

**January 2005**

## **ETNO Reflection Document on the European Commission Document on the draft Directive on the New Legal Framework for Payments in the Internal Market Version 5.0 (26/11/04)**

### **Executive summary**

ETNO is grateful to the European Commission for the opportunity to follow the debate on the New Legal Framework for Payments in the Internal Market within the Payment Systems Market Group and being able to provide comments on the last version on the future Directive.

ETNO members welcome the Commission's attempts to clarify and update the existing framework and develop an efficient market for payments services in the EU that fully takes into account new technologies. ETNO appreciates the Commission's efforts throughout the consultation process to better understand telecommunications operators' business activities, given the risk that this proposal may have on the provision of third party services offered by telecommunications operators and the extensive implications for existing and future business activities this were to be the case.

Against this background, ETNO believes that it is crucial that the final Commission proposal fully follows the core principles of proportionality and technological neutrality. It should also strive to ensure a clear separation between the areas of application of the E-Money-Directive and the New Legal Framework for Payments, to allow for the rapid and successful development of truly pan-European electronic payments (mobile payments, micro-payments and those over the Internet) services.

### **Introduction:**

As the representative of 41 major European telecom operators, ETNO welcomes the opportunity offered by the European Commission's consultation process within the Payment Systems Market Group to provide the Commission services with an initial overview of the potential impact of version 5 (26/11/04) of the draft Directive on a

New Legal Framework for Payments in the Internal Market (henceforth “the Directive”) on business activities of telecommunications operators. ETNO aims to provide both general and specific comments on the issues arising from the current draft proposal in order to ensure a better understanding of the European Commission of the potential impact of these proposals on the development of new and innovative payments services.

## **General remarks:**

- ETNO welcomes the Commission’s attempts to clarify the regulatory framework for payment services in the EU and the Commission’s recognition of the need to embrace new technological developments in the development of an efficient market for payments in the EU.
- ETNO members are, however, strongly concerned about the possible impact of the draft Directive on existing and future business activities (both core and ancillary activities) of electronic communications operators. ETNO sees that there is a risk that third party services offered by telecommunications operators could fall under the scope of the draft Directive, leading to extensive implications for existing and future business activities.
- ETNO believes that the development of the new framework for payments in the Internal Market must ensure a proportionate and level playing field, with due regards to the principles of technological neutrality allowing for the development of new, efficient and innovative payment mechanisms, such as electronic payments, mobile payments and micro-payments over the Internet.

## **Understanding electronic communications services:**

ETNO believes that it is crucial for the Commission to understand the nature of electronic communications and the billing/settlement activities related to the provision of third party services:

- Electronic communications operators are currently regulated by horizontal (eCommerce Directive, Distance-Selling Directive) as well as sector-specific regulation (Electronic Communications New Regulatory Framework) regarding key issues such as consumer protection, contractual rules or security systems, all of which have proved to be reliable for the protection of stakeholders against abuse and fraud.
- Electronic communications operators have “hybrid”, multi-purpose business activities (telecommunications services + Value Added Services) and these activities are to be seen as a natural development of traditional telecommunications services into

advanced electronic communications services. In light of the draft Directive, electronic communications operators are particularly concerned by the potential impact this may have on existing electronic communications services and the potential extension of this regulation to its entire business activities, particularly in relation to the difficulties they have already been experiencing with other payment services regulation such as the E-Money Directive.

- Electronic communications operators are in the process of developing new digital services in an increasingly convergent environment. These new business models are based on simple and user-friendly ways of charging for content and services, which take due account of the low risks involved (i.e. low value transactions and the restrictions on person-to-person payments).

## **Key messages on guiding principles:**

ETNO shares the Commission's concerns for an appropriate and proportionate application of the following guiding principles that should underpin the new legal framework for payments:

- Financial Services: ETNO understands the need to ensure the development of the market for financial services through its regulatory package (FSAP), but is particularly concerned by a potential disproportionate application of these (e.g. money laundering rules, particularly as operators do not offer person-to-person payments) to the application of obligations envisaged by the draft Directive on the existing and future business activities of its members.
- Consumer and merchant protection: ETNO fully supports the principle of consumer protection. However, it must be an utmost priority to find a balanced approach that does not hinder the market developments (e.g. the written delivery of detailed contractual provisions). As a general principle, regulation, if needed, should be proportionate to the risks involved. Merchant protection should be balanced against the commercial freedom to contract and should not reflect assumptions regarding the bargaining power of the respective parties.
- Risks: a clear identification of the risks and problems addressed by the draft Directive is necessary in order to ensure a meaningful discussion on necessary and appropriate regulatory methods and instruments. Without clarity concerning the problems addressed by the Directive it is not possible to evaluate the benefits of the planned legal instrument.

