



European Policy & Open Markets

# Swiss – EU relations: ***it is now time to act***

February 2, 2022

## At a glance

Swiss business is calling on the Federal Council to unblock European policy. Waiting until after the elections in 2023 will cause too much damage to Switzerland as a business location. It is now time to act in order to stabilise the bilateral agreements.

## Executive summary

The Swiss business community has argued forcefully in favour of the bilateral agreements, which are increasingly eroding after negotiations on the framework agreement failed. The medtech sector, banks, electricity suppliers and the Swiss research sector are directly affected. Measures in these four areas are a priority. At the same time, the Swiss government is called on to make fundamental decisions on European policy. The institutional questions must be clarified. Here, the Swiss economy needs the market integration agreements to be synchronised with the development of the relevant EU acquis and a procedure for dispute settlement. Sectoral solutions in combination with general rules is one possible approach.

### Positions *of economiesuisse*

- The erosion of the bilateral path is hurting Switzerland and the EU as a business location. It also harms the common strategic interests of both partners.
- The Swiss government is called on to act now to unblock European policy and ensure pursuit of the bilateral approach. The Swiss business community rejects any further delay.
- Solutions should be prioritised in the areas of banking institutions and stock exchange, medtech, research and energy supply.
- Swiss companies need legal certainty in their economic relations with the EU. Therefore, clarification of institutional aspects is essential. A sectoral approach combined with general rules is a possible solution.
- Additionally, measures are needed to strengthen the export economy.



## Switzerland's strategic *initial position in European policy*

Since the failure of the Institutional Framework Agreement on 26 May 2021, Swiss European policy has been in crisis. This has manifested itself in particular in the following areas:

- The EU refuses to update the bilateral agreement on technical barriers to trade.
- The EU refuses to associate Switzerland with the EU's Horizon Europe research framework programme (2021-2027) in accordance with the bilateral research agreement.
- All negotiations on bilateral market integration agreements are blocked.

The erosion of the bilateral market integration and cooperation agreements has thus begun and is causing damage (see below "Blockade in European policy hurts the economy"). For Switzerland, the strategic initial position is as follows: despite the considerable potential for damage, the Federal Council does not have a concrete plan on how to minimise the damage or how to proceed with its European policy. It was announced that after an assessment of the bilateral situation over the next two years, the Swiss government would seek a political dialogue with the EU. However, such a long timeframe is not in the interests of the Swiss economy. Further measures by the EU against Switzerland's

economic interests are possible. After the meeting with Federal Councillor Ignazio Cassis on 15 November 2021, the EU demanded a commitment and a binding roadmap from the Swiss government on how to proceed by the next meeting. This had to be postponed without a new date set after the cancellation of the World Economic Forum WEF.

Switzerland is facing major strategic challenges.

#### SWOT analysis from a Swiss perspective

Strengths	Weaknesses
<ul style="list-style-type: none"><li>• Resilient, innovative export economy; Swiss economy has weathered the pandemic well so far</li><li>• Switzerland remains an important investor in the EU and the fourth most important trading partner</li><li>• The bilateral agreements are supported by the population</li></ul>	<ul style="list-style-type: none"><li>• Federal Council does not have an alternative plan</li><li>• Erosion of the agreement on dismantling technical trade barriers</li><li>• No association of Switzerland with Horizon Europe; no negotiations on an electricity agreement</li></ul>
Opportunities	Threats
<ul style="list-style-type: none"><li>• Neighbouring countries (Austria, Germany, France) support good relations between Switzerland and the EU.</li><li>• Switzerland and the EU share the same values, interests and political views in many areas (including the WTO, export control, sanctions)</li><li>• Switzerland is an important research location in Europe with strong universities</li></ul>	<ul style="list-style-type: none"><li>• Erosion of market access affects 50 percent of all Swiss exports (i.e. 20 percent of Swiss GDP is negatively affected)</li><li>• EU lets the Bilateral Agreements I erode completely. Switzerland's status is as a third country in research programmes; blocked equivalence recognition in the financial sector, data protection, etc.</li><li>• Without an electricity agreement, stability of the electricity grid and security of supply in Switzerland are at risk</li><li>• New EU legal development leads to non-tariff trade barriers</li></ul>

