



HM TREASURY

**IMPLEMENTATION OF THE
ELECTRONIC MONEY DIRECTIVE**

A Consultation Document

OCTOBER 2001

IMPLEMENTATION OF THE ELECTRONIC MONEY DIRECTIVE

PREFACE

This consultation document seeks views on proposed legislative measures for implementing the Electronic Money Directive into UK law.

Drafts of the proposed Statutory Instruments are attached at *Annex A*.

A draft Regulatory Impact Assessment is attached at *Annex B*.

The Treasury would be grateful for any comments on the draft Statutory Instruments or on the draft Regulatory Impact Assessment to be sent by 8 January 2002 to the following address:

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Please could respondents give details of any organisation whose views they represent.

Unless respondents indicate to the contrary, it will be assumed that they have no objection to their response being made public.

This document can be accessed via the Treasury's website (<http://www.hm-treasury.gov.uk>). Paper copies are available, free of charge, by telephoning 020 7270 1634.

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CHAPTER 1: INTRODUCTION

THE DIRECTIVES

1. On 18 September 2000, the European Parliament and the Council of the European Union adopted two Directives on electronic money. The main one is Directive 2000/46/EC on the taking up, pursuit of and prudential supervision of the business of electronic money institutions (“the E-Money Directive” or “the Directive”)¹. The other Directive (2000/28/EC²) amends the Banking Consolidation Directive (2000/12/EC³) in such a way as to include electronic money institutions in the definition of ‘credit institution’.

WHAT IS ELECTRONIC MONEY?

2. Electronic money (“e-money”) is described by the Directive as monetary value that is stored on an electronic device (such as a chip card or computer memory), that is accepted by undertakings other than the issuer and that is generally intended to make payments of a limited amount. The Directive considers e-money to be an electronic surrogate for coins and banknotes.

OBJECTIVES OF THE DIRECTIVE

3. The E-Money Directive has several objectives:
 - *to protect the consumer and to ensure bearer confidence.* In order to achieve this, a prudential framework is set out to ensure the financial integrity and stability of e-money institutions (ELMIs). Moreover, the consumer benefits from the right to exchange his or her e-money back into notes and coins or a deposit of the same amount.

¹ Directive 2000/46/EC of 18 September 2000 of the European Parliament and of the Council on the taking up, pursuit of and prudential supervision of the business of electronic money institutions, OJ L 275 of 27 October 2000, p. 39.

² Directive 2000/28/EC of 18 September 2000 of the European Parliament and of the Council amending Directive 2000/12/EC relating to the taking up and pursuit of the business of credit institutions, OJ L 275 of 27 October 2000, p. 37.

³ Directive 2000/12/EC of 20 March 2000 of the European Parliament and of the Council relating to the taking up and pursuit of the business of credit institutions, OJ L 126 of 26 May 2000, p. 1.

- *to improve the single market in financial services* by introducing minimum harmonised rules and, more specifically, by providing for a single passport for ELMIs and for the principle of home country regulation. As a result, ELMIs that have been found by the competent authorities of the home Member State to fulfil the harmonised prudential rules receive an authorisation that entitles them to issue e-money throughout the European Union (EU).
- *to avoid any distortion of competition* for the issuance of e-money between traditional credit institutions and ELMIs by subjecting both kinds of institutions to prudential supervision. In order to level the playing field, the lighter prudential regime for ELMIs is balanced by the restrictions on ELMIs' business activities and investments.
- by harmonising the legal framework for e-money in the EU, the Directive aims at establishing the *legal certainty necessary for e-commerce to develop*.

THE TREASURY'S POSITION

4. The Treasury views the potential of e-money, and the possible emergence of non-bank ELMIs, positively: a chance to create modern and effective means of payment that will facilitate e-commerce and other novel ways of doing business; and an opportunity to encourage new entrants – such as large retailers, or computer and telecoms firms – into a sector dominated by the major retail banks.
5. In implementing the E-Money Directive into UK law, we are keen to strike the right balance between competition, consumer protection and financial stability. Our general approach is therefore to implement the Directive with as light a touch as is consistent with our obligations under the Directive. The intention is that the regulation of ELMIs will not unduly burden existing e-money issuers and will encourage new entrants, both from within the banking sector and elsewhere.

IMPLEMENTING THE E-MONEY DIRECTIVE

6. Our intention is to specify the issuing of e-money as a regulated activity under the Financial Services and Markets Act 2000 (FSMA). This will give effect to the principal requirements of the E-Money Directive. Firstly, it will ensure that persons not authorised to do so under FSMA (other than those with a waiver) will be prohibited from carrying on the business of issuing e-money. Secondly, the Financial Services Authority (FSA) will be able to impose the remaining requirements of the Directive, such as the restriction on the business activities of ELMIs to the issuance of e-money and the provision of closely related services. The FSA would be able to do this primarily by making rules under Section 138 of FSMA.
7. The activity of 'issuing e-money' will therefore be added to the list of other regulated activities in an amended Regulated Activities Order. The amendments will also cover: a definition of what constitutes e-money; the criteria that an ELMI will have to meet in order to be waived from the need to become an authorised person; and the transitional arrangements for existing issuers of e-money. Our proposals for implementing these key parts of the Directive are discussed in *Chapter 2*.
8. Making the issuing of e-money a regulated activity under FSMA has the effect of bringing into play a whole range of provisions under the Act. Some of those provisions are considerably wider ranging than the requirements of the E-Money Directive itself. It is therefore necessary to decide whether, as a matter of policy, those provisions should apply to the issuing of e-money, even though this is not strictly necessary in order to implement the Directive. If any of these provisions were not wanted for e-money, they would require to be expressly disapplied.
9. The principal aspects of the FSMA regime for regulated activities (authorised persons) that are not matched by equivalent requirements in the E-Money Directive are the Financial Services Compensation Scheme, the Ombudsman Scheme and the financial promotion regime. These aspects are discussed in *Chapter 3*. Our proposed timetable for implementing the Directive is then outlined in *Chapter 4*.

