

# Towards a Competitive Edge: Reforming the EU Regulatory Framework

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# Executive summary

Amidst an increasingly complex economic situation, Europe's decrease in competitiveness is one of the most dangerous threats to the bloc's long-term prosperity. Together with high energy prices, difficult access to finance, and skills and labour shortages, the EU's regulatory burden is cited by businesses across the Union as a major obstacle limiting investment, innovation, and productivity.

This problem has become more acute as the EU has responded to recent crises with an unprecedented regulatory push to advance its green and digital transitions. These goals are an integral part of the European Commission's long-term strategy, but they also come at a cost for European firms. The question, therefore, is **how to combine these ambitious objectives with a regulatory environment fit for competitive businesses.**

Looking at the EU's Single Market and Better Regulation agenda's unfulfilled potential, we present the main challenges weighing on the EU's evolving regulatory environment and accompany them with concrete policy recommendations to address the situation:

- 1. Turn competitiveness into an overarching goal of policymaking** to alleviate the cumulative regulatory burden affecting all European firms (big and small), which stems from legislative uncertainty and complex reporting requirements.
- 2. Make regulation more sensitive to business size** to relieve the disproportionate burden on small businesses and mid-caps, the 'hidden champions' falling just above the large-company threshold, which the EU has hitherto failed to identify.
- 3. Reinforce the Single Market as a top priority** to ensure a level playing field across member states, by ramping up enforcement, harmonising service markets, and reducing state aid where asymmetric fiscal capacities threaten competition.
- 4. Generate greater international efforts** to limit the possible fallout from supply chain regulation and to perpetuate Europe's Brussels effect, by flanking regulatory initiatives with international partnerships and by taking a more integrated approach to regulatory, trade, foreign and development policy.

# Recommendations for a competitiveness enhancing regulatory framework

## MAKE COMPETITIVENESS AN OVERARCHING GOAL FOR POLICY MAKING AND THE BETTER REGULATION AGENDA

**Recommendation 1:** The EU must adopt competitiveness as an overarching goal for its policy and law-making activities, on a par with environmental, digital, security, and social policy objectives. This should be reflected not only in individual legislative initiatives but also in strategies and programmes in their entirety, including the mandate of the Commission taking office in 2024.

**Recommendation 2:** A Commission Executive Vice-President for 'Economic strategy and competitiveness' should be appointed to oversee the overall economic portfolio of the next Commission, supervising everything from competitiveness and trade to industrial policy and economic security. (S)he should be granted a strong mandate regarding the application of competitiveness checks on EU regulatory initiatives and engage in regular political dialogues with the Council, the European Parliament, and other stakeholders, including industry leaders and business associations.

**Recommendation 3:** The Commission should aim to reduce not only reporting requirements in EU regulation by 25% but all administrative burdens by at least 25% over the next mandate. By running a competitiveness check on the entire *acquis*. This exercise should also remove as much as possible barriers to innovation and growth. To operationalise this, a "Stoiber 2" cross-DG taskforce of economists should be established, which could later be integrated together with the Regulatory Scrutiny Board (RSB) into a permanent European supervisory authority for regulatory scrutiny.

**Recommendation 4:** The Better Regulation agenda should be implemented more systematically and more effectively with a focus on enhancing competitiveness. For that, the RSB should be more independent and receive more resources to hold the Commission accountable, the Council and the Parliament should perform their own impact assessments for amendments, businesses should be earlier and more rigorously included in the legislative process and better use should be made of digital tools throughout the legislative process and for regulatory compliance.

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**The Better Regulation agenda should be implemented more systematically and more effectively.**

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## MAKE PROPORTIONALITY A CORE CRITERION FOR LEGISLATION

**Recommendation 5:** To counter Europe's businesses' 'Peter Pan syndrome', the European Commission should reconsider its "Think Small First"-principle, and the implicit political preference towards small size economic actors, in favour of an economic policy focussed on growth and scaling. This shift in focus could be formulated as a "Think Growth and Scaling First"-principle.

**Recommendation 6:** In order to create a positive "competitiveness shock" for a critical segment of European businesses and trigger scaling dynamics, the Commission should extend the SME definition with all its benefits and exemptions to firms with up to 500 employees, hence relieving and boosting Europe's small mid-caps, which suffer particularly from disproportional regulatory burdens.

**Recommendation 7:** Indissociably from the above, the Commission must also establish a new pan-European mid-cap category and definition covering companies from 500 to 3000 employees, which studies show present distinct characteristics. The establishment of this statistical and legal category should then serve to build a programme of legal simplification and support actions to boost these companies' role as Single Market growth and productivity champions and vectors of Europe's economic transitions.

**Recommendation 8:** The EU institutions, member states and business associations should facilitate SMEs and mid-caps' participation in regulatory sandboxes and public consultations. They should also ensure that burdensome reporting responsibilities are tailored to size and not passed on from large companies, while improving access to growth financing, concessional loans and grants.

## MAKE THE REINFORCEMENT OF THE SINGLE MARKET A TOP PRIORITY

**Recommendation 9:** The next Commission should better implement and enforce European legislation across all member states, by strengthening the Single Market Enforcement Taskforce (SMET), encouraging greater collaboration between national lawmakers and the Commission with the creation of national single market offices and strengthening SOLVIT centres in some key member states as a tool for businesses to report breaches of Single Market rules.

**Recommendation 10:** Single Market action plans with clear milestones should be launched for key sectors in a new drive towards deepening the Single Market for services. This should include energy, professional, financial, telecommunication and digital services as well as defence.

**Recommendation 11:** In areas where harmonisation is difficult to achieve, the EU should return to a more ambitious use and application of the Single Market's foundational principle of 'mutual recognition'. Article 3 of the e-Commerce Directive (2000/31) provides the template of a strong 'internal market clause' combining country of origin rule and mutual recognition. The EU should apply it to other strategic sectors where the benefits of Single Market depth and scale are urgently required.

**Recommendation 12:** The Temporary Crisis and Transition Frameworks for state aid should be gradually phased out to protect the Single Market from distortive subsidies. To finance the EU's transitions and industrial strategy, there should be more EU level funding in the form of a Sovereignty Fund. More use should be made of Important Projects of Common European Interest (IPCEIs), and they should be financed and managed primarily by the EU.

## INCREASE EFFORTS TO MANAGE GLOBAL REPERCUSSIONS OF SUPPLY CHAIN REGULATION

**Recommendation 13:** To better account for the international impact of regulation, the EU should pay consistent attention to international competitiveness in its competitiveness checks and invest more to facilitate company-led setting of standards, as those can often better anticipate the international effect of EU legislation.

**Recommendation 14:** The Commission should coordinate more with international partners, international standard setters and international organisations to try to gain support for new supply chain standards such as in the Corporate Sustainability Due Diligence Directive (CSDDD), or the deforestation regulation.

**Recommendation 15:** The EU must be ready to offer benefits and assistance particularly to countries in the Global South for the adoption of its standards and to protect its trade and business relationships in critical areas. The EU should consider all relevant policy tools – including trade and investment, technical assistance, development policy, and support of civil society – to help countries in the Global South to become more sustainable by themselves and abide by European standards to perpetuate the Brussels effect.

# Introduction

In recent years, Europe's economy has faced the multifaceted shock of high energy prices, tightening monetary policy and investment conditions, and a geopolitical landscape increasingly hardened by 'great power' competition. This has come along with greater state intervention and a more confrontational trade environment that has arguably weakened the EU's global standing.

The Union's flagship projects, the European Green Deal and the Digital Decade, represent unique opportunities for the continent to move toward carbon neutrality, achieve a more productive, digitalised economy, and increase strategic autonomy. However, they also come with significant compliance costs and burdensome reporting requirements that many fear will reduce Europe's competitiveness.

Looking at the EU's Single Market and Better Regulation agenda's unfulfilled potential, we analyse the main challenges businesses face in Europe's evolving regulatory framework.

First, European firms are confronted with a **cumulative regulatory burden** problem, resulting from years of intensive regulatory activity and a recent push to accelerate the EU's green and digital transitions. The high costs and legislative uncertainty associated with it are hurting companies trying to stay ahead of the competition and weather the already complex global economic environment.

Second, EU regulation has not been **sensitive to business size**, with many new measures imposing

reporting requirements that will affect (directly or indirectly) SMEs and mid-caps disproportionately. Without the same resources as larger companies, most will have to invest in compliance at a high cost to innovation.

Third, aside from the impact on specific companies or sectors, the new regulatory environment risks disrupting the **internal market's playing field** and exacerbating the imbalances between member states. The weak enforcement and insufficient harmonisation of rules have resulted in a weakened Single Market, and after years of neglect, Europe's biggest asset is endangered. This is exacerbated by recent state aid liberalisations, which will accentuate asymmetries between countries with more and less fiscal space.

