Internal Market Scoreboard

No 12
The Commission is keen to receive feedback on this Scoreboard, and to have suggestions for future editions. Please send reactions to Mr. Alexander Schaub, Director General, Internal Market DG, The European Commission, B-1049 Brussels, or to the following e-mail address: Markt-B1@cec.eu.int

Please also use this address if you would like to receive a copy of this or future Scoreboards.
MAIN FINDINGS

Transposition of Legislation
- The transposition deficit for Internal Market directives is rising again. It is now 2.4 % – up from 1.8 % only one year ago.
- Only 5 Member States (Denmark, Finland, Sweden, Spain, UK) meet the European Council’s target of a 1.5 % deficit or less. Italy ranks last, closely followed by Portugal and Ireland.
- Only Denmark, Finland, Portugal and the UK achieved the zero tolerance target for directives overdue more than 2 years.

Infringement Proceedings and Alternative Problem Solving
- The number of open infringement cases has gone up by 6 % compared to last year.
- The Commission has developed alternative mechanisms to tackle some problems and avoid infringement proceedings where possible.
- ‘Package meetings’ involve experts from Member States and the Commission coming together in order to discuss a ‘package’ of cases being examined by the Commission for violation of Community law. About 50 % of the cases are solved and even when there is no agreement positions are clarified so that infringement proceedings can be pursued more swiftly.
- The SOLVIT network is designed to deal with cases of misapplication of Internal Market rules by national and local administrations. Initial results show that SOLVIT solves more than 70 % of cases, mostly within the 10 week target deadline.

Tax Obstacles in the Internal Market
- 15 different systems of corporate taxation across Member States lead to important costs for companies and ultimately for consumers. A common consolidated corporate tax base would reduce these costs considerably without depriving Member States of the possibility to set taxation rates according to their national objectives.
- The complexity of VAT requirements represents a real barrier to cross border activities.
- Prices of new cars vary substantially across Member States. This is partly due to large differences in registration and value-added tax.
- Discriminatory tax treatment of foreign pension funds restricts the cross-border movement of workers and prevents companies from setting up a single cost-effective pension scheme for all their EU establishments.

Substantially Lower Prices in the Accession Countries
- Prices in the Accession Countries are on average almost 50 % below the EU15 average. Lower income levels explain only part of the difference.
- Services are on average much less expensive in Accession Countries while consumer electronics prices for example are closer to the EU15 average.
- Previous enlargements have sparked off price convergence. There is reason to believe that this enlargement will do the same.
**INTRODUCTION**

One year from now the European Union will have completed an enlargement unprecedented in size and significance that will truly change the face of Europe. This year’s Spring European Council emphasised the importance of a dynamic and efficient Internal Market in boosting productivity and growth and in making a success of enlargement. The Commission is responding to this challenge by proposing a new 3-year strategy for the Internal Market which focuses very firmly on strengthening the 'basics' or 'fundamentals'. The assessment of performance published in this Scoreboard therefore comes at a key moment for the Internal Market.

After many years of uninterrupted progress the trend in the transposition deficit has taken a significant turn for the worse. 12 months ago it stood at 1.8 % – it is now at 2.4 %. The 8 Member States who last year failed to meet the 1.5 % target set by the European Council but in some cases came close, all now have deficits of 3 % or more.

It is a measure of their poor overall performance that France who was bottom of the league a year ago has managed to jump 5 places although its deficit has worsened slightly over the period from 3.1 % to 3.3 %. Only 5 Member States meet the 1.5 % target and only 4 the zero tolerance target for directives overdue by more than 2 years.

The situation on infringements is not significantly better. The total number of infringements has increased by 6 % compared to last year and the speed at which they are solved remains roughly unchanged. The message is clear – with few exceptions Member States need to work harder and be more committed not only in order to meet the targets that they have set themselves but also to set an example to future Member States.

Every infringement is a problem for someone in the real world. The Commission has started to pioneer the use of new tools to try to solve some of these problems without the need for legal action unless it is in the Community interest. This Scoreboard features a preliminary analysis of the performance of these tools, which shows promising results thanks to the good co-operation between Member States and the Commission.

A section on tax obstacles uses 4 thumbnail sketches in the area of corporate taxation, VAT, motor vehicles, and occupational pensions to show how differing rates, bases, and systems of taxation prevent the Internal Market from delivering its full potential.

Finally, a short analysis of prices in the Accession Countries shows that as in previous enlargements, a fully functioning Internal Market can contribute to ensuring that price convergence goes hand in hand with an improvement in living standards in the new Member States.

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2 The Spring European Council decided to set July 2003 as the next target date.

1. Implementing the Internal Market’s Legal Framework

A. Transposition of Legislation

Agreed Community directives have to be turned into laws in every Member State for them to produce their desired legal and economic effects. It is, therefore, particularly worrying that the transposition deficit for Internal Market directives has worsened considerably since last year; the average rate now stands at 2.4% compared to 1.8% a year ago. This means that the Commission is still waiting for 558 notifications of national implementing measures to arrive on its desk and almost 9% of directives have not been transposed in all Member States.4

Figure 1: The transposition deficit is rising again

![Graph showing percentage of directives transposed over time](image)

Note: The transposition deficit shows the percentage of Internal Market directives not yet communicated as having been transposed, in relation to the total number of Internal Market directives which should have been transposed by the deadline.

