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Accompanying document to

**the proposal for a Regulation of the European Parliament and of the Council
on cross-border payments in the Community**

EXECUTIVE SUMMARY OF THE IMPACT ASSESSMENT

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1. INTRODUCTION

The smooth and efficient functioning of payment systems is indispensable for the internal market. Efficient payment systems are of systemic importance for Europe's competitiveness, the facilitation of economic transactions and the conduct of monetary policy. The integration of payments markets in the EU was identified in 2000 as one of the key measures to achieving the goals of the Lisbon Agenda.

With the launch of the Economic and Monetary Union (EMU) it became evident that there is a need for a modern, stable and efficient payment infrastructure to assist cross-border electronic payments within the EU. In the absence of initiatives by the payments industry to develop the necessary pan-European processing infrastructures and lower the charges for cross-border payments, the Commission decided to act.

Regulation (EC) No 2560/2001 of the European Parliament and of the Council on cross-border payments in euro ('Regulation 2560') entered into force on 31 December 2001. The Regulation applies to credit transfers, ATM cash withdrawals and card payments made in euro up to the amount of EUR 50 000. It guarantees that, when a consumer makes a cross-border electronic payment in euro, it costs him the same as making a corresponding payment in euro within his own Member State. Regulation 2560 can be considered as a kick-off for the establishment of an integrated market for euro payments.

This impact assessment builds on the extensive preparatory work and consultations that have been carried out by the Commission and follows the conclusions of the February 2008 report to the European Parliament and to the Council on the application of Regulation (EC) No 2560/2001 on cross-border payments in euro. The report identified three main problems as concerns the Regulation, which are discussed in detail in the impact assessment. These are:

- risk of high charges, market fragmentation and inconsistent legal regime for **cross-border direct debits**;
- **low efficiency** of cross-border payments, an unlevel playing field and higher costs of payments resulting from the **settlement-based statistical reporting obligations**;
- a lack of national **competent authorities** in charge of applying the Regulation and absence of **out-of-court redress bodies** for disputes related to it.

In addition, this Impact Assessment takes into account recent developments in the retail financial markets, including the gradual emergence of the Single Euro Payments Area (SEPA), and the Commission's commitment to align the text of the Regulation with the Payment Services Directive (Directive 2007/64/EC of the European Parliament and of the Council on payment services in the internal market – PSD).

2. PROBLEM DEFINITION

2.1. Risk of high charges, market fragmentation and inconsistent legal regime for cross-border direct debits

When Regulation 2560 was adopted, cross-border direct debits did not exist. Therefore, they were not covered by its scope. However, the PSD provides the necessary legal framework making it possible to set up cross-border direct debits. If direct debits were left outside the scope of the revised Regulation, there would be a serious inconsistency in the internal market, since an important electronic payment instrument would be allowed to have different prices for cross-border and national transactions, whereas other instruments would not.

Direct debits constitute around 25 % of all non-cash payments transactions in the EU. According to the Commission estimates the value of cross-border direct debits could relatively quickly reach some EUR 250 billion annually.

The fact that direct debits, unlike other electronic means of payment, are currently not covered by Regulation 2560 presents a clear risk of having different pricing for national and cross-border direct debits. Individual financial institutions are, in the SEPA and PSD context, free to differentiate prices on a cross-border basis. The increased profit opportunities may well lead them to apply such a strategy. The price difference could distort the functioning of an important part of the EU market in payments, perpetuating its current fragmentation along national lines. If the prices of cross-border and national direct debits were not equalised, there would be no incentive for the payment service providers to quickly migrate to modern and cost-effective SEPA infrastructures, as any costs could be recovered from the consumers and businesses.

2.2. Low efficiency of cross-border payments, unlevel playing field and higher costs of payments resulting from the settlement-based statistical reporting obligations

Community legislation and European Central Bank acts require Member States to collect statistics on the balance of payments (BoP). However, the methodology adopted by Member States varies. The methods used can be classified in two broad categories:

- systems based on **direct reporting and surveys**, which collect the information directly from resident enterprises and households involved in the economic activities;
- systems based on **settlements** (payments), which collect the information through intermediaries, i.e. the banks executing the payment orders.

Regulation 2560 introduced an exemption from BoP statistical reporting based on bank settlements up to a threshold of EUR 12 500. This speeded up the change to systems based on direct reporting, as no threshold applies when this method is used.

