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WORKING PAPER

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WORKING DOCUMENT

From:	Copenhagen Economics
To:	Working Party on Competitiveness and Growth (Better Regulation)
Subject:	Presentation by Copenhagen Economics: Subsidiarity and Proportionality in the Single Market

SUBSIDIARITY AND PROPORTIONALITY IN THE SINGLE MARKET

An EU fit for inclusive growth

Bertelsmann Stiftung



Agenda

1

Status on inclusive growth in EU: What are the problems to be addressed?

2

The economic rational for proportionality and subsidiarity

3

Examples of how proportionality and subsidiarity can be applied

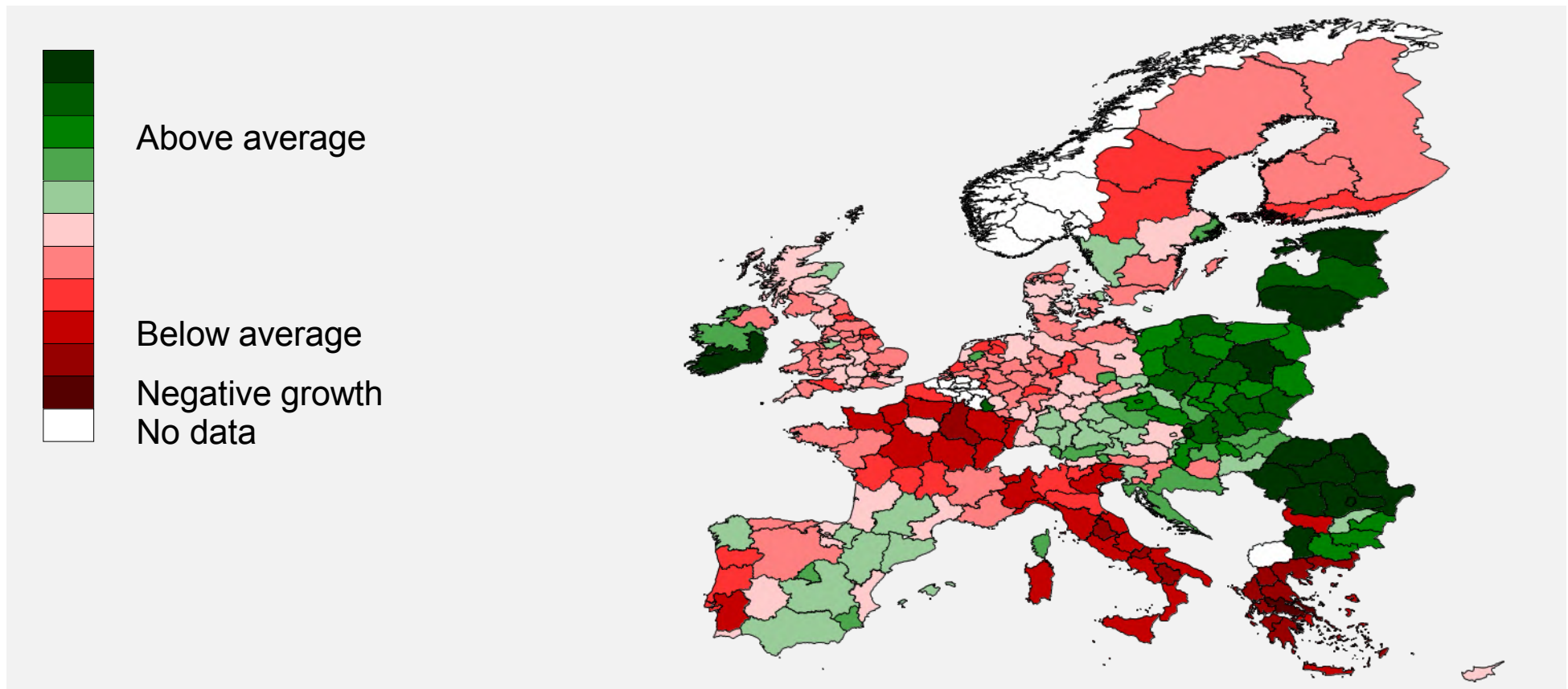
1

STATUS ON INCLUSIVE GROWTH IN EU: WHAT
ARE PROBLEMS TO BE ADDRESSED?

