16. The harmonisation of EU tort law: a law and economics analysis

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1 INTRODUCTION

It is important that a Research Handbook on European Union (EU) tort law also includes the law and economics perspective. Law and economics can provide a great many contributions to European tort law. One aspect is that the traditional economic approach to law could equally be employed to analyse the efficiency of specific rules of EU tort law.\(^1\) Many of the studies that have preceded the Principles on European Tort Law (discussed in Chapter 14 in this volume) have also included an economic approach, for example, to the concept of fault.\(^2\) However, this is not the approach that is taken in this chapter. There is yet another interesting role to be played by the economic approach, which is that economics equally provides criteria for centralisation or decentralisation of legal rules.\(^3\) The advantage of this approach, embedded in what is referred to as the ‘economics of federalism’, is that it provides clear criteria for the choice between either the central or the decentral level. Those criteria go beyond the question of the (economic) desirability of harmonisation of tort law in Europe and could be applicable to any jurisdiction in which choices have to be made about the optimal level of

\(^{1}\) For an overview of the economic approach to tort law see the basic handbook by Steven Shavell, *Economic Analysis of Accident Law* (Harvard University Press, Cambridge, MA 1987).


governance. A main part of this literature is also of American origin.\footnote{See, for example, Richard L. Revesz, ‘Rehabilitating interstate competition: rethinking the race-for-the-bottom rationale for federal environmental regulation’ (1992) 67 New York University Law Review 1210–54 and ‘Federalism and interstate environmental externalities’ (1996) 144 University of Pennsylvania Law Review 2341–416.} The advantage of this literature is that it does not provide bold statements either in favour of or against harmonisation but, rather, provides balanced criteria indicating that in particular circumstances and under specific conditions harmonisation may be indicated, but not in others. The economic approach would in some cases be more critical towards harmonisation, more particularly of rules of private law, especially in comparison to the sometimes enthusiastic reactions of some private lawyers in favour of further harmonisation of private law in Europe.\footnote{This critical perspective with respect to harmonisation of private law is well defended by Van den Bergh in 1998 (n 3) and also concerning the harmonisation of contract law (Roger Van den Bergh, ‘Forced harmonisation of contract law in Europe: not to be continued’ in Stefan Grundmann and Jules Stuyck (eds), An Academic Green Paper on European Contract Law (Kluwer Law International, The Hague 2002) 249–68) and consumer law (Roger Van den Bergh, ‘The uneasy case for harmonising consumer law’ in Klaus Heine and Wolfgang Kerber (eds), Zentralität und Dezentralität von Regulierung in Europa. Schriften zur Ordnungsfragen der Wirtschaft, vol 83 (Lucius & Lucius, Stuttgart 2007) 184–206).} It is not the goal of this contribution to provide a detailed discussion, neither of all arguments in favour of or against harmonisation of tort law from an economic perspective, nor to provide a critical analysis of all existing EU tort law rules. To some extent this has been done in earlier publications on which this chapter continues to build.\footnote{See, for example, Michael G. Faure, ‘Productaansprakelijkheid in België en Europa: quo vadis?’ in Patrick Senaeve, Walter Pintens, Sophie Stijns and Eric Dirix et al (eds), Liber Amicorum Jacques Herbots (Kluwer, Antwerp 2002) 111–30.} This chapter provides a summary of the main reasoning underlying the economic approach to harmonisation of (EU) tort law, reviews the arguments in favour of harmonisation in a critical way and provides examples based on current EU tort law.

The remainder of this chapter is therefore built up as follows: after this introduction (section 1) the basic principle of competition between legal orders as a starting point is presented (section 2). Next, it is shown that the transboundary character of specific problems may be an argument in favour of centralisation (section 3) as well as the danger of a race to the
bottom (section 4). A traditional argument often advanced in the European discourse is that harmonisation would be needed to 'level the playing field'. This is, so it is held, not a valid justification from an economic perspective (section 5). A reduction of transaction costs may be an argument in favour of harmonisation, but the room for such a reduction seems to be limited, especially in the light of experiences with harmonisation so far (section 6). In some cases (more particularly concerning non-pecuniary losses) harmonisation is advanced as a reason to provide a minimum level of protection, which is equally doubtful from an economic perspective, given differing preferences of citizens on that point (section 7). The contribution ends with a few policy considerations (section 8) and concluding remarks (section 9).

2 COMPETING LEGAL ORDERS AS A STARTING POINT

2.1 Tiebout

The starting point for the analysis is usually Tiebout’s theory about the optimal provision of local public goods. Tiebout argued that when people with the same preferences cluster together in communities, competition between local authorities will, under certain restrictive conditions, lead to allocative efficiency. If there are, for example, in one community citizens who greatly prefer sporting facilities and in another a majority of citizens with a preference for opera, the first community will probably construct sporting facilities, whereas the second may build an opera house. If someone living in the second community preferred sporting facilities to the opera house, he could then move to the first community, which apparently provides services more to his taste. The idea is that well-informed citizens will move to the community that provides the local services that are best adapted to their personal preferences. Through this so-called 'voting with the feet', competition between local authorities will lead citizens to cluster together according to their preferences.


indeed offer a variety of different services. The idea is that the citizen can have an effect on this provision of local public goods either by influencing the decision-making (vote) or by moving (exit).