CHAPTER 2: KEY ISSUES IN IMPLEMENTING THE DIRECTIVE

THE DEFINITION OF E-MONEY

10. The Directive's definition of e-money leaves room for interpretation. There is a wide range of schemes that could be considered as e-money and whether the Directive catches any given scheme will depend on the application of the definition to the details of a particular case. Given the emergent nature of the e-money industry, we do not believe it is possible to elaborate on this definition in such a way as to legislate explicitly for all the different types of scheme that might be developed.
11. We therefore propose effectively to copy out the Directive's definition of e-money in our implementing legislation. The FSA will then be responsible for interpreting this definition of e-money and for producing guidelines on how it will be applied in practice. The main advantage of a copy out approach is the flexibility it allows the FSA in its interpretation as the industry develops. It will be easier for the FSA to apply the definition to individual cases than for the implementing legislation to be amended.
12. E-money will be defined in the implementing legislation using criteria (i) and (iii) of Article 1(3)(b) of the Directive and by reference to Article 2(3). As such, e-money will mean monetary value as represented by a claim on the issuer which is stored on an electronic device and is accepted as means of payment by undertakings other than the issuer – so long as the funds received are immediately exchanged for e-money.
13. However, we propose not to refer in the definition to criterion (ii) – which states that e-money must be “issued on receipt of funds of an amount not less in value than the monetary value issued” – because we believe that this presents a loophole in the Directive's definition of e-money. Criterion (ii) implies that where “e-monetary value” is issued at a discount (i.e. more value is issued than funds received) it is not e-money as defined by the Directive. This means that we would be under no obligation to regulate its issuance.

14. It is our view that this criterion was aimed at stopping ELMIs from issuing e-money at a discount. As such, it was designed to prevent e-money issuers from creating monetary value in an uncontrolled way – which could, in the extreme, lead to the money stock expanding without central banks being able to monitor it and therefore hinder monetary analysis and affect the adequacy of monetary instruments. However, as it stands, criterion (ii) has the opposite effect in that it excludes the issuing of e-value at a discount from the scope of the Directive.
15. We therefore propose to close this apparent loophole by removing criterion (ii) from the definition in our implementing legislation. In this way, e-money issued at a discount will be brought within the scope of regulation. The FSA will then have the power to make a rule prohibiting the issuing of e-money at a discount.

Q1: Is it appropriate effectively to copy out the Directive's definition of e-money? Is this approach likely to cause any problems? Are we right to omit criterion (ii) from our definition and to rely on an FSA rule to prohibit the issuing of e-money at discount?

WAIVERS

16. Article 8 of the Directive provides that, under certain conditions, Member State competent authorities (i.e. the FSA in the UK) may waive the application of some or all of the provisions of the Directive in relation to e-money issuers. We believe that it is important for new entrants to be able to start up and grow initially without the burden of unnecessary regulation. We therefore propose to implement this Article as widely as permitted by the Directive - so as to allow as many e-money issuers as possible to be waived from authorisation (assuming they would like to be). This will exempt them from the detailed requirements imposed on authorised e-money issuers, as well as from having to pay the full authorisation fee.
17. In this way, we hope to foster competition and innovation in the e-money industry and therefore encourage its development. However, once an ELMI grows to such an extent that it can no longer be considered 'small'

or 'limited' and therefore ceases to meet the conditions for its waiver, it will be required to seek authorisation from the FSA and, if successful, to meet the prudential and other requirements of the Directive.

18. We propose to implement this Article by empowering the FSA to grant waivers on a case-by-case basis to all e-money issuers who wish to be waived that appear to it to meet the relevant conditions. These 'relevant conditions' will broadly follow the criteria set out in Article 8(1), though some of the terms used in the Directive will be elaborated upon in order to improve understanding of their meaning.

Waiver criteria

19. The Directive provides that a waiver may be granted when the amount that can be stored on an e-money issuer's electronic storage device is limited to a maximum of €150 and if at least one of following three criteria are met:
 - *if the aggregate amount of issued e-money is limited:* the total financial liabilities related to the e-money activities must not normally exceed €5 million and must never exceed €6 million;
 - *if the e-money is accepted only by related companies:* the e-money is accepted only: by subsidiaries of the ELMI which perform operational or other ancillary functions related to e-money issued or distributed by itself; by the parent undertaking of the ELMI; or by its sister companies (i.e. other subsidiaries of the parent);
 - *if only a limited number of undertakings accept the e-money and they are either located within a limited geographical area or they have a close financial or business relationship with the ELMI.*
20. The first criterion is straightforward, though it will need to be made clear that references to amounts in euros correspond to equivalent amounts in sterling. The second criterion does involve a degree of judgement in the phrase "operational or other ancillary functions", though the FSA will have

already considered the same issues in the context of the restrictions on business activities in Article 1(5) of the Directive. We therefore propose to simply copy out these two criteria in the implementing legislation.

21. The third criterion is somewhat less precise, particularly due to the use of phrases such as “limited local area” and “close financial or business relationship”. We therefore propose to elaborate on some of these terms:

- The original proposal for this criterion included the illustrative examples of “sports centres, shopping centres, campuses, railway stations, airports, etc.” In order to catch these sorts of examples and others, we propose to include such examples in the implementing legislation and to say that an e-money scheme is deemed to operate within a “limited local area” if it is confined to an area of 4 square kilometres. However, a scheme will not be treated as failing to satisfy the criterion merely because it does not fall within this deeming provision. The intention is to provide those firms looking to operate in an area of less than 4 square kilometres the certainty of being eligible for a waiver, and to allow those firms operating in an area slightly bigger than 4 square kilometres to argue their case for a waiver to the FSA in view of their particular circumstances.
- The original proposal for the provision “close financial and business relationship” noted that it should apply “where concerned undertakings (issuing and accepting) have close financial links, without being in a legal sense organised in a group structure” and included the illustrative example of “retail firms under the same franchising scheme”. The Directive also gives the example of “a common marketing or distribution scheme”. A close relationship would certainly not exist merely by virtue of a group of undertakings all accepting the e-money of a particular scheme. In the absence of a helpful way of clarifying this phrase without narrowing its possible application, we propose to copy it out and leave the FSA with the discretion to interpret it on the basis of specific cases presented to it. In doing so, the onus will be on the waiver applicant to demonstrate that it has such a relationship with its accepting undertakings.

