European Parliament, following which the Commission produced a revised proposal, accepting very many of the amendments voted by the European Parliament. This partial RIA has been revised to estimate the impact of the revised proposal, only drawing comparison with the original proposal where helpful in the analysis.

#### 3.2 The Objective

The objective of the Directive is to eliminate obstacles to the freedom of establishment for service providers and to the free movement of services between EU Member States (both remotely and where a service provider travels temporarily to another Member State), and give both providers and recipients of services the legal certainty they need in order to exercise these fundamental freedoms enshrined in the EC Treaty.

The proposal only applies to providers established in a Member State<sup>2</sup> and covers all economic service activities, except those for which specific exclusions or derogations are provided. The revised proposal excludes the following activities: all financial services; electronic communications (to the extent that they are covered by the European Community 2002 telecoms legislation package); all transport services and transport-related services falling under TEC Title V and port services; healthcare services; services of temporary work agencies; audiovisual services; gambling activities; activities connected with the exercise of official authority; social services relating to social housing; childcare and support of families and persons in need; private security services; and all taxation. Labour law and criminal law are also excluded.

In order to eliminate the obstacles to the freedom of establishment, the proposal provides for:

- Administrative simplification, particularly involving the establishment of **“single points of contact”**, at which service providers can complete the administrative procedures necessary to their activities, and the obligation to make it possible to complete these procedures at a distance and **by electronic means** (Articles 5-8)

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<sup>2</sup> Article 2(1) of the proposed Directive defines it as applying to “services supplied by providers established in a Member State”. Article 4 defines a service as “any self-employed activity, as provided for by Article 50 of the Treaty, normally provided for remuneration.”

- Certain principles (notably non-discrimination, necessity justified by an overriding reason of public interest and proportionality) that **authorisation schemes** applicable to service activities must respect, in particular relating to the conditions and procedures for granting authorisation (Articles 9-13)
- **The prohibition of certain particularly restrictive legal requirements** (e.g. nationality or resident requirements on staff or prohibitions on being established in more than one Member State, or an obligation to demonstrate economic need) which may be in force in Member States (Article 14)
- The obligations to **assess the compatibility of national legal requirements** with certain specified conditions laid down in the Directive (Article 15)

In order to eliminate obstacles to the free movement of services, the proposal provides for:

- Member States being allowed to make temporary or remote service providers subject only to requirements that respect the principles of **non-discrimination, necessity and proportionality**, where necessity is here defined as “justified for reasons of public policy, public security, public health or the protection of the environment” (Article 16(1)).
- The **prohibition of certain particularly restrictive requirements** (for example the requirement to set up an office, or the requirement to register with a professional body in the host Member State (Article 16(2)).
- **Derogations from the above to protect sensitive sectors** or matters covered by other specific pieces of legislation (Article 17). There is also provision for case-by-case derogations, in exceptional circumstances, relating to the safety of services (Article 19).
- The **right of recipients to use services** from other Member States, without being hindered by restrictive measures imposed by their home country or by discriminatory behaviour on the part of public authorities or private operators (Articles 20-21).
- A **mechanism to provide assistance to recipients** who use a service provided by an operator established in another Member State, by obliging Member States to supply information about, for example, their consumer protection law (Article 22).
- The **removal of total prohibitions on commercial communications** by the regulated professions, which ensures that professional rules on commercial communications must be non-discriminatory, justified by an overriding reason relating to the public interest, and proportionate.

With a view to establishing the mutual trust between Member States necessary for realising the aims of the Directive, the proposal provides for:

- Some **harmonisation** of legislation, particularly as regards service providers' obligations concerning the provision of information such as relating to their services and any after-sales guarantees, and as regards Member State rules covering multi-disciplinary activities and exchange of information on the quality of the service provider, and settlement of disputes (Articles 26-32).
- **Measures for promoting the quality of services**, such as voluntary certification of activities, quality charters or cooperation between the chambers of commerce and of crafts (Article 31).
- **Stronger mutual assistance between national authorities** with a view to effective supervision of service activities. In support of this, the Commission are to provide an electronic cooperation system to facilitate communication between Member States' competent authorities (Articles 33-37).
- Encouraging **codes of conduct** to be drawn up at Community level, particularly by professional bodies and associations, aimed at facilitating the provision of services or establishment of a provider in another Member State (Article 39).

The proposal is a horizontal framework Directive that will apply alongside and complement other European Community legislation applying to services. Article 3 provides that: *"If the provisions of this Directive conflict with a provision of another Community Act...(...)...the provision of the other Community Act shall prevail"*.

The most substantial exemption from the provisions of the Services Directive for other European Community law is to be found in the derogations from "freedom to provide services" in Article 17.

For most of the proposal, implementation is required within two years from the possible adoption in 2006 (i.e. 2008 as currently scheduled). This would be a major task for such a wide-ranging Directive, which explains why certain technical provisions, for example the setting up of single points of contact, are given three years for implementation.

Perhaps the largest component regarding the implementation of the Directive is set out in Article 15, which requires Member States to assess requirements imposed on access to, and exercise of, service activities and to make a report to the Commission on the results of that assessment under Article 41. The report must be completed by the final date for implementation of the Directive (2 years from its adoption) and must specify which requirements the Member States plan to retain and their justifications, and also those that have been abolished by that date. Further initiatives could result from the conclusions of

the Report. Member States must also report under Article 9(2) on authorisation systems, and under Article 30 on multidisciplinary activities.

### **3.3 Background – Why Is Action Needed?**

#### ***Barriers to trade in services in the EU***

In contrast to goods, the internal market for services in the EU is still incomplete. This is largely because service providers are subject to requirements and restrictions relating to establishment, cross-border supply and use of inputs, which providers of goods do not face.

In 2002, the European Commission published a report, “*The State of the Internal Market for Services*”<sup>3</sup> in which it identified 91 specific barriers preventing or hampering cross-border trade in services in the EU. The majority of these – which are discussed in greater detail in Annex A – were new or long-standing legal barriers<sup>4</sup> including:

- *Quantitative restrictions on the number of service providers operating in a given product/geographical market*
- *Territorial restrictions relating to the geographical market*
- *Nationality and/or residence requirements*
- *Length and complexity of registration and authorisation procedures*
- *Restrictions on multidisciplinary activities*
- *Requirements on the legal form and internal structure*
- *Requirements for professional qualifications*
- *Requirements relating to cross-border use of inputs and posted workers*
- *Rules on commercial communications (i.e. advertising)*
- *Pricing rules*

The report also identified non-legal barriers to trade in services relating to:

- *Lack of information*
- *Differences in language and culture*

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<sup>3</sup> This marked the completion of the first of the Commission’s two-stage strategy to create an internal market for service, which had begun in December 2000 with the publication of its report, “*An Internal Market Strategy for Services*.” This report can be found at: [http://europa.eu.int/comm/internal\\_market/services/docs/services-dir/com-2000-888/com-2000-888\\_en.pdf](http://europa.eu.int/comm/internal_market/services/docs/services-dir/com-2000-888/com-2000-888_en.pdf)

<sup>4</sup> The Commission attributes these barriers to a combination of the following factors: a lack of trust by Member States in the quality of regulation in other EU countries; a failure to update national legislation so that it remains compatible with EC law; and a deliberate intent by some Member States to protect national economic interests.

## ***UK experiences of barriers to trade***

In September 2005, the DTI published the results of a study carried out by PricewaterhouseCoopers (PwC) on the barriers to establishment and cross-border movement of services encountered by a selected number of UK firms in two of the major sectors covered by the Directive – construction and business services<sup>5</sup>.

The study focused on a sample of 38 firms of differing sizes that had provided or considered providing services to six Member States – France, Germany, Italy, the Netherlands, Poland and the Slovak Republic – in the last five years.

While the results may not be representative of the whole population of UK firms – owing to the deliberate criteria on which the selected firms were chosen – they do provide a useful first insight into the experiences of UK service providers which have traded or considering trading with other Member States.

The conclusions that emerged were:

1. The internal market is not yet a reality – most case study firms still think of the EU as consisting of distinct national markets. Most firms believed that creating an internal market in services would be beneficial to themselves and the UK as a whole, and supported the principles of the proposed Directive.
2. In expanding into the EU, firms' business development decisions rested on a number of factors other than barriers that the proposed Directive will address, and can be quite subjective.
3. Establishment – either by acquisition, branch office or new company – was seen as necessitating relatively high fixed costs. Consequently, larger case study firms were more likely to establish than the small and medium-sized firms.
4. The preferred approach for the smaller case study firms was provision of services without establishment as this was seen as less costly and more flexible with firms able to use a wide variety of delivery models to provide services cross-border on a temporary or remote basis.
5. Case study firms did not consider their costs of compliance with the Directive to be significant, based on their present understanding of it.

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<sup>5</sup> PricewaterhouseCoopers (2005) "*Impact of the proposed EU Directive on Services in the Internal Market: case studies of UK businesses*" This report can be found at: [http://www.dti.gov.uk/ewt/services\\_Directive\\_economics\\_studies.htm](http://www.dti.gov.uk/ewt/services_Directive_economics_studies.htm)

### **3.4 Rationale for Government Intervention**

#### ***Drivers for Action: The importance of creating a better functioning internal market for services in the EU***

In 2000, EU leaders committed themselves to an ambitious ten-year programme of economic reform aimed at making the EU the “*most competitive, dynamic and knowledge-based economy in the world, capable of sustained economic growth, with more and better jobs and greater social cohesion.*”<sup>6</sup>

The UK government is keen to see progress on the Lisbon process in order to help raise productivity, employment and living standards in the UK. Raising productivity is a particular priority for the UK government as productivity in the UK has historically been lower than in other major economies.

The UK productivity gap is illustrated in Charts 1 and 2 below, which compares two measures of labour productivity for the UK, France and US. Despite some convergence in productivity levels over the past decade, in 2003, labour productivity per person in the UK was 21% lower than in the US and 10% lower than in France<sup>7</sup>. Similarly, labour productivity per hour worked in the UK was some 16% and 17% lower than in the US and France respectively.



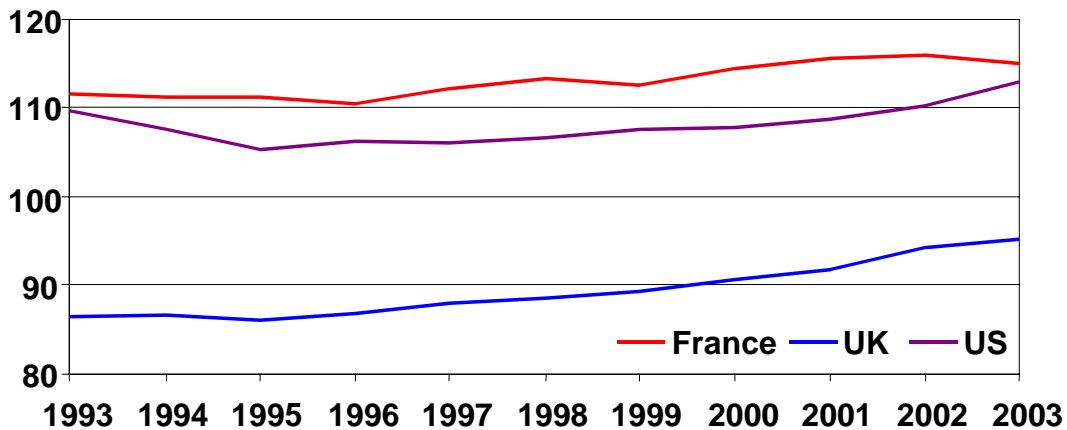
Source: European Commission, Eurostat data (2005)

Note: Labour productivity defined as Gross Domestic Products in Purchasing Power Standards per person employed

<sup>6</sup> Presidency Conclusions, Lisbon European Council 23-24 March 2000

<sup>7</sup> The productivity gap, measured on this basis, increased slightly in 2004 with the US.

**Chart 2: Labour productivity per hour worked (EU15=100)**



Source: European Commission, Eurostat data (2005)

Note: Labour productivity defined as Gross Domestic Products in Purchasing Power Standards per hour worked

The UK government sees greater openness to trade as playing a significant role in raising productivity because it strengthens the five ‘drivers’ of productivity: competition, enterprise science and innovation, skills and investment<sup>8</sup>.

It attaches particular importance to the creation of a better functioning internal market for services in the EU because it recognises that it can be a powerful spur to productivity, employment and prosperity not just in the UK but also in all Member States. This belief is based on the three key facts, all of which are discussed in greater detail in Annex D:

- i. Services form the backbone of the modern economy
- ii. Services are the engine of productivity growth
- iii. Services account for only a small proportion of total trade

Since the proposals were brought forward, the European Commission has carried out a Mid-Term Review of the Lisbon Strategy aimed at revitalising the process of economic reform in the EU. In its conclusions to the Spring European Council in February 2005<sup>9</sup>, the European Commission identified the creation of a better functioning internal market for services in the EU as key to making progress on the Lisbon Agenda and called for urgent action to achieve it<sup>10</sup>.

<sup>8</sup> See 2.7-2.9 of HMT study “Trade and the Global Economy: The role of international trade in productivity, economic reform and growth” [<http://www.hm-treasury.gov.uk/media/17B/42/17B42758-BCDC-D4B3-1B5E14759174F25A.pdf>]

<sup>9</sup> European Commission Communication (2005) “Working together for growth and jobs – a new start for the Lisbon Strategy”. Conclusions of the Mid-Term Review of the Lisbon Strategy presented to the 2005 Spring European Council.

<sup>10</sup> Two influential reports which fed into the Mid-Term Review – one by Wim Kok, former Primer Minister of the Netherlands and one by André Sapir – both recommended the creation of an internal market for services as a top priority for the EU.

## ***The economic impact of barriers to trade in the EU***

The different types of barriers can have a significant impact on service providers and the economy. These can be broken down into three broad categories:

- Higher administrative burdens
- Efficiency losses at the firm level
- Efficiency losses at the economy-wide level.

### Higher administrative burdens

Service providers that establish abroad or trade across national borders face much higher administrative burdens than those that do not operate outside the domestic market. This is because they must not only comply with the rules, regulations and administrative formalities of the *home* Member State but the *host* Member State as well.

The fact that many of these costs are independent of firm size means that small and medium-sized enterprises (SMEs)<sup>11</sup>, which form the majority of service providers in the UK, are disproportionately more adversely affected, with the greatest burden of all falling on micro businesses<sup>12</sup>. In extreme cases, these costs may be sufficiently large that they act as a barrier to entry, deterring smaller service providers from starting up in other Member States.

The cost of entering another Member State may be greater for UK service providers moving overseas than for service providers from other Member States coming to the UK. The process of starting up a business in many Member States can be significantly longer and more complex than in the UK. In some Member States the start-up process involves up to twice as many procedures as the UK while in others the start-up process can take two to three times longer to complete than in the UK. Annex B details the length and complexity of the business start-up process in different Member States while Annex C presents a comprehensive but not exhaustive inventory of the types of procedures and costs involved.

### Reduced efficiency

Cross-country differences in rules on advertising and multidisciplinary activities can prevent service providers adopting the most efficient business models and practices and limit their ability to respond quickly to changing economic

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<sup>11</sup> In this paper we use the UK Small Business Service (SBS) definition of a small and medium sized enterprise (SME) - a business employing fewer than 250 people. The EU definition is much narrower - a business employing fewer than 250 people with an annual turnover not exceeding €40m and/or annual balance sheet not exceeding €27m.