2.2 Competing Jurisdictions

This idea of citizens moving to the community that provides services which best correspond with their preferences can also be applied with respect to legal rules. Thus, it has been argued by Van den Bergh that competition between legislators will lead to legal systems competing with each other to provide the legislation that corresponds best to the preferences of the citizens.9 Ogus also argues that the various law-makers in the nation states will create a competitive market for the supply of law.10 In an optimal world, citizens will cluster together in states that provide legal rules that correspond to their preferences. Well-informed citizens who are dissatisfied with the legislation provided could move (voting with the feet) to the community that provides legislation that corresponds best to their preferences. Since different legal systems offer different legal rules to satisfy the demands of the citizens, there will unavoidably be a variety and many differences between the legal systems.11 Moreover, it also shows that differences between the various legal rules of different countries should not necessarily be judged negatively, as is often the case in Europe today. The idea of competing legal systems can probably best be seen ‘in action’ in private international law where actors can choose the legal system that best suits their needs in a choice of law regime.12 But also in the context of tort law, in principle, domestic preferences would be reflected in the market for tort law systems.13

9 Van den Bergh 2000 (n 3).
12 Although the choice for a particular legal regime may not always be related to the quality of the legal system but, say, to the quality of the court or arbitration system. The latter explains, according to Ogus, the popularity of English law in choice of law clauses in contracts: Ogus 1999 (n 10) 408.
Competition between legal orders can only lead to efficiency in the provision of legal rules, when particular strict conditions are met. One condition is that citizens have adequate information on the contents of the legal rules provided by the various legislators, in order to be able to make an informed choice. In addition, exit is often costly, so people may stay even if the (legal) regime does not best suit their needs. Moreover, a location decision is made under the influence of a set of criteria, in which the legal regime may not be decisive. Usually the job location and residence are so important that in reality there is little left for people to choose.

This brief summary of the economic perspective on federalism shows that the starting-point is a bottom-up federalisation. This means that there is a presumption in favour of decentralisation since the local level is presumed to have the best information on the local problems and on the preferences of the citizens. Decision-making should only be moved to a higher level when there is a good reason. Economic theory has suggested that there may be a variety of reasons why the local level may not be ideal for decision-making and why moving decisions to a higher legal order may therefore be indicated. Those reasons are now reviewed.

3 TRANSBOUNDARY CHARACTER OF THE PROBLEM

The Tiebout argument in favour of competition between local communities works only if the problem to be regulated is indeed merely local. Once it has been established that the problem to be regulated has a transboundary character, there may be arguments to be made in favour of centralisation. First, there is an economics of scale argument to shift powers to a higher legal order that has competence to deal with the

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14 As Ogus states, there should be no barriers to the freedom of establishment and to the movement of capital: Ogus 1999 (n 10) 407. For these conditions, see also Van den Bergh 2000 (n 3) 438.
15 That is one of the reasons why Frey and Eichenberger argue in favour of functional overlapping competing jurisdictions (FOCJ): the choice for one legal or institutional regime should not be exclusive; there may be ‘overlapping’ jurisdictions depending upon the different functions: Bruno S. Frey and Reiner Eichenberger, ‘To harmonise or to compete? That’s not the question’ (1996) 60 JPE 335.
16 Rose-Ackerman (n 7).
17 For a good summary of the economic arguments concerning the harmonisation of tort law see also Van Boom (n 13).
externality over a larger territory. This corresponds with the basic insight that if the problem to be regulated crosses the borders of competence of the regulatory authority, the decision-making power should be shifted to a higher regulatory level, preferably to an authority which has jurisdiction over a territory large enough to deal with the problem adequately.18 ‘Economic theory provides a straightforward but unrealistic answer to regional problems: draw optimal jurisdictional boundaries.’ 19

3.1 Transboundary Externalities

There is, however, another argument in favour of centralisation which relates to the fact that in cases of transboundary externalities states would have no incentive to impose stringent regulations upon their own citizens if the consequences of harmful actions were only felt outside their own territories. Transboundary externalities thus may create inefficiencies in the absence of central regulation.20

This argument in favour of centralisation could thus play a role with respect to transboundary torts. Thus, many have proposed central decision-making in the areas of environmental liability, since this area of private law is typically transboundary.21 However, this externality argument cannot provide a general justification for the harmonisation of rules of tort law as long as accidents are confined within national borders. Moreover, even with these typical transboundary torts, we should not move too hastily to centralisation, since there may be remedies within national law as effective in dealing with these transboundary problems.

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19 Susan Rose-Ackerman, Controlling Environmental Pollution: The Limits of Public Law in Germany and the United States (Yale University Press, New Haven, CT 1995) 38.


Moreover, Van den Bergh has demonstrated that, in some cases, and more particularly in the area of private law, European law cannot be considered an effective remedy to the interstate externality problem.\(^{22}\) In some cases European law goes further than would be necessary to cure transboundary externalities; in other cases, less comprehensive legal instruments than total harmonisation could be used to remedy the problem.\(^{23}\) Thus, there is always the risk that the cure may be worse than the disease. The first issue relates to the fact that European directives often cover both local and community-wide problems, such as pollution, without making a distinction between regional and interstate pollution.\(^{24}\) The second point is that, in some cases, transboundary externalities may also be internalised by national law. The simple fact of transboundary effects is therefore not sufficient to justify European law-making.\(^{25}\) Nevertheless, there certainly may be cases where we could hold that decentralised legal rule-making would not be able to remedy the transboundary externality.

### 3.2 Examples

Although the risk of transboundary externalities may, in principle, constitute an important argument in favour of harmonisation of tort law, it is doubtful that this argument can justify harmonisation in some of the areas in which the EU has been active, more particularly, environmental and product liability.

To some extent a harmonisation of the rules concerning environmental liability took place via the well-known Directive on Environmental Liability.\(^{26}\) It is doubtful whether the transboundary externality argument could be used as a justification for the way in which the EU harmonised environmental liability, for the simple reason that the Directive largely applies to damage to biodiversity and for example to soil pollution.

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\(^{22}\) Van den Bergh 1998 (n 3) 143.

\(^{23}\) Van den Bergh 1998 (n 3) 144–5.


\(^{25}\) Van den Bergh 1998 (n 3) 144–5.

