Integration within the European Single Market: accounting, computer and construction services

Poland and other EU countries can benefit from a balanced package of further services reforms

With its economy growing more than three times faster than that of the EU28 over the last ten years, and with the services sector accounting for an increasing share of its economy, **Poland has become both an attractive destination for the export of services as well as their efficient supplier**. Polish wages and labour costs still remain below the EU average while both the education as well as productivity levels of the domestic labour force are growing. These factors contribute to Poland's competitiveness, not only in more labour-intensive services such as construction or transportation, but also increasingly in services requiring more advanced skills or technologies - such as accounting or computer and IT services.

Reforms undertaken to liberalise trade in services within the European Single Market have so far delivered tangible benefits to services suppliers and consumers. Nevertheless, the **internal market for services has remained more fragmented and less competitive than that for goods** due to restrictive and heterogeneous national regulations. Some of the remaining restrictions are deliberate and aim at limiting competition with suppliers from lower cost countries such as Poland. Other restrictions stem from differing legal traditions and preferences with respect to the quality or security of business conduct. Yet, restrictions which are unintended, arising from outdated legislative standards or unnecessarily bureaucratic administrative systems are also present.

Polish service suppliers face many such barriers in other EU markets, but some of Poland's own regulations and practices also impede the access of foreign suppliers to the Polish market. Other EU Member States are similarly challenged, however, the balance of defensive and offensive interests is usually country-specific as it depends on the level of development, regulatory practices, and the given country's competitive strengths. This suggests that **there is potential for significant gains for all the EU countries from the implementation of a balanced package of further reforms of services within the European Single Market**.

As exemplified by case studies of accounting, computer and construction services in this report

The study "Integration within the European Single Market: accounting, computer and construction services" was commissioned by the Ministry of Foreign Affairs (in consultation with the Ministry of Entrepreneurship and Technology) and prepared by CASE – Center for Social and Economic Research, an independent think tank. It is intended as a **Polish contribution to the ongoing discussion on the future of the Single Market at the highest political level** as well as in the context of the upcoming programming of the agenda of the next European Commission.

The report delivers a comparative analysis of trade integration, recent trade developments, and regulation within the three services sectors: (1) construction services, (2) IT/computer services, and (3) accounting and auditing services, focusing each time on Poland's stakes in the services trade liberalisation agenda. The choice of sectors was not random: the situation in the three market segments represents challenges and opportunities faced by the EU services sector as a whole and provides a sound basis for more general conclusions. It includes services in which Polish suppliers compete on the basis of labour costs (construction), knowledge (audit and accounting) as well as the use of advanced technologies (computer services). Moreover, these **sectors present a typical array of regulatory issues appearing in services markets**, ranging from measures restricting competition from low cost countries (construction), through differences in regulatory traditions (accounting) or preferences regarding security, or, indeed, aiming to regulate so far largely unregulated activities (computer services).

The research provides a **detailed analysis of the remaining barriers within the Single Market in the three sectors** and discusses them in the context of potential benefits from further liberalisation of services trade , one which would ideally encompass a wider range of sectors. The investigation is set in a broader context of offensive and defensive interests of Poland and its three selected trading partners with a diverse set of comparative strengths - Germany, Hungary and Sweden.

Poland is a competitive services provider and stands to gain from advancing the services liberalisation agenda

The Polish services sectors are in a relatively advantageous position as compared with the EU28. Indeed, the country supplies highly competitive services to the EU markets. Since Poland's accession to the EU, it has strengthened its net position and it currently ranks as the 12th largest services exporter within the Single Market. Poland **possesses a significant revealed comparative advantage in accounting and auditing** as well as in **construction**; moreover, the country also **shows strong signs of developing it in computer services**. Quantitative trade data also indicate that there may be a considerable potential for further gains from trade for Polish services providers operating in these sectors.