- Given the kinds of schemes that may be covered by the geographic and ‘close links’ provisions set out above, we propose that an ELMI’s e-money is deemed to be accepted by a “limited number of undertakings” if it is confined to a specific number of accepting institutions. Deciding on a precise figure is difficult given that, for example, a geographically limited scheme could still contain a relatively large number of potential accepting institutions. We presently have in mind a figure of 100.

Q2: Are these waiver conditions appropriate? In particular, are the figures of 4 square kilometres and 100 accepting undertakings appropriate for the illustrative examples given?

22. In considering whether the above proposals for implementing the waiver criteria of Article 8 are appropriate, it would be helpful to consider examples of existing schemes that proponents think might meet the Directive’s waiver criteria. It must be stressed that the above are illustrative examples and that the details of individual schemes will be key in deciding whether they meet the waiver criteria. However, we are aware of the following possibilities:

- A number of closed e-purse schemes are in operation at UK universities. These use smart cards for such things as student ID, computer access cards, library cards and payment cards in campus bars and shops. These would appear to constitute e-money, but should be eligible for a waiver on the basis that a university campus is clearly distinguishable in terms of its limited geographical coverage and its limited number of accepting undertakings.
- There are several local authority schemes currently being piloted involving smart cards, which allow citizens to pay for services such as buses, a range of leisure facilities, parking and road tolls. In some cases, the local authority may itself be the e-money issuer, whereas in others it may have a close business relationship with the issuer. Such schemes would appear to constitute e-money. They could be eligible

for a waiver on the basis of either the fairly low level of e-money liabilities, or - for bigger schemes – due to the close relationship between the local authority and the accepting undertakings (e.g. local authority-run or franchised leisure facilities, museums, libraries).

- Several transport operators are planning to introduce smart cards, primarily for the purpose of recording that a ticket has been pre-paid for a particular journey, but perhaps also with e-money facilities to ensure tickets on connecting bus or train services can also be purchased, or goods bought in shops located at stations. As transport schemes are likely to exceed the geographical criterion, eligibility for waiver is likely to turn on whether a close business relationship exists between accepting institutions and the issuer.
- It is conceivable that shopping centres or airport terminals may introduce e-money schemes for the purpose of buying goods and services in retail outlets located within them. Here, waiver may depend on the number of outlets involved and the geographical area covered by the shopping centre or airport terminal(s) in question.

23. Given the range of potential interpretations of the waiver criteria set out in the Directive, we would especially welcome comments from respondents on our proposed approach. In particular, views are requested on the following questions:

Q3: Are the examples considered here reasonable? Are there other examples of genuinely 'limited' schemes worth considering? Are there any existing or planned e-money schemes that might wish to take comfort from any of these waiver conditions?

Contents of the waiver

24. As noted earlier, the Directive provides for Member States to allow their competent authorities to waive the application of *some or all* of the provisions of the Directive to eligible firms. In line with our desire for a light touch regime, we propose to disapply as many of the provisions of

the Directive as possible. The consequence will be that a waived firm will not be treated as carrying on a regulated activity under FSMA. The automatic result will be that the firm is not subject to most of the requirements of the Directive. This will free such firms from the Directive's prudential requirements, as well as the need for their e-money to be redeemable. Equally, waived firms will not be able to exercise passport rights in other Member States of the European Economic Area (EEA).

25. There are, however, specific provisions of the Directive that must be applied even to waived firms. In particular, Article 8(3) obliges waived firms to report periodically to the competent authorities on their activities. Furthermore, in order to verify the continued existence of the conditions for the waiver, the FSA will be able to collect information from waived firms using its powers under Section 165 of FSMA.
26. One important requirement that cannot be waived is the Money Laundering Directive. Therefore, all e-money schemes will continue to be subject to this Directive, as implemented in the UK by the Money Laundering Regulations 1993 (SI 1993/1933). This is on the grounds that they involve "issuing and administering means of payment" – as referred to in Annex 1 to the Banking Consolidation Directive. Consequently, there will be no difference between the money laundering regulations applicable to authorised ELMIs and those applicable to waived ELMIs – both will have an obligation to deter, detect and report money laundering activities.

Q4: Is it appropriate to waive the application of as many of the Directive's provisions as possible? Are there provisions that should not be waived?

Procedures for granting a waiver

27. The implementing legislation will set out the procedures for firms to apply to the FSA for a waiver. These will follow closely the procedures for applying for permission under Part IV of FSMA. For example, we propose to import from Section 52 the warning notice and decision notice procedure and the right of aggrieved applicants to refer matters to the Financial Services and Markets Tribunal.

28. The FSA will have the power to revoke a waiver on its own initiative if it considers that the conditions for the waiver are have been breached or if a waived firm fails to comply with the FSA's rules regarding the provision of information. We believe this is preferable to providing that a waiver is automatically revoked if any of the conditions are breached. Given the lack of precision of some of the conditions, that could put firms in the unacceptable position of not knowing from day to day whether they are lawfully carrying on business or not (for example, if they extend their operations marginally they might wonder whether that breaches the "limited local area" condition).
29. A waived firm will also be allowed to apply voluntarily for its waiver to be revoked. This covers the case of a firm that wishes to expand its operations in such a way that the waiver conditions would no longer hold and/or wishes to become authorised so that it can exercise passporting rights. It will be possible to make a request for revocation conditional on the granting of an authorisation.

Q5: Are the proposed procedures for granting and revoking waivers appropriate?

TRANSITIONAL ARRANGEMENTS

30. Article 9 of the Directive provides that e-money issuers operating before the date at which the implementing provisions enter into force (i.e. 27 April 2002) will be presumed to be 'authorised' as ELMIs. We propose to grant all such existing issuers a time-limited exclusion, whereby they will be treated as not carrying on a regulated activity under FSMA for the first six months (i.e. until 27 October 2002).
31. These arrangements will apply equally to those firms that are already authorised under FSMA (because they are carrying on other regulated activities) and those that are not – i.e. in neither case will the issuing of e-money constitute a regulated activity during the transitional period. The

arrangements will apply to firms with their head office in the UK and those with their head office in other EEA Member States.

