

EUROPEAN CENTRAL BANK

OPINION OF THE EUROPEAN CENTRAL BANK

of 18 January 1999

at the request of the Council of the European Union under Article 105(4) of the Treaty establishing the European Community and Article 4(a) of the Statute of the European System of Central Banks and of the European Central Bank on 1. a Commission proposal for a European Parliament and Council Directive on the taking up, the pursuit and the prudential supervision of the business of electronic money institutions, and 2. a Commission proposal for a European Parliament and Council Directive amending Directive 77/780/EEC on the coordination of laws, regulations and administrative provisions relating to the taking up and pursuit of the business of credit institutions

(1999/C 189/07)

1. On 24 November 1998 the European Central Bank (ECB) received a request from the Council of the European Union for an ECB opinion on 1. a Commission proposal for a European Parliament and Council Directive on the taking up, the pursuit and the prudential supervision of the business of electronic money institutions (hereinafter referred to as 'Draft Directive 1') and 2. a Commission proposal for a European Parliament and Council Directive amending Directive 77/780/EEC on the coordination of laws, regulations and administrative provisions relating to the taking up and pursuit of the business of credit institutions (hereinafter referred to as 'Draft Directive 2').
2. The ECB's competence to deliver an opinion is based on Article 105(4), first indent, of the Treaty establishing the European Community (hereinafter referred to as 'the Treaty'). In accordance with Article 17(5), first sentence, of the Rules of Procedure of the ECB, this ECB opinion has been adopted by the Governing Council of the ECB.
3. The ECB notes that Draft Directive 1 and Draft Directive 2 are aimed at fostering the single market in financial services by introducing a minimum set of harmonised prudential rules for electronic money issuance and by applying the arrangements for the mutual recognition of home supervision provided for in Directive 89/646/EEC to electronic money institutions (ELMIs). This includes the safeguarding of the financial integrity and the operations of ELMIs by, on the one hand, ensuring the stability and soundness of ELMIs and, on the other, ensuring that the failure of any one individual ELMI does not result in loss of confidence in this new means of payment.
4. The ECB also notes that the current regulatory initiative is motivated by the absence of a clear legal framework for electronic money issuance in the European Union and by the concern that the non-bank issuance of electronic money could otherwise be carried out on an unregulated basis. Early regulation is considered by the European Commission to be the most practical way to harmonise national approaches to electronic money. It would, in addition, enhance legal certainty and contribute generally to the development of electronic commerce.
5. The ECB further notes the concern to create a level playing-field for the issuance of electronic money by both traditional credit institutions (CIs) and ELMIs, thus ensuring that all issuers of electronic money are subject to an appropriate form of prudential supervision. In this perspective the ECB welcomes Draft Directive 2 to the extent that it amends the definition of credit institution in Article 1, first indent, of the First Banking Coordination Directive and obliges institutions that do not intend to enter into the full range of banking operations to issue electronic money in accordance with the fundamental rules governing all credit institutions. Such an amendment would promote the harmonious development of the issuance of electronic money throughout the Community and avoid any distortion of competition between electronic money issuers, even as regards the application of monetary policy measures.
6. In August 1998 the ECB issued a report on the issuance of electronic money (hereinafter referred to as 'the Report'). This Report specified, *inter alia*, that a material development of electronic money in the Community could have significant implications for the conduct of monetary policy by the ECB. The Report also elaborated on the role which central banks would have to assume with regard to electronic money schemes as part of their oversight responsibility for payment systems in the Community.
7. Given its interest in ensuring the effectiveness of monetary policy, the smooth operation and integrity of payment

systems, the avoidance of systemic risk and the protection of the stability of the financial markets, the ECB stated in its Report that it would be essential for the following minimum requirements to be met with regard to the issuance of electronic money: 1. issuers of electronic money must be subject to prudential supervision; 2. the rights and obligations on the part of the respective participants in an electronic money scheme must be clearly defined and disclosed; such rights and obligations must be enforceable under all relevant jurisdictions; 3. electronic money schemes must maintain adequate technical, organisational and procedural safeguards to prevent, contain and detect threats to the security of the scheme, particularly the threat of counterfeits; 4. protection against criminal abuse, such as money laundering, must be taken into account when designing and implementing electronic money schemes; 5. electronic money schemes must supply the central bank in each relevant country with any information, including statistical information, that is required for monetary policy purposes; 6. issuers of electronic money must be legally obliged to redeem electronic money against central bank money at par at the request of the holder of the electronic money; the details of this requirement are to be specified; and 7. it must be possible for central banks (for the ECB in Stage Three of EMU) to impose reserve requirements on all issuers of electronic money.

