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Consultation on the revision of the E-money Directive. A response from the Mobile Broadband Group

The Mobile Broadband Group (MBG, whose members are the UK mobile businesses of O2, Orange, T-Mobile, Virgin Mobile, Vodafone and 3) welcomes the opportunity to respond to the consultation by Her Majesty's Treasury on the revision of the E-money Directive.

In summary, the MBG is supportive of the proposals being made by the European Commission and welcomes the many changes incorporated in this revised Directive. Many of the concerns highlighted by the industry in relation to the first e-money Directive (i.e. definition, scope) have been addressed. We also welcome the alignment between this revised Directive and the Payment Services Directive.

However we have two main comments: the first is in relation to existing business models, the second is in relation to developing the market for e-money.

Existing business models

When the Commission issued guidance in 2005 on the applicability of the E-money Directive to mobile operators, it stated in paragraph 13 that:

“First, given the fact that in many cases (though not all), it appears that mobile operators themselves arrange for the payment of third party content providers, either as a result of a contractual relationship under which the mobile operator assumes the liabilities of its pre-paid customers towards a merchant or through a revenue-sharing arrangement with a merchant, it is arguable that many purchases of third-party content do not give rise to e-money.”

In other words, where there is no direct payment relationship between the customer and the merchant no e-money is created; fundamentally there is no payment service, as the mobile operator stands between the two parties.

A similar type of arrangement benefits from the negative scope under Article 3(b) of the Payment Services Directive (*payment transactions from the payer to the payee through a commercial agent authorised to negotiate or conclude the sale or purchase of goods or services on behalf of the payer or the payee*)

The MBG assumes it is envisaged that business models where the *mobile operator assumes the liabilities of its pre-paid customers towards a merchant or through a revenue-sharing arrangement with a merchant* will remain outside the scope of e-money.

Nevertheless, the MBG would prefer that the Commission put the matter beyond doubt by making specific reference this situation within the recitals of the Directive.

In this way, existing business models will be undisturbed. It would be unfortunate if the review resulted in taking a step backwards.

Future business models

The purpose of the review is promote competition in the development of e-money services and to extend its use by members of the public.

An absolutely key distribution channel for new e-money business models is the mobile phone, which enjoys almost universal adoption throughout the European Union. If E-money is to be truly successful, uptake within the mobile community is almost a necessity.

A potential route for e-money development is for mobile operators to implement hybrid models whereby pre-paid airtime could be used to make payments for third party goods **including** direct payment services (as opposed to the situation where the mobile operator assumes the liability of its customer, as described above) and even person to person payments.

The proposed rule revision is generally conducive to new business models, except in one regard: redeemability.

Of particular concern to mobile operators is the additional requirement on redeemability that was recently tabled by the Council. The proposed Article 10b(6) could be interpreted as an obligation to redeem **all** funds held on mobile prepaid accounts with an e-money functionality. Whilst we understand that the underlying policy objective is to protect consumers, such a requirement would be disproportionate for the following reasons:

- The danger of legal uncertainty. The scope of the Directive covers e-money rather than prepaid funds of any kind. The obligation to redeem the entire prepaid account is clearly beyond the scope and could lead to legal uncertainty.
- Prepaid services enables customers to limit their exposure to risk. Customers recharge their prepaid accounts with small amounts and make regular transactions, which allows them to mitigate the risk themselves.
- The primary function of prepaid accounts. As the original Commission consultation acknowledged only about 1% of current expenditure is for value added services. Even if hybrid models were to be developed, payment volumes would likely remain lower than expenditure on airtime and it would not be proportionate to require balances to be redeemed, when only a portion would ever be spent on e-money.
- The nature of the prepaid business model. In the prepaid business model, prepayment reflects a commitment by the customer to spend a certain amount in return for a service, namely access to a network and the possibility of being called by others. Redeemability of the entire prepaid account would mean that the customer gets access to the network for free.

- As above, we believe that Hybrid accounts provide certain attractions for customers (for example, keeping things simple and not complicating service (e.g. having to top up a separate e –money account)). We believe, requirements to redeem the entire pre-paid balance regardless of whether it is (or is likely to be) used by the customer will be a fundamental barrier to development of hybrid solutions.
- Such a barrier will be undesirable. The arrival of prepaid airtime in 1997 was absolutely fundamental to the development of the mobile market and is generally credited with bringing universal adoption of mobile telephony - including the “unbanked”. The MBG believes, that as with mobile adoption, the e-money market could be developed if hybrid models could be made to work. A requirement to redeem to cash would be a significant impediment to that development, as mobile operators could not make an economic case for reconverting prepaid airtime into cash, in particular in these times when businesses need to strictly control their cash outflows.

The MBG believes that there is no need for redeemability to be a requirement in the hybrid model (i.e. where the prepaid balance has been created with the primary intention of it being put to some particular purpose such as purchasing network airtime or travel), when the customer knows that any balances can be expended on the primary purpose, as and when required. Over the last few years customers have spent billions on prepaid airtime without the need for redeemability being apparent. There is demonstrably absolutely no issue with consumer confidence.

