

# DRAFT PARTIAL REGULATORY IMPACT ASSESSMENT

## 1. (i) Title of proposed measure:

### **The Information Society Services Regulations 2001<sup>1</sup>**

## 2. (i) The issue and objective:

**Issue:** Electronic commerce provides the UK and the rest of the European Community with an opportunity to stimulate economic growth, industrial competitiveness and employment. To facilitate this it is desirable to put in place an effective legal framework that would remove the chief obstacles to providing services electronically within the European Community. The Regulations will aim to do this and to meet legislative obligations in respect of the E-Commerce Directive. UK businesses will have to ensure that they are in compliance with the provisions of Regulations to be drafted and to come into force before the implementation date for the Directive in all member states, which is 17 January 2002.

**Objective:** The purpose of the Regulations will be to create a framework within which UK business, and SMEs in particular, and consumers will have the legal certainty needed to take full advantage of the opportunities offered by electronic commerce. The main areas to be addressed are:

- a) identifying and clarifying rules so that both consumers and business have greater confidence about whose laws apply to an online transaction;
- b) ensuring transparency and consistency in the information to be provided by sellers to consumers about themselves, their offerings and how to conclude a contract online;
- c) ensuring consistency in aspects of online commercial communications such as definitions of advertising, conditions for unsolicited emails, and lifting any restrictions on advertising online by the regulated professions;
- d) legal validity of electronic contracts;
- e) limiting the liability of intermediaries who transfer information from supplier to consumer, but are not aware of its content or legality; and
- f) encouraging business codes of conduct and alternative means of dispute settlement

## 2. (ii) Risk Assessment:

The risks discussed below correspond to the six areas identified in the previous paragraph:

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<sup>1</sup> [Provisional title of draft Regulations] Transposing Directive 2000/31/EC of the European Parliament and of the Council of 8 June 2000 on certain legal aspects of information society services, in particular electronic commerce, in the Internal Market (Directive on electronic commerce) (OJ L 178, 17.7.2000, p. 1). The text (PDF 106 KB) is at [http://europa.eu.int/ISPO/ecommerce/legal/documents/2000\\_31ec/2000\\_31ec\\_en.pdf](http://europa.eu.int/ISPO/ecommerce/legal/documents/2000_31ec/2000_31ec_en.pdf)

- a) A substantial barrier to the more confident and widespread use of electronic commerce within the EC is the risk of unwitting breach of any of the 15 different sets of national legislation. As the UK is a nation with a relatively high proportion of foreign trade, UK business is particularly exposed to any obstacle or risk associated with doing online business abroad. Compliance with regulations prevailing in the Member State in which the recipient of the service is located entails considerable expense for business wishing to provide electronic services across borders, both in terms of ensuring activities are lawful and keeping abreast of any alterations to the legal framework. Moreover, the absence of a harmonised legal framework may create uncertainty for the recipient of the service. The Regulations will implement a partial harmonisation of single market rules so as to reduce the cost and time burden.
- b) Without specific information, the consumer will not know where to complain if necessary, and it will be difficult to ensure that the service in question is supervised at source. Information about the seller, the relevant authorities in the seller's home country, the products and services and their prices, and what to do to order online, needs to be clear. In particular, consumer take-up is also likely to be inhibited by a diversification of approaches.
- c) Similarly, unless the consumer has information about an online advertiser (or the person on whose behalf he is advertising), he will not be able to protect himself effectively against unwanted or unsolicited advertising emails. Without requirements that advertising emails are flagged as such, and that senders of unsolicited emails check opt-out registers, users may be discouraged from entering into e-commerce by the potential costs and difficulties of managing their electronic inboxes.
- d) Businesses and consumers may also be discouraged from using e-commerce if there is concern that electronic contracts may be invalid or unenforceable just because they are electronic, or because their validity or enforceability depends in part on something being done physically.
- e) Without some harmonisation of the conditions under which intermediary providers of access and storage services could limit their liability for illegal or harmful information and activities, disparities in treatment by national authorities may grow, and competitiveness suffer.
- f) Unless member states remove barriers to codes of conduct and settlement of disputes without going to court, consumers and businesses in the EC will not benefit as much as possible from these informal means of improving quality of service and mutual confidence, in which practice in Europe is at present among the best in the world.

There are also major risks associated with a failure to implement the provisions of the Directive correctly into UK law. This could lead to proceedings being brought by the Commission in the European Court. Failure could also lead to the Government being held liable by UK courts for any losses suffered by those denied their rights under the Directive.

### **3. (i) Identification of options:**

Two principal options have been identified:

Option 1 - do nothing .

Option 2 – specific implementation of the provisions of the Directive, in general and in detail.

This assessment will be developed to cover the main options involved in each of the different subjects covered in the Regulations, in the light of consultation.

### **3. (ii) Issues of equity or fairness:**

- The harmonisation resulting from the draft Regulations should reduce the exposure of the public to certain risks.
- The Regulations should improve the confidence of actual and potential consumers to engage in e-commerce and promote a level playing field for SMEs.
- The draft Regulations are intended to impact evenly across all sectors of online service provision.
- Though the Regulations will apply to large and small businesses alike, SMEs in general have less administrative capacity to ensure compliance. However, they stand to benefit disproportionately, through easier access to new markets. SMEs trade less abroad than large companies, but even those confined to the UK market stand to benefit from the Regulations as most of the information, advertising and other provisions apply also to domestic transactions.

