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1. INTRODUCTION

Article 17 of Directive 2009/110/EC, on the taking up, pursuit and prudential supervision of the business of electronic money institutions, (hereafter "EMD2"), requires the Commission to present a report to the European Parliament, the Council, the European Economic and Social Committee and the European Central Bank giving a full assessment on the implementation and impact of the Directive, accompanied, where appropriate, by a proposal for its revision, no later than 1 November 2012. This report is the response of the Commission to this requirement.

The EMD2 review process is based on two dedicated external studies. The first study consisted of a legal conformity assessment of the transposition of EMD2 in the 27 Member States and was finalised in April 2013. The second study analysed the economic impact of EMD2 on the electronic money market and was finalised at the end of 2014. Furthermore, the Commission has taken account of the input from Member States and stakeholders gathered through its advisory committees for retail payments policy and has updated the data on the number of authorised, waived and passporting electronic money institutions as of January 2017.

This report covers the years 2009 to 2014. The production of this report was postponed as a majority of Member States failed to implement the Directive by the transposition date of April 2011. By the deadline for this report to be delivered, i.e on 1 November 2012, only 23 Member States had fully –and in most cases, recently- transposed the Electronic Money Directive into their respective national law. At that time, the electronic money market had too little practical experience with the EMD2 to provide meaningful feedback on the actual effects of the new legislation. The Commission also considered it important to take account of the results of the review process of the Payment Services Directive¹ (hereafter: PSD), which will have an impact on the legal framework for e-money institutions through the multiple cross-references in EMD2 to its legal framework. The revised Payment Services Directive (PSD2) was adopted by the European Parliament and the Council end 2015 and entered into force on 13 January 2016.

On 5 July 2016, the Commission also adopted a legislative proposal for amending the fourth anti-money laundering Directive ((EU) 2015/849) to address the more recent terrorist financing risks that have been detected after the Paris terrorist attacks (COM (2016), 450 (final)). It is likely that this proposal will also have an impact the e-money market in the Union, in particular where it concerns anonymous prepaid instruments, whose use could become more limited. The EMD2 report has not been able to take account of this latest development, but any potential changes to the anti-money laundering/terrorist financing framework for these instruments will have to be taken into account in a possible revision of EMD2.

¹ Directive 2007/64/EC on payment services in the internal market.

This report describes the transposition of the EMD2 (section 3), reviews its application and its impact to date (section 4) and the impact of the recent revision of PSD (section 5) and the relationship between EMD2 and the Fourth Anti-Money Laundering Directive² (AMLD4) (section 6). It identifies the main emerging issues resulting from the application of the Directive (section 7), and draws certain conclusions in section 8. Work on this report was undertaken before the adoption of the current Better Regulation Guidelines, so it does not represent an evaluation of EMD2 in line with these Guidelines.

2. BACKGROUND

Electronic money (e-money) is the digital equivalent of cash and can be software or hardware based. Card-based e-money, such as e-money stored on a prepaid card or an electronic purse, is usually depicted as hardware-based. Another option is to store e-money in a payment account on the Internet. It is then considered software-based.

The legal framework on electronic money was established by the Directive 2000/46/EC on the taking up, pursuit of and prudential supervision of the business of electronic money institutions (hereafter: the first Electronic Money Directive).

At the time of the review of the first Electronic Money Directive in 2006, figures on the limited number of fully licensed electronic money institutions or on the low volume of electronic money issued, demonstrated that electronic money had not yet really taken off in most of the Member States. Some of the provisions of the first Electronic Money Directive, in particular the capital requirements imposed on electronic money institutions, were viewed by many in retrospect as too high and therefore an obstacle to the development of the electronic money market. The 2006 review concluded, notably in the light of the forthcoming adoption of PSD, that further action was required to promote the emergence of a true single market for electronic money services in the European Union.

Following this, the Commission proposed the EMD2. This Directive focuses on modernising the provisions of the first Electronic Money Directive, with special reference to the prudential regime of electronic money institutions, ensuring consistency with the Payment Services Directive.

