

Governance through Mutual Recognition

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1. Introduction

Governance through mutual recognition is an alternative to governing via harmonization in the European Union. The introduction of mutual recognition dates back to the famous Cassis-de-Dijon case, in which the European Court of Justice decided that the freedom of goods requires Member states to mutually recognize each other's regulations, if these are equivalent. With this judgement, harmonization was no longer a precondition of building the internal market. Rather, mutual recognition is the rule and only where Member states invoke an exception to it, referring to mandatory requirements of the common good, is it necessary to agree on harmonized rules for building the internal market.

The 1992 programme of completing the internal market owed much to the invention of mutual recognition. While mutual recognition is well established for the trade of goods, it has played less of a role in trade in services. In fact, it has proven to be highly contentious in this field, as evidenced by the protest surrounding the original Bolkestein directive. However, in 1999, the European Council in Tampere decided to rely on mutual recognition for judicial cooperation. It is clear that governance through mutual recognition shows potential benefits while containing significant pitfalls. This policy brief inquires into the preconditions of this mode of governance by discussing firstly its characteristics, and secondly, analysing why it has proven to be so contentious for services.

2. The characteristics of governance through mutual recognition

Mutual recognition relies on the fact that there are several, functionally equivalent ways to achieve regulatory aims. Since it

would be difficult, time-consuming and costly to agree on a common solution, it is easier to simply mutually recognize these equivalent regulatory standards. This evades the costs of decision-making, gives customers greater product variety, and allows Member states to remain responsible for regulation. However, in implementation, mutual recognition is more complicated than harmonization. This is due to the fact that mutual recognition is never absolute. Member states retain the right to invoke mandatory requirements if regulation is not equivalent. For companies and authorities this means that there is in some cases uncer-

NEWGOV Policy Briefs

NEWGOV Policy Briefs are produced by the Integrated Project "New Modes of Governance – NEWGOV". The pan-European project examines the transformation of governance in and beyond Europe by mapping, evaluating and analysing new modes of governance. It is funded by the European Union under the Sixth Framework Programme from 2004 up to 2008. NEWGOV includes 24 projects and 3 transversal task forces and has more than 100 participating researchers from 35 institutions in Western and Eastern Europe.

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tainty as to whether Member states will accept or have to accept products from other Member states as being regulated in an equivalent way. In her seminal work on mutual recognition, Kalypso Nicolaidis (1993: 352) therefore speaks of a transfer of transaction costs from the stage of agreement of rules (as in harmonization) to the stage of implementing rules. Compared to harmonization, mutual recognition thus has costs and benefits which table 1 summarizes.

As mutual recognition implies that goods regulated and controlled by other Member states are being recognized on the same terms as domestic ones, it relies on a large degree of trust. Member states have to trust in the equivalence of other Member states' regulatory regimes and in the functioning of their authorities. Given that regulation, in general, has the goal of protecting the population from market or product failures, governments want to be assured that all good care is being taken given that they are being held politically responsible for whatever failures occur. The necessary depth of trust implies that mutual recognition is bound to work better under conditions of homogeneity than under conditions of heterogeneity.

3. Beyond goods: Transferring mutual recognition to other areas

The amount of trust necessary for mutual recognition to function implies that there must be important differences depending on the policy field: some policy issues are politically more sensitive than others! Thus, trade in goods is bound to be a relatively easy area for mutual recognition to function, as the setting up of rules is normally delegated to private actors and standardization com-

mittees. In justice and home affairs, in contrast, mutual recognition is being introduced for more contentious rules, even those which normally fall under parliamentary prerogative. Nevertheless, Member states have agreed to it which shows that even politically highly sensitive rules are not an absolute impediment to mutual recognition.

Why, then, was the Bolkestein directive so contentious? With the general principle of a home-country rule, the original services directive tried to build the services market on an extensive mutual recognition regime. This happened just at a time when heterogeneity in the Union increased significantly with the accession of ten new Member states. While trade in services follows a parallel rationale to trade in goods, i.e. profiting from differences in wages and specialization, trade in services exhibits a central characteristic that is crucial for the understanding of the difficulties faced by services liberalization: unlike goods, most services cannot be traded independently of their production. Rather, if services are being traded, either the provider or the consumer has to travel abroad. For home-country regulation and mutual recognition this implies that on the same territory the different rules of all Member states may become applicable, travelling along with the service providers. Moreover, home-country control means that authorities responsible for supervision are not active on the same territory. This creates considerable scope for illegal activities in the posting of workers for services provision. A common example is social security fraud where contributions are neither paid in the home nor the host Member state.

