

172

Financial Services Authority

Electronic money: Perimeter guidance

February 2003



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Annexes

Annex 1 Consolidated list of questions in text

Annex 2 Handbook text (proposed FSA guidance on definition of e-money)

The FSA invites comments on this Consultation Paper. Comments should reach us by 30 May 2003. Comments may be sent by electronic submission using the form on the FSA's website, which can be found at: www.fsa.gov.uk/pubs/cp/cp172_response.html).

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It is the FSA's policy to make all responses to formal consultation available for public inspection unless the respondent requests otherwise.

1 Executive summary

- 1.1 In April 2002 we introduced a regime of rules and guidance for electronic money issuers. This regime was designed to fulfil the UK's obligation to implement the EU Directives on electronic money. Electronic money is defined in UK law as "monetary value.....which is:
 - stored on an electronic device;
 - issued on receipt of funds; and
 - accepted as a means of payment by persons other than the issuer."
- 1.2 Most of our rules and guidance on e-money are contained in a specialist sourcebook (ELM) which you can find on our website www.fsa.gov.uk under 'FSA Handbook of Rules and Guidance'. However, we have also issued a block of 'perimeter guidance.' This guidance is intended to help people understand whether any of their proposed activities involve issuing e-money or not and to help somebody using a particular prepaid electronic payments mechanism to understand its status under the Financial Services and Markets Act 2000 (FSMA). You can find this perimeter guidance in Appendix 3 to our Authorisation Manual (AUTH), in the same section of our website as ELM.
- 1.3 In deciding whether a particular scheme involves e-money or not, we shall take into account the substance of the scheme. In particular it will be necessary to consider whether the scheme involves:
 - the issue of prepaid electronic monetary value that the holder can spend with third parties; or
 - the provision by the issuer of some other sort of service.

- 1.4 Therefore, in deciding whether or not a scheme involves issuing e-money, we shall not be influenced by artificial features of the scheme that seek to disguise the payment function as the supply of some other sort of service.
- 1.5 These principles underpin our approach to defining the e-money perimeter set out in this CP and in the draft guidance in Annex 2. They will also underpin our future approach to determining whether particular schemes do or do not constitute the issue of e-money.
- 1.6 Recent discussions with potential e-money issuers and other interested parties have raised some further questions which we propose to address by adding to our perimeter guidance. The principal questions relate to the use of prepaid airtime on mobile phones to buy Premium Rate Services (PRS). We have already issued individual guidance to certain telephone companies on these matters. The main purpose of this CP is to consult on superseding the individual guidance we have already presented to these telephone companies with general guidance to be included in our Handbook of Rules and Guidance. The individual guidance issued to these telephone companies was stated to be provisional because of the possibility that, as a result of this consultation, we might be persuaded that our conclusions on PRS should be changed. The other issues discussed in this CP relate to electronic travellers' cheques and e-money backed by funds held in trust accounts.
- 1.7 Prepaid airtime that may only be used to buy services provided by the telephone company which issues the airtime is not e-money. This is because it is not accepted as a means of payment by persons other than the issuer. We also believe that prepaid airtime used to call PRS numbers does not constitute e-money where:
 - the supply of telecoms services by the phone operator and the supply of services by the PRS provider can be seen as a single service; and
 - the supply of the airtime and the supply of the PRS take place in the same action.
- 1.8 So where the goods or services or data are delivered to a mobile phone and consumed while the phone is being used, paying for them out of prepaid airtime does not give rise to a use of e-money.
- 1.9 Electronic travellers' cheques are smartcards that carry a prepaid balance. They can be used abroad to withdraw foreign currency from ATMs or for making payments at point of sale. Our view is that electronic travellers' cheques that can only be used to withdraw cash from ATMs owned by their issuer do not constitute e-money. However, electronic travellers' cheques that can be used to withdraw cash from third parties' ATMs, or to buy goods and services in shops, restaurants and hotels, are likely to constitute e-money.

- 1.10 Some business models for e-money provide for the float moneys received against the issue of e-money to be invested in a trust account. In our view such trust arrangements are compatible with our regulatory regime and do not affect the regulatory status of the issued electronic monetary value.
- 1.11 We believe that the guidance issued with this CP is compatible with the European e-money directives. However, we have not received from the European Commission any formal statement of legislative proposals relating to e-money on mobile phones.
- 1.12 The consultation period ends on 30 May 2003, after which we will publish a Policy Statement in response, together with the definitive version of the new Handbook text.

Consumers

This document will be of interest to consumers. It addresses a range of perimeter issues which clarify the dividing line between what does, and what does not, fall within the regulated activity of issuing e-money. So it ties in with our market confidence, public awareness and consumer protection objectives. For example, consumers need to be confident that, where they use prepaid airtime as e-money, they are protected not only by the appropriate prudential rules but also by the specific consumer protection measures that apply to e-money. We also believe that it is appropriate to raise public awareness of what products are within, and which are outside, our e-money regime.

2 Introduction

Background

- 2.1 We introduced our e-money regime on 27 April 2002. This was based on two EU Directives on e-money, which were implemented into UK Law by the Financial Services and Markets Act 2000 (Regulated Activities) (Amendment) Order 2002.
- 2.2 We set out our general approach to the regulation of e-money issuers, together with draft rules and guidance, in CP 117: “*The Regulation of Electronic Money Issuers.*” This was published in December 2001.
- 2.3 Following consultation, we set out our final rules and guidance in a Policy Statement: “*The Regulation of Electronic Money Issuers – Feedback on CP117*”. This was published in April 2002. At the same time, we published these rules and this guidance in a specialist e-money sourcebook (ELM). General guidance on the definition of e-money was set out in Appendix 3 of the Authorisation Manual (AUTH). ELM and AUTH form part of our Handbook which can be found by going to our website at www.fsa.gov.uk, clicking on “FSA Handbook of Rules and Guidance”, scrolling down the table at the bottom of the page and clicking on the appropriate Handbook module.