\(^{26}\) Directive 2004/35/CE on environmental liability with regard to the prevention and remedying of environmental damage. For an economic analysis of the application of the subsidiarity principle to environmental liability see De Smedt (n 21).
which is not necessarily transboundary.\textsuperscript{27} The transboundary character of environmental damage could have led to a ‘transboundary only’ regime which would only apply to interstate pollution and not to local pollution.\textsuperscript{28}

Similar problems arise with respect to another domain that has been harmonised at the European level, being product liability (discussed in Chapter 5 in this volume). The risk of an externalisation of harm to other legal systems would only arise if consumers would have no possibility of filing a lawsuit against manufacturers located abroad that marketed harmful products under the protection of their ‘lenient’ national product liability law. This is, however, not a very realistic scenario since manufacturers remain liable in export markets and within the EU citizens have the possibility to sue manufacturers for harm that is suffered in another country. In sum, the mere fact that different states within the EU would hold different preferences with respect to product liability and that hence different regimes would exist can, as such, hardly be considered as an argument in favour of harmonisation as long as states are not capable of externalising harm to victims in third countries.\textsuperscript{29} States are not able to externalise harm as long as manufacturers remain liable in countries where they export their products, whereby the law in the victim’s state will apply.\textsuperscript{30}

These examples show that even though at first blush the transboundary character of externalities may seem an important argument in favour of centralisation of tort law, the concrete examples of the product liability and environmental liability directives make clear that, in these particular cases, it is very doubtful whether this argument could provide an economic justification for centralisation at the European level.

\textsuperscript{27} See Kristel De Smedt and Michael G. Faure, “The implementation of the Environmental Liability Directive. A law and economics analysis of the transposition of the ELD in Belgium, the Netherlands and Germany” (2010) Zeitschrift für Europäisches Privatrecht (ZEuP) 783, 787.
\textsuperscript{28} This had also been suggested by Van den Bergh 1998 (n 3) 143–5.
\textsuperscript{29} Compare Van Boom (n 13) 444–5.
\textsuperscript{30} That is, protecting manufacturers through lenient product liability law would make no sense for national states since manufacturers remain liable in export markets. See further on this, Michael G. Faure, ‘Product liability and product safety in Europe: harmonization or differentiation’ (2000) 53 Kyklos 467–508.
4 A RACE TO THE BOTTOM

4.1 Destructive Competition

There may be an economic argument for centralisation, in that there is a risk that a ‘race to the bottom’ would emerge between countries to attract foreign investments. As a result of this, prisoner’s dilemmas could arise, whereby countries would fail to enact or enforce effective legislation. Centralisation can be advanced as a remedy for these prisoner’s dilemmas. This race-to-the-bottom argument could, in theory, play a role in the case of product safety and environmental production. It would mean that local governments would compete with lenient safety standards to attract industry. The result would be an overall reduction of standards below efficient levels. This should correspond with the traditional game theory result that prisoner’s dilemmas create inefficiencies.

The race-to-the-bottom argument has had supporters as well as opponents in North American scholarship. Law and economics scholars tend to stress the benefits of competition between states and point out the dangers of centralisation, whereas some legal scholars tend to attach more belief to the race-to-the-bottom rationale for centralisation.

This race-to-the-bottom argument has not as such been explicitly discussed in the European legal debate. It only shows up in the argument that the conditions of competition should be harmonised. That is discussed below. From an economic perspective, the race to the bottom is only a rationale for centralisation if it can be established that states could attract industry with lenient tort rules. Whether there is such a race-to-the-bottom risk is hence to a large extent an empirical question.

4.2 Example

The question whether differences between legal rules can lead to the risk of a race to the bottom has been discussed extensively within the context of product safety and environmental production. For a detailed discussion of this argument, see Daniel C. Esty and Damien Geradin, ‘Environmental protection and international competitiveness: a conceptual framework’ (1998) 32(3) Journal of World Trade 5, 16–19.


32 Rose-Ackerman (n 7) 166–70.


35 Van den Bergh 2000 (n 3) 445.
of environmental law, where it is referred to as the so-called pollution haven hypothesis. It implies that environmental costs between states could be different, potentially leading to the relocation of firms to the member state with the lowest standards. If there were empirical evidence of such a pollution haven, this would constitute an argument in favour of centralisation.

This pollution haven hypothesis has been heavily debated in North American scholarship. Repetto argues that pollution control costs are only a minor fraction of the total sales of manufacturing industries.36 Moreover, Jaffe et al argue that empirical evidence shows that the effects of environmental regulations are ‘either small, statistically insignificant or not robust to tests of model specification’.37 They argue that the stringency of environmental regulations might have some effect on new firms in their decision to locate for the first time,38 but that this will not induce existing firms to relocate. They equally argue that other criteria such as tax levels, public services and the unionisation of the labour force have a much more significant impact on the location decision than environmental regulation. This empirical evidence has been somewhat contradicted by Xing and Kolstad,39 who argue that the laxity of environmental regulations in a host country is a significant determinant of foreign direct investment by the US chemical industry. The more lax the regulations, the more likely the country is to attract foreign investment, so Xing and Kolstad argue.

Arguments against the race-to-the-bottom rationale for central environmental regulation have also been formulated with respect to the American example. Many scholars,40 among them Revesz41 in particular, have argued that this race-to-the-bottom argument finds no support in existing

41 See (n 4).
models of interjurisdictional competition. In addition, Revesz stresses that central standard setting would not be an effective response to the race-to-the-bottom problem, since the local communities concerned would have other means to attract industry if they wish (relaxation of regulatory controls in other areas). Revesz has encountered opposition, especially from Esty, but he has provided a reply to his critics.

