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| From: | General Secretariat of the Council |
| To: | Working Party on Financial Services and the Banking Union (Digital Euro Package) Financial Services Attachés |

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| Subject: | Digital Euro Package: working party 19.07.23 Presentation by the Commission services on the impact assessment of the Digital Euro Package |
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Digital euro

Impact Assessment

July 2023

Outreach on the digital euro

ECB and national central banks

Public consultation on a digital euro (October 2021 – January 2022)

Survey and focus groups on users' preferences and prototype in 2021, 2022 and 2023

Market Advisory Group composed of payment experts from private sector

Rulebook Development Group to develop standards, rules and procedures, composed of national banks and payment experts from private sector and consumer associations

Commission

Call for evidence and targeted consultation on a digital euro (5 April 2022 - 16 June 2022)

High-level conference on 7 November 2022, bringing together representatives from national and EU authorities, Members of the European Parliament, private sector and civil society representatives and academia.

3 Roundtables chaired by Commissioners with representatives of merchants/businesses, consumers and payment service providers in February and March 2023.

Consultations with Member States:

- 12 Eurogroup and EWG discussions
- 7 technical seminars with Member States
- 7 expert group meetings (EGBPI) with Member States from September 2022 to March 2023 to discuss all building blocks of the proposal

Problem definition

Problem drivers

D1: In a rapidly digitalizing economy, central bank money in physical form, i.e. cash, is not available for payments in a growing part of the economy.

D2: Third country CBDCs and “stablecoins” not denominated in euro may gradually gain market share in the euro area’s payment markets and reduce the role of the euro

Problem

Physical central bank/ECB money (cash) alone is not sufficient in the digital age to support the role of public money in the EU’s economy: provide a monetary anchor and support the EU’s open strategic autonomy

Consequences

People:

- Limited choice in pan-European payments and innovative payments
- Financial inclusion may be eroded

Businesses:

- Merchants: Limited choice when accepting payments
- Innovative businesses: potential loss of competitiveness due to higher risks (credit, forex, political) when relying on innovative payment solutions provided by foreign CBDCs or “stablecoins” or other private solutions lacking monetary anchor.

Eurosystem and EU’s economy:

- Weakening monetary anchor can lead to weakened trust in the financial sector
- Potential limitations on monetary policy weakens open strategic autonomy
- Financial stability risks
- Weakening international role of the euro

Objectives

The **general objective** of this initiative is to ensure that the central bank money issued by the ECB can support the EU's economy in the digital age, while safeguarding the role of cash.

Specific objective 1:

Reinforce the **euro's monetary anchor** in the digital age by ensuring that central bank money in both its physical and future digital form is widely available to and accepted by all euro-area residents/businesses and tailored to their needs, while preserving financial stability.

Specific objective 2:

Strengthen the **EU's open strategic autonomy** by increasing the euro's competitiveness vis-à-vis other currencies, third country CBDCs and “stablecoins” not denominated in euro.

Enabling wide usage while ensuring a level playing field with private payment solutions

Policy Options: Legal tender

Option 1a - Digital euro without legal tender

Option 1b - Digital euro with legal tender, including general mandatory acceptance by payees

Preferred:

Option 1c - Digital euro with legal tender status with some exceptions to mandatory acceptance

Policy Options: Distribution

Option 1d - Compulsory distribution of digital euro by all PSPs

Preferred:

Option 1e - Compulsory distribution of digital euro by credit institutions with retail business

Option 1f - No compulsory distribution of digital euro by PSPs, subject to a review clause

Policy Options: Compensation

Option 1g: Merchant fee pricing left to the market

Preferred:

Option 1h: Determination of merchant fees on the basis of a methodology set by the legislature and developed by the ECB

Option 1i: Pricing recommendations on merchant fees on the basis of criteria set by the legislature

Red: preferred option included in the proposed Regulation

Orange: equally preferred option but not included in the proposed Regulation



European
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Impacts on users, PSPs, merchants

