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Activities of financial market participants

Review of the Activities of Electronic Money and Payment Institutions

2019

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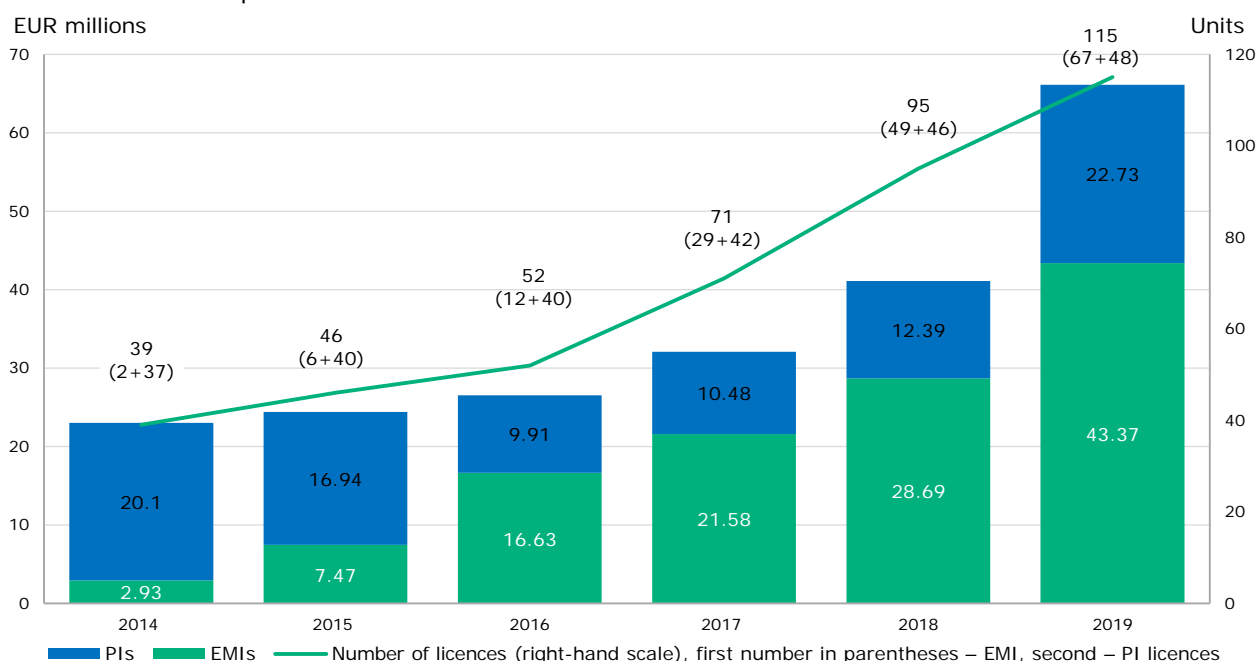
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Number of electronic money and payment institutions. At the end of 2019, a total of 115 electronic money institutions (EMIs) and payment institutions (PIs) operated in Lithuania – a one-fifth increase compared to the previous year.

As at 31 December 2019, the public list of electronic money and payment institutions included 67 EMIs and 48 PIs (see Chart 1), of which 6 EMIs and 12 PIs held a licence for restricted activity only valid in the Republic of Lithuania. Under this licence, monthly average outstanding electronic money must not exceed €900 thousand and/or the average amount of payment transactions performed over the last 12 months must not exceed €3 million per month. One PI held a licence for the provision of account information services only. Institutions holding this type of licence are not subject to capital requirements, although they must hold professional indemnity insurance or a comparable guarantee. In 2019, compared to 2018, the largest change was observed in the number of EMIs, which increased from 49 to 67 (including 2 former PIs which became EMIs).

It should also be noted that in 2019 market participants continued to show unabated interest in the possibility of obtaining an EMI or PI licence issued by the Bank of Lithuania. Within the framework of the Newcomer Programme, over 160 meetings with market participants interested in licensing opportunities in Lithuania were held in 2019. The majority (66%) of programme participants expressed their interest in EMI and PI licences. In 2019, the Bank of Lithuania received 71 new applications for an EMI or PI licence. Having completed examination of the applications received in 2018 and part of those received in 2019, 27 EMI and PI licences were issued in the course of 2019. Examination of a considerable share of applications was not started or was terminated later due to the established deficiencies, while the remaining applications will be further examined in 2020. The Bank of Lithuania is usually examining 40–50 applications for an EMI or PI licence at a time, although this number is constantly varying. Lithuania takes the leading position in continental Europe in terms of the number of licensed EMIs and PIs.