### **4. Identification of the benefits:**

Option 1: This has the benefit that there would be, for the time being at least, no change to the current legal framework. The immediate cost for government and business should therefore be lower, and consumers would continue to benefit from current levels of protection.

Option 2: This has the benefit of allowing UK providers of online services to comply with only one national legislation – that of the UK - in most matters, wherever they do business in the EC. It removes the need to track and comply with up to 15 national legislations when providing such services within the EC (or indeed up to 18 sets of legislation when implemented by Norway, Iceland and Liechtenstein under the EEA agreement). It ensures that services can be provided in all areas within the scope of the Directive without regulatory intervention other than in the service provider's home state (except where a derogation may apply). It also benefits businesses and consumers by strengthening contractual certainty. It has the potential for additional benefits through encouraging the adoption of codes of conduct at both the national and international level, and facilitating administrative cooperation between Member States, which should contribute to a lighter and more effective regulatory framework.

### **4. (ii) Quantifying and valuing the benefits:**

The Regulations will implement a complex Directive, with implications across several major areas of EC law. Only broad, qualified estimates of its financial impact can be made. It is possible, however, to give an indication of the costs which service providers operating in a number of EC states currently bear, and which the Regulations would remove or decrease substantially.

The explanatory memorandum accompanying the original proposal for a Directive cites several examples of the costs associated with compliance with multiple sets of Regulations, following a survey carried out by the Commission. In order to ensure compliance with different regulations, respondents indicated that they require considerable legal advice: examples were 50 days of legal advice to set up an appropriate system; 3-4 days of advice per month; and half an hour per month to maintain the system. One German estimate was 70,000 Deutschemarks per year. Another operator estimated that a review of the regulatory framework for online services in the UK alone had cost 60,000 euros. Assuming comparable review costs for each Member State, dependence on regulatory control in the state of destination might cost a company 900,000 euros were it to cover all of the EC, with ongoing costs of around 70,000 Deutschemarks a year thereafter. Given the implications of the EEA and the requirements of the applicant states to implement the directive on or before accession, these costs can be roughly doubled in respect of pan-single market operation in the medium term. This compares to costs of regulatory control in the country of origin, which might for such a business be £40,000 initially, with minor recurrent costs thereafter. These are very general indicative illustrations. The simple calculation below takes much lower figures as its basis.

There were 3.7 million businesses in the UK at the start of 1999. Only 7,000 were large i.e. over 250 employees; and 24,000 were medium i.e. 50 - 249 employees. Small businesses (those with less than 50 employees) made up 38% of all turnover and most were micro i.e. 1 - 9 employees. 2.3 million businesses were sole traders or those without employees. The UK Online Annual Report 2000 indicated that 450,000 SMEs were actually trading online, and seven out of ten entrepreneurs were pursuing e-commerce opportunities. Over 81% of all British businesses are now online (and over half of micro-businesses)

Assuming the benefits of doing without one-off review costs are on average £15,000 and yearly costs thereafter are £5000 for the 31,000 large and medium companies (who are assumed to want or need to trade online widely in the single market), and respectively £3000 and £1000 for say 200,000 SMEs likely to trade online in Europe, this produces one-off benefits for the UK of about £1 billion and yearly savings of about £350 million.

This calculation leaves out sole traders, and businesses not yet online. It disregards the likelihood that many businesses will either have already done a one-off review, or would still want to do a substantial periodic review of legal conditions for trading across borders in Europe.

Whilst this example is only illustrative, it does suggest the order of magnitude of the savings which may accrue to businesses - and ultimately to the consumer - through Regulations implementing Option 2. The calculation is also sensitive to the precise scope of implementation in UK national law and that of the different member states. Option 1 would not yield these benefits, but would avoid the costs associated with transposition, implementation and enforcement of the Directive.

## **5. Compliance Costs for Business. Charities and Voluntary Organisations**

### **5. (i) Business Sectors Affected:**

The Regulations will affect everyone providing online services within the internal market, given the definition of "Information Society Services" as any service normally provided for remuneration, at a distance, by electronic means and at the individual request of a recipient of services. It follows that the Regulations will affect a large number of businesses, charities and voluntary organisations now and their numbers should increase as the attractiveness of e-commerce grows.

#### **5. (ii) Compliance Costs for a "typical" business:**

The following costs are for option 2; option 1 imposes no immediate direct additional costs on business.

There will be costs relating to ensuring that the provision of services complies with all the relevant national legislation. In some cases there may be a cost of changing to compliance with UK legislation instead of that of particular markets in the EC. If these costs are greater than those which businesses bear at the moment, however, it is likely to be because of compliance with other instruments (covering advertising, licensing etc), since the present Regulations will merely require compliance with home state controls in such areas.