The EMD2 was adopted by the European Parliament and the Council in 2009 and aimed at establishing a modern and harmonised legal framework for the issuance and redemption of e-money, which would enable new, innovative and secure electronic money services to be designed. To this end, EMD2 provides a fully harmonised and simplified set of rules with regard to the licensing of e-money institutions and reinforces the rights and obligations linked to the redemption of funds by consumers. It applies to e-money service providers in all EU Member States as well as in Iceland, Liechtenstein and Norway.

By modernising the EU rules on electronic money, especially bringing the prudential regime for electronic money institutions in line with the requirements for payment institutions in PSD, EMD2 aimed at providing market access to new companies and fostering real and effective competition between all market participants to improve efficiency and reduce the cost of payments.

² Directive 2015/849/EU.

3. TRANSPOSITION OF EMD2

The Directive³ was to be implemented into national law by Member States by 30 April 2011. A conformity assessment of the national measures in 27 Member States (excluding Croatia) implementing the EMD2, covering most articles of the Directive, was carried out by an external consultant⁴ and finalised in April 2013.

This conformity assessment showed that overall, the implementing laws of the Member States were in conformity with the Directive. While EMD2's general approach was one of full harmonisation, some of its provisions left some flexibility to Member States. Cooperation between national regulators and the Commission to ensure the consistent, timely and equivalent transposition of these provisions into national law was therefore crucial. To this end, the Commission held best-practice workshops and put in place an interactive question-and-answer website known as YQOL (Your questions on legislation). Today, all EU Member States have implemented the Directive.

4. APPLICATION AND IMPACT OF EMD2

The economic study on the impact of EMD2 on the European electronic market concluded that the overall effect of the EMD2 on the market is positive.

4.1. Subject matter, scope and definitions (Title I EMD2)

The economic study confirmed that while the definitions of e-money and the overall scope of the EMD2 are broadly considered appropriate, both Member States and stakeholders face challenges in deciding the appropriate legal framework that should apply to more complex products. For these products, it is difficult to make a distinction between a payment account, an e-money account and a bank account. This is particularly the case for prepaid card schemes, which have in some instances been considered to be subject to PSD, and in other instances as e-money institutions.

There are also divergences of approach with regard to the legal concept of agent and the non-defined concept of distributor, which has a different status in EMD2. Clarifications are also sought with regard to the approach to limited networks, which are excluded from the scope of EMD2. The divergent interpretation between national authorities on that front, often based on a case-by-case application, is voiced as an issue of concern.

The different approaches with regard to the scope and subject matter of EMD2 have led a number of competent authorities to conclude that it would be better to merge PSD (now PSD2) and EMD2 in the future to ensure a more consistent application and interpretation across Member States.

4.2. Market access, structure and prudential rules (Title II EMD2)

Based on the market data provided in the context of the economic study, and the updated data gathered by the Commission on licensed, waived and passporting institutions in all Member States, there is evidence of increased interest in electronic money licenses and that e-money institutions active in the market today obtained their licenses since the entry into force of the

³ Article 22 EMD2.

⁴ Tipik study, published on the Commission's website:

http://ec.europa.eu/finance/payments/emoney/transposition/by-country_en.htm

Directive in 2011 (see table in Annex). Prepaid cards and e-wallets seem to be more popular, with a large variety in the number of services attached to these products.

Although there is a clear growth in the number of licensed e-money institutions since 2011, in view of the limited availability of comparable quantitative data, it is difficult on the basis of this empirical analysis to demonstrate the existence of a correlation between the modernisation of the legal framework with EMD2 and that positive trend.

The economic study nevertheless indicates that the fact that the Directive provides more clarity and lowers capital requirements compared to the first Electronic Money Directive is an important improvement to the legal framework governing e-money institutions. Furthermore, the fact that payment services and e-money services can be provided under one single licence is identified as positive, and many e-money institutions do provide payment services in addition to e-money services.