Lastly, there are potential spillover effects on international trade and investment that could undermine **Europe's global competitiveness**. The new rules have consequences that will inevitably affect third countries lacking the resources or commitment to comply with the EU's standards, which instead of triggering a 'Brussels effect' may end up backfiring.

Hence, the EU's challenge is to create a regulatory framework that is fit for purpose and can reconcile its ambitious green, digital, and economic security objectives. In doing so, it will need to consider the impact of new rules on competitiveness and the different administrative and fiscal capacities of European businesses and member states, both in terms of implementation and enforcement of regulation.

## Background: The urgent need for a European competitive edge

In recent years, the European Union has found itself at the epicentre of a rapidly changing economic landscape. The COVID-19 pandemic, the war in Ukraine, rising geopolitical tensions, and extreme weather events have put European economies under increasing pressure. Furthermore, businesses of all sizes have faced supply chain bottlenecks, high energy prices, tightened monetary policy conditions, skills and labour shortages, and rising climate-related costs. At the same time, the liberal free trade order as a basis of the EU's wealth has been increasingly undermined by discriminatory trade and industrial policy, while the EU has been lagging behind in productivity and key transversal technologies for quite some time.

The green and digital transitions can play an important role in cushioning the impact of recent crises, stimulating growth and supporting the shift towards greater economic security, another central goal of the von der Leyen Commission. EU member states have broadly aligned behind these ambitious objectives and supported the Commission's activities to make the EU more resilient and fit for a green and digital future with a range of new legislative proposals.

These efforts represent a unique opportunity to achieve the EU's long-term goals and increase strategic autonomy. However, they have also come with significant compliance costs and burdensome reporting requirements that negatively affect the competitiveness

of European businesses at a time of strong economic headwinds. From the industry's point of view, many of Brussels' recent legislative projects, such as the Fit for 55 package, the Taxonomy Regulation, the AI Act, the Carbon Border Adjustment Mechanism (CBAM), the Corporate Sustainability Reporting Directive (CSRD) and Corporate Sustainability Due Diligence Directive (CSDDD), have taken too little account of their impact on businesses.<sup>4</sup>

Europe's increasingly complex regulatory environment is demanding greater reporting requirements and creating additional costs that many observers see as potential barriers to growth and global competitiveness. To make matters worse, many firms feel that the Single Market has been weakened and that there is a high degree of uncertainty about how the new regulations will be implemented, as impact assessments have often been limited or disregarded.<sup>2</sup>

The EU's Better Regulation agenda has made some progress over the past 20 years but has struggled to keep up with the recent pace of regulatory change and technological innovation. In this context, business representatives have been calling for greater efforts to streamline legislation, reduce reporting requirements, and provide more regulatory certainty, with some even calling for a regulatory break. What is clear is that in the current situation, providing a leaner regulatory framework will be crucial to improve the EU's competitiveness.

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**58% of mid-sized 'Mittelstand' companies claim to not invest in Germany anymore due to red tape.**

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## State of play: Better regulation underway, but still short of the mark

### CUMULATIVE IMPACT OF REGULATION: HIGH COSTS AND LEGISLATIVE UNCERTAINTY

In recent years, the accumulation of environmental, social, and governance (ESG) legislation and reporting requirements has put Europe at the forefront of the global fight for sustainability and social rights. However, it has also taken a toll on European companies' competitiveness, arguably impeding investment, employment, and growth opportunities, and limiting their ability to navigate what is already an increasingly complicated global economic environment. Business associations warn of a potential

Ultimately, the political case for a competitiveness-enhancing regulatory framework has never been stronger. In the recent Antwerp Declaration on an European Industrial Deal, over a thousand organisations across Europe's economy call for an "urgent need for clarity, predictability and confidence".<sup>3</sup> The issue has not gone lost on Commission President von der Leyen, who dedicated significant time in her last State of the Union address to outline ways to make business in Europe easier.<sup>4</sup> In a climate of low growth and fear of decline, creating a regulatory environment fit for competitive businesses is a central theme for the approaching European Parliament elections and the next European Commission.

The forthcoming reports on the Single Market and enhancing EU competitiveness led, respectively, by Enrico Letta and Mario Draghi, are expected to go in this direction, as does the recent 2024 Annual Single Market and Competitiveness Report, which recognises the need for a better functioning Single Market and regulatory simplification.<sup>5</sup>

The faltering European economy, rising living costs, and the mounting price of the green transition to be borne by citizens have created a tense political climate with a sharp rise in polls for right-wing, euro-sceptic parties. A large regulatory burden and a weakened Single Market making life more difficult for businesses might eventually ramp up consumer costs and affect voters at their core. In this context, it is essential to improve conditions for companies and investment and convince the business community that the EU can deliver both sustainable growth and a competitiveness-enhancing regulatory framework.

risk of de-industrialisation, as companies relocate their production outside Europe and experience rising cases of bankruptcy.<sup>6</sup> For example, 58% of mid-sized "Mittelstand" companies claimed to not invest in Germany anymore due to red tape.<sup>7</sup>

One issue is the increase of highly complex and granular reporting requirements stemming from existing and upcoming EU regulations such as the CSRD and the CSDDD.<sup>8</sup> These obligations carry high costs, especially for non-capital-market-oriented firms, like industrial companies, which are critical to the EU's transition goals.

Excessively prescriptive legislations limit firms' options to find the best solution to a problem. By setting up such overhead structures, companies of all sizes sacrifice innovation, and weaken their ability to finance transformation, research, and additional sustainability.

Consequently, ESG obligations do not necessarily lead to a more sustainable economy. Often, valuable capacities that could be invested in developing innovative sustainable products end up being spent on additional administrative staff or on expensive consultations without which compliance could not be achieved. For example, in a factory with 9,000 employees, more than 80 may be involved in reporting duties.<sup>9</sup> Moreover, some requirements, such as the reporting on supply chains included in the CSDDD, are not only very costly but also reported by business as being hardly feasible. This is especially true in the high-tech sector, where supply chains can be extremely complex. For example, a large company like Dutch lithography machine producer ASML depends on around 5,000 suppliers, some of which in turn rely on even more.<sup>10</sup> Particularly for smaller suppliers, abiding by such supply chain monitoring prescriptions can be hard to realise.

The high burden in reporting requirements is compounded by the sheer amount of new legislation, which often creates duplications and overlaps that increase regulatory uncertainty, weighing on firms' ability to plan and invest. For example, many of the social requirements in the Ecodesign for Sustainable Products Regulation (ESPR), the CSDDD, and the CSRD overlap, unnecessarily increasing the regulatory burden. Similarly, between the proposed ESPR and the older regulation on the registration, evaluation, authorisation and restriction of chemicals (REACH), there are duplications, contradictions, and inconsistencies. Add existing national, regional, and local regulations (see below), and it is not hard to find examples leading to confusion and legal uncertainty. As a result, many firms prefer not to innovate and invest, instead of running the risk of having to pay high fines.

Such inconsistencies are also the result of the EU institutions and stakeholders' difficulties in processing the great amount of fast-track legislation in the past few years, such as the Fit for 55 package, the Net-Zero Industry Act, the reform of the Electricity Market Design, the Critical Raw Materials Act, and the Data Act. This greater speed in lawmaking might have been necessitated by the recent crises, but it has also demonstrated the limits of the EU's Better Regulation system and aggravated existing shortcomings.

For one, it has made it harder for stakeholders to react and for legislators to incorporate feedback in a timely and balanced manner. This has exacerbated existing weaknesses with the involvement of stakeholders in the policymaking cycle. Often, consultations do not take place early enough to impact the Commission's policy-making process decisively. Moreover, they are often structured in a way that does not allow for important concerns to be considered by the Commission, for

## WHAT BUSINESS REPORTS...: COSTS OF THE CORPORATE SUSTAINABILITY REPORTING DIRECTIVE

According to the Foundation for Family Businesses and Politics, a well-known family-owned company in the air filtration sector with around 22,000 employees faces the quantitative and qualitative assessment, and possible reporting, of up to 1,149 data points under the CSR Directive. Not only do one-off costs total €4-5 million, the work will also generate recurrent personnel costs that are many times higher, as well as fees from auditing and consulting services. This money will be spent exclusively on additional reporting and will be unavailable to finance the company's transformation, research, and additional sustainability.

