THE POWER SURPLUS

BRUSSELS CALLING, LEGAL EMPATHY AND THE TRADE-REGULATION NEXUS

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Abstract

The EU may not be a superpower but it holds a 'power surplus' when it comes to the trade-regulatory nexus. The strategic challenges posed by the deployment of this power surplus are the subject of this paper, which argues that in order to be a responsible regulatory power and positively influence the multilateral agenda, the EU needs to develop a coherent overall approach to the external dimension of its regulatory policies.

In this spirit, and in most cases, the EU would be ill advised to project itself as a model or to seek to 'weaponise' its regulatory powers in pursuit of unrelated foreign policy goals. Instead, it should wield this power to enhance the regulatory compatibility between its own and others' jurisdictions through cooperation rather than relying on the passive market-based influence of the so-called Brussels effect. This is simply a way to be faithful to its core defining philosophy of legal empathy.

The paper offers a typology of different forms of external EU regulatory impact, a discussion of the risks of either underuse or overuse of the regulatory power surplus, and considers the 'good global governance' model implied by a principled geopolitical role. It moves on to discuss a unifying conceptual framework to encompass this approach, under the umbrella of 'managed mutual recognition' as the operationalisation of legal empathy. It concludes with six specific suggestions as to how the EU can best exercise its regulatory power through a closer integration of trade and regulatory policies.

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"*If Europe wants to be heard, then it needs to set a good example.*"
Angela Merkel, interview to the European press, 26 June 2020

The EU "*shall work for a high degree of cooperation in all fields of international relations, in order to…promote an international system based on stronger multilateral cooperation and good global governance*." (Article 21(2) TEU)

1. Introduction

It is not an easy proposition for the EU to reconcile its use of trade and regulatory policy as its two main sources of influence on the global economy, while setting an example for multilateral cooperation in doing so. There is little question that the EU is a trade power with well-established policies anchored in a framework of rule-based governance.[1] Through the creation and development of the WTO and an extensive network of free trade agreements, it has played a decisive role in the development of global trade governance.[2] Nor is there any doubt about the impact of EU regulations abroad in fields ranging from competition policy to digital regulation, food and consumer safety and environmental protection. But how and to what extent the EU has exercised its regulatory influence in support of multilateral cooperation and global governance – in other words to help bring about, promote or implement multilateral agreements or standards, is a more open question.

We propose to tackle this question head on, at a time when many are asking in national capitals and in Brussels what the EU's strategic vision ought to be in a post-Trump, post-Brexit and (hopefully) post-Covid world. In order to do so, we propose two conceptual hooks.

On the one hand, the EU's holds what we call here a regulatory power surplus (e.g. a capacity to influence conduct beyond its jurisdiction) in the field of global regulatory politics, not only due to its sheer market size but also to its own experience in managing the trade-regulation nexus internally. If we accept this premise, and as with any wielding of power, the EU needs to deploy it with careful purpose and with an eye not only to *effective* external influence but also a *legitimate* claim to broker status when it comes to resetting multilateralism. In short, it needs to behave as a *responsible* regulatory power in how it uses its power surplus.

On the other hand, the EU does not come to this global regulatory game from a vacuum. Indeed, discussions on the external impacts of EU regulatory policies are not new.[3] Scholars

[1] S. Meunier and N. Kalypso (2006), "The European Union as a Conflicted Trade Power", *Journal of European Public Policy*, Vol. 13 No. 6: 906-925.

[2] I. Garcia Bercero (2020), "What Do We Need a World Trade Organization For? The Crisis of the Rule-Based Trading System and WTO Reform", Bertelsmann Stiftung, June.

[3] See, inter alia, J. Scott, "Extraterritoriality and territorial extension in EU law", *The American Journal of Comparative Law* 62.1 (2014): 87-126; K. Nicolaïdis and M. Egan, "Transnational market governance and regional policy externality: why recognize foreign standards?", *Journal of European Public Policy* 8.3 (2001): 454-473; E. Posner and N. Véron, "The EU and financial regulation: power without purpose?", *Journal of European Public Policy* 17, No. 3 (2010): 400-415; S. Lavenex, I. Krizic and O. Serrano, "EU and US regulatory power under strain?

have analysed these impacts under the broad categories of 'external governance' or "EU policy diffusion" (Borzel and Risse), "policy externality" (Egan and Nicolaidis), or more specifically, "functional extension" (Lavenex), "territorial extension" (Scott), "trading up" (Vogel), or the "Brussels effect" (Bradford). Scholars tend to argue on the basic distinction between the coercive, contractual and spontaneous adoption of EU regulatory templates and disagree analytically on the balance between them, and normatively on their relative desirability. The most benign view, dubbed the Brussels effect, is that the external impact of EU regulatory policies is essentially a consequence of 'market forces' that are independent of any proactive external policies by the EU institutions.[4] This dynamic might be passive but it is nevertheless a unilateral strategy.

But what we prefer to highlight is that the EU *already* possesses a regulatory template which is itself the result of inter-state cooperation – this is how it differs from other actors in the world. The EU already faces the task of having to compromise internally between different legal systems, including common and civil law but also the German, French, and Scandinavian legal traditions, etc. This provides EU law with a degree of completeness and reproducibility that other legal systems cannot match. Indeed, we refer to this EU template as one of 'legal empathy', or the idea that lawmakers and judges both lead and reflect a continuous dialogue between member states in which they have no choice but to engage with each other's different rules and legal systems, assess whether the differences between them are legitimate and adapt their behaviour accordingly.[5] So when the EU engages with the outside world the question is to what extent it should reproduce this philosophy of legal empathy when considering ways of using its regulatory power surplus.

In addressing these questions, we do not propose to review the extensive literature describing and analysing international regulatory cooperation (IRC), including the extensive work conducted by the OECD on regulatory policy and governance.[6] Our concern is essentially normative and prescriptive. While recognising the significance of the Brussels effect, we believe that the EU will only become a responsible regulatory power if it is ready to develop a coherent

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Emerging countries and the limits of external governance", *European Foreign Affairs Review* 22, No. 2/1 (2017): 1-18; S. Lavenex, "EU external governance in 'wider Europe'", *Journal of European public policy* 11, No. 4 (2004): 680-700; S.Lavenex, "The power of functionalist extension: how EU rules travel", *Journal of European Public Policy* 21, No. 6 (2014): 885-903; T. A. Börzel and T. Risse, "From Europeanisation to diffusion: introduction", *West European Politics* 35, No. 1 (2012): 1-19; F. Schimmelfennig (2012), "EU External Governance and Europeanization beyond the EU", in *The Oxford handbook of governance*; S. Lavenex and F. Schimmelfennig (eds) (2013), *EU external governance: Projecting EU rules beyond membership*, Routledge; R. Polanco Lazo and P. Sauvé, "The treatment of regulatory convergence in preferential trade agreements", *World Trade Review* 17, No. 4 (2018): 575-607; D. Vogel (2009), *Trading up: Consumer and environmental regulation in a global economy*, Harvard University Press.

[4] A. Bradford (2020), *The Brussels effect: How the European Union rules the world*, Oxford University Press, USA.

[5] See K. Nicolaidis, "Mutual Recognition: Promise and Denial, from Sapiens to Brexit", *Current Legal Problems* 70, No. 1 (2017): 227-266; K. Nicolaïdis (2016), "My Eutopia: Empathy in a Union of Others", in *Re-Thinking Europe: Thoughts on Europe: Past, Present and Future*, pp. 133-154. Amsterdam University Press.

[6] For a summary, see Organisation for Economic Co-operation and Development (2013), *International Regulatory Co-operation: Addressing Global Challenges*, OECD Publishing.

overall approach to the external dimension of its regulatory policies. As it seeks more systematically to extend its normative influence to the regulation of transborder concerns, developing a 'good global governance' approach to the external aspect of its regulatory policies through the territorial extension of legal empathy becomes increasingly necessary, both for reasons of legitimacy and effectiveness. To be sure, we will advocate a general philosophy while being mindful of the potential tension between the EU's external action objective (such as in the list of Art. 21(2) TEU) and the other aims, such as the protection and promotion of the EU's own values and interests – a tension to be managed on a case-by-case basis.

In this paper, we ask what the basic building blocks for such an approach might be and argue that 'leading by example' will require a greater degree of self-reflexiveness. In response to Kissinger's infamous quip about whom to call in Europe, it is actually for Brussels to do the calling in this realm, albeit backed up by the member states, of course. But if the call is to be answered, it needs a clear and principled message.

