Digital euro package

OVERVIEW

A digital euro can be understood as central bank money offered in digital form for citizens and businesses to be used for their retail payments. It would be a central bank digital currency (CBDC) – an electronic equivalent to cash, complementing banknotes and coins – and the central motivation to develop a CBDC can be explained by the increasing digitalisation of financial services. Banknotes and coins, currently the only public money, are considered the ultimate anchor of the financial system. However, in recent years the number of cash payment transactions has declined substantially while digital payments have soared. At the same time, private currencies, such as Bitcoin, are challenging the role of sovereign currencies. Another argument for pursuing a digital euro relates to Europe’s ‘strategic autonomy’ and the external dependency on foreign payment-related service providers.

In October 2021, the ECB launched the investigation phase for the digital euro project. It is the ECB’s prerogative to decide whether or not to issue a digital euro, but the decision requires the approval of a regulation establishing a legal framework for a digital euro. The European Commission has therefore put forward a digital euro package. While the proposal would grant legal tender status to the digital euro, the legal tender status of the physical form of central bank money would also be ensured for the first time in secondary legislation.

| Committee responsible: Economic and Monetary Affairs (ECON)  Rapporteur: Stefan Berger (EPP, Germany)  Shadow rapporteurs: Paul Tang (S&D, Netherlands); Gilles Boyer (Renew, France); Gunnar Beck (ID, Germany); Michiel Hoogeveen (ECR, Netherlands)  Next steps expected: Committee draft report

Committee Proposal National Parliament’s Opposition EESC Opinion Committee Report Plenary The vote is submitted to plenary Plenary ratification Adoption

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Members’ Research Service
PE 751.477 – September 2023

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Introduction

On 28 June 2023, the European Commission put forward a legislative package to establish a framework for a digital euro while at the same time ensuring continued access to and payment with physical euro banknotes and coins across the euro area. In order for people to have both payment options available when they want to pay with central bank money, the Commission proposes a digital euro package, which consists of three interconnected proposals:

- a proposal for a regulation on the establishment of the digital euro, as a complement to physical euro banknotes and coins, for the ECB to eventually decide whether it issues the digital euro. The legal basis for the new form of central bank money will be established and regulated based on Article 133 of the Treaty on the Functioning of the European Union (TFEU), which allows the laying down of measures for the use of the euro as a single currency by means of the ordinary legislative procedure;

- a proposal for a regulation on the legal tender of euro banknotes and coins that provides for detailed rules to preserve the effectiveness of the legal tender status of cash in practice and thus for citizens to have access to the physical form of central bank money. The scope and effects of the legal tender of cash is based on Article 133 TFEU;

- a proposal for a regulation to lay down rules for payment service providers in Member States whose currency is not the euro to allow them to distribute the digital euro. The legal basis for this proposal is Article 114 TFEU, which would secure the free movement of payment services across the Union, with payment service providers in non-euro Member States subject to similar requirements and supervisory standards as in Member states whose currency is the euro.

The digital euro package aims to complement the physical form of central bank money with a digital option. While the proposal would grant legal tender status to the digital euro, meaning, inter alia, that it is mandatory to accept payments from a payee, the legal tender status of the physical form of central bank money would also be ensured for the first time in secondary legislation.

Context

Cash is the only means of payment that allows direct in-person payments, with immediate settlement and without involvement of any third party or use of electronic equipment. In order to respond to the increasing demand for safe and trusted electronic payments, in 2021 the ECB launched an investigation phase into a central bank digital currency in Europe. Such a digital euro can be understood as central bank money offered in digital form for use by citizens and businesses for their retail payments.

Box 1: Central bank digital currencies (CBDCs)

CBDCs are digital representations of sovereign currencies, public money that is issued by a jurisdiction’s monetary authority and is reflected on its balance sheet. Retail CBDCs, such as the digital euro, are intended for general-purpose use and broad availability for citizens as a digital equivalent to cash, as opposed to wholesale CBDCs, which are limited to a set of pre-defined user groups, for instance financial institutions, to settle large value transactions.

Many central banks are exploring CBDCs with a view to ensuring the role of central bank money as a public good in the context of an accelerating digital transition.

