

FINANCIAL REGULATION

Digital finance and payments update: *European Commission's sectoral approach*

In her recent speech, "[Digital finance and payments: where are we headed](#)", Commissioner McGuinness gives a clear direction of travel on the European Commission's (**Commission**) approach to this sector.

In her speech, the Commissioner emphasises that trust in the financial system is a key factor underpinning the Commission's policy work in this sector, particularly as the financial system undergoes continued development and change. The Commissioner highlights the following key areas of focus:

- instant payments, PSD3 and open finance
- resilience
- the regulation of crypto
- distributed ledger technology (DLT)
- the retail investment strategy

5 MIN READ

The Commissioner also provides some indicative timelines for these developments and addresses the introduction of a digital euro.

We provide below an overview of these key focus areas, to which regulated entities, in particular payment services providers, e-money issuers and crypto-asset service providers (**CSPs**), should have regard as part of their horizon-scanning and regulatory and compliance planning.

Instant payments, PSD3 and open finance

Instant payments

The Commissioner references the proposal, tabled last year, to make instant payments the norm.

In October 2022, the Commission adopted a legislative proposal to make instant payments in euro available to all citizens and businesses holding a bank account in the EU. The proposal aims to ensure that payments in euro are affordable, secure, and processed without hindrance across the EU. In February, the European Central Bank published its opinion on the proposed Regulation and the European Parliament's Economic and Monetary Affairs Committee (**ECON**) is scheduled to consider the proposal in June 2023.

PSD3 and open finance

Last year, the Commission opened three consultations to progress the Commission's 2020 Digital Finance Strategy and separate Retail Payments Strategy. In particular, the Commission progressed its review of the Payments Services Directive (**PSD2**) and its work on open finance.

The Commission is currently reviewing the following four main PSD2 themes:

- fraud prevention
- implementation and enforcement
- ensuring a level playing field between banks and other providers in access to payment services
- open banking

The Commissioner highlights that PSD2 set out the foundation for open banking (by allowing payment account data to be shared with another provider, with a customer's consent), and that the PSD2 review will lay the basis for the Commission's work on open finance. The Commission's open finance policy aim is to put customers in control of their data, and to facilitate more data-based services, while ensuring customers know what data they are sharing and who it is being shared with.

The Commissioner further highlights that the open finance initiative is part of the Commission's cross-cutting data strategy, whereby it wants to encourage fair data sharing (in all directions), and for all economic players to operate on a level playing field.

On timing, the Commissioner sets out that further progression of the PSD2 review, and its work on open finance, is scheduled for the second quarter of this year.

Resilience

The Commissioner highlights that, from a customer's perspective, a key aspect of trust is resilience, in particular, digital and cyber-resilience, so that customers are protected against theft and fraud.

The Digital Operational Resilience Act (**DORA**) aims to help build up trust in the financial system, and the Commissioner highlights the following key aspects of the legislation:

- banks and other financial companies will be required to put measures in place to withstand cyber-attacks and other digital threats
- critical ICT providers for services like cloud computing will be subject to oversight

On timing, the Commissioner sets out that DORA should apply from 2025, with the European Supervisory Authorities (**ESAs**) issuing technical standards to give it full effect.

Crypto

The Commissioner states that trust is also important in the 'world of crypto', and cites the recent collapse of crypto projects such as FTX, Terra Luna, Celsius and Voyager, as examples of sectoral risks.

