European Payment Institutions Federation aisbl

EPIF Position Paper on the Digital Euro Proposal

On 28 June 2023, the European Commission adopted its legislative proposal for the digital euro. This proposal comes at a crucial time during the investigation phase being carried out by the European Central Bank (ECB) and for which a final decision is not expected until October 2023. This is an important step to bring much needed clarity to market participants and EU citizens about what a Eurozone retail central bank digital currency (rCBDC) might entail.

EPIF has been an active stakeholder in the various workstreams of the Euro Retail Payments Board (ERPB), including the Rulebook Development Group. We very much welcome the ECB's work to involve the industry in this important exercise of exploring a Digital Euro for Europe. We look forward to continuing to collaborate with both legislators and the ECB in order to ensure that the digital euro brings as much value as possible to citizens, businesses and public authorities.

EPIF welcomes many provisions in the proposal that bring further clarity to market participants, notably in terms of the legal certainty on the **issuance and issuance liability**, the possibility for citizens to **hold multiple wallets** and the **alignment with the future rules of the Payment Services Regulation (PSR)** for digital euro payment transactions.

However, some concerns remain with the draft Regulation. These include:

- The digital euro use cases should focus on **promoting innovation** and addressing market failures and not replicating existing solutions;
- The risk of creating an **unlevel playing field** between the digital euro instrument and current private payment solutions by subjecting them to different legislative rules;
- The digital euro should offer a **compelling value proposition** for consumers, for which value-added services offered by all PSPs are critical
- The rules foreseen for the **compensation model** and respective **charges and caps**;
- Th proposed **exemptions for mandatory acceptance**;
- The need to strengthen the provisions regarding **interoperability and reuse** of the existing schemes, as well as the need to ensure **open standards** to ensure competition and enable pan-European solutions and innovation;
- The need to ensure that **all Payment Service Providers (PSPs) can distribute** the digital euro.

Our more detailed views on these points and other elements of the proposal are explained below.

Legal Basis

The draft Regulation establishes clear issuance and issuance authorization responsibilities for the digital euro, which are to rest with the Eurosystem and the ECB, respectively. Moreover, it also establishes the legal basis for the issuance as a direct liability of the ECB. Both these legal clarifications and confirmations are welcomed by EPIF members.

The proposal also gives legal tender status to the digital euro, introducing mandatory acceptance of digital euro acceptance. We believe this to be an important and necessary legal consideration to ensure acceptance and uptake of the digital euro. EPIF was happy to see in the proposal envisaged **exemptions for mandatory acceptance**. This has been an issue which EPIF has raised on numerous occasions. While we believe the proposed exemptions to be a good starting point for the co-legislative process, further clarifications are needed to bring legal certainty and clarity for obliged entities. For example, further clarity is needed for what would constitute a *prior agreement* and *good faith* under this draft Regulation. Moreover, the current proposal does not necessarily envisage mandatory acceptance by those accepting euro cash but only by those already offering other digital payment instruments as an option to their customers. This is irrespectively of their size/characteristics or willingness, as the exemptions would not apply to those already offering other means of digital payments. This requirement seems disproportionate to some providers, even if they offer other digital payment instruments.

EPIF also very much welcomes the surcharging prohibition on the payment of debt with the digital euro. Such prohibition aligns the treatment of digital euro payments with cash and also creates a parallel with existing EU legislation, including the Payment Services Directive.

Distribution

Distribution has been one of the most discussed elements of the investigation phase of the digital euro and EPIF very much welcomes the clarity provided by the draft Regulation in this regard.

One issue of upmost importance for EPIF members is the assurance that the digital euro will be able to be **distributed by *all* payment service providers (PSPs)** under the PSD2. Ensuring that all bank and non-bank PSPs will be able to distribute the digital euro is crucial to guarantee a level playing field and a high level of consumer choice and ensure the digital euro is easily accessible by all European businesses. Under its Recitals, the draft Regulation foresees an inclusive distribution however we would call on the European Parliament and Council to maintain this inclusive language and ensure **consistency throughout the legislative text** in this regard. EPIF will continue to collaborate with the ECB to make sure that the technical features allow for this inclusive distribution.

We also note that the introduction of the digital euro reinforces the need to ensure a level playing field between bank and non-bank providers, guaranteeing that specific PSPs are not given privileged access to the distribution of the digital euro. The ongoing discussions on Instant Credit Transfers foresee that payment institutions will be able to directly access payment systems, which would allow them to settle digital euro transactions. From a timing and implementation perspective, EPIF members call for a **targeted amendment to the Settlement Finality Directive as soon as possible**.