According to a survey conducted by the Bank for International Settlement (BIS) over the course of 2022, 80 out of 86 surveyed central banks engaged in some form of CBDC. Such CBDCs must not be confused with the current form of crypto assets. In contrast to CBDCs, crypto assets do not represent a claim on a central bank, but are generally defined as a type of private sector-issued digital asset that depends primarily on cryptography and distributed ledger or similar technology.1
Existing situation

Along with the ongoing digitalisation of the economy, there has been a significant shift in the way citizens pay each other. According to a survey conducted by the ECB between 2021 and 2022 to investigate the payment attitudes and behaviours of euro area citizens ('Study on the payment attitudes of consumers in the euro area' (SPACE)), cash remains the payment method used most frequently at the point of sale. However, the share of cash payment transactions has declined substantially over recent years, from 79 % in 2016 to 59 % in 2022. Most of this decline is accounted for by increased use of card payments, up from 19 % in 2016 to 34 % in 2022. Furthermore, around 3 % of payments made use of mobile phone apps. When measuring monetary transactions in terms of value, the share of card transactions in 2022 (46 %) was higher than the share of cash transactions (42 %) for the first time.

The trend towards digital payments is expected to continue, all of which are currently based on commercial money, i.e. transfer of a claim on commercial banks, as opposed to public money issued by a central bank. This raises the question of how a central bank can ensure the issuance of public money should the share of cash payments, which is currently the only form of public money, further diminish. This would also have an indirect implication for the acceptance of commercial money. Meanwhile, more and more countries outside the EU are actively engaging in developing CBDCs, while there is continued interest in private sector payment solutions, including stable coins and other crypto assets. Those trends prompted the ECB to initiate its own investigation phase into a digital euro to look at solutions to uphold the value and sovereignty of the euro and ensure it is not supplanted by a digital currency from another jurisdiction or a private company.

Figure 1 – Share of payment instruments used at the POS in terms of number of transactions, euro area, 2016-2022 (in %)

Number of transactions

<table>
<thead>
<tr>
<th>Year</th>
<th>Cash</th>
<th>Cards</th>
<th>Mobile app</th>
<th>Other</th>
</tr>
</thead>
<tbody>
<tr>
<td>2016</td>
<td>79%</td>
<td></td>
<td>19%</td>
<td></td>
</tr>
<tr>
<td>2018</td>
<td>72%</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2022</td>
<td>59%</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>


Notes: ‘Other’ includes bank cheques, credit transfers, loyalty points, vouchers and gift cards and other payment instruments. Percentages may not add up to 100 % due to rounding.
Preparation of the proposal

The Commission’s digital finance strategy, issued in September 2020, featured the digital euro as part of the retail payment strategy. One month later, the ECB published its Report on a digital euro, as a first step to gather views on a possible design. On 14 July 2021, the ECB officially started its investigation phase for the digital euro project. Initially planned for 24 months, so far the ECB has published four progress reports. The progress reports provide information on the motivation to establish a digital euro, address key issues relating to the design and distribution of a digital euro, and lay down specific design options with regard to the infrastructure, distribution and privacy concerns.

- The ECB’s first progress report focused on the underlying functionalities and limits for digital euro users. Several key issues were analysed, including privacy considerations and online and offline usage.
- The second progress report clarified the roles of actors involved in the settlement and distribution of the digital euro. Users would have a direct claim on the central bank while distribution and direct interaction with the user would be done by intermediaries like PSPs.
- The third progress report established functionality categories, for core, optional and value-added functionalities. It further highlights the geographical distinction between euro area residents and non-residents with a digital euro account.
- The fourth progress report focuses on the compensation model for a digital euro, a core element of the legislative proposal, and presents progress on a draft rulebook that establishes use cases and user journeys for a digital euro.

Complementing an ECB consultation from 12 October 2020 until 12 January 2021, the Commission launched a targeted consultation on 5 April 2022 with the aim of collecting further information on expected impacts on key industries, users and other stakeholders. Based on this, and accompanying the legislative proposal, the Commission published its impact assessment. Four key trade-offs were examined: (i) wide usage vs. fair competition with private payment solutions, (ii) wide usage vs. protecting financial stability and credit provision, (iii) protecting privacy vs. ensuring traceability, and (iv) international use vs. risks for non-euro countries and the Euro system.