Source: economiesuisse (own representation)



## Blockade in European policy hurts ***the economy***

### **Erosion of the agreements**

Due to the EU Commission's unwillingness to adapt the existing bilateral market integration agreements to the changes in the EU acquis, the erosion of Switzerland's ability to participate in the European single market is already directly and concretely apparent in various areas. It affects in particular local SMEs and innovative industries with high value added and a high export share. MNEs with large production facilities in Switzerland are also affected.

### Financial services

- Non-recognition of stock exchange equivalence by the EU

Non-recognition of the equivalence of Swiss stock exchange regulation by the EU (since July 2019) affects the Swiss stock exchange SIX and companies listed on the Swiss stock exchange. The Federal Council's protective measure has so far been able to prevent the migration of trading in Swiss equity securities from Switzerland. On the other hand, non-recognition has negative effects on the activities of EU companies listed in Switzerland.



- Non-recognition of equivalence in financial market regulation/comprehensive revision of EU financial services law in the area of the third-country regime complicates market access for banking services

The ability of Swiss banking institutions to provide services from Switzerland to their clients in the EU is increasingly restricted due to the blocked equivalence recognition procedures. In addition, there is a trend in the EU to make cross-border business more difficult for banks from third countries, and thus from Switzerland. The partial relocation of certain banking services to the EU cannot compensate for the probable damage due to the lack of market access. Moreover, relocations harm the Swiss financial centre.

## Technical barriers to trade

- Blocked update of the Mutual Recognition Agreement (MRA) for medical devices

The Swiss medtech industry is already affected. Since 26 May 2021 it has been obliged to export its products to the European domestic market in accordance with third-country conditions. The one-off adjustment costs for the industry are estimated at 110 million Swiss francs and the recurring annual costs at about 75 million Swiss francs. Since medical devices from the EU must also be imported into Switzerland on third-country terms, problems arise as the import of small volumes is not profitable. About an eighth of all medical devices currently imported from the EU could be affected. Simplification of the import of EU products, temporarily adopted by Switzerland at the end of December 2021, is therefore appreciated by the industry.

- Predictable blockage of further industrial products

In 2023, a machinery regulation will replace the existing machinery directive and will be applicable from 2025/2026. From this point, machinery from Switzerland covered by the regulation will be treated as products from a third country. In practice, only a minority of machines will be subject to third-party certification. Nevertheless, the one-off adaptation costs are estimated at 300 million to 700 million Swiss francs and the annually recurring costs at 250 million to 500 million Swiss francs. The revised EU general pharmaceuticals

legislation is scheduled to come into force from 2025/2026. The Swiss pharmaceutical industry will be particularly affected by this. One-off adjustment costs of 450 to 900 million Swiss francs and annually recurring costs of 250 to 700 million Swiss francs are expected. In summary, the industries concerned face additional annual costs of between 0.6 billion and 1.3 billion Swiss francs as a result of the non-actualisation of the MRA.

## Research and operational innovation

Switzerland lacks full association with the EU research programmes Horizon Europe, Euratom, Digital Europe and ITER, leading to disadvantages for Switzerland as a location for research and innovation. Switzerland is excluded from a third of all research programmes, while the others require direct funding by Switzerland. In addition, project management by Swiss institutions is excluded – a very important area for leading research institutions. Business innovation funding also faces negative consequences. For example, start-ups and SMEs no longer receive contributions for international innovation projects.