Many economists remained sceptical of the empirical finding that environmental regulations were not a major determinant of industrial location, and more recent empirical work shows that there is indeed an inverse relationship between the stringency of air quality regulations and the level of capital flows in pollution-intensive industries. The US Clean Air Act distinguishes between relatively pristine ‘attainment’ areas and more heavily polluted non-attainment areas by imposing more stringent pollution standards on areas in non-attainment. Research found that even controlling for other observable factors that might influence capital movements, industrial plant growth is significantly higher in less stringently regulated attainment areas than in non-attainment areas. Recent work (which allows for the fact that attainment status is endogenous with respect to plant location decisions and carefully compares places that are similar in all respects except attainment status) finds an estimated cost to an area of being out of attainment with federal standards of between 0.7 and 1.3 new plants per year, a large percentage loss given that the average county in the sample studied gets only 0.4 new plants per year. List et al have also examined the effects of air quality regulation on the destination choice of relocating plants. In

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42 See for a similar conclusion with respect to natural resource legislation Johnston, who argues that regulatory centralisation may be just as tragic for natural resources as the regime of local control that it is designed to replace: Jason S. Johnston, ‘The tragedy of centralisation: the political economics of American natural resource federalism’ (2003) 74 University of Colorado Law Review 487–649.

43 See (n 18).


45 For example, Xing and Kolstad (n 39).


addition, that recent study shows that more stringent (air) pollution regulations play a critical role in the siting decision of relocating plants. Their results ‘provide strong evidence that air quality regulations matter’.48

Levinson, however, argues that notwithstanding large differences between states in hazardous waste disposal taxes, there has not been any pollution haven effect. He provides a variety of explanations, the most important one being that these state hazardous waste disposal taxes do not impose large employment losses on industries that generate waste.49

Other recent empirical work has tackled the problem of controlling for the full range of variables (besides just environmental regulatory stringency) that affect firm locational choice. Working with a more detailed dataset and again employing a propensity score matching estimator, Millimet and List50 found that even at the very local (US county) level, location-specific attributes such as unemployment levels and the overall level of manufacturing employment significantly impact the effect of environmental regulatory stringency. Millimet and List found that the cost of strict environmental regulations is lower both for counties with high unemployment – because they have relatively abundant, cheap labour – as well as for counties with a greater concentration of employment in manufacturing – because such counties generate agglomeration economies for manufacturing firms.

In summary, the new empirical literature on the ‘race to the bottom’ has found that environmental regulations have statistically significant, large effects on industrial location,51 effects that were previously either missed entirely or seriously underestimated.52 However, it should be

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52 Results of a meta-analysis of literally hundreds of studies by Tim Jeppesen, John List and Henk Folmer, ‘Environmental regulations and new plant location decisions: evidence from a meta-analysis’ (2002) 42 Journal of Regional Science 19, 21 show that the odd earlier results showing that the locational decisions of polluting and non-polluting industries were similarly influenced by
stressed that most of this empirical research focuses on competition between American states; the situation may be different in Europe where there is less evidence (at least as far as the old member states are concerned) of a ‘race to the bottom’.

Within the European context, especially when we consider the situation in the EU pre-enlargement, it was not that clear how member states could use environmental liability legislation to attract industry. If environmental liability were to have any effect, it is even more likely that states would wish to protect victims of environmental pollution instead of corporate interests. Hence, a race to the bottom in environmental liability in the EU was not considered very likely. However, it has been argued that the situation may have changed after EU enlargement in 2009.53 The capital mobility in Europe, more particularly the possibility for Western companies to invest in the East, led to a large change in the lobbying behaviour of firms. Increased investments by Western industry in Eastern Europe made those corporations benefit from lax environmental standards in Eastern Europe. That therefore created strong incentives to lobby in favour of regulatory decentralisation, making enterprises benefit from a weakening of standards. Post-enlargement (in 2004), the incentives of the industry may therefore have changed. In sum, the enlargement of the EU brings about important changes in incentives for industry to lobby in favour of (de)centralisation. The enlargement of the EU creates a situation where incentives for industry to lobby in favour of protectionist environmental standards at EU level is basically absent. Now that industrialised European nations have the possibility to export activities (and hence presumably pollution) to the new EU nations, we can expect less lobbying in favour of real environmental regulatory centralisation (uniform standards that are actually implemented and enforced uniformly). Western industry being active in the East may well benefit from lax environmental standards (and/or enforcement) in the new Central and Eastern European member states. That could equally apply to environmental liability rules in Eastern Europe as well. Companies from the

environmental regulations may have been due to the failure of earlier studies to control for variables such as factor composition and mobility and lobbying power.

West investing in Central and Eastern Europe may well benefit from lax rules, also with respect to, for example, soil clean-up.  

5 HARMONISATION OF MARKET CONDITIONS

5.1 No Economic Justification

Traditionally European legislation was often based on the argument that differences between member states’ laws would lead to different costs for industry and therefore create unequal conditions of competition.

The argument is that complying with legislation imposes costs on industry. If legislation is different, these costs would therefore differ as well and the conditions of competition within the common market would not be equal. The argument apparently assumes that total equality of conditions of competition is necessary for the functioning of the common market. ‘Levelling the playing field’ for European industry is the central message.

There are, however, some problems with this traditional European argument which claims that any difference in legislation between the member states might endanger the conditions of competition and therefore justifies harmonisation of legal rules. The latter argument seems particularly weak. From an economic point of view, the mere fact that conditions of competition differ does not necessarily create a race-to-the-bottom risk. There can be differences in market conditions for a variety of reasons, and if the conditions of competition were indeed totally equal, as the argument assumes, there would also be no trade.

Also, Europe has developed an elaborate set of rules which guarantee, inter alia, a free flow of products and services and thus contribute to market integration without the necessity of harmonising all rules and

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54 See Randall A. Bluffstone and Theodore Panayotou, ‘Environmental liability and privatisation in Central and Eastern Europe: toward an optimal policy’ (2000) 17 Environmental and Resource Economics 335–52, who (pre 2004!) showed that the potential of retrospective liability for cleaning up sites that were contaminated in the past limited the possibilities for privatisation since potential investors were scared away by the foresight of having to pay for the pollution of the past.


56 See Articles 34–37 of the Treaty on the Functioning of the European Union (the ‘old’ Articles 30–36).
standards. This shows that the goal of market integration can be achieved through (other) less comprehensive instruments than total harmonisation, which can remove barriers to trade just as effectively. Hence, one should make a distinction between the political ideal of creating one common market in Europe, on the one hand, and the (economic) race-to-the-bottom argument, on the other.