The changes the proposal would bring

The digital euro package would establish a new, digital form of central bank money, alongside euro banknotes and coins. The purpose of this legislation is to regulate the main aspects of a digital euro to ensure that the same rules and conditions are applied throughout the euro area when using the digital euro. In addition, the legal tender status of banknotes and coins, and the acceptance of and access to cash, is codified and clarified in relation to the legal tender status of the digital euro in an accompanying proposal. Lastly, to allow all EU payment service providers to distribute the digital euro across the euro area, a third proposal for a regulation aimed at Member States whose currency is not the euro complements the digital euro package. The digital euro package would bring the following main changes:

1. Complementing euro cash, a digital euro would, as a first step, be available to the euro area, for online as well as offline transactions. With a few exceptions, it would be obligatory for all payees to accept the digital euro and thus it would be equivalent to cash, while also being convertible at par with private money.

2. Transactions offline would be possible without an intermediary, and thus no personal or transaction data would be processed. Meanwhile, online payments would be treated the same way as other electronic means of payment. Through pseudonymisation or encryption of personal transaction data, neither the ECB nor national central banks...
Digital euro package

would be able to directly attribute transactions to an individual digital euro user, while payment service providers (PSPs) would manage digital euro accounts and provide funds to satisfy demand. There would be no contractual relationship between the digital euro user and the central banks.

3 The ECB would define policy instruments to limit the use of the digital euro as a store of value to safeguard financial stability. No interest would be paid on digital euro holdings.

4 On an equal footing to the digital euro, the legal tender status of banknotes and coins would be codified, based on a ruling of the ECJ, for the first time in secondary legislation.

5 To uphold the freedom to provide services and avoid fragmentation of the internal market, an additional piece of legislation provides for obligations for PSPs in non-euro Member States and for their supervision and enforcement in order for PSPs to distribute the digital euro.

Regulation on the establishment of the digital euro

What is being issued? The purpose of the regulation is to establish a digital euro, a retail CBDC that the Euro system may decide to issue. Like cash, the digital euro would be granted legal tender status, meaning that it is mandatory for payees to accept it, with very few exceptions (such as microenterprises or persons acting in a purely personal capacity). Additional future exceptions, due to technical specificities, are proposed to be delegated to the Commission. The euro in digital and in cash would be convertible at par; the responsibility for issuing the digital euro would lie with the ECB.

How is it distributed? All PSPs authorised in the EU would be able to provide their services and distribute the digital euro. While obligatory for credit institutions that are already active in retail business services, providing such services would be optional for electronic money institutions, payment institutions or post office giro institutions which are entitled under national law to provide payment services. PSPs would provide services from basic tasks like funding and defunding functionalities, to be offered for free (Annex II), to additional innovative services that they offer for comparable means of payment.

Is there a holding limit? A digital euro would not bear interest and would have a holding limit so as to limit its store of value function to safeguard financial stability. A policy tool to limit the digital euro’s use as a store of value could, for instance, include quantitative limits to individual digital euro holdings. The ECB would regularly report on the policy instruments to limit the use of the digital euro as a store of value as well as their parameters, including its impact on the role of financial intermediaries in the financing of the economy. Consequently, while natural or legal persons may have more than one digital euro payment account at several PSPs, they would be subject to an individual holding limit. To enforce individual holding limits, a single access point for digital euro user identifiers and the related holding limits would be established.

A so-called ‘waterfall functionality’ should allow for successful execution of transfers in situations where a holding limit becomes binding, either on the payer’s or the payee’s side, or the amount on the digital euro account is less than the transaction amount, by linking the digital with a non-digital euro payment account. This way, any surplus or deficit on the digital euro payment account due to a single transaction would be balanced through a non-digital euro payment account. A PSP cannot charge a digital euro account holder when using a linked non-euro digital payment account with another PSP when using the waterfall functionality.

Is on- and offline use possible? A digital euro could be used on- and offline. Transactions offline would be possible without an intermediary, and thus no personal or transaction data would be processed. Offline transactions would require a bearer instrument (peer-to-peer validated) which would encompass a specific user device (like a smartphone or a card) in order to work without internet connectivity. However, similar to the use of physical banknotes and coins, such a device
would need to be charged first for it to be used offline. This way, transactions executed offline would be anonymous and thus cash-like.