Source: Foundation for Family Businesses and Politics.

example, because of restricting input to multiple choice answers, or because it does not respond to the most material issues but to those that have been raised by the highest number of stakeholders.<sup>11</sup>

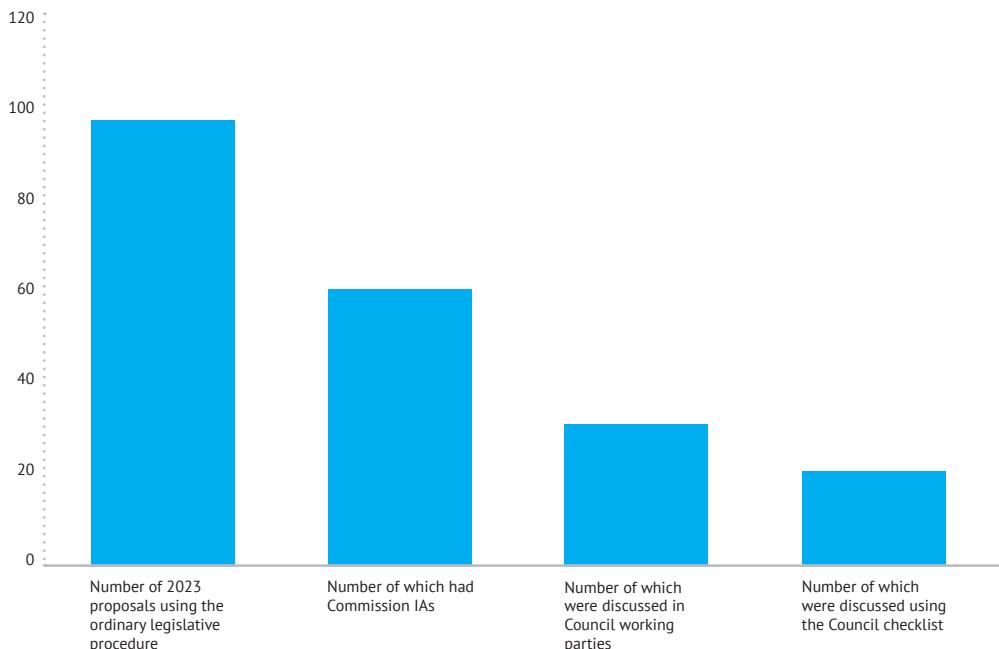
Regulatory sandboxes, which provide a powerful tool to simulate the effect of legislation in innovative industries<sup>12</sup> have been limited to a few sectors, such as pharma. The Commission's online public consultations through its "Have your say" portal attracts a low participation rate among businesses. One reason for this is insufficient information for and mobilisation of businesses by their associations and member states. Another the high degree of complexity of the Commission's Calls for Evidence, their insufficient visibility and often very limited periods of time for businesses to respond. This makes it difficult to include the views of smaller businesses as they often lack sufficient resources to react quickly and effectively to legislative proposals.

Moreover, co-legislators have often failed to examine legislation carefully on their impact on competitiveness. In significant regulatory files, both the European Parliament and the Council have been processing amendments very quickly, which then are not sufficiently checked for their effect on competitiveness due to the lack of systematic impact assessments. An example is the proposal for the deforestation directive, which despite substantial amendments did not receive proper impact assessment as the text evolved.

These problems are also compounded by the fact that member states are not very proactive in making data available to support impact assessments.<sup>13</sup> In certain cases, it is also the Commission that passes over the need for impact assessment, as was the case with the forced labour regulation proposed in September 2022 despite the substantial reporting requirements (and potential sanctions) it entails.<sup>14</sup>

Figure 1

### THE COUNCIL IS NOT MAKING PROPER USE OF COMMISSION IMPACT ASSESSMENTS



Source: CER.

Moreover, institutional cooperation in lawmaking is often suboptimal, as evidenced by the fact that the Parliament and the Commission use different criteria to evaluate legislation. The Commission's impact assessments mainly use very technical cost-benefit criteria, which are hard to integrate into the political process of agreeing on amendments in the Parliament or the Council.<sup>15</sup> As regulation is not assessed according to the same standards, inconsistencies become more likely. Moreover, the Commission has increasingly employed delegated acts to expand the scope of laws or to introduce substantive and onerous new requirements. Many were introduced without a proper impact assessment, while opinions of stakeholders and expert bodies have often been ignored, such as the recommendations of the European Banking Authority concerning new rules on payment security.<sup>16</sup>

But also, the Commission's ever-evolving better regulation agenda, which includes an extensive Better Regulation Toolbox with detailed rules for its ex-ante impact assessments have fallen short. These rules are often not adequately implemented and enforced. Especially, impacts on competitiveness and on SMEs have not been adequately considered.<sup>17</sup> This has been confirmed by the Commission's own Regulatory Scrutiny Board (RSB),<sup>18</sup> whose objections the Commission has not always respected, for example, in the case of the CSDDD. Currently, the RSB's ability to carry out its work to provide independent scrutiny and accountability is curtailed through a lack of resources, while five of its four members, including its chair, are Commission officials rather than independent experts.<sup>19</sup>

Moreover, despite a whole chapter on digital ready policymaking in the Better Regulation Toolbox, EU institutions and member states have done relatively little to better exploit the great potential of digitalisation to reduce regulatory burdens.<sup>20</sup> The Single Digital Gateway, introduced in 2018, has shown some success in reducing bureaucratic burdens by offering online administrative procedures in areas such as declaring corporate taxes or registering businesses across the Single Market.<sup>21</sup> But its scope so far is too limited, as it does not cover reporting requirements.

The new competitiveness check added to the Commission's Better Regulation Toolbox in March 2023 considers cost and price competitiveness, the international and SME dimension, as well as companies' capacity to innovate.<sup>22</sup> By bundling these important aspects together, which were considered in isolation before, it takes a more concentrated and holistic approach. This is clearly a welcome development, but the question is if it will be implemented and enforced adequately to be effective, given the mixed track record of the RSB to hold the Commission accountable<sup>23</sup> and the fact that there is no clear over-arching framework for the competitiveness check at the political level across all EU institutions.

The Commission has also updated its efforts to streamline existing legislation, announcing the "one-in-one-out" rule in 2021, which aims to offset additional compliance costs of new legislation through proportional cost reductions in the same or sometimes other policy fields. While the tool has some potential to

reduce overall regulatory costs, it has been criticised as an untransparent book-keeping exercise<sup>24</sup> which only puts the emphasis on quantity rather than quality of legislation with no distinction between necessary and unnecessary burdens and no comprehensive approach to the issue of competitiveness.<sup>25</sup> Furthermore, this approach solely aims at keeping regulatory burdens at the same level, not reducing it.

More promising seems to be the new Commission project to rationalise reporting requirements, with a view to reducing them by up to 25%, which was announced in 2022.

In this context, the Commission has begun with the reform of the Union Customs Code and proposed a revision of the Regulation on European Statistics which promise to hold significant burden reduction potential for businesses.<sup>26</sup> However, two weaknesses of this approach are that it only addresses reporting requirements and not administrative burdens and burdens to growth and innovation per se, which could have a much larger impact, and that it limits reductions to 25%, a random figure that might not fully reflect the extent of duplications, contradictions, and inconsistencies in EU regulation.

Overall, commentators have criticised a lack of clarity, transparency, focus, and coherence in the application of the Commission's better regulation tools. For one, the different DGs have at times lacked coordination.<sup>27</sup> Moreover, the Commission's better regulation agenda has suffered from a general proliferation of overall goals, with too many "north stars" resulting in a lack of clear direction.<sup>28</sup> In this respect, ESG objectives, recently updated with resilience goals might have overshadowed the need for a manageable regulatory burden for businesses in view of competitiveness.

Figure 2



## LACK OF PROPORTIONALITY IN LEGISLATION: EUROPE'S HIDDEN CHAMPIONS SUFFER MOST

Although the cumulative impact of EU regulation affects businesses of all sizes, it tends to fall disproportionately on SMEs and mid-caps. High compliance costs and regulatory uncertainty are particularly hurting smaller companies that produce at a limited scale. For example, a manufacturer of a 10-piece series will think twice before introducing new innovative processes that require lengthy and costly third-party certifications, whereas more established companies producing 500.000 pieces might see 6-digit-compliance costs and slow certification processes as less of a problem.