<sup>12</sup> The Small Business Services (SBS) defines micro businesses as enterprises employing fewer than 10 people. This definition includes enterprises with no employees, which form the bulk of micro businesses. The EU definition is much narrower. It defines a micro business as an enterprise employing fewer than 10 people with an annual turnover and/or annual balance sheet not exceeding €2 million (approximately £1.3million)

conditions. If a firm in one Member State is looking to establish in another Member State, then there may be an additional cost associated with adapting the business model so that it complies with the rules and regulations of the host Member State.

For example, in some Member States a service provider may be required to separate out its activities because of restrictions on multidisciplinary activities. As a result, opportunities to exploit potential economies of scale are reduced, since the costs of entering a particular Member State cannot be offset against entering any others<sup>13</sup>.

#### Reduced competition in domestic markets

Lengthy and complex administrative procedures, strict eligibility on market criteria (e.g. in the professional services) and restrictions on nationality and residence can all act as barriers to entry.

As a result, the economic benefits to the providers and recipients of services in Member States are reduced. For example, high barriers to entry can restrict competition from new service providers – domestic and foreign – hampering productivity growth, limiting consumer choice and keeping prices unnecessarily high.

Such barriers can also put a significant brake on the economy as SMEs are recognised as a key driver of productivity growth, promoting not only greater competition but also enterprise and innovation<sup>14</sup>.

#### **Why government intervention?**

Without action specifically targeted at removing unjustified barriers, services are likely to continue to be traded at a level far below their potential. The UK and EU Member States could miss out on significant potential benefits of increased trade and better regulation in services including higher productivity, employment, investment and a wider choice of better quality services at lower prices.

More competition in the EU internal market is also likely to make EU service providers better able to compete in global markets. There will also be knock-on effects for other sectors of the economy, including those not covered by the Directive. Recipients of services falling under the Directive will include other businesses. Business services in particular are key to the development and success of start-ups and growing firms in all sectors of the economy.

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<sup>13</sup> See CPB Netherlands Bureau for Economic Policy “*The free movement of services in the EU*” for a more detailed analysis of the implications of cross-country difference in regulation on the costs incurred by service providers establishing in other Member States or providing services across national borders. <http://www.cpb.nl/eng/pub/cpbreeksen/document/69/doc69.pdf>

<sup>14</sup> More information on the economy-wide costs of barriers to services can be found in European Commission (2002), “*State of the Internal Market for Services*” p.63-64 available at: [http://europa.eu.int/eur-lex/en/com/rpt/2002/com2002\\_0441en01.pdf](http://europa.eu.int/eur-lex/en/com/rpt/2002/com2002_0441en01.pdf)

## 4. OPTIONS

The Services Directive is essentially a deregulatory measure, and has substantial economic benefits for both the UK and other Member States. As analysts point out "reductions in barriers consistently yield economic gains". Moreover, larger barrier reductions lead to larger gains<sup>15</sup>. So further reform, beyond what is currently proposed, (for example reverting to the more ambitious original 2004 version of the Directive) would appear to make economic sense. However, the special characteristics of European legislation mean that the Commission, not the UK, has control of producing the proposal, and so the range of potential options is normally limited to: rejection, straight acceptance, and acceptance with pressure for further change. These are the alternatives considered for the current proposal.

### **Option 1 – No Directive**

While the UK could in principle vote to reject the amended Services Directive, the most likely outcome is that this would still result in the UK having to implement the Directive, or face infraction proceedings. This is because the proposal depends on Qualified Majority Voting in the Council of Ministers and on co-decision with the European Parliament. Given the commitment of all Member States (including the UK) to both the freedoms of the Treaty and the Lisbon Agenda, it is extremely unlikely that a blocking minority could be found to reject the proposal out of hand. For the purpose of this RIA, however, Option one will be taken as maintaining the status quo.

### **Option 2 – Accept the Amended Proposal entirely in its current form**

This option would entail accepting the current version of the text, which is mainly changed from the original in that:

- The country of origin principle has been replaced by a different mechanism for the free movement of services
- A number of additional service activities are excluded from the scope of the Directive (e.g. healthcare, social services, gambling, temporary work agencies and audio-visual services).
- Article 15 (h) and (i) on free price setting has been deleted.

Whilst a great many of the UK's negotiating objectives (agreed by EP Cabinet committee EP(C) in late 2004) have been met by the revised proposal, there are some further changes that the UK needs to see to meet our policy objectives, notably in order to ensure that we can uphold UK standards in health and safety and sensitive policy areas.

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<sup>15</sup> See CPB Netherlands Bureau for Economic Policy "*The free movement of services in the EU*" for a more detailed analysis of the implications of cross-country difference in regulation on the costs incurred by service providers establishing in other Member States or providing services across national borders. <http://www.cpb.nl/eng/pub/cpbreeksen/document/69/doc69.pdf>

### **Option 3 – UK to broadly accept the amended proposal whilst seeking further amendments**

The UK would seek to negotiate amendments to the present text in line with the UK's negotiating objectives (agreed by EP Cabinet committee late 2004). The main changes would be to ensure that:

- *Single points of contact are points of information<sup>16</sup>, not points of completion: the costs-benefit analysis of these two alternatives strongly favours the former. (Economic implication.)*
- *The Directive does not prevent the UK upholding standards on health and safety and sensitive policy areas. (Social and Environmental implications.)*

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<sup>16</sup> Gateways through which providers can access and complete all necessary procedures at the relevant authority websites – see page 35 in Section 5.3

## 5. COSTS AND BENEFITS

### 5.1 Summary of Costs and Benefits

The total net benefit of the Services Directive depends on the economic, the social and environmental impacts, and the administrative costs of the SPC. The economic benefit is by far the most important impact of the Directive. In terms of net economic benefits, the present version of the Services Directive will be massively positive for the UK, whether or not there are further minor changes affecting administrative costs. It will also be massively beneficial for other EU Member States, although those impacts are not included in the UK perspective used for this assessment.

**Table 1: Summary of UK impacts for each policy option (£m p.a.)**

Option	Economic Policy benefit*	Business admin benefit	Govt admin cost	Positive unquantifiable impacts	Negative unquantifiable impacts
1	0	0	0		
2	5,300 <sup>†</sup>	210	92		Expensive Single Point of Completion within 3 years is a <b>high-risk</b> and complex IT project that is not essential to achieving the aims of this Directive <sup>17</sup> Risk being unable to meet agreed policy objectives (e.g. upholding standards in health and safety and sensitive policy areas)
3	5,300 <sup>†</sup>	3	2	Good value for money Single Point of Information based on affordable improvement to existing Government-to-business services Secures agreed UK policy objectives such as upholding UK standards in sensitive policy areas	

Money values are annual, and admin figures have been annualised.

\*Economic Policy benefit is based on the midrange point the 0.9 - 1% increase in welfare. = £6.3 - 7 billion annually. This is adjusted to reflect benefits lost by a more limited liberalisation under 'freedom to provide services' (Article 16) and the effect of the deletion of the provision on free price setting – see Section 5.3.

<sup>†</sup> Approximate average value: net welfare benefit to the UK of the Services Directive will be in the region of £5 – 5.6 billion annually as per table 4.

<sup>17</sup> The high-risk nature of this project is likely to lead to a significant increase in the costs associated with the project. A study by Mott MacDonald undertaken for the UK Treasury on project cost overruns suggests that for equipment and development projects works duration may overrun by 54% and capital expenditure by as much as 214%. (Mott MacDonald 'Review of large public procurement in the UK' July 2002) [http://www.hm-treasury.gov.uk/media/A00/D3/greenbook\\_mott.pdf](http://www.hm-treasury.gov.uk/media/A00/D3/greenbook_mott.pdf)

Costs and benefits need to be expressed relative to a baseline. The research sources for this report assume a comparator scenario in which the Services Directive is not implemented in the EU. There will be net benefits from adopting the Services Directive, so the impact of not adopting it is shown as nil, and the impacts of the other options are shown as positive (benefits) or negative (costs) relative to the current situation.

Table 1 shows the economic benefit to the UK of the Services Directive will be in the region of £5 – 5.6 billion annually. The precise figure for the total net benefit of the Directive depends on whether option 2 or 3 is implemented. The quantifiable difference in net benefit between option 2 and option 3 can be considered to be negligible (£120 million compared with overall benefits of around £5 billion). However, taking the social and environmental impacts into account as well, Option 3 is clearly preferable, as it allows for amendments in line with agreed negotiating objectives to meet any UK concerns in sensitive areas, as well as delivering a higher benefit-cost ratio due to its reduced implementation costs.

Table 1 shows the benefits for the UK under each option. The final recommendation for which option to follow depends on three sets of information contained within table 1. Firstly, a distinction is made in the table between the welfare gain from the Directive (the economic policy benefit – referred to in the table and text as the economic benefit) and the administrative costs and benefits associated with the implementation of the Directive. The difference between options 2 and 3 depends on the net benefits of the two implementation options for the single point of contact (SPC) and is derived from business admin benefit and government admin cost.

The choice of implementation, single point of contact under option 2 or single point of information under option 3, is important in informing the final recommendation, since it has a significant impact on the cost of the Directive. The third factor to contribute to the final choice of option is that of the unquantifiable impacts, which can be shown to increase the relative benefits of option 3 compared to option 2. The three sets of information cannot be combined to create a final monetary estimate of the benefits under the different options since they contain unquantifiable economic, social and environmental effects. The final recommendation is based on the implications of these three sets of information for the total net benefits of the Directive.

Within those sectors covered by the Directive, SMEs should gain relatively more than larger firms. This is because the costs of overcoming barriers are often independent of firm size so impact disproportionately on small firms. Whilst the lowering of barriers to services trade will mainly benefit UK firms trading with other Member States, and vice-versa, the proposals may also reduce the costs of UK firms providing services to the UK market, regardless of whether they export services or not. The significance of this extra effect is likely to vary by sector, depending on the nature of barriers to trade and whether they also represent costs to domestic businesses. For example, non-service industries such as manufacturing and agriculture will benefit as recipients of

services. The barriers to trade in services are often discriminatory as regards foreign firms, that is, more difficult for foreign firms to overcome than for domestic firms, or only applying to foreign firms. However, non-exporting UK services firms may, for example, benefit from the use of “single points of contact” and administrative simplification measures.

As discussed by the Commission in their initial Extended Impact Assessment, the complexity of linkages between service activities and manufacturing operations and the lack of information on the cost of regulatory and other non-tariff barriers means that no suitable model to estimate the effects of the liberalisation proposed by the Directive currently exists. Even if one were developed, the services trade data is not sufficiently detailed to enable a reasonable estimate to be made.

There are, however, numerous estimates of the benefits of reducing *global* barriers to services trade, developed to support the negotiations on liberalising world services trade in successive rounds of WTO talks, which illustrate the extent to which trade in services is currently restricted and the scale of the potential benefits.

Hufbauer & Warren (1999) estimate the external barriers to services trade for selected industries and countries at the end of the Uruguay Round. According to their results, the EU's external barriers to services trade are twice those of the USA and Japan in wholesale and retail distribution and are relatively much higher in transport, storage and communications.

A study by the Australian Productivity Commission (2000) estimates that *the world as a whole* would be more than US\$130 billion better off if all post-Uruguay barriers to trade in services were eliminated. The lion's share of this benefit would go to developing countries, because economies with higher initial levels of protection tend to gain the most (as a percentage of GDP), but the study also predicts substantial benefits to developed economies.

A literature review by the OECD outlines the main models, assumptions and results of thirteen empirical studies analysing the impact of liberalising *global* services trade. The benefits of removing the barriers are shown to outweigh the costs under all modelling assumptions. The estimates of the EU's share of the benefits range from 0.1 to 1.9 per cent of EU GDP or €8.8bn to €167.7bn in terms of 2001 EU GDP.

The Commission's research into the impact of ten years of the Single Market Programme (SMP) reports that in 2002, EU GDP was 1.8 percentage points, or €165bn higher, than it would have otherwise been, due to the operation of the Internal Market, and that 2.5 million jobs had been created since 1992. These results include estimates of the gains from previous liberalisation of the services market. A better functioning internal market in *services* could generate further gains. The services sector accounts for 71% of the wealth generated by the UK economy, of which the Directive covers over 60% or £400bn of Gross Value Added. And yet services comprise only 32% of exports (27% of those to the EU) and 23% of imports (23% of those from the EU). On the foreign direct

investment side, services are more in line with GVA: services account for 59% of inward investment stocks (52% of those from the EU) and 60% of outward stocks (69% of those to the EU). There appears to be significant untapped potential for growth in UK services trade and investment.

## **5.2 Sectors and Groups Affected**

The scope of the Directive is set out in Annex E. Tables 2 and 3 below detail in broad terms the economic importance of service sectors covered by the provisions relating to the freedom of establishment and free movement of services in terms of their contribution to total UK GDP and employment.

The economic importance of the sectors covered by freedom of establishment account for 49% of UK GDP and 49% of UK employment. These sectors include: electricity, gas and water; construction; wholesale and retail trade; hotels and restaurants; postal services; and real estate, renting and business services. In this last category temporary work agencies and private security services are now excluded in the amended proposal. They account for at most 1.4% and their exclusion has been taken into account in the amount that real estate, renting and business services contribute to GDP. It is more difficult to quantify accurately the economic importance of other services covered by freedom of establishment (privately funded education, such social and personal services as remain within the Directive e.g. activities of membership organisations, washing and dry cleaning, hairdressing and beauty treatments) due to limitations of the data.<sup>18</sup> However, we estimate that it would be around 4% of UK GDP and some 6.5% of UK employment. These figures are already incorporated into the total figure of 49% for both the contribution of services covered to UK GDP and employment.

Sectors covered by the provisions on free movement of services (Article 16) account for less of the UK's total GDP as a number of sectors are derogated. There are derogations for all Services of General Economic Interest, including the electricity, gas and water sectors; postal services; sewage, refuse disposal and sanitation; and so called 'activities reserved to a particular profession.' The free movement of services provisions apply therefore to around 44% of UK GDP and 44% of employment. This may be a slight overestimate because the scope of 'activities reserved to a particular profession' differs between Member States and the UK reserves very few activities compared to some other Member States.<sup>19</sup>

Full assessment of impacts requires consideration of economic, social and environmental effects. The most significant impacts of this proposal will be economic, and accordingly most consideration is given to this in section 5.3 and 5.4. Social and environmental effects for all options are summarised in section 5.5.

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<sup>18</sup> For example, available UK data on gross value added in the education, health and social care sectors does not distinguish between *privately funded services* which are covered by the Directive and *publicly funded services* which are not.

<sup>19</sup> In the UK there are not many activities that fall under this category, examples include architectural, engineering, legal and medical professions. In other Member States this category is wider and may include for example bakers. This limits the ability of UK service providers in sectors considered reserved to a particular profession in another member state from providing their services to this member state. Consequently the scope of service sectors to which free movement applies is reduced.