In this context, we argue that the power surplus generated by the external impact of EU regulatory policies ought to support EU values – particularly if anchored in the broader sustainable development goals which the EU champions. The shift in global governance from a growth-based (or Washington- consensus-based) paradigm to one based on sustainability over the past decade provides a conducive environment for such a philosophy as well as a push-back against those who argue that the EU will no longer be relevant in the "Chinese century." [7]

In deploying this power surplus, it must better manage a fundamental tension. On the one hand, the EU would be ill advised to simply project itself as a model or to seek to weaponise its regulatory powers in pursuit of unrelated foreign policy goals. It should instead wield its power surplus to enhance the regulatory compatibility between its own and others' jurisdictions through cooperation rather than passive imposition. On the other hand, the EU should not be naïve, in a world where various powers increasingly engage in lawfare, a term coined by the US military 20 years ago to refer to 'legal warfare' that includes measures from extraterritorial enforcement of sanctions to cyberwarfare.[8] Indeed, we will argue that better use of the EU's regulatory power surplus may in specific cases imply a hardening of such power.

The argument unfolds as follows. Section 1 offers a typology of different forms of external EU regulatory impact based on the territorial scope of the regulatory objectives pursued and the aims and instruments of regulatory cooperation policies – arguing that the latter tend to take place as a 'residual'.

Section 2 discusses the broader context in which these policies are embedded, starting with the notion of 'power surplus' and the risks of either underuse or overuse of this power. On this basis it moves on to the three possible 'models' that the EU could follow in its external regulatory policies – the external projection of the single market, the EU as a global regulatory

[7] P. Drahos (2021), *Survival governance: Energy and climate in the Chinese century*, Oxford University Press, USA.

[8] S. Blockmans (2020), "Why Europe should harden its soft power to lawfare", CEPS In Brief, CEPS, 15 June; S. Blockmans (2021), "Exraterritorial sanctions with a Chinese trademark: European responses to long-arm legal tactics," CEPS Policy Insight, CEPS, 26 January.

hegemon, and the EU as a promoter of good global governance. Although these models are inevitably combined, we argue in favour of emphasising the third model as the one that would better contribute to enhancing EU power on the multilateral arena and therefore its 'principled geopolitical role'.

Section 3 proposes a unifying conceptual framework to encompass this array of intervention by revisiting the concept of 'managed mutual recognition' as the operationalisation of 'legal empathy', as it has developed in the context of the EU single market. While noting that mutual recognition is deeply embedded in an ecosystem that requires supranational institutions, we argue that certain of its principles could be relevant with proper adaptations to regulatory cooperation policies pursued with countries outside the single market, and suggest a relevant typology. In this context we conclude with six specific suggestions as to how the EU can best exercise its regulatory power.

2. Cooperation as residual: the global impact of EU regulatory policies

If the EU has been rightly critical of the US's extra-territorial application of its legislation and cautious not to reproduce it, it may be because it knows better than to stand accused of reproducing patterns of action reminiscent of the imperial past of some of its member states.[9] Yet, as Scott argues, while the enactment of extraterritorial legislation by the EU is extremely rare, it does make frequent recourse to what she calls "territorial extension" in order to gain regulatory traction over activities that take place abroad.[10] Whereas extraterritoriality covers the efforts by a state to regulate the foreign conduct of persons not present within its territory, territorial extension "occurs when the application of a State's law rests upon a territorial 'trigger' in that it requires conduct or presence within the territory of the regulating State."

In other words, the application of an EU law or regulation abroad is usually triggered by something happening in the EU itself, but once it has been triggered in this way, the EU's regulatory determination (most frequently of market access) is influenced by or made conditional upon how foreign actors conduct themselves abroad, from production processes to more general characteristics of the foreign ecosystem. We may call this pattern *de facto* extraterritoriality since territorial jurisdiction is exercised with a view to and to the effect of incentivising or provoking third country behavioural or regulatory change. In this way, a wedge is created between sovereignty and regulatory jurisdiction.

EU circles and some scholars prefer to emphasise the voluntary nature of such extraterritorial reach, whether because it is the result of contractual relations or (even better if one wants to paint the EU as a benign regulatory hegemon) the result of spontaneous adoption of EU

[9] K. Nicolaidis, C. Vergerio, N. Fisher Onar and J. Viehoff, "From metropolis to microcosmos: The EU's new standards of civilization", *Millennium* 42, No. 3 (2014): 718-745.

[10] J. Scott (2013), "Territorial Sovereignty and Territorial Extension in an Interconnected World", in R. Rawlings, P. Leyland and A. Young (eds), *Sovereignty and the Law: Domestic, European and International Perspectives*, OUP Oxford, pp. 269-285.

regulatory templates, resulting in either *de jure* or *de facto* adoption of EU regulatory standards. In the latter case, global firms rely on EU rules for their activities both inside and outside the EU market. By labelling this pattern, the Brussels effect, Bradford emphasises the passive nature of the EU's regulatory reach through an 'effect' that happens mostly structurally as a function of the EU's market size, regulatory capacity and the non-divisibility of production. While this emphasis provides a solid analysis of and a welcome boost to Euro-optimism, it also risks being read as justifying some degree of complacency about the challenges being faced by the EU regulatory model.

Our ultimate concern here is with the nature of the 'regulatory cooperation' associated with different variants of EU regulatory power whereby such cooperation seems to occur as a residual corollary to the exercise of the latter.

Our starting point is to point out that the 'market led' external influence of EU regulatory policies may be affected by three developments that may limit the Brussels effect unless combined with proactive and principled regulatory cooperation policies. First, the emergence of China as a regulatory power for new technologies and its increasing economic presence in the EU neighbourhood. Second, the nature of the regulatory challenges relating to the digital and green transitions which make it more difficult for the EU to rely exclusively on the leverage provided by its market either for technological reasons or because of the need to avoid external challenges to the legitimacy of its action. Third, this emergence of new actors and regulatory challenges takes place at a time when the EU needs to reconsider its relations with neighbouring countries and explore ways of maintaining regulatory proximity other than incorporation into the single market.

In order to better understand the sources of EU external regulatory influence, we propose to distinguish three types of regulatory intervention, based on the territorial scope of the objectives pursued, and including for each the aims the EU is seeking to achieve through regulatory cooperation policies and the instruments used to achieve those goals (Table 1).

Table 1. Types of EU regulatory intervention and concomitant regulatory cooperation

Type of regulatory intervention	Aims of regulatory cooperation policies	External instruments of regulatory cooperation
1. *Exclusive domestic focus*	Market access and trade facilitation	Shaping international standards; FTAs; regulatory 'dialogues'
2. *Primary domestic focus/ partial conduct abroad*	Trade facilitation and regulatory efficiency through division of labour	Equivalency; Mutual Recognition Agreements
3. *Transborder focus*	Change in practices in third countries	Promoting international agreements

2.1 Type 1: Regulations with exclusive domestic focus (domestic regulations)

These are primarily regulations dealing with consumption externalities (health, safety, environment protection and so on) where the regulator's only concern is that a product or service placed in the market complies with domestic rules. How the product or service is regulated in third markets is of no regulatory concern provided the product conforms with EU rules when exported to the EU. Most of the rules relating to the single market for goods fall under this category. This does not mean, however, that the EU is indifferent to third country regulations. As an economy heavily dependent on exports, the EU has an interest in promoting compatible regulations in third countries, most often **through active participation in international standard setting bodies,** which then provide the basis for EU standards or regulations. Such standards can serve as defaults or voluntary standards, as common minimum standards, or as hard constraints on regulatory diversity.[11] Industrial standards in particular, which have played a critical role in the development of the single market are often based on ISO/IEC standards and EU regulations in the car sector are almost entirely based on UN/ECE regulations.[12] Codex standards are also frequently used in the agricultural sector, although in a number of areas the EU applies stricter standards. Through its support for international standards, the EU has therefore contributed to global governance in the regulatory field, which in turns serves as a vehicle to further EU regulatory goals.

Given the EU-friendliness of many international standards, it should come as no surprise that the EU has used its bilateral trade agreements to promote them. This is reflected in horizontal provisions of the chapters on Technical Barriers to Trade and Sanitary and Phytosanitary measures, but also in specific sectoral commitments. For instance, the free trade agreements with Korea and Japan include car sectoral annexes through which both sides accept to largely base their car regulations on UN/ECE Regulations. This commitment reflects pre-existing EU practice but implies a broader acceptance by Korea and Japan of UN/ECE Regulations, thereby facilitating EU exports. The conclusion of the free trade negotiations has also resulted in closer cooperation between the parties in the UN/ECE framework.[13]

In certain areas of regulation – such as chemicals or aspects of food safety – either there are no constraining international standards (albeit certain voluntary standards) or the EU is seeking domestically a level of protection that is higher than that applied internationally. While third country producers often complain when those regulations are initially introduced and thus become regulatory barriers to trade, the 'de facto Brussels effect' has in a number of instances

[11] See for instance R. Howse (2012), "Regulatory Measures," in M. Daunton, A. Narlikar and R. M. Stern (eds), *The Oxford Handbook on The World Trade Organization,* May.