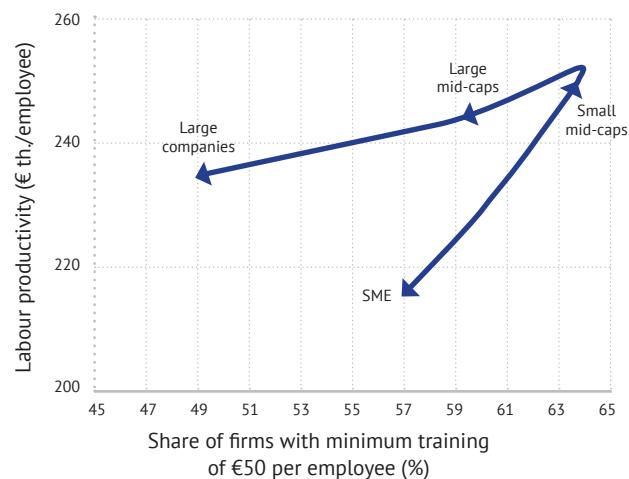
SMEs are exempt from some regulatory requirements as they are subject to a simplified reporting regime and have been granted derogations in many areas, such as competition rules, taxation and company law. However, this is often not the case for mid-caps, enterprises with at least 250 but less than 3000 employees,<sup>29</sup> which falls just beyond the SME threshold. Instead, mid-caps tend to be grouped with large companies, despite not having the same capacities in terms of regulatory compliance know-how, expertise, and resources.

This is particularly counterproductive considering that studies have evidenced that mid-caps are, in fact, Europe's "hidden economic champions" with a strong capacity for innovation, productivity enhancement and growth.<sup>30</sup> As highly internationalised and innovative companies they are more likely to invest than SMEs and large companies, and can, therefore also play a pivotal role in the EU's green, digital and economic security transitions.

Mid-caps are also more likely to report investment gaps than SMEs and large companies, pointing to further unexplored potential and lost spill-over effects into the

Figure 3

## MID-CAPS HAVE A HIGHER LEVEL OF LABOUR PRODUCTIVITY



Source: EPC/EIB.

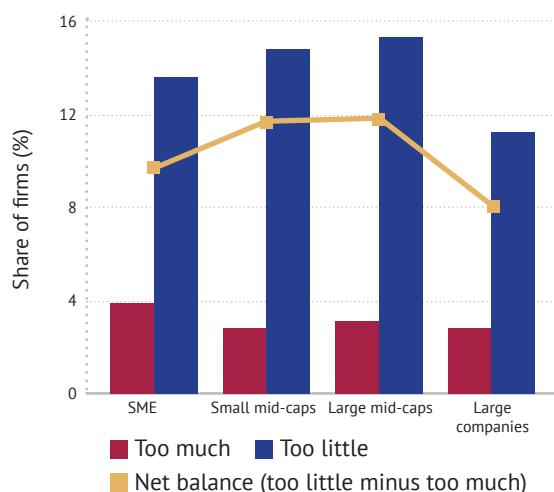
wider economy. Despite often having difficulty accessing finance, mid-caps receive less public support in the form of grants or bank finance on concessional terms than large firms and SMEs.<sup>31</sup> Innovation support is a further example of this. At present, EU and member state R&D programmes primarily target SMEs, while the largest companies are the ones that have the most resources to apply for support schemes.<sup>32</sup> As a consequence support will tend to favour small companies in local markets or major projects led by large companies, with insufficient support in between to meet the needs and potential of mid-sized companies.<sup>33</sup>

These issues also link up with Europe's scale-up problem or what could be described as Europe's 'Peter Pan syndrome', namely the unwillingness or incapacity of businesses to grow. Threshold effects linked to benefits and exemptions under the SME definition discourage SMEs to scale-up and grow into mid-caps,<sup>34</sup> and mid-caps are themselves held back on their growth path by a lack of recognition, regulatory burdens and an insufficiently supportive economic framework. The lack of deep capital markets in the EU play a key role here, but the constraining regulatory environment exacerbates this problem. Many innovative start-ups grow to become mid-caps but do not continue expanding to become large enough to turn into global leaders.

## Europe must deal with its 'Peter Pan syndrome', the unwillingness or incapacity of its businesses to scale and grow.

Figure 4

### MID-CAPS ARE MORE LIKELY TO REPORT INVESTMENT GAPS THAN SMEs AND XLs



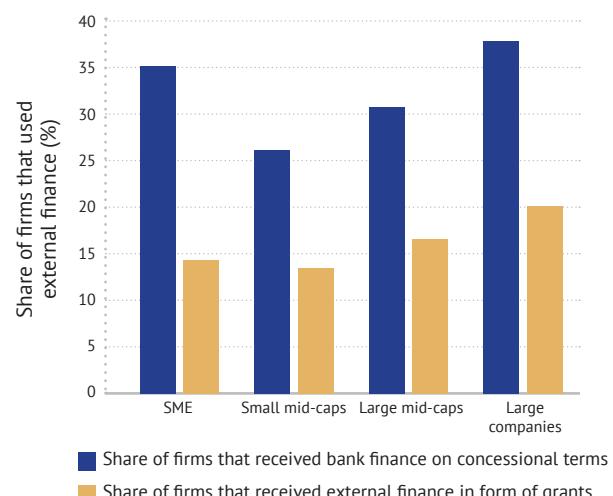
The Commission has recently dedicated more attention to mid-caps. Through the revised General Block Exemption Regulation<sup>35</sup> and the Guidance on Risk Finance,<sup>36</sup> it facilitates state aid for small mid-caps. Under the Accounting Directive 2013/34, the Commission recently increased the thresholds of the current SME definition by 25% to provide for higher SME turnover and balance sheet figures in the context of inflation.<sup>37</sup> However, without also raising the number of employees criterion this will not extend important SME benefits to mid-caps. In parallel, the Commission has promised to develop an EU-wide definition for 'small mid-caps' with 250 to 500 employees in the SME relief package.<sup>38</sup> While this is a step in the right direction, it does not address the need for more immediate action.

To create a new 'small mid-cap' definition the Commission rightly first wants to build a corresponding data set and then assess possible measures, such as extending to them certain SME benefits. After this process, legislation would still have to be identified and updated with the new mid-cap definition, which likely will take a lot of time. Moreover, the Commission's envisaged 'small mid-cap' definition would leave out what has also been identified by an EPC-EIB study as a critical segment of firms, namely between 500 and 3000 employees.<sup>39</sup> European competitiveness would benefit from a better regulatory treatment of these larger mid-caps, too.

Despite their more privileged position, SMEs are also set to be affected beyond their capacities by new legislation. The CSRD and CSDDD, for example, are not supposed to apply to SMEs, but it is likely that larger companies will end up transferring part of the responsibility down the supply chain, as is already the case with the German supply chain law.<sup>40</sup> This will have a significant impact on smaller firms that cannot easily switch to suppliers, which comply with the sustainability and social standards of the

Figure 5

### MID-CAPS ARE LESS LIKELY TO RECEIVE GRANTS OR BANK LOANS ON CONCESSIONAL TERMS



Source: EPC/EIB.

new legislation. The fact that SMEs were largely left out of impact assessments, given that the rules did not apply directly to them, likely played a role in underestimating the impact.

The application of the SME test to make sure that legislation is SME-friendly has been patchy across different services of the Commission.<sup>41</sup> The appointment of a new SME envoy to help screen EU initiatives and identify where the impact on SMEs requires special attention could herald a more coordinated approach.

Similarly, the SME relief package published last autumn, includes several very promising legislative proposals. The late payment regulation would introduce a single maximum payment term of 30 days for all commercial transactions across the EU, alleviating one of the greatest risks for bankruptcy for SMEs. The creation of a head office tax system would allow SMEs with operations across the EU to interact with the tax administration of only one member state which would imply a significant reduction in administrative burdens.

Moreover, the European Commission promises to systematically consider in the future specific SME-friendly provisions in new legislative proposals. These include for example longer transition periods for SMEs, SME-targeted guidance, consideration of the impact of delegated and implementing acts on SMEs, and review and sunset clauses in secondary legislation. The problem is that these benefits are not extended to mid-caps, which are exposed to similar problems to SMEs.