32. During the six-month transitional period, both UK and EEA e-money issuers will benefit from the exclusion, and there will be no need for EEA e-money issuers to have gone through the inward passporting procedure. If other EEA Member States take a similar approach, any UK e-money issuer that is operating in another EEA Member State will similarly benefit from the six-month exclusion. After the expiry of the six-month period, UK e-money issuers will not be able to carry on the business of issuing e-money in other EEA Member States unless they have complied with the requirements in Part III of Schedule 3 to FSMA. Similarly, after six months, any EEA e-money issuers will not have permission to carry on that activity under FSMA unless they have gone through the inward passporting procedure under the Banking Directive and Part II of Schedule 3 to FSMA.
33. E-money issuers are warned to actively make use of this six-month period to prepare for the full impact of the E-Money Directive with effect from 27 October 2002. They should take whatever steps are necessary to secure FSMA authorisations, waivers or passports before the end of this period, and - by the same date - to comply fully with relevant FSA rules. Failure to do so will result in an abrupt end to their ability to legally issue e-money from 27 October 2002. Meanwhile, for the duration of the six-month exclusion, issuers will be able to continue their e-money activities without interruption, and without needing to comply with any of the requirements of the Directive, or of FSA rules.

Q6: Do these transitional arrangements adequately reflect the requirements of the Directive? Are they appropriate? Will they cause problems for any existing e-money issuers operating in the UK?

CHAPTER 3: CONSEQUENTIAL AMENDMENTS TO FSMA

34. As explained earlier, making the issuing of e-money a regulated activity under FSMA has the effect of bringing into play a whole range of provisions under the Act. As a matter of policy, it is necessary to decide whether or not to apply certain provisions of FSMA to authorised e-money issuers. In doing so, our general approach is to maintain consistency with the treatment of other regulated activities under FSMA, except where there are good policy reasons for doing otherwise. Some of these provisions are discussed below:

THE FINANCIAL SERVICES COMPENSATION SCHEME

35. The Financial Services Compensation Scheme (Part XV of FSMA) is a scheme for compensating people in cases where relevant persons are unable, or are likely to be unable, to satisfy claims against them. The scheme therefore aims to protect the customers of a regulated firm unable to satisfy claims against it by compensating them with money levied from the other firms authorised to carry out that type of business. The scheme is generally limited in application to cover individuals and small businesses.
36. Although FSMA provides for regulated activities to be covered by a compensation scheme, its application is not a requirement of the E-Money Directive. Equally, the Directive does not preclude the application of such a scheme. Indeed, the need for measures to protect the bearers of e-money, including the possible need to introduce a guarantee scheme, is one of the issues upon which the European Commission must present a report to the European Parliament by April 2005 (under Article 11 of the Directive).
37. The compensation scheme would provide an e-money issuer's customers with some degree of protection if that issuer were to be unable to satisfy claims against it. However, the level and nature of the risks involved in issuing e-money are such that at the present time it is debatable whether they justify the creation and maintenance of a compensation scheme.

38. The provisions of the Directive are designed to ensure the integrity of ELMIs and the protection of the funds that they hold. These include: limitations on investments, requirements regarding initial capital and ongoing funds, restrictions on business activities and requirements for the sound and prudent operation of ELMIs. It might reasonably be expected that these prudential supervisory requirements will adequately address the risks involved in issuing e-money.
39. Given the cash-surrogate nature of e-money, consumers are unlikely to hold significant amounts at any one time; indeed, the Directive notes that e-money is largely used for lower value payments. The losses that consumers may suffer in the event of an ELMI's failure are likely to be correspondingly low. Small businesses accepting a particular ELMI's e-money may stand to lose larger amounts in the event of its failure but, again, these losses are likely to be relatively low.
40. Whilst the low level of risk means that the cost of funding a compensation scheme would likely be similarly low, a concern is that potential new entrants may still perceive a substantial risk that, although they are successful themselves, they will have to find potentially significant sums, relative to what may be tight margins, to fund a compensation scheme where others firms have failed. This could prove a barrier to entry into a market still very much in its infancy. The potential benefit to bearers of e-money of a compensation scheme may not therefore justify the potential detriment to competition of raising such a barrier to entry.
41. We believe that the risks to consumers involved in e-money do not warrant the application of the compensation scheme at this time. We therefore propose to expressly disapply the compensation scheme for e-money issuers by making a provision in the amended Regulated Activities Order under Section 22 of FSMA. The matter will, however, be kept under review – to take into account developments in the industry and the findings of the European Commission's report on the subject in 2005.

Q7: Is it appropriate not to introduce a compensation scheme for e-money at the present time? Is there any indication of the potential costs and benefits of applying such a scheme to e-money issuers?

OMBUDSMAN SCHEME

42. The Ombudsman Scheme (Part XVI of FSMA) provides for a scheme under which certain disputes may be resolved quickly and with minimum formality by an independent body - the Financial Ombudsman Service.
43. Although FSMA provides for regulated activities to be covered by the Ombudsman Scheme, its application is not a requirement of the E-Money Directive. Equally, the Directive does not preclude the application of such a scheme.
44. The arguments for and against the application of the Ombudsman Scheme in relation to e-money are finely balanced. On the one hand, the application of the Scheme would provide a reliable and consistent mechanism of redress for consumers and may also benefit e-money issuers by providing a preferable alternative to arbitration or the courts. On the other hand, it could be argued that while the business of issuing e-money is emergent the benefits of such a scheme do not justify the costs to the industry.
45. We propose to allow the FSA to determine in the usual way whether the Ombudsman Scheme will be applied to e-money. Under FSMA, the FSA has the power to specify the activities that are covered by the Ombudsman's jurisdiction and could, if they saw fit, choose not to apply the Scheme in relation to e-money. In accordance with its normal procedures, the FSA will therefore carry out a full assessment of the potential costs and benefits, consulting with interested parties, before making a decision on whether to apply the Scheme in relation to e-money.