8. In addition to the abovementioned minimum requirements, the ECB identified in its Report two further objectives which it deemed desirable to pursue: (i) the interoperability of electronic money schemes; and (ii) the adoption of adequate guarantee; insurance or loss-sharing schemes aimed at protecting customers against losses and at preserving confidence in electronic money.

Draft Directive 1

9. The ECB would welcome a reference in the recitals to the oversight competence of the European System of Central Banks (ESCB) with regard to electronic money schemes. (This competence is based on Article 105(2), fourth indent, of the Treaty and on Article 3(1), fourth indent, of the Statute of the European System of Central Banks and of the European Central Bank (hereinafter referred to as 'the Statute').) In such reference the ECB would also propose that the need for cooperation between the relevant overseers and supervisory authorities in evaluating the integrity of electronic money schemes should be identified.
10. As regards Article 1, the ECB notes in the first instance that the application of Draft Directive 1 is limited to those issuers of electronic money that are ELMIs. The ECB wonders whether it would be conceivable for Draft Directive 1 also to contain some provisions related to the issuance of electronic money that would be equally applicable to both CIs and ELMIs. For example, and as indicated above, the ECB stated in its Report the need for issuers of electronic money, i.e. both CIs and ELMIs, to be legally obliged to redeem electronic money against central bank money at par at the request of the holder of the electronic money. In view of the need to create a level playing-field for the issuance of electronic money and on account of the monetary and payment systems policy considerations (see also paragraph 19 below), this type of requirement should apply to both CIs and ELMIs. Furthermore, the ECB would welcome the introduction of a prohibition preventing persons or undertakings other than credit institutions (i.e. CIs and ELMIs) from engaging in the business of issuing electronic money.
11. With regard to the definition of an electronic money institution in Article 1(3)(a), the ECB would like to introduce the specification that 'electronic money institution' shall mean an undertaking, other than a credit institution as defined in Article 1, first indent, of Council Directive 77/780/EEC, which engages principally in the issuance of instruments of payment of electronic money and/or in the investment of the proceeds from such activities without being subject to Council Directive 93/22/EEC.
12. In respect of the definition of electronic money in Article 1(3)(b), the ECB is of the view that the proposed definition of electronic money may focus too closely on the technical features of electronic money and be difficult to translate into legal terms. From this perspective, the ECB would like to suggest the introduction of the concept that electronic money represents a claim on the issuer of electronic money, which claim is redeemable in either legal tender or scriptural money, that is incorporated in an electronic medium, and accepted as an instrument of payment by (non-affiliated) undertakings other than the issuing institution. Moreover, in relation to Article 1(3)(b)(iv), the ECB is unclear about the added value of referring to 'electronic transfers of limited value' since such a reference may give the impression that electronic transfers of large value may somehow not be covered by Draft Directive 1.
13. With regard to Article 1(4)(a), the ECB is of the view that the wording 'and the issuing and administering of other means of payment within the meaning of point 5 of the Annex to Directive 89/646/EEC' (this includes, for example, credit cards, travellers' cheques and bankers' drafts) is too broad. For example, allowing ELMIs to issue and administer instruments of payment which involve the granting of credit to individual or corporate customers (e.g. credit cards) would expose ELMIs to risks that do not seem to be addressed. In addition, if the ELMIs enter into areas of business other than the issuance and administration of electronic money, ELMIs cease to be the specialised institutions that they were intended to be, which may call into question the advisability of having a special regulatory framework for ELMIs which could, in effect, only marginally be engaged in the issuance of electronic money. It is also problematic from the perspective