Large variations in GDP growth across EU since 2000

GDP growth in EU regions, 2000-2016

Percent growth compared to the EU average of 24 percent (net of inflation)

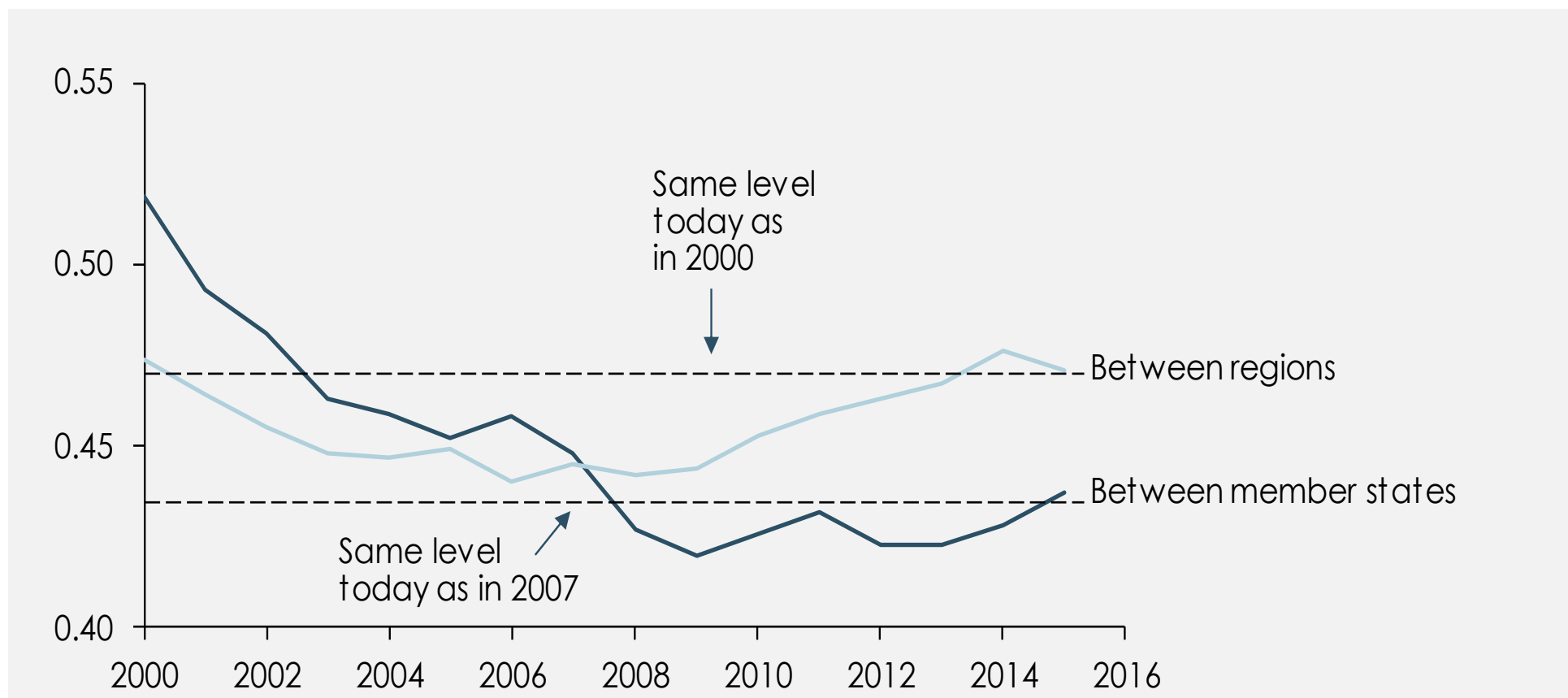


Bertelsmann Stiftung (2018): Subsidiarity and Proportionality in the EU Single Market – An EU fit for inclusive growth, figure 2