Q8: Should the FSA be left to decide upon the application of the Ombudsman Scheme in relation to e-money?

FINANCIAL PROMOTION

46. The financial promotion regime of FSMA (Section 21) prohibits the marketing of investments and investment services by persons that are not authorised by the FSA. Generally speaking, the activities regulated under FSMA are subject to the financial promotion regime. However, the Directive does not require the issuing of e-money to be subject to any such regime. Equally, the Directive does not preclude the application of such a regime.
47. At present, the activity of issuing e-money is not regulated in the UK, so it is not subject to any financial promotion regime, although general laws on misrepresentation do protect consumers to a certain extent. Making the activity of issuing e-money subject to the financial promotion regime would mean that it could only be promoted by authorised persons or where an authorised person had approved the content of the promotion. For example, a retailer that accepted and distributed e-money would not be able to promote it without first getting the promotion approved by an authorised e-money issuer. This could significantly raise the cost of promoting e-money. We consider that the low level of consumer risk posed by e-money does not warrant the burden on the industry of having to comply with the financial promotion regime.
48. We therefore propose not to make the activity of issuing e-money subject to the financial promotion regime of FSMA. However, we propose that the situation should be subject to later review. If, at a later date, it is perceived necessary to include the activity within the financial promotion regime this can of course be done.

Q9: Should the activity of issuing e-money not be made subject to the financial promotion regime of FSMA? Is there any indication of the potential costs and benefits of applying such a regime to e-money?

CHAPTER 4: TIMETABLE FOR IMPLEMENTATION

49. The consultation period on the proposed legislative measures for implementing the E-Money Directive into UK law closes on 8 January 2002. We will then consider any amendments necessary to our proposals in time to allow for the implementing legislation to go into Parliament by early February.
50. We propose that the regime should come into force on 27 April 2002 – the latest date permitted by the Directive – so as to allow existing and potential e-money issuers and the FSA as much time as possible to prepare themselves for the new regime.
51. We understand that the FSA proposes to consult separately later in the year on the actions it will be required to take in order to implement the remaining provisions of the Directive. It will then make the necessary rules under FSMA (as applied and amended by these proposals) in the months leading up to the implementation date.

CHAPTER 5: SUMMARY OF QUESTIONS

THE DEFINITION OF E-MONEY

Q1: Is it appropriate effectively to copy out the Directive's definition of e-money? Is this approach likely to cause any problems? Are we right to omit criterion (ii) from our definition and to rely on an FSA rule to prohibit the issuing of e-money at discount?

WAIVERS

Q2: Are these waiver conditions appropriate? In particular, are the figures of 4 square kilometres and 100 accepting undertakings appropriate for the illustrative examples given?

Q3: Are the examples considered here reasonable? Are there other examples of genuinely 'limited' schemes worth considering? Are there any existing or planned e-money schemes that might wish to take comfort from any of these waiver conditions?

Q4: Is it appropriate to waive the application of as many of the Directive's provisions as possible? Are there provisions that should not be waived?

Q5: Are the proposed procedures for granting and revoking waivers appropriate?

TRANSITIONAL ARRANGEMENTS

Q6: Do these transitional arrangements adequately reflect the requirements of the Directive? Are they appropriate? Will they cause problems for any existing e-money issuers operating in the UK?

FINANCIAL SERVICES COMPENSATION SCHEME

Q7: Is it appropriate not to introduce a compensation scheme for e-money at the present time?

OMBUDSMAN SCHEME

Q8: Should the FSA be left to decide upon the application of the Ombudsman Scheme in relation to e-money? Is there any indication of the potential costs and benefits of applying such a scheme to e-money issuers?

FINANCIAL PROMOTION REGIME

Q9: Should the activity of issuing e-money not be made subject to the financial promotion regime of FSMA? Is there any indication of the potential costs and benefits of applying such a regime to e-money?

ANNEX A: DRAFT ORDER AND REGULATIONS

Order made by the Treasury, laid before Parliament under paragraph 26(2) to (5) of Schedule 2 to the Financial Services and Markets Act 2000, for approval by resolution of each House of Parliament within 28 days beginning with the day on which the Order was made (no account being taken of any time during which Parliament is dissolved or prorogued or during which both Houses are adjourned for more than four days).

STATUTORY INSTRUMENTS

2002 No.

FINANCIAL SERVICES AND MARKETS

The Financial Services and Markets Act 2000 (Regulated Activities) (Amendment) Order 2002

Made 2002

Laid before Parliament 2002

Coming into force in accordance with article 1(2)

Whereas, in the opinion of the Treasury, one of the effects of the following Order is that an activity which is not a regulated activity (within the meaning of the Financial Services and Markets Act 2000⁽⁴⁾) will become a regulated activity (within the meaning of that Act);

The Treasury, in exercise of the powers conferred on them by sections 22(1) and (5) and 428(3) of, and paragraph 25 of Schedule 2 to, that Act, hereby make the following Order:

PART I PRELIMINARY

Citation, commencement and interpretation

1.—(1) This Order may be cited as the Financial Services and Markets Act 2000 (Regulated Activities) (Amendment) Order 2002.

(2) This Order comes into force —

- (a) on [], for the purpose of making rules under article 9G of the principal Order; and
- (b) otherwise, on 27th April 2002.

⁽⁴⁾ 2000 c. 8.

(3) In this Order, “the principal Order” means the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001⁽⁵⁾.

PART II

AMENDMENT OF THE PRINCIPAL ORDER

Definition of “electronic money”

2. In article 3(1) of the principal Order (interpretation), after the definition of “deposit” insert—

““electronic money” means monetary value, as represented by a claim on the issuer, which is—

- (a) stored on an electronic device; and
- (b) accepted as a means of payment by persons other than the issuer;”.

Sums received in exchange for electronic money not to constitute deposits

3.—(1) In paragraph (2) of article 5 of the principal Order (accepting deposits), for “articles 6 to 9” substitute “articles 6 to 9A”.

