



# Legal fragmentation of digital services and the Digital Single Market

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# Internet regulation

- Should we regulate the Internet?
  - No consensus
  - National security; Protection of minors; Protection of human dignity; Economic security; Information security; Protection of privacy; Protection of reputation; Intellectual property
- Early regulation:
  - USA: Telecommunications Act (1996) [Communications Decency Act (Title V)]
  - EU:
    - E-Commerce Directive (**2000**)
    - Telecomm Package (2002), amended in 2009 and 2015

# Evolution of the Internet

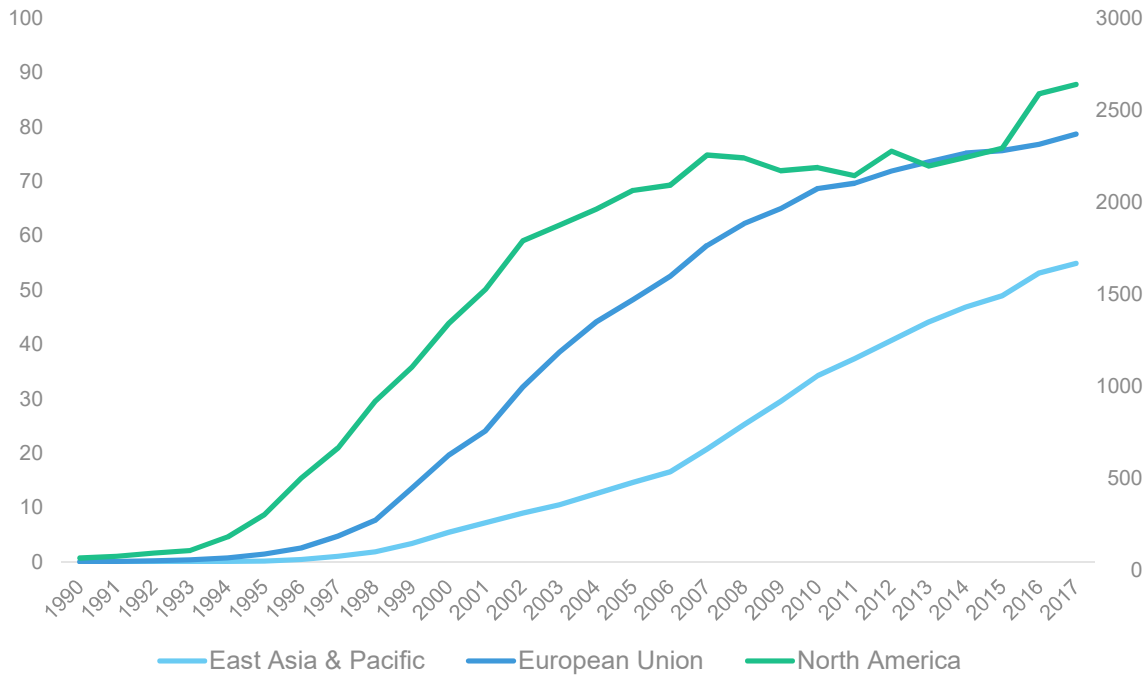
- 60's: ARPANET
- Early 70's: first international connections (UK, Sweden)
- Early 80's: worldwide expansion of ARPANET
- 1989: First commercial internet service providers (USA, Australia)
- 1990: First Web browser and first Web pages
- 1995: Internet is fully commercialised in the US and soon after in Europe

Global network of voluntarily interconnected autonomous networks.