On the other hand, e-money institutions notice that there are differences in the national implementation and interpretation of the provisions on supervision which have an impact on the level playing field for E-money institutions in the EU. As a result, e-money institutions engage in "forum shopping", choosing to register in the Member States that provide the most beneficial legal frameworks from their viewpoint.

The compliance costs for e-money institutions differ depending on the size of the institution concerned, the country in which it is licenced and the nature of its business model. Overall, these compliance costs are estimated to represent between 1 and 5% of the overall costs (ranging from EUR 25,000 to EUR 0.5 million). In absolute terms these costs could thus be relatively high for some e-money institutions. However, in these and other cases they should be offset by the reduction in capital requirements brought about by EMD2 (from EUR 1 million to EUR 350,000).

Cross-border activity through the use of passporting has increased in Member States since 2011. Feedback from competent authorities in the economic study confirms that there is still room for improvement in the cooperation between Member States in the case of passporting.

The optional waiver regime for smaller e-money institutions proposed in Article 9 has been used by a number of Member States. The option is overall considered as positive by the e-money institutions that have benefited from it. Some industry stakeholders would prefer a more gradual approach with intermediate categories of e-money institutions, to avoid an "all or nothing" approach.

4.3 Issuance and redeemability of electronic money (Title III EMD2)

The economic study has not identified serious issues in relation to the provisions on issuance and redeemability of electronic money. No evidence was found that EMD2 had an impact on the quality and prices of products and services provided by the issuers, nor on the confidence of consumers in such products and services. Consumer associations have not reported specific concerns or problems related to electronic money from the point of view of consumers.

As regards the costs associated with the obligation for issuers to redeem at any time e-money upon request by the e-money holder, the study did not report serious issues or significant costs associated to consumers invoking this right.

5. IMPACT OF PSD2 ON EMD2

There is significant crossover between the PSD and the EMD2. The latter follows the logical framework contained in the PSD. As laid out in Article 3 (1) of EMD2, Articles 5 and 10 to 15, Article 17(7) and Articles 18 to 25 of PSD apply to e-money institutions. These articles relate to applications for authorisations, granting of authorisations, communication of the decision, withdrawal of authorisation, registration, maintenance of authorisation, accounting and statutory audit, notification requirements when outsourcing operational functions of payment services, liability, record keeping, designation of competent authorities, supervision, professional secrecy, right to apply to courts, exchange of information and exercise of the right of establishment and freedom to provide services.

The PSD has recently been revised. In July 2013, the European Commission published its proposal. The final compromise text was voted by the Parliament on 8 October 2015 with adoption by Council on 25 November 2015. Among the major changes brought forward by PSD2 (regulation of the so-called third party payment service providers, increased security requirements for electronic payments, partial coverage of international transactions in or out of the EU), the one with the most impact on electronic money institutions relate to the strengthening of the prudential rules for payment institutions which foresee a stronger supervisory role and competences for the host Member State where a payment institution is passporting its services to another Member State.

Also the clarifications in PSD2 on the exemption on limited networks, combined with the obligation for all limited networks to notify their activities once the size of their business reaches a certain threshold, will provide better guidance to competent authorities to assess the applicability of the legal framework of PSD2 or EMD2 to these networks. As these limited networks shall also be registered in the national registers and the central register managed by EBA, there will also be more transparency on the way limited networks are assessed by the different authorities.

6. ANTI-MONEY LAUNDERING AND EMD2

E-money institutions are subject to anti-money laundering legislation. The fourth anti-Money Laundering Directive (AMLD4) which was adopted in 2015, will also apply to them. The date for transposition of the AMLD4 was June 2017.

The economic study does not make any short to medium term recommendation in this respect. The study found that industry stakeholders see most e-money transactions as low risk partly due to the small size of the e-money market. However, a recommendation for the longer term would be to ensure that specific provisions are harmonised to the maximum, in particular the thresholds for due diligence under the anti-money laundering provisions and the possibility to register as small e-money institutions. This would help secure a more level playing field. The thresholds for due diligence could be examined after the transposition of AMLD4.