The economic disparity between EU regions is on the same level today as in 2000

Economic disparity between EU regions

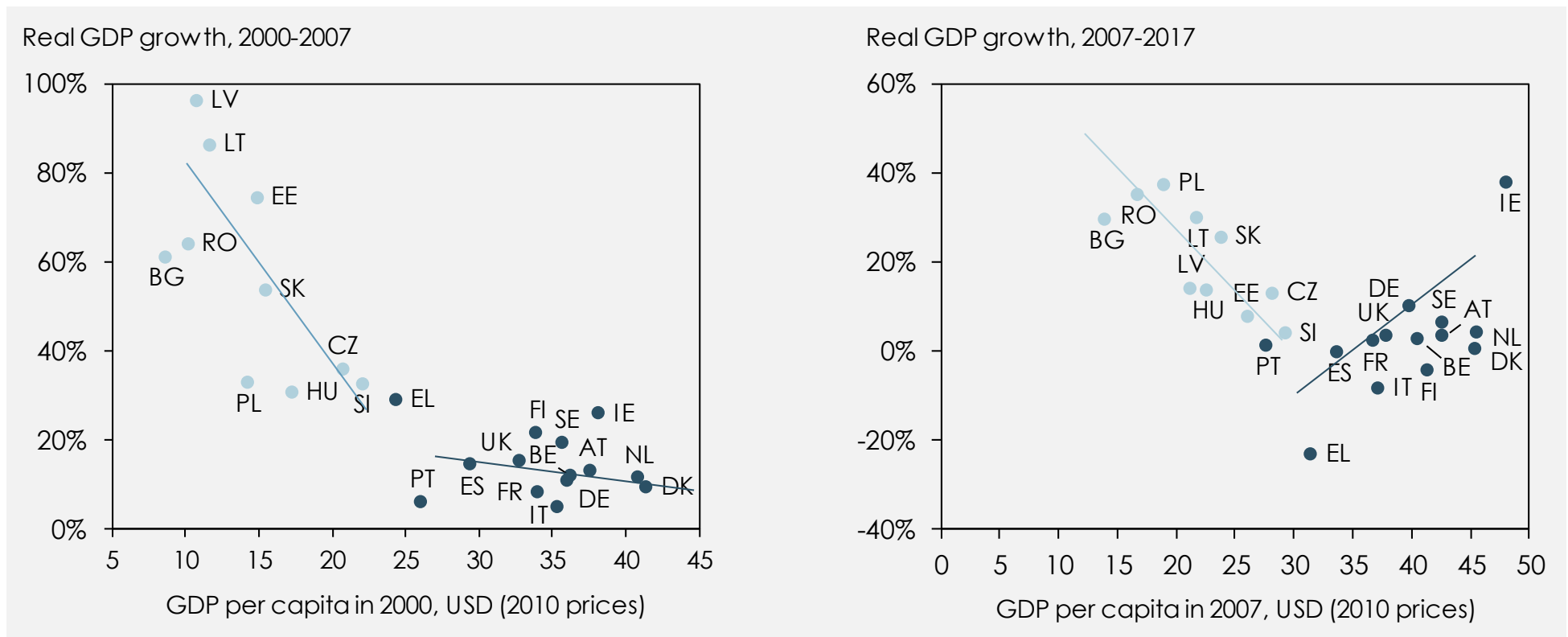
Variation in GDP per capita (measured by a variation coefficient) between regions/countries



Bertelsmann Stiftung (2018): Subsidiarity and Proportionality in the EU Single Market – An EU fit for inclusive growth, figure 3

Strong economic convergence for CEE countries – but not for EU15 countries

Correlation between level of real GDP per capita in 2000-2007 and subsequent growth, in percent