There will be some additional expense involved in ensuring that the details provided on a website or other means of promoting the service are correct. However, the type of information provided is not expensive to procure, the majority of responsible businesses would aim to provide such information anyway, and the costs and effort concerned would probably be integrated with the burden of meeting the interrelated information requirements of the Distance Selling Regulations 2000.

There may also be some costs for certain businesses (those standing to benefit from the sending of unsolicited commercial communications) from the requirement for information provision and software changes, and consulting opt-out registers, though much of this is already undertaken by advertisers in accordance with industry standard practice.

The Regulations may result in some one-off expenses for affected organisations. These would result from any necessary alterations to the systems in place, and would vary according to the organisation. They are very hard to estimate with any degree of accuracy. None of the 100 respondents was able to give an estimate of any of these costs in DTI's consultation exercise on the draft Directive in 1999, and only one respondent felt able to suggest the areas in which costs would be reduced or increased, despite a specific question about this.

#### **5. (iii) Total Compliance Costs:**

The costs of compliance with these Regulations will depend on the size of the organisation, its current level of involvement in e-commerce, the extent of the changes required to comply with the Directive, the level of systems change required and the extent to which alterations resulting from this Directive are made as part of the process of updating and upgrading required to provide an effective online service

#### **6. Consultation with Small Business: "The Litmus Test"**

Small businesses and small business have not yet provided figures for compliance costs. In principle, costs for small businesses would in themselves be lower (but greater in proportion

to revenues) and benefits higher, than for larger businesses. During the remainder of the consultation process we shall have discussions with organisations representing small business interests and identify and contact a small cross section of small businesses trading online to obtain first hand views on cost/benefits of the options. The Small Business Service will continue to offer advice on the development of this assessment.

## **7. Identification of any other costs**

Option 1: The absence of specific implementation of the Directive is likely to cause uncertainty that will inhibit the growth of electronic commerce, and therefore potentially impose costs on the UK resulting from e.g. reduced competitiveness, lower employment and less economic growth.

Option 2: Transposition of the Directive by legislative and non-legislative means and enforcement of the Regulations will entail additional costs for Government and other organisations as set out below.

There will be enforcement costs for UK national regulatory authorities (Director General of Fair Trading, Trading Standards Officers, Financial Services Authority etc) acting on behalf of consumers in other Member States and encouraging other Member States' authorities to act on behalf of UK consumers.

There will be additional costs for industry and consumer organisations and their members to develop and apply Codes of Conduct and means of alternative dispute resolution (though balanced by savings from necessarily having recourse to court procedures).

Additional administrative functions also flow from Articles 16, 17, 19 and 21 of the Directive that are not directly implemented by the Regulations. Activities that will need to be resourced include:

- Implementing and monitoring the Regulations and other obligations under the directive
- Encouraging the development of Codes of Conduct (eg in the areas of intermediaries' liability, consumer information, treatment of advertising) and means of alternative dispute resolution
- Establishing and acting as contact points for the provision of advice and assistance to business and consumers
- Forwarding information to the Commission on developments in the UK, attending discussions on the implementation of the Directive, and participating in the review of the Directive in 2003 and every two years thereafter
- Providing information and assistance when sought by other member states, co-operating with their requests for regulatory enforcement action and the search for acceptable solutions to cross-border problems before Community legal action is invoked.
- The operation of the procedures associated with the exercise of the possible derogations from the country of origin principle, whether invoked by the UK or by other member states in respect of services originating in the UK.

## **8. Results of Consultation**

DTI consulted generally on the draft Directive in 1999 and received over 100 contributions from businesses, consumers, their representative organisations and others. In the course of general discussions with interested parties, a number of other unquantified points about the costs and benefits of the Directive have emerged. These are additional to points dealt with above and might be summarised as follows:

- Regulations which genuinely facilitate the use of electronic commerce are likely to reduce business costs by encouraging the use of cost-effective delivery mechanisms which are able to reach the maximum number of consumers;
- Regulations which eliminate the need to track and observe multiple sets of national legislation should keep business costs down (including say website development, promotional and advertising text development, legal and compliance costs);
- SMEs and microenterprises are particularly handicapped by inconsistent implementation of the Directive, since they are less likely to be able to afford sound legal advice, and are therefore discouraged from exploiting the opportunities afforded by the internal market and investing in the European development of their businesses.

This partial RIA is available on DTI's website with the documents for consultation. A revised partial RIA will also be published with the draft Regulations in due course. We would hope to be able to improve its accuracy in the light of comments received.

## **9. Summary and recommendation**

Option 1 is not attractive, since it foregoes substantial likely net benefits, and could be in breach of EU legislation.

Option 2 will bring some costs in the form of business systems changes required to ensure compliance with the Directive; these should on the whole be relatively small, and may not apply to those entering the electronic market in the future, though clearly they will need to comply from day one. It will also bring costs with regard to transposition and enforcement. Offsetting these, business costs will be reduced considerably through the ability to rely on knowledge of and compliance with the rules of the home state when doing business with customers in other member states. Improved legal certainty will also benefit consumer and business confidence. The Department's assessment is that the benefits of draft Regulations are likely to outweigh the costs, and justify option 2.

## **10. Enforcement, Sanctions, Monitoring and Review**

See Section 7 above.

DTI

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