When there are delays in transposing measures, this is not just a legal problem. It leaves a void in the regulatory framework, which disrupts business, deprives citizens of their rights and undermines confidence in the European Union. The Commission’s Report on the functioning of product and capital markets ('Cardiff Report')5 identified slow implementation as one of the Union’s main handicaps in achieving its objective of becoming the most competitive knowledge-based economy by 2010.

4 This figure is also known as the fragmentation factor. It is currently 8.8%.

The European Parliament in its recent report on the Internal Market Strategy asked the Commission to try to quantify the costs of late transposition. The Commission will undertake a feasibility study to examine whether it is methodologically and practically possible to put a figure on the cost of the transposition deficit. There are serious challenges in coming up with reliable estimates. For example, the deficit applies to a constantly changing body of directives as outstanding directives are finally transposed and new directives pass their implementation deadline. It is also not obvious how the behaviour of business and citizens is affected by legal insecurity across a wide variety of situations.

Only Denmark, Sweden, Finland, Spain and the UK currently meet the European Council’s target for Member States to keep their deficits to 1.5% or below. The EFTA states Norway and Liechtenstein are also within the target. It is noteworthy that both Spain and Denmark who already had low deficits were able to improve their scores even further. However, 2 Member States who achieved the target last spring (the Netherlands and Belgium) have fallen back since, but with some extra effort should be able to catch up soon.

Figure 2: Currently only 5 Member States meet the 1.5% target

Note: The situation as at 15 April 2003. 1530 directives and 377 regulations currently relate to the Internal Market as defined in the Treaty.


7 The Internal Market also covers 3 EFTA States, Iceland, Liechtenstein and Norway, as a result of their membership of the EEA Agreement.
There is little or no good news to report on the performance of the 8 other Member States since the last Scoreboard in November 2002. Their transposition deficits are at least twice that of the European Council’s target. Only France has managed to reduce its percentage in the last 6 months, although its deficit is still worse than a year ago. This could be an indication that the political initiative announced by the French government in November 2002 is beginning to produce results, although more is clearly needed. Only 4 Member States, France, Spain, Belgium and Denmark have fewer directives outstanding compared to 6 months ago (see figure 3).

Figure 3: All Member States except France, Spain, Belgium and Denmark have seen their backlogs increase since the last Scoreboard

The situation of Portugal is disappointing given that until recently it had been one of the better performing Member States. In 2000, Portugal was in a similar situation to now and thanks to determined political efforts improved its score rather quickly. There is no reason why it could not do so again. Italy, future Presidency of the European Union, now finds itself in last position. This is the consequence of a slow but steady fall in the ranking since 2001. It is time for Italy to look into the reasons for this worrying development and find ways to speed up the process.

The Barcelona European Council of March 2002 added a 'zero tolerance' target for directives whose transposition is 2 years or more overdue. As figure 4 shows, Denmark, Finland, Portugal and the UK are the only Member States that have achieved the target – with Spain, the Netherlands and Sweden coming close. All Member States, however, succeeded in reducing the number of directives overdue by more than 2 years. Only Denmark, Finland and the UK have met both the 1.5% and the 0% target. It is disappointing – at the least – that targets set by our Heads of State and Government are missed by so many Member States.
10 key overdue directives were already highlighted in Scoreboard 10 a year ago and again in Scoreboard 11. Only one of these directives is now fully transposed (96/48: Interoperability of high-speed trains). For these key directives which are more than 2 years beyond their transposition deadline, 22 notifications of national implementing measures have arrived over the last year, but the Commission is still waiting for a further 20 notifications. Almost no measurable progress has been made on the transposition of directive 98/44 on the legal protection of biotechnical inventions, where 8 Member States are still in breach of their legal obligations.\footnote{The Commission sent these Member States a Reasoned Opinion in December 2002.}
Figure 5: Key directives still overdue by more than 2 years and the Member States responsible for missing the target

<table>
<thead>
<tr>
<th>Directive</th>
<th>Not yet transposed by</th>
<th>Impact</th>
</tr>
</thead>
<tbody>
<tr>
<td>95/46: Protection of personal data</td>
<td>IRL*</td>
<td>No level playing field, potential abuse of data, hampers the free flow of information</td>
</tr>
<tr>
<td>96/48: Interoperability of the trans-European high-speed rail system</td>
<td>NOW ADOPTED BY ALL MEMBER STATES</td>
<td>Allows the development of an integrated European high-speed rail system</td>
</tr>
<tr>
<td>96/61: Integrated pollution prevention and control</td>
<td>EL, L</td>
<td>No level playing field, potential health and environmental risks</td>
</tr>
<tr>
<td>97/7: Protection of consumers in respect of distance selling contracts</td>
<td>L</td>
<td>Delays development of e-commerce</td>
</tr>
<tr>
<td>98/5: Practice of the profession of lawyer on a permanent basis</td>
<td>F, IRL</td>
<td>Hampers the free movement of lawyers</td>
</tr>
<tr>
<td>98/8: Placing of biocidal products on the market</td>
<td>F</td>
<td>No level playing field, potential health risks, frustrates trade in these products</td>
</tr>
<tr>
<td>98/27: Injunctions for the protection of consumers’ interests</td>
<td>L</td>
<td>No level playing field, lower level of consumer protection</td>
</tr>
<tr>
<td>98/44: Legal protection of biotechnological inventions</td>
<td>B, D, F, I, L, NL, A, S</td>
<td>Hampers innovation and research in biotechnological products, continuing fragmentation and uncertainty about the legal framework</td>
</tr>
<tr>
<td>99/36: Transportable pressure equipment</td>
<td>IRL</td>
<td>Frustrates trade in these products, potential safety risks</td>
</tr>
<tr>
<td>99/94: Availability of consumer information on fuel economy and CO₂ emissions</td>
<td>D, F, I</td>
<td>Diminishes transparency and integration of markets, continuing price differences</td>
</tr>
</tbody>
</table>

* Ireland is about to implement this directive, but the Commission has not yet received a notification.

