

Where the FSA has got to with Implementing the “E-money Directive”

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Milestones to Implementation

- EU Directive passed and published in OJ on 27th Oct 2000.
- UK has 18 Months to implement (ends 27th April 2002).
- This is done by adding e-money to the Regulated Activities Order.
- Debated in Parliament Yesterday (10th April 2002).
- The FSA then has to incorporate the detailed provisions of the directive into its own Handbook.

The Significance of 4/27



- 18 months since publication of the e-money directives in OJ of the EU
- Actually it's a Saturday, so think of 4/29 instead
- Commencement of e-money regulation in the UK
- FSA acquires supervisory powers over Authorised e-money issuers
- Issuers must decide whether to apply for authorisation or certification
- 6 month grand-fathering period begins for existing issuers

Overview of Financial Regulation in the UK



- Financial Services and Markets Act 2000
- Vesting Day (N2) was 1 December 2001
- One stop shop at Canary Wharf
- We are responsible for regulating deposit taking, insurance and investment business
- Our goal: "To maintain efficient, orderly and clean financial markets and help retail consumers achieve a fair deal"

The Four Regulatory Objectives of the FSA



- Maintaining market confidence in the financial system
- Promoting public understanding of the financial system
- Securing the appropriate degree of protection for consumers
- Reducing the extent to which it is possible to use a regulated business for a purpose connected with financial crime

A New Regulator for the New Millennium



- Future supervision to be risk based
- “Risk” means risk to any of the 4 Regulatory Objectives
- Firm-specific risk assessment and prioritisation looks at:
 1. Impact of the problem if it occurs
 2. Probability of the problem occurring
- All Firms graded “A” (High) to “D” (Low) for impact/probability

FSA's View of E-Money



- Not much of it about
- Those schemes we know about likely to be small
- They would therefore rank as “D” firms and draw minimal supervision
- There may be a generational element to acceptance
- If the platform is already there it could become popular (HK/Singapore)

FSA's Progress So Far



- Extensive pre-consultation
- CP117 published in December 2001
- Responses received from the public in February 2002
- Now working on our feedback statement
- This and definitive rules will be published on the FSA website later this month under Publications – Handbook – ELM. (www.fsa.gov.uk)

Principles for Businesses – Part 1



- A firm must conduct its business with integrity
- A firm must conduct its business with due skill, care and diligence
- Management and control must be responsible and effective
- A firm must maintain adequate financial resources
- A firm must observe proper standards of market conduct
- A firm must pay due regard to consumers' interests and treat them fairly

Principles for Businesses – Part 2



- Communications with customers must be clear, fair and not misleading
- Conflicts of interest must be managed fairly (B2C & C2C)
- Care must be taken over advice to customers and discretionary decisions
- Adequate protection of client assets
- A firm must deal fairly and openly with its Regulators

Threshold Conditions



- Legal status – issuers must be bodies corporate or partnerships
- Location – UK firms must have Head and Registered Offices in the UK
- Close links – these must not threaten effective supervision
- Adequate resources – finance, personnel and systems
- Suitability – firms must be “fit and proper”

What our Regime Covers



- Application, contents, purpose and general
- Initial and continuing own funds requirements
- Management of the e-money float
- Limitation on activities - Systems and controls
- Redemption, information requirements and purse limits
- Consolidated Financial Supervision
- Small e-money issuers

Application, Contents, Purpose and General



Shows what rules apply to ELMIs and what apply to credit institutions

- States purpose of the various chapters of our rules
- Sets out restrictions on issuing e-money
- Sets out what other parts of FSA handbook apply to ELMIs

Capital



- Purpose to underpin financial robustness and public confidence
- Ensure continuing ability to meet redemption requests
- Basically 1 Million Euros or 2% of outstanding e-money
- Firms may hold additional capital on self certified basis
- FSA will be able to apply differential capital requirements in relation to specific systems and controls concerns or exceptional business risks.

Management of the E-Money Float



- Our rules impose prudent limits on ELMIs investments
- Helps ensure e-money is always backed by sufficiently liquid low risk assets
- Involves addressing credit risk, market risk (FX or IRR), large exposure risk and liquidity risk

Limitation on Activities



- Activities strictly limited to e-money and closely related services
- May issue and administer other means of payment and store data for third parties
- Cannot give credit or invest in other businesses
- Cannot pay interest on e-money
- Cannot issue e-money at a discount

Systems and Controls



- Segregation of duties (four eyes principle)
- Guidance on systems covers authentication, authorisation controls, data protection, anti-fraud measures, audit trails and customer protection
- Guidance that systems should address:
 1. Unauthorised creation transfer or redemption
 2. Incorrect attribution of funds within the system
 3. Loss of e-money within the system and loss of function of any part of it
 4. Use of the system for the purpose of crime

Redemption, Information Requirements & Purse Limits



- Must redeem at par to lawful holders within five days
- Issue of e-money with less than a year's validity is banned
- There must be full written disclosure of risks, fees and redemption rights
- Uniform purse limits of £1000 unless
 1. Consumers acknowledge that they could lose everything in an insolvency
 2. The issuer can "freeze" lost, damaged or stolen purses
 3. The issuer can ensure continuing redemption by the lawful owners of the "frozen" purses

Consolidated Financial Supervision



- If an ELMI is part of a group that is subject to supervision as a bank, building society or an investment firm, the consolidated supervision shall also be carried out under the rules applicable to that category of firm
- Consolidated supervision is designed to:
 1. Protect a firm from losses in another group entity with resultant financial or reputational pressure
 2. Ensure capital is not subject to double counting or leveraging
 3. Prevent business from being booked in an unauthorised group entity to escape supervision

Small E-Money Issuers



- Small issuers may apply for a waiver from regulation
- This captures three potential categories of issuer, namely:
 1. Small schemes never having e-money liabilities in excess of 6 Million Euros and a purse limit of 150 Euros; or
 2. They are intra-group schemes and limited in size to 10 million Euros; or
 3. They operate in a limited local area (shopping centre, transport terminal or educational establishment) of less than 4 square kilometres and have fewer than 100 acceptor members
- The only rule applying to small issuers requires semi-annual reports

Compensation and Complaints Handling



ELMIs to be exempt from Financial Services Compensation Scheme at least for the first three years

ELMIs to be subject to the jurisdiction of the Financial Ombudsman Service from the outset

ELMIs to be excluded from the remit of Financial Promotions Order but where quality of communications is consistently bad, we could take enforcement action under our Principles for Business

2005 Review by the European Commission



- European Commission must report on the application of the Directive to the European Parliament and Council of Ministers no later than 27th April 2005
- This report must cover, among other things:
 1. Bearer protection measures and a possible guarantee scheme
 2. Capital requirements
 3. Waivers
 4. The possible need to prevent the payment of interest on electronic money