Chart 1. EMI and PI performance indicators



Source: Bank of Lithuania.

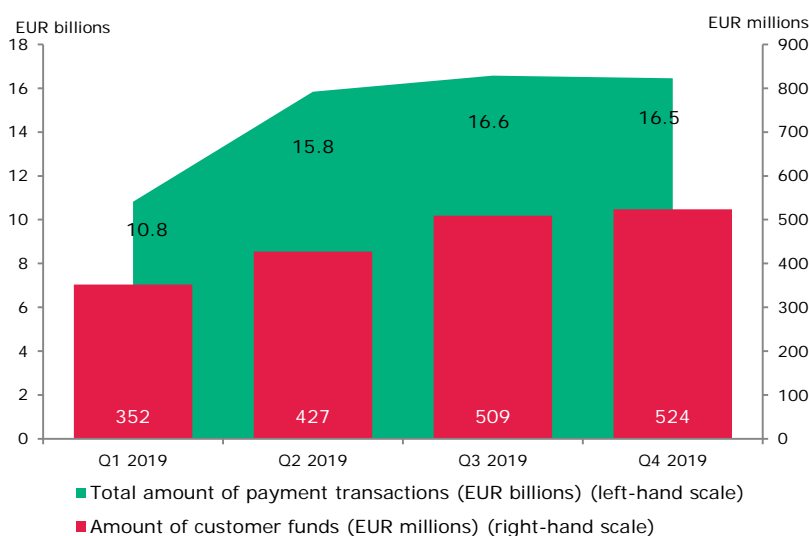
Corporate income from licensed activities (according to audited data) increased 1.6 times over the year, the amount of EMI and PI customer funds grew 1.7 times, while payment transactions performed by EMIs and PIs amounted to €16.5 billion. According to the audited (where audit is

mandatory) annual financial statements approved by the general meeting of shareholders, in 2019 EMIs and PIs earned €66.1 million from electronic money issuance and provision of payment services. Compared to 2018, their profit increased 1.6 times. Given the rapidly increasing number of new market participants, EMIs earned 66% of the sector's total income from licensed activities (PIs – 34%).

During the reporting period, taking into account the financial performance only of EMIs and PIs which were mainly engaged in the provision of licensed services, the sector – even though 54 EMIs and PIs incurred losses – earned €3.6 million in profits, and the corporate income tax due amounted to €2.7 million. It should be noted that the EMI/PI market is still in its early development stage; thus the break-even point is usually reached in the third year of operation. The average number of employees at these institutions was 605, with 545 positions occupied in Lithuania.

In Q4 2019, the total amount of payment transactions performed over the last 12 months stabilised and stood at €16.5 billion (see Chart 2). It is likely to increase once results for the first half of 2020 are available, given more active use of various alternative means of payment instead of cash in Q2 2020, as the result of the coronavirus (COVID-19) outbreak. The amount of EMI and PI customer funds held with central banks, Lithuanian and EU credit institutions and/or invested in safe, liquid and low-risk assets grew at a moderate quarterly pace of 2.9% (compared to 2018, it increased 1.73 times). On 31 December 2019, average outstanding electronic money¹ amounted to €379.7 million, a year-on-year increase of €156.8 million, or 1.7 times.

Chart 2. Amount of payment transactions performed by EMIs/PIs and amount of EMI/PI customer funds