It is difficult to assess the precise reasons why Member States fail to transpose into their own legislation texts that they have agreed in Council. But as some Member States consistently outperform others, it cannot simply be coincidence. The involvement of regional governments in the implementation process cannot explain why some do better than others. The deficits of the UK and Belgium, for example, are considerably lower than those of Greece and Portugal whose national parliaments have sole competence to implement Community law. From what Member States have told the Commission, success often seems to be linked to 3 factors: careful planning, starting while negotiations are still ongoing, and close co-operation with parliaments.
Figure 6 shows that the Member States with the best overall ranking also have the shortest delays even when they miss the transposition deadline. Finland and Sweden, for example, usually rectify any breaches within 3 months, while France tends to take well over a year before coming into compliance with Community law.

**Figure 6: The length of delays varies considerably: the Member States with the lowest transposition deficits are quicker**

![Graph showing delays in months for different Member States.](image)

Note: Average delay in months of directives which have passed the transposition deadline.

Transposition delays add wholly unnecessarily to the total duration of the legislative process, which is already very long in most policy areas. It is telling that in today’s fast-moving world, it has taken the Union on average 7 years to adopt and implement legislation in the area of financial services and more than 4 years in general.\(^9\)

Slow transposition remains a serious concern for the European Union. The active prodding of the European Council has not yet resulted in decisive action across-the-board. This may change if Heads of State and Government would personally commit their governments to meeting these targets. The Commission also believes that Member States should be more critical of each other’s transposition performance. Those Member States which are consistently late in transposing Internal Market measures undercut the Union’s competitiveness and may even tilt what should be a level playing field to their advantage. It also conveys a negative message to the Accession Countries who are required to implement the full Internal Market acquis by the time of accession – just 12 months away now. It should not just be for the Commission and the Parliament to call on the laggard Member States to step up their efforts.

Effective implementation will be one of the priority areas for action in the new Internal Market Strategy (Priorities 2003-2006), which the Commission will present around the same time as this Scoreboard.\(^10\) It will include a number of actions aimed at reversing the

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negative trend of growing deficits and creating a situation whereby all Member States will be better placed to achieve the European Council’s targets.

In anticipation of the strategy, the Internal Market Directorate General has already started a ‘preventive dialogue’ with Member States. It has begun to hold meetings with Member States to help with the implementation of Internal Market directives.\footnote{These meetings are a development of the 'package meetings' that are described in the following section.} The objective is to improve both the speed (by starting shortly after the adoption of a measure) and the quality (through early identification of potential difficulties) of transposition. It is hoped that this kind of preventive action will reduce the number of infringement proceedings arising from late or incorrect transposition of directives. Over the last year such meetings have been held with France, Italy, Belgium, Portugal, Greece and Austria.
B. Infringement Proceedings and Alternative Problem Solving

Infringement proceedings are the Commission’s ‘classic’ tool to ensure respect for Community law. The number of infringement proceedings has increased considerably over the last decade\(^\text{12}\) and their handling today takes up a considerable amount of resources both in the Commission and in Member States. With enlargement, the number of infringements is set to rise further.

In its recent Communication on ‘Better Monitoring of the Application of Community Law’ (COM (2002) 725 final\(^\text{13}\)), the Commission has opted for a differentiated approach to the handling of complaints. In light of the seriousness of an alleged breach of Community law, the Commission decides on a case-by-case basis whether alternative problem solving mechanisms should be given a chance to resolve the problem or whether formal legal action needs to be initiated. The underlying philosophy is, where possible, to find rapid solutions\(^\text{14}\) (which conform to Community law) to the problems faced by complainants.

If a problem concerning a Member State is referred to the Commission or if it becomes aware of alleged breaches of Internal Market law on its own account, it can use complementary mechanisms as alternatives to infringement proceedings:

- PACKAGE MEETINGS
- SOLVIT

PACKAGE MEETINGS

Package meetings involve experts from Member States and the Commission coming together in order to discuss a ‘package’ of cases being examined by the Commission for violation of Community law. The experts from Member States and the Commission examine the cases together in an informal and constructive atmosphere. The purpose of these meetings, which have been taking place since 1987, but which have been stepped up in recent years, is of course to solve cases without the need for further legal action.

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\(^\text{13}\) Available at http://europa.eu.int/eur-lex/en/index.html

\(^\text{14}\) The majority of infringement cases take more than 2 years to be resolved. See Internal Market Scoreboard no 11.
Figure 7: Package meetings focus on Member States with most infringement cases

Note: Number of cases discussed in package meetings organised by DG Internal Market, DG Enterprise and DG Environment between 2000 and 2002.

Nearly half of all cases discussed in package meetings are solved or can be considered to be on the way to being solved (e.g. the Member State concerned undertakes to change its legislation). Even when cases remain unresolved, positions are clarified so that infringement proceedings can be pursued more swiftly.