Increasingly it is now held that harmonised tort law is unnecessary for the creation of a common market. Moreover, empirical research has also shown that cross-border mobility is not so much affected by differences in rules of private law, but rather by non-legal elements such as differences in language, prize and transportation costs.

It should be stressed that the European argument that markets will be distorted without the harmonisation of the conditions of competition is not only constantly repeated in a stereotypical way, but its validity is hardly ever questioned. The argument, as it is usually presented in Europe, cannot be fitted into the economic criteria for centralisation, since it suggests that removing any difference in legal systems would be necessary to cure the race-to-the-bottom risk, which is neither supported by economic theory, nor by empirical evidence. Also, even if one were to take the (political) ‘common market’ goal as a starting point and private law were to be harmonised on that ground, this would still not create a level playing field since differences in, for example, energy sources, access to raw materials and atmospheric conditions will still lead to market conditions that favour trade.

There is, in addition, a strong counter-argument, in that there are many examples showing that economic market integration is possible (without

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59 See also Revesz, who equally argues that these are separate points which should be distinguished: Richard L. Revesz, ‘Environmental regulation in federal systems’ in Han Somsen (ed), 1 Yearbook of European Environmental Law (OUP, Oxford 2000) 1, 19.
60 Van Boom (n 13) 442–3.
the distortions predicted by the race-to-the-bottom argument) with unstandardised legal orders. Public choice scholars have often advanced the Swiss federal model as an example where economic market integration goes hand in hand with differentiated legal systems. It is apparently possible to create a common market without the total harmonisation of all legal rules and standards. The same is also the case in the United States where rules of private law, more particularly tort law, belong principally to the competence of the individual states. Again, this apparently does not prevent products from travelling without any restrictions or without causing undue distortions of competition.

5.2 Example

The harmonisation of the conditions-of-competition argument has played an important role in the area of product liability and it has even been used explicitly as (one of the) rationales for the European Product Liability Directive. The considerations preceding the Directive read: ‘Whereas approximation of the laws of the Member States concerning the liability of the producer for damage caused by the defectiveness of his products is necessary because the existing divergences may distort competition and affect the movement of goods within the common market.’ The weakness of this argument is that it assumes that differences in market conditions are always and necessarily a problem for the creation of a common market. Conditions of competition are never equal, as the levelling-the-playing-field argument assumes. In addition, we should realise that even if product liability law were totally harmonised in Europe, this would still not create a level playing field, since differences in, for example, energy sources, access to raw materials and atmospheric conditions will still lead to market conditions that divert trade. Moreover, looking at the text of the Product Liability Directive it is absolutely clear that it is not able to harmonise market conditions. According to Article 13 all the different, already existing, product liability laws remain in effect, which means differences that already exist will remain unchanged. In addition, at many points the Directive itself refers to national legislation, for example, with respect to the rights of

65 Van den Bergh 1999 (n 24) 6.
contribution or recourse (Articles 5 and 8.1), with respect to non-material damage (Article 9), the suspension or interruption of the limitation period (Article 10.2) and with respect to nuclear accidents (Article 14). It should also be mentioned that in three cases the original Directive expressly allowed the member states to derogate from the provisions of the Directive, namely, liability for primary agricultural products,66 liability for development risks and the introduction of a financial limit on liability. Moreover, the Directive cannot bring any harmonisation for product accidents to which it does not apply, because of limitations in the definitions of ‘product’, ‘producer’ and ‘damage’. Many notions in the Directive are also unclear and can give rise to interpretation problems.67 These problems might lead to different interpretations of the provisions of the Directive by the legislator and courts of the different member states. This example therefore shows that this harmonisation of the conditions-of-competition argument is not a useful basis for European action in the domain of tort law. It has to be seen in the context of the EU competences at the time which needed the ‘harmonisation of market conditions’ as a justification for EU competence. From an economic perspective, however, this cannot be supported.

6 REDUCTION OF TRANSACTION COSTS

6.1 The Need for Cost–Benefit Analysis

It is often argued that the existence of differentiated legal rules today leads to high costs for industry. If it were hence possible to remove all remaining differences between the domestic tort laws in EU member states, this would potentially lead to a reduction of transaction costs. As such, the argument seems to make sense, but it is based on two fallacies. The first problem is that it assumes that the current differentiation of tort rules only has costs and no benefits. This neglects the fact that some (but certainly not all) of those rules may reflect differing preferences of citizens.68 If harmonisation would hence remove those benefits, that should be taken into account as a cost as well. The second problem is that the argument assumes that harmonisation can be realised without any costs. The reality has shown differently. Some scholars have predicted

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66 See now Directive 1999/34/EC.
67 Consider the defect notion in Article 6 of the Directive, which might have different interpretations.
68 See Section 2 above.
that the differences between the legal systems in Europe are so large that a harmonisation of rules of private law is totally impossible.\(^{69}\) Van Dam also showed that the different shapes of tort law rules between the European legal systems are to a large extent connected to differences in legal culture, for example, between the United Kingdom (strongly relying on autonomy) and France (where solidarity is more important).\(^{70}\) In economic terms this means that harmonisation may lead to cost reduction, but that the process of harmonisation itself is also extremely costly and in some cases these costs are even prohibitive.\(^{71}\)

### 6.2 Potential for Transaction Cost Reduction

If we could argue that many existing tort law rules today only differ as far as the legal techniques are concerned, but not concerning underlying values and preferences, there may be an economic argument in favour of a transaction cost reducing harmonisation. If it were possible to unify liability rules which do indeed reflect similar values and preferences at relatively low costs, this should be considered as an important advantage. This is the leading thought behind many initiatives which have been developed by many academic tort lawyers in Europe and who examined whether it is possible to proceed to a harmonisation of tort law.\(^{72}\)

Many of these harmonisation projects are undertaken by academic lawyers who examine the existing differences between tort rules in the legal systems and try to find the largest common denominator. Such an

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\(^{70}\) Van Dam uses Hofstede’s framework on cultural differences to understand and analyse differences between tort law regimes in Europe: Cees van Dam, ‘European tort law and the many cultures of Europe’ in Thomas Wilhelmsson (ed), *Private Law and the Cultures of Europe* (Kluwer Law International, Alphen aan den Rijn 2007) 53–76.