**Table 2: GVA (£m) and contribution to total UK GDP (2004)**

	FREEDOM OF ESTABLISHMENT		FREE MOVEMENT OF SERVICES	
	GVA (£m)	% UK GDP	GVA (£m)	% UK GDP
Electricity, gas and water	16,321	1.5	--	--
Construction	67,610	6.2	67,610	6.2
Wholesale and retail trade	128,365	11.9	128,365	11.9
Hotels and restaurants	33,753	3.1	33,753	3.1
Postal services	7,724	0.5	--	--
Real estate, renting and business activities	233,395	22.27	191,871	19.67
Education	2,963	0.2	2,963	0.2
Other social and personal services	36,235	3.74	30,044	3.35
<b>Total share of sectors covered in the economy</b>	<b>526,366</b>	<b>49%</b>	<b>454,606</b>	<b>44%</b>
<b>TOTAL ECONOMY</b>	<b>1,082,649</b>	<b>100</b>	<b>1,082,649</b>	<b>100</b>

Source: Eurostat

**Table 3: Employment and contribution to total UK employment (2004)**

	FREEDOM OF ESTABLISHMENT		FREE MOVEMENT OF SERVICES	
	Number (000s)	% UK Employment	Number (000s)	% UK Employment
Electricity, gas and water	136	0.5	---	---
Construction	1,474	4.8	1,474	4.8
Wholesale and retail trade	5,303	17.4	5,303	17.4
Hotels and restaurants	2,079	6.8	2,079	6.8
Postal services	301	1	---	---
Real estate, renting and business activities	3,786	12.4	2,898	9.4
Education	786	2.6	786	2.6
Other social and personal services	1,135	3.7	1,055	3.4
<b>Total share of sectors covered in total employment</b>	<b>15,000</b>	<b>49%</b>	<b>13,595</b>	<b>44%</b>
<b>TOTAL ECONOMY</b>	<b>30,452</b>	<b>100</b>	<b>30,452</b>	<b>100</b>

Source: Eurostat 2004

## **5.3 Analysis of Benefits**

### **Summary**

In this section we identify the quantifiable economic benefits that can be gained from the Services Directive (i.e. not the social and environmental benefits, which are dealt with separately in section 5.5). The most important of these by far is the welfare gain to the UK from the Services Directive, which provides an estimate of the economic benefit. The welfare gain captures the benefits that accrue to all those affected by the Directive, the main groups being: service providers; UK government and regulators; and consumers and employees. Where possible the welfare gains for these groups are monetised to illustrate how different groups are affected, but are not in addition to the figure for the welfare gain.

A difference in the benefits under option 2 and 3 due to the different implementation options for the single point of contact is also examined under the section on benefits to service providers/business. The benefits derived from the different implementation of the single points of contact are considered separately to the welfare gain and provide additional information in the assessment of the total benefits of options 1, 2 and 3 of the RIA.

The benefits for each option are:

**Table 4: Summary of UK benefits for each policy option (£m p.a.)**

<b>Option</b>	<b>Economic benefit</b>	<b>Business admin benefit</b>
1	0	0
2	5,000-5,600	210
3	5,000-5,600	3

Total benefit is based on a 0.9 - 1% increase in welfare = £6.3 - 7 billion annually. This is adjusted to reflect benefits lost by a more limited liberalisation under 'freedom to provide services' (Article 16) and, the effect of the deletion of the provision on free price setting.

### **Welfare Gain to society**

The welfare gain to the UK economy is taken as a measure of the economic benefit from adopting the Services Directive as opposed to not doing so. In the presentation of benefits described in this section the welfare gain is described in

terms of gains in final consumption expenditure for the UK economy.<sup>20</sup> Several recent studies attempt to estimate the welfare gains from the Services Directive for the EU25 as a whole but they also present the results for the different member states individually. These studies provide a basis for the estimation of the welfare gain for the UK under the different options. The most reliable study is Copenhagen Economics 2005a (see Annex I), although the study has limitations as to how accurate a result it can present of the total benefits from the Services Directive.

The studies on the Services Directive also present results for other indicators of the economy-wide benefits of the Services Directive. See Annex I for a comparison of these results. These macroeconomic (economy-wide benefits) can be used to show benefits for individual groups and are discussed further in the relevant group sections. Again these are just illustrative of benefits for different groups, not in addition to the overall figure obtained.

#### Benefits to Service providers/Business

The Services Directive should lead to increased trade liberalisation and improved service sector regulation in Member States. The former promotes greater cross border trade and FDI in services in the EU, which results in the benefits for service providers shown in the left hand column of Table 5. The benefits to service providers of improved service sector regulation are presented in the right hand column. Annex F provides greater details on these benefits.

**Table 5: Economic effects of trade liberalisation and better regulation**

Increased trade liberalisation in services in the EU	Improved service sector regulation in Member States
<ul style="list-style-type: none"> <li>• More efficient allocation of resources</li> <li>• Realisation of economies of scale</li> <li>• Greater innovation</li> <li>• Stronger competition</li> <li>• Access to new technology</li> <li>• Increased incentives for foreign direct investment (FDI)</li> </ul>	<ul style="list-style-type: none"> <li>• Administrative simplification</li> <li>• Removal of anti-competitive rules</li> </ul>

The gains to service providers presented in Table 3 deliver the following high-level macroeconomic benefits:

<sup>20</sup> This is the closest aggregate to measure welfare defined by Copenhagen Economics as comprehensive consumption.

- Increased productivity in the UK services sector and other parts of the economy, improving its competitiveness in the global economy.<sup>21</sup>
- High-levels of domestic output, employment, investment, wages and standards of living.
- A wider range of new, more innovative and better quality services at lower prices.<sup>22</sup>

The first of these macroeconomic benefits is the end result benefit to service providers from realising economies of scale, accessing new technologies and reducing administrative burden etc. The non-service-based business community also benefits from the greater productivity in the UK services sector because services provide inputs into their activities. The other macroeconomic benefits accrue to different groups and are discussed in the relevant sections.

#### Benefits to UK government and regulators

The government and regulators benefit from greater compliance of business with regulations due to a better comprehension on the part of business and greater ease of complying.

For the government there is the additional benefit of higher fiscal revenues, stemming from the macroeconomic benefit of ‘higher-levels of domestic output, employment, investment, wages and standards of living.’

#### Benefits to other groups

Consumers also gain from the overall beneficial macroeconomic effects: there is a wider range of new, more innovative and better quality services at lower prices, whilst an increase in employment leads to greater opportunities for job seekers to find employment. In addition, higher wages and improved standards of living mean society as a whole benefits.

### **Benefits of Option 1**

Option 1 involves the UK rejecting the amended proposal with enough other Member States to ensure that the Directive is not passed. In this event the UK will ‘do nothing.’ Option 1 should therefore be viewed as the benchmark, base case scenario against which to measure the benefits of the other options. The benefits of option 1 are set at zero.

#### **Benefits: Zero**

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<sup>21</sup> ONS analysis finds that SMEs that trade internationally are more productive than those that do not. As such, there may be a further fillip to productivity if the number of SMEs trading with other countries increases – since this greater competition may drive out less efficient firms in the domestic market.

<sup>22</sup> Greater innovation and investment could arise in two ways: first, by firms investing the cost savings made from the reduction in legal and administrative barriers, and secondly by the transfer across national borders of new technologies and more efficient business models and processes.

### Welfare Gain to society

The welfare gains stimulated by trade liberalisation in services would not occur and there would be no increase in GDP.

### Benefits to Service providers/Business

Service providers in the UK looking to establish in another Member State or supply services across national borders would continue to face national rules and requirements which act as significant barriers to entry. Accordingly, they would miss out on the gains from increased trade with Member States and the benefits of better regulation.

### Benefits to UK government and regulators

The UK Government would have lost an excellent opportunity to raise productivity, employment and standards of living, and would fail to reap the benefit from the higher fiscal revenues these increases would induce.

### Benefits to other groups

None of the benefits to other groups (greater variety, better quality, lower prices, higher wages, and more jobs) would be realised.

## **Benefits of Option 2**

Option 2 is for the UK to accept the amended proposal in its current form.

### **Benefits: A continuing annual benefit of £5,000-5,6000m.**

Estimates of the benefits from the amended proposal on the Services Directive are based on studies Copenhagen Economics 2005a and 2005b, CPB 2006 and Detica 2006. The results of these studies have been modified in view of the subsequent changes made to the scope of the Directive after the publication of the studies.

### Welfare Gain to society

There are significant uncertainties as to the actual economic impact of the Directive. This is because modelling trade liberalisation in services is still an imperfect science and the complexity of the Commission's proposals is difficult to capture accurately with an analytical framework. Annex G discusses these difficulties in greater detail.

However, the economic evidence on previous rounds of service sector liberalisation in the EU - set out in Annex H – strongly suggests that the economic benefits achievable could be significant. Analyses carried out so far on the Commission *original* proposal all suggest that the economic gains could be large with all Member States benefiting from greater productivity, increased output and employment, higher wages and cheaper services

Table 6 presents the results of the various studies for the UK. The welfare gain is given in terms of a single, sustained increase in the level of welfare. In the case of the Copenhagen Economic 2005a study for example this means that

the UK's welfare will be permanently 0.9 to 1.0% higher than it would have been without adopting the Services Directive and not just a one-off gain in welfare. This means the UK's welfare will be around £6.3 - 7 billion<sup>23</sup> a year higher than without adopting the Services Directive.

**TABLE 6: Summary of economic studies detailing the macroeconomic benefits to the UK of the original proposals**

<b>STUDY</b>	<b>GDP/ Total economic benefits</b>	<b>Country of Origin principle</b>
<b>Copenhagen Economics (2005)</b>	Total economic benefits up 0.9%	Accounts for around 10% of total benefits
<b>CPB Netherlands Bureau for Economic Policy Analysis (2006)</b>	GDP up 0-0.1%	Accounts for less than 20% of total benefits

Study 1: Copenhagen Economics (2005). *“Economic assessment of the barriers to the internal market for services.”* Study prepared for the European Commission. The figures reported in the above table relate to the Direct Policy Scenario.

Study 2: CPB Netherlands Bureau for Economic Policy Analysis (2006) *“The trade-induced effects of the Services Directive and the country of origin principle.”* The country of origin principle accounts for around 30% of the total economic benefits arising from increased cross-border trade following the Services Directive. This figures falls to less than 20% once the economic benefits of increased Foreign Direct Investment are taken into account.

The result from Copenhagen Economics 2005a provides the starting point for analysing the benefits under option 2. The reason why this study's result is preferred to that of the CPB is explained in Annex I, which provides a comparison of various studies on the services directive. The principle explanation however is that Copenhagen Economics provides a more comprehensive coverage of the Services Directive's impacts.

In reviewing the Copenhagen Economics result on welfare gains for the UK in the light of changes to the Commission's original proposal, it should be noted that the result cited in table 6 (for the original proposal) was a lower-bound estimate of the potential impact on the UK. This is because:

<sup>23</sup> Based on UK GDP (total final consumption expenditure) in 2004 of £1,007,488 million. The CE definition of comprehensive consumption covers goods and services and also the economic value of leisure. Leisure is not represented in ONS aggregates, but there is nothing to suggest that the gain envisaged would disrupt the normal trade-offs which people make between work and leisure.

- Their analysis only covers two thirds of the sectors covered by the proposed Directive which together account for 25% of EU GDP<sup>24</sup>;
- Their model does not allow for the longer-term effects of the proposed Directive – e.g. the increased rates of innovation that may ensue from increased competition.

The Copenhagen Economics result of a 0.9% increase in UK welfare from implementing the original Services Directive has to be reviewed in light of two developments concerning the European Commission's revised proposal.

First, the scope of the Directive has been reduced. All healthcare, most social services, gambling, services of temporary work agencies, private security services and audio-visual services have been removed from the scope of the Directive, along with certain official services of professions such as notaries. The exclusion of activities reserved for a particular profession from article 16 on the free movement of services may also affect the result. The impact of these deletions on the overall welfare benefits estimated by Copenhagen Economics is not likely to be that important because for the most part they were not included in Copenhagen Economics' original analysis. Their study only covered 2/3 of the services included in the original proposals: the regulated professions, business services and distributive trades. Only the widening of the exclusion for official services to cover those of notaries and the exclusion of activities reserved for a particular profession could affect the Copenhagen Economics result. The effect would be to reduce the overall welfare gain in terms of GDP. However, official services provided by notaries and activities reserved for particular professions do not contribute much at all to UK GDP (but regulated professions are forecast to show above average growth). Nevertheless, any reduction in Copenhagen Economics' result would be extremely small on this account.

The deletion of a provision on free price setting in article 15 (h) and (i) also serves to reduce the impact of the directive. This provision along with those in article 29 is explicitly mentioned by Copenhagen Economics as being of potentially greater economic importance than other provisions in the Directive. Fortunately article 29 remains in the Directive and it seems that this article was of greater significance than that of article 15 (h) and (i). The benefits of the Directive have been reduced by a magnitude of 5% to reflect the affect of the deletion of the provisions on free price setting.

The effect of the replacement of the Country of Origin Principle (CoOP) by the 'freedom to provide services' mechanism is more difficult to evaluate. Overall the changes to article 16 (formerly Country of Origin Principle) have weakened the impact of provisions to facilitate cross border provision of services.<sup>25</sup>

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<sup>24</sup> These are regulated professions (e.g. legal and accountancy services), wholesale and retail distribution and business services (e.g. IT services). The sectors not included in the study are construction services, leisure services and some educational services.

<sup>25</sup> The main changes in the new mechanism are a reduction in scope, the switch to a country of destination starting point and the widening of some of the derogations in Art 17. These changes are negative for service providers as they reduce the benefits of the former CoOP. As regards the economics, these

Consequently, the benefits of the Services Directive, which were derived from the freedom to provide cross border services, are lower. What proportion of the benefits of the Country of Origin Principle and therefore total economic benefits of the Services Directive are lost cannot be known with certainty because there are a multiplicity of uncertainties with respect to how the new Article 16 will be interpreted. The new 'freedom to provide services' mechanism does at least mean that some of the former benefits are retained i.e. things will be made easier for temporary providers.

As Table 4 shows, studies by Copenhagen Economics (2005b) and the CPB (2006) suggest that at a minimum around 10-20% of the total economic benefits of the original Directive could be attributed to the country of origin. On the basis of these results if the CoOP had been totally deleted the welfare gain in terms of GDP from the directive would be 10-20% lower. The 10% lower limit is considered to be an underestimate of the total value of the CoOP according to Copenhagen Economics themselves. For this reason we take the loss in benefits from the replacement of CoOP by 'freedom to provide services' to be the midpoint value of the range 10-20% assumed by Copenhagen Economics and the CPB i.e. 15%. This we feel is reasonable given that the new article 16 on the 'freedom to provide services' means that not all benefits of the CoOP are lost.

It can be concluded that the revised proposal would still deliver significant economic benefits. Adjusting the Copenhagen Economics result of a 0.9% increase in GDP for the reduction in benefits due to the new Article 16, we find a conservative estimate of the benefits to be an annual increase of between £5 and 5.6 billion in UK GDP.

#### Benefits to Service providers/Business

Significant benefits to UK service providers are expected from greater liberalisation of trade on the one hand and reducing administrative costs on the other.

- Reducing the regulation faced by service providers will encourage more services trade amongst EU Member States leading to the benefits identified in Table 5 above. The Directive would potentially reduce 40% of the barriers to establishment cited by service providers in the PWC report surveying a selection of UK businesses.<sup>26</sup>
- The Directive will reduce the administrative burden on business in two ways:
  - By requiring Member States to review their legislation regulating the access to and exercise of service provision to ensure that it is consistent with the 'better regulation' rules laid out in the Directive.

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negative changes probably outweigh the positive effects of deleting some other general derogations and the clearer limits on what host Member States may impose.

<sup>26</sup> For example, multiple requirements from different organisations for the same information but in different formats and with different certifications; restrictions over the legal form which a branch can take; and the need for senior staff to make personal representation in order to obtain authorisations

Member States will be obliged to amend or remove rules that are discriminatory, disproportionate or unnecessary.

- By the creation of single points of contact to facilitate compliance with the screened regulations.