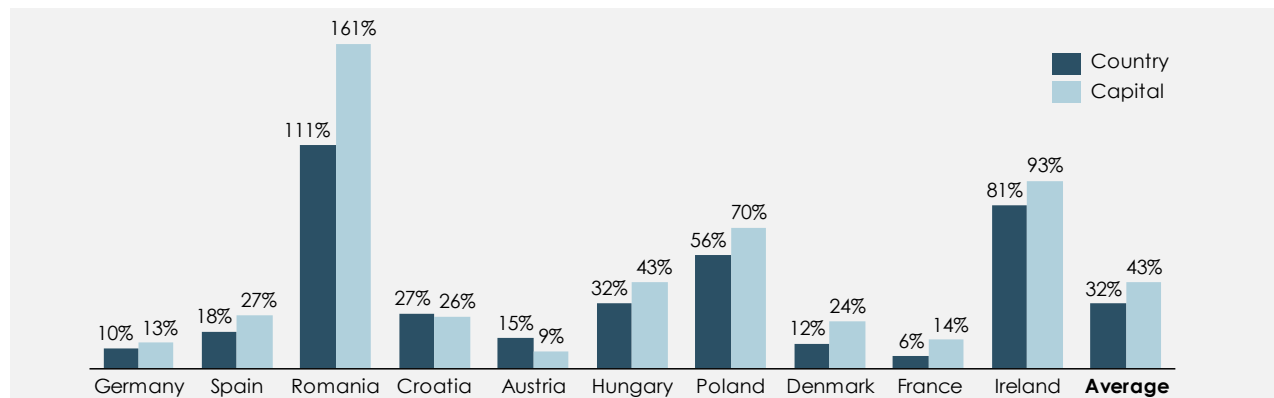


Bertelsmann Stiftung (2018) Subsidiarity and Proportionality in the EU Single Market – An EU fit for inclusive growth, figure 4