After all, in a hybrid situation, balances are held primarily for the main purpose and are really only *potentially* e-money in that they can be used for third party services. The MBG believes that requirements to redeem the entire pre paid balance on hybrid accounts will be a significant disincentive to the introduction of hybrid models.

The MBG suggests that within the recitals of the Directive, it is made clear that redeemability is not applicable when outstanding balances can be applied to the primary purpose.

This is a perfectly reasonable solution, as customers would be in a position to accept or reject the terms and conditions as they see fit. Issuers that offer to redeem for cash may have a competitive advantage (in this respect at least) but the customer would be free to choose the service that suited his or her requirements best. The MBG does not understand why this requirement has to be centrally regulated.

If the Commission wishes to see the e-money market develop, removing the ‘redeemable for cash’ requirement is essential.

1. Do you agree that the proposed new definition of e-money, and the exemptions for limited networks and digital payments where the operator is not acting only as an intermediary, are positive developments?

Yes.

Please note our comments above, that it would help if the recitals to the Directive made it clear that there is no e-money where there is no direct payment relationship between the supplier and the customer.

2. Do you agree that the exemption for digital payments could be further refined, with the aim of achieving technological neutrality between digital and material goods, and if so, how?

The MBG wants the exemption to be identical to the Payment Services Directive so as not to cause confusion between the two regimes.

3. Do you agree that the proposed definition of outstanding e-money should be based on float (i.e. financial liabilities in issue at a point in time)?

Yes – but for hybrid models, Method D should be adjusted in accordance with an average of funds used for e-money transactions as a proportion of total funds outstanding.

Compare Payment Services Directive Article 9(2). *Where a payment institution is required to safeguard funds under paragraph 1 and a portion of those funds is to be used for future payment transactions with the remaining amount to be used for non-payment services, that portion of the funds to be used for future payment transactions shall also be subject to the requirements under paragraph 1. Where that portion is variable or unknown in advance, Member States may allow payment institutions to apply this paragraph on the basis of a representative portion assumed to be used for payment services provided such a representative portion can be reasonably estimated on the basis of historical data to the satisfaction of the competent authorities.*

4. Do you agree with the Commission's proposed change to the status of ELMIs from credit institutions to financial institutions?

Yes

5. Do you agree that Sterling payments should remain outside the scope of the Regulation? Please give reasons.

Chapter 3: The prudential regime for e-money institutions

6. Do you support the Commission proposal to align the qualitative EMD prudential requirements with those of the PSD?

Yes

7. Do you support the Commission proposal to reduce initial capital from €1m to €125,000?

Yes

8. Do you agree that Method D own funds for e-money institutions should be based on float (i.e. financial liabilities in issue at a point in time) rather than on payment volume?

Yes

9. Do you support the Commission proposal to remove the prohibition on mixed business for ELMIs?

Yes

10. Do you support the Commission proposal to extend the PSD safeguarding requirements to ELMIs and agree that PSD Article 9(2), enabling a representative portion to be safeguarding, should also be extended to ELMIs?

Yes

11. Do you agree that a more appropriate EMD waiver criterion would be one based on float (i.e. outstanding liabilities in issue at any time) rather than payment volume, and with a minimum threshold of €5-6m, as contained in the existing EMD?

Yes, subject to response to question 3, although consideration should also be given to raising the waiver threshold in line with inflation.

EMD Regulation

Chapter 4: EMD conduct of business requirements

12. Do you support the Commission's proposed clarification of the redeemability requirements?

No.

We do not agree that e-money has to be redeemable for cash to maintain bearer confidence. Customers have bought billions of pounds worth of prepaid airtime in the last ten years, with total confidence that the balance will be redeemable and useful for network airtime.

As explained more fully in our introductory remarks, if e-money is to take off and hybrid business models are to emerge, it is absolutely essential that this aspect is re-examined.

After all, a customer makes a prepayment primarily for airtime. At the time of purchase, he or she only has a balance that is potentially e-money. Whether it is e-money will not actually be known until the moment when the decision to purchase occurs.

The requirement should only be to redeem for the service for which the prepayment was primarily intended (in a mobile operator context – network airtime). We do not agree with the bearer confidence point. This is not borne out by the evidence of the last ten years.

13. Do you support the Commission's proposed increase in threshold values beneath which e-money issuers need not comply with full anti-money laundering due diligence requirements?

Yes

Chapter 5: Supervision

14. Do you consider the transitional provisions in the Commission proposal to be appropriate?

Yes

15. Do you agree that the FSA and FOS should take responsibility for the applicable aspects of Articles 6-10 (including complaints procedures, cooperation with other Member State authorities, and penalties) in the Commission's proposed revision of Regulation 2560?

Yes