The draft Regulation also provides for users to be able to hold **multiple digital euro wallets** which EPIF members have always supported. The possibility for multiple wallets is a crucial element not only to ensure sound competition amongst market players for the provision of digital euro services but also essential to safeguard consumer choice and financial inclusion. This freedom not only mirrors the current practice of maintaining accounts with multiple physical banks but also encourages a more dynamic and adaptable digital economy. One element that EPIF would call for to be included in the legislative framework is the possibility for **self-custody** in digital euro. In self-custody wallets, the user directly holds the key to sign a transaction, meaning that transactions remain private between the parties to the transaction. It also brings the digital euro closer to physical cash in its design. EPIF members envisage a model where customers can choose between custodial and self-custody wallets.

For EPIF members, it is also crucial that **easy switching between digital euro wallet providers** is enshrined in the legislation. This will ensure that PSPs effectively cooperate to make the switching process as easy as possible.

Other important considerations for the distribution of the digital euro relates to the **alignment with the future PSR rules**. Our members fully support this alignment, which should cover all elements from the rules on Strong Customer Authentication, liability and AML in order to ensure a level playing field for all the actors in the payments market. Moreover, the draft Regulation mandates both online and offline functionalities for the digital euro. Whilst we fully agree with the European Commission on the importance to guarantee both functionalities, our members are still assessing the risks and technical feasibility of offline digital euro payment transactions, especially in the given timeline of first issuance. This is a point that should deserve further consideration during the co-legislative process and close cooperation with the ECB technical work and PSPs in this regard. Therefore, we also caution **against mandating all distributing PSPs to offer offline digital euro services**. PSPs have a variety of business models and services that can support the distribution of the digital euro but not all of them are prepared, nor are they suitable, to ensure such offline functionality. We would call for additional clarifications in the Level 1 text that the offline functionality does not need to be offered by all PSPs.

Digital Euro App

We have certain reservations about the ECB developing its **own front-end services** ("ECB Digital Euro App"), which would directly compete with the front-end services provided by PSPs. EPIF members call for a reconsideration of the digital euro app. As the app entails relevant challenges, it should exist only, and if needed, as an option to address specific gaps and not be imposed by default on all distributing intermediaries.

PSPs that can offer digital euro services through their front-end services should not be obliged to offer digital euro services via the digital euro app.

Moreover, according to the current work in the Digital Euro Rulebook Development Group, the Digital Euro App is envisaged to be a fully-fledged front-end solution for the digital euro, rather than following the initial "white label app" approach, which would allow users to instruct their intermediaries to initiate transactions. This would entail unnecessary additional complexity, challenges and costs when it comes to maintaining both channels (duplication of adaptation and operational costs), without evident added-value to the consumers, which do not seem proportionate or addressing a market need. We also have concerns about requiring intermediaries to provide support for a channel they cannot control, neither technically not operationally.

The Digital Euro App shall not constitute a tool for the provision of payment services by non-PSPs, as stated in the legislative proposal and overall payment services regulatory framework.

The use of the digital euro

EPIF members **welcome many of the elements** included in the draft Regulation with regards to the usage of the digital euro, notably the possibility to incorporate distributed ledger technologies (DLTs). This will allow the development of innovative digital euro solutions leveraging on DLT applications, with the potential to increase the efficiency of transactions.

We also note that the European Commission mandates the ECB to calibrate **individual holding limits**, which will have to be done on the basis of concrete criteria to account for financial stability and overall control over monetary policy. We appreciate that the concrete holding limits' definitions fall within the remit of the ECB and fully agree on the need to have limits in place for macroeconomic considerations. Nevertheless, we stress the importance of having these thresholds to be carefully assessed. The limits need to be high enough, within reason, to provide incentives for European citizens and other digital euro users to adopt the digital euro as a means of payment and to ensure that high quality user experience is not impaired (which will have a material impact on the uptake of the digital euro). Again, we will continue to collaborate with the ECB to calibrate these limits.

However, we note that the draft Regulation does not make a **differentiation between holding limits for individuals and holding limits for merchants.** Higher holding limits or defined technical windows for defunding for merchants would be imperative to ensure a smooth operation of their services without triggering high-frequency waterfall/reverse waterfall operations that can impeded the good functioning of the digital euro end-to-end processes and settlement, with the potential to add to costs and inefficiency for merchants.