A study<sup>27</sup> on behalf of the DTI by Detica estimated the administrative costs of two of the provisions in the Directive, namely Single Points of Contact (hereafter referred to as “SPC”) in Articles 6-8, and Mutual assistance in Articles 33-37, using a model based on the Dutch Standard Cost Model<sup>28</sup>. Their estimated benefits of the SPC to the UK are presented in Table 7 below, which provides an insight into the potential cost savings to business that are achievable from the creation of a single point of contact. There is great uncertainty as to what the actual cost savings would be since there is a lack of information about how much time is spent by non-UK businesses researching the UK prior to establishment. For this reason, the estimates should be treated with some caution.<sup>29</sup>

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<sup>27</sup> Study available at: [http://www.dti.gov.uk/ewt/services\\_directive\\_economics\\_studies.htm](http://www.dti.gov.uk/ewt/services_directive_economics_studies.htm)

<sup>28</sup> See Detica study, EU Services Directive: Evaluation of Administrative Costs, Section 2.1 Overview.

<sup>29</sup> The Directive could lead to estimated cost savings varying from a one-off reduction of £10,000 to a drop in ongoing costs of around £50,000 according to a report by PwC.

**Table 7: Estimated annual benefits to businesses in the UK arising from the creation of single points of information or completion**

	Single point of information	Single point of completion
<b>Benefits to non-UK business researching the UK</b>	£1.1m	£1.1m
<b>Benefits to non-UK businesses establishing</b>	£1.9m	£3.4m
<b>Benefits to UK business establishing in the UK</b>	--	£47.9m
<b>Benefit to UK business already operating (reduced operating costs)</b>	--	£160m
<b>Total annual benefit</b>	<b>£3m</b>	<b>£212.4m</b>

Source: Detica, table 2-12

Detica recommended that the SPC should initially offer a single point of information rather than a single point of completion for the following reasons:

- The scale and complexity of a single point of completion implementation project would make it very difficult to achieve within the 2-3 year period proposed in the Directive;
- Imposing a requirement to support all government to business transactions at the SPC removes any flexibility to target resources at those areas where most benefit can be achieved;
- A single point of information would align the SPC service with existing government to business services and the strategy for their ongoing development in support of government objectives in areas such as administrative simplification.
- The main effect of the single point of completion would be streamlining the administration of UK businesses. While this may be a desirable outcome, it is not the part of the remit of the Directive.

From table 7, it can be shown that 75% of the benefits of a single point of completion would accrue to UK businesses already operating in the UK. While it may therefore be a worthwhile exercise, the additional cost cannot be justified under the Directive's aim of encouraging cross-border services trade.

A single point of information would be a great improvement on what is currently offered by UK Government to businesses as it would allow a provider to:

- access all information
- complete all formalities (such as forms for licenses and authorisations)

necessary to provide a service in that Member State.

This means, for example a commercial construction company should be able to access and complete electronically via the point of single contact applications for: a scaffolding and hoarding licence, a skip permit, a petrol licence, a private business radio licence, waste carrier registration and registration to work on gas appliances or fittings. The company would also be able to access at the point of single contact information regarding regulations on: financial control, tax, national insurance, payroll, health and safety, data protection, pricing, advertising standards and so on.

What we envisage would be based upon existing services but those services would need improvements to ensure that the aims of the Directive are fulfilled. We would implement a point of single contact within UKinvest.gov, which would encourage providers to invest in the UK, and then introduce them to BusinessLink.gov where they can access all the necessary information and procedures. BusinessLink.gov would clearly explain what procedures were necessary, and in the case where a form was needed, it would direct the providers through deep links straight to the web page where the necessary form exists and can be submitted electronically.

#### Limitations to the benefits

The Directive would not address a number of the many factors that influence firms' business development decisions in expanding into the EU. Some of the barriers to the provision of services without establishment faced by UK firms would be reduced, but the more significant natural barriers, particularly those relating to culture, would remain.<sup>30</sup>

#### Benefits to UK government and regulators

There are potentially significant gains in government revenue, which would follow from the increased growth of consumption. The supply side impact on output will produce a consequent increase in tax revenue, in the absence of any reduction in rates. In the UK, total tax receipts are about 36% of GDP.

Additionally, the study by Detica suggests that the creation of single points of contact (SPC) may lead to increased compliance among service providers. The SPC may lead to a higher proportion of businesses complying with regulations without intervention by regulators being necessary. This would be achieved by providing businesses with clear information on applicable regulations, and simplifying the process of complying.

A small positive effect on the likelihood of non-UK businesses complying fully with regulations when they establish in the UK would provide a significant benefit to regulators.

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<sup>30</sup> Based on comments raised by firms surveyed as part of the PWC report

If the SPC leads to a 1 percentage-point increase in the proportion of businesses complying fully with regulations when they establish in the UK, this model predicts a 3.2% reduction in the overall long-term non-compliance rate. In the scenario where the SPC leads to a 1 percentage point increase in the proportion of compliant businesses remaining compliant each year, the model predicts a 16% reduction in non-compliance. These results indicate that a small change in the probability of each business complying has a significant effect on the overall rate of compliance, and that the effect is much greater if the operating compliance probability is increased rather than the establishment compliance probability. These impacts in turn lead to a reduction in enforcement costs for regulators.

Benefits to other groups

Consumers and producers in the UK will benefit from a fall in the cost of services that they purchase from both domestic and foreign firms. The significant changes are as follows:

**Table 8: Price reductions for services**

	<b>Regulated professions</b>	<b>Business services</b>	<b>Distributive trade</b>
Cost of services provided by UK firms	-8.0	-0.6	-2.9
Cost of services provided by other EU firms	-7.7	-0.9	-2.8

Source: Copenhagen Economics (2005a)

As a consequence of the increase in welfare (comprehensive consumption), total employment in the UK would increase by up to 0.5%, or 100,000 - 144,200 jobs. Concurrently, real wages would increase by an average of 0.7%.

**Benefits of Option 3**

Option 3 involves the UK accepting the Amended Proposal subject to seeking the following further amendments:

- Single points of contact are points of information, not points of completion: the costs benefit analysis of these two alternatives strongly favours the former. (*Economic implication.*)
- The Directive does not prevent the UK upholding standards on health and safety and sensitive policy areas. (*Social and Environmental implications.*)

**Benefits: A continuing annual benefit of £5,000-5,600m.**

Welfare Gain to society

There will be no change in the economic benefit to the UK economy from adopting option 3 as opposed to option 2.

The welfare gain to the UK under option 2 has been estimated taking into account the impact of the Directive on 38 regulatory barriers. Only 2 of these 38 barriers are relevant to the SPC. Therefore the way in which the SPC is implemented (whether by single point of *information* or single point of *completion*) will have no significant impact on the macroeconomic benefits of the Services Directive.

#### Benefits to Service providers/Business

Table 7 above showed a summary of estimated annual benefits under the single point of information and the single point of completion. There are fewer benefits from a single point of information as opposed to a single point of completion but the benefit-cost ratio for the single point of information is much higher.

The benefits of the two different options should be evaluated in relation to the objective of the Directive. Detica in their analysis make the following point:

“While the total annual benefit of a single point of completion is much higher than that of a single point of information, over 98% of that benefit accrues to UK businesses. This suggests that while a single point of completion may be a worthwhile exercise for the UK, its major effect does not contribute to the Directive’s aim of encouraging cross-border services trade.”  
(Detica 2006)

#### Benefits to UK government and regulators

In addition to the cost reduction for a single point of information, there is also the benefit of having avoided undertaking a high risk implementation project of the “scale and complexity”<sup>31</sup> of the single point of completion within the 3 years allocated by the Commission.

#### Benefits to other groups

These remain the same as under option 2.

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<sup>31</sup> Detica recommendations, section 2.9, EU Services Directive: Evaluation of Administrative Costs, [http://www.dti.gov.uk/ewt/eu\\_services\\_directive\\_evaluation\\_admin\\_costs.pdf](http://www.dti.gov.uk/ewt/eu_services_directive_evaluation_admin_costs.pdf)

## **5.4 Analysis of Costs**

### **Summary**

Costs (and benefits) need to be expressed relative to a baseline. The research sources for this report use as a comparator a baseline scenario in which the Services Directive is not implemented in the EU. There will be some costs from adopting the Services Directive, whereas the impact of not adopting it is nil in cost terms. The costs of the other options are shown relative to the 'do nothing' option, so no costs (or benefits) arise if the Directive is not implemented.

**Table 9: Summary of UK costs for each policy option (£m annualised over 5 years)**

<b>Option</b>	<b>Total cost</b>	<b>Policy cost</b>	<b>Business admin cost</b>	<b>Government admin cost</b>
1	0	0	0	0
2	92	0	0	92
3	2	0	0	2

As table 9 shows, the business admin costs are not calculated here but they are already incorporated into the Copenhagen Economics results for the overall welfare gains to the UK. The costs to Government of implementing the Directive are however not included in the Copenhagen Economics study and are instead estimated on the basis of the DTI-commissioned study undertaken by Detica.

The relevant costs that may arise under the various options consist of:

### **Policy costs**

These are resource costs imposed on the private sector by a proposal. The Services Directive is a deregulatory proposal, so it is anticipated to deliver net benefits to the private sector, i.e. its policy costs will be nil.

### **Administrative costs to business**

These are the costs to business of administrative compliance with regulation – such as familiarisation with the requirements, monitoring and demonstrating compliance. These are estimated using a standard cost model. In the case of the Services Directive some admin costs are provoked by the information obligations required by the Directive. These are already covered in the Copenhagen Economics study. More generally, however, the Services Directive is a deregulatory measure and so reductions in the administrative costs to business are expected, i.e. they will be negative (and expressed as benefits).

### Administrative costs to government

The Services Directive imposes some additional costs on the UK Government and regulators. These will depend largely on the way in which the provisions relating to the creation of Single Points of Contact and Mutual Assistance are implemented.

### **Costs of Option 1**

Option 1 involves the UK rejecting the amended proposal with enough other Member States to ensure that the Directive is not passed. Option 1 maintains the *status quo*/business as usual, so the costs of continuing without implementing the Services Directive are nil.

### **Costs of Option 2**

Option 2 is to accept the amended proposal in its current form.

### Policy costs

The Services Directive is expected to be of net benefit to business in the UK and other Member States, so there should be a net reduction of policy costs arising from implementation: this is scored under the welfare gain to society or economic benefit.

### Administrative costs to business

The Services Directive is expected to be of net benefit to business in the UK and other Member States, so there should be a net reduction of administrative costs to business arising from implementation: this is scored under business admin benefits (Table 4).

### Administrative costs to government

Additional administrative costs for the UK government and regulators will occur as a result of the Directive. Their size will depend largely on the way in which the provisions relating to the creation of Single Points of Contact and Mutual Assistance are implemented.

**Table 10: Potential range of total administrative costs to government.**

	<b>Lower bound</b>	<b>Upper bound</b>
<b>Total annual cost</b>	<b>2</b>	<b>92</b>

Source: Detica, tables 2-13 and 3-11 Single Points of Contact. Figures have been annualised over 5 years.

Articles 6-8 of the Directive provide for the creation of SPCs, at which service providers can complete all the administrative formalities necessary to establish or provide services in a Member State.

Two different approaches to meeting the SPC requirement were identified and compared in a study carried out for DTI by Detica<sup>32</sup>. These are effectively the minimum and maximum levels that define the range of possible provision:

**Approach 1: *Single point of information (minimum provision):***  
 providing information on relevant regulations and signposts to online processes managed elsewhere; or,

**Approach 2: *Single point of completion (maximum provision):***  
 providing a single location where all government to business transactions can be completed.

Within these two approaches, two strategies were short listed as the most cost effective ways of implementing them. The results for the strategy of adapting or extending the existing services of Business Link and UK Trade & Investment’s inward investment portal are reproduced in Table 10<sup>33</sup>.

As Table 10 below shows, setting up a single point of information would be considerably cheaper than a single point of completion. The single point of information provides the more cost-effective solution: annual benefits could amount to £3m, around 25 times its annual costs of £0.12million. The equivalent calculation for the single point of completion shows a benefit to cost ratio of less than three.

**Table 10: Implementation and annual operation costs of single points of information and completion using different strategies.**

	Single point of information	Single point of completion
	Strategy 2	Strategy 2
<b>Implementation costs</b>	£0.1m	£342m
<b>Annual operation costs</b>	£0.097m	£14.1m
<b>Total annual cost</b>	<b>£0.12m</b>	<b>90m</b>

Source: Detica, tables 2-11 and 2-13. Total costs assume implementation costs arise only in the first year and operating costs occur annually thereafter.

<sup>32</sup> Detica (2006) “EU Services Directive – Evaluation of administrative costs.” A study prepared by Detica for the DTI [http://www.dti.gov.uk/ewt/services\\_directive\\_economics\\_studies.htm](http://www.dti.gov.uk/ewt/services_directive_economics_studies.htm)

<sup>33</sup> Page 70 in the Detica report sets out the reasons as to why this implementation strategy is preferred.

### Mutual Assistance

Articles 33, 33a and 36 provide for mutual assistance aimed at promoting greater exchange of information between relevant competent authorities in the different Member States.

The provisions relating to mutual assistance include the adoption of the Internal Market Information (IMI) system comprising a Structured Information Exchange (SIE) module and a Competent Authorities Database (CAD).

Analysis by Detica considered (1) lower and (2) upper implementation options: (1) a limited implementation concentrated on rolling out to a relatively small number (100) of Competent Authorities (CAs); (2) a roll-out to all 750 CAs. The study showed that the costs were likely to be slightly lower for the limited option 1, and also states the limited option is likely to provide a lower risk approach to implementation and would provide a closer match with other similar UK implementation projects.

The main difference between the two implementation options is likely to be in the costs of implementing and operating IMI. There may be some benefits of IMI that are realised to a different extent depending on the implementation option. However there are two competing factors affecting the relative benefits of the two options, one that favours option 1 (limited option) over option 2 and a second favouring option 2. Without practical experience it is difficult to judge which factor will turn out to be most significant. This implies a judgement on the choice of option should be based on a comparison of the costs and the level of risk associated with implementing the options.

Option 1 – a lower implementation of the IMI system - should be preferred to option 2 at this moment in time as it offers the lower cost scenario and lower risk. However, Detica recommends that the level of CA involvement be reviewed frequently, especially early in the project, so that an optimal approach can be developed.

**Table 11: Government administrative costs of each implementation option (NPV over 5 years)**

	Lower limit	Upper limit
<b>UK Competent Authorities registered</b>	100	750
<b>Cost of National Contact Points</b>	£0.8m	£0.5m
<b>Cost of Competent Authorities</b>	£0.8m	£1.2m
<b>Total annual cost</b>	<b>£1.6m</b>	<b>£1.8m</b>

Source: Detica, table 3-11. Figures have been annualised over 5 years.

### **Costs of Option 3**

Option 3 is to accept the amended proposal but subject to the UK seeking further amendments covering single points of contact and some other economically neutral technical changes to meet policy objectives. The assessment of costs here assumes that these amendments are achieved.

#### Policy costs

The policy costs are not expected to differ from those shown under Option 2. The benefits to UK businesses arising from the Directive's net reduction of policy costs are scored under the welfare gain to society or economic benefit.

#### Administrative costs to business

The administrative costs to UK businesses are not expected to change significantly from those shown under Option 2. Again there is a net reduction of administrative costs, which is treated as a Benefit and shown in Table 4.

#### Administrative costs to government

The range of expected annual costs under Option 2 was £2 - 92m, consisting of the costs of providing a national contact point and the costs of appropriately equipping the competent authorities to play their role. The key difference between Option 3 and Option 2 is that the single point of completion (the high end of the range of costs) is replaced by single point of information.

So for Option 3 the costs are expected to be very much less than those of Option 2, and whilst the absolute benefits are less, the benefit-cost ratio is much better. This is because every £1 spent on a single point of information will deliver £25 of benefits to business, as opposed to a single point of completion that will deliver £2.50 of benefits for every £1 spent.