Purpose of the paper

- 2.4 Recent discussions with potential e-money issuers and other interested parties have raised issues which are not currently addressed in our rules and guidance. We did not explicitly address these issues at that time because the EU Directives did not specifically deal with these issues and there was very little opportunity for us to take account of all eventualities, given the very short timetable available for implementing the Directives. We have now fully considered some of these issues (namely perimeter issues relating to prepaid airtime and Premium Rate Services; electronic travellers’ cheques; and trust arrangements) and have reached a view.

- 2.5 We have already communicated our view on prepaid airtime and PRS to certain telephone companies. We have done this by issuing these companies with individual guidance. We now want to consult on superseding that individual guidance with general guidance, which will be added to the existing guidance on the definition of e-money in AUTH.
- 2.6 The guidance contained in this paper is based on the definition of e-money set out in the European e-money directives as implemented into UK law by The Financial Services and Markets Act 2000 (Regulated Activities) (Amendment) Order 2002 – SI 2002 No.682. It is intended to help businesses determine whether any of their activities might constitute Regulated Activities under FSMA, as a result of the UK's implementation of the e-money Directives.
- 2.7 We believe that the guidance issued with this CP is compatible with the European e-money directives. However, we have not received from the European Commission any formal statement of legislative proposals relating to e-money on mobile phones.
- 2.8 Meanwhile, there are some other issues that we have not yet fully considered. These include possible ways in which undertakings that offer core services on a prepaid basis using a store of electronic monetary value in the hands of the customer (for example mobile phone operators, transport companies) may distribute electronic money to their customers without themselves becoming e-money issuers. We are still working towards a final view on these issues and will publish the results of our thinking in a further consultation to take place at a later date.
- 2.9 This CP contains the draft text of additional perimeter guidance on the scope of the regulatory activity of issuing e-money. This guidance will be incorporated with the existing perimeter guidance in Appendix 3 of the Authorisation module of the FSA Handbook of Rules and Guidance. We are seeking the views of interested parties on this. The consultation period will last for three months and will end on 30 May 2003.
- 2.10 The policy approach will be formulated in line with our four regulatory objectives, with the principles of good regulation and with the objectives of efficient regulation as set out in our publication "*A New Regulator for a New Millennium*".
- 2.11 The issues covered in this paper link with our market confidence, public awareness, and consumer protection objectives. For example, consumers need to be confident that, where they use prepaid airtime as e-money, they are protected not only by the appropriate prudential rules but also by the specific consumer protection measures that apply to e-money. We also believe that consumers may be more willing to use e-money if they are made aware of how it is expected to operate in relation to technological advances, for example in the mobile telecommunications infrastructure.

2.12 Our powers to make guidance are conferred on us by section 157 of FSMA.

Next Steps

2.13 After 30 May 2003, we will publish a response paper setting out the responses to this consultation and any changes we will be making to our draft perimeter guidance as a result. At the same time we will publish our definitive guidance.

2.14 We are committed to developing a regulatory system which meets the needs of e-money issuers and their users. So we recognise the need to keep our existing policy under review and to develop new policy in light of the evolving e-money industry and in light of the actual operational experience of the current regime. Responses to this paper will help us maintain an effective and workable system of regulation for e-money issuers.

2.15 Where people approach us to ask whether a particular product is or is not electronic money, we intend to take a pragmatic and common sense view of the proposition that is put to us. If, taking a common sense view, a scheme looks like a pre-paid electronic payments system where electronic value is accepted by persons other than the one who issued it, then we will look to regulate the scheme. If it does not, then we will not seek to bring the scheme within the framework of regulation.

Structure of the paper

2.16 This paper deals sequentially with the following issues:

- e-money, prepaid airtime and Premium Rate Services (PRS);
- e-money and electronic travellers' cheques; and
- trust arrangements.

2.17 We are also extending the guidance we have issued on the definition of e-money in Annex Three of the Authorisation Module (AUTH). This is being done in order to clarify our approach in deciding whether a particular scheme is or is not e-money. In coming to decisions of this nature we shall take account of the substance of the scheme, irrespective of any artificial features that may disguise the underlying payments function.

2.18 Annex One contains a list of questions on which we should like to hear your views. Annex Two contains the draft text, which we are proposing to add to our Handbook of Rules and Guidance. This draft Handbook text is further guidance on the definition of e-money and it is intended to sit alongside the existing perimeter guidance in Annex Three of the Authorisation Module (AUTH).

3 Our proposals

Introduction

- 3.1 This chapter covers the areas on which we are issuing our perimeter guidance in respect of the regulated activity of issuing e-money. We look at three separate areas, namely:
- prepaid airtime and premium rate services
 - electronic travellers' cheques
 - trust arrangements
- 3.2 In deciding whether a particular scheme involves e-money or not, we shall take into account the substance of the scheme. In particular it will be necessary to consider whether the scheme involves:
- the issue of prepaid electronic monetary value that the holder can spend with third parties; or
 - the provision by the issuer of some other sort of service.
- 3.3 Relevant factors which we shall take into account when deciding these questions include the following:
- the risks incurred by the holder of the prepaid value;
 - the nature of the rights and obligations of the holder of the prepaid value, the issuer of such value and third parties involved in the scheme; and
 - what the scheme allows the holder of the value to do.
- 3.4 Therefore, in deciding whether or not a scheme involves issuing e-money, we shall not be influenced by artificial features of a scheme that seek to disguise the payment function as the supply of some other sort of service.
- 3.5 These principles underpin our approach to defining the e-money perimeter set out in this CP and in the draft guidance in Annex 2. They will also underpin our

future approach to determining whether particular schemes do or do not constitute the issue of e-money.

- Q1. Do you agree with our proposed approach, outlined above, to determining whether a scheme is or is not e-money?
- Q2. Is this guidance clear and comprehensive?
- Q3. Are there any additional areas you would like us to address under this heading?