## **Specific comments on the draft Directive on the New Legal Framework for Payments in the Internal Market v 5.0 (26.11.2004)**

### **Preliminary remarks:**

ETNO acknowledges that the new Version 5.0 of the draft Directive on the New Legal Framework for Payments in the internal market contains some improvements compared to the preceding version. Namely:

- the situation of hybrid institutions has been taken into account to a certain extent (e.g. Recital 39 and Art. 6 (2) clarify, that the prudential requirements of Title II shall only apply to the payment part of the business and not to the non-payment activities)
- the distinction between „corporate users“ and other “payment service users” enables differentiated stipulations between payments service providers and corporate users
- the creation of specific rules for information requirements for payments, where the transaction volume is less than 10 Euro (article 21) reduces the burden of information requirements for micropayments

ETNO welcomes the publication of the Explanatory Memorandum facilitating the understanding of the Directive by presenting the basis and the objective of the regulation. ETNO supports the objective of the NLFP to create common standards by 2010 for cross-border payments in Europe and to provide a contribution to the implementation of the Lisbon-strategy. However the fact that innovation and competition are essential conditions for a profitable growth cannot be ignored. Therefore each regulatory tool must not exclusively be used for harmonisation but should also be measured against its contribution to the promotion of innovation and growth. Its application must not create legal uncertainty.

ETNO supports the upcoming impact assessment of the Directive by the Commission and calls for the inclusion of innovative payment products offered by telecom operators in the scope of the assessment. Over-regulation hampering further innovations and investments as the possible result of the NLFP initiative has to be avoided. The Commission itself has repeatedly pointed out the need for an “impact assessment” of regulation in order to enhance the competitiveness when adopting Directives (e.g. Commission Communication: „Fostering structural change: an industrial policy for an enlarged Europe“as of April, 20, 2004 KOM (2004) 274, as well as the conclusions of the European council March 26, 2004).

ETNO calls for a well-defined separation of the areas of application of the E-Money-Directive and the New Legal Framework for Payments.

There is an overlap of both regulations as Title III of the NLFP applies also to E-Money institutions. Hence suppliers of payment services already regulated, as E-Money institutions are subject to additional regulation by the NLFP.

It is still unclear which services offered by telecommunications operators could potentially fall under the definition of 'payment services' in Art. 2. Given the ongoing discussion with regard to the E-Money Directive, in the worst case telecommunication services, e.g. in particular pre-paid and post-paid services will have to comply with different legal requirements. Consequently the products are less user friendly, the introduction of new products is hindered and economies of scale for development of services are diminished. Furthermore telecommunication services lose their unique selling point compared to traditional financial services, when they have to compromise on the simplicity of their products. This does not correspond to the objective of the Commission to enable market entry for new players, which provide simple and comprehensive services to the customer.

### **Art. 2 definitions**

For ETNO it is critical that the NLFP includes a clear demarcation line between payment and non-payment services, in order to avoid regulatory uncertainty. Electronic communications operators are providers of multi-purpose or hybrid services. In order to avoid over-regulation, it is necessary to establish a mechanism to enable the application of regulation only to payment services and not to electronic communications. The Directive should therefore contain provisions that enable the separation of regulated services from other services.

The definition of a "payment service" put forward in Art. 2 and in Recital 19 is not clear in this regard. Electronic communications services used to provide the payments service could be included in this definition if the communication service is understood as an ancillary service. It has to be stressed, that the payment services offered by ETNO Members can only be seen as ancillary services to the communication services. ETNO therefore assumes that communication services as such will not fall under the scope of the Directive. However ETNO urges the Commission to clarify the interpretation of "related ancillary services".

### **Article 5 – authorisation**

The requirement of prior authorisation may result in problems regarding existing payment services. Network operators and consumers would need guarantees that current business is not affected by the authorisation process laid down in this Article. The text should therefore clarify that there is no requirement to cease the provision of existing business carried out before the date of entry into

force of the NLFP, pending application for an authorisation under the NLFP.

Furthermore, the meaning of evidence of “good repute” is unclear. ETNO further questions whether this means that operators would need a person with ‘banking’ skills within their Board. Such a requirement would be disproportionate for companies offering low risk payments.

#### **Art. 11 – the use of funds**

According to this article it is not allowed to use funds for other purposes than for the execution of the payment services. It is unclear which funds are concretely determined for payment services and where the limits of their usability are. This is another example of the risk of a spill over of financial regulation on the core business of telecom operators due to their “hybrid”, multi-purpose business activities.