- of achieving a level playing-field between CIs and ELMIs, particularly since the list of instruments of payment is not exhaustive and could, as a consequence, be read as including instruments of payment which ELMIs could not issue without becoming a credit institution under the current definition (e.g. debit cards which imply the maintenance of deposit accounts. For the reasons set out above, the ECB is of the opinion that the wording 'and the issuing and administering of other means of payment' should either be deleted with the introduction of a prohibition in this respect or be restricted to prepaid instruments of payment.
14. In respect of Article 1(4)(b), the ECB notes that the possible range of non-financial businesses may be too broad because they may prove to play a very important role and to bear varying levels of inherent risk. In this respect it should be reiterated that the own funds requirements and limitations of investments applicable to ELMIs are based only on the financial liabilities of ELMIs related to outstanding electronic money. The ECB would welcome a more specific wording on the non-financial activities in which the ELMIs are allowed to engage and would propose that the reasoning for this be given in the explanatory memorandum. In any case, if the ELMIs are allowed to undertake non-financial activities, the risks inherent in such activities as well as the risks inherent in the investment of the proceeds of such activities should be addressed.
 15. In relation to Article 2(1), the ECB would prefer to reverse the wording to the effect that references to credit institutions in all relevant Community legislation would be generally applicable, except of course in those cases, to be listed in this Article 2, in which such application would not be appropriate or relevant.
 16. In relation to Article 2(2), the ECB would like to express its concern, with reference to Article 5 of Directive 77/780/EEC, about the appropriateness for ELMIs, even though they will be categorised as credit institutions, to use the word 'bank' in their denomination. Such use of the word 'bank' by ELMIs could confuse the public at large, if account is taken of the fact that ELMIs will not, as part of their activity of issuing electronic money as stated in Article 2(4), take deposits. Any possible confusion in this respect should be avoided.
 17. The ECB welcomes the application to ELMIs of Council Directive 91/308/EEC on the prevention of the use of the financial system for the purpose of money laundering as well as that of Council Directive 92/230/EEC on the supervision of credit institutions on a consolidated basis.
 18. With regard to the first part of Article 2(4) the ECB would welcome the introduction of measures (such as a guarantee, loss-sharing or insurance scheme) to protect holders of electronic money against losses and to preserve their confidence in this instrument of payment. This would be even more desirable if the use of electronic money in the Community were to develop substantially over time.
 19. With regard to the second part of Article 2(4), the ECB would like to reiterate its view, based on considerations of monetary and payment systems policy, that ELMIs, as well as any other institutions engaged in the business of issuing electronic money, should be under an obligation to offer the possibility of redemption, at par value, of their electronic money liabilities *vis-à-vis* holders of electronic money. From the monetary policy point of view, the redeemability requirement is necessary in order, *inter alia*, to preserve the unit-of-account function of money, to maintain price stability by avoiding the unconstrained issuance of electronic money, and to safeguard both the controllability of liquidity conditions and the short-term interest rates set by the ESCB. These considerations would be addressed by introducing continuing redeemability, i.e. holders of electronic money would have the possibility of redeeming their electronic money at all times. In addition, the holders of electronic money should have the unconditional right to leave the relevant electronic money scheme at their discretion. Redemption payments by electronic money issuers to holders of electronic money as described above should be made either in legal tender or, with the respective electronic money holder's consent, via banking channels by making an irrevocable payment order to credit the electronic money holder's bank account. In the latter case, the electronic money holder must have the possibility of freely choosing the bank account to which the redemption payment is credited. Such redemption payments should be denominated in the same currency as the currency in which the relevant electronic money liability is denominated. Such redemption payments would have to be made at the latest on the local business day following the day on which the request for redemption is received by the relevant issuer of electronic money. Redemption of electronic money should be allowed — at least for a certain period of time (to be determined) — after the expiry date of such electronic money or of such device on which the electronic money value is stored, if it is still technically possible to ascertain the value of such electronic money. Disposable and reloadable cards should be treated equally in respect of this redeemability requirement. In principle, redemption should be free of charge. Fees or commissions payable on redemption of electronic money could only be accepted if they did not exceed a reasonable and fair estimate of the costs for the relevant electronic money issuer related to the redemption. If such fees or commissions were deemed to be acceptable, they should be clearly communicated to customers in advance. The redeemability requirement should be applied indiscriminately to all electronic money schemes irrespective of their size. In other words, the redeemability requirement should not be waived for any issuer of electronic money, however small. Lastly, the ECB understands the second sentence of the second part of Article 2(4) as meaning that Member States should not address in their