Thanks to considerable liberalisation efforts so far, **barriers faced by the European service providers across EU markets remain lower than those which exist outside the area**. The Services Directive and the integration of the Single Market have alleviated several barriers to the free flow of services throughout the EU, **adding an estimated 0.9% to the EU's GDP over the last decade alone.** As a result of the implementation of the Services Directive, Germany, Hungary, and Poland were estimated to have achieved GDP gains in the range of 0.5-0.7% each, and, in the case of Sweden, of 1.1%.

Notwithstanding the Services Directive (which remains not fully implemented) and other initiatives (e.g. Professional Qualifications Directive), the level of integration within the Single Market for services has lagged behind that for goods and it currently remains lower than in federal economies such as the US. Furthermore, the degree of **integration with the Single Market differs among EU Member States,** especially when it comes to both progress made since they joined the EU and the current level of integration. Poland's integration within the Single Market for services appears to be just below the EU-wide average whereas the country's increase in services trade flows was the third highest in the EU.

Extant studies estimated that further integration with the Single Market and the **elimination of the remaining barriers to services trade may lead to a subsequent increase of between 2.2% and 14% in the EU's GDP**. One specific study indicated that a mere full implementation of the Services Directive could add an extra of 1.7% to the EU's GDP, with Germany and Sweden benefitting the most: between 1.6 and 1.7% of their respective GDPs; for Poland and Hungary gains would be in the range of 1%.[1] On a more

1 American Chamber of Commerce (2017).

disaggregated level (assuming that all EU Member States would achieve the highest possible level of integration with the Single Market and that the intra-EU trade in services would grow by 50%), the investigation delivered modelling results indicating that the per capita GDP gains could amount to an average of 0.59% in the EU28 (country-specific results varied, with +0.42% in Hungary, +0.61% in Sweden, +0.51% in Poland and +0.59% in Germany). Moreover, the study also suggested that the further elimination of barriers would have job-creating properties, especially in Germany (+231.4 thousand jobs) and Poland (+80.7 thousand jobs).

The remaining barriers to services trade across the three sectors are heterogeneous

The **remaining barriers to services trade within the Single Market are diverse in terms of the type and magnitude of the restrictions**. Some of them are overtly protectionist (e.g. discriminatory regulations) while others appear unintentional and stem from cultural, legal and economic heterogeneity among the Member States. Indeed, distinguishing between the two cases is often difficult. Yet, some of these regulations serve important societal standards and goals, both of which vary between the Member States and cannot be viably reduced.

The restrictiveness of EU trade barriers manifests a strong variation across sectors. For example, **computer services are among the least regulated** within the Single Market, **construction services are more constrained**, yet still below the Single Market average, while **accounting and auditing services are among the most restricted** services when it comes to trade.

Accounting and auditing

The barriers to trade of **accounting and auditing services** within the Single Market are estimated to be the highest among the three analysed sectors. They reflect strict **regulatory requirements faced by auditors** in the Member States rather than refer to significant barriers to cross-border trade. Additionally, **the heterogeneity of country-specific regulations is the highest in this sector**. Overall, accounting and auditing services remain the most 'protected' in some of the old Member States. For example, Hungary and the Czech Republic are also slightly above the EU average.

Construction

Regulations in the **construction services sector** have been moderately restrictive, still they take the form of **restrictions to the cross-border provision of services** more often than in other sectors. Restrictions to the establishment of a (permanent) foreign presence or to (temporary) cross-border provision of services as well as barriers to the movement of professionals pose significant difficulties for businesses aiming to operate internationally. The existing barriers relate to the following areas:

- recognition of qualifications in regulated professions;
- diverging administrative and regulatory barriers for companies aiming to export services;
- proliferation of administrative requirements and authorities;
- fragmentation of information and the fact that it is available often only in the local language.

Construction services providers are also relatively more exposed to costly administrative procedures related to accessing another Member State's market, including the **amount of data and information required and processed** by the relevant host Member State's authorities. This administrative burden may turn out to be a natural deterrent more effective than any financial barrier.