A E-money, Prepaid Airtime and Premium Rate Services (PRS)

- 3.6 We recognise that there will be considerable development in electronic communications networks (for example 3G telephony and platform convergence) over the next few years. Future Consultation Papers will consider how these developments might fit within our e-money regime. This Consultation Paper concentrates on PRS as currently marketed by the telephone companies.
- 3.7 The majority of mobile phones operate on a prepaid basis, where consumers pay in advance for the future use of airtime. Using the phone uses up the prepaid airtime balance. The prepaid airtime balance can be used for a variety of services including, amongst others, normal phonecalls, SMS messaging, and calls to PRS numbers (usually beginning with 090). Some calls from landline phones are also prepaid by virtue of the use of phone cards.
- 3.8 Where phones operate on a post pay basis, the cost of making the calls is charged to the subscriber's account. This is settled in arrears at the end of each billing period. Since there is no element of prepayment, this mode of operation is unlikely to involve the issue of e-money.
- 3.9 PRS are services where the overall cost of the call covers both the call connection charge (airtime) and the content of the call, that is to say the goods or services bought from third parties and delivered in the course of, or as a consequence of, the call. The network operator passes on a part of the total cost of the call to the content provider, either directly or indirectly. These goods and services can be:
 - live 'voicecall' services (such as weather forecasts); or
 - online services (such as website access); or
 - 'pay-for-product' services (such as ring tones or phone fascias).
- 3.10 PRS are defined and regulated by The Independent Committee for the Supervision of Standards of Telephone Information Services (ICSTIS). PRS calls are limited under ICSTIS guidelines to services costing less than £20.
- 3.11 PRS services work as follows. The subscriber rings the PRS number and orders the relevant goods or services from the PRS seller. However, the PRS seller does not charge subscribers directly. Instead the cost to subscribers of buying the PRS

is reflected in the cost to them of making calls to PRS numbers. This cost is then charged against subscribers' prepaid airtime or debited to their postpay accounts, as the case may be. The airtime provider and the PRS seller then split the revenue earned from the call between them.

- 3.12 As with any other product, prepaid airtime must satisfy all the conditions in the definition of e-money if it is to be regarded as e-money. That is to say:
- the prepaid airtime must form monetary value, represented by a claim on the issuer;
 - the prepaid airtime must be stored on an electronic device (generally the computer system of the network operator); and
 - the prepaid airtime must be issued on receipt of funds, as it is prepaid.
- 3.13 In deciding whether accessing an individual PRS number involves the spending of e-money, the key factor to be considered is who is accepting the prepaid balance as a means of payment. Where the prepaid balance is accepted only by the issuer or where payment is made on the basis of a postpay account, accessing a PRS number does not involve the use of e-money.
- 3.14 However, where the prepaid balance effectively pays third parties for the provision of goods and services, there must be a presumption that the issuance and use of e-money arises. In our view, it is not necessary for there to be a direct conventional payment obligation between the phone subscriber and the PRS seller. So where a subscriber acquires goods and services from a third party by way of a PRS call, it is necessary to trace the flow of payments for the product acquired. If the telephone company deducts the cost of the goods acquired from the subscriber's prepaid account and rewards the PRS seller with an increase in the credit balance it maintains with the network operator, then it can be said that value has flowed from the subscriber to the PRS seller, even though this has occurred indirectly. All the necessary arrangements will have to be set up in advance of the supply of the PRS. The system is analogous with the way credit cards work. PRS sellers only deliver the service to the subscriber because they know the network operator will pay them. Subscribers know that the network operator's charge to them will reflect the cost of the PRS.
- 3.15 The third limb of the e-money definition requires the prepaid value to act as a means of payment. Prepaid call time can be used to buy PRS in that it acts as the trigger that starts a series of arrangements that result in the seller of the PRS being paid.
- 3.16 The lack of a direct connection linking the arrangements between the seller of the PRS and the network operator on the one hand, with those between the subscriber and the call time provider on the other, is not enough to mean that there is no payment. This is a feature of other types of payment as well. For

instance, there may be no direct connection linking two bank accounts between which a payment is made.

- 3.17 The fact that the amount the subscriber pays for a service may be different to what the PRS provider receives for providing that service is not sufficient evidence to show that there is no payment flow between them, where the features described above apply.
- 3.18 Our conclusions are not affected by the fact that the seller of the PRS may not know whether the value it receives is prepaid or postpaid. Although the seller of the PRS may not know whether the subscriber is on a prepay contract, it only supplies the services on the basis that there will be a flow of value from the network operator. The definition of e-money is satisfied by the fact that the third party seller accepts, as a means of payment, electronic monetary value issued by an e-money issuer on behalf of the network operator.
- 3.19 We have written to several mobile phone companies providing them with individual guidance on this issue. Our view is that prepaid airtime used to call PRS numbers does not constitute e-money where:
- the supply of telecoms services by the mobile airtime provider and the supply of services by the PRS provider can be seen as a single service; and
 - the supply of the airtime and the supply of the PRS take place in the same action.
- 3.20 This means that the goods or services must be delivered or consumed either by way of the mobile phone used to make the call or another mobile phone. This includes the use of a mobile phone as the modem that links a PC to the Internet. In this context 'mobile phone' is also taken to mean Personal Digital Assistants (PDA) which also operate as mobile phones.
- 3.21 We have reached this view because we consider that:
- the use of prepaid airtime to call PRS numbers to order goods or services; and
 - the delivery and consumption of those goods or services, either by way of the mobile phone used to make the call or another mobile phone

can be described as a single service. This service is the use of the prepaid airtime together with the supply of the goods or services from the PRS. So prepaid airtime is not being used as a means of payment of persons other than the issuer, but instead is being used to pay for a service provided only by the prepaid airtime issuer.

- 3.22 Where prepaid airtime is used to acquire goods or services which are delivered or consumed by means other than the mobile phone (for example physical delivery of goods) we consider that the use of prepaid airtime does constitute a use of e-money. This is because the use of the prepaid airtime and the supply of the goods

or services from the PRS are separate services which are both paid for by the prepaid airtime. So the prepaid airtime is accepted by third parties as payment for goods and services and the mobile airtime provider is providing an e-money payment facility.