[12] According to the May 2020 Global outreach report of CEN/CENELEC, 33.5% of the CEN catalogue of standards is based on ISO and 77% of CENELEC catalogue is based on IEC. When CEN or CENELEC standards are developed in response to a request by the European Commission, they provide a presumption of conformity with the relevant EU regulations.

[13] On the incorporation of UN ECE Regulations into EU law see presentation to the TBT Committee of 25 February 2020 in www.puntofocal.gov.ar With very few exceptions all EU car regulations transpose UN ECE regulations.

led multinational companies to adopt EU rules for their global operations, thereby limiting the external contestation of EU policies by other states. To be sure, the interpretation made by the WTO Appellate Body of the TBT and SPS agreement leaves considerable scope for members to pursue non-discriminatory product regulations based on a high level of protection. This implies that a WTO challenge to the type 1 regulations discussed here is unlikely to be successful.[14]

It is interesting to note that, outside 'neighbourhood countries', which pursue regulatory approximation because of their desire to associate more closely with the EU or even aspire to EU membership, the EU has not used trade agreements for the purpose of seeking adoption of those product regulations that are stricter than international standards. Compare for instance the provisions of the EU-Korea sectoral annex on cars with those of the sectoral annex on chemicals. While the first includes binding commitments based on UN/ECE Regulations, the latter only includes rather general cooperation provisions. The decision by Korea subsequently to adopt legislation closely modelled on REACH is better understood therefore as an instance of the Brussels effect rather than of FTA commitments. Indeed, the initiative to include a chemical annex in the FTA came from Korea and was only reluctantly agreed by the EU, which at that time was concerned about external criticisms of its chemical policies. Clearly, it was in Korea's interest to converge to EU standards for the sake of market access even if this meant adopting standards that were still contested.

To summarise, the main motivation for the EU to engage in international regulatory cooperation activities for type 1 regulations is to facilitate market access for EU exporters. The EU's preferred tool to achieve this objective has been a policy of active participation in the development of international standards, sometimes supported by the negotiation of free trade agreements. While EU regulators may also engage in dialogues to promote EU rules based on higher standards than those agreed internationally, this has not been consistently pursued as a policy or identified as a priority external objective. This is probably due to the fact that the focus of the stricter policies is essentially domestic and that the EU tends to be on the defensive when responding to third country criticisms of the impact of its strict regulations on access to its market.

Finally, EU trade and development cooperation policies have also played a role in responding to third country market access concerns and supporting regulatory convergence. The main instruments in this regard are the procedures under the WTO TBT and SPS committees that provide for early notification and discussions to seek to solve specific trade concerns. Outside WTO, there are also technical cooperation activities to facilitate compliance with EU norms by developing countries.

[14] For an excellent overview of AB jurisprudence on Art XX and on the TBT and SPS agreements see R. Howse, "The World Trade Organization 20 years on: Global Governance by judiciary", *The European Journal of International Law* 27(1)2016.

2.2 Type 2: Regulations with primary domestic focus, but including some aspects of conduct abroad (mixed regulations)

A significant number of EU regulations, while aimed at achieving domestic regulatory objectives, include provisions that regulate certain aspects of conduct abroad. As discussed above, the EU has been careful not to claim extraterritorial jurisdiction, but such rules nevertheless amount to what Joanna Scott has called the territorial extension of EU law: the EU regulator is required, as a matter of law, to take into account conduct or circumstances abroad, in granting access to the single market or authorising certain transactions with foreign subjects.

The regulation of conduct abroad is a feature of those product regulations where the safety or effectiveness of a product is linked to the conditions under which a product is manufactured. Most countries require that pharmaceutical products or medical devices be manufactured in facilities that comply with international standards of good manufacturing practices (GMPs). The import of many food products must originate in facilities that have been subject to proper inspections. These patterns are even more pronounced in trade in services where the safety and consumer characteristics of the service are intrinsically linked to regulation abroad, be it how doctors are trained or how banks are supervised.

While as with type 1 regulations, the primary aim of regulatory cooperation remains to facilitate **market access**, for type 2 regulations, the corollary aim is to achieve **regulatory efficiencies** through a division of labour with foreign regulators who are entrusted to take action to verify compliance with EU standards. The greater the differential between the cost of oversight in the EU vs the home country of the exporter, the greater the incentive for various degrees of subcontracting and re-allocation of responsibility. It is important to note that regulatory cost savings go together with a **significant reduction of compliance costs** for the regulated subjects which can rely upon supervision by their home regulator and avoid duplication of inspections or more burdensome procedures to accede the EU market. It is much easier for the regulators in the country of origin to verify compliance with EU rules. The key is to determine that their standards and procedures are 'equivalent' or 'adequate' when compared with those of the EU.

As we move to fields like data privacy, the link between the aim of protecting EU citizens and the extension of EU rules abroad becomes more explicitly supplemented by a broader ambition, that of promoting EU values in the hope that as foreign entities seek to comply for the sake of market access, they will effectively comply for all their users, not only Europeans.

The most frequently used instrument for the EU to address conduct outside its territory is an autonomous determination that the legislation of the third country is **equivalent** to that of the EU. In the absence of such a determination, individual transactions may still be possible but at greater cost. There are of course variations as to what is meant by 'equivalence' and the procedure to be followed depending on the provisions of individual pieces of legislation. In some cases, the main concern of the EU may relate to **effectiveness**, e.g. the **same standards of protection** or supervision by third country authorities. In other cases, the bar is lowered to requiring that the standards or supervision applied are **comparable** to those of the EU.

The EU has developed an extensive practice of territorial extension as regards financial services regulations. There are around 40 equivalence provisions in different EU rules in the financial services sector and the Commission has so far adopted almost 300 equivalence decisions for more than 30 countries.[15]

The EU GDPR includes a form of equivalence provision through the procedure to establish that the legislation of a third country provides adequate protection of personal data privacy. To date the EU has reached 12 adequacy decisions for third countries, as well as a *sui generis* arrangement with the US 'privacy shield', which was however invalidated by the ECJ in July 2020.[16] Many more countries have adopted legislation that is modelled on the GDPR, in order not to fall foul of the EU's market access conditions, in what constitutes possibly the best illustration of the *de jure* Brussels effect.[17] Nevertheless, cooperation with non-EU authorities for the enforcement of GDPR has not been an easy task.

It is important to note that an equivalence determination by the Commission may be subject to judicial review by the ECJ and that the Commission therefore needs to be mindful that its decision complies with EU law requirements. The Schrems II landmark decision invalidating the GDPR adequacy regime for the US of July 2020 is a case in point.[18]

Ultimately, the GDPR speaks to the tendency to build 'law as code'. In this case, compliance is in effect obtained 'by design." But this also means that increasingly, it is more difficult for outsiders to ensure and demonstrate their 'compatibility' with EU rules. While this may be unavoidable when regulatory policies involve fundamental rights, a possible consequence is a loss of capacity to influence regulatory developments abroad.

Crucially, the EU need not stop at purely unilateral determination of equivalency. Its assessment of conduct abroad is often made easier if there are appropriate cooperative arrangements, formal or informal, with regulators in the third country that is home to the conduct being regulated. This is where regulatory cooperation enters the picture. The prerequisite for subcontracting inspection, supervision and enforcement of course entails a modicum of trust between the EU and the home country. The question is: how is this trust generated?

For one, in the case of unilateral adequacy determination, even in the absence of a formal agreement, equivalence decisions are often preceded by substantial discussions with the third country concerned. These can be quite intensive and, in some instances, result in changes of third country practices or even legislation. Most interesting for our purposes: the discussions

[15] See https://ec.europa.eu/info/publications/190729-equivalence-decisions_en.

[16] See https://curia.europa.eu/jcms/upload/docs/application/pdf/2020-07/cp200091en.pdf.

[17] Competition policy is another domain where such territorial extension takes place. This paper does not discuss the role of cooperation between competition authorities, although several of the principles considered here could also be relevant in that context.

[18] July 16, 2020 Schrems II. See C-3111/18. https://curia.europa.eu/jcms/upload/docs/application/pdf/2020-07/cp200091en.pdf.

sometimes include an element of **mutuality or reciprocity** where the EU too adjusts its modus operandi.[19] This suggests that the main reason why the EU prefers autonomous decision-making is to maintain **greater flexibility as to the ex post management of equivalence** and to avoid the complexities of formal conclusion of international agreements. This point goes to the heart of whether EU action ought to be unilateral or mutual.

Nevertheless, formal agreements may sometimes be preferable, from the third country or the EU viewpoint. International trade agreements have played a role in regulating certain aspects of conduct abroad in a manner that facilitates trade in goods. This is particularly the case for issues relating to the certification of compliance with product regulations. But while the EU has concluded a **number of mutual recognition agreements on conformity assessment**, starting with the six MRAs signed with the US in 1997, these have been notoriously hard to implement due to differences in the approach to conformity assessment and excessively burdensome procedures. This is to some extent not surprising: the very fact that these agreements pertain to certification or supervision rather than the underlying standards on which such oversight is based implies that foreign inspectors on both sides need to be familiar with each other's underlying regulatory standards.