### **Social and Environmental Effects**

Broad social and environmental impacts of the Services Directive are hard to identify let alone quantify. In terms of broad social impacts services are more important for employment in London and the South East of England than elsewhere in the UK, a slightly larger proportion of the benefits might be expected to go to London and the South East. The Directive is not intended to have any significant effect on the environment, and the UK is committed to ensuring that the Directive does not negatively impact on UK standards in sensitive social and/or environmental areas.

Option 3 allows for the UK to press for amendments to the Directive to meet agreed policy objectives these areas. In this sense Option 3 has additional net benefits to Option 2 because the costs under Option 2 of social or environmental objectives not being met are avoided.

## CONSULTATION WITH SMALL BUSINESS: THE SMALL FIRMS' IMPACT TEST

SMEs are disproportionately affected by the barriers to establishment and cross-border trade in services because the costs of overcoming them are often independent of firm size. These costs may be particularly high for those UK services providers which are SMEs as the process of setting up a business in other Member States can be longer and more complex than in the UK (see Annex A).

In extreme cases, these costs may be sufficiently large that they act as a barrier to entry, deterring the smaller UK service providers from starting up in other Member States. This may help to explain the results of preliminary analysis carried out by the Office for National Statistics (ONS) for the DTI which showed that small UK service providers tended not to feature prominently in cross-border trade with other Member States (see Annex J).

The proposed Directive, which aims to reduce the administrative burden through the creation of single points of contact and other simplification measures, should therefore benefit UK SMEs significantly<sup>34</sup>. This view is supported by initial feedback from the Small Business Service and small business organisations.

As illustrated previously, the creation of any form of single points of contact should deliver cost savings to service providers considering establishing in other Member States like the UK. In some cases, the reduction in administrative costs may be sufficiently large that they no longer constitute a barrier to trading in other parts of the EU. This may lead to increased numbers of UK SMEs benefiting from the business opportunities and efficiency savings that the larger market offers them (e.g. realisation of economies of scale).

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<sup>34</sup> The benefits that SMEs could enjoy from the Directive were set out in section 5.3 on benefits.

## 7. COMPETITION ASSESSMENT

### *The affected markets*

Annex E sets out the markets affected by the proposed Directive. As Table 8 below shows, SMEs account for the bulk of total turnover and employment in many of the service sectors covered by the Directive although its share varies across the different sectors<sup>35</sup>. In 2004, SMEs accounted for between 47% and 83% of sectoral employment and 50% to 87% of sectoral turnover. The SME share was lowest in the wholesale and retail trade sector and highest in the health and social work sector.

**Table 12: Importance of SMEs and micro businesses in different service sectors in the UK, 2004**

	Enterprises	Employment	Turnover
<b>Construction</b>	100 (98.2)	82.9 (59.6)	66.1 (40.4)
<b>Wholesale and retail trade; repairs</b>	99.8 (93.5)	47.2 (25.7)	49.9 (19.1)
<b>Hotels and restaurants</b>	99.8 (87.7)	55.4 (26.6)	59.7 (33.1)
<b>Real estate, renting and business activities</b>	99.8 (96.4)	68.1 (41.2)	68.9 (37.3)
<b>Education</b>	-- (79.5)	-- (23.8)	-- (32.5)
<b>Other community, social and personal services activities</b>	100.0 (98.1)	74 (54.9)	52.3 (34.4)

Source: Small Business Service figures (2005) [www.sbs.gov.uk](http://www.sbs.gov.uk)

Data for electricity, gas and water cannot be reported due to problems of disclosure.

Education: Figures likely to be larger as they do not include enterprises without employees (for disclosure reasons). Figures in brackets denote the contribution of micro businesses to total enterprise numbers, employment and turnover. The majority of micro businesses are sole proprietorships and partnerships run by owner-managers without any staff.

### *Impact on competition*

The Directive should have a pro-competitive effect on the affected markets. In reducing the national rules and regulations, which foreign service providers must comply with to enter the market of another Member State, it is reducing the barriers to entry that they face.

Increased competition should be reflected in the form of falling prices and higher output and employment. This is illustrated in Table 13 below, which shows that the Directive should have the greatest impact in the regulated profession sector where the barriers to entry are greatest. The results of Copenhagen Economics suggest that the regulated professions sector – which

<sup>35</sup> Variations may in part reflect differences in barriers to entry. High SME shares may suggest that barriers to entry are low while lower SME shares may suggest the contrary. However, there are likely to be a number of other factors involved. There may also be significant variations in SME within particular service sectors – e.g. the real estate, renting and business services sector that includes some highly regulated service activities such as law, architecture and accounting.

has the highest barriers – should experience the largest relative fall in price and increase in value added and employment.

**Table 13: Results of the Copenhagen Economics study: UK sectoral gains**

	<b>Regulated business services (e.g. accountancy)</b>	<b>Unregulated business services (e.g. IT services)</b>	<b>Distributive trade</b>
<b>Employment (% change)</b>	<b>5.4</b>	<b>1.3</b>	<b>2.0</b>
<b>Market size<sup>36</sup> (% change)</b>	<b>2.2</b>	<b>1.8</b>	<b>0.6</b>
<b>Cost of services<sup>37</sup> (% change)</b>	<b>-8.0</b>	<b>-0.6</b>	<b>-2.9</b>
<b>Cross border trade<sup>38</sup> (% change)</b>	<b>12.2</b>	<b>2.7</b>	<b>5.4</b>
<b>Value added<sup>39</sup> (% change)</b>	<b>7.5</b>	<b>2.1</b>	<b>2.9</b>

Source: Copenhagen Economics (2005a)

### ***Compensatory Simplification Measures***

By definition, the Directive is deregulatory. The creation of single points of contact and other simplification measures contained in the Directive should reduce the administrative burdens on services providers establishing in other Member States or providing services across national borders.

These should more than outweigh the costs to service providers of complying with additional information requirements contained in Article 26, 27(2) and (3) (information concerning professional indemnity insurance), 28 (information concerning after-sale guarantees) and 30(3) (information concerning conflicts of interest for multidisciplinary activities).

<sup>36</sup> Market size is defined as the total value of output by domestic and foreign firms.

<sup>37</sup> Cost of services is defined as the weighted average of the price of outputs provided by domestic and foreign firms.

<sup>38</sup> Cross border trade is defined as the value of total exports within the EU

<sup>39</sup> Value added is defined as the sum of payments to input of labour and capital. It is an alternative approach to measuring the value of services output.

## **8. ENFORCEMENT AND SANCTIONS**

The general intention of the proposed Directive is deregulatory – it is aimed at lowering the barriers to the European internal market in services, both regarding the freedom of establishment of service providers in the Member States and the free movement of services between Member States. The key challenges in the implementation of this Directive will be to review the regulatory framework of the UK with a view to ensuring that any such barriers do not continue to exist here, unless they can be justified under the terms of the Directive. Much of the work to achieve this will be within Government and with those bodies that have regulatory functions.

It follows that much of the enforcement of this Directive will require ensuring that Government and other regulatory bodies apply rules in relation to the establishment of service providers which accord with the principles laid out in the Directive, and that they abide by mutual recognition rules as regards other Member States' service providers.

Enforcement will in principle be achieved by imposing statutory duties on bodies responsible for the various regulatory regimes and rules dealing with access to and exercise of service activities that are covered by the Directive. This approach to enforcement will apply to the bulk of the Directive. It could be that, where Government does not itself deal with an activity that is regulated, consideration will have to be given to the need for sanctions should the relevant body fail to comply with the Directive.

Beyond matters requiring implementation primarily through legislative means, there is the requirement to set up “single points of contact” set out in Articles 6 to 8. The role of “single points of contact” is to facilitate access to services markets for service providers, by providing a single point of contact for all the procedures and formalities needed to access and operate in the market, including applications for authorisation from the competent authorities.

However, there will also be provisions that will require more than the imposition of statutory duties on regulatory bodies. The proposed Directive will impose obligations on service providers, for example, in the areas of provision of information and in relation to complaint handling.

Member States currently operate their own services consumer protection regimes (underpinned by harmonised minimum EC standards) with differing levels of consumer protection around Europe. The same issues apply to other fields covered by the proposed Directive, for example environmental protection. The proposed Directive poses a challenge to this by requiring greater access to service recipients across the Community by service providers from all Member States, as a result of the simplification of establishment rules and of the free movement of services rules for services delivered by providers established in other Member States. The proposal may have to deal with sensitive areas of law and care will be required to avoid undue impacts on such areas.

For the Directive to be acceptable to Member States there will have to be mutual trust between them on issues such as relative levels of consumer protection. One way in which the proposed Directive seeks to achieve that trust is by including obligations on service providers to give significant amounts of information to customers before and at the time that any contract is made. For the proper enforcement of these obligations it will be necessary that national measures provide for sanctions in the event of non-compliance.

There are requirements to provide information in Articles 26, 27(2) and (3) (information concerning professional indemnity insurance), 28 (information concerning after-sale guarantees) and 30(3) (information concerning conflicts of interest for multidisciplinary activities) which require, among other things, the service provider to give their contact details, company registration number if appropriate, VAT number, their governing regulatory body (if the provider is a member of a regulated profession), and, at the request of the customer, other service-related information. In the implementation of the Directive, the UK will be under an obligation to ensure that these requirements on service providers are adequately and effectively implemented and that breach of the provisions of the Directive is subject to sanctions that are effective and dissuasive, whilst not being disproportionate to the breach.

The options available to Government for the types of sanctions which could be introduced in relation to the breach of such provisions range from providing remedies to customers of service providers (for example, a cause of action for breach of statutory duty), to administrative fines, and finally to criminal penalties. Also, given the broad extent of the measure, which will apply to the vast majority of contracts for the supply of services, the ability of Government itself to ensure compliance in relation to such an immense field may be limited.

Article 32 of the proposed Directive requires providers to respond to complaints by service recipients as soon as possible and to make best efforts to find appropriate solutions. Again, this is of importance in relation to consumer protection concerns of Member States and the Government will need to consider the appropriate sanction for failure to comply.

The Directive also requires Member States, and their competent authorities, to provide mutual assistance to each other to facilitate the monitoring and supervision of the activities of service providers operating cross-border in other Member States. This throws up significant legal and practical difficulties and whilst the Directive does seek to deal with some of these, there is likely to be a considerable amount of work to do to ensure that such a system could work in practice.

## 9. MONITORING AND REVIEW

As part of the implementation process, the Government should put in place arrangements to collect information on compliance from both Government and non-Government regulatory bodies. It may also be advisable to investigate the experience of service recipients in the UK in accessing services from other Member State providers and of service recipients in other Member States in accessing services from UK providers.

The levels of UK services trade and investment (both with other EU Member States and the rest of the world) can be monitored using UK trade and investment statistics issued by the Office of National Statistics. They should give a good indication of whether the Directive has increased the UK's trade in services with the EU.

Monitoring of prices for services in the UK and other EU Member States will also give an indication of whether the Directive has delivered more competition in UK service markets. Increased trade and competition should mean more choice and lower prices for recipients of services, both businesses and private individuals.

Monitoring is built into the Directive itself in so far as there are requirements for reporting and mutual evaluation. The proposal prohibits certain requirements concerning access to and the exercise of a service activity (Article 14) and, during the transposition period, requires Member States to examine systematically whether they exist in its legal system and, if so, eliminate them. There is also a 'grey list' of other requirements to be evaluated, and Member States must review their regulatory systems in the light of the conditions laid down in the Directive. Requirements must be non-discriminatory, objectively justified by an over-riding reason relating to the general interest and satisfy the principle of proportionality. Member States must report on this evaluation by the end of the transposition period (currently scheduled for 2008). Each report will be submitted to other Member States and the Commission will consult interested parties. This "peer review" process will enable exchange between Member States of best practice in the modernising of the regulation of services. The Commission will then produce a synthesis report with proposals, where appropriate, for future initiatives.

All of these forms of monitoring could feed into any review by the Commission of the success of the Directive: progress on the completion of the Internal Market for services. It could also be useful as an input to the Internal Market Scoreboard.

Given the high degree of uncertainty associated with the exact magnitude of the costs and benefits of the proposals, DTI will undertake a review of the Directive three years after implementation. This is in line with the Government's commitment to systematic post-implementation reviews of major pieces of legislation.

There is also an obligation imposed on the Commission, following the completion of reporting procedures referred to above, to report every three years on the application of the Directive. This would be accompanied, where appropriate, by proposals for amendments to the Directive.

## 10. CONSULTATION

### Within Government

A large number of Government Departments and Agencies were consulted by DTI: see Annex C4 of the consultation document  
<http://www.dti.gov.uk/ewt/servgen.pdf>

### Public Consultation

The consultation was completely open and the consultation document is available on the DTI website:

<http://www.dti.gov.uk/ccp/topics2/servicesDirective.htm>

A summary of the response received is also available

A large number of groups or organisations received the consultation document directly – see Annex C5 of the consultation document.

## **11. RECOMMENDATION**

Option 3, which is for the UK to broadly accept the amended proposal while seeking further amendments, is recommended. The economic policy benefit to the UK of the Services Directive will be in the region of £7.7 to 8.6 billion annually. The precise figure for the total net benefit of the Directive depends on whether option 2 or 3 is implemented (see Table 3). The quantifiable difference in net benefit between option 2 and option 3 can be considered to be negligible (£200 million compared with overall benefits of around £8 billion). However, taking the social and environmental impacts into account as well, Option 3 is clearly preferable, as it allows for amendments to meet agreed UK policy objectives, as well as delivering a higher benefit-cost ratio due to its reduced implementation costs.

## Annex A: The barriers to trade in services in the EU

In 2002, the European Commission published a report, “*The State of the Internal Market for Services*” in which it presented the results of a consultation exercise on the specific barriers hampering the development of cross-border trade in services in the EU<sup>40</sup>. The report drew up an inventory of 91 different barriers preventing or slowing down cross-border trade in services between Member States. The majority of the barriers identified were new or long-standing legal obstacles<sup>41</sup> including:

- *Quantitative restrictions on the number of service providers that can operate in a given geographical market.* These restrictions can be based on surface area or population size and generally place national operators at a distant advantage over new potential entrants
- *Territorial restrictions relating to the geographical market.* These restrictions can limit the trading activities of service providers to a particular area or region meaning that new potential entrants will have to establish in several locations if they wish to operate on a national scale
- *Nationality and/ or residence requirements.* These requirements mean that shareholders, managers and / or staff may have to be nationals or permanent residents in the country of establishment.
- *Length and complexity of registration and authorisation procedures.* The requirement to complete a large number of administrative procedures and/or register with numerous trade associations, chambers of commerce and professional bodies can impose significant costs on services providers
- *Restriction on multidisciplinary activities.* Providers of different services (e.g. accountants and lawyers) may be prevented from working together in some Member States in order ensure their professional independence and autonomy
- *Requirements on the legal form and internal structure.* Service providers may only be able to establish in another Member State for example if they take the form of a company with limited liability
- *Requirements for professional qualifications.* Some Member States require service providers - particularly in the professional services – to

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<sup>40</sup> This marked the completion of the first of the Commission’s two-stage strategy to create an internal market for service, which had begun in December 2000 with the publication of its report, “*An Internal Market Strategy for Services*.” This report can be found at: [[http://europa.eu.int/comm/internal\\_market/services/docs/services-dir/com-2000-888/com-2000-888\\_en.pdf](http://europa.eu.int/comm/internal_market/services/docs/services-dir/com-2000-888/com-2000-888_en.pdf)]

<sup>41</sup> The Commission attributes these barriers to a combination of the following factors: a lack of trust by Member States in the quality of regulation in other EU countries; a failure to update national legislation so that it remains compatible with EC law; and a deliberate intent by some Member States to protect national economic interests.

have proof of professional qualifications which may not be required in other EU countries

- *Requirements relating to cross-border use of inputs and posted workers.* Restrictions exist which prevent service providers from using regular suppliers of materials and equipment from their home Member State. The cross-border movement of permanent and temporary workers can also be hampered by lengthy and burdensome administrative procedures and high complex rules on their use.
- *Rules on commercial communications.* Advertising and promotion by the professional services is banned in some Member States while for other services, restrictions on the content and medium of advertising and promotion may exist
- *Pricing rules.* Fixed, minimum, maximum and recommended pricing arrangements are common practice in many Member States, particularly in relation to services provided by the professional services

There were also a number of non-legal barriers to trade in services in the EU identified in the Commission's report, in particular:

- *Lack of information.* Service providers lack information about the rules and regulations in the Member State in which they are looking to establish and knowledge about the competent authorities and the appropriate procedures and formalities.
- *Differences in language and culture.* In the course of establishing in another Member State, documents may need to be translated and notarised which can impose a significant cost on service providers, particularly SMEs. There may also be difficulties associated with adjusting to the business culture, consumer values and habits of the Member State or region.