## Electricity sector/security of supply

The EU refuses to conclude a bilateral agreement with Switzerland in the area of electricity. The exclusion from the European electricity market leads to steadily rising costs of about 120 million Swiss francs per year. By 2030, these costs could amount to more than 300 million Swiss francs. In addition, supply bottlenecks in the winter half-year and an increased risk of blackouts must be expected from 2025, primarily as a result of insufficient domestic electricity production. The costs of a blackout are estimated at 4 billion Swiss francs per day and would affect the entire economy. In addition, grid stability is no longer guaranteed, as the EU wants to exclude Switzerland from the European coordination platforms for electricity and ENTSOE (European Network of Transmission System Operators for Electricity).





## Common economic interests ***of Switzerland and the EU***

The bilateral market integration agreements are of great economic importance to both the EU and Switzerland.

### Agreement on the free movement of persons

Currently, more than 1.4 million EU citizens live and work in Switzerland. Each day, 340,000 come to Switzerland to work as cross-border commuters. They generate an annual average income of 27 billion Swiss francs and thus generate important tax revenues in the near border regions. The generally well-qualified European professionals contribute significantly to the competitiveness of the Swiss economy.

### Agreement on overland transport

Thanks to the overland transport agreement, Switzerland is optimally integrated into the European transport network. This benefits the Swiss logistics sector the industrial location and also the EU: 900,000 European lorries pass through Switzerland every year without any major delays. There are also positive environmental aspects, as the agreement makes a significant financial contribution to the shift of transalpine freight transport from road to rail.

## Agreement on air transport

The air transport agreement has led to a greater choice of flight connections, particularly to the EU, and to lower prices. This is of great importance for international companies in Switzerland. Zurich airport, as an international hub, has also benefited significantly from its participation in the European aviation area. For its part, the EU benefits greatly from the use of Swiss airspace, which is one of the busiest in Europe. Over the last 11 years, an average of 1.2 million aircraft movements per year were registered in Switzerland. Half of these were transit flights.

## Technical barriers to trade

The MRA reduces the time and cost of commercialising products in the foreign market concerned and has allowed Swiss industrial companies to integrate successfully into regional value chains. Thus, they have become important suppliers to EU companies. Thanks to mutual market participation and harmonised industrial standards, Switzerland and the EU neighbouring regions have merged to become Europe's leading industrial location. Companies on both sides benefit from this. It also strengthens product diversity in Switzerland (e.g. in the field of medicine). For EU manufacturers of products with small sales volumes in Switzerland, the non-updating of the MRA creates a new trade barrier, affecting about an eighth of all medical devices sold in Switzerland.

## Research and innovation

The EU's research programmes make an important contribution to the innovative capacity and ultimately the international competitiveness of Europe as a whole. With the ETH in Zurich and the EPFL in Lausanne, two of the

world's top 20 universities could in principle participate in Horizon Europe. Moreover, more than 40 percent of all researchers at Swiss universities and research institutions are EU citizens. Without close networking of its research institutions, Europe has no chance of maintaining its position globally vis-à-vis the dominant US and the increasingly strong Asian research institutions (China in particular). Business innovation in Europe is also suffering. In international comparison, Switzerland has a very high density of innovative companies.

## Electricity

A total of 41 unregulated power lines connect Switzerland with the EU's electricity grid. Ten percent of the electricity transit in Europe is flowing through Switzerland. Neighbouring countries benefit greatly from this. Up to 30 percent of the electricity traded between Germany and France is routed through Switzerland. Such transit flows will continue to increase as a result of the energy transition in Europe and put additional strain on the transmission grid. In order to maintain sustainable stabilisation of the European electricity grid, the inclusion of Switzerland is in the interests of both sides. Switzerland's hydropower plants could also play an important storage function in the European electricity grid and balance the fluctuations from renewable energy sources. A blackout in Switzerland would inevitably also affect the electricity grids of neighbouring regions and cause high costs.

## Mutual interests prevail

A stable and close relationship between Switzerland and the EU is in the interest of both sides, not only for individual sectors and policy areas, but in general. Fragmentation of European economic research and supply networks weakens the competitiveness and resilience of the entire continent in the mid and long term. In addition to the harmful erosion of further parts of the market integration and cooperation agreements through their non-application by the EU, the missed opportunities due to the lack of new agreements should also be emphasised. These concern all key policy areas, such as climate and health policy, digitalisation and financial services.