MRAs related to good manufacturing practices in the pharmaceutical sector have been more successful since they rely on internationally aligned standards and cooperation in international bodies. Such agreements have been concluded with Australia, Canada, Israel, Japan, New Zealand, Switzerland and the United States.[20] The free trade agreement with Canada includes, for the first time, a simplified procedure to accept certification of conformity assessment by bodies established in the other party. In the case of self-standing veterinary agreements or the SPS chapters of trade agreements, there are procedures for equivalence based on those included in the WTO, although their use has been relatively limited.[21]

EU trade policy has played a much more limited role in support of the EU's external objectives for regulations in the services sector. The financial services chapter in EU trade agreements does not go significantly beyond reaffirming the WTO prudential carve-out under GATS. In the context of the TTIP negotiations, the EU made proposals to include a chapter on regulatory cooperation in financial services, but these were strongly opposed by the US Treasury Department. Instead, the EU and the US agreed on a number of improvements in their bilateral dialogue on regulatory issues.

[19] Consider for instance discussions with Japan on data privacy, as further noted below. Discussions on financial services regulation with the US often cover both equivalence under EU rules and the similar concept of 'substitute compliance' under US law.

[20] On medicines, for instance, see https://www.ema.europa.eu/en/human-regulatory/research-development/compliance/good-manufacturing-practice/mutual-recognition-agreements-mra.

[21] For a description of the functioning of the CETA Protocol on Conformity Assessment see European-accreditation org, November 2017; for an example of a well-functioning veterinary agreement see the veterinary agreement with New Zealand concluded on 17 December 1996, Council Decision 97/132/EC.

The EU has also taken the view that **trade agreements are not an appropriate forum to consider regulatory issues relating to data privacy.** When third countries have raised the issue of facilitating data flows in trade negotiations, the EU has proposed to open up separate discussions on the conditions for an adequacy decision. Hence, in the case of Japan, both sides reached decisions as to the adequacy of their respective privacy regimes at around the time of the conclusion of the free trade negotiations which came into force on 1 February 2019. India first raised the issue of adequacy in the context of free trade negotiations, but the EU insisted that such discussions be held separately and indeed discussions have continued despite the suspension of trade negotiations. An adequacy decision relating to the UK was reached shortly after the conclusion of the new Trade and Cooperation agreement.

Regulatory cooperation for type 2 regulations is therefore primarily informal and linked to equivalence determinations, although mutual recognition agreements have played a role as regards conformity assessment with product regulations. International standards provide the basis for EU regulation of the pharmaceutical sector, food safety and financial services, although in a number of instances the EU has adopted regulations that are stricter than international norms. As discussed with type 1 regulations, the EU and its member states are active participants in relevant international regulatory fora where standards are being developed. As regards digital, the EU has played the leading role in privacy regulation, but so far there is no cooperation forum that brings together like-minded regulators, despite the fact that the GDPR has provided the inspiration for privacy regulation in a large number of countries.

2.3 Type 3: Regulations that respond to transboundary concerns

In a limited number of regulatory domains, the EU's primary objective is more purely 'extraterritorial' – as it seeks to contribute to tackling **global externalities.** A territorial connection is maintained insofar as imports of the products affected contribute towards the transboundary concerns that the regulations seek to address. EU rules seek to address global externalities or at least to ensure that the EU market does not contribute to such negative externalities. Ideally, EU action aspires to be combined with actions by others or inspire others to take comparable action.

In this context, the EU can in certain instances rely on its own standards while delegating the monitoring to other bodies. Alternatively, it can subcontract 'labelling' or certification entirely to other parties, including transnational private regulatory certification bodies promoting good practices such as Global GAP (good agricultural practices), GRI (Global reporting initiative), the UN Global Compact and the like.

The most pressing global challenge is of course climate change. Until recently the EU has focused primarily on the regulation of emissions within its territory. Climate-related action affecting external trade has included due diligence legislation relating to preventing imports of illegally harvested timber, which implies that importers must ensure supply chain transparency

and exercise due diligence through approved monitoring mechanisms (which are waived if an agreement has been conducted with the exporting country to ban such trade).[22]

The EU also adopted legislation that provided for the inclusion in its own emissions trading scheme of emissions relating to the portion of flights outside EU territory.[23] These provisions were subject to strong external contestation and were never applied. Instead, an international agreement was concluded in 2016 under International Civil Aviation Organisation (ICAO) regulating aviation emissions through an offsetting scheme.[24] The scheme may be a first, but does not address the problem directly, according to its critics. The EU has adopted a similar approach to shipping under the aegis of the International Maritime Organisation (IMO). In both shipping and aviation, the EU has sought to use an approach dubbed by Joanne Scott as "contingent unilateralism", by signalling that it will revisit its domestic regulation if multilateral agreement is achieved.[25] The EU has also introduced biofuel sustainability standards, which are currently subject to WTO dispute settlement procedures launched by Indonesia. This dispute is likely to raise most of the legal questions relating to the interpretation of WTO rules in relation to measures aiming to mitigate climate change and combat deforestation.

More recently, the Commission has announced a number of initiatives that would more directly regulate external conduct with an impact on climate change or other global sustainability challenges. The Commission has launched an impact assessment on the introduction of a border carbon adjustment mechanism (BCAM)to address the problem of so-called carbon leakage, e.g. the undermining of domestic reductions of emissions as domestic production is replaced by imports not subject to similar constraints.[26] The justification and design of such a BCAM has been amply discussed and a legislative proposal is expected in the first half of 2021.[27] As part of the Green Deal, other legislative proposals that deal with production methods abroad can be expected, including new legislation on deforestation, horizontal legislation on mandatory due diligence or product-specific regulations in the fields of agriculture or certain industrial products.

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[22] Regulation (EU) No 995/2010 of the European Parliament and of the Council of 20 October 2010 laying down the obligations of operators who place timber and timber products on the market Text with EEA relevance.

[23] Directive 2008/101/EC of the European Parliament and of the Council of 19 November 2008 amending Directive 2003/87/EC so as to include aviation activities in the scheme for greenhouse gas emission allowance trading within the Community (Text with EEA relevance)

[24] See https://www.icao.int/environmental-protection/CORSIA/Pages/default.aspx.

[25] J. Scott and L. Rajamani (2012), "Contingent Unilateralism: International Aviation in the European Emissions Trading Scheme", in B. Van Vooren, S. Blockmans and J. Wouters (eds) (2013), *The EU's Role in Global Governance The Legal Dimension*, Oxford Scholarship Online.

[26] See https://ec.europa.eu/clima/sites/clima/files/eu-climate-action/docs/impact_en.pdf and specifically see consultation on the carbon border adjustment mechanism https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/12228-Carbon-Border-Adjustment-Mechanism.

[27] For a discussion, see for instance https://www.bruegel.org/wp-content/uploads/2020/03/PC-05-2020-050320v2.pdfComment.

But of course, these various domains of external regulatory intervention remain controversial, with fears of a slippery slope towards protectionism or the unilateral imposition of European standards. The strong negative reaction to the EU proposal in 2021 (under the Carbon Offsetting and Reduction Scheme for International Aviation (CORSIA) to include emissions outside its territory in the aviation directive, and the WTO challenge to the ban on the marketing of seal products are signs that the EU needs to be mindful of possible external contestation of regulations primarily aimed at activities outside its territory. To be sure, the WTO Appellate Body has upheld the right to apply trade restrictive measures to respond to global environmental challenges or for ethical reasons as seen with GATT/WTO case law going back to the 90s (tuna, dolphins, shrimps, turtles, seals). The design of the measure needs to be however particularly careful so as to be able to fulfil the conditions of Article XX of GATT, including reassurance with regards to the non-protectionist motivation of the regulation.[28]

The Commission is conscious of the importance of ensuring the legitimacy of regulations dealing with global externalities. Hence the insistence that any BCAM should be consistent with WTO obligations. In the first instance, it would be important to ensure that importers would not be subject to a higher burden than domestic producers – i.e. that the measure is non-discriminatory in its design and in its application. A further complication is how far account should be taken of measures taken by the exporting country to internalise carbon costs. Such measures may be based on different forms of carbon pricing or regulatory measures, which raises the question of how to evaluate the comparability of measures adopted by different jurisdictions.

The practice so far of type 3 regulations is too limited to draw definitive conclusions about the objectives pursued through regulatory cooperation and the preferred type of instruments to be used. The legitimacy of EU action is clearly enhanced the more the EU is seeking to achieve an internationally recognised goal. This '**purity of motives'** is also important in terms of defending autonomous measures under WTO law. In particular, it is critical to be able to show that the measure is clearly motivated by a legitimate objective covered by Art. XX of GATT and is not intended or designed to address competitiveness concerns. As to the instruments used, most of the actions taken so far by the EU have included the option of concluding international agreements as an alternative to autonomous measures restricting imports. It is clear, however, that reaching an international agreement on comparable measures to achieve goals such as climate neutrality would take time and is unlikely to cover all large emitters, thereby raising the question of how to avoid carbon leakage by non- participants in the agreement.