On top of the administrative procedures, entrepreneurs wishing to establish a permanent market presence or aiming at a temporary cross-border provision of services face **significant and largely disproportionate financial costs** which need to be incurred in several host countries (therefore creating a financial burden, if not an outright barrier to market entry).

Overall, currently construction services are still the most 'protected' in some old Member States. In the near future the **costs of posting Polish construction (and other) workers** to higher-income countries may increase as a result of the adopted revision of the relevant rules. It remains unclear how the sector will tackle this change, as these developments are likely to undermine the sector's competitive edge. As the revision of the Posting of Workers Directive adopted in June last year raises serious questions about its negative impact on the freedom to provide services and the competitive position of services providers, Poland and Hungary decided to contest the revised Directive before the Court of Justice of the European Union.

Computer services

The **computer (ICT) services sector has been a benchmark barrierfree sector**. This reflects the fact that the development of this sector over the last three decades preceded its regulation. Still, there are two kinds of restrictions in this sector (as opposed to up to five different kinds of barriers identified in other sectors), specifically: **barriers to competition and regulatory transparency**. The barriers that are in place relate, above all else, two horizontal market entry obstacles – the most prominent being capital requirements for starting a business (which vary across countries) and legal forms of economic entity.

With e-Privacy, cybersecurity, AI, cloud computing, data flows and intermediary liability gaining more importance (mainly from the national security perspective), **there is an increasing threat of overregulation of the Digital Single Market** driven by ethical, technological, fiscal and legal concerns.

The balance of Poland's defensive and offensive interests in the three sectors

Poland is moderately restrictive as regards protecting services sectors (either at, or slightly above, the EU-average). Thus, European services providers already enjoy relatively uncompromised access to the Polish market. On the other hand, there is still potential for Poland to liberalise domestic policies, with benefits for its own economy and its EU trading partners.

Taking estimated *ad valorem* equivalents of barriers to intra-EU trade by sector and country into account:

1. In the accounting and auditing sector, Polish exporters on average face barriers which are 25% lower than those faced by companies from Germany, Sweden and Hungary. At the same time, the Polish market appears relatively protected, with barriers more than twice as high as in the three other countries. Still, Polish and Hungarian companies from the accounting and auditing sector have manifested higher comparative advantages than the Swedish or German ones. Thus, as the sector benefits from a strong competitive position, its protection by non-tariff barriers seems futile (this is not to say that the protectionist approach prevails in this sector over other regulatory aims). Significant benefits are to be gained from

liberalisation in the domestic market (most likely the liberalisation of the tax advisor profession), while the risk of foreign competition remains limited.

2. Polish construction companies face the same level of barriers as companies from Hungary and Sweden. German construction companies deal with slightly higher barriers. As regards the protection of the Polish construction market, only the Swedish market emerges as more protected. Hungary and Germany do not seem to strongly protect their construction markets. Again, the Polish construction sector possesses a higher comparative advantage than its counterparts in Sweden, Germany, and Hungary. Thus, as the sector benefits from a strong competitive position, its protection by non-tariff barriers seems unnecessary. In fact, Polish companies could benefit from an EU-wide lifting of the non-tariff barriers as in some countries (e.g. Sweden) they are more restrictive than in Poland.
3. Trade in computer services meets negligible barriers within the Single Market across the analysed countries. Nevertheless, the Polish computer services market is estimated to have moderate protection[2][1], which reflects the insufficient market contestability, competitive pressures, and lower levels of development of the Polish digital market as compared to other EU countries.