(2) After article 9 of the principal Order insert—

“Sums received in exchange for electronic money

9A. A sum is not a deposit for the purposes of article 5 if it is immediately exchanged for electronic money.”

Issuing electronic money: the specified activity

4. After article 9A insert—

“CHAPTER IIA ELECTRONIC MONEY

The activity

Issuing electronic money

9B. Issuing electronic money is a specified kind of activity.

Exclusions

Persons certified as small issuers etc.

9C.—(1) There is excluded from article 9B the issuing of electronic money by a person to whom the Authority has given a certificate under this article (provided the certificate has not been revoked).

⁽⁵⁾ S.I. 2001/544, amended by .

- (2) An application for a certificate may be made by—
- (a) a body corporate, or
 - (b) a partnership,
- (other than a credit institution as defined in Article 1(1)(a) of the banking consolidation directive) which has its head office in the United Kingdom.
- (3) The Authority must, on the application of such a person (“A”), give A a certificate if it appears to the Authority that—
- (a) the first, second or third condition is met; and
 - (b) A does not issue electronic money except on terms that the electronic device on which the monetary value is stored is subject to a maximum storage amount of 150 euro.
- (4) The first condition is that A’s total liabilities with respect to the issuing of electronic money do not (or will not) usually exceed 5 million euro and do not (or will not) ever exceed 6 million euro.
- (5) The second condition is that electronic money issued by A is accepted as a means of payment only by—
- (a) subsidiaries of A which perform operational or other ancillary functions related to electronic money issued or distributed by A; or
 - (b) other members of the same group as A (other than subsidiaries of A).
- (6) The third condition is that electronic money issued by A is accepted as a means of payment by not more than [one hundred] persons where—
- (a) those persons accept such electronic money only at locations within the same premises or limited local area; or
 - (b) those persons have a close financial or business relationship with A, such as a common marketing or distribution scheme.
- (7) For the purposes of paragraph (6)(a), locations are to be treated as situated within the same premises or limited local area if they are situated within—
- (a) a shopping centre, airport, railway station, bus station, or campus of a university, polytechnic, college, school or similar educational establishment; or
 - (b) an area which does not exceed four square kilometres;
- but sub-paragraphs (a) and (b) are illustrative only and are not to be treated as limiting the scope of paragraph (6)(a).
- (8) In this article, references to amounts in euro include references to equivalent amounts in sterling.

Applications for certificates

9D. The following provisions of the Act apply to applications to the Authority for certificates under article 9C (and the determination of such applications) as they apply to applications for Part IV permissions (and the determination of such applications)—

- (a) section 51(1)(b) and (3) to (6);
- (b) section 52, except subsections (6), (8) and (9)(a) and (b); and
- (c) section 55(1).

Revocation of certificate on Authority's own initiative

9E.—(1) The Authority may revoke a certificate given under article 9C if—

- (a) it appears to it that the conditions for giving the certificate are not met, or have not been met at any time since the certificate was given; or
- (b) the person to whom the certificate was given has contravened any rule or requirement to which he is subject as a result of article 9G.

(2) Sections 54 and 55(2) of the Act apply to the revocation of a certificate under paragraph (1) as they apply to the cancellation of a Part IV permission on the Authority's own initiative.

Revocation of certificate on request

9F.—(1) A person ("B") to whom a certificate has been given under article 9C may apply to the Authority for the certificate to be revoked, and the Authority must then revoke the certificate and give B written notice that it has done so.

(2) An application under paragraph (1) must be made in such manner as the Authority may direct.

(3) If—

- (a) B has made an application under Part IV of the Act for permission to carry on a regulated activity of the kind specified by article 9B (or for variation of an existing permission so as to add a regulated activity of that kind), and
- (b) on making an application for revocation of his certificate under paragraph (1), he requests that the revocation be conditional on the granting of his application under Part IV of the Act,

the revocation of B's certificate is to be conditional on the granting of that application.

(4) For the purposes of paragraph (3), in determining whether B's application under Part IV of the Act is granted no account is to be taken of any limitations incorporated, or any requirements included, in B's permission.

Obtaining information from certified persons etc.

9G.—(1) The Authority may make rules requiring certified persons to provide periodic information to the Authority about their activities so far as relating to the issuing of electronic money, including the amount of their liabilities with respect to the issuing of electronic money.

(2) The Authority may, by notice in writing given to a certified person, require him—

- (a) to provide specified information or information of a specified description; or
- (b) to produce specified documents or documents of a specified description.

(3) Paragraph (2) applies only to information or documents reasonably required for the purposes of determining whether the conditions for giving a certificate are, or have been, met.

(4) Subsections (2), (5) and (6) of section 165 of the Act (Authority's power to require information) apply to a requirement imposed under paragraph (2) as they apply to a requirement imposed under that section.

(5) Subsection (4) of section 168 of the Act (appointment of persons to carry out investigations in particular cases) has effect as if it provided for subsection (5) of that section to apply if it appears to the Authority that there are circumstances suggesting

that the conditions for giving a certificate under article 9C are not met, or have not been met at any time since the certificate was given, with respect to a certified person.

(6) Sections 175 (information and documents: supplemental provisions), 176 (entry of premises under warrant) and 177 (offences) of the Act apply to a requirement imposed under paragraph (2) as they apply to a requirement imposed under section 165 of the Act.

(7) In this article—

- (a) “certified person” means a person to whom a certificate has been given under article 9C (other than one which has been revoked); and
- (b) “specified”, in paragraph (2), means specified in the notice mentioned in that paragraph.

Transitional exclusion for existing issuers

9H.—(1) An existing issuer is not to be treated as carrying on an activity of the kind specified by article 9B at any time until the beginning of 27th October 2002.

(2) In paragraph (1), an “existing issuer” means a body corporate or partnership which, immediately before 27th April 2002—

- (a) has its head office in the United Kingdom, and is carrying on by way of business in the United Kingdom the activity of issuing electronic money; or
- (b) has its head office in an EEA State other than the United Kingdom, and is carrying on such an activity by way of business in the United Kingdom without contravening the law of that other EEA State.

