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The EU Digital Market Regulations: Rule-Maker or Deal-Breaker?

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Background

The digital transformation of the economy and society gives rise to a need for updated regulations and rules of the game for the digitised market. Within the EU, this need has been reflected in a number of legislative initiatives, most recently the Digital Markets Act (DMA), the Digital Services Act (DSA) and the Artificial Intelligence Act. This work affects not only the European market but also international trade relations that extend beyond the EU's borders. The EU is also part of the Joint Initiative (JI) on E-Commerce which was launched at the 11th WTO Ministerial in 2017 and aims at setting the global rules for digital markets.

At its 2021 Annual Conference in Sweden, the Jean Monet Network: Trade & Investment in Services (TIISA) in collaboration with The Ratio Institute and Swedish Entrepreneurship Forum organised a Policy Roundtable of experts from academia, politics, and business to discuss the relationship between the EU's legislative initiative for the internal market and developments in international trade governance, notably the JI on E-Commerce:

- Is it the EU's comparative advantage to be a leader in regulating these areas?
- How are the EU's relations with the outside world affected?

The starting point for the discussion is the question of whether the EU succeeds in taking on the role of an international "rule-maker" or whether the EU risks becoming a "deal-breaker". The conversation centered around two main topics: 1) Privacy and cross-border data flows, and 2) digital markets, services trade and competition. The discussion took place under Chatham House Rules.

Privacy and Cross-Border Data Flows

The EU is a rule-maker on privacy in the sense that its sheer market size is sufficient for major firms to comply with EU rules in the way they conduct business anywhere. In this sense, the General Data Protection Rules (GDPR) has advanced towards being a global privacy standard. On the other hand, the GDPR has proven to be difficult to interpret in a predictable way, making compliance harder and potentially creating a regulatory moat and raising barriers especially to small and medium-sized firms (SMEs) and startups, but also to less digitally savvy firms. One issue that was repeatedly raised was the definition and delineation of what constitutes personal data. Thus, what may be hailed as a success in setting a legislative standard, may also prove to have unintended or adverse effects in the market.

Privacy is considered a human right in the EU and is therefore not on the table in trade negotiations. Other countries have different approaches to privacy and both the OECD and APEC have developed privacy guidelines for their members that fall short of EU's adequacy requirements. This difference in approach is an obstacle for the EU to move forward on any trade deal that contains provisions on cross-border data flows, which most

modern trade agreements do. An example of such difficulties is the invalidation by the European Court of Justice of the adequacy decision under the EU-US privacy shield. Nevertheless, the recent trade agreement between the EU and the UK shows that compromises are possible.

Going forward, to what extent EU regulation becomes an obstacle to entering trade and data governance agreements depends largely on the definition of personal data. Currently, an estimated 10% of global data flows (after the fact) fall under the definition. Much data flow is non-personal and machine-to-machine in nature, for example, providing manufacturers with data on how their products are performing and whether or not they need maintenance. Should the EU introduce strict regulation also on non-personal data – or interpret the definition of private data (any information relating to an identified or identifiable natural person) more strictly, the EU could become isolated in the global effort to introduce global governance on data.

Global governance of data flows, including protection of privacy and security, may not lend itself easily or usefully to trade agreements. A data governance body along the lines of the Financial Stability Board (FSB) would be best suited for global data governance.¹

Digital Markets, Services Trade, and Competition

Services are often subject to market imperfections such as asymmetric information and dominant firms. Therefore, regulation is in many cases needed for markets to function. That being said, regulation must correct the market failures it aims for without hampering innovation.

Furthermore, services are by nature heterogeneous, and standards should be used sparingly such that services industries can grow and innovate and reach their potential to outgrow trade in goods. However, getting services regulation right is as important for manufacturing, where services are increasingly in focus in sourcing, production and domestic as well as foreign sales. Services account for almost two-thirds of world GDP and provide almost half of the value added in world exports.