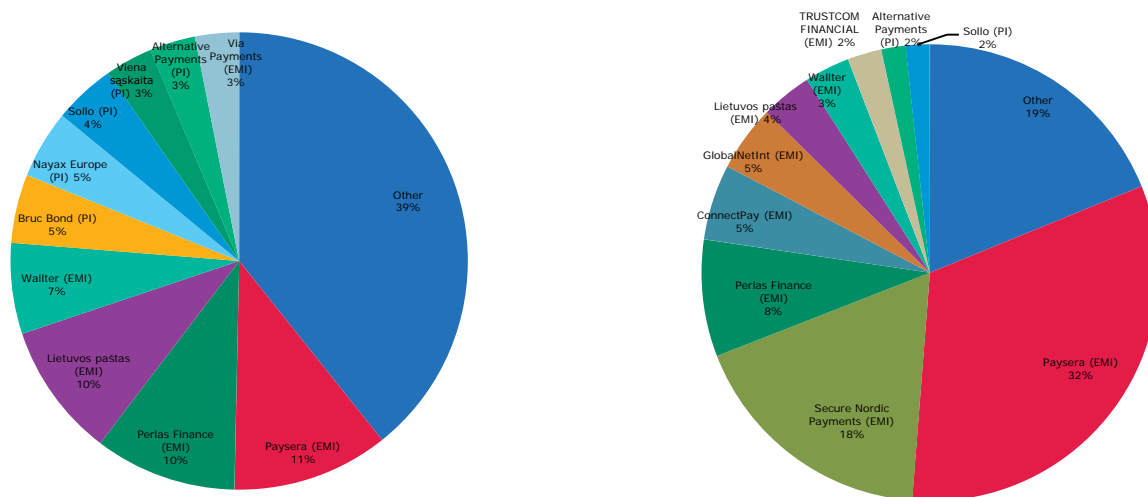


Source: Bank of Lithuania.

In 2019, in terms of income generated through electronic money issuance and provision of payment services, the share of income earned by the three major market participants shrank, thus reflecting the expanding EMI/PI market. Having earned almost half of the sector's income in 2018, the three major market participants accounted for only 31% of total income generated by the market in 2019, while income from licensed activities earned by the ten largest EMIs and PIs declined from 75% to 61% of the total sector's income – a year-on-year decrease of 14 percentage points (see Chart 3).

¹ Average outstanding electronic money is calculated as the average of the total amount of an EMI's financial liabilities related to electronic money issued at the end of each day during the last six months.

Chart 3. Largest EMIs and PIs by income from licensed activities and amount of payment transactions

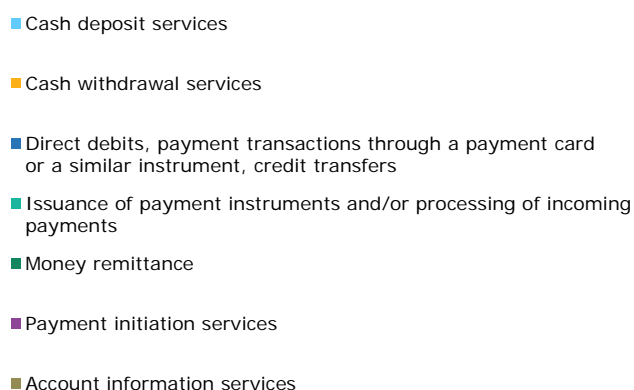


Source: Bank of Lithuania.

In terms of the total amount of payment transactions performed over the last 12 months, almost one third of the market was held by Paysera LT, followed by Secure Nordic Payments, UAB, and UAB Perlas Finance. Payment transactions performed by these three EMIs accounted for 58% of the total amount of payment transactions.

The activities of institutions were focused on payment account services as well as issuance of payment instruments (e.g. payment cards) and processing of incoming payments. As at 31 December 2019, the major share (42%) of payment services consisted of direct debits, payment transactions through a payment card or a similar instrument and credit transfers, as shown by reports on services that have for the first time been submitted by EMIs and PIs to the Bank of Lithuania. Issuance of payment instruments and processing of incoming payments also accounted for a sizeable share (34%) (see Chart 4). The latter services as well as services enabling cash to be placed on or withdrawn from a payment account were predominant among EMIs. PIs were mostly engaged in money remittance and payment processing services. Payment initiation and account information services were launched only in recent years following the entry into force of [Directive \(EU\) 2015/2366 of the European Parliament and of the Council on payment services in the internal market](#) (PSD2); therefore, their number was still relatively low at the end of last year.

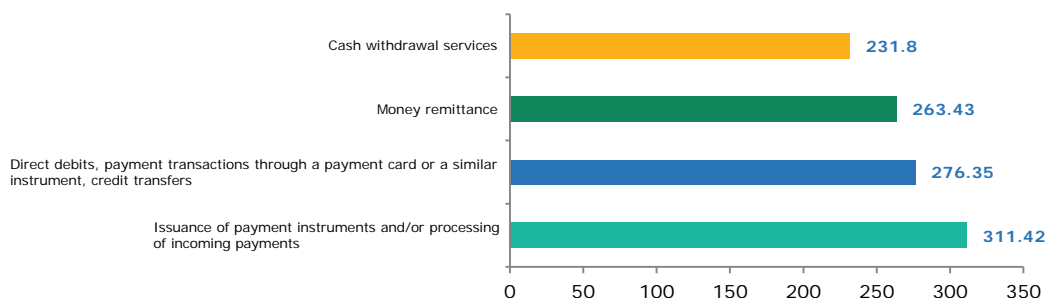
Chart 4. Breakdown of payment services



Source: Bank of Lithuania.