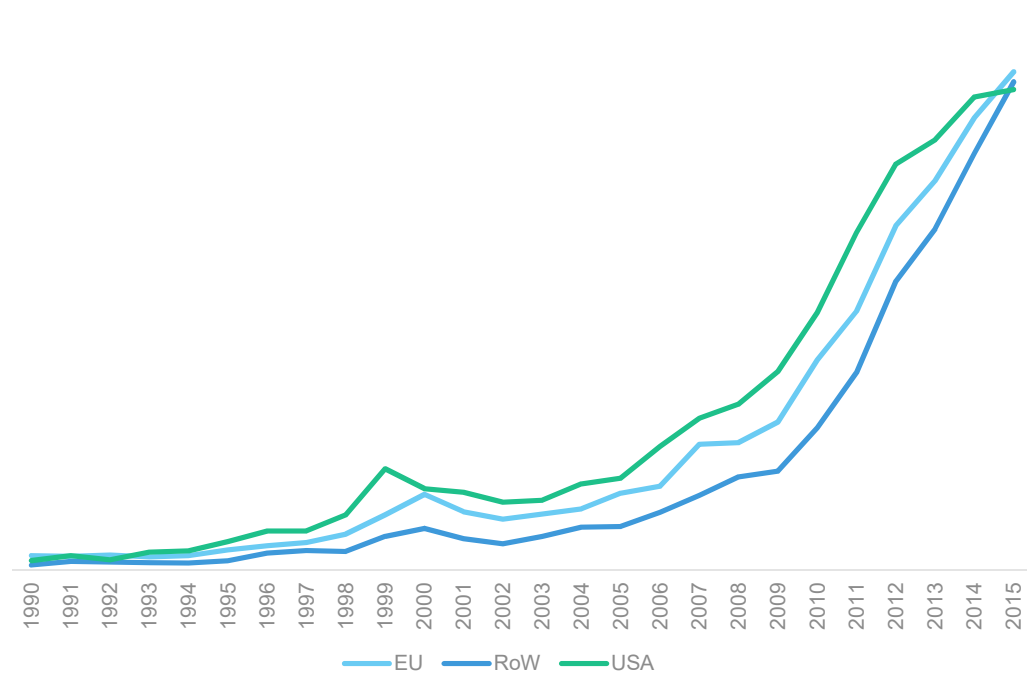
It operates without a central governing body.

# Evolution of Internet usage

Proportion of individuals



Number of platforms and hosting services



# Technology evolution

## **Web 1.0:** 1991 to 2004

- Consuming content in a passive manner
- Static websites, few content producers

## **Web 2.0 (Social web):** From 2004

- Websites emphasize user-generated content
- Interoperability (compatible with other products, systems, devices)

## **Web 3.0 (Semantic web):** From 2012

- Internet data machine-readable (automation)

# A patchwork approach...

Since ECD: Problem-specific approach

- **Regulatory initiatives:** Copyright, AVMSD, P2B, New Deal for Consumers, ePrivacy, Digital Services Tax, Terrorist Content Online
- **Non-binding initiatives:** Codes of Conduct (Hate Speech, Disinformation, Counterfeit, Better Internet for Kids, ...), Illegal Content Recommendation, Communications on Platforms, Illegal Content, Collaborative Economy, ...

## Digital services have evolved significantly since 2000

- E-Commerce Directive was not designed specifically for business models such as the new types of online platforms

# Problem definition

## Serious risks and harms brought by digital services

- Illegal activities online are on the increase
- Online platforms pose systemic societal risks
- Protection of fundamental rights is insufficient

## Ineffective supervision of digital services

- Underspecified and underused cooperation mechanism
- Lack of trust between Member States
- Authorities lack data and information to supervise appropriately

## Legal barriers for digital services in the single market

- Legal fragmentation across Member States
- Legal uncertainties in particular for online intermediaries
- Disproportionate and prohibitive impacts on start-ups and SMEs

## Problems amplified

- By large scale, reach and cross-border nature of services



# Objectives

Ensure the functioning of the **single market** for digital services

Ensure best conditions for innovative cross-border digital services to prosper

A safe online environment, with responsible and accountable behavior from digital services

Empower users and protect and enhance fundamental rights online, and freedom of expression in particular

Appropriate supervision of digital services and cooperation between authorities for cross-border issues

# But...what about the principle of subsidiarity?

## Article 5(3) of the TEU

*The general aim of the principle of subsidiarity is to guarantee a degree of independence for a lower authority in relation to a higher body or for a local authority in relation to central government. It therefore involves the sharing of powers between several levels of authority, a principle which forms the institutional basis for federal states.*

*When applied in the context of the EU, the principle of subsidiarity serves to regulate the exercise of the Union's non-exclusive powers. It rules out Union intervention when an issue can be dealt with effectively by Member States themselves at central, regional or local level. The Union is justified in exercising its powers only when Member States are unable to achieve the objectives of a proposed action satisfactorily and added value can be provided if the action is carried out at Union level.*

# (Digital Single) Market fragmentation

Legal disparity causes and aggravates market fragmentation

Other causes:

- Consumer preferences for local offers or domestic providers
- Language, or cultural proximity

These factors would reduce the cross-border trade and increase the fragmentation

Even in the provision of digital services where the physical distance should be highly irrelevant in the consumer choices.