There is an income gap between urban and rural areas in the EU

Growth in EU countries and their Capitals

Panel A

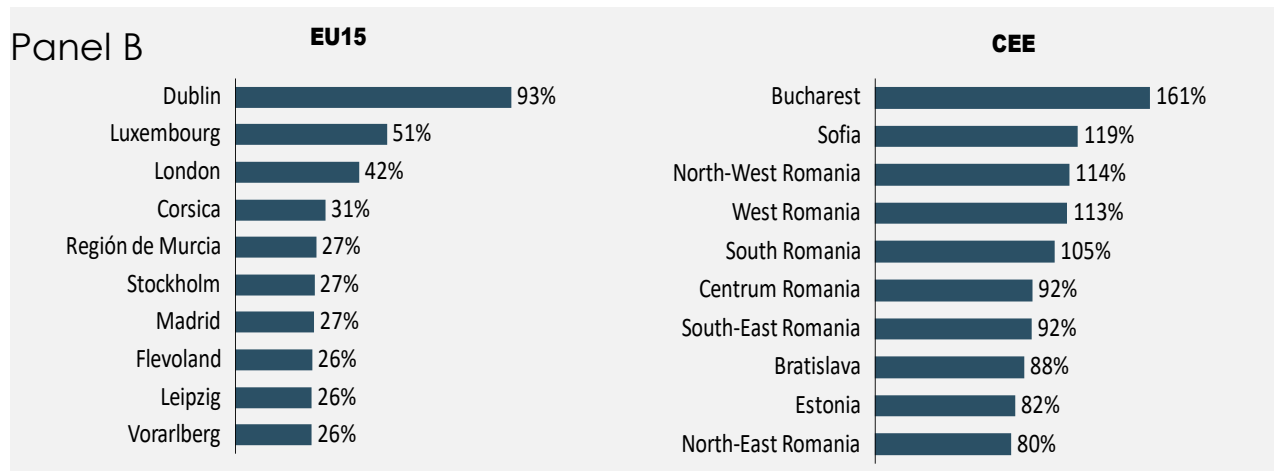


Populated areas have seen higher GDP growth rates

Non-urban regions, especially in South Europe have been underperforming

Job creation seems to be increasingly concentrated on urban regions

Panel B

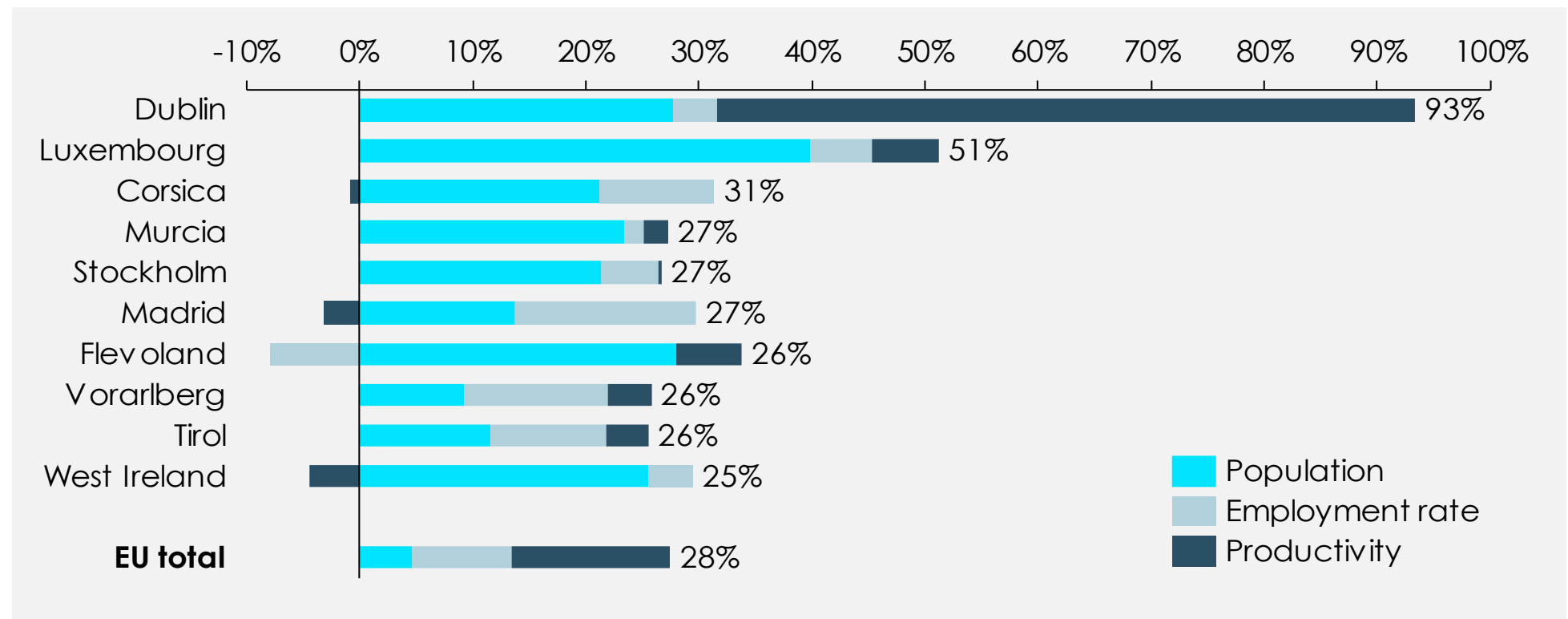


Bertelsmann Stiftung (2018) Subsidiarity and Proportionality in the EU Single Market – An EU fit for inclusive growth, figure 5 and 6

Labour is migrating to cities where jobs with high productivity and wages are found

Decomposition of growth in real GDP in selected EU regions, 2000-2016

Percentage points



Bertelsmann Stiftung (2018) Subsidiarity and Proportionality in the EU Single Market – An EU fit for inclusive growth, figure 7

2

THE ECONOMIC RATIONALE FOR PROPORTIONALITY AND SUBSIDIARITY

Application of subsidiarity: Centralised decision making vs. regional governance

Decisions on central level

vs

Decisions on regional level



- Existence of spatial externalities, e.g. research
- Ensure that companies can exploit economics of scale, e.g. EU inner market
- Prevalence of large economies of scale in public policies, e.g. infrastructure projects

- Regionally heterogeneous preferences are prevalent
- There is a scope for creating inter-jurisdictional competition



Application of proportionality

The EU principle of proportionality ensures that actions of EU is limited to what is necessary in order to achieve the policy objectives.

