
Minutes

Minutes of the first meeting of the 2EMD STAKEHOLDER LIAISON GROUP

Held on 22 April 2010 at 14:00

In Committee Room E, FSA

Attendees

FSA:	Chair: Jean Cooper (JC) Dominic Peachey (DP) John Burns (JB) Jody Whitehorn Andrew Sheen Liz Meneghello Rosalie Langley-Judd Karen Wells	HMT: Brian Garcia (BG) HMRC: Andy Watson
		Industry: Stefan Marx (BBA) Andrew Hopkins (BSA) Helmut Bauer (EMA) Veronica Studsgaard (IAMTN) Hamish MacLeod (MBG) Meredith Pearson (MBG) Kiron Farooki (PO) Robert Courtneidge (PIF) Andrew Johnson (UKGCVA) Siobhan Moore (UKGCVA)
Apologies	Ed Harley (FSA) Leon Isaacs (IAMTN) Thaer Sabri (EMA) Jacqui Tribe (UKC)	

Minute No		Action
1.	The group were welcomed to the first meeting of the Second Electronic Money Directive (2EMD) Stakeholder Liaison Group and after introductions, the draft Terms of Reference were agreed.	
2.	Key changes in the 2EMD DP made a presentation of the key prospective changes to the e-money regime arising from 2EMD implementation. The salient points are as follows. <ul style="list-style-type: none">• The new Directive is maximum harmonising.• It applies many provisions of the Payment Services Directive (PSD), <i>mutatis mutandis</i>.• Electronic Money Institutions (ELMIs) will no longer be defined as credit institutions but will be reclassified as financial institutions. The effect of this is to switch off those provisions of the Banking Consolidation Directive that currently apply to ELMIs.	

**Minute
No**

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- The current waiver for small ELMIs will no longer apply and consideration is being given as to what extent small ELMIs (ie those having average outstanding electronic money – calculated in arrears over the preceding six months – that does not exceed a limit of no more than € million) should be exempted from prudential rules by making use of the national options in the Directive. Further consideration is also being given to the parameters of the exemption for limited scope schemes (ie those operating within a limited network of accepting merchants or for purchasing a limited range of goods and services).
- Initial (and minimum) capital for authorised ELMIs will reduce from €1 million to €350,000. The old investment rules will be replaced by safeguarding along the lines of PSD although Member States' discretion to define what constitute "secure, low-risk assets" is greatly reduced. ELMIs will now also be able to carry on mixed business.
- The redemption obligation will now apply to small ELMIs as well as to authorised ELMIs.
- It was confirmed that the provisions of PSD would not be affected by the implementation of 2EMD.

3. **Overview of HMT's approach to implementation of 2EMD**

HMT then gave a short presentation of their approach to implementing 2EMD. Brian Garcia stressed that HM Treasury want to hear from as many people as possible in order to flush out every conceivable issue so as to get the draft regulations into good shape and minimise the changes likely to arise from the formal consultation process.

The FSA said that the experience of PSD implementation had been that it was best to try and bottom out difficulties well ahead of implementation time. Both firms and the FSA need adequate notice to make the relevant systems changes.

HMT confirmed that the next meeting of the Transposition Group was scheduled for 24 June, to cover all outstanding issues. Brian Garcia commented that the UK appeared to be in good shape compared with the other Member States (MS).

The draft regulations would be published in August. There would be a two month consultation and the response would be published in November. Regulations would be laid before Parliament in early December. It was still to be clarified whether they would be subject to a positive (requiring a vote) or a negative resolution (they would be passed provided nobody prayed against them within 28 days), but JB commented that the Payment Services Regulations had been subject to a negative resolution.

Treasury's starting position on the EMRs was that they were aiming for 'intelligent copy out' of the Directive's provisions.

On the subject of limited networks, HMT confirmed that the UK would adopt a "case-by-case" approach. There would be no rigid thresholds. HMT's current expectation is that prepayment for a merchant's own goods, and electronic replacements for paper vouchers (eg book tokens, luncheon vouchers) and pure transport ticketing would be likely to be excluded.