**Annex B: The length and complexity of the business start-up process in the EU**

<b>COUNTRY</b>	<b>PROCEDURES (Number)</b>	<b>DAYS (Number)</b>
Austria	9	29
Belgium	4	34
Czech Republic	10	40
Denmark	3	5
Estonia	6	35
Finland	3	14
France	7	8
Germany	9	24
Greece	15	38
Hungary	6	38
Ireland	4	24
Italy	9	13
Latvia	7	18
Lithuania	8	26
Netherlands	7	11
Poland	10	31
Portugal	11	54
Slovak Republic	9	25
Slovenia	9	60
Spain	10	47
Sweden	3	16
<b>United Kingdom</b>	<b>6</b>	<b>18</b>

Source: Doing Business in 2006

Does not include Cyprus, Luxembourg and Malta

## Annex C: The costs of starting up a company in the EU

This is a comprehensive but not exhaustive inventory of the different costs incurred in start-up a company in 22 Member States. Cyprus, Luxembourg and Malta are the three countries not included.

COUNTRY	ESTIMATED COST OF ESTABLISHMENT
<b>Austria</b>	<ul style="list-style-type: none"> <li>• Notarising Articles of Association (€1000-1500)</li> <li>• Registration of company (€130)</li> <li>• Additional court fees (€31 plus a further €23 per director)</li> </ul>
<b>Belgium</b>	<ul style="list-style-type: none"> <li>• Notarise deed of incorporation (approx €1300)</li> <li>• Publicise formation of company (€202.31)</li> <li>• Registration of company (€130 plus €38 for VAT registration)</li> </ul>
<b>Czech Republic</b>	<ul style="list-style-type: none"> <li>• Certificate of clear criminal record (approx €2)</li> <li>• Certificate of ownership of premises (approx €3.5)</li> <li>• Notarise Articles of Association (approx €620 including VAT plus approx €1 per notarised signature)</li> <li>• Trade license (approx €35 or €70 per trade license)</li> <li>• Registration of company (approx €172)</li> </ul>
<b>Denmark</b>	<ul style="list-style-type: none"> <li>• No charge</li> </ul>
<b>Estonia</b>	<ul style="list-style-type: none"> <li>• Notarise company formation (approx €160 + 18% VAT)</li> <li>• Registration of company (approx €192-1925)</li> </ul>
<b>Finland</b>	<ul style="list-style-type: none"> <li>• Registration of company (€330)</li> </ul>
<b>France</b>	<ul style="list-style-type: none"> <li>• Publish notice of incorporation (€150)</li> <li>• Registration of company (€116.19)</li> <li>• Purchase company books (€40 per book + €3.11 stamping fee)</li> </ul>
<b>Germany</b>	<ul style="list-style-type: none"> <li>• Notarise Articles of Association (€769 + 16% VAT)</li> <li>• Register Articles of Association (€422)</li> <li>• Publicise formation of company (€31)</li> </ul>
<b>Greece</b>	<ul style="list-style-type: none"> <li>• Approval of company name (€30)</li> <li>• Filing of company files (€440-approx 30,000)</li> <li>• Signing of Articles of Association (€740-1320)</li> <li>• Stamp (€0.30)</li> <li>• Obtain legal certification (€5.8)</li> <li>• Registration of Articles of Association (€5 for photocopying and stamp dues)</li> <li>• Print summary of Articles of Association (€280)</li> <li>• Registration of company (€130 annual fee)</li> <li>• Official seal (€40)</li> </ul>
<b>Hungary</b>	<ul style="list-style-type: none"> <li>• Preparation of legal documents (approx €1025)</li> <li>• Notarise signature and documents (approx €150)</li> <li>• Registration of company (Stamp duty approx €400 +</li> </ul>

	publication fee approx €100)
<b>Ireland</b>	<ul style="list-style-type: none"> <li>• Official Oath (€5)</li> <li>• Filing of necessary materials (€60 + 0.5% of issued capital)</li> <li>• Company seal (€20.28)</li> </ul>

Source: Doing Business, World Bank, 2005

Note: Where appropriate national currencies have been converted into euros using the exchange rates set out on the European Central Bank's website on 30<sup>th</sup> November 2005.

(Cont...)

<b>COUNTRY</b>	<b>ESTIMATED COST OF ESTABLISHMENT</b>
<b>Italy</b>	<ul style="list-style-type: none"> <li>• Execution of incorporation (€3000 – 4000)</li> <li>• Cost of corporate books and authentication fees (€11 per 100 pages + €30 register fee per 500 pages)</li> <li>• Government grant tax (€309.87 per year)</li> <li>• Registration of company (€1,100 including annual membership fee, stamp duty and registration tax)</li> </ul>
<b>Latvia</b>	<ul style="list-style-type: none"> <li>• Notarise signatures (approx €12)</li> <li>• Registration of company (approx €145)</li> <li>• Publish notice of formation (approx €6)</li> </ul>
<b>Lithuania</b>	<ul style="list-style-type: none"> <li>• Notarise agreement/ incorporation (approx €115)</li> <li>• Registration of company (approx €35)</li> <li>• Official seal (approx €9-26)</li> </ul>
<b>Netherlands</b>	<ul style="list-style-type: none"> <li>• Approval of company name (€85)</li> <li>• Signing of Articles of Association (€1750)</li> <li>• Notarise company details (€90.76)</li> <li>• Registration of company (€155-930 annual fee)</li> </ul>
<b>Poland</b>	<ul style="list-style-type: none"> <li>• Notarise company agreement (€1280 - 6410)</li> <li>• Register for VAT (approx €400)</li> <li>• Registration of company (Registration fee approx €255 + publication cost approx €125)</li> </ul>
<b>Portugal</b>	<ul style="list-style-type: none"> <li>• Approval of company name (Certification €56 + Identification card €14)</li> <li>• Deed of incorporation (Fixed fee €86 + stamp duty 0.4% of total share capital)</li> <li>• Registration of company (Fixed fee €56 + extra €28 if urgent + €34 for final ID card and €76 per page publication fee)</li> <li>• Declaration of commencement of activities (€17.80 + €0.78 for required forms)</li> <li>• Stamp company books (€14 plus tax stamp; €0.50 for each page)</li> <li>• Register shareholders meeting book (€14 + tax stamp; €0.5 for each page)</li> </ul>
<b>Slovak Republic</b>	<ul style="list-style-type: none"> <li>• Certificate of clean criminal record (approx €2.5 per person)</li> </ul>

	<ul style="list-style-type: none"> <li>• Company name check (approx €2.5)</li> <li>• Notarise Articles of Association (approx €1 per signature)</li> <li>• Application for trade license (approx €26 or €53 for a special license)</li> <li>• Opening a bank account (approx €13)</li> <li>• Registration of company (approx €265)</li> </ul>
<b>Slovenia</b>	<ul style="list-style-type: none"> <li>• Notarise company deeds (approx €990)</li> <li>• Registration of company (approx €120-275 depending on number of founders)</li> <li>• Company stamp (approx €16-25)</li> </ul>
<b>Spain</b>	<ul style="list-style-type: none"> <li>• Approval of company name (€7-14)</li> <li>• Public deed of incorporation (€500)</li> <li>• Registration of company (€350)</li> </ul>
<b>Sweden</b>	<ul style="list-style-type: none"> <li>• Registration of company (approx €210)</li> </ul>
<b>United Kingdom</b>	<ul style="list-style-type: none"> <li>• Prepare memorandum of association (approx €140)</li> <li>• File incorporation documents (approx €75)</li> </ul>

Source: Doing Business, World Bank, 2005

Note: Where appropriate national currencies have been converted into euros using the exchange rates set out on the European Central Bank's website on 30<sup>th</sup> November 2005.

## **Annex D: The importance of creating a better functioning internal market for services in the EU**

The creation of a better functioning internal market for services in the EU can be a powerful spur to productivity, employment and prosperity not just in the UK but also in all Member States. This belief is based on three key facts:

1. Services form the backbone of the modern economy
2. Services are the engine of productivity growth
3. Services account for small proportion of total trade

### **1. Services form the backbone of the modern economy**

In the post-war era, the structure of the UK economy has changed considerably with a shift away from agriculture and manufacturing towards services industries. This process has accelerated considerably in the last two decades as illustrated in Chart D.1 below.

[Insert Chart D.1 here]

Today, services are not only purchased for final consumption (e.g. tourist services) but are used intensively by businesses to help promote, distribute and sell other goods and services in the economy (e.g. management consulting services). Indeed, services have become so embedded in the production of manufactured goods that the boundary between manufacturing and services has all but disappeared<sup>42</sup>.

As such, the economic importance of services in an economy may actually be much greater than official statistics suggest. In 2004, total services in the UK – comprising the electricity, gas and water sector, construction, market services (e.g. business services) and non-market services (e.g. health and social care) – was valued at some £839.5bn and employed some 21.8 million people. This represented some 81% and 86% of UK GDP<sup>43</sup> and employment respectively<sup>44</sup>.

### **2. Services are the engine of productivity growth in the economy**

There is much evidence to show that productivity growth in the service sector is the key driver of total productivity growth in the economy. For example, a recent paper by the European Commission<sup>45</sup>, reported that productivity growth in *business-related services*<sup>46</sup> contributed around 75 percent to total annual productivity growth in the US and the EU15 between 1995 and 2001.

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<sup>42</sup> For example, goods are increasingly being sold as part of a wider package that includes services such as repairs and insurance.

<sup>43</sup> Gross Domestic Product (GDP) is defined as Gross Value Added (GVA) at current basic prices, where GVA is equal to the difference between the value of output and the value of inputs used to produce it plus subsidies less taxes (such as VAT).

<sup>44</sup> Employment figures include the total number of employed and self-employed.

<sup>45</sup> European Commission (2004), "*Business-Related Services: a key driver of European competitiveness – an enhanced economic analysis*" DG Enterprise working paper. This can be found at:

[http://www.europa.eu.int/comm/internal\\_market/services/docs/brs/competitiveness/2004-workingpaper-econanalysis\\_en.pdf](http://www.europa.eu.int/comm/internal_market/services/docs/brs/competitiveness/2004-workingpaper-econanalysis_en.pdf)

<sup>46</sup> These comprised network services, distributive trade, financial services and business services

Yet, as evidence from various OECD studies on the economic performance of specific services sector clearly shows (see Table 1 below), in most cases productivity growth in the US – both for the economy as a whole and for individual service sectors – tends to be higher than the EU average and the largest Member States including the UK<sup>47</sup>. The European Commission attributes this in part to the fragmentation of the internal market for services in the EU and the resulting lack of competition<sup>48</sup>.

Table 1: Labour productivity growth by activity for selected countries, 1995-2003

	US	EU15	France	Germany	UK
Distributive trade	4.7	1.0	0.3	0.8	2.4
Hotels and restaurants	0.1	-1.4	-0.7	-6.3	-0.1
Transport and storage	0.6	3.9	1.0	2.3	2.0
Post and telecommunications	3.9	--	7.1	14.5	7.9
Finance and insurance	5.2	1.6	-1.2	3.5	2.8
Real estate, renting and business services	-0.3	-1.8	-1.4	-1.8	0.6
Community, social and personal services	-0.1	0.0	0.6	0.0	0.6
<b>Total business related services</b>	<b>2.8</b>	<b>0.7</b>	<b>0.0</b>	<b>1.4</b>	<b>2.1</b>
<b>Total economy</b>	<b>1.6</b>	<b>0.9</b>	<b>0.9</b>	<b>1.4</b>	<b>1.7</b>

Source: Vogt, L. (2005) "The EU's Single Market: At Your Service?" OECD Economics Department Working Paper, No 449.<sup>49</sup>

### 3. Services account for a low proportion of trade

Cross-border trade in services in the EU has risen dramatically in recent years, driven in part by advances in technology and communications, which have improved the "tradability" of services. Over the period, 1994-2004, trade in commercial services<sup>50</sup> within the EU15 more than doubled from some £141.9m to £301.3m. Yet, despite this growth, services still account for around 20% of total trade in the EU. As Chart D.2 below illustrates, this figure has changed little since 1994, even falling slightly during the mid 1990s.

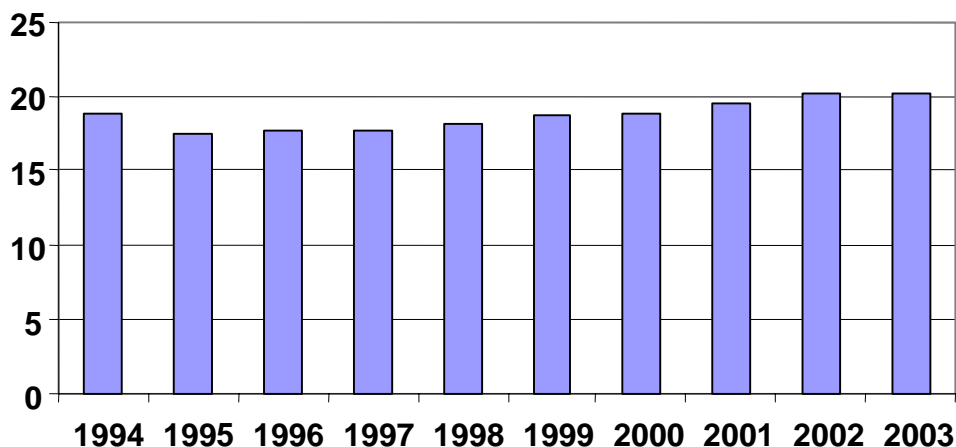
<sup>47</sup> For more information on differences in productivity growth between the US and EU see European Commission (2004), "Business-Related Services: a key driver of European competitiveness – an enhanced economic analysis"; Netherlands Ministry of Economic Affairs (2004) "Fostering excellence: challenges for productivity growth in Europe" [http://www.ggdc.net/pub/fostering\\_excellence.pdf](http://www.ggdc.net/pub/fostering_excellence.pdf); Van Ark (2005) "Does the European Union need to revive productivity growth?" Groningen Growth and Development Centre [http://www.ggdc.net/pub/online/gd75\(online\).pdf](http://www.ggdc.net/pub/online/gd75(online).pdf) and Van Ark., B. and O'Mahony, M. (2003) "EU productivity and competitiveness: an industry perspective" Publication by DG Enterprise of the European Commission. This report can be found at: [http://europa.eu.int/comm/enterprise/enterprise\\_policy/competitiveness/doc/eu\\_competitiveness\\_a\\_sector\\_al\\_perspective.pdf](http://europa.eu.int/comm/enterprise/enterprise_policy/competitiveness/doc/eu_competitiveness_a_sector_al_perspective.pdf)

<sup>48</sup> European Commission (2005) "Second Implementation Report of the Internal Market Strategy, 2003-2006", COM (2005) 11 final 27.01.2005, page 7-8

<sup>49</sup> Vogt, L. (2005) "The EU's Single Market: At Your Service?" OECD can be found at: [http://www.oilis.oecd.org/oilis/2005doc.nsf/43bb6130e5e86e5fc12569fa005d004c/a7ce5a97ea540230c1257099002cc1dc/\\$FILE/JT00191215.PDF](http://www.oilis.oecd.org/oilis/2005doc.nsf/43bb6130e5e86e5fc12569fa005d004c/a7ce5a97ea540230c1257099002cc1dc/$FILE/JT00191215.PDF)

<sup>50</sup> Commercial services are all services less government services. Given that trade in government services is negligible, these two measures are more or less the same.