\(^{71}\) See, for a further discussion of those arguments, Van Boom (n 13) 443–4.

\(^{72}\) Within the scope of this contribution it is not possible to mention all the projects that aim to achieve a harmonisation in the area of tort law (see Nils Jansen, ‘Auf dem Weg zu einem Europäischen Haftungsrecht’ (2001) ZEuP 30). A European Group on Tort Law, coordinated by Professor Helmut Koziol (of Vienna) has developed principles of tort law: see Spier and Haazen (n 55), *European Group on Tort Law, Principles of European Tort Law: Text and Commentary* (Springer, Vienna 2005), and Chapter 14 in this volume.
approach, looking for a common denominator on the basis of comparative legal studies and of case law seems far more promising than the approach followed by the European Commission so far.

The opportunities for harmonisation (from the perspective of lowering administrative costs) should especially be seen where preferences do not differ, but only legal techniques are different. The economic approach to tort law can be very helpful to achieve this goal. Indeed, the economic analysis of tort law has the advantage of focusing on functions and goals of tort law and, hence, enables the study of tort law at a higher level of abstraction. Thus this higher level of abstraction, essential for the economic analysis of tort law, may well enable the focus on the common roots between the various legal systems. The economic approach to tort law can thus provide an important contribution to the search for an *ius commune* of tort rules in Europe.

6.3 Example

Again the Product Liability Directive, as well as the Environmental Liability Directive, can show the high costs of the harmonisation process and hence the difficulty of reaching a real reduction of transaction costs. It was already mentioned that the Product Liability Directive is still strongly dependent upon national law and leaves all already existing product liability rules in effect. Therefore the Product Liability Directive has not been able to reduce transaction costs for manufacturers. It

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74 This is also suggested by Roger Van den Bergh and Louis Visscher, ‘The principles of European tort law: the right path to harmonisation?’ (2006) 14 *European Review of Private Law* (ERPL) 511–43.

75 Van den Bergh rightly points at lots of interpretation problems in the European Product Liability Directive which backs up the conclusion that the transaction cost savings may be small, simply because a full harmonisation of the rules of private law is apparently difficult to achieve: Van den Bergh 1998 (n 3) 146–7.
only adds an additional layer of complexity instead of reducing transaction costs.\textsuperscript{76}

The same argument can be made with respect to the Environmental Liability Directive. Again, the (political) costs of reaching uniformity were apparently so high that most of the important issues, really determining the scope of environmental liability, have not been addressed by the Directive. One problem is that the scope is limited to damage to the soil and underground water in specifically designated areas; another is that, for example, the question whether compliance with a permit excludes liability has been deferred to national law. Also the question whether the liability of an operator should be supplemented with mandatory solvency guarantees (like compulsory insurance) has not been decided by the Directive, but left to national law. The same is the case for the crucial question how causation will be determined.\textsuperscript{77}

Those examples show that, on the one hand, the costs of full harmonisation are apparently higher than expected; on the other hand, this equally implies that the expected transaction cost reduction cannot be realised in many cases.

There is therefore probably more to be expected from the bottom-up scholarly harmonisation projects than from the top-down approach followed by the European Commission, forcing member states to implement specific directives in the national legislation.

7 MINIMUM LEVEL OF PROTECTION

7.1 No Economic Argument

Leaving the economic criteria for harmonisation aside, we could wonder whether other, non-economic arguments, could be advanced in favour of the harmonisation of EU tort law. Some may indeed argue that it is not economic arguments that demand the harmonisation of tort law in Europe but, for example, the desire to provide a minimum level of protection to accident victims in the whole of Europe.


At first sight this idea of guaranteeing a minimum quality to European victims of accidents sounds appealing. However, we should then realise that, as argued below, a minimum level of protection may be imposed upon citizens, even if this would not correspond with their preferences. This amounts to paternalism. Moreover, if that were a political desire it would have been far more important to provide, for example, minimum social security, basic health care and harmonisation in the area of minimum wages. Those areas are traditionally still very sensitive and related to national sovereignty, and Europe has not intervened in them yet. It would therefore be strange to harmonise tort law on the basis that European citizens should receive adequate protection, when such a minimum protection is not provided for more basic needs.

Moreover, it is questionable whether tort law itself is an appropriate instrument to provide this minimum level of protection. The human rights arguments for harmonisation may be quite valid, but it can hardly be seen how these could be applied to the area of tort law.\textsuperscript{78} Other instruments, based on the European Convention on Human Rights, would be more appropriate to provide this minimum level instead of the top-down harmonisation approach followed by the European Union.

### 7.2 Example

There are probably areas in tort law where the differing preferences are much stronger than the reduction of transaction cost benefits. The example of the amounts awarded for non-pecuniary losses may provide an illustration. Many have argued that there are still considerable differences between the member states in that respect.\textsuperscript{79} However, it is relatively difficult to argue that these differences themselves lead to huge economic problems. We could argue that these differences reflect differing national preferences and therefore there seems to be no point in favour of harmonisation in this area. In this case the differences are probably not just differences in legal technique and so cannot be reduced to pointless incompatibilities. It is therefore difficult to see any transaction cost benefits from harmonisation there, whereas the disadvantages (in terms of not respecting national preferences) under harmonisation would be huge. From an economic perspective there would thus not be an argument to harmonise, say, the specific amounts awarded in the various cases of non-pecuniary losses.

\textsuperscript{78} Unless the principle of equality is used as a justification for the harmonisation of tort law: see Spier and Haazen (n 55) 479–80.