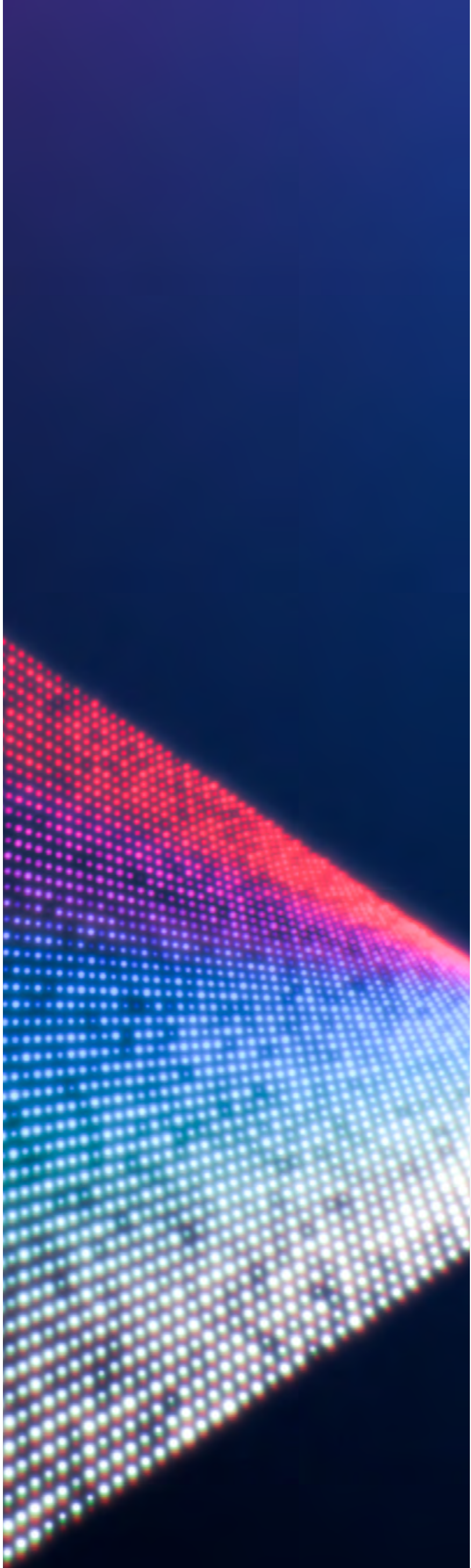
Whilst acknowledging that some regulators think that crypto should not be regulated as, to do so, gives it legitimacy, the Commissioner stresses that ignoring crypto is not the answer. In support of regulation, the Commissioner again references FTX, as an example of the volume of people (in particular, retail investors) who are now investing in crypto-assets. The Commissioner also points out that the increasing links between crypto-markets and traditional regulated financial service providers could trigger financial stability concerns in the future, justifying more crypto sector regulation.

The Commissioner then sets out the following key requirements of the Markets in Crypto-Assets Act (**MiCA**), stating that it addresses many of the issues that led to the FTX collapse:

- stablecoins marketed in the EU must be backed by a reserve of assets
- CSPs must have appropriate risk management, governance and conflict of interest arrangements
- CSPs must segregate clients' assets and not use them for their own account
- introduction of a disclosure obligation for issuers and trading venues, with clear guidance on how disclosures should be made

The Commission will also review the environmental impact of crypto-assets as part of the general review of MiCA, and consider the need for additional policy measures in the future.

On timing, MiCA is expected to apply at the same time as DORA, i.e. from 2025.



DLT

The Commissioner flags the need to separate the technology behind crypto from the recent crypto project collapses, and emphasises that DLT has many current and future applications that could make the trading and settlement of securities much more efficient.