Given the significant wage differences present in the enlarged EU, the services direc-

Table 1: A comparison of harmonization and mutual recognition

	Harmonization	Mutual recognition
Benefits	Companies/ authorities know which rules are valid	Member states keep the regulatory competence. Product variety for customers
Costs	Agreement costs; competence is transferred to the supranational level	Rules from other MS become valid; incentive for regulatory competition; implementation costs

tive roused hitherto unknown protests. The compromise therefore deleted any references to home-country rule. Nevertheless, as Article 16 prohibits Member states requiring authorization, registration, identification, specific tools or materials from service providers, and prohibits them prescribing distinct contract relations if this hampers the

Further reading

This policy brief is based on research carried out within the NEWGOV project no. 13 on “The Domestic Impact of European Law”. The project analyses what happens when new Member states conflict with Community law in domestic economic policy-making. Moreover, conflicts may also emerge on a horizontal level, i.e. between old and new Member states, due to the impact of European Treaty law.

By dealing with a central feature of ‘old’ European governance – the constraints that European economic law poses for domestic policies and institutions – the project is concerned with an issue that is at the core of several important concerns: the division of competencies between the national and the European level (i.e. the issue of subsidiarity); the legitimacy of the European order; the potential of new modes of governance; and the functioning of the European legal order after accession of CEE countries. Ultimately, this project discusses the question how new modes of governance help to cope with the increased heterogeneity of Member states after enlargement.

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provision of services, mutual recognition enters through the back door. At the same time, the directive lets the host country rule labour relations, with the caveat that only binding minimum wages, but not collective agreements, can be imposed.

Some of the difficulties discussed in the context of the original services directive are

therefore likely to reappear. What solutions does the directive offer for mutual recognition to work with services? The most notable is the duty of cooperation among Member states’ administrations that is imposed in Art. 28-36. While in general home and host country are responsible for controlling their respective regulations, the fact that the home-country authority may not become active in the territory of the host state means that it can ask for administrative assistance from the host state. Likewise, when in doubt whether companies abide by their home country rules, the host state can demand information. Importantly, the directive requires national administrations to cooperate with the Commission intervening with infringement procedures in cases of non-compliance.

The administrative interaction is interesting in two respects. First of all, it is an important institutional support structure allowing mutual recognition to work better. In general, mutual recognition requires trust to function. The structure of the services trade even increases the necessary trust. Here, the home country has to control compliance with regulations, from which only the host country profits, where the service provider offers her/his services. This is different to the case of goods. Goods are produced and controlled, to be partly consumed domestically and partly traded. In the services trade, the home country controls those companies which are active abroad much more exclusively for this host country. The latter, correspondingly, has to trust the former much more as it has to behave not only egoistically but altruistically. Egoistically, poor Member states with high employment rates might have more of an interest in exporting services, than assuring that they comply with all regulations. The extent of fraud, and suspicion of fraud, in the services trade shows that trust is in particular demand here. By answering to this need for trust with binding requirements for administrative cooperation, the services directive secondly lays the basis for an increasing harmonization of administrative law. While mutual recognition lets Member states decide on the content of their rules, in implementing this heterogeneous regime there might therefore be more har-

monization. The normal community method, in contrast, is to agree on European rules but to let Member states decide on the form of their implementation.

The services directive thus tackles one difficulty of unifying services markets via mutual recognition. But the amount of trust necessary to overcome incentives for fraud is only one issue. The other one is the reverse discrimination of nationals that arises, with its challenge to the basic right of equality. As with goods, mutual recognition leads to the simultaneous presence of differently regulated products on a market. With services, however, differently regulated service providers work side-by-side. In as far as domestic providers are regulated more strictly than service providers from other Member states, they face the difficulty that on their own national territory they are being discriminated against by domestic rules. While the reverse discrimination of nationals also arises with goods, there is a difference between consumers picking among differently regulated products and service providers noticing by working alongside each other that they are being discriminated against by their own domestic rules. It is this reverse discrimination of nationals that makes mutual recognition so difficult to accept.

4. Conclusion

Governance through mutual recognition can achieve integration without resorting to common rules through harmonization. Mutual recognition offers several advantages. It may be the only option when harmonization

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is unfeasible. However, it has significant preconditions, most of all that Member states trust each other in maintaining and controlling equivalent regulations. The amount of trust needed makes mutual recognition more difficult among heterogeneous Member states. As the discussion of the services directive shows enforced administrative cooperation can compensate for a lack of trust. Equally challenging is the breach of the principle of equality which occurs if domestic providers are discriminated by their own national rules. Here, it seems necessary to emphasize an interpretation of the basic freedoms that honours not only the need of Member states to be loyal to the internal market via mutual recognition but also to the basic right to equality of their own population.