- 3.23 There are a number of circumstances where acquiring PRS may involve spending e-money. First, where PRS are recorded on a computer disk and sent through the post, the delivery is clearly one of physical goods outside the medium of the telephone company's network. So this is likely to convert any prepaid airtime used to acquire the goods into e-money. Secondly, where PRS are delivered to the subscriber's PC over an Internet connection (which is provided under a contract separate from that for the supply of the mobile telephone services) and that connection is over another network such as a landline, delivery is likewise outside the telephone company's own network. Charging for such delivery out of prepaid airtime is therefore likely to convert such airtime into e-money. However, where the phone is web-enabled or is a 3G model, delivery to the subscriber's PC is able to take place over the phone line used to order and pay for the goods so e-money is unlikely to be created.

Q4. Do you agree with our proposed guidance on e-money, prepaid airtime and Premium Rate Services?

Q5. Is this guidance clear and comprehensive?

Q6. Are there any additional areas you would like us to address under this heading?

B E-money and electronic travellers' cheques

- 3.24 Electronic travellers' cheques are plastic smartcards which carry a prepaid balance. They are used to withdraw currency at foreign ATMs or to pay for goods and services in foreign shops, restaurants and hotels.
- 3.25 We have considered whether the use of electronic travellers' cheques involves payment to third parties for goods and services. Our view is that the use of electronic travellers' cheques to pay for goods and services in foreign shops, restaurants and hotels involves payment. We also consider that the use of electronic travellers' cheques to withdraw currency at foreign ATMs involves payment to the foreign bank in exchange for the currency. Electronic travellers' cheques that can be used for these purposes are likely to constitute e-money. This is because the prepaid balance is accepted by third parties as payment for goods and services.
- 3.26 However, our view is that electronic travellers' cheques that can only be used to withdraw cash from ATMs owned by their issuer do not constitute e-money.

Q7. Do you agree with our proposed guidance on e-money and electronic travellers' cheques?

Q8. Is this guidance clear and comprehensive?

Q9. Are there any additional areas you would like us to address under this heading?

C Trust arrangements

3.27 The proposition has been put to us that a prepaid electronic value system may involve the “float” being placed in a trust account and that this action may result in the prepaid value being taken outside the definition of e-money. This float is the running balance of money held by the issuer of the electronic value, representing payments received for the issue of electronic value (less the amount of any electronic value that has been redeemed). E-money issuers are required to invest 100% of their e-money float in highly liquid, low risk assets. We have considered whether transferring legal ownership of the float to trustees might prevent the issuer of the electronic value from meeting the pre-conditions for issuing e-money. Our view is that it does not. In particular, putting the float into a trust account does not prevent the person who accepts the prepaid value from issuing e-money and the electronic value remains monetary value represented by a claim on the issuer.

Q10. Do you agree with our proposed guidance on e-money in relation to trust arrangements?

Q11. Is this guidance clear and comprehensive?

Q12. Are there any additional areas you would like us to address under this heading?

D Miscellaneous amendments to existing Handbook text

3.28 The definition of e-money contained in the Regulated Activities Order is not an exact copy of the definition contained in the e-money Directive. We have therefore deemed it helpful to include the full text of the Directive definition in our guidance, rather than just a summary.

3.29 We have also made some minor amendments to the Handbook text covering perimeter guidance which was published in April 2002. In Annex 3 of AUTH, we are removing the guidance in 3.2.19 and filling the resultant gap by expanding what we currently say in 3.2.18 into two paragraphs. We are deleting the text currently in 3.2.19 on the grounds that it has been pointed out to us that it is not directly relevant to the question of e-money being issued some time after the payment for it is made.

3.30 We have added new text to 3.3.13 to emphasise the potential significance to a business if its prepaid value were found to be e-money.

3.31 We have amended 3.4.1 to reflect the inclusion in the Handbook of guidance on financial promotion.

Q13. Do you consider the proposed miscellaneous textual changes to our existing perimeter guidance on e-money achieve their stated purpose?

Q14. If not, why not? What alternatives would you propose?

4 Compatibility with the FSA's objectives and general duties under FSMA

Introduction and statement of purpose

- 4.1 This chapter explains why we believe that the proposed perimeter guidance in Annex 2 to this CP is compatible with our general duties under section 2 of FSMA and why it is the most appropriate way of meeting our regulatory objectives. In presenting the proposed guidance set out in this CP, we are satisfied that it is compatible with the general duties conferred upon us.
- 4.2 This CP contains only perimeter guidance. The purpose of this perimeter guidance is to help people decide whether their business is one to which our ELM sourcebook applies or not. Since this CP contains no rules and no guidance on rules, we have not undertaken any cost benefit analysis as part of the present consultation process. A full cost benefit analysis of our regulatory regime for e-money issuers was included in chapter 14 of CP 117.

Compatibility with the Statutory Objectives

- 4.3 The regulatory framework for e-money issuers set out in the specialist sourcebook for e-money issuers (ELM) is aimed at meeting our regulatory objectives, that is public awareness, consumer protection, market confidence and the reduction of financial crime. The Compatibility Statement that was included in Chapter 15 of CP 117 covers our general approach to the regulation of e-money and remains valid for the purposes of this present CP.
- 4.4 We believe that the perimeter guidance contained in the present CP is compatible with our statutory objectives in the following respects.

Public awareness

- 4.5 By issuing this perimeter guidance we are raising public awareness of what products are within, and which are outside, our e-money regime. E-money is

an innovative product and many new electronic payments schemes are likely to be coming onto the market in the foreseeable future. The guidance contained in this CP is issued in response to a number of issues that have been raised with us by persons considering new e-money schemes. We have already issued individual guidance to a number of telephone companies and we are now placing this guidance in the public domain. In addition, we have felt it necessary to issue guidance setting out our views on electronic money in the context of electronic travellers' cheques and trust accounts.