HMT confirmed that paying interest on electronic money balances was banned as were all other benefits linked to the length of time a person had held electronic money. Alternative benefit and reward arrangements based on other factors, such as velocity of spend, would need to be considered on a case-by-case basis.

Under Article 6.1 (b) of 2EMD firms were allowed to grant credit where certain conditions were met. HMT were keen to encourage innovation – eg micro-finance loans providing the opportunity to make purchases linked to electronic money. PIF raised the example of 'Credit Builder' products where the monthly fees were rolled up as loans which were repayable at the year's end. If e-money holders met these repayments, it created evidence of credit-worthiness which could

be picked up by Credit Reference Agencies.

HMT confirmed that ELMIs could not issue electronic money through agents but could redeem through agents and could provide other payment services through agents. The Issuer/Distributor model which was common in the UK was not familiar in many of the Member States. Issuers were not required to register pure Distributors, but were required to notify the CA of their structural organisation (including a description of outsourcing arrangements) and remained liable for the acts of any entity to which activities were outsourced.

On Safeguarding, the FSA confirmed that they knew of no insurance option currently available for safeguarding purposes. So they expected the market to stick to safeguarding through depositing funds in a separate account in a credit institution or investing in secure low-risk assets within the meaning of Article 7. HMT proposed that the insurance option would nevertheless be left open in the Regulations and the FSA would give guidance in respect of it.

On the subject of mobile electronic money, the application of the Directive was not entirely clear. The Commission had withdrawn the 2005 guidance and was not proposing to say any more on the subject at the present time. He was flagging the point and asking for examples of mobile commerce that the UK (as market leader) could show to the Commission. MBG agreed to come forward with examples of new business models and how these were differentiated between Prepaid and Contract customers.

HMT believe that in the area of mobile payments it is important that there is an objective test against which business models could be assessed.

On issuance and redeemability, the key issues for HMT were timing and fees. 2EMD places no time limit on redemption. Redemption should, in general, be granted free of charge. However, 2EMD permits the imposition of a redemption fee as long as it is clearly and prominently stated in the contract and only in one of the following situations (i) where redemption is requested before termination of the contract; (ii) where the contract provides for a termination date the electronic money holder terminates the contract before that date; or (iii) where redemption is requested more than one year after the date of termination of the contract. Any fee for redemption must be 'proportionate and commensurate' with the actual costs incurred by the electronic money issuer. It might not be easy to assess what would constitute a 'proportionate and commensurate' fee.

Gift cards were a particular issue in terms of redemption as there is traditionally a high incidence of "breakage" with this product (ie many cards are only ever partially redeemed or not redeemed at all). The question was raised that, if there was no limit on the time at which a consumer could ask for redemption, did firms also have to safeguard

unclaimed customer funds in perpetuity. It was suggested that it is not clear whether e-money should fall into a regime similar to that for dormant bank accounts.

The FSA acknowledged this concern and indicated that it will need to be given further consideration in the context of the full harmonisation provisions of the Directive – it may be an issue for the Q&A section of the Commission’s website.

On the reference to consumers in Article 11 (7), HMT suggested that the definition of “consumer” in this context and the effect of Article 11 (7) would need to be given further consideration. JB pointed out that the PSD does contain a definition of “consumer” and that it would appear to be consistent to adopt that same definition in dealing with e-money. HMT thought that the PSD definition might be too wide for the EMD.

HMT mentioned that the Financial Services Act 2010 provided for the establishment of a Consumer Finance Education Body (CFEB) which would be financed by a levy on the industry. Following the precedent set for PSD firms, this levy was likely to be payable not only by authorised ELMIs but also by small ELMIs. This proposal would be consulted on.

4. **Overview of FSA’s approach to implementation of 2EMD**

DP gave another presentation on the FSA’s proposed approach to 2EMD implementation. It was stressed that the views being expressed are provisional and subject to development. In general, 2EMD is a maximum harmonising directive that applies various provisions of PSD mutatis mutandis. In future, ELMIs would cease to be FSMA firms. It was expected that issuing e-money would remain a FSMA regulated activity for banks and building societies. The bulk of the rules would reside in regulations made under the European Communities Act rather than the FSA Handbook, although some parts of the Handbook would continue to apply to ELMIs (DISP, PERG and FEES). It was proposed that guidance would be contained in an FSA Approach Document. Responsibility for taking reasonable steps to ensure regulatory compliance by pure distributors of e-money (ie those distributors who did not undertake other regulated payment services) would rest with issuers. It was stressed by the FSA that the effect of 2EMD was that issuers would be liable for the acts of their distributors.

