



Open Up

How to fix the flaws in the EU's Digital Single Market

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Executive Summary

Europe is a laggard in both the development and the deployment of digital technologies. It urgently needs to do more to foster digital enterprise. Even more importantly, it needs to speed up and deepen the adoption of digital technologies across the economy, and thus reap their many benefits (section 1).

Yet policymakers in Brussels – pressured by those in Berlin and Paris who have been captured by corporate dinosaurs from the analogue age – wrongly tend to view digitalisation as an American threat, against which Europe cannot compete in the marketplace (section 2). So while EU policymakers claim to want to encourage digitalisation, in practice they are often seeking to limit digital competition.

The European Commission has produced a blizzard of digital initiatives in recent years, the latest of which is due on 11 January 2017. Many are part of the wide-ranging Digital Single Market (DSM) strategy. Others are closely associated, notably the General Data Protection Regulation (GDPR), the EU's new data-privacy rules. The Commission has also launched a bevy of antitrust cases against US technology firms.

This report's assessment of the DSM strategy and associated initiatives is that they are not fit for purpose. They amount to a jumble of outdated, corporatist, counterproductive industrial policies that favour producers over consumers, big companies over small, traditional incumbents over digital start-ups and EU firms over foreign ones.

Contrary to the Commission's sales pitch – and unlike the original drive to create a Single Market in goods – **the DSM strategy does not seek to tear down regulatory walls and mesh national markets**

into a single EU one. In fact, it contains hardly any liberalisation and seeks to impose new regulatory burdens on the digital economy – and thus on the economy as a whole. Worse, if intra-EU commerce continues to move online, ill-founded DSM rules will become the new Single Market rules, in effect supplanting the old liberal ones.

The Commission's claim that the DSM strategy could boost the EU economy by €415 billion a year does not stand up (section 3). Its only liberalising measures so far are minor. The Commission wants to ban companies from refusing online sales (except for copyright reasons) or setting different prices on the basis of a customer's home country. And it wants to enable Europeans to watch the TV shows available to them at home on streaming services such as Netflix when roaming in another EU country.

Fortunately, there already is a digital single market in many areas. With the exception of national copyright rules and media laws, there are few barriers to cross-border data flows within the EU (section 4). Online retailers are also able to export freely to other EU countries.

The real barriers to trade lie offline. The EU lacks a comprehensive single market in services and has yet to liberalise sectors that are crucial for digitalisation – such as retail, telecoms, payments and transport services – because of protectionist interests in some major EU countries. While the internet has fostered innovative new services that bypass national regulations – including online payments systems (such as PayPal and Stripe), e-books (such as Amazon's Kindle), car-sharing platforms (such as France's BlaBlaCar) and online call services (such as Skype, a European start-up now owned by Microsoft)

– this has prompted a corporate backlash against “unfair” online competition.

Regrettably, EU policymakers are mostly siding with the offline dinosaurs. Instead of viewing digitalisation as an opportunity to integrate EU services markets, **the DSM strategy does nothing to tackle offline barriers to competition while seeking to impose new ones online.**

In some cases, the Commission wants to impose new EU regulations in areas that were mostly unregulated at a national level, notably on online call and chat services such as WhatsApp (section 5). In others, it is introducing excessively bureaucratic harmonised EU rules, notably on data privacy. In effect, these inflict the red tape that prevails in France and Germany on more liberal EU economies too. The Commission has already inflicted more burdensome value-added tax (VAT) rules on online services. These measures will harm the digital economy and favour big established companies that can bear the compliance costs and legal liabilities over digital start-ups that can't.

The DSM strategy also explicitly targets (mostly American) online “platforms” – such as online retailers, operating systems, streaming services, search engines and social networks – in an unduly burdensome way (section 6). EU authorities are already able to intervene if digital firms breach data-protection, competition or consumer-protection laws. But they are now also seeking to regulate online platforms *ex ante* – in effect, presuming harm before it occurs (or doesn't). The Commission's antitrust cases against American tech giants also misunderstand the dynamic nature of competition on the internet.

The EU's digital initiatives aren't just corporatist; they are protectionist (section 7). The GDPR explicitly discriminates against foreign firms. The Commission is also embarking on a digital industrial policy that seeks to hamper big European companies' foreign competitors.

Yet far from nurturing European champions, regulatory hurdles and protectionist measures will stifle Europe's digital economy. In an era of global supply chains, where data is an increasingly important input for all firms, EU businesses – not least in manufacturing – need access to the best and latest digital services from around the world at the lowest cost.

To salvage the DSM strategy, it needs rethinking. **To unleash economic growth, stimulate digital enterprise and enhance consumer welfare, the EU needs to turn the DSM project into a true Single Market project – an Open DSM** (section 8). This would keep digital markets open to the rest of the world and reframe the “threat” of online competition as an opportunity to open up offline markets – and thus create a genuine single market in services. An Open DSM would be based on four key principles: non-discrimination, appropriate deregulation, data openness and dynamic competition.

At the very least, the EU should not impose discriminatory regulatory burdens on online businesses. Nor should the EU seek to “level the playing field” by trapping internet start-ups in the excessive regulation that bedevils offline sectors such as retail, taxis, hotels, telecoms and broadcasting in many EU countries. Unlike most

of the proposals in the DSM strategy, prospective digital regulations ought to be both necessary and proportionate.

Rather than trying to overregulate the internet as much as offline services markets often are, **the EU ought to subject all existing market rules, both EU and national, to a searching examination of whether they are fit for purpose in a globalised digital age** – in particular, whether they encourage innovation, enterprise and market integration. Such a colossal undertaking has been successfully achieved before: the 1986 Single European Act streamlined EU and national regulations on a wholesale basis.

On the basis of such a review, the EU and national governments should then deregulate markets to spur digitalisation and eliminate regulatory requirements that unduly hamper traditional industry. **The top priority should be addressing the lack of dynamism in services sectors key to the internet, such as retail, consumer financial services, telecoms, transport and distribution.**

Increased competition is particularly vital to ensure greater investment in Europe's antiquated telecoms infrastructure. Far from sheltering telecoms companies from competition, they should be encouraged to take the competition to online firms.

Ensuring that data flows freely within the EU is a pre-requisite for opening up EU services markets. **An EU-wide ban on local storage and processing requirements would improve efficiency, bolster integration and act as a ratchet against future protectionism as services move online.**

The EU ought to protect data privacy in a way that keeps markets open and Europe's services exporters competitive. GDPR determinations of whether third countries' privacy rules are “adequate” – and thus whether data is allowed to flow freely to them – ought to be expedited and based on objective criteria of the actual protection achieved, not on the legal approach that the country has chosen. The Privacy Shield that enables US-based companies to self-certify their compliance with EU rules also ought to be extended to other reliable jurisdictions.

EU competition policy also needs rethinking in the digital age. In the fluid and fast-changing digital world, its narrow, static analysis of competition issues based on rigid definitions of market structure is particularly inappropriate. It ought to embrace a broader, dynamic analysis of competition that gives more weight to the benefits of innovation.

As it stands, the DSM strategy is not fit for purpose. It is corporatist, protectionist and anti-innovation. What the EU needs instead is a seamless, non-discriminatory and dynamic digital single market that enables companies and consumers to operate smoothly across the EU and globally; does not discriminate against online suppliers, challenger companies and non-EU firms; and encourages innovation that boosts productivity and benefits consumers. **Europe needs to open up markets to digital technologies, not do digital down.**