## Measures taken by Switzerland ***to minimise economic damage***

### Stock exchange equivalence

Since the EU still does not recognise Swiss stock exchange regulation as equivalent, the Federal Council decided on 17 November 2021 to extend the emergency ordinance for the protection of Swiss stock exchange infrastructure, which expires at the end of 2022, by six months and adopt it into ordinary law. With this protective measure, the Federal Council has so far achieved its goal of preservation of the functioning of the Swiss capital market. The business community supports this approach. However, from the perspective of the financial industry, the strategic goal must continue to be the unrestricted equivalence recognition of Swiss stock exchange regulation by the EU Commission. Switzerland fulfils all technical requirements in this respect.

### Medical devices

As a countermeasure to the EU Commission's decision of 26 May 2021 to no longer recognise Swiss medical devices as equivalent (third-country regulation), the Federal Council amended the Swiss Medical Devices Ordinance (MepV) in order to ensure security of supply and market surveillance in the area of medical devices in Switzerland. However, the Federal Council had additionally tightened the law adopted from the EU's MDR requirements ('Swiss Finish').

This created high import hurdles for foreign manufacturers. The industry clearly rejected this: the substitute measures in the area of medical devices, and in particular 'Swiss Finish', are in violation of the existing MRA, do not achieve their purpose and are counterproductive in some cases. Fortunately, a pragmatic solution was found with the industry at the end of 2021, which not only helps the domestic medtech industry, but also Swiss healthcare.

## Cohesion contribution

The release of the second cohesion contribution was considered by the EU Commission a prerequisite for opening negotiations on Switzerland's participation in Horizon Europe. By releasing the cohesion contribution, already approved in 2019, without conditions, Switzerland has attempted to break the spiral of linking unrelated topics in the bilateral relationship. The Federal Council approved the associated Memorandum of Understanding with the EU on 24 November 2021. The business community supports this approach. However, the hoped-for unblocking of Switzerland's association with the European research framework programme Horizon Europe has so far failed to materialise.

## Horizon Europe

On 17 September 2021, the Federal Council decided to introduce transitional measures until the targeted association of Switzerland; they involve the Swiss National Science Foundation, Innosuisse, the European Space Agency ESA and other actors. The proposed transitional measures were submitted to Parliament with a supplementary notification on the budget 2022 in the winter session 2021. In addition, on 20 October 2021, the Federal Council instructed the Federal Department of Economic Affairs, Education and Research to ensure funding for Swiss participants in those parts of Horizon Europe that are open to them. Further supplementary and compensatory measures will be examined until 2023 and will take effect if Switzerland cannot participate in Horizon Europe as a full member. The action plan and the chronological order are supported by the business community. However, the measures cannot fully compensate for the opportunities that full association reserves for a country's researchers and companies. For this reason, association remains the main objective.

## Electricity crisis provision

As of 1 December 2021, the Penta countries (Belgium, Germany, France, Luxembourg, the Netherlands and Austria) signed a Memorandum of Understanding on risk preparedness in the electricity sector with Switzerland. This puts Switzerland in a better position to cooperate with neighbouring countries in the event of supply shortages. This is a positive development, but it is limited to crisis situations and cannot replace full participation in the European electricity market.