On the side of providers, market fragmentation may be part of intended profit-maximizing strategies.

# Costs of legal fragmentation

The cost of determining the applicable legislation and diseconomies of scale

Understanding legal compliance costs

Unpredictability and legal uncertainty increase legal costs.

The cost of legal heterogeneity on liability rules

**The larger the difference between the solutions adopted at the MS level in relation to the ECD transposition, the larger the legal distance becomes, and therefore, stronger the disincentive to provide cross-border services.**

# Legal fragmentation indicator

Comparative legal analysis

- Map differences in national laws transposing and implementing the ECD

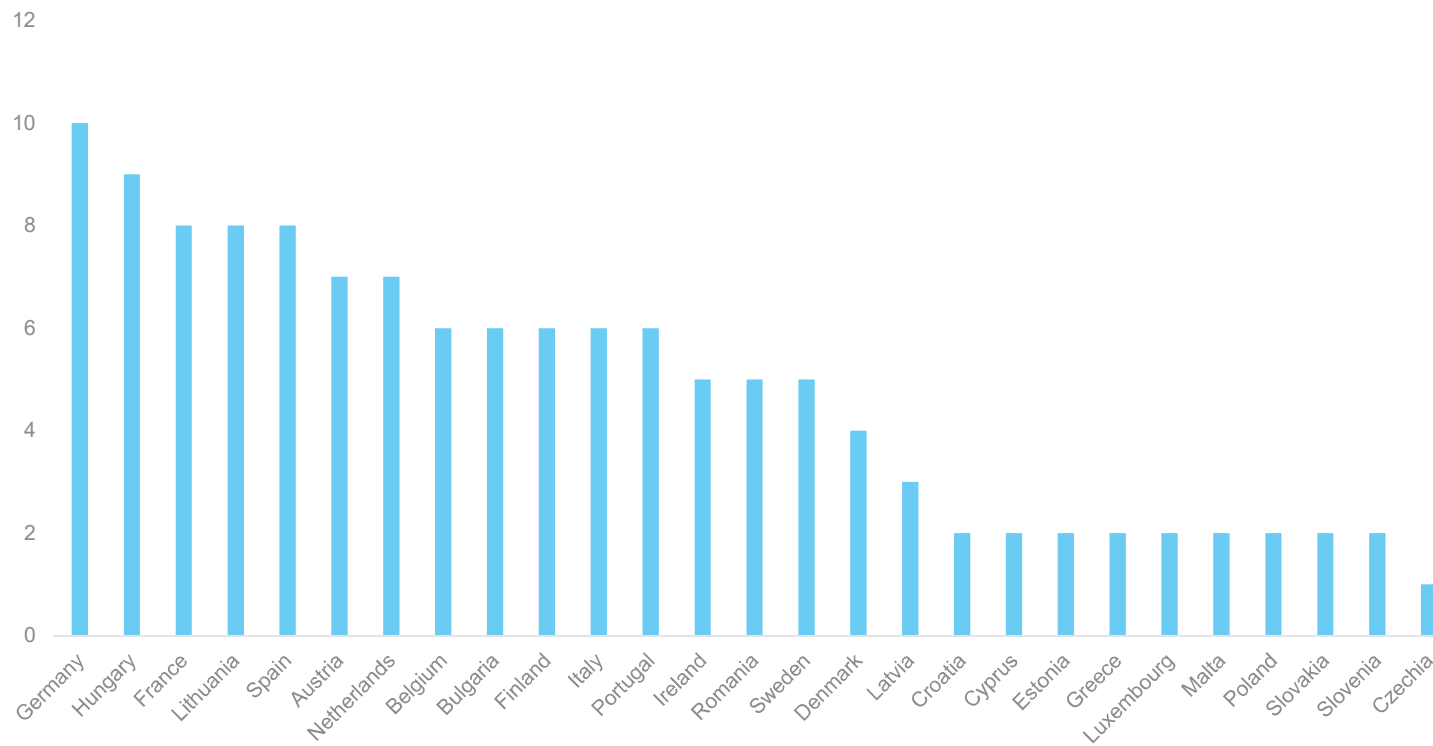
Composite indicator:

- Trace differences in national laws relating to the liability safe harbour
- Assessment of a level of a regulatory burden for a service provider
- Cost of a regulatory burden – (cost of compliance reflected in the cost of adaptation to the specific legal setup)