Figure 8: Solutions are found to almost half of all cases

Note: Percentage of cases treated in 2002 in package meetings organised by the Internal Market Directorate General.
SOLVIT\textsuperscript{15}

SOLVIT deals with cases of misapplication of Internal Market rules by national and local administrations, such as the refusal to recognise a valid diploma or the refusal to allow market access to a product which conforms to the requirements of European directives. The main advantage is speed – SOLVIT sets target deadlines of 10 weeks to resolve complaints.

\begin{table}[h]
\centering
\begin{tabular}{|l|}
\hline
\textbf{Box 1: How SOLVIT works} \\
\hline
The system operates through a network of SOLVIT Centres\textsuperscript{16} based in the national administration of each Member or EFTA State. \\
\hline
\hspace{0.5cm} Complainants can contact their local SOLVIT Centre (known as the ‘Home’ SOLVIT Centre) who will first check if the complaint is justified. \\
\hline
\hspace{0.5cm} A case will then be entered into an on-line database system, allowing it to be forwarded immediately to the SOLVIT Centre in the other Member State where the problem has occurred (known as the ‘Lead’ SOLVIT Centre). \\
\hline
\hspace{0.5cm} The Lead SOLVIT Centre should confirm within one week, whether or not it will take on the case (‘electronic handshake’). \\
\hline
\hspace{0.5cm} Once accepted by the Lead SOLVIT Centre the target deadline for finding a solution to the problem is 10 weeks. The SOLVIT Centres liaise with each other during the period of investigation and keep the complainant informed of progress and the proposed solution. \\
\hline
Proposed solutions are non-binding for the complainant. If a problem goes unresolved, or if a complainant considers a proposed solution to be unacceptable, more formal proceedings can still be initiated. \\
\hline
\end{tabular}
\caption{How SOLVIT works}
\end{table}

SOLVIT has been operational since the end of July 2002. There are not yet enough SOLVIT cases to draw statistically valid conclusions. But the available statistics give some indication of the potential of the network and how it is functioning.

As at 15 April, 111 cases have been entered into the system. 33 cases are currently under investigation. Of the 78 closed cases, 56 have been resolved.

\textsuperscript{15} Further information on SOLVIT can be found at: http://europa.eu.int/comm/internal_market/solvit/

\textsuperscript{16} Contact details for all SOLVIT Centres can be found at: http://europa.eu.int/comm/internal_market/solvit/centres_en.htm
Figure 9: SOLVIT finds solutions to more than 70% of cases

Solved 72%

Unresolved 28%


SOLVIT Centres have in general acted within the 10 week target deadline for finding solutions (figure 10).

Figure 10: Most Member States solve cases in less than 10 weeks

Source: SOLVIT database. Average time between case input by the Home SOLVIT Centre and acceptance of the solution by Home SOLVIT Centre for accepted cases as at 15 April 2003. Austria, Liechtenstein and Norway so far have not resolved any cases.

The use made of SOLVIT is uneven. Germany, Portugal and the Netherlands have made the most active use of SOLVIT on behalf of their businesses and citizens. The fact that large Member States like Italy, Spain and the UK have entered relatively few cases into the system seems more an indication of a lack of visibility of SOLVIT in those countries than a sign that their businesses and citizens somehow have fewer difficulties in exercising their rights.
In autumn 2003, SOLVIT will be opened up to allow cases to be input online directly by organisations such as Euro Info Centres, the Citizen Signpost Service, Euroguichets, Chambers of Commerce and Trade Associations etc. This is expected to increase significantly the flow of cases. SOLVIT Centres will require adequate resources in order to be able to continue to meet customer needs.

**Box 2: Spanish authorities return fine to Portuguese breakdown service**

A Portuguese ‘specialised breakdown vehicle’ was transporting a damaged Portuguese car from Belgium to Portugal. It was stopped in Spain by Spanish traffic police and forced to pay a 600 € fine because the vehicle was not fitted with a tachograph.

The Portuguese SOLVIT Centre complained to the Spanish, because the relevant EC Regulation exempts breakdown vehicles from the obligation to install such equipment.

The Spanish administration accepted within 3 weeks that they had made a mistake and promptly repaid the fine.

**Box 3: Danish job-seeker’s husband gets residence permit in the Netherlands**

A Danish citizen was looking for a job in the Netherlands. She was registered with the Dutch Aliens Police as an EU-job-seeker. According to EU law, her Mexican husband was entitled to the same status, but the Dutch authorities refused to grant that status until she found a job.

After the intervention of the Dutch SOLVIT Centre the client’s husband was granted a residence permit with de facto the same rights as the client. The case was closed after 51 days and the client was satisfied with the proposed solution.

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17 The new Internal Market Strategy (2003-2006) commits the Commission to providing an information portal bringing SOLVIT together with other existing initiatives and contact points in order to facilitate public access.
INFRINGEMENTS

Alternatives to infringement proceedings are sometimes not suitable or fail to produce results. In those cases, the Commission takes vigorous action to ensure that Member States fulfil their legal obligations and that citizens and businesses can benefit fully from their Internal Market rights.

Regrettably, the number of open infringement cases\(^{18}\) has gone up by 6\% from 1505 in the November 2002 Scoreboard to 1598 today. The distribution of cases has hardly changed during the last 2 years; France and Italy continue to account for almost 30\% of all cases.