[28] See discussion of AB jurisprudence in Howse, op. cit. Depending on its design a BCAM may not require justification under Art XX insofar as it can be considered an internal tax or regulation compatible with Art III of GATT. It should be noted that, unlike in the case of aviation, a BCAM would clearly fall within the scope of WTO disciplines. Countries that consider that the measure is not consistent with WTO rules can have recourse to WTO dispute settlements. Unilateral retaliation would be a clear breach of WTO law. This point illustrates that, contrary to what some have argued, a functioning dispute settlement system is a guarantee that countries can enact to protect the environment without being subject to undue pressure by its trading partners.

The Nordhaus concept of a 'climate club' is intellectually attractive but very hard to implement in practice.[29] What we are likely to see are messier and more tentative approaches in which a significant number of countries take action to enhance climate ambition, including different forms of addressing the problem of carbon leakage. Dialogue among regulators will be critical for both efficiency and legitimacy and to ensure a maximum level of coordination and compatibility between different autonomous actions.

Another important initiative relating to transboundary concerns is the broadening of the scope of due diligence legislation. This can have an important impact in promoting sustainable value chains, especially to the extent that it is accompanied by a regulatory cooperation approach on a parallel track – an important topic beyond the scope of this paper.

3. The EU's regulatory power surplus: how should it be used?

In light of the mosaic of aims and instruments pertaining to the trade-regulation nexus described above, we now turn to the broader context to ask how we should assess the nature of the EU's regulatory power and how it should be used in the future. We start with the question of power per se, or what we have referred to as the EU's power surplus. We then ask where this leaves external aspects of EU regulatory policies and the different models the EU can turn to reset its global role in this realm.

3.1 The limits of geopolitical motives

As it considers the use of its regulatory power surplus in a world of increasingly unfettered power politics, the EU's ambition naturally bends towards seeking to increase its weight as a geopolitical actor. To be sure, apart from regulatory efficiencies and trade facilitation, the external projection of EU regulations can be seen both as a form of hard power, insofar as compliance with certain requirements is a conditions to access the EU market, and as a form of soft power to the extent that normative influence on issues of transboundary concern can be based on an attractive model for others around the world.[30] This is particularly the case for type 3 regulations, although other regulations may also be seen as a reflection of EU standards (privacy, and ethical aspects of artificial intelligence) whose character as allegedly 'universal values' can be the subject of debates we will not enter into here.

But this is not a simple equation. As such the EU is often caught between two conflicting logics, although both can to some extent serve its geopolitical aspirations: on the one hand, an aspiration to use access to its market simply as a means to exercise geopolitical goals; to use

[29] William Nordhaus, "The climate club: how to fix a failing global effort." *Foreign Aff.* 99 (2020): 10.

[30] There is an extensive literature on the role of power in international relations, including in its early variant; Keohane and Nye considered how systems to manage interdependence can be media of power, in R. O. Keohane and J. S. Nye Jr., "Power and interdependence", *Survival* 15, No. 4 (1973): 158-165. J. Nye explored the facets of power in a series of influential books including J. S. Nye (2011), *The future of power*, Public Affairs. For an overview see M. Barnett and R. Duvall, "Power in international politics", *International organization* 59, No. 1 (2005): 39-75.

the closest thing it has to a unilateral power tool, 'simply because we can'; and on the other hand, to play a role in the world as a 'responsible power' through the projection of a principled approach to regulation whereby territorial extension is grounded on normatively clear goals that reinforce international institutions (from the WTO to the Paris agreement or functional standard setters).

The question we raise here is under what conditions the two ambitions – to assert itself geopolitically and to bolster the multilateral system – are compatible. We believe that the EU needs to base its regulatory strategy on the latter logic and that in addition, reinforcing rule-based multilateralism is in itself a central geopolitical goal for the EU. Pure geopolitical goals are generally best pursued through other mechanisms of diplomacy, for reasons of both effectiveness and legitimacy. If the EU were to use its power surplus to pursue extraneous geopolitical goals it would undermine its reputation as a principled regulatory power.

To be sure, it is tempting to exercise market power if you can convince yourself that your ends are good and legitimate. But as the direct territorial trigger for such influence becomes more tenuous from type 1 to type 3 regulations, the search for effectiveness, for example how the EU affects others in exchange for access to the single market, must be weighted more stringently against considerations of legitimacy as perceived by its trading partners. In other words, short-term effectiveness in exercising regulatory hegemony can be costly in terms of legitimacy and therefore ultimately erode the EU's effectiveness in the multilateral arena. Thus, its power surplus can be both under- and over-used.

Let us indicate three ways in which this may be so:

First, the coercive use of regulatory power ought to be strategically targeted through a clear distinction between the types of actors on the receiving end of EU regulatory power. The EU needs to be able to respond when third countries seek to weaponise their own power against its interests, and do so credibly. But such moves will be more effective if reserved for very specific instances in which the EU needs to react against coercive measures by others. In other words, such responses should not be arbitrary or ad hoc, lest this affects the EU's reputation for a principled approach and opens the way for others to deny market access on arbitrary or non-regulatory grounds. Instead, they are best handled through legislation that authorises the EU Commission to take countermeasures in accordance with international law. In that context, and provided that this remains exceptional, the suspension of certain regulatory benefits could be an appropriate remedy.

Second and relatedly, the EU's reputation as an objective regulator would be negatively affected if it engages in issue linkages, i.e. unilaterally withdrawing regulatory benefits in response to concerns, outside the scope of the regulation per se. To be sure, linkages can be seen as warranted when they serve the holistic approach called for by new generation of FTAs.

This does not mean however that linkages ought not to be handled with care.[31] Apart from responses to coercion, the withdrawal of regulatory benefits should be limited to cases in which there is a regulatory justification or following arbitration if such benefits are part of an international agreement. In this context, if we consider the kind of evaluations we are discussing in this paper across the board – from unilateral periodical assessments of equivalence (finance, data) to the continuous assessment of regulations under contractual agreements) – to wield the regulatory stick beyond carefully defined circumstances would become counter-productive and risk opening Pandora's box. Brazen uses of power need to be handled with care, not only because they may alienate partners and unleash retaliatory cycles but, perhaps more importantly, it will hinder the EU's ambition is to reinvigorate its regulatory influence globally.

Third and more generally, the EU could be more ambitious and proactive in channelling its power surplus towards what some would call 'productive power', for instance its influence on how other actors see what is possible and desirable.[32] When regulation is focused on the protection of citizens where effectively enforcing one's regulations upon importers is paramount, as with most type I and type 2 regulations, efforts must be made to mitigate the negative impacts of the regulatory change demanded from vulnerable developing countries and signal readiness to engage in cooperative developmental dimension. When it comes to type 3 regulations and transborder concerns, the EU needs to ensure the legitimacy of its external regulatory action, which is key to long-term sustainability of regulatory influence.

EU soft power cannot simply be the result of either market forces or the unilateral reliance on market power by EU regulators.[33] Rather, it should inevitably entail an element of proactive engagement and political agency. Moreover, and to the greatest extent possible, such political agency must be exercised on both sides and be based on mutuality of interest. Cooperation needs to be supported by reference to internationally endorsed goals rather than arguments that EU values are universal, given that the EU cannot define what is 'universal' unilaterally.[34] Ultimately, this would mean in part realigning internal regulation with global public goods through greater compatibility with the Sustainable Development Goals, a strategy that is beyond the scope of this paper. In short, the EU needs to be more self-reflective on how it puts its power surplus to work at the service of genuine cooperation.

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[31] K. Nicolaidis (2020), "Brexit negotiations: linkages need to be handled with care", *UK in a Changing Europe*, March.

[32] M. Barnett and R. Duvall, "Power in international politics", Op cit.

[33] See for instance, C. Damro, "Market power Europe", *Journal of European Public Policy* 19.5 (2012): 682-699; see also S. Meunier and K. Nicolaïdis, "The European Union as a conflicted trade power", *Journal of European Public Policy* 13.6 (2006): 906-925.

[34] See K. Nicolaidis (2015), "Southern Barbarians? A post-colonial critic of EUniversalism" in K. Nicolaidis, B. Sebe and G. Maas (eds), *Echoes of Empire: Memory, Identity and Colonial Legacies,* London: IB Tauris.

3.2 Three models of EU regulatory power

How does the power surplus lens help us assess the alternative EU models regarding the trade-regulatory nexus?