This means that the extent of **EU regulatory initiatives must measure up to the aims pursued**

3

EXAMPLES OF HOW PROPORTIONALITY AND
SUBSIDIARITY CAN BE APPLIED

Case 1: Building the future digital infrastructure highlights the dilemma in terms of **subsidiarity**

Situation	Dilemma	Recommendation
<ul style="list-style-type: none">• EU's digital infrastructure is currently <u>not sufficient</u> to ensure inclusive growth in the digital transformation.	<ul style="list-style-type: none">• Should broadband be included as a USO?• Risk of not taking local business structures into account.	<ul style="list-style-type: none">• Implemented through a flexible scheme• Minimum standards on national level• Target the cohesion fund on digital infrastructure• Example: Satellites providing internet in rural areas

Case 2: A call for a unified EU single digital market strategy

Situation	Problem	Recommendation
<ul style="list-style-type: none">• Borderless nature of digital companies• Physical proximity matters little.• EU have created a digital single market strategy but little concrete initiatives	<ul style="list-style-type: none">• 28 sets of national contract laws: Keeping digital business from getting sufficient scale in the early stages• Each MS: Little negotiation power in regulating tech giants	<ul style="list-style-type: none">• No virtual borders• A single EU point of contact for compliance and legal purposes.

Case 3: Financial regulation have lost track of proportionality

Situation	Problem	Recommendation
<ul style="list-style-type: none">• Current system designed to prevent large banks creating systemic risks• Not scaled down to suit smaller local banks, primarily servicing SMEs and households	<ul style="list-style-type: none">• Compliance costs soared in small banks since financial crisis, e.g. net stable funding ratio and reporting requirements• Give uneven playing field• Hurts economic growth in less populated areas.	<ul style="list-style-type: none">• Differentiated compliance requirement, e.g. small banking box?• More flexible capital requirements for smaller banks, e.g. "IRB-light"

Case 4: Regulatory sandboxes in finance as an example of more proportionality

Situation	Advantage	Recommendation
<ul style="list-style-type: none">• Some countries have established regulatory sandboxes• Give small fintech start-ups less restrictive and comprehensive regulation	<ul style="list-style-type: none">• Allows start-ups to gain sufficient scale, before full-scale regulation	<ul style="list-style-type: none">• Regulatory sandboxes in finance could be applied in all EU MS?• Regulatory sandboxes could be extended to other heavy regulated sectors?