## After the breakdown of negotiations: ***specific demands of Swiss business***

### For an active European policy

economiesuisse, in cooperation with its members, has drawn up key demands for Switzerland's European policy. The central question is what the economy will need from European policy in the next two to three years and where exactly the priorities must be set. In order to achieve timely solutions in the prioritised areas, action must be taken now. A policy of 'wait and see' until after the federal elections in 2023 is clearly not acceptable. After unilateral termination of the negotiations on the Institutional Framework Agreement, the Federal Council is now responsible for ensuring the future viability of European policy. The demands are divided into four thematic areas:

1. Decisions of principle
2. Priority areas and mitigation measures

3. Institutional demands

4. Call for a targeted structural policy to strengthen the export economy

## **Decisions of principle by the Swiss government on the unblocking of European policy**

It is time to act now. A stalling of European policy will clearly put Switzerland at a political and economic disadvantage. Therefore, the Swiss business community demands that the Federal Council take immediate action to unblock its European policy. The pursuit of the bilateral approach is a recognised and widely supported objective of Swiss European policy – the EU has also expressed its interest in continuation of the bilateral path on several occasions. Unblocking requires three fundamental decisions to be made by the Federal Council:

### **1. Continuation of the five market integration agreements**

- The Federal Council faces a basic question on the continuation of the five existing market integration agreements. If it wants to continue with these agreements, it must make a clear commitment to resolution of the institutional issues with the EU. After all, there has not been a single indication since 2018 that the EU is willing to extend the existing market integration agreements without clarification of the institutional questions.
- If the Federal Council decides not to continue with the market integration agreements, it must develop an alternative European policy for the regulation of economic relations. This must also include an updated assessment of a comprehensive free trade agreement, with the advantages and disadvantages in terms of state policy and the economy.

### **2. Active development of a common agenda**

- Based on the common strategic interests of Switzerland and the EU, the Federal Council must quickly develop an agenda and a proposal for the

EU. It should indicate both short-term priorities for the next two years and medium-term perspectives.

- With a view to the medium-term timeline of this agenda, the economic issues of the bilateral path should be defined from the perspective of the fundamental, strategic goals of both sides. The Federal Council and the EU should define in concrete terms how they intend to cooperate on common strategic interests in industrial and financial sectors, research and innovation, infrastructure (land and air transport, electricity supply) and climate and health policy.

### 3. Active assertion of interests

- The Swiss business community demands the continued application of all bilateral agreements already in force (*pacta sunt servanda*).
- If the EU continues to refuse to apply the existing agreements, all legal measures must be examined and used. This includes legal support for companies and organisations willing to take legal action to defend themselves against discriminatory measures by the EU. In the event of continued or future discrimination, Switzerland should also make use of the existing option to take legal action before the European Court of Justice or the WTO.

## Priority areas and mitigation measures

### Priority areas

For *economiesuisse*, solutions in four areas are a priority for the next two years:

- Equivalence recognition in financial regulations for third countries (stock exchange regulation, financial services) and market access for banking and securities services
- Measures to reduce technical trade barriers in medical products, other industrial products and production processes for medicines
- Research and industrial innovation promotion

- Electricity market and supply security

The blockage in these four areas harms Swiss companies significantly as well as their suppliers and customers in the EU. Switzerland as a research location is also seriously damaged. The economic harm has already occurred and will continue to occur over the next two years if the EU continues its course of non-application of existing agreements. This damage cannot simply be passively accepted, but must be minimised through a package of measures.

## Mitigation measures in the priority areas

The immediate and direct harm resulting from Switzerland's unilateral termination of negotiations must be minimised as quickly as possible through the following mitigation measures:

- **Swiss stock exchange and financial sector:** The fiscal and regulatory framework must be improved to strengthen its international competitiveness. Furthermore, improvements in cross-border market access for banking and securities services from Switzerland should be achieved through practicable approaches in accordance with the Federal Council's financial market strategy (December 2020).
- **Medical devices:** No rules will be introduced to MepV that go further than the MDR and render trade more difficult (no 'Swiss Finish').
- **Research and business innovation promotion:** If the EU continues to refuse Switzerland association to the Horizon Europe research framework programme, Switzerland should invest additional funding in research and innovation promotion over the next 10 years. These funding resources are to be used to promote projects both in Europe and in third countries (for projects with a sufficient link to Switzerland). In-house innovation promotion must be rapidly expanded in cooperation with the leading business locations.
- **Energy policy:** Without an electricity agreement with the EU, Switzerland needs a fundamental adjustment of its energy strategy. In addition, it needs investment in grid stability.