Consumer protection

- 4.6 By issuing this perimeter guidance we are also making clear to consumers where they receive the protection afforded by our prudential regime and conduct of business rules and where they are not so protected. We are therefore taking into account the information needs of consumers. Issuing guidance on the topics covered by this CP also takes into account the risks involved in electronic payments products that come from the fact that this is a new area where the boundaries between what is and what is not regulated are not always clear. Moreover, by raising the issues contained in this guidance, we increase consumer protection by prompting those who want to make available an e-money product to seek authorisation, thereby giving the protection of our regime to their customers.

Market confidence

- 4.7 Issuing this guidance helps reduce uncertainty about what is, and what is not, e-money.

Reducing financial crime

- 4.8 This guidance should assist our financial crime objective in that it will prompt issuers who are carrying on a regulated activity to seek authorisation from us and thereby become subject to our money laundering rules.
- 4.9 Our rules on Systems and Controls and on Money Laundering take account of the desirability of:
- regulated persons being aware of the risk of their businesses being used in connection with the commission of financial crime;
 - regulated persons taking appropriate measures (in relation to their administration and employment practices, the conduct of transactions by

them and otherwise) to prevent financial crime, facilitate its detection and monitor its incidence; and

- regulated persons devoting adequate resources to the matters mentioned in the immediately preceding bullet point of this paragraph.

Compatibility with the need to have regard to the principles of good regulation

- 4.10 Under section 2(3) of the FSMA, we must have regard, in carrying out our general functions, to the specific matters referred to below. We believe that our regime of rules and guidance in relation to e-money issuers, as applied by the perimeter guidance contained in this CP, observes the principles of good regulation as described below.

The need to use our resources in the most efficient and economic way

- 4.11 Issuing this guidance in its current form as general guidance helps with the efficient use of our resources because it substitutes for the need to answer lots of individual queries.

The Responsibilities of those who manage the affairs of authorised persons

- 4.12 Putting our guidance in the public domain enables senior management to take responsibility for ensuring that the business considers whether authorisation is necessary by itself applying our guidance to its business.

The principle that a burden or restriction should be proportionate to the benefits, considered in general terms, which are expected to result from the imposition of that burden or restriction

- 4.13 We believe that issuing this perimeter guidance in its current format is proportionate in that it restricts financial regulation to the issue of e-money, where consumers may be at some risk. It does not seek to extend financial regulation into the area of telephone services, where consumers are already protected by Oftel, by the rules of ICSTIS and by telecommunications legislation.

The desirability of facilitating innovation in connection with regulated activities

- 4.14 Putting this guidance into the public domain reduces the scope for the regulated activity of issuing e-money to affect a new product in an unexpected way, enabling the business to introduce the product with more certainty about its regulatory status.
- 4.15 Our pragmatic approach to determining what is and what is not e-money outlined in paragraph 2.15 above is a practical and robust way of dealing with new products in an innovative area of financial technology.

The need to minimise the adverse effects on competition that may arise from anything done in the discharge of the FSA's functions

- 4.16 By restricting the application of our e-money regime to payments to third parties for the delivery of goods and services outside the boundary of the telecoms networks we are aiming to avoid placing any telecoms company at a competitive disadvantage in respect of other providers of communications or information services.
- 4.17 We are improving competition by making sure that our views on the scope of e-money regulation are available to the public and not just to those who have asked us for individual guidance.

The most appropriate way for the FSA to meet its regulatory objectives

- 4.18 We consider that the proposals contained in this CP form the most appropriate way of meeting our statutory objectives in relation to PRS and the other issues discussed. We believe that these matters are best dealt with by putting them into the public domain as soon as possible. This should enable e-money issuers and the general public to understand how our e-money regime will or will not apply to PRS offered by telephone companies and to the other issues discussed in this CP.

Q15. Do you have any comments on this compatibility statement?

Consolidated list of questions in text

- Q1. Do you agree with our proposed approach, outlined above, to determining whether a scheme is or is not e-money?
- Q2. Is this guidance clear and comprehensive?
- Q3. Are there any additional areas you would like us to address under this heading?
- Q4. Do you agree with our proposed guidance on e-money, prepaid airtime and Premium Rate Services?
- Q5. Is this guidance clear and comprehensive?
- Q6. Are there any additional areas you would like us to address under this heading?
- Q7. Do you agree with our proposed guidance on e-money and electronic travellers' cheques?
- Q8. Is this guidance clear and comprehensive?
- Q9. Are there any additional areas you would like us to address under this heading?
- Q10. Do you agree with our proposed guidance on e-money in relation to trust arrangements?
- Q11. Is this guidance clear and comprehensive?
- Q12. Are there any additional areas you would like us to address under this heading?
- Q13. Do you consider the proposed miscellaneous textual changes to our existing perimeter guidance on e-money achieve their stated purpose?
- Q14. If not, why not? What alternatives would you propose?
- Q15. Do you have any comments on this compatibility statement?

Handbook text
(proposed FSA guidance on
definition of e-money)

MISCELLANEOUS AMENDMENTS TO AUTH APP 3

- 3.2.7 G The definition of e-money in the Regulated Activities Order is based on copies out the definition of electronic money in the E-Money Directive with one exception. The definition in the E-Money Directive is that e-money is "monetary value as represented by a claim on the issuer which is:
- (i) stored on an electronic device;
 - (ii) issued on receipt of funds of an amount not less in value than the monetary value issued;
 - (iii) accepted as means of payment by undertakings other than the issuer".
- 3.2.8 G The main difference exception is that the words "of an amount not less in value than the monetary value issued" in article 1(3)(b)(ii) of the E-Money Directive are not reproduced in the Regulated Activities Order.
- 3.2.18 Some e-money products may be charged up by means of scratch cards that can be purchased from shops. The price paid for the card is the monetary value of the e-money. The card contains a number. The purchaser then enters the number on a web site to activate the e-money account. There is thus a delay between the payment for the e-money and its use by the holder. ~~Such a delay does not make the payment for the e-money a deposit. This is because the means of spending the e-money is put into the hands of the purchaser when he purchases the card.~~
- 3.2.19 G ~~A person may also pay for e-money by cheque. The e-money issuer will not receive the value until the cheque has cleared. This delay does not make the payment for the e-money into a deposit. The purchaser has paid for the e-money even though his payment obligation has only been satisfied conditionally. The delay referred to in AUTH App 3.2.18G does not make the payment for the e-money a deposit. This is because the means of spending the e-money is put into the hands of the purchaser when he purchases the card.~~

[To be added at the end of the existing text]

- 3.3.13 This is so even if in practice most of the e-money is spent with the issuer and only a small portion is ever spent with third parties.