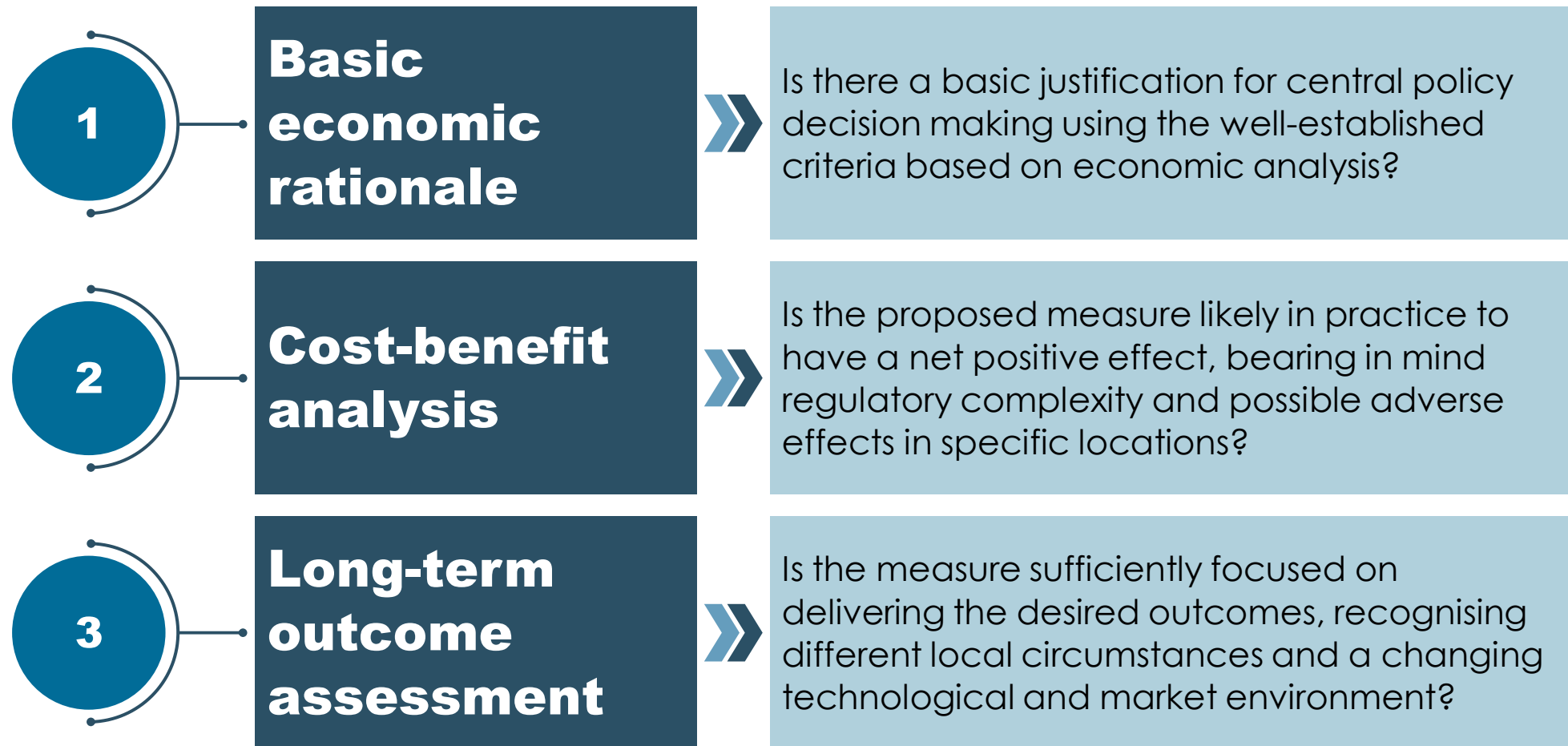
Case 5: Lack of **proportionality** in organic food regulation

Situation	Problem	Recommendation
<ul style="list-style-type: none">• EU has implemented stricter regulation on organic food production	<ul style="list-style-type: none">• Makes it more costly to shift from conventional to ecological farming• Especially in areas with small producers	<ul style="list-style-type: none">• An increased focus on proportionality and simplicity

Case 6: The Universal Service Obligation in line with the **subsidiarity** principle

Situation	Advantage	Recommendation
<ul style="list-style-type: none">• USO is securing minimum standards across EU• Opportunities for MS to define how to implement• Postal sector is rapidly changing, although with different speed in each country	<ul style="list-style-type: none">• Gives freedom to implement it, adapted to national general standards and structures on the market	<ul style="list-style-type: none">• Regulatory options evaluated on national level• Separate cost-benefit analysis in each MS• Lower min. requirements of Postal Service Directive?

Summing up: **Subsidiarity** and **proportionality** for a **common good** perspective



Bertelsmann Stiftung (2018) Subsidiarity and Proportionality in the EU Single Market – An EU fit for inclusive growth, page 27

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