The EU has so far followed three models to project its domestic regulations externally:

1) Exporting the single market: it has been tempting at times for the EU to simply seek to export a version of the single market, for a start because this is a formula that has served it well internally, whereby there are legal and technocratic modus operandi to make it work. Indeed, the 90s push in this direction was driven in part by the (partial) completion of 'Europe 1992' and the need to retool many of the experts who had been involved. And of course, the story of territorial extension we have told here is linked to the single market's strong gravitational pull. However, exporting the single market without the 'eco system' that comes along with it is an extremely ambitious exercise. Moreover, such a model is only relevant for countries that have particularly close trade and investment relations with the EU and are ready to base their regulatory regime on EU rules. This is clearly the case for countries that are candidates for enlargement, although their capacity to do so is often wanting. The European Economic Area (EEA) is the only EU agreement that entails participation in the single market. It has functioned well because of the high degree of homogeneity among its members and because non-EU members are ready to accept EU hegemony. Even there, it is fair to say that a country like Switzerland has sought to evade being subsumed entirely under the single market umbrella. The relationship with Switzerland is in any case being reconsidered through negotiations on a new framework agreement. As regards neighbourhood countries, the EU has offered the perspective of **"internal market treatment"** to countries that conclude Deep and Comprehensive Free Trade Agreements (DCFTAs), including commitments to align with a significant part of the EU *acquis*, although the concept has never been properly defined. Some Eastern Partnership countries like Ukraine have already substantially incorporated most EU regulations in areas relating to technical regulations, sanitary and phytosanitary measures (including animal welfare) and public procurement. [35] DCFTA negotiations have however failed to make progress in relation to countries in the southern neighbourhood, although some of them have also been autonomously introducing regulations based in EU rules.

2) The EU as a global regulatory hegemon: as the EU seeks to influence global regulatory developments, it can simply try to maximise the reach and impact of its market power to establish regulatory norms and standards that de facto become globally applicable regulations. The difference to the previous model lies with a more direct and unilateral exercise of power. As we discussed above, in a number of cases the EU has seen this role conferred upon itself as a result of a combination of market size and political will to regulate on the basis of high levels of protection. However, the EU has also consciously sought to

[35] M. Emerson and V. Movchan (eds) (2018), *Deepening EU-Ukrainian Relations What, why and how?,* 2nd edition, CEPS, Brussels.

influence third country regulations through the territorial extensions of domestic rules combined with equivalence determinations. Such an approach is likely to be effective in areas where the legitimacy of EU action is not challenged and where there are no competing regulatory models. The gravitational pull of EU rules is likely to be stronger if there are substantial benefits attached to an equivalence determination. But the question is open as to how far the EU could simply rely on its market power in emerging areas of regulation, particularly if these are of a transboundary nature.

3) A good governance model: as suggested in our discussion of power, going beyond an 'hegemonic model' would imply **combining market power with active cooperation policies more proactively based on mutuality of influence and benefits**. This could be described as a 'good global governance approach', to cite the Treaty of European Union. Arguably, this is what the EU has already tried to do since the early days of the single market through its support for the development of international standards in many areas of goods and services regulation. But as China becomes an increasingly important player in international standards bodies and the EU focuses its attention on the climate and digital transitions, there is a need to reflect on new means of enhancing the impact of EU external regulatory policies. A key for a sustainable 'good global governance' model is that the EU should be ready to offer its partners cooperation based on mutual benefits, both in terms of regulatory efficiencies and trade facilitation. This also implies that the EU must accept a more explicit mutuality and symmetry of influence. Regardless of whether the instruments chosen imply some form of cooperation agreement or autonomous decisions, there should be a commitment towards consultation and transparency and a readiness to progressively build up relationships based on mutual trust. Cooperation could proceed on a step-by-step basis, gradually increasing as trust is developed, while always maintaining regulatory autonomy and reversibility. The more the EU is able to base its regulatory action on a good governance model, the more credible it will be in promoting regulatory good governance globally.

Clearly, the difference between these models lies in the normative ambition of the EU and the extent to which it seeks to link its external regulatory action to broader issues of global governance. We argue for the third – the good governance model. But of course, these three models are not mutually exclusive and will inevitably be combined in the EU's global regulatory strategy. They overlap to the extent that in each case regulatory cooperation is linked to some degree of export of the single market model and therefore potentially to applying the lessons of managed mutual recognition, to which we now turn.

4. An integrated approach to managed mutual recognition: legal empathy and the regulatory compatibility paradigm

To be more specific, we now turn to what could be the next frontier in regulatory cooperation, in other words, the common thread in this story. For this, it is useful to go back to the way in which the EU has dealt with the nexus between trade and regulation within its own territory

over its own history and ask what policy would look like if we sought to maximise the consistency between this internal approach and the external regulatory governance discussed in this paper. This, we argue, is the most promising path towards the good governance model we advocate.[36]

4.1 Internal market

In a nutshell, the single market has been developed over the years along two paths, namely ECJ jurisprudence and law-making in Brussels – both of which have involved conversations and negotiations with national judges, politicians, lawmakers, scholars and sometimes the public at large. To simplify, the EU has seen a changing mix of three core principles underpinning trade liberalisation in a regulated world, namely national treatment (or host country rules), harmonisation, and mutual recognition (or home country rules). This story has been widely told and analysed through countless textbooks, Commission papers, and legal journal articles on ECJ jurisprudence.[37] For our purposes, three main points can be made.

First, since the 1987 Single European Act, the EU has dealt with so-called non-tariff or regulatory barriers to trade in a piecemeal and pragmatic way. On the one hand, the ECJ is tasked with assessing national rules *as they are* when they may hinder free movement to assess whether the differences between them might justify the hindrance. This is the first space where 'legal empathy' operates. Then EU-level rule making enters the scene to carry such legal empathy from the judicial to the political sphere. Even when member states agree on common substantive standards, the key to good regulation is good supervision. And in this regard, even when it sets up regulatory agencies, the EU tends to rely on national regulators. So if goods and services are to move freely across borders, their country of destination must trust the 'home state' regulator to provide the right stamp, certification, licence, supervision and the like. This mutual recognition is at the heart of the system, even when some underlying harmonised standard has been adopted.[38] On both paths, we have referred to variants of legal empathy.

Nevertheless, and this is the second point, there is no such thing in the EU as pure mutual recognition, blindly recognising each other's rules and standards for ever more. Instead, the EU single market has become a complex and layered system, which we should refer to as **managed**

[36] For a version of this argument, see https://ukandeu.ac.uk/wp-content/uploads/2018/03/Brexit-and-the-compatibility-paradigm.pdf.

[37] For a recent overview see S. Weatherill (2016), *The internal market as a legal concept*, Oxford University Press.

[38] A. Heritier, "Mutual recognition: comparing policy areas", *Journal of European Public Policy* 14, No. 5 (2007): 800-813; S. Lavenex, "Mutual recognition and the monopoly of force: limits of the single market analogy", *Journal of European Public Policy* 14.5 (2007): 762-779l; P. Genschel, "Why no mutual recognition of VAT? Regulation, taxation and the integration of the EU's internal market for goods", *Journal of European Public Policy* 14.5 (2007): 743-761; J. Pelkmans, "Mutual recognition in goods. On promises and disillusions", *Journal of European Public Policy* 14.5 (2007): 699-716; For a broad interdisciplinary approach see K. Nicolaidis (2017), "Mutual Recognition: Promise and Denial, from Sapiens to Brexit", *Current Legal Problems*, *70*(1), 227-266.

mutual recognition.[39] Whether as the ECJ's recognition of equivalence, or regulatory mutual recognition, the process has been predicated on assessing whether differences between sides are indeed legitimate differences, and if they are then to base free movement on the *compatibility, comparability,* or *similarity* between regulatory regimes, restricted by a strong rule of reason, and allowing for legitimate concerns on the part of host states when it comes to 'competition over rules.' Legal empathy is a way of describing the intuition that this process involves a deep engagement with each other's system and with the necessary calling to respect rather than deny our differences. This is no doubt a messy and complex story. How mutual recognition is managed varies with each specific area, whether we are talking about agricultural products, toys, the recognition of professional licences or banking services or, beyond the single market, court decisions and arrest warrants. But in each of these areas, we find a variant of the same overall managed mutual recognition approach, namely that the host state of the consumer extends as much deference to the home state of the producer as possible, and exercises as much interference as necessary.

Thirdly, the managed mutual recognition game is an ingenious dynamic process, involving trade-offs that may change over time. There may be many ways of forging trust by, say, preliminary agreement on 'minimal' standards and, crucially, the inclusion of safeguards against change through the partial or total reversibility of recognition. If trust is broken, if the exporting state downgrades its regulations, host states where exports land are allowed to re-assert their own control.

In light of the EU's considerable track record it is fair to say that the machine works because it is constantly tweaked by judges and regulators. This approach was designed to avoid one- size-fits-all standards and supervision, allowing for a high degree of national regulatory autonomy throughout the EU within the overall framework of the single market ecosystem, developed over time by legislators, regulators and the judiciary.