**Figure 12: Number of open infringement cases has gone up by 6 \%**

![Graph showing the number of open infringement cases by country](image)

Note: Open infringement cases as at 28 February 2003. Figures include associated cases (‘cas traité sous’), which are processed together with the respective main cases.

The Commission sometimes combines several cases, which are based on similar complaints, and pursues these as one principal case. This means that a large number of complaints would be solved if the principal case could be closed (see figure 13).

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\(^{18}\) Scoreboard infringement cases relate to cases of non-conformity or incorrect application of Internal Market law. They do not include cases of late transposition (for which infringement action is automatic) which are covered in the preceding section.
Figure 13: Some Member States could reduce the number of open cases significantly by solving just one principal case

<table>
<thead>
<tr>
<th>Number of associated cases</th>
<th>Principal case</th>
<th>Type of infringement</th>
<th>Stage reached</th>
</tr>
</thead>
<tbody>
<tr>
<td>D</td>
<td>German packaging legislation ('Töpfer law')</td>
<td>Non-conformity</td>
<td>European Court</td>
</tr>
<tr>
<td>UK</td>
<td>Surveillance of Lloyd's of London</td>
<td>Bad application</td>
<td>Letter of formal notice</td>
</tr>
<tr>
<td>EL</td>
<td>Insufficient environmental impact assessment</td>
<td>Non-conformity</td>
<td>European Court</td>
</tr>
<tr>
<td>IRL</td>
<td>Insufficient environmental impact assessment</td>
<td>Non-conformity</td>
<td>Court judgement + Reasoned opinion Art. 228</td>
</tr>
<tr>
<td>E</td>
<td>Water pollution</td>
<td>Bad application</td>
<td>Court judgement + Letter of formal notice Art. 228</td>
</tr>
<tr>
<td>F</td>
<td>Certain food additives not authorised by French legislation</td>
<td>Bad application</td>
<td>European Court</td>
</tr>
<tr>
<td>I</td>
<td>Absence of public tender in public procurement</td>
<td>Bad application</td>
<td>Letter of formal notice</td>
</tr>
<tr>
<td>B</td>
<td>Discriminative tax and prior authorisation requirements for the installation of satellite dishes</td>
<td>Bad application</td>
<td>Reasoned opinion</td>
</tr>
<tr>
<td>NL</td>
<td>Waste shipment</td>
<td>Bad application</td>
<td>European Court</td>
</tr>
<tr>
<td>FIN</td>
<td>Tax discrimination against cars from other Member States</td>
<td>Bad application</td>
<td>Letter of formal notice</td>
</tr>
<tr>
<td>TOTAL:</td>
<td></td>
<td></td>
<td>202 associated cases</td>
</tr>
</tbody>
</table>

Note: Principal cases with a high number of associated cases (‘cas traité sous’) as of 28 February 2003.

Not only has the total number of infringements gone up, but there has also been little or no progress in Member States’ ability to solve them quickly. Germany and Sweden have the best records. The performance of the Netherlands, Portugal and Denmark has deteriorated since last November. Overall, only one in about 3 cases is solved early (see figure 14).
Figure 14: Only a third of infringement cases are solved early

The Commission set a target in the last Internal Market Strategy Review for Member States to reduce the number of proceedings involving misapplication in which they are involved by 10% by June 2003 (see figure 15). So far progress has been disappointing. 11 Member States have even more infringement cases than a year ago. Only Germany and Luxembourg are on target.

Figure 15: Practically no progress towards reducing infringement cases involving misapplication of legislation

Note: Number of cases closed by 28 February 2003 as a percentage of the number of cases opened between 1 July 2000 and 30 June, 2002.

Note: Open infringement cases for incorrect application of secondary EU law (i.e. excluding Treaty law) as at 28 February 2003 compared to 28 February 2002 figures. Corresponding figures in Scoreboard 10 are not strictly comparable due to revision of the data set.
2. TAX OBSTACLES IN THE INTERNAL MARKET

Introduction

Tax obstacles play an important role in the under-performance of the Internal Market. At worst, they prevent the Internal Market from functioning correctly. More frequently they lead to significant and unnecessary compliance costs for business and all too often it is the consumer who ultimately pays for the resulting inefficiencies. This Scoreboard provides 4 thumbnail sketches which illustrate different facets of the problem.

Corporate taxation

Companies are currently faced with 15 separate tax systems in the Internal Market. After enlargement this will increase to 25. In 2001, the Commission identified a number of targeted measures to remove some of the individual tax obstacles, but concluded that in the longer term the only real solution is to introduce a consolidated tax base. Companies would then be able to operate across the Internal Market with the same ease as they currently do across each Member State by complying with a single set of computational rules.

Figure 16 shows that by and large it is the different nominal tax rates levied by Member States which determine the overall effective tax rate* for a profitable business and not the complex calculations which each State requires to establish the taxable profits or tax base. In general the higher the nominal tax rate, the higher the overall effective tax rate, and vice versa.

Figure 16: No major differences between nominal and effective tax rates

Source: European Commission, DG Taxation and Customs Union. 2002 Effective Average Tax Rates (EATR) and nominal rates.

* The Effective Average Tax Rate compares the after-tax present value of an investment project with the pre-tax present value of the project. It is a common measure to compare the real tax burden of companies across countries, as it sums up the combined effects of different nominal tax rates and tax bases taking into account tax exemptions, allowances etc. An in-depth discussion of the EATR and other methods can be found in ‘Company Taxation in the Internal Market’, a Commission Staff Working Paper (SEC 1681 issued October 2001).
A single consolidated tax base for companies with EU-wide activities would not restrict Member States in their choice of tax rate. This fits in with the Commission’s current view that rates are a matter for Member States, and would bring a number of benefits such as:

(i) A far greater degree of transparency and simplicity. It would be easier for companies to decide where to locate their investments within the Internal Market and it would lower the risks of the tax system distorting such decisions.

