

**Status Report of the
Network Governance Working Party**

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UNNECESSARY OR UNFIT FOR PURPOSE?

This report is to advise members of issues that arose at the first meeting to look at the Draft Directive on "The Distance Selling of Personal Financial Services".

The purpose of the Directive is "to establish a harmonised and appropriate legal framework for distance contracts pertaining to financial services". This statement invites the question as to how the proposal relates to the legal frameworks for:-

- Distance selling of other goods and services;
- Financial services generally;
- Consumer protection generally;
- Electronic commerce.

The definition of financial service is a 'catch-all' which leaves scope for member states to decide precisely what to include. However many goods sold at a distance, e.g. personal computers, are bundled with extended credit and warranty terms. Where these are backed by formal contracts with credit institutions and insurance companies, the Directive clearly applies, but where the vendor carries the credit/warranty risk the situation is not clear. However, from the consumer point of view, this is a single transaction to which a uniform code of protection should apply.

The proponents of this Directive seem to believe that the Internet is a high pressure selling environment but that face-to-face selling is somehow less threatening. In practice the reverse is true. The Internet is essentially a reactive medium where formal procedures can be applied consistently and with the facility for comprehensive audit trails. By contrast, face-to-face selling is dependent on the knowledge, ability and honesty of the salesperson for adherence to formal procedures; furthermore, audit trails depend on subjective reporting by the salesperson, post-event.

The proposal relies on 'periods of reflection' as a consumer protection device. These periods conflict with existing legislation and practice, being in some cases better, in some cases worse and in others totally inappropriate, depending on the product and member state involved. For consumer protection, the most important factor is provision of clear and easily understood information. This requirement is the same regardless of the sales method used.

The conflicts with existing legislation are in areas such as insurance, which is governed by an existing EU Directive, and consumer credit, governed by national legislation. In implementing the Directive, member states will therefore face the choice of:-

- implementing the periods of reflection for distance sold products only, thus introducing differences in the level of protection between distance and face-to-face sales;

or

- bringing the level of protection for face-to-face sales in line with distance sales.

In either case, to meet existing local levels of protection, periods of reflection for some products in some member states will have to be set at levels exceeding the minima laid down in the Directive. As a result, there will not be a truly harmonised regime throughout the community.

More importantly, the proposal attempts to define the process for making an electronic contract. However, there is another proposed Directive (on Certain Legal Aspects of Electronic Commerce in the Internal Market) which attempts to define the conditions for making electronic contracts, generally. Needless to say, the two Directives conflict with each other. It seems to be absolute nonsense to attempt to legislate for financial services contracts before the general principles relating to electronic contracts have been established.

Another area of potential conflict between the two Directives lies in the area of liabilities of intermediaries. The Distance Selling Directive, although presumably aimed at financial intermediaries such as insurance brokers, adopts a catch-all definition which could be construed to include "mere conduits", that is to say organisations such as Internet Service Providers which are facilitators rather than principals or agents. On the other hand, one of the principal purposes of the Electronic Commerce Directive is to limit the exposure to liability of "mere conduits". This is another example of why the Distance Selling Directive should follow the Electronic Commerce Directive so that it can be considered in the context of an established regime for electronic commerce.

Overall, there are mixed views in the business community regarding this proposal. Generally speaking, the larger multinational companies who wish to transact substantial volumes of cross-border business are seeking harmonisation. On the other hand, smaller organisations in industries such as insurance, where there is an existing EU legislative regime, would prefer to leave the existing regulatory structure unchanged. Therefore, once again, we face the political issue of Common Market vs. Single Market.