[Insert the following as new text]

Substance of the scheme

- 3.3.22 G When deciding whether a particular scheme involves *issuing e-money* or not, it is necessary to take into account the substance of the scheme. In particular it is necessary to consider whether:
- (1) the scheme involves the issue of prepaid electronic monetary value that the holder can spend with third parties; or
 - (2) the provision by the issuer of some other sort of service.
- 3.3.23 G In considering the question in *AUTH* App 3.3.22G, relevant factors include:
- (1) the risks incurred by the holder of the value;
 - (2) the nature of the rights and obligations of the holder of the prepaid value, the issuer of the value and third parties involved in the scheme; and
 - (3) what the scheme allows the holder of the value to do.
- 3.3.24 G Therefore artificial features of a scheme that disguise, or try to disguise, the payment function as the supply of another sort of service are not likely to prevent the scheme from involving *issuing e-money*.
- 3.3.25 G An example of the application of this approach can be found in *AUTH* App 3.5 (Premium Rate Services).

3.4.1

Guidance on the restrictions on ~~financial promotion~~ *financial promotion* under section 21 of the Act (Restrictions on financial promotion) can be found in *AUTH* App 1~~[to be added to the Handbook at a later date]~~. *AUTH* App 3.4 gives further *guidance* on its application to *e-money*.

3.5 Premium Rate Services

Purpose

- 3.5.1 G This section of *AUTH* App 3 contains *guidance* on whether premium rate services ("PRS") supplied by means of a telephone network involve *e-money*.

Description of premium rate services covered by this guidance

- 3.5.2 G The *guidance* in *AUTH* App 3.5 relates to PRS as defined by the Code Of Practice issued by the Independent Committee for the Supervision of Standards of Telephone Information Services ("ICSTIS") (Ninth Edition (published in March 2002)). ICSTIS is the *United Kingdom* body that regulates the supply of PRS.
- 3.5.3 G The Code Of Practice referred to in *AUTH* App 3.5.2G defines PRS as "services where part of the overall charge paid by a customer to the network operator for the service, being payment for the content of the call or other product or service delivered in the course of, or as a direct consequence of, the call, is passed on by the network operator, directly or indirectly, to the service provider".
- 3.5.4 G The *guidance* in *AUTH* App 3.5 relates to PRS supplied in accordance with the ordinary operation of the Code Of Practice issued by ICSTIS and referred to in *AUTH* App 3.5.2G. One consequence of that is that the *guidance* in *AUTH* App 3.5 only covers goods and services costing less than £20. This is because that Code Of Practice provides that products bought through PRS should generally not cost more than £20.
- 3.5.5 G A simple PRS arrangement works as follows:
- (1) A person (the "subscriber") who wants to buy a PRS will do so by ringing a telephone number used for providing PRS. In the *United Kingdom* those telephone numbers generally have the prefix 090.
 - (2) The PRS seller supplies the PRS. However, the PRS seller does not directly charge the subscriber and the subscriber does not directly pay the PRS seller. The PRS seller looks only to the network operator for payment.
 - (3) The cost to the subscriber of buying the PRS is reflected in the cost to him of making the call to the telephone number in (1).
 - (4) The subscriber pays for that call in the same way as he pays for his other telephone calls.
 - (5) The network operator and the PRS seller share revenues earned by the network operator from calls made to the telephone number in (1).
- 3.5.6 G A more complicated PRS arrangement is described in *AUTH* App 3.5.24G.

Calls paid for after being made

- 3.5.7 G PRS charged to a subscriber's account and paid for later are unlikely to involve *issuing e-money*, as there is no element of prepayment. As explained in *AUTH* App 3.3.5G - *AUTH* App 3.3.9G, prepayment is one of the features of *e-money*.

Calls paid for before being made: Explanation of the potential application of the e-money regime to PRS

- 3.5.8 G If call time is paid for on a prepaid basis, it is necessary to decide whether or not that prepayment is *e-money*. A prepayment arrangement involves the subscriber buying call time from the network operator before making his calls. This prepayment entitles the subscriber to make calls of a value up to the amount of the prepayment.
- 3.5.9 G As with any other product, prepaid call time must satisfy all the conditions in the definition of *e-money* if it is to be *e-money*.
- (1) As explained in *AUTH* App 3.3.1G, part of the definition of *e-money* is that it is monetary value as represented by a claim on the issuer. Prepaid call time complies with this condition.
 - (2) As explained in *AUTH* App 3.3.2G - *AUTH* App 3.3.4G, part of the definition of *e-money* is that the value is stored on an electronic device. Prepaid call time complies with this condition. That device will generally be the computer system of the network operator. Computers run by the issuer of prepaid electronic value can be an electronic device for the purpose of this part of the definition of *e-money* (see *AUTH* App 3.3.14G - *AUTH* App 3.3.21G (Accounted e-money schemes)).
 - (3) As explained in *AUTH* App 3.3.5G - *AUTH* App 3.3.9G (Prepayment), part of the definition of *e-money* is that it is prepaid. Prepaid call time complies with this condition.
- 3.5.10 G The final element of the definition of *e-money* is that the value must be accepted as a means of payment by *persons* other than the issuer. This requirement is explained in *AUTH* App 3.3.10G - *AUTH* App 3.3.13G.
- 3.5.11 G The *FSA* believes that the payment arrangements described in *AUTH* App 3.5.5G can involve payment by the subscriber to the PRS seller. This is for the following reasons.
- (1) Value flows from the subscriber to the PRS seller and the arrangements for this flow of value are set up in advance of the supply of the PRS. The seller of the PRS only delivers the service to the subscriber because he knows the network operator will pay him. The subscriber knows that the charge to him by the network operator will reflect the cost of the PRS.
 - (2) The fact that value does not flow directly between buyer and seller does not mean that there is no payment. This is a feature of other methods of payment, such as some credit card transactions. Any interpretation of the *E-Money Directive* and the provisions of the *Regulated Activities Order* that implement the *E-Money Directive* that place an interpretation of the idea of payment narrow enough to exclude this sort of transfer of value is not likely to be correct.
 - (3) Prepaid call time is used as a means of payment, in that it is the trigger that starts a series of arrangements that result in the seller of the PRS being paid. Without value being loaded by the subscriber, there will be no provision of PRS or payment to the seller of the PRS.
- 3.5.12 G For the reasons in *AUTH* App 3.5.9G - *AUTH* App 3.5.11G, prepaid call time that can be used to buy PRS is potentially *e-money*. As explained in *AUTH* App 3.3.13G, this conclusion is not affected by the fact that very little of the prepaid call time may be used to buy PRS.