Serious differences still exist, both with respect to the question of whether some victims (and their relatives) are entitled to compensation for non-pecuniary losses, but also as far as the amounts awarded are concerned. Some have therefore argued that it is unacceptable that within Europe a victim who, for example, suffers the loss of an arm would receive less in, say, Portugal than in, say, Germany. They implicitly argue that there is no reason to treat those victims differently and that the call for harmonisation of the amounts awarded for non-pecuniary losses is justified.

What can, again, be said about this argument from an economic perspective? First, differences in amounts awarded for non-pecuniary losses are certainly not pointless, but may reflect differing preferences of the citizens in the various states. In this respect we should, second, also remember that Coase taught that every increase in protection can always be passed on via the price mechanism. That is, if, for example in the area of product liability, we would argue that the Portuguese should pay higher amounts for non-pecuniary losses for victims of product accidents, this would lead to an increase in prices. Indeed, the manufacturer will add the additional damage costs to the price of the products. The effect, therefore, is that consumers pay a higher price for the protection awarded. It may well be that consumers in Portugal are not willing to pay this higher price. A European intervention forcing all Europeans to come up to, say, the German level, would therefore amount to paternalism.

Some argue that given the increasing mobility in Europe today, it cannot be understood why, say, a German professor would receive less for his pain and suffering if he were to have an accident in Portugal rather than in Germany. That fact is, again, hardly an argument in favour of harmonisation. Indeed, the fact that the Portuguese would choose a lower level of damages awards for pain and suffering than the

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80 For an overview of the current differences between the member states as far as the amounts awarded for pain and suffering are concerned, see W.V. Horton Rogers (ed), Damages for Non-Pecuniary Loss in a Comparative Perspective (Springer, Vienna 2001).


83 Magnus and Fedtke (n 81).
Germans reflects differing preferences. There is no reason why the Portuguese would – paternalistically – have to come up to the German level, just to please the German tourist. The latter can, moreover, being aware that they will not enjoy the same level of protection abroad as in Germany, seek additional protection – if they so desire – in the form of a voluntary first party insurance. Such insurance for tourists is widely available on the market. The mere fact of tourism and mobility can therefore hardly be considered as an argument in favour of harmonisation.

Contrary to what is sometimes assumed, there may be hence very clear reasons why some countries have lower or higher levels of compensation for non-pecuniary losses than others. If this corresponds to differing preferences, one can, at least from an economic perspective, see no need for a general harmonisation merely based on the reason that the existence of such differences is ‘unjust’. The example, again, shows that harmonisation cannot be addressed in black and white statements. Some issues may be harmonised at relatively low cost, whereas others (which are closely related to preferences) can be differentiated. In the area of compensation for non-pecuniary losses, harmonisation could lead to a paternalistic measure and to disrespect for the preferences of citizens. Even a call for the need to provide the same minimum protection to all accident victims within Europe can hardly justify such a paternalistic measure. However, with this statement and the reference to the need for providing a basic level of victim protection, we have left the area of economics. Indeed, the reader should recall once more that in this chapter I have only provided ‘one view of the cathedral’.

It is still thinkable that other, non-economic arguments would be advanced to argue that a harmonisation of, for example, damages for pain and suffering would still be necessary in Europe, for instance to guarantee the minimum level of protection to all European victims. Those who would advance this argument should, however, realise that Europe today does not provide such a minimum protection to accident victims either. Social security is to an important extent not yet harmonised. Also the compensation after industrial accidents or occupational diseases can still be very different between the member states. If we would therefore argue that a minimum level of protection of accident

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84 For a similar analysis, see Ton Hartlief, ‘Comments on Magnus, U, “Towards European Civil Liability”’ in Faure, Smits and Schneider (n 81), 225–30.
85 See also Hartlief (n 84) and Ton Hartlief, ‘Op weg naar een Europees aansprake-lijkheidsrecht?’ (2002) 39 Tijdschrift voor Privaatrecht 945–53.
victims is necessary, it seems better indicated to focus on those areas first instead of pleading for a harmonisation of compensation for non-pecuniary losses.

8 POLICY

From the above economic analysis, it follows that arguments in favour of centralisation of tort law at EU level are in fact relatively limited. There would be arguments in favour of European tort law, (1) if inefficiencies were created by national tort law so that damage could be externalised to other countries or, (2) if it could be established that states would attract industry by their lenient tort law standards. The latter is, however, unlikely since states would, on the contrary, be more likely to enact legislation to protect victims of accidents within their own jurisdiction with high standards. However, there may be transaction cost savings if European intervention were able to create legal certainty and achieve full harmonisation. Other arguments, such as the need to create a ‘level playing field’ or ‘the harmonisation of market conditions’ cannot, at least from an economic perspective, justify centralisation.

To some extent it was indicated that the EU action in the domain of tort law, for example concerning product liability, does diverge from the economic criteria. Indeed, we notice that many of the harmonisation efforts do not fit into the economic theory of centralisation and would hence, at least from an economic perspective, not be considered as promoting social welfare. If a certain legislative action cannot be said to promote public interest, public choice scholars would ask the question whether the legislation favours special interest groups. We can generally hold that the lack of transparency at the European level is a highly useful cover for lobbying activities. In fact, the desire to create a European liability regime sometimes simply serves the interests of industry and is the result of lobbying. The question has inter alia been asked whether the Environmental Liability Directive was to some extent the result of lobbying by interest groups.