Electronic money could be issued by credit institutions; credit unions; municipal banks; ELMIs; Post Office Giro Institutions; central banks (when not acting in their capacity as monetary authorities); and national and local governments when acting as public authorities.

Existing ELMIs meeting current requirements will be eligible for grandfathering and will be told of the procedures to be followed in due course. Small ELMIs currently benefiting from a waiver will need

either to get authorised (allowing them to passport) or to take advantage of any optional exemptions available under the 2EMD regime (an area of policy that is still under consideration). Passporting will be available to authorised firms but not to small firms benefiting from an exemption. A 2EMD passporting group had been established along the lines of the PSD one and was chaired by the UK with France providing the secretariat.

The prudential regime for ELMIs in relation to the activity of issuing e-money would, in broad terms, involve:

- **Capital** – an initial and minimum figure of €350,000 and firms must always maintain the higher of this figure or 2% of average outstanding electronic money.
- **Safeguarding** – safeguarding funds received in exchange for electronic money by investing them in secure low-risk assets, depositing them in an account with a credit institution or ensuring they are covered by an insurance policy or guarantee. This regime is different from that under PSD since MS discretion to determine what constitutes ‘secure, low risk assets’ had been constrained (certain asset items referred to in CAD are deemed to constitute secure low risk assets – MS can determine otherwise only “in exceptional circumstances and with adequate justification.” The Directive contains a national option to allow competent authorities to specify which safeguarding method is to be used by firms. At present this option is not likely to be taken up in the UK implementation.
- **Systems and controls** – (as per Article 5 of PSD).
- **Optional exemptions** – small issuers (ie those whose activities generate average outstanding electronic money, calculated six monthly in arrears, up to a specified limit of no more than €5 million) may be given waivers from some of the provisions of 2EMD relating to authorisation and prudential requirements.

E-money issuers will need to continue to comply with the relevant conduct of business requirements of the PSRs. The consumer right of redemption is no longer time limited and the de minimis (€10) redemption threshold is abolished. Interest and any other benefits related to the length of time for which e-money is held are prohibited.

The PSD mandates risk-based supervision and currently prudential supervision comprises monitoring semi-annual returns; dealing with crystallised risks; and considering appropriate thematic work. COB compliance is dealt with on a complaints led basis unless there is evidence of a systemic problem or there is a history of non-compliance. Our approach to enforcement is expected to mirror the FSMA and PSD enforcement approach.

The Approach Document is expected to be published in December 2010 and is likely to follow the precedent and structure of the PSD Approach Document. It will be a living document and the Stakeholder Liaison Group would initially be used as the Consultative Forum for this document.

On timing, consultation (by HM Treasury on the Regulations and by FSA on relevant Handbook changes) would be undertaken in September 2010. The FSA aimed to roll out application packs in December 2010 (though the latest possible date was 20 January) and there would be three months for processing completed applications. The FSA had asked HMT for fast track grandfathering powers. Transitional arrangement for existing ELMIs would last until 30 October 2011. Article 18(3) also allows small e-money issuers registered under EMD to continue operating until 30 April 2012 before they would need to seek further authorisation under 2EMD.

5. **Market intelligence**

The FSA said it was seeking more information about electronic money business models and would therefore be sending out a questionnaire to firms through their Trade Associations in order to help us understand how the business models work and the risks arising. Deepening our knowledge of how the industry functioned in practice would strengthen our negotiating position in Europe.

The EMA made the point that it would be a good idea to talk before the FSA drafted the questions and offered to help formulate the questions.

BBA and BSA were asked if they would circulate it to their members.

The Prepaid International Forum said they had a lot of information on outstanding balances but would need to check with their members what information can be released to the FSA.

6. **AOB**

It was agreed that the next meeting of this group would be in July.

JC then thanked the attendees for their input into the meeting and the consensus was that the meeting had gone well.