Benefits

- Users: additional choice for retail payments also in central bank money; available the same way in all payment situations (P2P, P2B (e-commerce, POS), P2G) throughout the euro area; no charge for basic services; strengthen financial inclusion
- Merchants: increased choice for payment acceptance, less reliance on ISCs; more competition on the pan-European payment market and thus hopefully lower fees,
- PSPs: digital euro standards to be used for pan-European private payment services; options for additional services, fee income
- Businesses: future use cases in industry 4.0 and web 3. M2M
- Eurosystem: supports the conduct and effectiveness of the monetary policy; contributes to financial stability and a stable macroeconomic environment,
- All : maintained trust in the monetary system due to a digital monetary anchor

Impacts on users, PSPs, merchants

Risks and costs

Consumers: learning costs, use of a device

Merchants: costs of making their terminals capable of accepting digital euro payments, annual maintenance and license fees & transaction fees. Some risk of overcharging by PSPs which is nevertheless mitigated by policy option 1h

PSPs: one-off costs (adapting front-end systems (apps, online banking, ATMs), back-end systems and AML/KYC, anti-fraud, accounting and other business processes); operating cost (customer support, AML/CFT & fraud checks, transaction management); reporting on costs to ECB; potential lower income due to lower fees from retail payments.

Eurosystem: setting up the digital euro infrastructure and operating costs; monitoring the fees on the market and determining acceptable fee levels.

All: cyber, IT and other operational risks

Policy Options: Privacy

Option 2a – No processing of personal data related to a user's identity or transactions

Option 2b – Processing of personal data related to a user's identity, but not to transaction data

Preferred:

Option 2c – Processing of personal data related to a user's identity and transaction data

Option 2d – Processing of personal data related to a user's identity, but not to transaction data for offline low value payments – non-exclusive option

Option 2e - Processing of personal data related to a user's identity, but not to transaction data for online low value payments – non-exclusive option

Impacts on users, PSPs, merchants

Benefits

Online payments:

- Fully coherent with existing payment solutions both for data protection and AML/CFT rules

Offline payments:

- Cash-like privacy for in person proximity payments in both P2P and POS situations

Risks and costs

Online payments:

- Similar risk of fraud and AML/CFT risks as for private payment means
- PSPs to bear costs and risks of onboarding customers, due diligence, data management and handling, cyber risks, filtering suspicious transactions in real time

Offline payments:

- Risk of tempering with the devices, double spending, operational risks
- High potential cost for developing, producing and managing completely secure offline solutions, which also may take longer development time
- Merchants to bear additional costs for accepting offline payments

Ensuring wide usage while protecting financial stability and credit provision

Policy Options: Financial stability and credit provision

Option 3a – Digital euro with unrestricted store of value function

Preferred

Option 3b – Possibility of introducing limits to the digital euro's store of value function

Impact on financial stability

Benefits of restricting the store of value function of the D€

- E.g. holding limits, ...
- Prevent excessive deposit outflows, preserving financial stability, mitigating the risks to credit provision to the economy
- Without undue effect on means of payments functionality [(reverse) waterfall]
- Conditions to frame restrictions

Risks and costs

- Attractiveness of holding digital euro, simplicity of use
- Competitiveness vis-à-vis other currencies, foreign CBDCs and stable coins
- Slow to adjust to changing macroeconomic and monetary circumstances if set too rigidly.

Impact on financial stability

Technical analysis /scenarios

- Difficult to have proper / model-based estimates about the demand for the digital euro:
 - depends on, inter alia, ultimate digital euro design
 - no historical data available to base estimates of take-up on
 - elasticity of substitution with deposits unknown
- Hence, the impact assessment focuses on scenario analyses, with three scenarios (take-up 1k€/resident, 3k€/resident, 10k€/resident). This broadly corresponds to ECB scenarios for comparability reasons.
- Caveats:
 - Scenarios are conservative: they assume that every depositor replaces their deposits with the maximum amount of D€ at day 1.
 - This should not be interpreted as demand estimates, especially because in many MS, the median deposit is below 3000€.