87 De Smedt and Faure (n 27) 788–9.
Some have argued that the comparative lawyers themselves can be considered as a lobby group. Harmonisation efforts will undoubtedly serve their interests since harmonisation requires knowledge of the various legal systems that need to be harmonised. A call for harmonisation does undoubtedly create a demand for comparative lawyers and may hence serve their interests.88

Finally, in the context of public choice analysis, we should also mention the interests of the European bureaucracy itself. Public choice scholarship has indicated that bureaucrats also have an interest in centralisation. Shifting powers to the European level will increase the budgets and hence the importance of the bureaucrats, and may therefore explain the tendency of the European bureaucracy to increase rather than to decrease competences at EU level.89 However, more recent studies analysing preferences of EU bureaucrats, show that European Commission officials do not systematically prefer more supranational decision-making. They only do that to the extent that this would improve public good provision.90

This may generally apply to the domain of tort law as well. Until 1985 Europe had done relatively little as far as the harmonisation of private law was concerned (because differing legal cultures hampered it). Perhaps a European Product Liability Directive, although it did not fulfil the economic criteria for centralisation, might have served the interests of the Brussels bureaucracy to show that Europe could bring about a piece of legislation in an area which is considered important by many lawyers. Hence, the fact that the Commission wanted, for example, a European Product Liability Directive may to some extent also simply have been due to the prestige that this Directive, as one of the first in the area of private law, would give the European Commission.

9 CONCLUDING REMARKS

This chapter has provided economic criteria for the harmonisation of tort law. Whereas we can often notice a general enthusiasm, at least in the

88 So Ogus 1999 (n 10) 405 and 2001 (n 10) 28–32, as well as Van den Bergh 2000 (n 3) 449.
past decades, among private lawyers in favour of increasing harmonisation of rules of private law (such as tort) at the EU level, the starting points of the economic approach are slightly different. Economists stress that differences as such are not a bad thing at all, provided that those differences also reflect the differing preferences of citizens.\(^9\) If that is the case, the starting point is that these differences should be respected and that they may even contribute to an increased quality of the legal system because legal systems will compete to provide the best legal order to their citizens.

However, it was equally indicated that, in some cases, this basic idea of competition between legal orders may not provide optimal outcomes. The economic literature makes clear that there may be an argument in favour of harmonisation where transboundary externalities exist, but this does not justify a total harmonisation of tort law. It merely calls for a regulation of transboundary accidents at the centralised level. The other economic argument in favour of harmonisation is the risk of destructive competition, also referred to as the ‘race to the bottom’. However, it seems very unlikely that within the European context states will compete in order to attract industry with lenient tort laws. There is no empirical evidence at all that currently European member states would have engaged in such a race to the bottom with an inefficient tort law. It is much more likely that a race to the top would take place, since states would probably prefer to protect those of their national citizens who might also suffer accidents.

Moreover the traditional ‘economic’ European argument – that harmonisation of the conditions of competition is necessary in order to create a level playing field – was critically discussed and rejected as being wrong. This argument has been used in Europe for a long time. To some extent this was understandable, since the argument for the ‘harmonisation of market conditions’ was necessary to give Europe competencies in specific matters. However, it is very doubtful whether such harmonisation of market conditions is desirable, since this could justify a (largely unnecessary) harmonisation of all sorts of legal rules, because all kinds of legislation could arguably have an influence on market conditions. Moreover, the initiatives that Europe has taken so far with respect

\(^{9}\) Some lawyers also follow this line of reasoning. See eg Jan Smits, *The Good Samaritan in European Private Law* (Kluwer, Deventer 2000) 43, who presents ‘In praise of Diversity’.
to tort law have not proven to be a major success. All legal writers agree, for example, that the European Product Liability Directive could never lead to the harmonisation of market conditions. Moreover, the European directives generally seem to have the problem that they follow a ‘top-down’ approach, whereby the European regime is mandatorily imposed upon the member states, sometimes as an additional layer of protection, such as in the case of the European Product Liability Directive. This should lead to a critical review of the harmonisation efforts undertaken by the European Commission. Unfortunately, the Commission seems only interested in promoting further harmonisation instead of focusing on less (and maybe better) harmonisation.92

It is important to stress that from an economic perspective probably the most important reason in favour of centralisation of tort law is the potential for reducing transaction costs. To some extent we can certainly argue that various tort rules in the member states reflect similar preferences and only differ as a result of differing legal techniques. If it were possible to align rules of tort law that reflect similar preferences, this could certainly be considered a gain. That is precisely the approach chosen in a variety of (mostly privately initiated) academic projects on harmonisation of tort law. In most of these projects the academics involved analyse the existing differences between the various aspects of tort law in the member states and try to find a common denominator. This approach seems to be more promising than that chosen by the European Commission. That top-down approach of imposing directives on member states has so far not been very successful. The approach chosen by the academic groups focuses on the search for an *ius commune* and can therefore be called ‘bottom up’. If these groups succeed in showing that some differences are merely of a technical nature and can thus be considered as pointless incompatibilities which do not touch upon or relate to differing preferences, then this harmonisation approach of searching for a common denominator may well prove to be more successful than the approach chosen by the European Commission so far.

The conclusion at the normative level, however, should not necessarily be that there is no need for any European action at all with respect to tort

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However, the Commission still seems to be stuck in the old jargon of the ‘harmonisation of conditions of competition’, even though that seems to be a weak reason for harmonisation. There may be other, non-economic, reasons to justify harmonisation. However, then these goals and expectations should be spelled out more specifically. Even those who dream of a European tort law as a political ideal can still benefit from economic analysis. Economics can help to show whether the methods of harmonisation chosen in a particular case can lead to the goals advertised. Moreover, those who blindly follow an unbalanced harmonisation dream should also be aware of the fact that in some cases they may (probably unknowingly) be instruments in the hands of powerful lobby groups who can benefit from harmonisation. In this respect the important lesson from the public choice school that whenever inefficient regulatory measures are enacted there is usually a special interest group that benefits from this action, should not be forgotten.

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93 Compare Spier and Haazen (n 55) 477: ‘Nor is convergence or unification of private law ever strictly speaking necessary … If we favour convergence of European private law, we deem it simply desirable, perhaps highly desirable, but nothing more.’ This desirability of the harmonisation of private law in Europe is, however, highly criticised – *inter alia* – by Smits (Jan M. Smits, *Waarom harmonisering van het contractenrecht (via beginselen) onwenselijk is* (2001) 3 *Contracteren* 73–4).