(ii) A reduction in compliance costs – the current 15 sets of rules would be replaced by a single set.

(iii) A solution to the growing transfer pricing problem which brings uncertainties and the risks of double or non-taxation of company activities.
Box 4: The transfer pricing problem

Currently a business with activities in several countries has to ensure that every transaction between its entities in different Member States is recorded at the ‘arm's length price’\(^{19}\), so that each Member State can tax the ‘correct’ amount and the business cannot, for example, simply allocate profits to the State with the lowest tax rate. In the diagram above there are 3 prices to be agreed by the tax authorities in the relevant Member States: the amount of licence fee (UK & France), the price of the raw materials (Germany & France) and the price of the finished plastic (France & Italy). However, there are a number of different methods for determining the ‘arms length price’ and no guarantees that the tax authorities in the different Member States will agree on the price to be charged as there is no single ‘correct’ answer. Arrangements do exist for attempting to solve this problem, but the whole process of computing the correct price, preparing the supporting documentation and finding agreements to resolve disputes is costly and time consuming for both business and administrations. In addition, there is no guarantee that any double or non taxation will be removed.

Short term solution: the Commission has established a Joint Transfer Pricing Forum composed of Member State and business experts to consider non-legislative pragmatic improvements to the existing process. A number of meetings have already been held.\(^{20}\)

Long term solution: the Commission is convinced that the best solution is to establish a common consolidated tax base across the EU thereby removing the need to establish prices for every single intra-group transaction. A new agreed mechanism would be required for allocating the overall tax base of each business between Member States.

Value Added Tax

Business also faces obstacles as a result of the value added tax system. In November 2000 a Commission survey showed that 26 % of businesses considered difficulties related to the VAT system and VAT procedures to be an obstacle to doing business in the Internal Market. In September 2001 a further survey showed that VAT payments and refunds were

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\(^{19}\) The 'arm's length principle' means that a subsidiary should be charged the same price as an external customer.

rated third among regulatory burdens that are the most costly for companies.\textsuperscript{21} The multiplicity and complexity of the VAT requirements in the 15 Member States, combined with difficulties in obtaining foreign refunds leads to substantial costs and represents a real barrier to cross border activities.

The Commission is currently examining the possibility of simplifying and modernising VAT obligations. In addition to technical discussions with Member States, it is carrying out a public consultation on possible improvements. It is hoped to present a proposal in 2004.

**Motor vehicles**

Successive Internal Market Scoreboards have illustrated the point that excessive price dispersion for products is an indication that the Internal Market is not working as it should.

*Purchasing a car*

Taking the example of passenger cars, figure 17 indicates clearly that the European consumer is being charged very different prices in different national markets for what is essentially a homogeneous product.

**Figure 17: Still substantial pre-tax price differences for new cars**

<table>
<thead>
<tr>
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<th>A</th>
<th>B</th>
<th>D</th>
<th>DK</th>
<th>E</th>
<th>EL</th>
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<th>IRL</th>
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<th>NL</th>
<th>P</th>
<th>S</th>
<th>UK</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Ford Fiesta</strong></td>
<td>119</td>
<td>112</td>
<td>126</td>
<td>102</td>
<td>103</td>
<td>104</td>
<td>107</td>
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<td>112</td>
<td>103</td>
<td>100</td>
<td>114</td>
<td>121</td>
</tr>
<tr>
<td><strong>VW Golf</strong></td>
<td>121</td>
<td>124</td>
<td>132</td>
<td>102</td>
<td>125</td>
<td>103</td>
<td>121</td>
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<td>132</td>
<td>123</td>
<td>121</td>
<td>122</td>
<td>126</td>
</tr>
<tr>
<td><strong>Peugeot 307</strong></td>
<td>120</td>
<td>116</td>
<td>123</td>
<td>89</td>
<td>109</td>
<td>100</td>
<td>119</td>
<td>109</td>
<td>117</td>
<td>103</td>
<td>116</td>
<td>112</td>
<td>110</td>
<td>105</td>
<td>130</td>
</tr>
<tr>
<td><strong>Opel Vectra</strong></td>
<td>114</td>
<td>123</td>
<td>114</td>
<td>122</td>
<td>100</td>
<td>105</td>
<td>114</td>
<td>107</td>
<td>120</td>
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<td>123</td>
<td>110</td>
<td>117</td>
<td>119</td>
<td>122</td>
</tr>
</tbody>
</table>

Source: European Commission, DG Competition. Index values: lowest Euro-zone-price (as of 1 November 2002) excluding taxes = 100 (adjustments are made for differences in standard equipment). See http://europa.eu.int/comm/competition/car_sector/price_diffs/

These differences result primarily from 2 components: Member States’ taxation policies and manufacturers’ pricing policies. Figure 18 indicates clearly the differences in taxation (details of both registration tax (RT) and value added tax (VAT) are shown). The large differences in tax levels between Member States induce manufacturers to set different pre-tax car prices in each Member State. For example the pre-tax prices are in general higher in Member States applying no, or a low, RT and vice versa; and the same goes for VAT. The car industry can take the level of taxes into consideration when setting pre-tax prices because, up to now, cross-border retailing and purchasing in the Internal market has not

\textsuperscript{21} See Internal Market Scoreboard no. 9.
taken place to any significant extent. However, this situation should change as a result of the reform by the Commission of the competition rules for car sales and servicing. These new rules introduced in October 2002 should make such cross-border shopping easier. The attraction for the consumer is that when a car is purchased in a ‘high tax’ Member State for personal import he/she is able to pay the lower pre-tax price with the taxes being paid in the ‘home’ State, thereby achieving a lower total price.