national legislation the matter of whether or not electronic money is to be redeemable. The foregoing is, in any event, without prejudice to the competences of the ECB.

20. With regard to Article 3, the ECB assumes that a well-founded analysis was carried out to conclude that the proposed level of initial capital as well as the ongoing capital requirements are proportionate to the risks inherent in the range of electronic money activities that can be carried out by ELMIs.
21. As regards Article 4(1), the ECB notes that ELMIs would be able to grant credit, through the instruments of payment that they are authorised to issue and administer, to their individual and corporate customers to the extent that they hold low-risk investments, in accordance with this Article, of an amount which is not less than their financial liabilities related to outstanding electronic money. The risks inherent in the granting of credit do not seem to be addressed by Draft Directive 1 in spite of the fact that such risks may have a material impact on the financial stability of ELMIs. As a consequence, and with a reference to paragraph 13 above, the ECB would like to propose the introduction of a general prohibition for ELMIs to grant credit to their individual or corporate customers. Moreover, with regard to Article 4(4), the ECB would be in favour of requiring a minimum level of harmonisation pertaining to the imposition of limitations on the market risks which ELMs may incur on the basis of their investments, rather than leaving it up to each Member State to choose the appropriate limitations. A minimum level of harmonisation could be considered a prerequisite for granting ELMIs an EU passport.
22. As regards Article 5, the ECB wonders whether its wording does not hamper the relevant authorities' right to conduct on-site inspections. The ECB would therefore like to suggest deleting the wording 'on the basis of data supplied by the electronic money institutions'.
23. As regards Article 6(2), the ECB would see merit in making a general reference in the recitals of Draft Directive 1 to the issue of the outsourcing of certain activities of ELMIs. On the other hand, the ECB has some doubts about whether the proposed unilateral, immediate and unconditional repudiation by ELMIs of the contractual arrangements underlying the cooperation between them and other undertakings would be practically feasible if the effective exercise of the ELMIs' right to

monitor and contain the risks associated with the outsourced activities were to be impaired.

24. As regards Article 7, the ECB would favour an approach whereby all ELMIs irrespective of their size would be fully subject to a minimum level of regulation at the Community level. In particular, and as outlined above, the redeemability requirement should be applied indiscriminately to all electronic money schemes irrespective of their size and, similarly, the possibility should be preserved in all cases for the ECB to impose minimum reserve requirements on ELMIs and to collect statistical information from them.

Draft Directive 2

25. As already pointed out in the Report, the ECB sees great merit in suggesting an amendment to the First Banking Coordination Directive to include all issuers of electronic money in the definition of 'credit institution', along with institutions which receive deposits or other repayable funds from the public and grant credit for their own account. It was noted at the time that this would indeed provide a level playing-field, particularly as it would ensure that all issuers of electronic money would be subject to an appropriate form of prudential supervision and would fall into the category of institutions which, in accordance with Article 19(1) of the Statute, are potentially subject to ECB reserve requirements and statistical reporting requirements in stage three of EMU. This possibility for the ECB to impose reserve requirements and statistical reporting requirements on all issuers of electronic money in stage three of EMU is crucial, in particular with a view to ensuring preparation for a substantial growth in electronic money with a material impact on monetary policy. These requirements are also necessary in view of the need for equal treatment compared with issuers of other types of instruments of payment which are already subject to reserve requirements and statistical reporting requirements.
26. This ECB opinion shall be published in the *Official Journal of the European Communities*.

Done at Frankfurt am Main on 18 January 1999.

The President of the ECB

W. F. DUISENBERG