Sector	Tariff equivalents faced in the Single Market by exporters from:			
	Poland	Germany	Hungary	Sweden
Accounting and auditing	3%	4%	4%	4%
Construction	3%	4%	3%	3%
Computer services	1%	2%	1%	1%
	Tariff equivalents faced by EEA service providers in:			
	Poland	**Germany**	**Hungary**	**Sweden**
Accounting and auditing	7%	2%	3%	4%
Construction	5%	1%	2%	7%
Computer services	3%	1%	2%	1%

Note: Sectoral estimates of the ad valorem equivalents for each analysed country from Rouzet, D. and F. Spinelli's (2016: 21-23) were proportionately scaled down taking the respective ratios of MFN to intra-EEA trade restrictions into account. In order to obtain ad valorem equivalents as perceived by the companies from a given country, ad valorem tariff equivalents for other Single Market players were averaged using export weights related to specific destinations.

Source: own calculations based on estimates from Rouzet, D. and F. Spinelli's (2016) and the OECD Services Trade Restrictiveness database.

Smaller businesses are the most vulnerable to regulatory burdens

The remaining barriers, which often take the form of fixed costs, **in particular hamper the chances of profitable businesses participation in services trade for small and medium enterprises (SMEs)**, among others, in the construction and business services. For these two sectors, the European Commission reported that the major barriers boiled down to:

- cumbersome authorisation systems;
- registrations and notifications requirements / obligations;
- requirements regarding the legal form of services suppliers, ownership structure, allocation of voting rights, and management positions;
- multi-disciplinary restrictions;

2 [1] This stems not from formal barriers to trade but rather from the market structure.

- organisational requirements of health and safety standards;
- obligatory certification schemes;
- needs to uphold certain financial capacities (or, for example, to purchase professional indemnity insurance);
- inadequate regulations enforcement;
- low levels of cross-border public procurement accompanied by insufficient political support for structural reforms.

SMEs are particularly affected by the costs of dealing with regulatory hurdles and complying with diverging regulations in every new market. For micro companies which engage in cross-border exports, an average level of services trade restrictiveness represents **an additional 7% in trade costs relative to large companies.** Establishing an affiliate abroad is costlier: for a small company an average level of services trade restrictiveness is estimated to be equivalent to an additional 12% tariff compared to large companies.

The role of digital services is growing significantly

Digitisation has a significant impact on all sectors of the EU economy, including the services market and its future performance. The Digital Single Market (DSM) has been an important factor shaping the EU-wide business environment - with regard to trade both in goods and services. While it is conceivable that the digital progress and the "traditional" single market will work to reinforce each other, **the fact that the Single Market could have trouble keeping up with the digital economy cannot be ignored**.

Poland should pay particular attention to the computer services sector alongside other digital sectors and **advocate a coordinated policy action for boosting security of digital services trade where appropriate**. However, attention needs to be paid **not to damage the relatively barrierfree environment found there**. There are several reasons underpinning this insight: firstly, the sector's potential in terms of added value and innovation generation is higher than that of most other segments, including accounting and auditing and construction services. The further development of digitalisation, particularly as regards the DSM, may help unlock this potential and diversify the economy towards more knowledge and technology-intensive services. Secondly, exports are essential to Polish IT services, acting as a stimulus for the development of the segment. Thirdly, if a widescale liberalisation across sectors proves difficult or impossible, it may be more effective to defend the relatively barrierfree status rather than to bring down the existing barriers elsewhere.

Key messages and recommendations:

- **Economic simulations show considerable gains from liberalisation for all countries**.
- Poland – being a moderately restrictive market and competitive services provider – **has mainly offensive interests as regards the liberalisation of trade in services within the Single Market.** It also has the potential to liberalise its own policies which would bring additional benefits for the domestic economy and its EU trading partners. The further liberalisation of services within the Single Market is unlikely to undermine the strong competitive position of the Polish companies. It would rather open new opportunities for them.
- To maximise the chances of moving the services negotiations forward, joint policy efforts should focus on developing proposals aiming to ensure **an even distribution of benefits from further services trade liberalisation among the EU**

economies via coordinated EU-level actions. These efforts should also take **the importance of regulatory convergence** into account, especially removing unnecessary heterogeneity in regulations. A special focus is required in the areas with the highest potential for growth, such as business services, where providers could benefit from better access to digital technologies and a smoother exchange of data.