**Figure 18: Enormous differences in car taxation**

![Graph showing differences in car taxation across Member States.](image)


As more consumers take advantage of this aspect of the Internal Market the manufacturers’ pre-tax prices in different Member States have already started converging and part of the excessive price dispersion should disappear. However, as long as the other factor remains – the wide range of taxation levels across the Internal Market, some differences in prices will remain. It is hoped that Member States will play their part by more closely aligning their taxation policies on motor vehicles.

**Taking a car to another Member State**

Another example of problems within the Internal Market concerns taking a car to another Member State when a car-owner either moves from one Member State to another or purchases a second-hand car in another Member State. Different tax structures and administrative problems lead to a lack of transparency, and increased transaction costs for the consumer. Not only can the consumer end up being taxed twice – paying a second set of registration taxes – but the whole process is often very complex and there is a lack of comprehensive and easily accessible information for EU consumers. Taxation is not the only cause of the problem but it plays a significant role. Registration Taxation (RT) is a particular culprit and the Commission has suggested\(^22\) that RT levels should be gradually reduced, stabilised at low levels and preferably abolished over a transitional period of 5 to 10 years. Instead, Member States should raise revenue from car owners by switching over to increased annual circulation taxes and fuel taxes. Not only will taking a car to another

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Member State become easier but, because RT is also an element of the price of a new car, this should also have a positive effect on the approximation of car prices.

**Pension taxation**

The elimination of tax obstacles to the cross-border provision of occupational pensions is a priority for the Commission. Many Member States deny equal treatment to foreign pension funds: pension contributions paid to domestic funds are tax deductible, contributions paid to foreign funds are not. Not allowing mobile workers tax deductions for pension contributions paid to their original scheme restricts their right of free movement. Equally, the tax discrimination restricts pension funds’ ability to use their freedom to provide services. And companies with establishments in different Member States are prohibited from centralising their occupational pension arrangements into a single scheme for all their employees throughout the Union. Such centralisation would bring companies considerable economies of scale and cut administrative costs significantly.

Following the legal analysis in its pension taxation Communication of 19 April 2001 the Commission has examined the complex national tax rules governing contributions to complementary pension schemes. As a result of this examination the Commission sent a Reasoned Opinion to Denmark on 5 February 2003 under Article 226 EC, asking it to change its tax legislation and give pension contributions paid to pension funds located in other Member States the same tax treatment as contributions to domestic funds. At the same time the Commission opened infringement proceedings against Belgium, Spain, France, Italy and Portugal, which have similar rules. The Commission continues its examination of national laws and more infringement procedures may follow. The Finnish rules on pension taxation were already found to breach Community law in the Danner case, decided by the European Court of Justice on 3 October 2002 (Case C-136/00). The Swedish pension taxation legislation is currently also being examined by the ECJ on the basis of a request for a preliminary ruling (Skandia/Ramstedt, Case C-422/01).

**Conclusion**

The examples described above, drawn from 4 quite different areas of taxation: corporate taxation, value-added tax, motor vehicles and pensions, show how differing rates, bases and systems can create obstacles which frustrate the operation of the Internal Market. Business suffers, the consumer suffers and administrations themselves incur additional costs and may lose out on tax revenues. Such obstacles can only increase as the EU expands to include 25 States and 25 tax systems. The Commission response is consistent – seeking to remove the obstacles and improve the functioning of the Internal Market – and, as the examples show, it includes a range of policy instruments.


3. NEW MEMBER STATES HAVE SUBSTANTIALLY LOWER PRICES

In May next year the EU is set for its biggest enlargement ever in scope and diversity. The addition of 75 million citizens from 10 Accession Countries will create the largest Internal Market in the world in terms of purchasing power.

This enlargement poses a big challenge for the Internal Market but also promises large rewards. At the macroeconomic level the enlargement has the potential to increase trade, growth and employment\textsuperscript{24}. Citizens will benefit both from new professional opportunities and from more competition leading to a wider choice of better and cheaper products. Businesses will have many new market opportunities to exploit.

This enlargement is noteworthy for its size – but there are also many other important aspects, including some very interesting issues in relation to prices:

- Most Accession Countries have a very low price level compared to current Member States. When Portugal and Spain joined in 1985 their price level was respectively 60 and 72\% of the EU12 average\textsuperscript{25}. Half of the new Member States have a price level below 50\% of the EU15 average.

- Member States with very high price levels are geographically close to new Member States with very low price levels. For instance, the Baltic countries are close to the Scandinavian countries, which currently have some of the highest prices in the EU. Germany with a price level around the EU average will have 2 new EU neighbours with prices half the German level.

This Scoreboard focuses on the price differences between the 10 Accession Countries and EU15. It also draws comparisons with previous enlargements.