In contrast, transactions online would be validated by third-party intermediaries and PSPs would be able to process the personal data necessary to ensure a proper functioning of the digital euro. While the digital euro would allow for conditional payments, for instance for automatic payment instructions, it would not be programmable, meaning there are no time and product-specific limits to using the digital euro.

**How is privacy and data protection ensured?** For offline digital euro payment transactions, no personal transaction data would be transmitted, thus offering a higher privacy level than online payments. However, should a user be suspected of money laundering or terrorist financing, data on funding and defunding transactions should be transmitted to Financial Intelligence Units and other competent authorities.

To settle online digital euro payments, the personal data would need to be processed, by the intermediary to execute the transaction and by the ECB to record the new balance on their account. However, before it reaches the central bank, the personal and related transaction data would be anonymised through pseudonymisation or encryption. This way, personal transaction data would be protected and neither the ECB nor the national central bank could directly attribute transactions to an individual digital euro user. For PSPs, online digital euro payment transactions would follow the same data protection, privacy and anti-money laundering requirements as other electronic means of payment. Anti-money laundering aspects are considered through regulatory technical standards on customer due diligence when opening a digital euro payment account and simplified due diligence measures for low-risk transactions or business relationships that PSPs would apply.

**What about fees and compensation?** As the digital euro is a public good with legal tender status, the combination of mandatory acceptance and free basic services implies costs for intermediaries and merchants. To ensure that fees and charges (e.g. merchant service charges or inter-PSP fees) are uniform across the euro area and proportionate, such costs would be regulated. The ECB would regularly monitor the relevant costs, fees and charges to ensure that they do not exceed the lower amount of either (i) the relevant costs of PSPs, which would include a reasonable margin of profit, or (ii) charges for comparable means of payment. Similarly, the ECB would incur costs to support the provision of digital euros, including a front-end service which users might use to access and use the digital euro. Also, in this case, the Euro system would not have a contractual relationship with the digital euro user. PSPs would provide either their own or a third-party front-end solution but may use the ECB front-end service themselves without charge.

**Who can use the digital euro?** The digital euro would be first available to residents of the euro area or visitors. Subject to arrangements between the ECB and the respective central banks in non-euro Member States and bilateral agreements between the Union and third countries, the digital euro could be available outside the euro area at a later stage and thus might cover cross-currency payments.

**Legal tender of euro banknotes and coins**

The concept of legal tender, as interpreted by the European Court of Justice (ECJ), implies that accepting euro cash is (i) mandatory, (ii) at full face value, and (iii) has the effect of discharging payment obligations. The draft regulation on the legal tender of euro banknotes and coins codifies a ruling of the ECJ (C-422/19 and C-423/19) that it must be possible, as a general rule, and in accordance with the concept of cash as legal tender, to be able to pay in cash for services and goods across the Eurozone.

Besides the acceptance of cash, which poses relatively little margin for policy choices, another aspect to the legal tender of cash considered in this regulation is access to cash. Member States would have the responsibility to designate oversight and regulatory powers to national competent authorities to ensure acceptance and access to cash and to provide an assessment of sufficient and
effective access in their country-specific context. This assessment by Member States, through an annual report to be addressed to the Commission and the ECB, would be based on an implementing act by the Commission defining common indicators which would allow Member States to assess acceptance of (e.g. level of ex ante unilateral exclusions of payments in cash) and access (e.g. density of cash access points in relation to the population) to cash. Should the assessment yield a negative outcome, the report should highlight policy measures to remedy the situation, for instance prohibiting exclusion of cash or geographical access requirements. If no or insufficient remedial measures are taken by the Member State, the Commission would be empowered to adopt implementing acts to address country-specific measures.

Similar to the exceptions for accepting the digital euro, the regulation lays down conditions under which a refusal to accept euro cash would be legally possible, for instance where an enterprise has no change available at the relevant time. Here again, additional future exceptions are proposed to be delegated to the Commission.

 Regulation for payment service providers in non-euro Member States

As all PSPs within the EU’s internal market should be able to provide services to digital euro users (see Article 56 TFEU), this regulation specifies obligations for PSPs in non-euro Member States and their supervision and enforcement in order for PSPs to offer such services. Thus it ensures the free movement of payment services across the Union and avoids fragmentation of the payment services sector. Based on a directive for payment services in the internal market and a directive for anti-money laundering, competent authorities would be responsible for supervising and enforcing any obligations with respect to the digital euro.