For reasons of political expediency as well as regulatory efficiency, managed mutual recognition also relies on a kind of magic trick: accelerating trade liberalisation thanks to a shift from exclusive reliance on ex ante agreement on common standards to ex post conflict management, relying on ongoing cooperation and adjudication to determine whether the conditions for recognition continue to be met. Contrary to what many believe, this kind of recognition dynamic is not deregulatory – it is what governments, regulators and indeed the ECJ make of it – as the latter adjudicates conflicts over recognition. Managed mutual

[39] K. Nicolaïdis, "Trusting the Poles? Constructing Europe through mutual recognition", *Journal of European Public Policy* 14.5 (2007): 682-698; K. Nicolaïdis (2005), "Globalization with human faces: Managed mutual recognition and the free movement of professionals", in F. Schioppa, *The principle of mutual recognition in the European integration process*, Palgrave Macmillan, London, 129-189; K. Nicolaidis (1997), "Managed mutual recognition: The new approach to the liberalization of professional services", in *Liberalization of Trade in Professional Services,* OECD Publication; M. Poiares Maduro, "So close and yet so far: the paradoxes of mutual recognition", *Journal of European Public Policy* 14.5 (2007): 814-825.

recognition is a complex eco-system involving intense coordination over time that can only work if underpinned by a philosophy of legal empathy.

4.2 External dimension

It is correct to say that international regulatory cooperation, as discussed in Part I, does not rely on the same depth of supranational institutions as the type of regulatory cooperation that underpins the single market. Also, when it comes to the global arena, parties to different forms of cooperation arrangements are obviously much keener than EU member states to maintain their regulatory autonomy.[40] In the absence of a common legislation with direct effect and a judiciary with legitimacy to adjudicate on regulatory preferences, the benefits of the single market cannot be replicated abroad.

Nevertheless, we must not throw out the baby with the bathwater. There are in fact margins of freedom offered by the history of the single market that offer subtle guidelines rather than fixed rules for interpreting the exercise of EU regulatory powers externally. For one, we can harp back to the early 90s when the EU did design a project to extend the rule of its single market globally – which led at the time to a few relatively disappointing MRAs, as discussed in part I above.[41] But the potential is still there, if we care to be inspired by Maimonides, who, in his Guide for the Perplexed, argued that it was important to offer truths that were at the same time apparent and concealed. This may be what EU political-economic history can offer.

To the extent that the EU system results from a constantly renegotiated compromise between different national legal approaches and governance philosophy, this exercise in legal empathy is indeed more suitable for export – even without an 'ecosystem' – than the US one, which critically depends on an ex post litigation apparatus that is almost impossible to replicate abroad.

Indeed, we believe that the design and dynamics of regulatory cooperation can certainly be inspired by the EU approach and the lessons we have drawn from it over the years. Common to both the internal and external dimensions of EU regulatory cooperation regimes is what we can call the "compatibility paradigm", a paradigm grounded on legal empathy.

Despite crucial differences, the EU experience can help identify certain principles that could guide regulatory cooperation in the spirit of 'managed mutual recognition,' along four dimensions:

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[40] See the OECD programme on better regulations, A. C. de Brito, C. Kauffmann and J. Pelkmans (2016), "The contribution of mutual recognition to international regulatory co-operation", OECD Regulatory Policy Working Papers, N2. On the EU side, see inter alia K. Nicolaïdis and M. Egan (2001), "Transnational market governance and regional policy externality: why recognize foreign standards?", *Journal of European Public Policy*, *8*(3), 454-473.

[41] K. Nicolaidis and G. Shaffer, "Transnational mutual recognition regimes: governance without global government", *Law and contemporary problems* 68.3/4 (2005): 263-317.

1) Compatibility of underlying regulatory regimes: this first dimension, powered by legal empathy, is to ask on what grounds the regimes can be deemed 'compatible' or not. Such a criterion is less strict than to require the same or harmonised standards but acknowledges that the parties need to pursue the same regulatory ends or at least be similar enough. This prerequisite is obviously stricter for type 1 regulations where a product can only be marketed if it complies with EU standards (although these may be defined in a sufficiently broad manner to allow for regulatory diversity). In type 2, it may be less focused on the convergence of standards and more on trust in the capacity of the home regulator to verify compliance with EU standards. In type 3, recognition of greater regulatory divergence may be appropriate provided EU rules are not undermined. In order to attain regulatory compatibility it will often be more necessary to enter a process of regulatory cooperation externally than internally, to the extent that parties are further apart at the outset and that trust between regulators starts at a lower level. A formal process to assess what is necessary to ensure regulatory compatibility can only take place case by case. For some neighbouring countries, regulatory alignment may provide the best way of anchoring to the EU regulatory regime, but such an approach is unlikely to be valid outside the context of particularly close relationships. In cases concerning protection of fundamental rights (e.g., privacy), a high degree of regulatory approximation may be necessary to avoid a legal challenge. For certain issues it might be sufficient for both sides to rely on internationally agreed standards while the focus would be whether there is enough trust in the supervision capacity of the other side. In view of the variety of equivalence regimes in the EU, it is important for legitimacy purposes to have as much clarity ex ante regarding the criteria to be used for an equivalence assessment. Thus, when new regulations are developed there should be a much greater focus on what type of compatibility assessment fits the regulatory purpose.

2) Transparency: in the end, compatibility is in the eyes of the beholder. Citizens of the host country (as consumers) need to be reassured that their protections are not undermined by any determination of compatibility with home country regulations. This is particularly the case for type 1 and 2 regulations where the centre of gravity is on maintaining the domestically set level of protection. But citizens of the home country (as producers) also need reassurances against arbitrary or discriminatory restrictions on trade, particularly in the case of type 3 regulations. In this regard, it is critical to underpin any external regulatory compatibility assessment with transparency exigencies that will in turn empower both the host state citizens but also the home state citizens who have an interest in 'compatibility' with the EU. Transparency in short is critical for domestic legitimacy. It should relate both to the identification of initiatives for regulatory cooperation and to their implementation, including the opportunity to consult stakeholders. To be sure, in the case of digital tech, transparency is all the more necessary given the challenges posed by algorithms and inspecting data flows.

3) Limitations of scope: the liberalising power of managed mutual recognition lies in its dynamic nature – to the extent that the degree of regulatory compatibility and

transparency to enforce it may vary, parties do not have to adopt an all-or-nothing approach. Instead, they may enter into partial and conditional recognition, thus limiting the scope of recognition. It is important to dispel illusions that international regulatory cooperation can provide benefits that are comparable to those of the single market. Even if regulations are identical, the absence of common institutions and enforcement procedures implies that cooperation needs to be sustained on mutual trust and that the benefits would inevitably be more limited than single market treatment. But these limitations are dynamic. Partial recognition in the EU has meant that insurers, say, can ask to sell corporate risk but not all mass risk on the basis of their home state rules. Conditional access may mean that a firm or individual, for example, may find residual requirements when operating in the host country requirements. Externally, restrictions in scope may be more radical.

4) Mechanisms for ex post assessment, including reversibility: the dynamic nature of managed mutual recognition implies that ex post assessment of the continued compatibility between regulatory regimes is critical. Since cooperation is based on trust, there should be mechanisms to maintain dialogue among regulators. Crucially, and to the extent that the EU's counterpart shares basic notions of democracy and the rule of law, these mechanisms need to be reciprocal. These should include an exchange of views on possible changes to the regulatory framework or on concerns relating to implementation. At any point in time, reversibility should be possible, although this should be preceded by consultations and a willingness to explain decisions and make good faith efforts to address concerns. Transparency and consultation could apply regardless of whether regulatory cooperation is based on a legally binding agreement or an autonomous decision. In any event, it does not appear feasible to subject decisions on reversibility to binding dispute settlement, although if one of the parties decides to terminate equivalence, the other may be justified in taking mirror action in the same sector.

5. Recommendations: globalising legal empathy

At a time when the EU is seeking to develop its geopolitical influence and its capacity to act strategically, it is important to reflect on a more coherent approach to the external aspects of EU regulatory policies that also makes full use of the synergies between EU trade, regulatory and development cooperation policies. The EU has just adopted a new Trade Policy Strategy that identifies as one of its priorities the strengthening of the EU's regulatory impact.[42] While the Communication recognises that supporting regulatory cooperation activities will become an increasingly central objective for EU trade policy, it does not offer an overall rationale for the trade-regulation nexus or draw institutional consequences as to how to ensure better integration of trade and regulatory policies. In this regard, we would wish to offer six proposals to reinforce EU external action in the field of regulation:

[42] Trade Policy Review: An open sustainable and assertive trade policy, COM(2021)66 final of 18.2.2021.