**How big are the price differences between Accession Countries and EU15?**

The 10 new Member States that will join the EU next year all have price levels for goods and services significantly below the EU15 average. Their average price level is only 54\% of the EU average\textsuperscript{26}.

Malta and Cyprus stand out among Accession Countries as their income and price levels resemble those found in Portugal, Spain and Italy. Figure 19 shows that their aggregate price level is significantly higher than in the other Accession Countries, but still around 20\% below the EU15 average.


\textsuperscript{25} Private final consumption in 1985. Source of all price data in this chapter: Eurostat (purchasing power parities dataset).

\textsuperscript{26} Unweighted average of the price level for private final consumption in 2000. Private final consumption includes all goods and services purchased by people.
Figure 19: Prices for goods and services in the new Member States are significantly below the EU15 average

Source: Eurostat. The figures show the price level for goods and services (private final consumption, 2000) in the new Member States compared to the EU15 average (EU15 average = 100). * 1999-price level for Malta.

A second group of countries, Latvia, Poland and Slovenia, have a price level somewhat higher than 50% of the EU15 average but still significantly below the EU Member State with the lowest aggregate price level (Portugal). The remaining 5 countries have quite similar price levels - between 40 and 50% of the EU15 average price level.

In international price comparisons it is normal to find a fairly close connection between price levels and income levels. The lower price levels in the Accession Countries are indeed partly a result of lower income levels in these countries.

However, differences in incomes across the Accession Countries cannot explain all the observed differences in prices (see figure 20). Hungary, the Czech Republic, Slovenia and the Slovak Republic all seem to have a low price level compared to their income levels. On the other hand Cyprus, Poland, Estonia, Lithuania and Latvia all seem to have high price levels relative to their income level.

This is an indication that other factors – differences in market structure, the competitive pressure in the economies, differences in the retail structure, taste etc. – contribute to the price differences. Figure 20 therefore shows that although price differences are not that big across many of the new Member States, the economic structures in the Accession Countries might in fact be rather different.

For more information about factors explaining international price differences see Scoreboard no. 10.
Figure 20: Differences in income levels can only explain some of the differences in prices

![Graph showing differences in income levels and price levels for various countries.](image)

Source: Eurostat and DG Internal Market calculations. The figure compares income levels (GDP per capita in PPS, EU15 = 100) with aggregated price levels (GDP price levels, EU15 = 100) for 2000. No information available for Malta in 2000.

The low aggregate price level found in the Accession Countries seems to be explained to a large extent by their relatively low wages and rents. Products with a high input of local labour and produced in the new Member States thus have significantly lower prices, whilst prices for product groups where many goods are imported are similar to EU prices (see figure 21).
Figure 21: Soft drink prices in the Accession Countries are close to the EU15 average whereas services are still considerably cheaper

Very low price levels relative to the current EU countries are thus found for a number of services such as hairdressing. Other examples are repair services, medical services, educational services and some insurance products. In many of the new countries prices for these services are only a third of the EU-level.

Food is also much cheaper in the Accession Countries. Different kinds of meat, bread, flour, butter etc. are in general half the price in the present Member States. Again it should be borne in mind that there are big differences across the Accession Countries. For example, the price of flour and other cereals in Cyprus is more than in the Netherlands (cheapest EU country), whilst the price in the Czech Republic is only a third of the EU average.

Prices for furniture, clothing and footwear are in the Accession Countries on average 75% of the EU15 average. In a number of the new Member States prices are therefore similar to those in many EU countries.

Finally, prices for soft drinks in some of the new Member States are above the EU15 average. And for some consumer electronics and white goods, for instance washing machines, dryers and dishwashers, the average prices in the Accession Countries are even above the EU15 average.

What could happen when the new Member States join the EU?

Monitoring price convergence across Member States and Accession Countries provides us with valuable hints to the extent to which markets are really integrating. The experience from previous enlargements shows that catching up starts very quickly – often even before enlargement has taken place. Figure 22 shows that in the last enlargements, price differences in the enlarged EU were reduced after enlargement and that this was to a large extent a result of convergence driven by the new Member States.
Figure 22: History shows that new Member States converge towards old Member States

![Figure 22: History shows that new Member States converge towards old Member States](image)

Source: ESTAT and DG MARKT calculations.

After the Accession Countries become part of the EU they will continue to catch up with EU15 living standards. Wages and incomes will increase as the countries get richer and this will naturally spill over into prices, especially non-tradable goods and services. The large differences in prices of services between the new and the old Member States described in the previous section is therefore likely to be reduced over time.

However, enlargement might actually deliver downward pressure on the prices of some tradable goods and services in the new Member States. More efficient economic structures in the new Member States can lead to lower prices in some sectors. For instance, the experience with the liberalisation of telecommunication industries in EU15 shows that competition can deliver lower prices to consumers. In this context the Internal Market plays an important role not only by ensuring competitive pressure, but also by facilitating cross border investment and exchange of know-how.

There is therefore every reason to believe that this enlargement will follow the example of previous enlargements and lead to price convergence. Indeed, for the 10 new Member States that will join next year convergence seems to have begun already. Currently, information for only 3 years is available for the new Member States\(^{28}\). It is therefore too early to draw firm conclusions. However, from 1999 to 2001 the price dispersion in EU25 has been reduced from 27.2 % to 25.6 %. In the same period the price dispersion in EU15 has remained stable. The narrowing of the gap seems therefore to be a result of a convergence process starting in the new Member States.

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\(^{28}\) Data for 2001 is preliminary.