EPIF understands the importance of having a business model behind the digital euro and we welcome that such a principle is acknowledge in EU legislation. It would be important to ensure that such a principle is horizontal to all payment instruments and European payment schemes and not limited to this specific proposal where the ECB will participate directly in the market. However, there are some elements of concern regarding the **compensation and pricing model** envisaged in the proposal.

We believe that the digital euro will be most likely to succeed if it **promotes the greatest possible level of innovation**. The remuneration model is a critical component in enabling an innovative space as PSPs/intermediaries must be incentivized to offer innovative services that will off-set the cost of integrating a digital euro. To enable innovation, the compensation model for the digital euro should **not** mandate an inter-PSP fee and therefore leave more flexibility to the market to develop pricing schemes. Ultimately, direct negotiations between merchants and PSPs would achieve the most competitive pricing outcome, while overcoming the limitations inherent in markets with rigid price regulation. Moreover, we believe that is vital for digital euro wallet issuers to be able to charge users for basic account management services in order to recoup the costs of offering these services, which would be in line with the Payment Account Directive (PAD).

The draft Regulation, rightly, provides for the transactions themselves to be **free of charge** for individual consumers but this will of course come with a cost for digital euro intermediaries, especially considering the exhaustive list of core services established in Annex II. A viable commercial model for enhanced-value digital euro services is therefore necessary. As such, market players should be allowed to set their own fees, which would incentivise innovation and competition amongst them in order to offer the best possible services and experiences to merchants, beyond just competing on price. The freedom to set fees according to the value they provide would, therefore, promote a more robust and dynamic digital euro ecosystem.

We therefore believe that the digital euro should offer an innovative framework in which value-added services can be offered by intermediaries. Conditional payments and new service bundles (such as allowing for KYC to be performed by a standalone entity) could become useful levers for this.

Moreover, we would welcome additional clarifications throughout the legislative process with regards to the **information requests and certified auditing** which the ECB is empowered to request from financial institutions. EPIF members remain available to provide the ECB with necessary information to allow the institution to fulfil its fee-evolution monitoring activities but stress that conditionalities for information requests and auditing (e.g., in relation to detailed pricing models) must be in place.

In parallel to the pricing caps introduced in the proposal, it is also envisaged for **basic digital euro payment accounts to be provided free of charge.** Our members have concerns on this point. First, we note that under the Payments Account Directive (PAD) there is no requirement mandating basic payment accounts to be offered free of charge. Second, the list of "basic digital euro payment services" provided in Annex II of the draft Regulation is extensive and incorporates elements which, at this stage, are expected to have high implementation and operational costs. This is the case, for example, for all transactions that involve funding/defunding activities, in particular with cash. We also take note that the proposal envisages Member States to designate a specific authority to ensure the provision of this basic services, free of charge, in order to further enhance financial inclusion. EPIF members consider that financial inclusion can be a by-product of innovation in digital euro, should intermediaries be given enough incentives to do so. We also call for additional clarifications on how these public authorities would be selected to distribute the digital euro and once they are selected how they would be incentivized to distribute the digital euro. Against this background, we would call for the proposal to leave enough space for the market to price basic accounts and services, just liked under the PAD, while ensuring financial inclusion through the provision of this services through a dedicated designated authority.

Digital euro functionalities

EPIF welcomes most of the provisions proposed by the European Commission with regards to the digital euro functionalities. In particular, EPIF has always been a strong proponent of an **easy to use and accessible digital euro**, including by leveraging the **EU Digital Identity Wallet**, as well as the possibility to include **conditional payments** into the digital euro design, which will require some foundational conditions to be built in the core ledger of the digital euro. We agree that the ECB should provide core additional functionalities at the core settlement layer so that value added services can then be built by intermediaries. We do however see scope to decouple and decentralize the settlement layer from the Scheme, as is currently the case for Instant Payments[1]. We believe that conditional payments can become a useful way for intermediaries to monetize in the digital euro space.

We believe that, as it is done for Instant Payments, the digital euro settlement services should be conducted in combination with other clearing houses and not rely solely on the ECB central platform. The digital euro settlement services should be based in the existing networks to ensure a smooth functioning and minimize risks of a single point of failure.

We believe that the **front-end services for the digital euro**, including the full customer journey and necessary fraud prevention elements, should **remain under the full responsibility of the intermediary PSPs**. We believe this would be the best possible way to foster adherence to the digital euro and reach a certain threshold of market penetration as consumers tend to rely on and use their preferred payment methods first and foremost.