## DIMINISHING SINGLE MARKET DIVIDENDS: EUROPE'S BIGGEST ASSET ENDANGERED

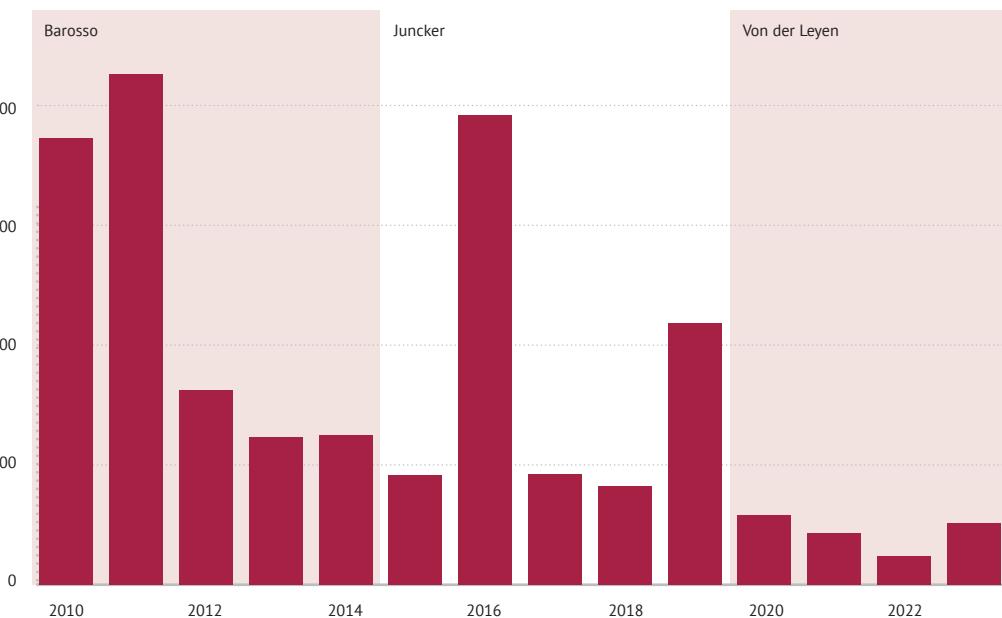
A functioning Single Market is the foundation of the EU's long-term competitiveness and indispensable for its transition goals and its economic security. Allowing for the free flow of goods, services, capital and people, it is not only a key driver for investment, competition and economies of scale. It is also an effective instrument to reduce regulatory burdens as it is meant to entail either the replacement of 27-member state laws with a single EU one or the mutual recognition of member state laws. However, the von der Leyen Commission's very ambitious legislative agenda has taken the spotlight off Europe's biggest asset, much to its detriment.

Indeed, the European Commission's actions against internal market infringements have decreased significantly over the past three years.<sup>42</sup> Moreover, infringement procedures take too long. The average time from reception of a complaint and the launch of an infringement procedure by the Commission is between 6 and 12 months, while the average duration of pending infringement cases against member states are around four years.<sup>43</sup> The procedures are also too bureaucratic and not transparent enough. Furthermore, SOLVIT as a tool for businesses to report breaches of Single Market rules is weakened by critical understaffing in the SOLVIT centres of a number of important member states like France and Italy.<sup>44</sup> All this compounds the risk of fragmentation.

Figure 6

### EUROPEAN COMMISSION INTERNAL MARKET ACTIONS HAVE DECREASED UNDER VON DER LEYEN'S WATCH

Total infringement actions taken by the commission in relation to the internal market excluding case closures



Source: Financial Times.

Indeed, the total number of barriers and shortcomings in the Single Market seems to be growing.<sup>45</sup> One reason for this is that new legislation is often not sufficiently harmonised across member states. The average transposition deficit of Single Market directives now exceeds the threshold set by the European Council in March 2007, with only five member states currently meeting the agreed target.<sup>46</sup>

This is compounded by inconsistencies between national and EU legislation, overlapping rules, and so-called national “gold plating”, whereby member states extend the power of directives when transposing them into national law, sometimes to complicate market access for businesses from other EU countries.<sup>47</sup> These national, regional, and even local administrative burdens also have to be taken into account when considering the overall bureaucratic weight.

This is also because of the uptake of the Better Regulation agenda among member states has been patchy and heterogeneous. Some countries, including the Netherlands, Denmark or Germany, have developed elaborate better regulation systems and launched initiatives to reduce regulatory burdens.<sup>48</sup> Together with other like-minded administrations, they have created an eight-member network called RegWatchEurope, which is oriented on exchanging good practices for reducing administrative burdens and regulatory budgeting.<sup>49</sup> However, in many member states, the Better Regulation agenda is still underdeveloped.<sup>50</sup> Altogether, there is too little effective collaboration among member states and between the Commission and member states to guarantee a regulatory level playing field.

This comes on top of a set of existing legislation where a genuine level playing field has never been created. member states still maintain different rules and standards for various service sectors, making it challenging for companies to operate across borders, particularly so for SMEs and mid-caps. In fact, trade integration in services stands only at 7.5%, compared to 26.3% for trade in goods, roughly the same as the level of EU trade in services with the rest of the world.<sup>51</sup>

For example, professions are still largely regulated differently across member states,<sup>52</sup> creating obstacles to labour mobility precisely when labour and skills shortages represent a major threat to European competitiveness. Another sector without a proper Single Market is telecoms. Protected by national networks and regulators, an excessive number of telecoms operators exists with little capacity to invest.<sup>53</sup> This has kept up prices, representing a competitive disadvantage for European businesses. On top of that, member states have largely acted on their own on spectrum frequencies, creating uncertainty and higher prices for European companies. With the recent connectivity package including the Gigabit Infrastructure Act, the Commission proposed a more coordinative approach such as the EU-wide reduction of administrative burden for network rollout, notably streamlining permit procedures and limiting administrative fees, which is a step in the right direction.<sup>54</sup>

Since the 1990s, there has been progress in energy and electricity market integration. The revised renewable energy directive caps permitting periods for green energy projects across the EU,<sup>55</sup> and the EU electricity market design reform of 2023<sup>56</sup> encouraged some simplification and harmonisation, but there is still ample leeway for member states to use national instruments and micro-manage the development of their power systems.<sup>57</sup> Moreover, the electricity infrastructure across member states still lack sufficient capacity and interconnectors for a more efficient use of renewables across the EU.

Closer energy market integration could significantly reduce energy and electricity prices and their volatility while increasing resilience. For example, annual benefits from fully integrating Europe’s electricity markets could reach €43 billion in 2030.<sup>58</sup> But many national interventions and proposals have been brought forward that distort Europe’s electricity market and risk moving it towards a more fragmented system.<sup>59</sup> This is stunting the competitiveness of Europe’s industry and slowing the transition to carbon neutrality.

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## Loosening of state-aid rules under the Temporary Crisis and Transition Framework represents an additional threat to the functioning of the Single Market.

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Financial markets are still predominantly national, with different national supervisors and insolvency, insurance, and tax laws, for example, making cross-border financing very burdensome. This precludes the development of deeper capital markets through a pooling of financial resources across the EU. Similarly, the European banking union still lacks a common deposit insurance scheme, impeding a further integration of an EU market for banking services. As a result, not enough money is channelled into the EU’s triple transition goals and European companies lack sufficient funding to scale and remain competitive compared to their American and Asian peers. As with other insufficiently integrated service markets, the onus to act on Capital Markets and Banking Union lies largely on some member states who have so far been unwilling to agree to more harmonisation.

Finally, an integrated and more efficient European defence market would not only be desirable in the face of mounting geo-political threats. Economies of scale and a harmonised regulatory framework could also increase the competitiveness of the European defence industry, which can work as an important multiplier for innovation in other industries.<sup>60</sup>

Lastly, the loosening of state-aid rules under the Temporary Crisis and Transition Framework represents an additional threat to the functioning of the Single

Market, carrying significant implications for businesses in countries with different fiscal capacities. Consider that around 80% of state aid was granted to Germany and France alone since the liberalisation of state aid rules in the wake of Russia's invasion of Ukraine.<sup>61</sup> Moreover, Germany plans to subsidise the electricity of its industry, while France announced a price cap for its electricity from nuclear.<sup>62</sup> This puts smaller member states at a competitive disadvantage and risks to trigger a subsidy race within the EU threatening the cohesive integrity of the internal market even more drastically.

In particular, the lack of a functioning Capital Markets Union or an expanded central fiscal capacity has hindered Europe's ability to move beyond state aid and present a convincing EU-wide response to foreign subsidy programmes, such as the American Inflation Reduction Act, without undermining the Single Market. This can entice European companies to move abroad to profit from more generous foreign subsidies to the detriment of the EU economy. For example, 2023 saw \$15.7bn, a record amount of capital investment from German companies into the US.<sup>63</sup> Important Projects of Common European Interest (IPCEIs) are, in principle, a great instrument for coordinating large industrial projects in strategic sectors across different member states. But a lack of central governance and transparency and purely national funding, has led to large member states and their champions profit disproportionately from such initiatives at the expense of the Single Market and European wide industrial policy.<sup>64</sup>

## **GLOBAL COMPETITIVENESS UNDER THREAT: THE END OF THE 'BRUSSELS EFFECT'?**

EU regulation does not only impact the competitiveness of European businesses within the Single Market but also abroad. Many European rules and standards have been taken up around the world in what has been dubbed the "Brussels Effect". This has eased trade with other countries and provided EU companies with a significant competitive advantage.