PRS and prepaid call time that may not involve e-money

- 3.5.13 G Despite the conclusion in *AUTH* App 3.5.12G, the *FSA* believes that in many or most cases PRS have features that mean that the fact that prepaid call time can be used to buy them does not cause that prepaid call time to be *e-money*.

- 3.5.14 G As explained in *AUTH* App 3.3.22G - *AUTH* App 3.3.25G (Substance of the scheme), when deciding whether a particular scheme involves *issuing e-money* or not, it is necessary to take into account the substance of the scheme. Therefore, in the case of PRS, if:
- (1) the prepaid call time, when it is used to acquire PRS:
 - (a) is not being used as a means of payment of *persons* other than the network operator; and
 - (b) is being used to pay for a service provided by the network operator; and
 - (2) the services provided by the network operator cannot be described as including payment facilities for the acquisition of goods and services from third parties;
- that prepaid call time is not *e-money*.
- 3.5.15 G In other words, under the approach in *AUTH* App 3.3.22G - *AUTH* App 3.3.25G (Substance of the scheme), one must ask whether in substance what is offered is a telephone service or a means of payment for other goods and services.
- 3.5.16 G The reason for concluding that the use of prepaid call time used as described in *AUTH* App 3.5.14G does not involve *e-money* is that the prepaid call time is being used to pay for a service supplied by the network operator and not as a means of paying the PRS seller. The service provided by the network operator is the supply of data. That means that the prepaid call time does not satisfy the requirement in the definition of *e-money* that the prepaid value should be accepted as a means of payment by *persons* other than the issuer of the prepaid value (see *AUTH* App 3.3.10G - *AUTH* App 3.3.13G).
- 3.5.17 G In the *FSA*'s view, prepaid call time will in principle fall into *AUTH* App 3.5.14G (with the result that the ability to use prepaid call time to buy PRS does not make that prepaid call time *e-money*) if the prepaid call time can only be used to buy PRS in accordance with the following:
- (1) the supply of telecommunications services by the network operator and the supply of the services by the PRS seller can be seen as a single service (the supply of data) paid for by the prepaid call time;
 - (2) the supply of the call time and the supply of the PRS take place in the same action;
 - (3) they are provided to the subscriber through the network operator's network and while the subscriber is consuming the call time or in another way that is consistent with (1) and (2);
 - (4) the network operator delivers the PRS to the subscriber;
 - (5) what the subscriber pays for the PRS is charged against his call time account;
 - (6) the network operator pays the PRS seller; and
 - (7) the PRS seller is not privy to or concerned with the contract between the network operator and the subscriber.
- 3.5.18 G The reasons for the conclusion in *AUTH* App 3.3.17G is that the *FSA* does not believe that prepaid call time should be regarded as being used to pay a third party, the PRS seller, where it is being used to pay for a single, indivisible, service, and that service is being supplied by the network operator. That service is the supply of data.

- 3.5.19 G Examples of types of PRS that can be consistent with prepaid call time not being *e-money* include the supply of the following:
- (1) recorded spoken information such as weather reports;
 - (2) data, such as stock market prices;
 - (3) images, such as a cartoon strip;
 - (4) video clips;
 - (5) the output of a radio station;
 - (6) ring tones; and
 - (7) electronic games.

- 3.5.20 G The following methods of delivering PRS can be consistent with prepaid call time not being *e-money*.

- (1) Transfer over two networks as follows:
 - (a) PRS are routed for part of the way over another network operator's network;
 - (b) the subscriber pays the issuer of the prepaid call time for the whole call; and
 - (c) the arrangements for the carriage over the second network operator's network are purely a matter between the two network operators.
- (2) Transfer to a multi-use device as follows:
 - (a) the PRS are supplied to a telephone that is also a mini-personal computer or to a PDA (i.e. a personal digital assistant) that works as a personal computer and telephone;
 - (b) the PRS are supplied to the subscriber over the Internet to the electronic device; and
 - (c) the prepaid call time pays for the delivery of the PRS to the subscriber.
- (3) The PRS are supplied to a telephone that acts as a modem that links a personal computer to the Internet and those PRS are supplied to the personal computer via the telephone. The prepaid call time pays for the delivery of the PRS to the subscriber.
- (4) The subscriber uses his airtime to pay for services that are supplied to another subscriber. For instance, one subscriber may buy the supply to another subscriber of football results by way of SMS (i.e. a short message service) as a present, with payment for the delivery of the results being made by charging the first subscriber for the messages sent to the second.

PRS and prepaid call time that may involve e-money

- 3.5.21 G However if prepaid call time can be used to buy PRS that fall outside *AUTH* App 3.5.17G, that prepaid call time is likely to be *e-money* for the reasons in *AUTH* App 3.5.9G - *AUTH* App 3.5.12G.