We would even welcome innovation in this space so that KYC can be performed by a separate entity (such as eIDAS) which can then be leveraged by PSPs to offer the custody of funds. We believe this approach would bring more innovation but also more financial inclusion into the design of the digital euro. It would also provide cost saving opportunities for intermediaries if the KYC credential issued by the entity performing KYC could then be re-used by other parties without having to replicate the same process. Against this background, a full alignment with the PSD rules is very much welcomed including on authentication methods, exemptions and delegation.

Our members also have a number of concerns regarding the possibility for the ECB to create and manage other **fraud prevention mechanisms**, as well as managing its **own dispute mechanisms**. With regards to dispute mechanisms, EPIF notes that such considerations should remain within the responsibilities of the Digital Euro Rulebook. The Rulebook has been under development since February 2023 by the Euro Retail Payments Board (ERPB). EPIF has been calling for the Digital Euro Rulebook to be, when appropriate, managed under a specific Scheme manager, more experienced in scheme management, outside the ERPB remit. Agreeing on a Scheme manager does not, of course, dismiss the ECB’s role and participation in the Scheme arrangements.

We welcome the intention of Article 26 to promote **interoperability** and reuse of existing schemes, to the extent possible, for the sake of efficiency of the ecosystem and to avoid duplication of costs. This is particularly relevant when considering the recent investments in instant payments and related payment solutions.

[1] For example, IberPay does the settlement for domestic Instant Payments in Space whilst settlement for cross-border payments is done by the ECB.

Data Privacy and AML/CTF Considerations

Data privacy is a core consideration for the digital euro project in order to ensure trust and uptake by EU citizens. We welcome that the draft Regulation reinforces this important element by very clearly specifying, including through Annexes III to V, the limitations for the processing of personal data by PSPs, the Eurosystem and providers of support services. However, we would see value in further analysing the design of the “single access point of digital euro user identifiers and the related digital euro holding limits” envisaged under Article 35(8) and to be established by the Eurosystem. For this centralized database it is essential to avoid creating a single point of failure that could create concerns in case of cybersecurity and operational unavailability. The communication of this central database, managed by the ECB, would also need to be very carefully designed.

Simultaneously, privacy-enhanced specifications for the digital euro also need to be balanced with the need to minimize ML/TF risks in digital euro transactions. EPIF members see merit in permitting **higher levels of privacy for close-proximity and low-risk digital euro payment transactions**. To ensure higher levels of privacy we would welcome a tiered approach to KYC by which higher levels of control are applied to riskier transactions. This would also allow the digital euro to replicate more cash-like features. Nevertheless, to this end, it is crucial to subject the digital euro to the same levels of privacy and controls as those applying to existing electronic payment solutions. Drawing from our experience, this is best achieved through a risk-based approach that allows a targeted allocation of resources, the leveraging of new technologies and a focus on “out-of-pattern” transactions.

However, we stress again that the exemption for offline lower-value and close proximity payments from certain customer due diligence (CDD) measures is currently not envisaged under the ongoing AML/CTF Regulation (AMLR). Effectively, these mandates oblige entities to carry out CDD checks on all non-digital euro transactions, regardless of the transaction amount. We note that it is essential to ensure a regulatory level playing field between payments in digital euros and those carried out by existing payment solutions. We call for the **legislative rules** applying to the digital euro to be equivalent to those applicable to existing electronic payment solutions.

ABOUT EPIF (EUROPEAN PAYMENT INSTITUTIONS FEDERATION)

EPIF, founded in 2011, represents the interests of the non-bank payment sector at the European level. We currently have over 190 authorised payment institutions and other non-bank payment providers as our members offering services in every part of Europe. **EPIF** thus represents roughly one third of all authorized Payment Institutions ("PI") in Europe. All of our members operate online. Our diverse membership includes a broad range of business models, including:

- Three-party Card Network Schemes
- E-Money Providers
- E-Payment Service Providers and Gateways
- Money Transfer Operators
- Acquirers
- Digital Wallets
- FX Payment Providers and Operators
- Payment Processing Services
- Card Issuers
- Independent Card Processors
- Third Party Providers
- Payment Collectors

EPIF seeks to represent the voice of the PI industry and the non-bank payment sector with EU institutions, policy-makers and stakeholders. We aim to play a constructive role in shaping and developing market conditions for payments in a modern and constantly evolving environment. It is our desire to promote a single EU payments market via the removal of excessive regulatory obstacles.

We wish to be seen as a provider for efficient payments in that single market and it is our aim to increase payment product diversification and innovation tailored to the needs of payment users (e.g. via mobile and internet).

EPIF c/o Afore Consulting European Payment Institutions Federation aisbl

Rue du Trone 100 | 1050 Brussels Belgium |