The review should also take into account the further changes that will be made to AMLD4, which were proposed by the Commission in its legislative proposal of 5 July 2016 (COM (2016), 450 (final)), and which are currently under negotiation by Council and European Parliament.

7. REVIEW OF EMD2 AND EMERGING ISSUES

One of the key challenges identified by the economic study is the classification of products and services as e-money or as payment services, as e-money accounts or payment accounts, and thus the application of the appropriate legal framework. Also the different approaches by national authorities to agents and distributors is identified as an issue of concern.

The issue of divergent interpretations with regard to limited networks is of particular concern for e-money services and the so-called closed loop schemes (such as gift cards, store cards, petrol cards), semi-closed loop (a variant of the close loop category, determined by the scope of the network in which the card can be used) and open loop schemes (such as general purpose prepaid debit cards). The improvements made within the context of the review of PSD2 will also have a positive effect on the application of this exemption in EMD2.

Another key challenge raised by the economic study is the cooperation between Member States in the context of cross-border supervision. With the adoption of PSD2 and its detailed provisions in this area, the information exchange and cooperation will be further strengthened with a stronger role for the host Member State to oversee the activities of the passporting EMI in its territory.

The study notice that E-money institutions face problems in relying on the commercial banks for deposits. The solutions envisaged by e-money institutions to address these difficulties would consist in improving their access to the interbank system or to central banks for deposit holding. PSD2 will improve the situation for e-money institutions on this point, with its new provisions on access to bank accounts and on non-discriminatory access to payment systems.

Although the study shows that there was support from some stakeholders for merging the PSD and the EMD2, this support was not unanimous. Such a merger would also not provide a solution to issues faced by stakeholders in relation to the classification of products as electronic money. This is particularly evident from the Member States that have a single regulation governing both the Payment Services Directive and the Electronic Money Directive and are still faced with that challenge.

8. CONCLUSIONS

The overall assessment of the EMD2 is positive. The objective of the EMD2 was to remove barriers to market entry and to facilitate the take up and pursuit of the business of electronic money issuance, by creating a level playing field for all players in the market. It seems that EMD2, to a large extent, has fulfilled this objective. There is evidence of an increased interest in electronic money licenses and cross-border activity through the use of passporting has increased since 2011. The offer of electronic prepaid cards in particular is growing, including through their distribution by institutional actors such as national Post Offices. E-money remains a niche market, which paradoxically seems to have been hardly affected by the recent technological changes, be it the emergence of virtual currencies – little used as means of payments – or of the Fintechs, which are leading digital change in the more traditional segments of the payments market.

further improvements could be made to enhance the current regulatory framework. Concrete improvements could thus be delivered in the short or medium term by providing guidance in three areas, namely the classification of products as e-money, the application of the limited network provision and the distinction between the concept of an agent and a distributor in the context of e-money. The challenges encountered in the cross-border supervision of E-money

institutions seem to be addressed adequately in the context of the PSD2, which, through the relevant cross-references, will also apply to e-money institutions.

Further consideration could be given, in the longer term, to promoting maximum harmonisation for specific provisions, in particular with regard to the currently optional waiver regime foreseen for small electronic money institutions under Article 9 of the EMD. Likewise, a further analysis could be conducted on the development of an intermediate category of a 'large limited network' that would be subject to some but not all EMD2 requirements. At the same time, on that latter aspect, the improved clarity provided in PSD2 on limited networks already brings about increased legal certainty for entities operating a limited network and may already provide a satisfactory response to market's expectations.

A future revision of the Directive and its merger with the revised Payment Services Directive would require further analysis. It seems appropriate to consider such steps only after Member States and stakeholders will have been able to gather experience with the adapted framework following the adoption of PSD2, which will also have an impact on e-money institutions.