- 3.5.22 G A PRS will not fall into *AUTH* App 3.5.17G if it is not in the form of services. A PRS in the form of a supply of physical goods is therefore likely to result in prepaid call time being *e-money*.
- 3.5.23 G The following are examples of ways in which PRS may be supplied to the subscriber that fall outside *AUTH* App 3.5.17G (with the result that they are likely to cause prepaid call time to be *e-money*):
- (1) the PRS are recorded on a computer disk and sent through the post;
 - (2) the PRS are delivered as follows:
 - (a) they are delivered to the subscriber's personal computer over an Internet connection;
 - (b) that connection is over another network, such as a landline;
 - (c) the contract for the provision of the Internet connection is separate from the arrangements for the telecommunications services for which the prepaid call time pays; and
 - (d) as a result the prepaid airtime does not pay for the delivery to the PC.

Interconnection

- 3.5.24 G Buying PRS may involve more than one network operator, as follows:
- (1) a subscriber has a contract for telephone services with network operator A;
 - (2) the subscriber buys PRS from a PRS seller whose contract is with network operator B rather than network operator A;
 - (3) therefore the telephone number referred to in *AUTH* App 3.5.5G(1) is a number on network operator B's network and the revenue sharing arrangement referred to in *AUTH* App 3.5.5G(5) is between the PRS seller and network operator B;
 - (4) network operator B charges network operator A for the call by the subscriber as part of the arrangements between the two network operators for charging for calls originating on the network of one of them and terminating on the network of the other; and
 - (5) the charge in (4) is the basis for the revenue sharing between the network operator and the PRS seller referred to in *AUTH* App 3.5.5G(5).
- 3.5.25 G *AUTH* App 3.5.25G - *AUTH* App 3.5.28G consider whether prepaid call time issued by network operator A is *e-money* if:
- (1) it can be used to buy PRS in the way described in *AUTH* App 3.5.24G; and
 - (2) those PRS include PRS that do not comply with the *guidance* in *AUTH* App 3.5.17G, such as the sale of physical goods, with the result that the simple application of that *guidance* would mean that that prepaid call time would be *e-money*.
- 3.5.26 G As with PRS generally, it is necessary to look at the substance of the transaction, as described in *AUTH* App 3.3.22G - *AUTH* App 3.3.25G (Substance of the scheme).

- 3.5.27 G In the FSA's view, the factors in *AUTH* App 3.5.24G do not result in prepaid call time issued by network operator A being *e-money* if:
- (1) the PRS seller has no relationship with network operator A;
 - (2) network operator A has no control over the contractual arrangements between network operator B and the PRS seller;
 - (3) network operator A cannot stop prepaid call time issued by it from being used to buy PRS on network operator B's network falling outside *AUTH* App 3.5.17G; and
 - (4) the acceptance of prepaid call time issued by network operator A by the PRS seller is not under the control of network operator A.

- 3.5.28 G The reason for the conclusion in *AUTH* App 3.5.27G is that, as between network operator A and the subscriber, network operator A sells the subscriber telephone services, not a means of paying third parties.

Artificial schemes

- 3.5.29 G The conclusion that prepaid call time does not become *e-money* merely because it can be used to buy PRS in a way that complies with the conditions in *AUTH* App 3.5.17G puts great weight on the services supplied by the network operator. That means those services should have real substance. Therefore, as described in *AUTH* App 3.3.22G - *AUTH* App 3.3.25G (Substance of the scheme), artificial schemes that disguise the payment function as the provision of a telecommunications service are unlikely to fall into *AUTH* App 3.5.17G.

3.6 The application of the e-money definition to various products

- 3.6.1 G This section of *AUTH* App 3 contains *guidance* on whether certain products involve *issuing e-money*.

Electronic traveller's cheques

- 3.6.2 G An electronic traveller's cheque is a product, based on a plastic card, designed to replace paper traveller's cheques. There are two types of electronic traveller's cheques:
- (1) ones whose only function is to allow the holder to withdraw cash in a foreign currency from automated teller machines ("ATMs") when abroad; and
 - (2) ones that can also be used to buy goods and services from third parties.
- 3.6.3 G The card referred to in *AUTH* App 3.6.2G is loaded with value. The holder pays for the value on issue. The value therefore complies with the part of the definition of *e-money* that says that the value must be issued on receipt of funds (see *AUTH* App 3.3.5G - *AUTH* App 3.3.9G). The card is likely to be an electronic device for the purpose of paragraph (a) of the definition of *e-money* (which is explained in *AUTH* App 3.3.2G - *AUTH* App 3.3.4G).
- 3.6.4 G The remaining condition that value must meet if it is to be *e-money* is that the value must be accepted as a means of payment by *persons* other than the issuer. This part of the definition is explained in *AUTH* App 3.3.10G - *AUTH* App 3.3.13G.
- 3.6.5 G An electronic traveller's cheque falling into *AUTH* App 3.6.2G(2) meets the part of the definition of *e-money* referred to in *AUTH* App 3.6.4G.
- 3.6.6 G An electronic traveller's cheque falling into *AUTH* App 3.6.2G(1) does not meet the part of the definition of *e-money* referred to in *AUTH* App 3.6.4G if the scheme is set up in such a way that:
- (1) it can only be used to withdraw foreign currency from ATMs owned by the issuer of the value; or
 - (2) (if (1) does not apply) the withdrawal of foreign currency by a cardholder will never involve the purchase of the currency from the owner of the ATM but instead the repayment of the prepaid value by the issuer of the prepaid value.

Trust accounts

- 3.6.7 G A prepaid electronic value payment system may involve the "float" being paid into a trust account. The float is the running balance of money held by the issuer of the electronic value representing payments for the issue of electronic value less the amount of electronic value that has been redeemed.
- 3.6.8 G Holding the float on trust:
- (1) does not prevent the electronic value from being monetary value as represented by a claim on the issuer (this part of the definition of *e-money* is described in *AUTH* App 3.3.1G);
 - (2) is not relevant to the other elements of the definition of *e-money*; and

(3) does not mean that the *person* who accepts the payment for the electronic value is not the issuer of that value.

3.6.9

G The result of *AUTH* App 3.6.8G is that putting the float into a trust account does not prevent the *person* who accepts the payment for the electronic value from *issuing e-money*.

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