# Construction of the indicator

- Obtaining knowledge
- Existence of a specific and platform-managed N&A procedure
- Specification of information to be provided in a notice
- Timing of the removal
- Existence of the counter-notice procedure
- Abusive notice remedies
- Reporting obligation
- Internal appeal system

# Results



# Evidence?

Difficult: No official statistics on cross-border digital trade

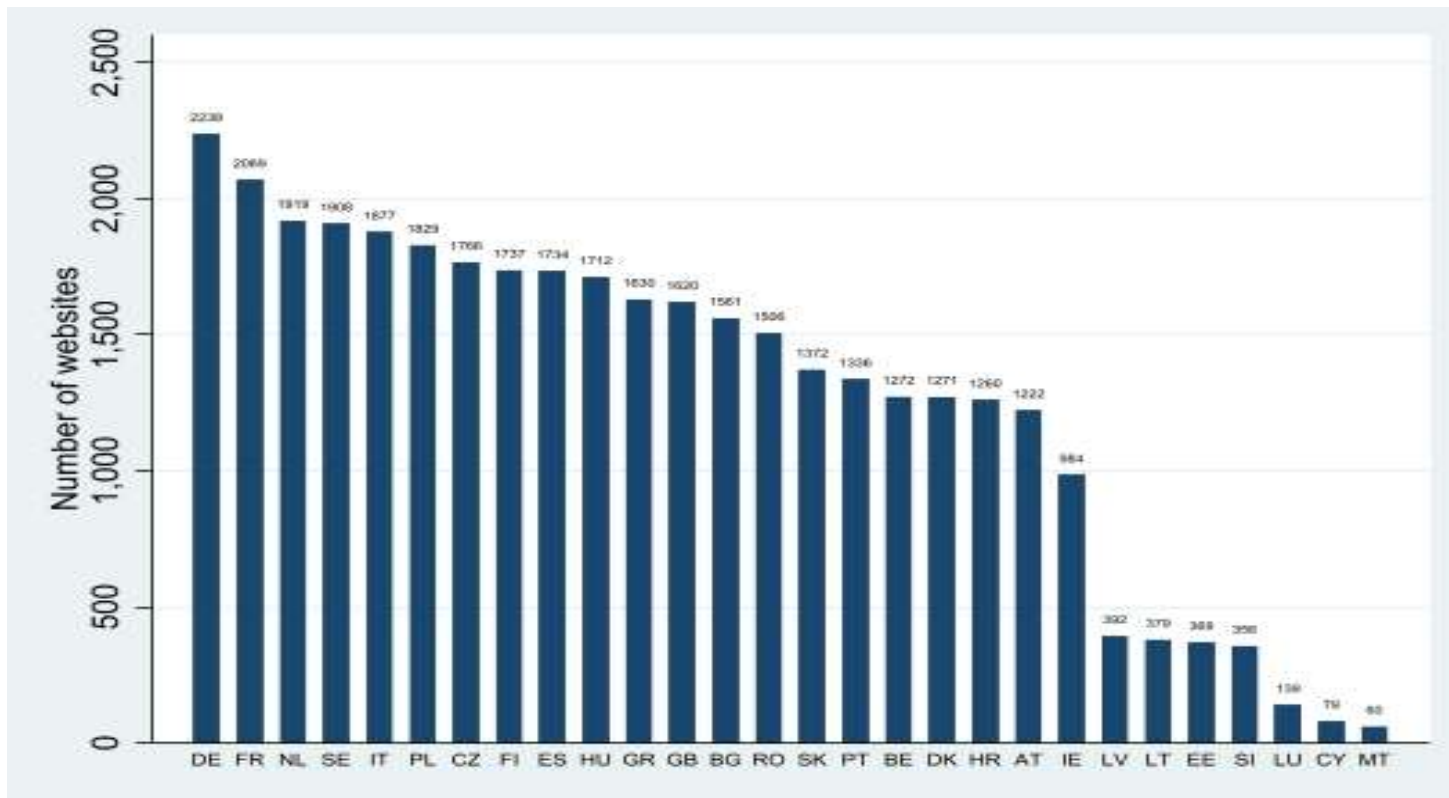
Solution: Internet traffic as a proxy for digital trade (UNCTAD)

Data:

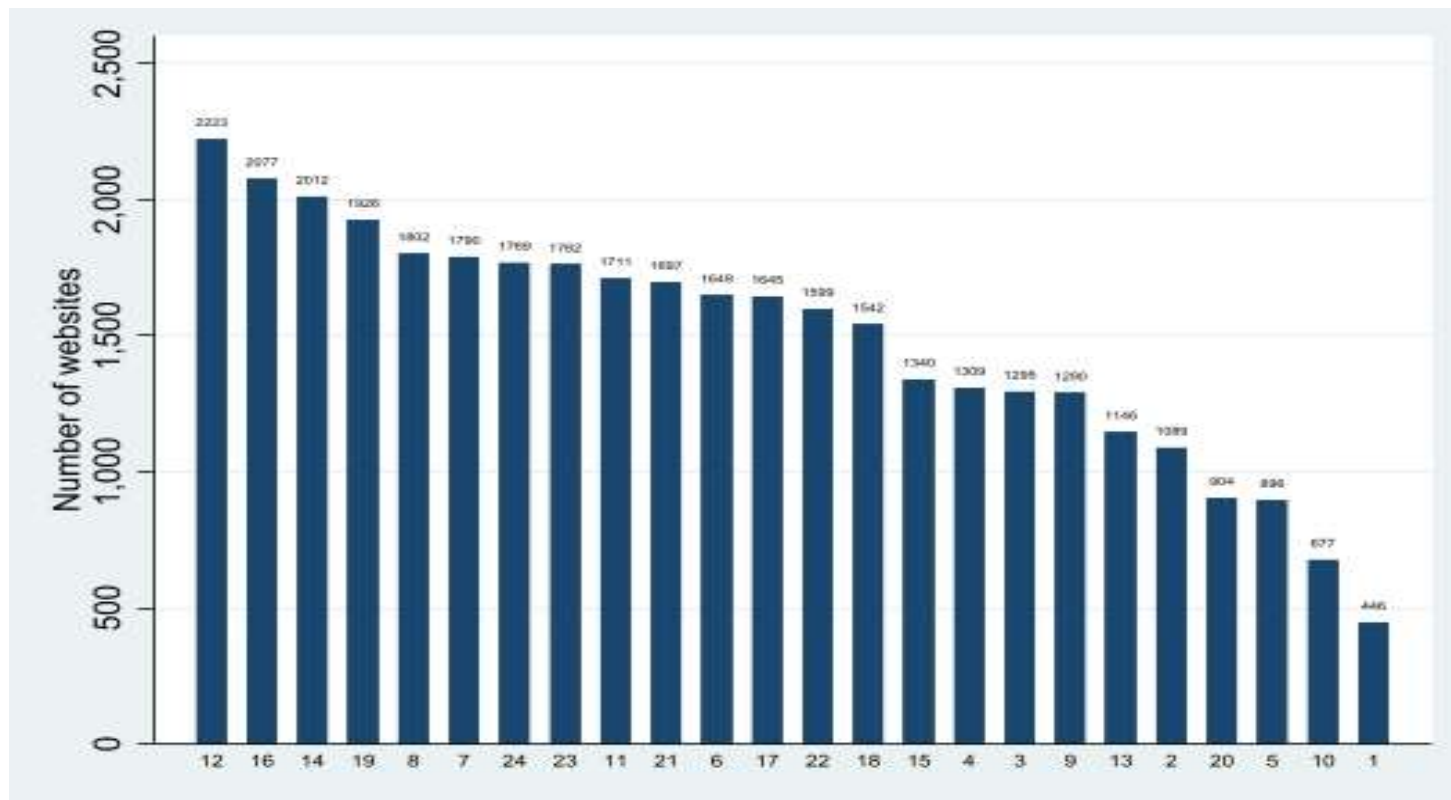
- 21 EU countries + UK (still EU MS during the period)
- 24 categories
- 3 years (2018-2020)
- Total: 35k websites offering diverse digital services