 Advisory committees and European authorities

In its own-initiative opinion of 26 October 2022, the European Economic and Social Committee (EESC) supports the steps taken by the ECB/Euro system towards the introduction of a digital euro. Furthermore, it calls on the ECB to set out various design options, given the complexity of the project.

Beyond the four progress reports, the ECB also established a Rulebook Development Group (RDG) in January 2023. The group is composed of 22 senior professionals from the public and private sector with experience in finance and payments. It has a mandate to develop a digital euro rule book and is tasked with establishing the main framework for the digital euro, developing functionalities and user experiences, and developing the digital euro’s compensation model, including economic incentives and fees for distributors.

 National parliaments

In accordance with Article 3(1) TFEU, the Union has exclusive competence in the area of monetary policy for the Member States whose currency is the euro. In this area, action by the euro area Member States is not possible and the principle of subsidiarity thus does not apply.

 Stakeholder views

The targeted consultation ran from April 2021 until June 2022, complementing an ECB consultation. The aim was to collect further information on expected impacts on key industries, users and other stakeholders.

The European Banking Federation (EBF), representing 33 national banks and 3 500 banks in total, published a vision paper for a digital euro. In this paper, the EBF argues that a retail digital euro could be envisaged in the mix of new tools and solutions to meet evolving payment needs, as long as it adds value to consumers, is appropriately designed, in close cooperation with the private sector,
and mitigates ex ante the accompanying risks'. However, in their view a retail digital euro is one element in a digital money ecosystem of the future, which would also include a wholesale CBDC and bank-issued money tokens. While, in general, the outlined ideas are reflected in the Commission proposal, the EBF argues for a cross-border payment functionality, compatible with DLT, that should be factored into the ECB’s work on a wholesale digital euro at an early stage.

Contrary to the EBF, the German Banking Industry Committee’s position on the Commission’s legislative proposal is opposed to a digital euro as a retail payment scheme, as it should be issued purely as a means of payment. In their view, the market-driven design of retail payment schemes must be left to the private sector. According to their position paper, the ECB’s design of the digital euro would put existing and future European private-sector retail payment schemes at a disadvantage and thus counteract the digital euro’s goal of strengthening Europe’s sovereignty.

The Digital Euro Association Working Group (DEA), a think tank specialising in CBDCs, stablecoins, crypto assets and other forms of digital money, responded to the digital euro proposal with detailed comments and recommendations. The latter, in particular, focus on (i) holding limits and the necessary exchange of data, (ii) fees for digital euro payments and the fee structure that, according to the DEA, should be closer to the legislative proposal on instant credit transfer, and (iii) undefined privacy-preserving measures in the legislative proposal.

**Legislative process**

The three proposals were referred in the European Parliament to the Committee on Economic and Monetary Affairs (ECON); the rapporteur for all proposals is Stefan Berger (EPP, Germany).

The ECB Governing Council is set to review the outcome of the investigation phase in the autumn of 2023 and will decide, on this basis, whether to move on to a potential realisation phase. In this next phase, technical solutions and business arrangements would be developed and tested. This exercise might, to some extent, depend on the legislative framework that is the core subject of this briefing. Importantly, the project phase is not equivalent to an eventual decision on issuance of a digital euro.

**Parliament's starting position**

In October 2021, Parliament adopted an own-initiative report on the ECB’s annual report, welcoming the ECB’s preparations to introduce a digital euro and stressing that a digital euro must not endanger cash as a means of payment. At the same time, in a resolution on the Banking Union report and in response to the report on the ECB's public consultation, Parliament points out the impact on the banking sector, depending on the precise design features of a digital euro, and invites the ECB to conduct further analysis of the implications of a digital currency for the banking sector.

The following year, in its resolution on the ECB annual report 2021, Parliament calls on the ECB to address concerns about privacy, security, accessibility, the ability to pay across the euro area, preventing additional costs, and offline usability. Furthermore, the resolution recalls that cash payments are a very important means of payment for EU citizens and should not be endangered by a digital euro.