At the beginning of 2008, 14 Member States were using direct reporting/surveys to compile their balance of payments statistics, while 13 Member States relied on settlement-based BoP reporting. Six countries of the latter group decided to raise the threshold to EUR 50 000 on a voluntary basis, while the remaining seven continued to apply the EUR 12 500 threshold. Seven out of the 13 countries applying settlement-based reporting are currently in the process of migrating or designing the changeover towards the direct reporting/survey collection method.

Statistical reporting arrangements differ across those 13 Member States. This seriously affects the efficiency of EU payment systems, since it means that, in many cases, fully automated, straight-through-processing of cross-border payments above the exemption threshold may not be possible. According to estimates made by the national banking associations, around 50 % of the payments subject to reporting require manual intervention, which significantly increases the costs and time needed for processing.

Consequently, the settlement-based BoP reporting has a clear EU policy dimension, as this collection method constitutes a barrier to the creation of the internal market in payments and perpetuates the administratively imposed distinction between national and cross-border payments. From a competition perspective, a distinction between payments made within and between Member States creates an unlevel playing field for payment services providers located in different Member States. It further limits competition by creating barriers to entry, which could be too high for some categories of the payment service providers.

The burden of reporting and of maintaining the reporting infrastructure has a significant impact on the costs of credit transfers. For example, according to the assessment of the Italian Banking Association, the direct cost of BoP reporting is around EUR 3.40 for every single cross-border credit transfer. Calculations made by the Spanish banking industry indicate similar values (around EUR 3 per credit transfer).

Moreover, the usefulness and accuracy of reporting based on settlements may gradually decline. When the SEPA project is fully implemented, payments data will often no longer reflect the underlying economic transactions, as economic agents will be able to make all their payments through one account, not necessarily situated in the Member State where they are physically located. This may in turn have an impact on the reliability of BoP data provided through settlement-based reporting and used for various purposes at the EU level, for example when preparing trade negotiations or initiating excessive deficit procedures.

2.3. Lack of explicit reference to the national competent authorities in charge of applying the Regulation and to the out-of-court redress bodies for Regulation-related disputes

Out-of-court redress bodies for consumer complaints exist in all Member States. Nevertheless, in some Member States, they refuse to handle complaints related to Regulation 2560, giving as their reason that they have not been empowered to do so in their national legal system. As a result, in some countries the complainant still has to go to court to seek redress. For a customer domiciled in another state, this causes difficulties and is questionable in terms of cost/benefit.

As regards the competent authorities, the majority of Member States have informally communicated to the Commission the identity of the competent authority in charge. Nevertheless, in some situations, where a general problem of incorrect application of the Regulation has been identified, some Member States have refused to address the problem, arguing that they had no legal obligation to do so.

3. OBJECTIVES

The general objective of the review of the Regulation is to achieve an Internal Market for payment services in euro, subject to effective competition and where there is no distinction between cross-border and national payments, thereby providing significant savings and benefits to the wider European economy. In order to achieve this general objective, three

operational objectives have been identified: (1) eliminate the administrative obstacles hampering the efficient functioning of the internal payments market (2) extend the guarantee of equal prices for national and cross-border payments to include direct debits and (3) ensure the consistency of European payments legislation and its applicability in the Member States. This would lead in the medium term to the achievement of the specific objectives which seek to encourage and facilitate the use of cross-border electronic payment services by consumers and businesses, secure a level playing field from a competition perspective, enhance legal certainty as regards cashless payments in euro and reduce the costs of payments for European consumers, businesses and payment service providers.

4. THE IMPACTS

4.1. Impacts related to the extension of the scope to direct debits

The options in terms of extending the scope of the Regulation to include direct debits are: (1) not to extend the scope of the Regulation to direct debits (2) encourage industry self-regulation and/or recommend regulatory action by Member States and (3) extend the scope of the Regulation, by means of legislation, to cover direct debit payments.

In Option 1, payment service providers have the possibility to set different prices for national and cross-border direct debit payments. Many are likely to do so. As a result, direct debit would most probably not achieve its full cross-border potential (other, regulated payment instruments would be used) and the social benefits of the Internal Market in payments (low payment prices) would be reduced.