#### **Art. 12 – supervision**

There is only an indirect reference in recital 33 and in article 12 (4) (second b) (should this be c?) to money laundering rules. The Directive should clarify which rules are applicable in a very clear way, as it otherwise creates legal uncertainty. As previously highlighted by ETNO members in the context of discussions on the e-money Directive the money laundering rules are cumbersome and disproportionate for operators to comply with. We therefore welcome the progress made in the draft for a revised 3<sup>rd</sup> money-laundering directive.

#### **Art. 13 – waiver**

ETNO appreciates the potential relief offered by a waiver. But even in these exceptional cases Title III is still applicable, which can be a considerable burden. However, in comparison with the 4<sup>th</sup> version it is unclear whether the conditions of the letters a-c, like the achievement of a certain total transaction volume or the provision of financial services for „underprivileged social groups“, has to be fulfilled alternatively or cumulatively.

#### **Art. 16 - contracts with corporate users**

The term “corporate user”, as defined in article 2 of the draft Directive, should be replaced by „merchant“. “Merchant” is wider and would also include suppliers falling under the definition of small and medium sized enterprises (SME). The main objective of the rules, which can differ in contracts with „corporate users“, is consumer protection. Especially small companies offering e.g. Internet and mobile content would like to negotiate reasonable conditions for the

use new modern payment instruments. The present definition of "corporate user" would not include these small companies.

### **Art. 21 – micropayments**

ETNO considers that the threshold for micropayments should be initially set within the region of 50 euros and would like to see this issue (including how this threshold would develop over time) further explored and discussed. Furthermore, ETNO believes that in principle micropayments should not be subject to information obligations (including the "main characteristics" according to article 17) and would like to see further clarification on the applicability of existing horizontal legislation -such as the Distance Selling Directive and E-Commerce Directive- in order to ensure that information requirements imposed before and after the execution of a payment transaction are oriented towards and limited to what is indispensable information of the payment user.

### **Art. 25, 26 and 27 - disputes and liabilities**

In case of disputes Art. 25, 26, 27 impose the burden of proof on the supplier of the payment – even in case of an abuse of a lost payment verification instrument of the user of a payment service. This presents an incentive for fraudulent behaviour of the final customer.

### **Art. 37 - implementing measures**

Clause 1 (b) of this article indicates that clarification of the payment services to which it applies and referred to in the annex will not occur until the Directive is actually implemented. This means that it does not seem to be the objective of the Directive to clarify its own terms, nor whether the specific clarification regarding the same should occur with the transposition into law in each Member State (which would produce a heterogeneous effect in its application) or beforehand, without specifying any time frame.

### **Art. 40 – restriction of contractual freedom**

Art. 40 prohibits the contractual exclusion or limitation of obligations and liabilities by the Payments service provider. Due to the imponderabilities mentioned above, the contractual freedom should only be reduced to the "disproportionate limitation of obligations".

### **Art. 43 – transposition**

The temporary reference to the timeframe the Commission has in mind for the transposition of the new Directive into local law is not indicated; this is clearly an item that the Commission should put into context as soon as possible.

## **Conclusions**

As ETNO has stated in its previous letters in connection with the E-Money consultation and the draft Directive on Payment Services, it supports the Commission's initiative in this field with the understanding that its ultimate aim is to establish a clear legal framework where new and innovative payment services can flourish. As stated in the draft of the „Explanatory Memorandum”, the NLFP should not represent a disproportionate high burden for new entrants, who are not in the first instance financial service providers. The above-mentioned examples show, that the present draft does not meet these requirements. Uncertainties for payment service providers still exist due to the unclear relationship between the e-money directive and the NLFP. Therefore there is a need for close co-ordination between these two regulatory instruments.

In ETNO's view, it is crucial that the new legal framework enables the development of fixed and mobile innovative services. Financial regulation should not be a barrier to the development of new broadband and 3G content. New and flexible means of payment are essential for the take-up of commercial broadband and 3G services. The new legal framework needs to take proper account of business realities and actual risks. It should enable and not hinder the development of innovative telecommunications services.

ETNO therefore calls upon the Commission to:

1. Urgently clarify the applicability (scope) and purpose of the draft Directive to the business activities of electronic communications operators.
2. Clarify the definition of "payment services" in order to obtain a clear demarcation line between regulated and unregulated services.
3. Analyse the potentially harmful effect of the draft Directive on the business activities of electronic communications operators.
4. Take into account that the money laundering rules are cumbersome and disproportionate for the low risk and low value transactions carried out by electronic communications operators.
5. Have a holistic approach to payments legislation by closely co-ordinating its work on the draft Directive with that on the E-Money Directive.
6. Have the utmost regard for the development of new and innovative payment mechanisms within a proportionate, forward-looking and truly technologically neutral legal framework for payments in the Internal Market.