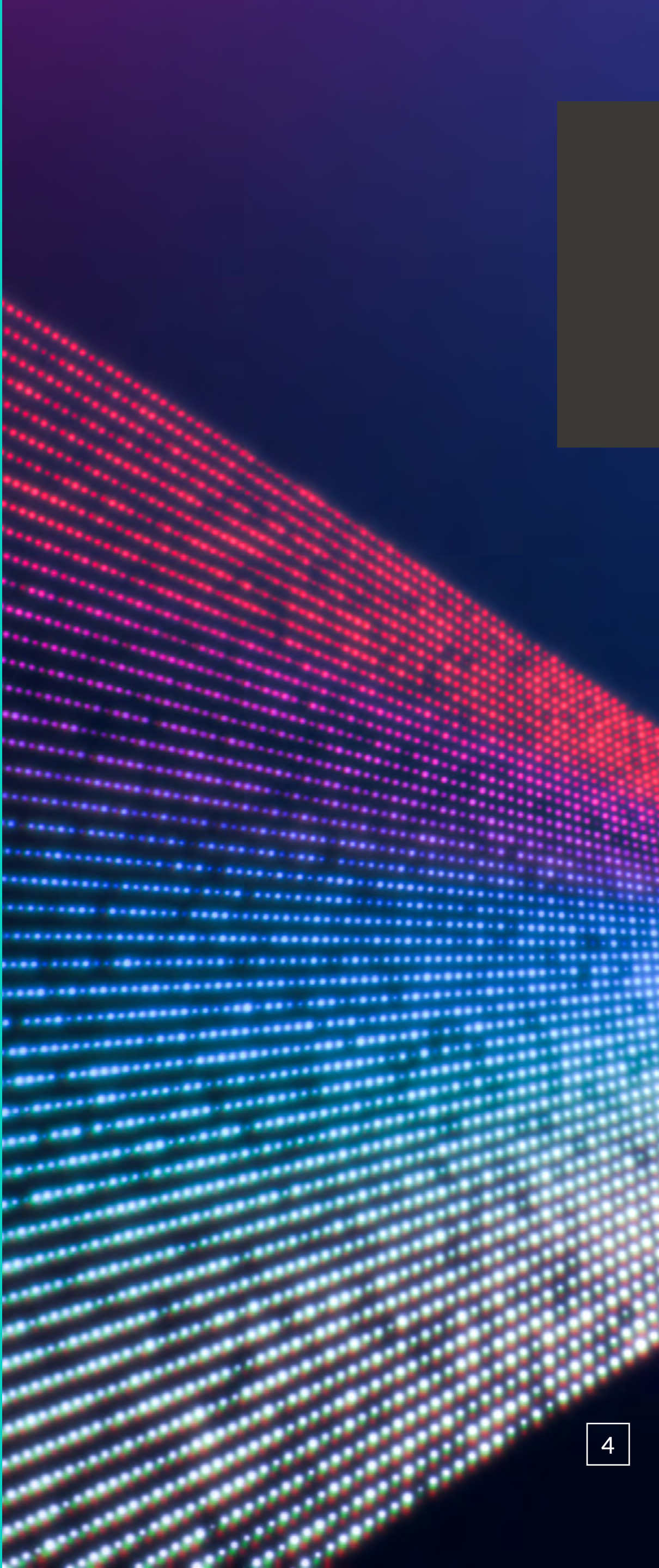
In 2020, the Commission introduced the DLT Pilot Regime (**Regime**) as part of its Digital Finance Package, to further enable and support the potential of digital finance while mitigating associated potential risks. This month, the Commission launched the European blockchain regulatory sandbox, which is scheduled to run until 2026 and establishes a pan-European framework for regulatory dialogue, to increase legal certainty for innovative blockchain solutions.

The Commissioner highlights that eligible firms will be able to experiment with this technology in a safe environment, which will enable the Commission to look at how DLT works in real-world situations and, depending on the lessons learned, propose possible changes to legislation.

Retail investment strategy

The Commissioner mentions the Commission's retail investment strategy, highlighting that this will consider how consumers behave in a digitalised economy.

The Commission launched this strategy in 2021 with the aims of ensuring that consumers who invest in capital markets can do so with confidence and trust, that market outcomes are improved, and that consumer participation is increased.



Digital euro

The Commissioner addresses the introduction of a digital euro, highlighting the following key benefits:

- facilitating a pan-European payment system across the euro area
 - supporting financial inclusion, as it could be usable offline – giving another payment option to people who don't have access to the internet or in remote areas
 - supporting the EU's open strategic autonomy by reducing reliance on international card schemes, even for European card transactions and e-commerce payments
 - providing an alternative to EU businesses looking to use digital money, and avoiding the risks of relying on private 'stablecoins' or foreign central bank digital currencies
- the ECB's investigative work points to a digital euro primarily used as a means of payment, not a store of value – so it should not create an incentive to move deposits away from commercial banks
 - the Commission's aim is that a digital euro would co-exist with private payment solutions, and that payment service providers would distribute the digital euro and maintain competition with private means of payment

The Commissioner also flags that the Commission will be holding roundtables with consumers, banks, merchants and others to discuss all the technical, legal and policy issues that it needs to get right.

On timing, the Commission, in May 2023, will propose a legal framework to regulate the essential elements of a digital euro, which will then be considered by the European Parliament and Member States.

The Commissioner addresses the following concerns as regards how the introduction of a digital euro may impact commercial banks and payment service providers:

Next steps

This speech provides invaluable insight into the Commission's current approach to digital finance and payments. Regulated entities, in particular payment services firms, e-money issuers and CSPs, should have regard to the above key Commission focus areas as part of their 2023 horizon-scanning, and regulatory and compliance planning.

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