1. Adopt a 'compatibility' approach to external regulatory cooperation

The aim of EU regulatory cooperation policies should be to progressively work towards the greater compatibility of regulatory regimes based on common values and high levels of protection. How this compatibility is to be achieved would of course need to be issue-specific and contingent on the regulatory objective pursued. The more they relate to transboundary concerns, the greater the importance of a strong external cooperation dimension. Working towards the compatibility of regimes would involve, inter alia, mutualising equivalence assessments to ensure that regulatory changes in the counterpart country benefit from local ownership rather than be perceived as a mere function of a market access imperative. Second, transparency, especially aided by digital tools, will become an increasingly important part of global regulatory cooperation, which in turn will help empower local actors in their role as local enforcers of commitments. Third, the dynamic aspect of trade-cum-regulation deals implies that they can provide for progressive expansion of scope as a function of mutual trust and of a greater degree of regulatory compatibility. Last but not least, ongoing cooperation, including reversibility of access, is critical to maintaining regulatory autonomy.

2. Set up a coordinating structure on the external aspects of regulatory policies

The Commission services responsible for different regulatory policies normally take the initiative to develop dialogues with third countries and participate in different organisations or informal fora bringing together regulators from different countries. Maintaining ownership by regulators is essential for international regulatory cooperation, but there would be significant value added in setting up a coordinating structure that sets EU-wide priorities and explores synergies between different instruments of external action, in particular regulatory, trade and development cooperation policies. One of the tasks of the coordinating structure could be to ensure that the external aspects of regulatory initiatives are properly considered in the impact assessment of new legislative initiatives. This should go beyond 'defensive' concerns such as analysing impacts on trade or WTO compatibility and include a discussion of the opportunities for international regulatory cooperation and a review of what would be the tools most appropriate to achieve the external goals of EU regulatory policies, including work in international organisations, equivalence or different forms of plurilateral or bilateral agreements. This should also include specific consideration of the type of equivalence assessment that best fits the regulatory purpose pursued.

3. Identify strategic priorities for regulatory cooperation linked to the s climate and digital transition

Many aspects of EU regulation will need to be overhauled or developed in response to the two political priorities of the green and digital transitions. This will happen in a complex external environment characterised by the US-China geopolitical conflict. In this context, rather than being conceived as a purely internal exercise, the development

of EU regulations should be embedded in an overall strategy that identifies priorities and partners for international regulatory cooperation (in Canada for instance, IRC is regularly included in impact assessments). This strategy could build upon the EU areas of comparative strength such as the impact that the EU regulatory framework for privacy has already had in a number of important trading partners. Could this provide the basis for a plurilateral initiative to cooperate on other priority aspects of regulation of the digital economy such as artificial intelligence? What would be the best fora and alliances for the EU to promote regulation or standards that contribute to the goal of climate neutrality by 2050? In view of the election of Joe Biden as US President, the EU could also envisage a close transatlantic partnership to promote shared regulatory goals based on common values and seek to cooperate within the framework of international standard bodies. This could be one of the tasks of the recently announced Trade and Technology Council.[43]

4. Explore synergies between trade and regulatory cooperation policies

An important objective of regulatory cooperation is to facilitate trade. Insofar as this is achieved without compromising regulatory objectives, **there is no reason why trade and regulatory policies should not continue to be mutually supportive.** Nevertheless, the TTIP experience has illustrated the risks of including broad regulatory cooperation objectives within the framework of trade negotiations. Despite maximum efforts on the part of the EU to ensure transparency, there was an unavoidable suspicion that there could be trade-offs between regulatory and market access issues in the context of comprehensive negotiations. It is preferable therefore not to overload the agenda of trade negotiations with regulatory elements that go beyond the promotion of international standards, although upgrading such standards in light of evolving priorities remains key. This should not mean, however, that the EU should waste the opportunity provided by its extensive network of free trade agreements to promote regulatory cooperation. Free trade agreements provide the most important framework for economic cooperation between the EU and third countries and can attract more high-level attention than sectoral bilateral dialogues. The CETA Regulatory Cooperation Committee has illustrated that it is possible to use the structures of a trade agreement to develop a process of cooperation that is fully transparent vis a vis civil society and is led and owned by the regulators on both sides. Regardless of whether there is or not a regulatory cooperation committee, the EU could make best use of the institutional structures of its free trade agreements to explore regulatory cooperation initiatives based on mutual interests. Any such activity should be fully transparent and led by the competent regulators building upon the good practices developed in the context of CETA.

[43] See "A new EU-US agenda for global change", JOIN (2020)22 final.

The WTO continues to provide the framework of rules that ensures that domestic regulations do not have a discriminatory or protectionist impact. The Appellate Body has interpreted the rules in a manner that is respectful of regulatory diversity. Respect for regulatory autonomy can however be combined with the **encouragement of good regulatory practices and greater compatibility of regulatory regimes**. This should be done not through deeper binding commitments in the field of regulation, but rather through **enhancing the WTO deliberating function**, supported by other deliberative bodies such as the OECD or UNCTAD and technical organisations in the field of regulations and standards. As part of the process of WTO reform, the EU could support a reinforcement of the role of WTO committees in the early discussion of regulatory initiatives, as fora to facilitate an exchange of information about international standards and regulatory cooperation initiatives. Moreover, the EU could be ready to lead by example through **early notification of regulatory initiatives with a significant trade impact,** including the proposals to introduce a border carbon measure or mandatory due diligence legislation.

5. Enhance participation of neighbourhood countries in EU regulatory activities

A number of countries in the neighbourhood have made a substantive effort to incorporate EU regulations into their domestic law. This includes countries that have concluded a DCFTA with the EU or countries in the Western Balkans. Since EU regulations are by nature dynamic, it would be important to identify ways of associating those countries to the work undertaken by EU experts or regulatory agencies in those areas where they have completed the process of alignment. **Another way of increasing the 'agency'** of non-EU countries would be through enhanced modalities of participation in the work of the European standardising bodies, as is already the case for EEA countries and to some extent Turkey. In the future such expanded '**regulatory clubs'** could also be extended to other neighbourhood countries for sectors where regulations are substantially aligned.

6. Reinforce investment focused partnerships with African countries

In its new trade policy strategy, the EU has identified relations with Africa as a core strategic priority whose central objective is the promotion of sustainable investment. As African countries develop their own economic integration and regulatory capacities, the EU could offer to strengthen regulatory cooperation, with a particular focus on sectors where there is a potential to attract European investment. This could form part of broader partnerships to support sustainable investment and facilitate the integration of African companies in value chains, including to meet sustainability requirements. A dialogue on regulatory issues of common interest could be established both at the level of the African Union and of those regional subgroupings or individual countries that wish to further develop these partnerships so as to agree on priorities and possible cooperation modalities. This dialogue could also provide early warning of EU regulatory

initiatives that may impact on trade with African countries and identify areas where support can be provided to reinforce regulatory capacities. This would require a willingness on the part of the EU to follow a coordinated and integrated approach to policies relating to development cooperation, trade and regulation.

6. Postscript

We started writing this paper as the Brexit saga was unfolding, and finished it as it came to a close of sorts with the signing and implementation of the Trade and Cooperation Agreement (TCA) between the EU and the UK by the start of 2021. It would be disingenuous to pretend that the dilemmas associated with the terms of this agreement were absent from our minds as we discussed and conceived this paper and the philosophy that underpins it. Indeed, while we take the TCA agreement as a given, with its limited reach in terms of regulatory cooperation, we also believe that it opens up many options for cooperation in the future.

We applaud the fact that all the clauses of the agreement are reciprocal, symmetric and constrained by arbitration, and that the deal leaves little scope for unilateral measures and is constrained by agreed procedures. Whatever the balance in the future between areas of regulatory convergence and divergence, the two sides will have an interest in managing these ever-changing dynamics in a constructive way, devoid of the grand rhetoric, one-upmanship and power games that would appear quite pathetic within the European family.

To be sure, when we advocate a partial consistency between internal and external 'managed mutual recognition,' we need to distinguish between the initial scope for negotiating reciprocal access and the conditions and norms that should govern access over time. In the internal EU context, all sectors pertaining to the single market are legitimate candidates for engaging in an exercise in legal empathy through regulatory approximation or recognition, irrespective of the balance of market gains that this will be create. This is obviously not the case in the external context where parties first consider a balance of interests in economic terms before engaging in the kind of regulatory politics we are concerned with in this paper. This may mean, for instance, that sectors that are 'compatible' in regulatory terms may be excluded from negotiations, as we saw in the Brexit case. In keeping with our argument on the use of the EU's power surplus, we believe that this logic ought to be softened at the edges, with a strong presumption, in the future, in favour of enlarging the scope of access and legal empathy irrespective of these asymmetrical commercial gains.

In sum, when it comes to the trade-regulatory nexus, both sides will have an interest in practising legal empathy and adopting a regulatory compatibility paradigm. This is all the more true because, in the best of all worlds, how this agreement unfolds may in the end constitute an example for the rest of the world.