Supplemental

False claims to be a certified person

9I.—(1) A person who is not a certified person is to be treated as guilty of an offence under section 24 of the Act (false claims to be authorised or exempt) if he—

- (a) describes himself (in whatever terms) as a certified person;
- (b) behaves, or otherwise holds himself out, in a manner which indicates (or which is reasonably likely to be understood as indicating) that he is a certified person.

(2) In paragraph (1), “certified person” has the meaning given by article 9G(7)(a).

Exclusion of electronic money from the compensation scheme

9J. The compensation scheme established under Part XV of the Act is not to provide for the compensation of persons in respect of claims made in connection with any activity of the kind specified by article 9B.

Record of certified persons

9K. The record maintained by the Authority under section 347 of the Act (public record of authorised persons etc.) must include every certified person (as defined in article 9G(7)(a)).”

Agreeing to issue electronic money not to be a regulated activity

5. In article 64 of the principal Order (agreeing to carry on specified kinds of activity), after “article 5,” insert “9B,”.

Electronic money: the specified investment

6. After article 74 of the principal Order insert—

“Electronic money

74A. Electronic money.”

PART III

SUPPLEMENTAL AND TRANSITIONAL PROVISIONS

Amendment of the Financial Services and Markets Act 2000 (Professions) (Non-Exempt Activities) Order 2001

7.—(1) In the Financial Services and Markets Act 2000 (Professions) (Non-Exempt Activities) Order 2001⁽⁶⁾, after sub-paragraph (a) of article 4(1) (activities to which exemption from the general prohibition does not apply), insert—

“(aa) article 9B (issuing electronic money);”.

(2) In article 8 of that Order, after “article 4(a),” insert “(aa),”.

Variation of threshold condition

8. In paragraph 1(2) of Schedule 6 to the Financial Services and Markets Act 2000 (threshold conditions: legal status of deposit-takers), after “accepting deposits” insert “or issuing electronic money”.

Anticipatory consultation on rules

9. If—

- (a) before [the date mentioned in article 1(2)(a)] any steps were taken in relation to a draft of rules which the Authority proposes to make under article 9G(1) of the principal Order (as inserted by article 4 of this Order), and
- (b) those steps, had they been taken after that day, would to any extent have satisfied the requirements of section 155 of the Financial Services and Markets Act 2000,

those requirements are to that extent to be taken to have been satisfied.

Date

Two of the Lords Commissioners of
Her Majesty’s Treasury

⁽⁶⁾ S.I. 2001/1227, amended by .

EXPLANATORY NOTE

(This note is not part of the Order)

This Order amends the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001 (“the principal Order”). It gives effect to Directive 2000/46/EC of the European Parliament and of the Council of 18 September 2000 on the taking up, pursuit of and prudential supervision of the business of electronic money institutions (OJ L275, 27.10.2000, p.39); and Directive 2000/28/EC of the European Parliament and of the Council of 18 September 2000 amending Directive 2000/12/EC relating to the taking up and pursuit of the business of credit institutions (OJ L275, 27.10.2000, p.37).

The Order provides for the issuing of electronic money to be a regulated activity under the Financial Services and Markets Act 2000 (“the Act”).

Article 2 inserts a definition of “electronic money” into the principal Order. Article 3 amends that Order to provide that a sum is not a “deposit” for the purposes of that Order if it is immediately exchanged for electronic money.

Articles 4 to 6 insert provisions into the principal Order relating to the regulated activity of issuing electronic money. They include provisions excluding from the scope of that activity certain persons whose operations are on a limited scale, and to whom the Financial Services Authority (“the Authority”) has issued a certificate. The Authority is given powers to obtain information from such “certified persons”. There is also a transitional exclusion, until 27th October 2002, for firms who were already issuing electronic money by way of business immediately before 27th April 2002. Provision is made excluding the issuing of electronic money from the Financial Services Compensation Scheme established under Part XV of the Act, and providing for details of “certified persons” to be included in the public record maintained by the Authority under section 347 of the Act.

Articles 7 and 8 of the Order make supplemental amendments to provide that the issuing of electronic money is not an exempt activity for the purposes of Part XX of the Act (provision of financial services by members of the professions); and to provide that persons seeking permission under the Act to carry on the regulated activity of issuing electronic money must comply with the threshold condition in paragraph 1(2) of Schedule 6 to the Act (i.e. they must be either bodies corporate or partnerships). Article 9 makes provision about anticipatory consultation on rules to be made under the new power conferred by article 9G(1) of the principal Order.

2002 No.

[FINANCIAL SERVICES AND MARKETS]

**The Electronic Money (Miscellaneous Amendments)
Regulations 2002**

<i>Made</i> - - - -	2002
<i>Laid before Parliament</i>	2002
<i>Coming into force</i> -	2002

Whereas the Treasury are a government department designated⁽⁷⁾ for the purposes of section 2(2) of the European Communities Act 1972⁽⁸⁾ in relation to measures relating to credit and financial institutions and to the taking of deposits or other repayable funds from the public;

Now therefore the Treasury, in exercise of the powers conferred on them by—

- (i) section 2(2) of the European Communities Act 1972, and
- (ii) paragraph 13(1)(b)(iii) of Schedule 3 to, and sections 417(1)⁽⁹⁾ and 428(3) of, the Financial Services and Markets Act 2000⁽¹⁰⁾,

hereby make the following Regulations:

Citation and commencement

1. These Regulations may be cited as the Electronic Money (Miscellaneous Amendments) Regulations 2002, and come into force on [27th April 2002].

Amendments to primary legislation

⁽⁷⁾ S.I. 1990/1304.

⁽⁸⁾ 1972 c. 68. By virtue of the amendment of s. 1(2) made by s. 1 of the European Economic Area Act 1993 (c. 51) regulations may be made under s. 2(2) to implement obligations of the United Kingdom created by or arising under the Agreement on the European Economic Area signed at Oporto on 2nd May 1992 (Cm 2073) and the Protocol adjusting the Agreement signed at Brussels on 17th March 1993 (Cm 2183).