It is still unclear to what extent new legislation like the EU taxonomy on sustainable economic activities, the CBAM, the Deforestation Regulation or the CSDDD will be emulated internationally. If so, they could have significantly positive effects on the climate and help entrench the EU as a regulatory leader in shaping the global trajectory of sustainable and ethical business. However, there are worries that Europe could find itself disadvantaged by such legislation, as many companies and jurisdictions may be unwilling or unable to implement it.

This is because ESG rules and standards are much more difficult and costly to ensure than EU product standards such as for chemicals under the REACH regulation, which have widely been copied by foreign companies and states.<sup>65</sup> Widespread non-adoption could not only diminish the EU's regulatory clout but also legally precludes European companies' access to affordable

supply chains, making European goods and services less competitive on the world market.

So far, most EU ESG requirements such as sustainability reporting obligations are much more demanding than international ones, such as the International Financial Reporting Standards (IFRS). This lack of coherence might complicate trade with third countries, especially in light of the demanding supply chain standards of the CSDDD or the CBAM and create uncertainty or additional costs for European companies and investors.

Moreover, non-European companies, which have been driving the Brussels effect by adopting European standards and lobbying for their adoption by their governments, might find compliance with the CSDDD for example more costly than renouncing access to a European market which has been shrinking in relative size. On top of that, the monitoring of ESG standards is much more difficult than that of product standards such as for chemicals under the REACH regulation. This would likely lead to a much higher incidence of circumvention by non-European companies, leaving rule-abiding European firms at a disadvantage. The EU's Conflict Minerals Regulation which came in force in 2021 for example has not led to heightened due diligence on the part of foreign suppliers, demonstrating the limits of the Brussels effect with respect to ESG standards.<sup>66</sup>

At the same time, third countries have criticised the requirements and liabilities created by legislation such as the CBAM, CSDDD, and the EU deforestation regulation for disadvantaging their firms, while European demands for higher environmental standards on the EU-Mercosur Free Trade Agreement, for example, have led to accusations of neo-colonialism.<sup>67</sup> Altogether, countries in the Global South have become less willing to adopt Western positions, and EU influence in many important resource rich African, Latin American, and Asian countries is waning at the expense of others with less onerous demands for doing business.<sup>68</sup> This includes powers like China or Türkiye, which increasingly operate on a different value-base than the EU, or nations like South Korea and Japan, which take a less value-driven approach to trade.<sup>69</sup>

But even where there is a will to implement the EU's social and environmental standards, the lack of bureaucratic infrastructures and financial means make it difficult for foreign companies and countries to comply, particularly so in the Global South.<sup>70</sup>

Widespread disregard for European ESG regulation abroad would make European companies liable to switch to suppliers which abide by European standards. Those, however, are usually more expensive. Together with the high price of screening suppliers around the world on their adherence to social and environmental standards this could increase overall costs and make European products less competitive. In the case of critical raw materials, which are vital for the EU's triple transition, switching suppliers would be particularly costly or, in some cases where few countries dominate supply, impossible.

# Recommendations: Reforming the EU regulatory framework

## MAKE COMPETITIVENESS AN OVERARCHING GOAL FOR POLICYMAKING AND THE BETTER REGULATION AGENDA

To address the impact of cumulative regulation burdens, the EU must adopt competitiveness as an overarching goal for its policy and law-making activities, on par with environmental and social policy objectives.

Competitiveness checks should be performed not only on individual legislative initiatives but also on strategies and work programmes, including the mandate of the Commission taking office in 2024. Competitiveness should also be adopted as a top priority by successive Council presidencies through the troika or other cooperative mechanisms to provide more continuity in the Council. This will help to ensure that the cumulative and overlapping effects of existing legislation and new initiatives are taken into account.

A Commission Executive Vice-President for Economic Strategy and Competitiveness should be appointed to oversee the overall economic portfolio of the next Commission, supervising everything from competitiveness and trade to economic security and industrial policy. (S)he should be granted a strong mandate regarding the application of competitiveness checks on EU programmes and regulatory initiatives and engage in regular political dialogues with the Council, the European Parliament, and other stakeholders, including industry leaders and business associations. A competitiveness check should be consistently applied to all policy and law-making processes and across EU institutions. Particular focus should lie on the cumulative impact of legislation.

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**The RSB could be integrated into a permanent European supervisory authority for regulatory scrutiny, uniting ex-ante with ex-post regulatory scrutiny.**

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The Commission's quest to reduce reporting requirements by 25% should be extended to all administrative burdens by effectively applying a competitiveness test on the whole *acquis*. This exercise should also remove as much as possible barriers to innovation and growth, which are often less easily quantifiable. The process should be transparent and ensure that legislation with proven net benefits must be kept in place, especially when it is crucial for the triple transition. The appointment of a well-staffed taskforce of economists with key people

from the different DGs and external experts could help to accelerate this process and ensure a key role for competitiveness considerations. Important learnings could be drawn from the Stoiber group which worked between 2007 and 2012 to reduce overall administrative burdens by 25%, and whose recommendations were only partially implemented.<sup>71</sup>

To hold the Commission accountable and achieve a more systematic implementation and effectiveness of competitiveness checks and impact assessments in general, the Regulatory Scrutiny Board (RSB) should be strengthened. Its members should be increased, focusing on adding people with good competitiveness- and SME/mid-cap-specific expertise, and strong links to the academic and scientific community. It should also recruit a chair from outside the Commission, to ensure independence from the Commission's internal political dynamics. Further down the line, the RSB could be integrated together with the above-mentioned taskforce into a permanent European supervisory authority for regulatory scrutiny, uniting ex-ante with ex-post regulatory scrutiny.

To better ensure the effectiveness of the Commission's impact assessments, member state delegations in the Council and MEPs should consider them more in their own legislative activities. In turn, the Council and the European Parliament should establish their own competitiveness check processes backed with adequate resources and systematically apply them whenever they introduce substantive amendments. Given their increasing scope, both the Council and the Parliament should also dedicate more resources to scrutinise Commission delegated acts.

In particular the European Parliament, whose staffing numbers and overall budgets have ballooned in recent years, should play a more active, informed and evidence-based role in assessing impact of amendments in the co-decision process, with a clearer joint role for Committee secretariats and the European Parliamentary Research Service (EPRS) in this endeavour. The latter could further help to scrutinise and better explain Commission impact assessments and delegated acts and perform competitiveness checks on proposed amendments, while MEPs should be more encouraged to make use of these resources. Moreover, the Commission could provide supplementary impact assessments whenever its proposals are significantly amended.

To better reflect companies' needs, EU institutions and member states should include them timelier in the legislative process by publishing draft impact assessments for public comment early on. To ensure a more rigorous involvement of industry in the legislative process, regulatory sandboxes should be expanded

to relevant legislation where possible. This will also require member states to become more active in taking up Commission proposals to set up sandboxes and disseminate information on the national level.

Similarly, business associations and member states should work to increase firms' participation rate of the Commission's online public consultations, while the Commission should spend more resources on understanding, analysing and reacting to material feedback. It should also improve the outreach and accessibility of their calls of evidence, for example by extending periods for contribution. This is important because more data and inputs from stakeholders are essential for the effectiveness of the Better Regulation agenda.

Moreover, EU institutions and member states should make better use of digital tools, from impact assessments to automated reporting to the implementation of regulation, and the enrichment of the Union's foresight capability. For example, firms should be enabled to prepare and submit their reporting requirements digitally, allowing for the collection and pooling of company financial and sustainability data at the European Single Access Point (ESAP). Similarly, the Single Digital Gateway should be expanded rapidly to allow for more digitalised administrative procedures across the Union. To ensure progress, effective digital-readiness checks should be conducted consistently.

When it comes to the substance of regulation, lawmakers should focus more on providing the right incentives rather than micro-manage companies with granular prescriptions. In cases where a winning technology for solving a problem has not been materialised, legislation should be technology neutral. The Emissions Trading System (ETS) is a good example for this as it provides incentives to reduce emissions while not prescribing the way to get there. Moreover, more experimental regulatory practices, such as testing legislation in one sector before expanding it to others or learning from differential member state approaches could help in providing better regulation.

## MAKE PROPORTIONALITY A CORE CRITERION FOR LEGISLATION

Europe's regulatory burden should not fall disproportionately on SMEs and mid-caps. To ensure this, the EU must move beyond its current binary system, which only differentiates between SMEs and large companies, and improve the recognition of European mid-caps, tailoring their regulatory burden proportional to their size and administrative capacities.