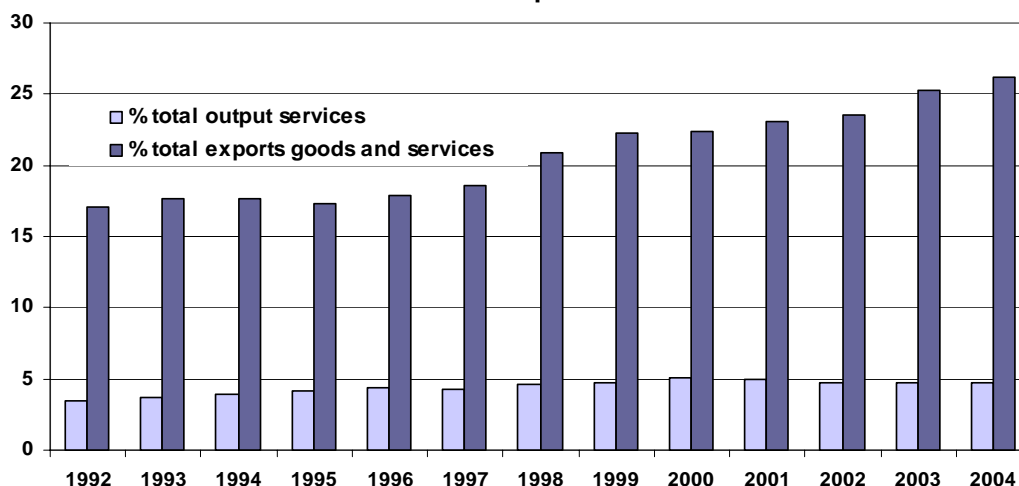
**Chart D.2: Services as a % of total trade within**



Source: WTO International Trade Statistics, 2005

The same is true for the UK. UK exports to the EU nearly trebled between 1992 and 2004, rising from some £13.5bn to £39.4bn<sup>51</sup>. Yet, as Chart D.3 below reveals the proportion of total UK exports to the EU accounted for by services over the same period only rose from 17% to 26% while UK service exports to the EU as a proportion of total UK domestic output in services increased only slightly from 3.5% to 4.8%. These figures reinforce the low level of trade in services<sup>52</sup>.

**UK service exports to the EU**



Source: DTI estimates based on ONS figures in the National Accounts Blue Book and UK Balance of Payments Pink Book

<sup>51</sup> This covers the following types of service products: transportation, travel, communications, construction, insurance, financial, computer and information, royalties and license fees, other business, personal, cultural and recreational and government.

<sup>52</sup> A European Commission paper, "EU sectoral competitiveness indicators" published in 2005, showed that the proportion of services produced in Member States which are exported to other parts of the EU tends to be much lower than goods and that for many services, the percentage of domestically produced services exported to other EU countries is close to zero. For more information see page 65 of the report which can be found at: [http://europa.eu.int/comm/enterprise/enterprise\\_policy/competitiveness/doc/eu\\_sectoral\\_competitiveness\\_indicators.pdf](http://europa.eu.int/comm/enterprise/enterprise_policy/competitiveness/doc/eu_sectoral_competitiveness_indicators.pdf)

Taken together, these three facts suggest that the creation of an internal market for services in the EU may deliver significant increases in productivity, employment and standards of living in the UK services sector with substantial knock-on effects on other sectors of the economy<sup>53</sup>.

The actual size of the gains achievable will depend in part on how much the level of trade in services in the EU can feasibly be raised. Owing to the specific nature of trade in services – namely that they are often produced and consumed locally – it may not be possible to raise the level of trade in services to that of goods.

However, as we will see later, the fact that today services are of greater economic importance relative to goods in many Member States, means that the benefits achievable have the potential to be larger than those arising from the Internal Market Programme (IMP) for goods, even though the level of trade in services within the EU remains comparatively lower<sup>54</sup>.

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<sup>53</sup> For example, manufacturing firms who are also customers of other service providers will benefit from lower prices and improved services. This is particularly true for business services, which can be key to the development and success of start-ups and growing firms.

<sup>54</sup> In its report *"The Internal Market – Ten Years without Frontiers"*, published in 2002, the European Commission reported that ten years after the completion of the internal market in 1992, EU GDP was 1.8 percentage points or €165bn higher than it would otherwise have been and that 2.5 million new jobs had been created as a result. This report can be found at:  
[http://www.europa.eu.int/comm/internal\\_market/10years/docs/workingdoc/workingdoc\\_en.pdf](http://www.europa.eu.int/comm/internal_market/10years/docs/workingdoc/workingdoc_en.pdf)

## Annex E: The scope of the Directive

NACE BRANCH AND ACTIVITY	FREEDOM OF ESTABLISHMENT	FREE MOVEMENT OF SERVICES
<b>E ELECTRICITY, GAS AND WATER SUPPLY</b> <ul style="list-style-type: none"> <li>• Electricity, gas, steam and hot water supply</li> <li>• Collection, purification and distribution of water</li> </ul>	YES YES	NO NO
<b>F CONSTRUCTION</b>	YES	YES
<b>G WHOLESALE AND RETAIL TRADE, REPAIR OF MOTOR VEHICLES ETC</b> <ul style="list-style-type: none"> <li>• Sale, maintenance and repair of motor vehicles etc</li> <li>• Wholesale trade</li> <li>• Retail trade</li> </ul>	YES YES YES	YES YES YES
<b>H HOTELS AND RESTAURANTS</b>	YES	YES
<b>I TRANSPORT, STORAGE AND COMMUNICATION</b> <ul style="list-style-type: none"> <li>• Land transport, transport via pipelines</li> <li>• Water transport</li> <li>• Air transport</li> <li>• Supplementary and auxiliary transport agencies</li> <li>• Postal services</li> <li>• Telecommunications</li> </ul>	NO NO NO NO YES NO	NO NO NO NO NO NO
<b>J FINANCIAL INTERMEDIATION</b> <ul style="list-style-type: none"> <li>• Financial intermediation</li> <li>• Insurance and pension funding</li> <li>• Activities auxiliary to financial intermediation</li> </ul>	NO NO NO	NO NO NO
<b>K REAL ESTATE, RENTING AND BUSINESS ACTIVITIES</b> <ul style="list-style-type: none"> <li>• Real estate</li> <li>• Renting of machinery and equipment</li> <li>• Computer related activities</li> <li>• Research and development</li> <li>• Other business activities</li> </ul>	YES YES YES YES YES	YES YES YES YES YES
<b>L PUBLIC ADMINISTRATION AND DEFENCE; COMPULSORY SOCIAL SECURITY</b>	NO	NO
<b>M EDUCATION</b>	ONLY PRIVATELY FUNDED SERVICES	NO

<b>N HEALTH AND SOCIAL WORK</b> <ul style="list-style-type: none"> <li>• Health</li> <li>• Social work</li> </ul>	ONLY PRIVATELY FUNDED SERVICES	NO
<b>O OTHER COMMUNITY, SOCIAL AND PERSONAL SERVICE ACTIVITIES</b> <ul style="list-style-type: none"> <li>• Sewage and refuse disposal, sanitations and similar activities</li> <li>• Activities of membership organisations</li> <li>• Recreational, cultural or sporting activities</li> <li>• Other service activities</li> </ul>	YES  YES [YES] YES	YES  YES [YES] YES
<b>P PRIVATE HOUSEHOLDS WITH EMPLOYED PERSONS</b>	YES	YES
<b>Q EXTRA TERRITORIAL ORGANISATIONS AND BODIES</b>	YES	YES

## **Annex F: The economic benefits of the Services Directive**

The economic benefits generated by the Services Directive can be broken down as follows:

1. The benefits arising from the removal of cross border barriers to trade in services in the EU
2. The benefits arising from the better regulation of service sectors in Member States

### ***The benefits arising from the removal of cross border barriers to trade in services in the EU***

In 2004, the UK government published a paper, "*Trade and the Global Economy: The role of international trade in productivity, economic reform and growth*"<sup>55</sup> in which it identified six economic effects of trade liberalisation:

#### **1. More efficient allocation of resources**

Increased trade in services in the EU will likely lead to a re-allocation of resources (e.g. capital and labour etc) within and between EU economies as Member States including the UK move to specialise further in the provision of those services which they can supply most efficiently.

#### **2. Realisation of economies of scale**

The increase in market size will provide some service providers in the UK to reduce further their unit costs of production by allowing them to operate on a larger scale than may have been possible previously.

#### **3. Greater innovation**

A larger market will provide UK service providers will an even greater economic incentive to develop new products and apply more efficient methods of providing services since the rewards to be made from doing so would be comparatively greater.

#### **4. Stronger competition**

The removal of some regulations and restrictions should lower the barriers to entry in all Member States, allowing more foreign competitors to enter the market, resulting in more competition. In the UK, the impact of reducing such barriers, in terms of stronger competition - is likely to be small since many service sectors are already highly competitive.

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<sup>55</sup> HM Treasury and DTI (2004) "*Trade and the Global Economy: The role of international trade in productivity, economic reform and growth*". This report can be found at: <http://www.dti.gov.uk/ewt/trade170504.pdf>

#### 5. Access to new technology

Improved trade in services between Member States may promote the cross-border transfer of new technologies and more efficient product processes leading to the availability in the UK of new and more innovative types of services<sup>56</sup>

#### 6. Increased incentives for FDI

There may also be new opportunities for UK service providers to invest in the development of new technologies and processes being carried out in other Member States, the results of which can be applied domestically<sup>57</sup>.

### ***The benefits arising from the better regulation of service sectors in Member States***

#### 1. Simplification of administrative procedures and authorisation schemes

The creation of single points of contact (SPCs) and other simplification measures should make it easier for service providers looking to establish in another Member States or supply services across borders to do so in two ways. First, it should make it easier for service providers to find all the necessary information about the laws and regulations of other Member States. Second, it should help reduce the length and complexity of the administrative formalities that must be completed before the service provider can start trading.

The overall reduction in the administrative burden brought about by these measures may, in some cases, be sufficiently large that search and set-up costs no longer constitute a barrier to supplying services to other Member States. As a result, some of the service providers which had been previously deterred from expanding into other Member States may now do so, benefiting from the business opportunities and efficiency savings which the larger market offers them (e.g. realisation of economies of scale).

#### 2. Better quality regulatory environment

The removal of restrictions, regulations and requirements (e.g. those relating to advertising in the professional services sector) that can act as barriers to entry and prevent firms operating efficiently should increase the level of competition in the service sectors covered by the Directive.

By virtue of the Country of Origin Principle (CoOP), service providers operating across borders will no longer need to modify their business merely to take account of differences in national regulatory regimes or seek legal advice on issues relating for example to national rules on advertising and promotion. This should reduce further the costs to service providers choosing to expand operations into other Member States.

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<sup>56</sup> See for example Coe and Helpman (1993) and Eaton and Kortum (1995)

<sup>57</sup> See for example Proudman and Redding (1997)

### Economic evidence

In a separate piece of work, the CPB<sup>58</sup> have estimated that reducing the administrative burden on all businesses by 25% may deliver an initial increase in EU25 GDP of 1.0%, rising to 1.7% in the longer-term once the effects of extra investment and research and development spillovers are taken into account. In value terms, we estimate this would correspond to an increase in EU25 GDP at market prices of approximately €104bn (around £70.7m) and €177bn (around £120m) respectively<sup>59</sup>.

[Assuming that the economic impact of lowering administrative burdens on the UK economy is similar to the EU, then we estimate that an additional 1% reduction in the administrative burden on service providers in the UK brought about by the Directive will increase UK GDP by an extra £290m in the first instance and £500m in the longer term<sup>60</sup>.]

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<sup>58</sup> See CPB Netherlands Bureau for Economic Policy Analysis (2004) "*Reducing the administrative burden in the European Union*" <http://www.cpb.nl/nl/pub/memorandum/93/memo93.pdf>

<sup>59</sup> EU25 GDP at market prices for 2004 was some €10409bn (Source: European Commission, Eurostat). Euro values are converted into sterling using the exchange rate £1=€1.46)

<sup>60</sup> UK Gross Value Added in 2004 stood at £1,033,324m (ONS Blue Book). The number of businesses in service sectors, F, G, H, K, O, P and Q in 2004 stood at 3,059,930, representing 71.45% of all businesses in the UK (SBS figures). A 1% reduction in the burden on businesses in these services sector will therefore deliver initial benefits of: £1,033,324m x 0.7415 x 1 x 1/25 = £289m. A 1.7% reduction in the burden will deliver longer-term benefits of: £1,033,324m x 0.7415 x 1.7 x 1/25 = £491.9m. Of course, UK service providers operating solely in the domestic market will experience smaller reduction in the administrative burden than for example businesses from other Member States supplying the UK market.

## **Annex G: The difficulties of quantifying the economic benefits of trade liberalisation in services and the proposed Directive**

There are significant uncertainties as to how large the economic benefits arising from the creation of a better functioning internal market for services in the EU are likely to be. These uncertainties stem from a number of difficulties associated with modelling trade liberalisation in services:

- There are complex linkages between the services sectors and other sectors of the economy which as yet have not been perfectly captured in any analytical framework<sup>61</sup>
- Many of the barriers to trade in service are non-tariff in nature (e.g. language) which are difficult to identify and measure accurately
- There is a paucity of good quality disaggregated economic data on services (e.g. output, employment, trade and investment) which limits any detailed sectoral analysis
- Available trade data does not capture all cross border movements in services – in particular those resulting from the cross-border movement of labour<sup>62</sup>.

The actual economic impact of the Directive is even harder to predict accurately because of three further difficulties with the modelling:

- The Commission's proposals are extremely complex with numerous sectoral and horizontal derogations which cannot be fully captured in an analytical framework
- There is incomplete information about service sector regulation in each of the 25 Member States, which makes it difficult to identify and quantify the legal and regulatory barriers to trade in services and the actual effects of lowering them.
- It is difficult to determine accurately the extent to which the Directive will lower legal and regulatory barriers to trade in services and what the actual economic effects will be.