Impact on financial stability

Technical analysis /outcomes

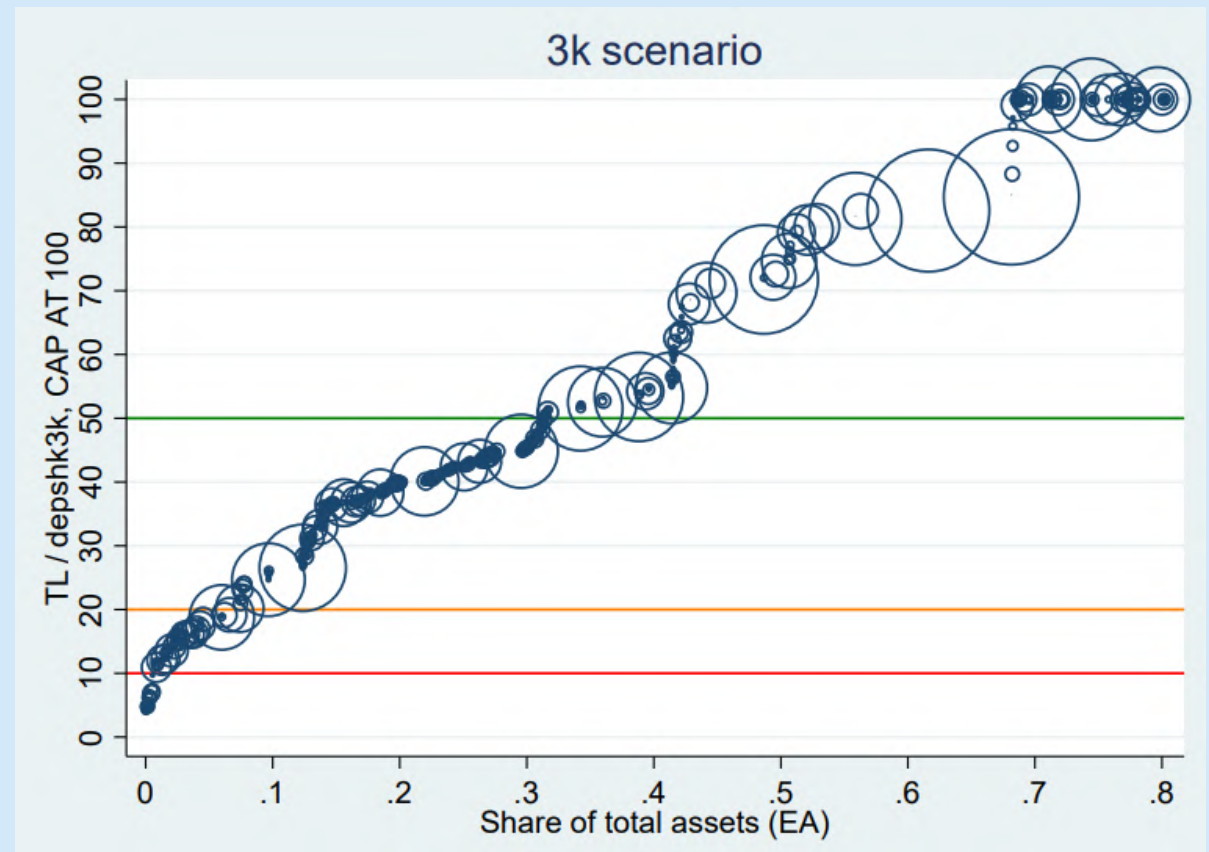
- In the moderate take-up scenarios, the aggregate banking sector can adjust to the deposit outflows in an orderly manner. More difficult in the third, more severe one.

3k€/resident scenario:

- Max shock to deposits **<5%** of total liabilities **for 90% of banks**
- **15%** of banks have available reserves smaller than the amount of the deposit shock.

10k€/resident scenario:

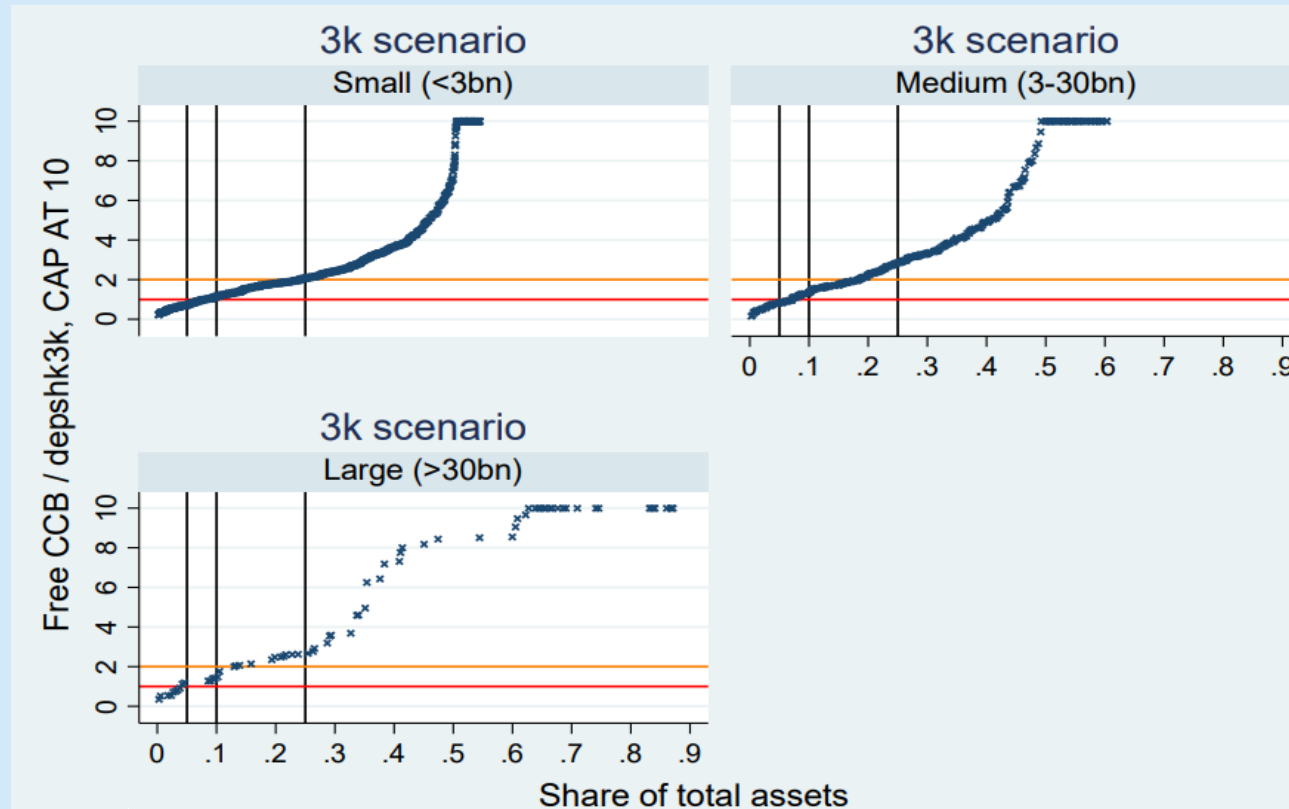
- Max shock to deposits **<25%** of total liabilities **for 90% of banks**
- **80%** of banks have available reserves smaller than the amount of the deposit shock.



Impact on financial stability

Technical analysis /outcomes

- Impact dependent on the size, business model and funding structure of the bank.
- For instance, regarding the adjustment with available reserves, there are differences by bank size: 25% of small banks (in terms of assets) have less than twice the amount of the deposit shock in available reserves (compared to a bit more than 10% of large banks).



Supporting the euro internationally while mitigating risks for non-euro countries and the Eurosystem

Policy Options: International use

Option 4a - Digital euro available for all EU residents/businesses and third countries residents/businesses

Preferred at inception:

Option 4c - Digital euro available only for euro-area residents/businesses and visitors to the euro-area

For later stages:

Option 4b - Digital euro available for visitors and under conditions for non-euro area residents/businesses and third countries residents/businesses

Impacts of international use

Benefits

- Support the EU's open strategic autonomy and the (future) international role of the euro
- Benefits for tourism sector
- Promote trade and help remittances by facilitating more efficient cross-border payments

Risks and costs

- Financial stability and monetary sovereignty risks in third countries / non EA MS; higher capital flow volatility in these countries
- Risks for the Eurosystem balance sheet
- Increased operational risks and technical challenges posed to the digital euro settlement infrastructures due to cross border operations
- Cross country supervisory cooperation and privacy challenges