In order to create a positive "competitiveness shock" for a critical segment of European businesses and trigger scaling dynamics, the Commission should extend the SME definition with all its benefits and exemptions to firms with up to 500 employees, hence relieving and boosting Europe's small mid-caps, which suffer particularly from disproportional regulatory burdens.

A change of threshold would automatically extend SME benefits, such as simplified reporting requirements and eligibility to SME targeted support programmes to what has hitherto been identified as small mid-caps and immediately relieve those companies which have arguably endured the heaviest regulatory burden in proportion to their size.

However, this alone will not be enough to better account for mid-caps in the EU regulatory framework. Additionally, the Commission should establish a new mid-cap definition that includes companies from 500 to 3000 employees, which studies show present distinct and unexploited potential. The establishment of this statistical and legal category should then serve to build a programme of legal simplification and support actions to boost these companies' role as Single Market growth and productivity champions and vectors of Europe's economic transitions.

For example mid-caps' administrative burden could be alleviated in particularly onerous legislation like the CSDDD and CSRD where application thresholds are currently set at 1000 and 500 employees respectively. Similarly public procurement rules and tendering processes for mid-caps should be examined and sought to facilitate and simplify. To generate more innovation financing, mid-caps falling under the new category could also be targeted for facilitated access to Horizon funding. In parallel, EIB and EIF schemes providing scale-up financing and R&D project support for innovative mid-caps should be further developed.

The European Commission should also reconsider its "Think Small First"-principle, and its implicit political preference towards small size economic actors, in favour of a clearly articulated economic policy in favour of growth and scaling that could be formulated as a "Think Growth and Scaling First"-principle. This does not mean that European legislators should not consider the needs of small companies, particularly at the early stages of policy development, yet the focus should be on pushing scale and growth paths not on validating existing situations.

In this regard, the Commission should consistently apply an SME and mid-cap test in impact assessments and aim to ensure that burdensome reporting responsibilities are not passed from large companies to smaller ones in legislation such as the CSDDD. To better account for the needs of SMEs and mid-caps in regulation, the EU institutions and member states should also make sure to include them in regulatory sandboxes wherever these could be directly or indirectly affected. Relevant business associations should provide the necessary resources and expertise to assist companies to do so.

## MAKE THE REINFORCEMENT OF THE SINGLE MARKET A TOP PRIORITY

The next Commission should devote more resources to effectively implementing and enforcing European legislation across all member states. Infringement

procedures must be quicker, less bureaucratic, and more transparent. This requires increasing staff resources, as well as adopting new digital tools and technologies in the Single Market Enforcement Taskforce (SMET) to strengthen surveillance. At the European Parliament, the Internal Market and Consumer Protection (IMCO) Committee should hold regular sessions that give citizens and business a chance to present problems with Single Market barriers, which could help to identify infringement cases and increase the pressure on the Commission to act.

Member states will need to do their part too. As suggested by the Commission, they should set up well-staffed national Single Market offices to address Single Market barriers and propose solutions within national decision-making systems.<sup>72</sup> These offices could function as direct point of contact between the Commission and member states on Single Market issues and help ensure that new rules are consistently and timely transposed and implemented across the EU and contribute to addressing remaining barriers for services. Moreover, member states should prioritise SOLVIT and ensure that their SOLVIT centres have sufficient staff with the appropriate profiles and qualifications to ensure that cases which are in conflict with EU law are handled timely and effectively.

Moreover, member states should synchronise with the Commission's Better Regulation agenda to reduce regulatory complexity at the national, regional, and local levels. The EU could support this process by encouraging greater collaboration between national lawmakers to exchange best practices on how to create leaner and simpler regulatory frameworks, as well as fostering dialogues with businesses to find the best ways to meet digitalisation and carbon reduction targets without sacrificing competitiveness.

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### **In domains where harmonisation is difficult to achieve, the EU should return to a more ambitious application of the single market's foundational principle of mutual recognition.**

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These efforts should be accompanied by a commitment on behalf of national leaders to facilitate a growth-enhancing regulatory environment with as few barriers and burdens as possible. This harmonised competitiveness drive should be encouraged across all member states and kept under a transparent framework. Wherever member states are not capable of performing market surveillance and guaranteeing compliance, the EU should provide technical and if necessary financial support.

In addition, the EU should launch a new drive towards deepening the Single Market for services. In the

energy sector, some measures could include further homogenisation of standards and processes aimed at reducing the regulatory burden for the green energy sector. Moreover, member states must cooperate more on improving the electricity grid with more capacity and cross-border interconnectors to move renewable energy more efficiently from supply to demand areas. To achieve progress, energy market integration should receive the high-level political attention it deserves given its potential to significantly increase European competitiveness.

Financial, professional, telecommunication and digital services as well as defence should be addressed with similar urgency. Ambitious Single Market action plans with clear milestones should be created for each of these strategic sectors. These should be driven forward by a new Commission Executive Vice President responsible for Economic Strategy and Competitiveness and put on the agenda at relevant Council and European Council meetings, to get the necessary high-level political backing required for decisive progress.

In domains where harmonisation is difficult to achieve, the EU should return to a more ambitious application of the Single Market's foundational principle of mutual recognition, which used to be the engine of Europe's Single Market integration. Article 3 of the e-Commerce Directive (2000/31) provides the template of a strong 'internal market clause' combining country of origin rule and mutual recognition. Of course, mutual recognition has also a long history of sensitivities, in particular in services. Therefore, rather than undoing legacy problems of the past, member states should agree to apply it to new strategic sectors where the benefits of Single Market depth and scale are urgently required.

Lastly, as state aid has proven to be a threat to the Single Market's level playing field, the Temporary Crisis and Transition Framework (TCTF) should be gradually phased out to return state aid to its original purpose of remedying market failures. Whenever they undermine the functioning of the Single Market, state aid tools should be avoided in favour of EU-level financing for strategic investments.<sup>73</sup> For example, introducing a Sovereignty Fund could serve this end well. Moreover, Important Projects of Common European Interest (IPCEIs) should be created in all suitable strategic sectors with access to them facilitated for all specialised companies, independently of the fiscal capacity of the member states where they are located. This could be achieved by moving the overall management as well as a substantial amount of the funding of IPCEIs to the EU level.

### **MAKE SIGNIFICANT EFFORTS TO MANAGE GLOBAL REPERCUSSIONS OF SUPPLY CHAIN REGULATION**

To prevent EU regulations such as the CSDD from limiting access to affordable supply chains and reducing international competitiveness of European businesses, the EU will need to better account for external impacts of its regulation and make significant efforts to convince

and help others to comply with new legislation and thereby promoting and protecting the Brussels effect.

The EU should pay consistent attention to international competitiveness in its competitiveness checks. If there is a threat of negative external effects on the competitiveness of European firms, the EU should flank implementation with diplomatic, trade and development policy efforts (see more below). At the same time, the EU should invest more to facilitate company-led setting of standards, as those can often better anticipate the likely international uptake of standards.

As suggested in its Strategy on Standardisation,<sup>74</sup> the Commission should coordinate more with international partners, such as the United States, Japan, and other G7 members, to try to gain support for its new standards. In addition, the EU would be wise to increase its efforts to align new corporate climate and social responsibility legislation with similar negotiation processes in international organisations such as the OECD, the United Nations, and international fora like the G20 and strive for the adoption of its standards by international standard setters.

Wherever countries are unable to adopt EU standards, the EU must be ready to offer benefits in return for the abidance by ESG standards, especially if this can be aligned with geo-economic interests. Such an approach is likely necessary in resource rich countries of the Global South, where compliance with EU standards is often too expensive and seen as an encroachment on sovereignty.

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**The EU should expand technical or financial assistance through the Global Gateway Initiative to help local companies to abide by green and social standards and assist administrations in introducing and enforcing them.**

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## Conclusion

Europe's policymakers find themselves in a conundrum. The climate crisis, the shift to new technologies and the emergence of a more fragmented and confrontational geo-economic order demands radical change. However, the legislation put in place to achieve the triple green, digital and economic security transition have created a regulatory burden that weighs heavily on the competitiveness of European businesses. Without the innovativeness of European companies, the EU will not only fail in its transitions but also lose its prosperity, which has been the bedrock of the European project.

For example, the EU should expand technical or financial assistance through the Global Gateway Initiative to help local companies to abide by green and social standards and assist administrations in introducing and enforcing them. It could also include innovation cooperation, assistance in building administrative capacity in developing countries and support for local civil society initiatives in favour of social rights and sustainability. Such efforts should also be supported by targeted development aid.