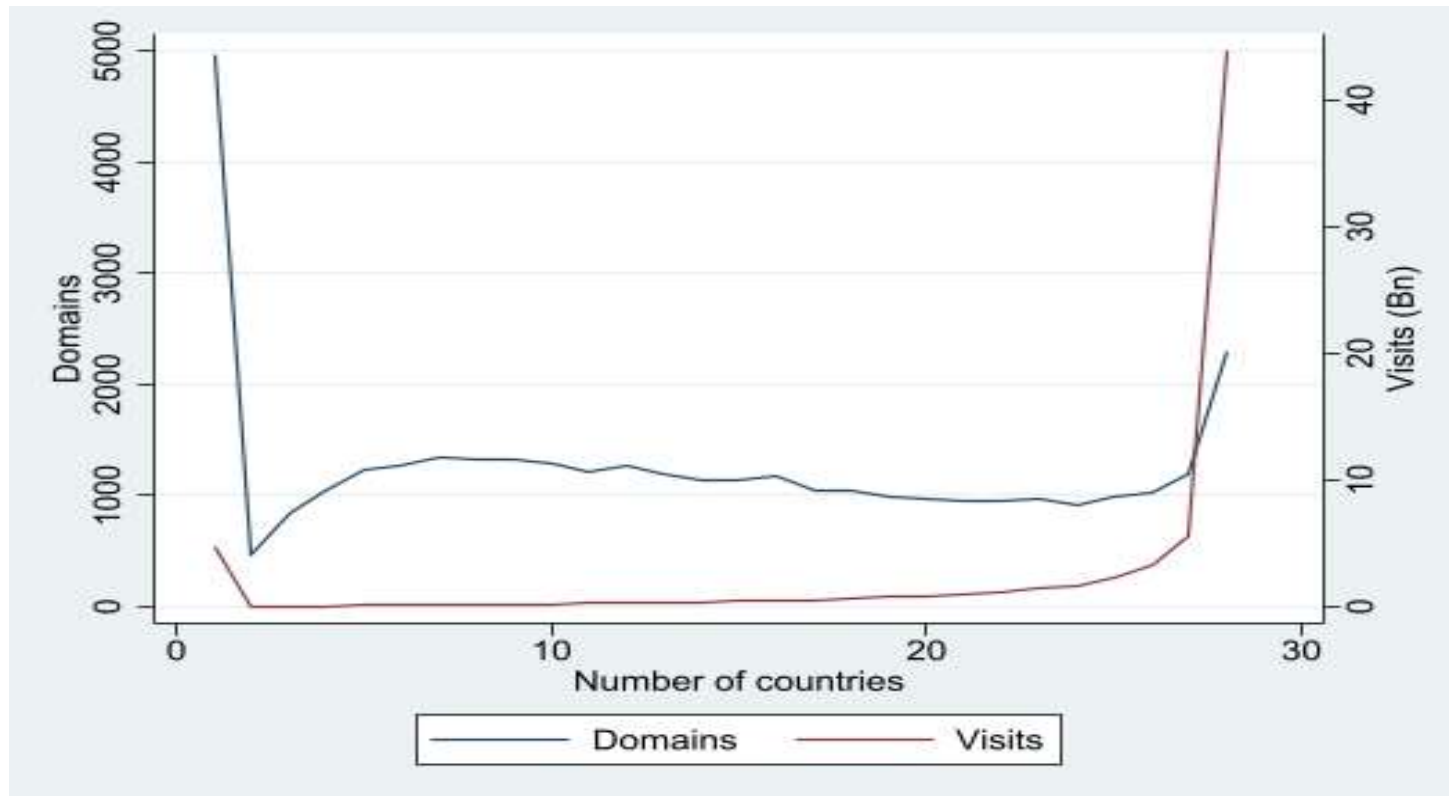
# Number of websites by country



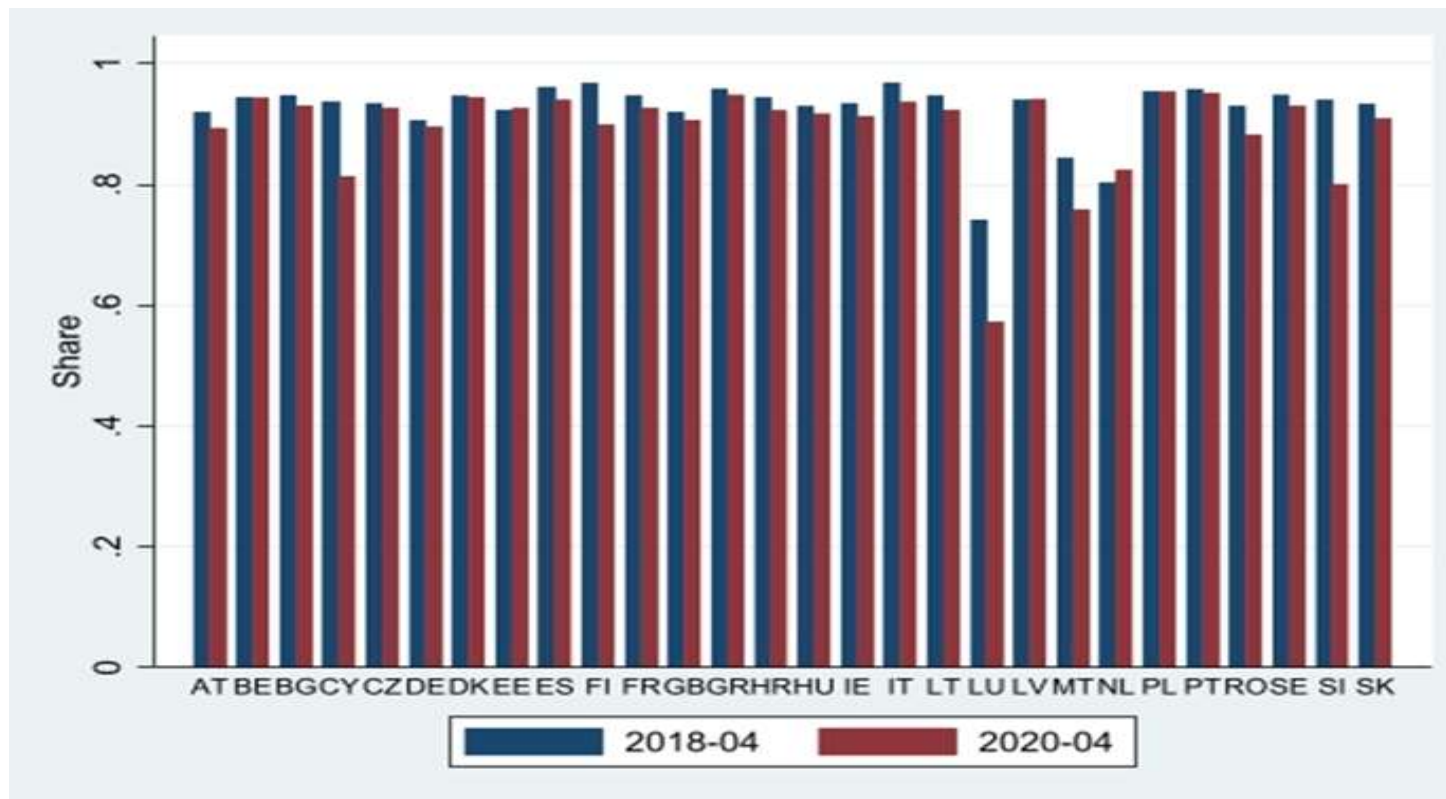
# Number of websites by category



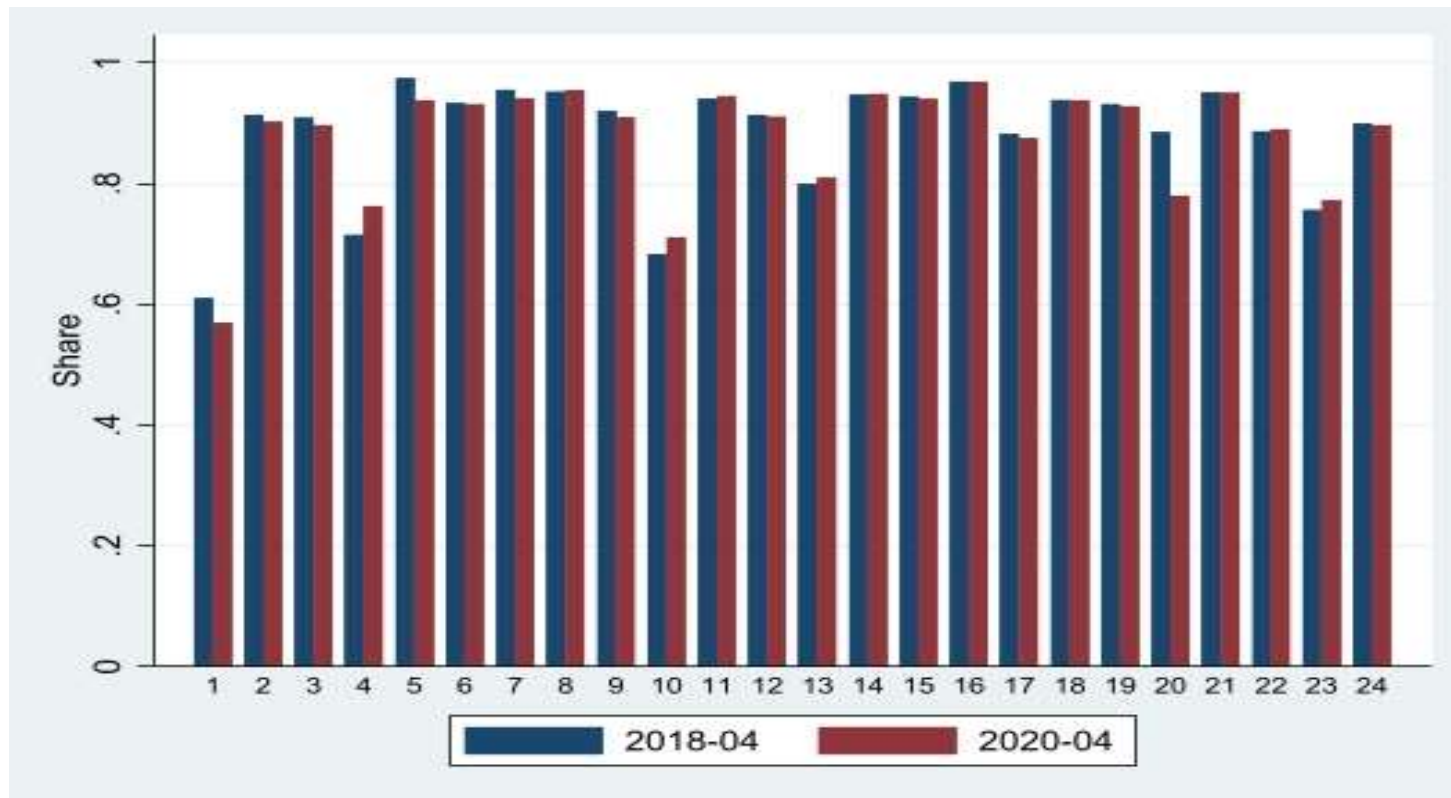
# Geographic distribution



# The “home market” effect



## The “home market” effect (II)



# Legal and market fragmentation

Gravity model (standard in economic analysis of trade)

Bilateral (digital) trade between two countries:

- Bilateral trade costs
  - Physical distance / contiguity / cultural / **LEGAL**
- Size (economic)
- Policy (trade, other?)

# Results

	Dependent variable: log of real visits			
	(1)	(2)	(3)	(4)
Physical distance (log)	-0.171*** (0.00210)		-0.159*** (0.00214)	-0.180*** (0.00209)