These mitigation measures must be introduced now, as it will take several years before European policy is fully deblocked.

Furthermore, in the area of free movement of workers, the business community is calling for efficiency gains in wage protection and accompanying measures by means of digitalisation. Digitalisation should simplify registrations, verification and controls, increasing the effectiveness of the measures and reducing costs. For instance, thanks to digitalisation, the pre-registration period for EU companies that offer services in Switzerland can be shortened considerably.

## **Institutional demands: economy needs legal certainty**

Swiss companies need legal certainty in terms of economic relations with the EU. Thus, clarification of the institutional aspects is essential.

### Sectoral approach in combination with general agreement to regulate market participation

- It is the Federal Council's responsibility to strive for and negotiate institutional solutions with the EU. Here, there are several possibilities.
- Since the institutional rules concern only the existing five market integration agreements (free movement of persons, overland transport, air transport, technical barriers to trade, agriculture), these can be regulated through specific agreements.
- In addition, basic rules applicable to all market integration agreements can be laid down in a general market participation agreement.

### Synchronisation of market integration agreements and equivalence recognition

- For companies, the timely updating of the market integration agreements to the relevant EU law is central to participation in the internal market. Problems arise for companies if the EU blocks the updating process.

- This synchronisation is particularly important in the case of technical trade barriers and land and air transport.
- Timely recognition of Swiss rules is also important in equivalence procedures.

## Dispute resolution procedure in the interests of Switzerland

- A dispute settlement mechanism is equally important: if Switzerland and the EU cannot reach political agreement on a contentious issue, a balanced legal procedure to settle disputes is necessary.
- Politically motivated retaliatory measures by both sides at the expense of companies must be avoided at all costs.

## Call for better framework conditions for the export industry

Since the export economy is affected the most by the continued EU irritants, structural measures are needed to strengthen the export industry in a targeted manner. This becomes all the more urgent the longer the EU refuses to apply existing agreements. For Switzerland's foreign trade, in addition to relations with the EU, multilateralism (WTO) and bilateral relations with other important trading partners are also strategically highly relevant. Among the latter, the US and China in particular are likely to continue to gain in importance. On these grounds, the following fields of action can be outlined:

- Improvement of the good framework conditions for taxation in Switzerland as a business location, taking into account OECD standards.

- Consistent expansion of Switzerland's free trade network: conclusion of new agreements (in particular Mercosur, Malaysia, Vietnam, US, India, Australia) and modernisation of existing free trade agreements (in particular Canada, China, Mexico, Japan, South Korea). In the case of free trade agreements, the linking of rules of origin (cumulation) with partner countries should be sought.
- Agreements in the field of digital trade (multilateral and bilateral, stand-alone or as part of free trade agreements).
- Prompt and proactive exploration of participation in plurilateral free trade areas with a focus on the Pacific/Asia/Africa (e.g. RCEP, CPTPP, AfCFTA).
- Participation in relevant plurilateral and trade facilitation WTO initiatives (e.g. Healthcare Products Initiative).
- Reduction of non-tariff trade barriers through global harmonisation (e.g. GHS).
- Greater emphasis on foreign trade priorities: as Switzerland depends on a strong export economy, purely domestic interests must be considered to a lesser extent in future, such as agricultural protectionism, renunciation of technology bans (e.g. genetic engineering bans), renunciation of unilateral measures ('Swiss Finish', food regulations), renunciation of export bans/restrictions (e.g. plant protection products), examination of trade union power and financial interests, to name just a few.
- Rapid implementation of the agreed abolition of all import duties on industrial products.
- Increased attractiveness of Switzerland as a business location for foreign direct investment. Renunciation of state investment controls and other protectionist measures.
- Digitalisation of administrative procedures in order to reduce costs for export companies.
- Expansion of export promotion.
- Further development of consular protection for companies.



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