Altogether, the EU should take a more integrated approach linking trade, development and foreign policy with regulatory initiatives affecting foreign business and trade relationships. A good example is the Sustainable Cocoa Initiative which supports local cocoa projects in West Africa through the Global Gateway combining investments with a trade partnership and support to abide by higher labour and environmental standards, such as meeting requirements of the deforestation regulation.<sup>75</sup> Such partnerships should be further expanded to other fields, particularly critical minerals and other important inputs for European companies.

Similarly, better trade deals for resource rich countries could be linked to the promotion of European ESG standards. This would create a better bargaining position for the EU to demand the observance of European rules and standards. For example, to help them step out of the role of mere raw material suppliers and move up the value chain, the EU could allow resource-rich trade partners to sell raw materials at a lower price at home, which would facilitate the local processing and refining industries and could help foster economic development and the creation of own green industries.

To facilitate such integrated initiatives, there should be more coordination between different Commission services, for example between DG INTPA and DG TRADE, but also between EU and member state programmes and partnerships with third countries. The proposed Executive Vice-President for Economic Strategy and Competitiveness would provide a focal point for such a cooperative approach with the external action portfolios.

At the same time, the costs of the transitions are playing into the hands of Eurosceptic forces in the run-up to the European election.

Apart from the need to manage the social fallout of the triple transition, competitiveness should therefore be added as an overarching goal of EU policymaking, on a par with green, digital and resilience objectives. This certainly requires trade-offs. Regulation is always the result of political compromises, particularly in the multi-levelled political system of the EU. No better

regulation system will guarantee legislation that is always good for business, saves the environment and is socially just. But keeping in mind these limitations, this Discussion Paper has proposed several solutions for what we believe are the key dimensions for creating a more competitiveness enhancing regulatory framework while not losing sight of other objectives.

Given that the EU has passed most of its ambitious Green Deal and digital decade legislation, the next Commission would be wise to focus on consolidating

existing regulation and embrace a more careful approach in law making. This could help reduce uncertainty for businesses and provide precious breathing space to adapt to new legislation. Ultimately, this is also what can free up the public and private energies now needed to secure Europe's industrial future and achieve the triple green, digital and economic security transition in the face of unprecedented international competition. At this crossroads, Europe must do whatever it takes to reconquer its competitive edge.

<sup>1</sup> We would like to thank Blake Arnold for his valuable research assistance.

<sup>2</sup> European Round Table for Industry, “[Coalition of 25 European associations calls for 'more love for the Single Market'](#)” (Accessed 13 February 2024).

<sup>3</sup> “[The Antwerp Declaration for a European Industrial Deal](#)” (accessed April 2024).

<sup>4</sup> European Policy Centre, “[The Commission's balance sheet is positive, but the level of ambition is still too low](#)” (Accessed 11 January 2024).

<sup>5</sup> The report identifies nine drivers of competitiveness: (i) a functioning single market, including simplified regulation (ii) access to private capital, (iii) public investment and infrastructure, (iv) research and innovation, (v) energy, (vi) circularity, (vii) digitalisation, (viii) education and skills, and (ix) trade and open strategic autonomy (European Commission (2024), [The 2024 Annual Single Market and Competitiveness Report](#), Brussels, COM(2024)77).

<sup>6</sup> Eurostat “[Q2 2023: Business bankruptcies at highest level since 2015](#)” (Accessed 14 December 2023).

<sup>7</sup> Bartz, Tim; Hage, Simon; Hesse, Martin and Müller, Martin U., “[So lähmt die Bürokratie Deutschland](#)”, *Der Spiegel*, 8 January 2024.

<sup>8</sup> For example, the proposal for a Delegated Act on reporting standards under the Corporate Sustainability Reporting Directive. The draft published by EFRAG last November, in its current form, represents a gigantic sum of extremely granular legislation reporting obligations in the environmental, social and governance fields (Business Europe (2023), “[Reduction of reporting obligations - Letter from Fredrik Persson and Markus J. Beyer to Ursula von der Leyen](#)”, Brussels).

<sup>9</sup> Depending on the exact size of a mid-sized company, sustainability reporting can cost approx. 50,000 to 200,000 euros p.a. (VDMA, “[Member Survey 2017](#)” (Accessed 3 November 2023).

<sup>10</sup> ASML (2023), [Small Patterns. Big impact](#). Annual Report 2023, p. 24.

<sup>11</sup> Meyers, Zach (2024), “[Better Regulation in Europe: an action plan for the next Commission](#)”, Brussels: Centre for European Reform, pp. 6-7.

<sup>12</sup> Regulatory sandboxes are schemes that enable the testing of innovations in a controlled real-world environment, under a specific plan developed and monitored by a competent authority.

<sup>13</sup> Business Europe (2024), “[Impacts of regulations on competitiveness - Letter from Markus J. Beyer to Héctor José Gómez Hernández](#)”, Brussels.

<sup>14</sup> SME United, “[Proposal to ban forced labour products lacks clear priorities](#)” (Accessed 11 January 2024).

<sup>15</sup> Renda, Andrea (2022), “[Assessment of current initiatives of the European Commission on better regulation](#)”, Brussels: European Parliamentary Research Service.

<sup>16</sup> Meyers (2024), *op. cit.*, p.18.

<sup>17</sup> Bausch, Christoph, “[A mandatory competitiveness check for European legislation](#)”, Bundesverband der Deutschen Industrie (Accessed 3 November 2023).

<sup>18</sup> European Economic and Social Committee, “[A competitiveness check to build a stronger and more resilient EU economy](#)” (Accessed 3 November 2023).

<sup>19</sup> Meyers (2024), *op. cit.*, p.10.

<sup>20</sup> In an effort during the Portuguese Presidency in 2021, Member States adopted comprehensive conclusions on data technologies to improve Better Regulation, urging “the Commission and Member States to come together at EU level to consider how to promote the use of data technologies in support of data-driven, digital-by-default and high-quality legislation.” The Portuguese initiative, however, has not been followed up since (Council of the European Union (2021), [Council conclusions on data technologies to improve 'Better Regulation'](#), Brussels, 2021/C 241/04).

<sup>21</sup> Pelkmans, Jacques (2024), “[Empowering the Single Market: a 10-point plan to revive and deepen it](#)”, Brussels: Centre for European Policy Studies, pp.21-22.

<sup>22</sup> European Commission (2023a), “[Better Regulation' toolbox – July 2023 edition](#)”, Brussels.

<sup>23</sup> Meyers (2024), *op. cit.*, p.10.

<sup>24</sup> Van den Abeele, Éric (2021), “['One in, one out': an incongruous approach to the major European challenges](#)”, Brussels: European Trade Union Institute.

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<sup>26</sup> European Commission (2023b), [Commission work programme 2024: Delivering today and preparing for tomorrow](#), Brussels, COM(2023) 638.

<sup>27</sup> European Economic and Social Committee, “[Leaving no one behind when implementing the 2030 Sustainable Development Agenda \(own-initiative opinion\)](#)” (Accessed 11 January 2024).

<sup>28</sup> Renda (2022), *op. cit.*

<sup>29</sup> This is the definition of the EIB. Different member states use different definitions. This lack of a common EU wide definition makes research and policy on mid-caps on the European level particularly difficult.

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<sup>31</sup> *Ibid.*

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<sup>33</sup> KPMG Private Enterprise (2022), “[Bridging the mid-cap gap. A proposal to recognise, promote and support the growth of mid-caps companies in the European Union](#)”, p.25.

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<sup>36</sup> European Commission (2021), [Communication from the Commission – Guidelines on State aid to promote risk finance investments \(europa.eu\)](#), Brussels, (2021/C 508/01).

<sup>37</sup> Delegated Act (EU9 2023/2775).

<sup>38</sup> European Commission (2023d), [SME Relief Package](#), Brussels, COM/2023/535.

<sup>39</sup> Maurin, Delanote, Tran, Riekeles & Lausberg, Georg (2024), *op. cit.*

<sup>40</sup> Bartz, Hage, Hesse, and Müller (2024), *op. cit.*

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<sup>44</sup> [https://single-market-scoreboard.ec.europa.eu/enforcement-tools/solvit\\_en](https://single-market-scoreboard.ec.europa.eu/enforcement-tools/solvit_en).

<sup>45</sup> Pelkmans (2024), *op. cit.*, p.18.

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<sup>47</sup> European Commission (2024), *op. cit.*

<sup>48</sup> Bundesministerium für Wirtschaft und Klimaschutz, “[Drittes Bürokratieentlastungsgesetz \(BEG III\)](#)” (Accessed 3 November 2023).

<sup>49</sup> See RegWatchEurope, “[Together for a better regulatory oversight](#)”.

<sup>50</sup> Renda (2022), *op. cit.*

<sup>51</sup> European Commission (2024), *op. cit.*

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## NOTES

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