In the EU, seen from the lens of creating a digital single market – let alone a digitised single market – regulation leaves a lot to be desired. The emphasis on the consumer and consumer rights is important and should feature prominently in the regulatory framework such as in the Digital Services Act (DSA) and the Digital Markets Act (DMA). However, consumer rights should not be allowed to inhibit the free movement of services.

¹ The FSB monitors and makes recommendations about the global financial systems and coordinates national regulatory bodies and international standard setting bodies. It works through its members, which commit to implement the recommendations, but are not legally bound at doing so. However, transparency, peer review and moral persuasion have proven effective in pursuing the FSB's goals.

Most regulations in the services area induce fixed costs of compliance. Such costs are disproportionately burdensome for SMEs. Regulation at the EU level often comes on top of national regulation that may differ significantly between countries. Such regulatory fragmentation may create insurmountable compliance costs for SMEs and there is a continued need for regulatory harmonization within the EU.

Moving to the multilateral stage, transparency in rules and their enforcement in the WTO would be a great help for SMEs to expand their business by exporting to new markets. The JI on Services Domestic Regulation will further strengthen transparency as well as cut red-tape and will save businesses a considerable amount of regulatory compliance costs each year.

The Digital Market Act (DMA) aims to support fair competition and contestability in the digital single market. On the one hand, digital platforms provide a means for increasing market reach for SMEs and facilitating the export of services, but on the other hand regulation needs to be adapted to the characteristics of these multi-sided platforms. The DMA aims to regulate large tech companies with the implicit assumption that this may enable European alternatives to these firms to grow competitive. There is a risk that the new legislation is geared too heavily towards paving the way for a European Google, but what the EU really needs is to promote new innovative businesses rather than substitutes to existing ones. At worst, the DMA may promote substitute competition at the cost of innovation. For example, the DMA restricts the interlinking of platform services and data from different services, which inhibits the potential for heterogeneous innovation in services as stated above.

There is also a friction between the DMA and the GDPR concerning the push to publish data openly in the former and the restrictions in the use of personal data in the latter. Because both regulatory frameworks are vague on the definition and demarcation of different categories of data, there is a considerable risk for conflict between them.

Concluding Remarks

The digital transformation of the economy has gathered pace over a long time, while regulation of data management for privacy and security purposes is fragmented and has not kept up with developments on the ground. Therefore, many businesses have developed their own rules to facilitate doing business in a data-driven global economy. One recent example is the use of so-called federated learning in devices such as smart-phones to preserve privacy while providing the benefits of merging data with modern prediction tools.

Policy makers around the world are currently scrambling to catch up, while pursuing different sets of objectives related to privacy, cyber security, competition, and innovation. Although interoperability is a stated objective in trade talks and collaboration among regulators in different international institutions, regulatory differences remain a major

concern while it is far from clear how interoperability could be operationalised. Furthermore, unilateral regulation by large players has extraterritorial implications. In short, regulation is no end in itself and neither should it be - what is needed are regulatory frameworks that are easy to adopt and comply with, and which translate easily across jurisdictions because at the end of the day national lawmakers will want to regulate their own businesses.

“The US innovates, China replicates, and the EU regulates” is a punchline in the policy debate. The panel agreed that Europe will not become a technology leader through regulation. What is needed are better policies for innovation, including promotion of venture capital and capital for scaling up production. Furthermore, much remains to be done for the EU to become a single market for services, particularly in the area of harmonising regulation and introducing common standards where relevant.

The EU constitutes a large market and is the largest services trader in the world. Its ambition for setting the global rules should not come from fear, and by implication take a defensive and protective approach. Instead, the EU should build on its strengths and collaborate with the US in the recently established Trade and Technology Council. The will to be a rule-maker that sets global standards for the regulation of platforms and tech companies must be balanced against the trade agreements and the promotion of trade and data flows in a globally interconnected economy.

On a final note, venues for discussion and the exchange of ideas, such as this Policy Roundtable, are vital to disentangle complex issues and bridge differences in understanding that otherwise risk hampering the legislative regulatory process. The gap between technology, business and regulation is best bridged through multi-stakeholder dialogues that shed light on both opportunities and risks.

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