<b>Legal distance (log)</b>		<b>-0.0562*** (0.00126)</b>	<b>-0.0399*** (0.00130)</b>	<b>-0.0424*** (0.00125)</b>
Contiguity	0.118*** (0.00310)	0.272*** (0.00244)	0.128*** (0.00313)	0.137*** (0.00301)
Common language	0.281*** (0.00360)	0.262*** (0.00367)	0.266*** (0.00366)	0.287*** (0.00353)
Common currency	0.0424*** (0.00229)	0.0170*** (0.00231)	0.0317*** (0.00233)	0.0312*** (0.00229)
Home	0.928*** (0.00444)	1.172*** (0.00266)	0.895*** (0.00453)	0.914*** (0.00443)
Constant	2.099*** (0.0368)	0.989*** (0.0328)	1.949*** (0.0337)	2.239*** (0.0338)
Observations	1,516,830	1,516,830	1,516,830	1,516,830
R-squared	0.299	0.296	0.300	0.338

# Results extended

This relationship holds for:

- Different measures of bilateral trade
- Over time (the effect is increasing: 3,9% in 2018 – 4,8% in 2020)
- By category (all 24 have negative legal distance coefficients)

Interesting result:

- Holds for small digital services providers
- Does not hold for large DSPs (Top 10, Top 20, Top 30)



# Main takeaways

- Current Internet regulation was designed for Web 1.0
- Digital services have evolved significantly since 2004
- 2004-2020: Problem-specific approach (Regulatory initiatives + Non-binding initiatives)
- Digital Single Market is heavily fragmented
- Legal fragmentation is just one of the many digital trade costs
- Removing legal fragmentation of DSA can help the further integration of the DSM

# Thanks!

Questions/comments?

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