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<sup>61</sup> For example, some services are embedded in the production of manufactured goods while others are sold as part of a package (e.g. after sales services)

<sup>62</sup> The World Trade Organisation (WTO) distinguishes between four different modes of trade in services: Mode 1 (cross-border supply) relates to the movement of services from the territory of one Member States into that of another. Mode 2 (consumption abroad) refers to situations where a service recipient moves into another Member States' territory to obtain the service. Mode 3 (commercial presence) relates to the establishment of a territorial presence (e.g. setting up a new company or acquiring a local firm) in another Member State in order to supply a service. Mode 4 (presence of natural persons) refers to persons moving to the territory of another Member States in order to provide a service (e.g. construction workers). More information can be found on the WTO website on the General Agreement of Trade in Services (GATS) [http://www.wto.org/english/tratop\\_e/serv\\_e/gatsqa\\_e.htm](http://www.wto.org/english/tratop_e/serv_e/gatsqa_e.htm)

## **Annex H: The economic gains of previous service sector liberalisation in the EU**

Since the mid 1980s, the EU and Member States have taken positive steps to liberalise various service sectors including telecommunications, financial services, transport and energy.

The conclusions of a recent study by Copenhagen Economics<sup>63</sup> suggest that the economic benefits generated by market opening measures carried out in the network industries during the 1990s in the EU15 are substantial.

The study by Copenhagen Economics focused on seven network industries: electricity, gas, postal services, telecommunications, air (passenger) transport, urban (passenger) transport and rail (passenger and freight) transport – which together accounted for nearly 6% of total EU GDP in 2001.

They estimated that by 2001, the market opening measures carried out since 1990 would have had led to:

- An increase in EU15 welfare of some 1.9% or €98bn with the largest gains in those Member States which began the process of liberalisation early and/or have made the most progress
- A rise in total net employment in the EU15 of some 500,000 with the bulk of the new jobs created in the services sector which rely heavily on the network industries, particularly electricity and telecommunication services

The study concluded that the UK would be among the Member States gaining most from the liberalisation of the network industries. It estimated that between 1990 and 2001, total welfare would increase by some 1.4% or around €17bn and total net employment would rise by around 0.4%.

### ***Supporting evidence***

These results are supported by evidence on the economic performance of three EU service sectors since liberalisation in the 1980s and 1990s: telecommunications, air transport and energy.

#### Telecommunications sector:

- EU15 employment increased by almost 9 percent between 1997 and 2003
- EU15 turnover nearly doubled between 1997 and 2001
- EU15 productivity – crudely measured in terms of turnover per person employed – rose between 1995 and 2001

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<sup>63</sup> Copenhagen Economics (2005) “Market Opening in the Network Industries” This can be found at: [http://www.copenhageneconomics.com/publications/Market\\_opening.pdf](http://www.copenhageneconomics.com/publications/Market_opening.pdf)

- The price of local, national and international calls has fallen between 1997 and 2004
- Consumers have greater choice of telephone operators and internet and broadband operators

#### Air transport sector:

- EU15 employment rose by 12 percent between 1988 and 1996
- The average productivity of the ten largest European airlines increased by 53% between 1990 and 1996 in terms of output per employee while operating costs per unit of output fell by around 13 percent over the same period
- The price of promotional fares has fallen by some 41 percent between 1992 and 2000 driven in part by the entry of low-cost carriers into the market while the price of business and economy fares has also fallen
- Consumers now have greater choice in terms of carriers offering scheduled passenger and freight services and destinations in different Member States

#### Energy sector:

- The price of electricity and gas for households and industry has dropped in many Member States between 1995 and 2001.

## Annex I: A comparative analysis of studies on the potential economic impact of the Commission's original proposals

This annex sets out to assess to what extent the various studies<sup>64</sup> on the Services Directive are complements or substitutes for one another in the analytical literature base on the Services Directive. Secondly the annex evaluates the relative merits of the studies. The overall aim is to judge how useful the different studies are in informing the debate and guiding the decisions of policy makers.

Below is a summary table showing the estimated gains from implementing the services directive in full and the CoOP for the EU25 according to the different studies. A similar table, table 3 presents the main scope and methodology of the studies on page 5. They serve as a tool for an easy comparison of the studies.

Table 1: Impact of the Services Directive and CoOP on the EU25

	Welfare Gains			Country of Origin Principle	Trade Flows	FDI Flows
	GDP	Employment	VA in services			
<b>CPB (2004)</b>					30-62%	20-35%
<b>CPB (2005)</b>	0.3 - 0.7% (€32-74bn)	0	0.5-1%	33-42% of total GDP gains (€10-33bn) 40% of consumption gains and VA in services		
<b>CE(2005a)</b>	0.6% (€37bn)	600 000	1.10%	N/A		
<b>CE (2005b)</b>	0.6% (€37bn)	600 000	1.10%	7-9% of total welfare gains (€2-4bn)  Loss of 12000 jobs		
<b>Europainstitut</b>	0.70%	612 000	1.65%	N/A		

### Compliments or Substitutes?

Answering this question allows us to determine how comparable different studies on the services directive are. If the studies are more complements it is useful in that they can be used to explain or defend particular issues relating to the services directive that they tackle but this may limit the scope for comparison. With studies that analyse the same question it is possible to judge their relative strengths and weaknesses. This is important for policymakers

<sup>64</sup> The studies evaluated are Copenhagen Economics 2005a, Copenhagen Economics 2005b, CPB 2004, CPB 2005, and Europainstitut. A full bibliographical reference for the studies is contained in the main bibliography of the RIA.

because it is important to know which sources provide the most robust evidence, in this case on the services directive.

In terms of the analytical literature that exists on the services directive the following observations were made:

- There is some variation among the studies reviewed here in relation to the aspect of the Services Directive explored (cross border trade only – CPB 2004 & 2006; cross border trade and FDI – CE 2005a & 2005b and Europainstitut)
- Secondly, to some extent the studies are complementary due to differences in approach e.g. the way they model the effect on regulation.
- On the whole the studies deal with the same research questions relating to the services directive
- CPB 2006, CE 2005A, and Europainstitut 2005 all research the welfare benefits of the directive for the EU. CPB 2006 and CE 2005b also treat the impact of the CoOP.
- There is scope for comparing the strengths and weaknesses of the studies to determine whether one study is superior to the others.

#### **Who should we trust? – The relative merits of the studies**

The paper judges the relative merits of the studies' results for welfare benefits and the CoOP on the basis of differences in scope and methodology. For a comparison of the scope and methodologies of the studies see table 3 on page

#### **Welfare effects – Services Directive implemented in full i.e. in accordance with 2004 EU Commission draft.**

Of the three studies that deal with this question, two of them CE 2005A, and Europainstitut 2005, have very similar results. The CPB 2006 study also on the face of it appears to estimate the same GDP gains but closer inspection of the scope of the study reveals the results are not exactly comparable. The bullet points below present the main conclusions from the comparison of the **Europainstitut study** with the other two.

- Although the results of *CE2005a* and the *Europainstitut* are very similar. The proportion of the benefits attributed to FDI and cross border trade in the overall benefits of the services directive differs.
- The CE study attributes much more of the overall benefits to FDI than the Europainstitut study does.
- Evidence supports the CE view that FDI effects are relatively more important in the overall gains from services trade liberalisation than cross border trade effects.
- Unlike the *Europainstitut*, the *CPB2006* only looks at the gains due to increased cross border trade and not FDI too.
- In order to estimate its gains from cross border trade, the Europainstitut uses the CPB 2004 study's estimate of increases in cross border trade.
- The GDP increase for the CPB study assuming an increase in cross border trade of 44% is 0.46%. This is the same result as the

Europainstitut for its scenario without FDI effects. This means the GDP gains from the cross border trade effects are the same in both studies.

The study by the Europainstitut while providing useful analysis to contribute to the overall evidence base on the services directive does not use as sophisticated techniques in the estimation of the welfare effects as studies by the CPB and CE. For example Europainstitut adopts partial equilibrium analysis whereas the other two studies apply complex general equilibrium models to assess the welfare effects.

The focus will now be on the relative merits of **CPB 2006** and **CE2005a** in order to determine which results give the most accurate assessment of the welfare benefits from the services directive. Table 2 helps this analysis by highlighting some of the characteristics of the studies and whether these are likely to lead to an underestimation or an overestimation of the final results.

Table 2 Comparison of factors impacting on the accuracy of the results

	<b>Factors that underestimate benefits</b>	<b>Factors that overestimate benefits</b>
<b>Copenhagen Economics</b>	<ol style="list-style-type: none"> <li>1. Reduction in level of regulations only</li> <li>2. Excludes sectors covered by directive – only 2/3 covered</li> <li>3. Dynamic effects excluded</li> </ol> <p><u>CoOP</u> Data Coverage, treatment of supporting provisions Cross border trade effects underestimated</p>	<p>Excludes policy costs and transformation costs of sectoral shifts</p>
<u>CPB</u>	<ol style="list-style-type: none"> <li>1. Reduction in cross country differences in regulation only</li> <li>2. Excludes sectors covered by directive</li> <li>3. Dynamic effects excluded</li> <li>4. Not account for FDI</li> <li>5. Assumes fixed Labour Supply</li> </ol>	<p>Excludes policy costs and transformation costs of sectoral shifts</p> <p>Includes sectors not covered</p> <p><u>CoOP</u> FDI excluded Cross border trade effects?</p>

- The significant advantage of the CE 2005a study is that it includes the effects for FDI in addition to cross border trade.
- The CPB's result is underestimated in this regard. If the FDI were to be included in the CPB results, its estimate of the overall gains would be larger than CE.

- CE's result is likely to be underestimated because (i) it underestimates the cross border trade effects (ii) it only covers 2/3 of the sectors included in the directive
- That the Services directive will impact on employment is a more realistic than the assumption made by the CPB that the labour supply is fixed, implying it cannot expand to meet greater demand.
- CE underestimates total gains to the services directive but the CPB's top estimate of an increase in GDP of 0.7% should be viewed cautiously as an estimate of gains from cross border trade alone.

### **Welfare effects - Country of Origin Principle**

Two of the studies examine the effects of this controversial part of the Services Directive, CPB 2006 and CE 2005b.

- The benefits from the CoOP should be higher than CE suggests because it underestimates the cross border trade effects.
- However the lack of FDI effects in the CPB's estimate, leads to an overestimation of the benefits from the CoOP.
- The CPB state that with FDI effects included in their model they could expect the CoOP to account for less than 20% of the total trade and FDI induced effects.
- This could still be almost double CE result.

### **Final assessment**

There seems more scope for the analytical literature base on the services directive to be used as complements rather than substitutes. Although the overarching research questions covered are the same in CPB 2006, CE 2005a and Europainstitut and in CPB 2006 and CE 2005b, their differences in scope and methodology imply particular issues are raised by one paper and not in others. For example the CE studies shows gains due to reduced levels of regulation whilst in the CPB studies the gains arise from reducing cross-country differences in regulation. In addition, the Europainstitut study can provide insights into the link between the trade, competition and productivity effects of the services directive.

The differences in scope and methodology give rise to the limitations of the studies and in comparing these it is possible to make an assessment as to whether one study provides a more complete picture of the welfare benefits and the contribution of the CoOP. The study by the CPB only looks at the cross border trade induced effects and not the FDI effects which are if anything more important. From this point of view CPB 2006 cannot be as authoritative a source of the overall benefits of the services directive as CE2005a. This implies CE2005a is a stronger source. However taking the CPB study together with the CE2005a gives a better picture of the accuracy of the CE's studies. For example it was found that CE2005a underestimates the cross border trade induced effects and this reflected on its estimate of the benefits of the CoOP. The view that seems to have formed during the course of this analysis is that

the most realistic estimates of the welfare benefits are somewhat higher than illustrated in the CE reports. In terms of the CoOP the benefits will fall somewhere between the estimates provided by the two papers accounting for 10% in the CE2005b paper and less than 20% for the CPB - to be confirmed in the CPB's next empirical study on the services directive.

Currently, there is a limited analytical literature base on the services directive. All the studies have a role to play in informing the debate but obviously some have more weight than others. CE2005a and 2005b provide the most reliable estimates as to the welfare benefits and those of the CoOP but for the most complete picture this study should be used in conjunction with the research by the CPB. The services directive is evolving as it goes through the legislative process and the analytical evidence based will do too. Therefore the studies reviewed here will not have the final word on the subject.

Table 3: Comparison of the study methodologies.

	<i>CPB 2004</i>	<i>CPB 2006</i>	<b>CE 2005a</b>	<b>CE 2005b</b>	<b>Europainstitut</b>
<b>Modelling approach for Service Directive impacts</b>	Cross-country differences	Cross-country differences	Level of regulation	Level of regulation	Cross-country differences
<b>Services coverage</b>					
<b>Excluded but in SD</b>	Travel	Travel	Construction, leisure, health, education	Construction, leisure, health, education	Travel
<b>Included but not in SD</b>	Financial services	Financial services			
<b>Impact on cross border trade and FDI</b>	Cross border trade & FDI	Cross border trade	Cross border trade & FDI	Cross border trade & FDI	Cross border trade & FDI
<b>EU Countries used in data</b>	14 ; 17 countries	14 ; 17 countries	19 countries	19 countries	11 countries
<b>General equilibrium (GE) or Partial equilibrium (PE) analysis.</b>	General Equilibrium	General Equilibrium	General Equilibrium	General Equilibrium	Partial Equilibrium

## Annex J: UK patterns of trade in services with EU

The ONS analysed patterns of cross-border trade and investment in services between the UK and the EU for the period 2000-2003 and the characteristics of UK service providers that trade and do not trade with the EU. Some of their conclusions are summarised in Tables J.1 and J.2 below.

They found that most trade in services between the UK and the EU takes place in computer services, other business services (i.e. professional services) and, to a lesser extent, wholesaling. Trade in retailing, hotel and restaurant and construction services was considerably lower<sup>65</sup>.

It was noted that the propensity of the large UK firms (i.e. those employing more than 250 people) to trade with other Member States tended to be greater than for SMEs and that a greater proportion of larger SMEs traded with other Member States than small SMEs<sup>66</sup>.

On the basis of the ONS initial findings, we conclude that SMEs in the computer and business services sectors would benefit the most from the Directive, as these are the main types of services currently traded. There may be some increase in the propensity of SMEs to supply services such as hotels and restaurants, however, this is likely to be small given that such services are usually produced and consumed locally.

*Table J.1: UK –EU trade patterns in selected services and the importance of SMEs*

	Level of UK trade	Direction of UK trade	% of SMEs that export	% of large firms that export
Construction	Low	Importing	1 – 3	6
Wholesaling	Moderate	Exporting and importing	6 – 13	15
Retail	Low	Importing	1 – 3	6
Hotels and restaurants	Low	Importing	1 – 3	6
Real estate	Low	Importing	1 – 3	6
Computer services	High	Exporting	6 – 49	46
Other business services	High	Exporting	9 – 24	26

Source: ONS (2005) “A picture of UK trade and foreign direct investment in services” A study carried out by the ONS for DTI

*Table J.2: UK-EU patterns in other business services and the importance of SMEs*

<sup>65</sup> The level of trade in construction services may be higher than the ONS analysis suggests. This is because the study focused on services supplied across borders or establishment in other Member States. It did not include services supplied by the cross-border movement of labour, which is key mode of supply in the case of construction services.

<sup>66</sup> While this may suggest that there are barriers to trade in services that disproportionately affect SMEs, another possibility is that the EU market for services is not well suited to small firms.

	Level of UK trade	Direction of UK trade	% of SMEs that export	% of large firms that export
Legal, accounting etc	High	Exporting	9 – 37	54
Architecture and engineering	High	Exporting	7 – 49	60
Advertising, market research, management consultancy	High	Exporting	13 – 45	24
Miscellaneous business activities	High	Exporting	10 - 30	50

Note: Miscellaneous business services include photographic activities, packaging activities, secretarial and translation activities.

Source: ONS (2005) “ *A picture of UK trade and foreign direct investment in services*” Preliminary analysis carried out by ONS for DTI

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