- **The challenge is to identify the most discriminatory or restrictive barriers** for both foreign and domestic companies and, particularly, to **differentiate between the measures stripped of any domestic regulatory value** and the regulations which, **while discriminatory, may have legitimate domestic regulatory objectives**.
- Another issue is **the strong variation in barriers restrictiveness across sectors at the EU level**: for example, construction and accounting services remain the most 'protected' ones, mainly in the old Member States.
- Further **liberalisation is threatened by some unfavourable policy scenarios such as regulatory tightening at the EU and Member State levels** in certain areas, e.g. as regards posted workers in the construction sector or in the digital economy. **Preventing new restrictions is thus one of the main priorities**.
- **An ambitious agenda for further integration of the services sector** in the coming years is required. To ensure that the joint policy efforts are not wasted and individual EU Member States' voices are heard in the discussion, it is important to launch a comprehensive debate based on **relevant empirical evidence** provided by the European Commission and Member States. It should identify solutions to specific problems and barriers.
- Given the sensitivity of the dossier, a **sectoral approach would be the most desirable**. Consideration, however, may also be given to **horizontal initiatives in some cases**. Lessons learned (in particular works on proposal for the European Services e-card initiative) combined with qualitative and quantitative cross-country research could provide the much-needed starting point for engaging in public consultations with business and political stakeholders.
- **Policy efforts should focus on digital development and the IT sector,** including a coordinated policy action for boosting the security of the digital trade of services, yet with an aim of not damaging the relatively barrierfree environment. In this area, **well-calibrated horizontal approaches may manifest high potential.** In the digital sphere, following the implementation of the 2016 NIS Directive and the 2018 EU General Data Protection Regulation, proposals for the amendment of the existing regulatory frameworks pertaining to e-privacy are already under development. These drafts, despite strengthening law enforcement and shielding users from aggressive content, also provide new business opportunities, both for traditional companies as well as digital ones. While the overriding aim has been to streamline the digital market as a whole, the EU-wide regulatory efforts carry considerable policy uncertainty and the risk of overregulation, not only in the context of particular national interests but also as regards potential misalignment with the extant DSM goals. These factors may deter the development of start-ups and capital inflows before the envisaged reform has been agreed upon and transposed into national law. **If successful**, the regulatory change will likely result in **levelling out the EU market, providing unified, and clear-cut requirements and the relaxation of barriers to trade in all services subject to analysis via a boost to the digital economy and regional competitiveness.**

Specific proposals regarding the further liberalisation of trade in services:

- There is a need to **reduce restrictions** regarding the provision of services by foreign-registered companies as well as the removal of unjustified restrictions to posting of workers in the framework of provision of services.
- **The 'overregulation'** of auditing sector should be reduced. In this aspect, the efforts should centre on licencing requirements on different tiers of management in some EU countries[3].
- There is room for improvement of both the **mutual recognition of qualifications** (transposition of the EU-wide legal framework and enforcement of the regulations) and **public procurement** (the proper transposition and application in some Member States of Directives on public procurement and concessions).
- As for **regulatory and administrative frameworks** pertaining to horizontal authorisation and building permits, construction services providers may reap significant gains from the **simplification of the relevant procedures** and **handling them online**.
- Any measures ensuring an equilibrium between social aspects and the four freedoms are worth considering.
- It is also worth considering a new horizontal **proposal of a tool which would build on the idea of the services e-card** (taking lessons learned into account and addressing the main obstacles to its adoption) or efforts aimed at the **extension of the European Professional Card**.
- **Digitalisation efforts are desirable, in particular those which improve access to high-speed internet, cloud storage and e-government.** Policy efforts should also focus on further development of digital markets in the Member States and their alignment (both regulatory and technology-wise) with the EU economy.

3 Given the sensitivity of the auditor and tax advisor professions all such initiatives need to be considered with much care.