For the ECB annual report 2022, Parliament adopted a resolution in February 2023, welcoming the dialogue with Parliament in this regard and looking forward to the Governing Council reaching a decision on the start of the process for launching the digital euro once the legal base for this is provided by the co-legislators.

Through regular hearings, Fabio Panetta, Member of the Executive Board of the ECB, reported to the ECON committee and provided updates on the ECB’s progress throughout the investigation phase of the digital euro project. In a plenary debate on 19 April 2023, Parliament discussed progress on the digital euro project with members of the Council and the Commission.
The Council's starting position

Member States have expressed their views mostly through Eurogroup meetings. Informed by the preliminary work of the ECB and the European Commission, in March 2021 the Eurogroup invited the exploratory work on the possible introduction of a digital euro to be taken forward. In July 2021, the Eurogroup agreed on a process for holding discussions on the key political dimensions of the digital euro. Through continued discussion, including several stock-takings, the Eurogroup reaffirms its support for the preparatory work on the potential issuance of a digital euro. In its latest meeting in July 2023, the ministers continued their discussions on the digital euro.

There is broad agreement on the potentially vital role of a digital euro for ensuring access to public money in an increasingly digitalised global economy.

EUROPEAN PARLIAMENT SUPPORTING ANALYSIS


OTHER SOURCES

ENDNOTES

1 Distributed Ledger Technology (DLT) refers to a novel approach to recording and sharing data across multiple data stores (or ledgers). This technology allows for transactions and data to be recorded, shared, and synchronised across a distributed network of different network participants. The network can be a publicly accessible database or may be restricted to a specified group of users. From a technical perspective, it can be used, for example, to record transactions across different locations. A particular type of distributed ledger is often referred to as ‘blockchain’, which makes a shared ledger possible to run. All individual transactions are stored in groups, or blocks, which are attached to each other in chronological order to create a long chain. This long chain is put together using a mathematical formula – complex cryptography – which ensures the security and integrity of the data within a network in an immutable manner. This chain then forms a register of transactions that its users consider to be the official record.

2 A retail CBDC differs from existing forms of cashless payment instruments (i.e. credit transfers, direct debits, card payments and e-money), as it represents a direct claim on a central bank rather than the liability of a private financial institution.

3 See first, second, third and fourth progress report published by the ECB.

4 Generally referred to as ‘privacy enhancing technologies’ (PETs), these are digital solutions allowing for information to be collected, processed, analysed, and shared while protecting data confidentiality and privacy. See, for instance, OECD, Emerging privacy-enhancing technologies, OECD Digital Economy Papers, March 2023.

5 Johannes Dietrich and Norbert Häring v Hessischer Rundfunk (C-422/19), Judgment of the Court (Grand Chamber) of 26 January 2021.

6 The ECB’s third progress report states that ‘individuals would be subject to uniform holding limits, which would cover day-to-day payments in each euro area Member State. Merchants and governments in the euro area would have zero-holding limits’, meaning that they can receive and make payments in digital euros but will not have holdings. In a speech in June 2022, ECB Executive Board Member Fabio Panetta disclosed preliminary estimates for the total digital euro holdings ranging between one and one and a half trillion euro, which would avoid negative effects for the financial system. This would allow for holdings of around €3 000 to €4 000 euro per capita. See also Meller B. and Soons O., Know your (holding) limits: CBDC, financial stability and central bank reliance, Occasional Paper Series No 326, August 2023, who simulate how individual banks respond to outflows of deposits, suggesting that €3 000 would contain a liquidity risk for Eurosystem balance sheets.

7 A compensation model for intermediaries and merchants is developed in the fourth progress report published by the ECB.

8 So far, the legal basis of the legal tender of banknotes and coins is based on a Commission recommendation from 2010 (2010/191/EU).

9 See the European Parliament Legislative Observatory 2023/0212(COD), 2023/0211(COD) and 2023/0208(COD) for the main dates and the details about the legislative procedure in Parliament.

10 While the Euro system intends to retain control over the issuance, redemption and settlement of digital euros, it has not shed light on the underlying technology to be used. Additionally, the impact assessment states that a ‘digital euro is technology-neutral i.e. it may or may not use DLT/blockchain technology’.

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First edition. The 'EU Legislation in Progress' briefings are updated at key stages throughout the legislative procedure.