⁽⁹⁾ See the definition of “prescribed”.

⁽¹⁰⁾ 2000 c. 8.

The Companies Act 1985

2. In section 699A(3) of the Companies Act 1985⁽¹¹⁾ credit and financial institutions to which the Bank Branches Directive (89/117/EEC) applies), in the definition of “credit institution”, [omit the words from “a credit institution” to “that is to say”] **or** [for “article 1” substitute “article 1(1)(a)”].

The Financial Services and Markets Act 2000

3. In paragraph 20(4) of Schedule 11 to the Financial Services and Markets Act 2000⁽¹²⁾ (offers of securities: Euro-securities), for “Article 1” substitute “Article 1(1)(a)”.

Amendments to secondary legislation

The Cross-Border Credit Transfer Regulations 1999

4. In regulation 2(1) of the Cross-Border Credit Transfers Regulations 1999⁽¹³⁾ (interpretation), in the definition of “credit institution”, [omit the words from “a credit institution” to “that is to say,”] **or** [for “Article 1” substitute “Article 1(1)(a)”].

The Financial Markets and Insolvency (Settlement Finality) Regulations 1999

5. In regulation 2(1) of the Financial Markets and Insolvency (Settlement Finality) Regulations 1999⁽¹⁴⁾ (interpretation), for “Article 1” substitute “Article 1(1)(a)”.

The Financial Services and Markets Act 2000 (EEA Passport Rights) Regulations 2001

6.—(1) The Financial Services and Markets Act 2000 (EEA Passport Rights) Regulations 2001⁽¹⁵⁾ are amended as follows.

(2) In regulation 1(2) (interpretation), after the definition of “credit institution” insert—

““electronic money institution” means an electronic money institution as defined in Article 1 of directive 2000/46/EC of the European Parliament and of the Council of 18 September 2000 on the taking up, pursuit of and prudential supervision of the business of electronic money institutions⁽¹⁶⁾,”.

(3) In paragraph (3)(d) of regulation 2 (establishment of branch: contents of consent notice), at the beginning insert “except where the firm is an electronic money institution,”.

(4) In paragraph (4)(a)(ii) of that regulation, after “credit institution” the first time it occurs insert “(other than an electronic money institution)”.

Two of the Lords Commissioners of
Her Majesty’s Treasury

Date

⁽¹¹⁾ 1985 c. 6. Section 699A was inserted by S.I. 1992/3179, and the definition of “credit institution” was inserted by S.I. 2000/2952.

⁽¹²⁾ 2000 c. 8. Paragraph 20(4) was amended by S.I. 2000/2952.

⁽¹³⁾ S.I. 1999/1876. The definition of “credit institution” was amended by S.I. 2000/2952.

⁽¹⁴⁾ S.I. 1999/2979. The definition of “credit institution” was inserted by S.I. 2000/2952.

⁽¹⁵⁾ S.I. 2001/2511.

⁽¹⁶⁾ O.J. L275, 27.10.2000, p.39.

ANNEX B: DRAFT REGULATORY IMPACT ASSESSMENT

1. This regulatory impact assessment accompanies the proposed Statutory Instruments that implement the E-Money Directive into UK law and deal with the consequential amendments to FSMA necessitated by the specification of e-money issuance as a regulated activity.
2. To date, the activity of issuing e-money has not been subject to a formal system of regulation and supervision. We do not propose to carry out an overall assessment of the regulatory impact of implementing the E-Money Directive into UK law as the Government is obliged to do so under European Community law. However, we are only obliged to implement the new regime in the minimum way consistent with the Directive. We therefore believe it is worthwhile to conduct an assessment of the measures that we propose to introduce over and above the minimum requirements of the Directive.
3. There are two areas in which our proposed regime for e-money institutions goes further than the requirements of the Directive. These are:
 - (i) specifying e-money issuance as a regulated activity under FSMA; and
 - (ii) including “e-monetary value” issued at a discount within the definition of e-money.

Costs

4. In relation to (i), e-money issuers will not only be subject to the specific rules made by the FSA to implement the requirements of the Directive, but it will be subject to certain general requirements of persons authorised under FSMA.
5. In relation to (ii), there will be costs involved for those firms issuing “e-monetary value” at a discount. Under a strict interpretation of the Directive, these firms would fall outside the scope of the regime and would effectively be unregulated. By bringing “e-monetary value” issued at a

discount within the definition of e-money, such firms would fall to be regulated by the FSA. However, we intend for the FSA to make a rule prohibiting the issuing of e-money at a discount.

Benefits

6. In relation to (i), there are benefits in implementing the Directive by regulated the issuing of e-money under FSMA. We will achieve a basic consistency of treatment between the activity of issuing e-money and with other regulated activities under FSMA, which will have the advantage of being a process that the financial services sector is already familiar with. It is, however, hard to quantify these benefits meaningfully.
7. In relation to (ii), we believe it was the intention of the Directive to prohibit the issuing of e-money at a discount. In reality, we are therefore only implementing the Directive in the spirit we believe it was intended. The benefits of such a prohibition are that it prevents e-money issuers from creating monetary value in an uncontrolled way. As a result, the Bank of England will be able to monitor any expansion of the monetary stock and therefore maintain the effectiveness of its monetary analysis and the adequacy of monetary instruments. Again, however, it is hard to quantify these benefits meaningfully.

Business sectors affected

8. The regulations will apply to UK-based e-money issuers. However, the regulations will not impact directly or specifically on small businesses and so no small business litmus test has been carried out.

Compliance and enforcement

9. The FSA will be responsible for enforcing the regulation of the activity of issuing e-money. People against whom the FSA decides to take action have the right to refer the matter to the Financial Services and Markets Tribunal if they so wish.

Consultation

10. Our proposals for implementing the Directive are being put out for consultation to parties with an interest in the regulation of e-money issuers.

Comments

11. We would welcome further information on the costs and benefits associated with our proposals for implementing the E-Money Directive into UK law.

Q10: Are the kinds of costs and benefits envisaged here appropriate?