In Option 2, the payments industry is encouraged to adopt, through self-regulation, the same prices for national and cross-border direct debit transactions. As an alternative, or in parallel, the Commission would issue a Recommendation to the Member States, inviting them to equalise the charges. The equalisation of charges would extend most probably only to some Member States and/or banks, with the result that fragmentation of the EU payments market would persist. The social benefits of the internal market would still be lower than they could be.

Under Option 3, the prices charged for a national direct debit and a cross-border direct debit are the same within each Member State. Consumers would be protected from the possible discriminatory pricing of cross-border direct debits. European enterprises would benefit even more, since businesses act also in a payee capacity. As a result of the equalisation of prices, payment transaction costs for businesses would be the same, irrespective of the payer's location.

4.2. Impacts related to BoP reporting

The options related to BoP reporting are (1) maintain the existing exemption threshold of EUR 12 500, (2) create a voluntary additional Optional Service (AOS) Community within SEPA that would enable the collection of statistical data from settlements to continue, (3) encourage voluntary adjustments by the Member States and (4) address the BoP reporting problems through legislation, with three sub-options: (4a) raise the exemption threshold to EUR 50 000; (4b) abolish the BoP reporting obligations imposed on payment service providers; and (4c) raise the exemption threshold to EUR 50 000 and, in a second phase, by January 2012, abolish BoP reporting based on settlements.

Under Option 1 the unlevel playing field for competition between payment service providers continues to exist and the efficiency of the internal market in payments is hampered by the reporting on cross-border payments. Consumers and businesses in the 13 Member States where reporting is maintained continue to face higher charges (either directly, through pricing of payment services or indirectly, through higher account service fees and/or other related charges).

Option 2 would make it possible to continue the statistical reporting based on payments in the SEPA environment and enable automated payment processing. It would reduce costs of settlement-based reporting and raise the exemption threshold to EUR 50 000 for the voluntarily participating Member States. However, the fixed costs of maintaining the reporting infrastructure would still constitute an important financial burden for banks, and the different treatment of national and cross-border payments would be maintained. Data on payments incoming from non participating Member States (a majority of Member States would not join the AOS, as it is not necessary for them) would also be unavailable.

Under Option 3 the negative developments described in Option 1 would be somewhat mitigated, although the degree to which they disappear would depend on the reaction of the Member States.

If the exemption threshold is raised to EUR 50 000 (Option 4a), a greater homogeneity between the EU members would be achieved, as the distortions of competition -at least for retail payments - are reduced. However, maintained reporting would still constitute an important barrier for cross-border payments.

In Option 4b the costs of payments would be reduced to the maximum possible extent, no administrative distinction would be made between national and cross-border payments, and the level playing field for payment service providers would be achieved from a competition perspective. The use of cross-border payment services, especially for businesses, would be facilitated.

Option 4c would present the same benefits as Option 4b, the only difference being that the BoP requirements would be phased out, after an initial phase during which the reporting threshold would be raised. This would allow the BoP compilers to gradually adapt their collection methods to the necessary changes, thus minimising the impact on the quality of the BoP statistics.

4.3. Impacts related to the competent authorities and out-of-court redress

The options related to the competent authorities and out-of-court redress bodies are (1) do not appoint competent authorities and out-of-court redress bodies and (2) appoint competent authorities and out-of-court redress bodies to deal with the Regulation issues.

Under Option 1 the unavailability of a clear way of ensuring quick and cost-efficient redress would be detrimental to the consumer and to the efficiency of the internal market in payments. It would create a legal inconsistency between the PSD and the Regulation and cause confusion in cases of payments falling under both payment laws. As regards the competent authorities, the lack of a clearly appointed administrative body supervising the application of the Regulation would make it much more time consuming and difficult for the Commission to address any misinterpretation or market failure concerning the application of the Regulation.

In Option 2, Member States would be requested to indicate which competent authorities would be responsible for the correct application of the Regulation at national level. Consumers and businesses would have the possibility to limit the legal costs of judicial intervention and to accelerate the resolution of payment disputes through arbitration and mediation.

5. CONCLUSIONS

The following are the preferred options from the Community policy point of view: (1) extension of the scope of Regulation 2560 to include direct debits; (2) phasing-out of the payments-based reporting obligations by January 2012; and (3) appointment of competent authorities and out-of-court redress bodies.

The proposed amended Regulation would be aligned with the wording and the definitions used in the PSD, so as to ensure legal consistency and clarity between both payment laws.