Commencement of licensed services takes up to 9 months. According to the reports on services, the average time for EMIs and PIs to start the provision of licensed activities is 8 months and 24 days (268.68 days). Launching payment initiation, account information and cash deposit services took the shortest time, as institutions were ready to provide these services as soon as they were licensed, while the process of starting issuing payment instruments and processing incoming payments was the most time consuming and took, on average, 10 months and 7 days (311.42 days) (see Chart 5). It also took more than 7 months on average for institutions to start providing other payment services.

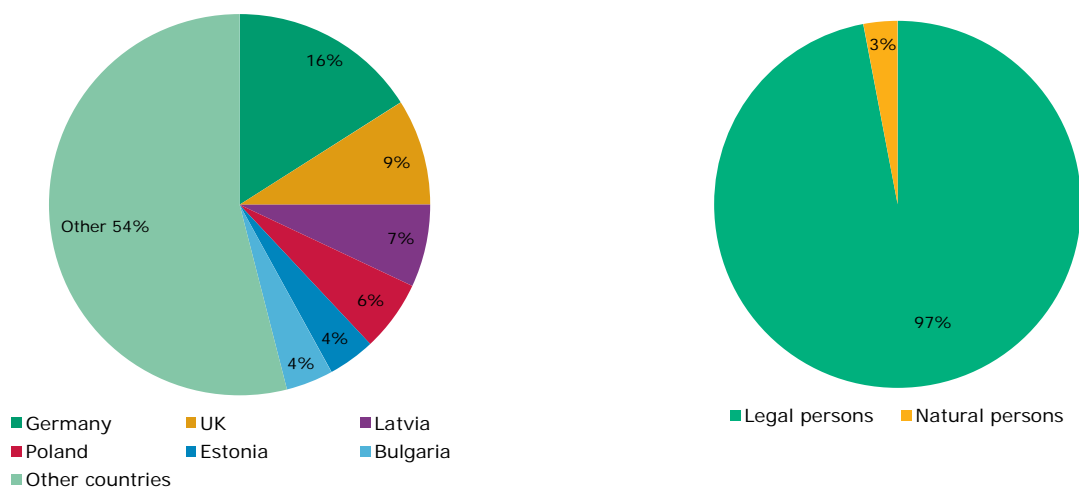
Chart 5. Average number of days before commencing licensed activities by payment services



Source: Bank of Lithuania.

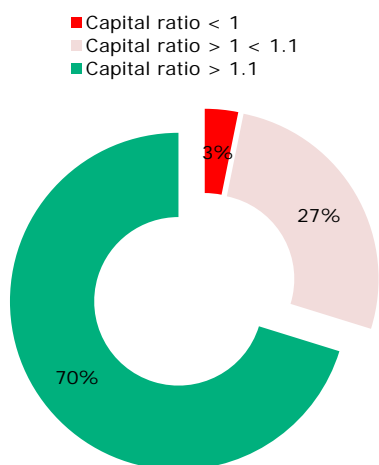
The highest payment transaction turnovers of EMIs and PIs were generated by payments made by legal persons, with payments from/to the EU being most prevalent in terms of the value of payment transactions. Reports for supervision of the implementation of anti-money laundering and/or counter terrorist financing (AML/CTF) measures submitted by EMIs and PIs by 31 December 2019 show that, in terms of the value of payment transactions, the majority of payment transactions were carried out between EU Member States, with Germany ranking first (16% of payment transactions). In the EMI/PI sector, payment transactions made by customers (legal persons) accounted for the largest share of payment transaction turnover (97%) (see Chart 6).

Chart 6. Value of payment transactions by country and customer type



Compliance with prudential requirements. On the reference date, all EMIs and/or PIs holding a licence for restricted activity complied with their prudential requirements (the requirement for the average outstanding electronic money and/or for the average amount of payment transactions). On 31 December 2019, the own capital ratio of licensed EMIs and PIs, which is calculated as the ratio of own funds to the calculated own funds requirement and must be at least 1, was exceeded by 70% of EMIs and PIs, amounting to 1.1 (see Chart 7). However, one EMI and two PIs had to take measures to ensure that their calculated own funds meet the own funds requirement. Therefore, these institutions met their own funds requirement after the reference date, having increased their authorised and/or reserve capital or covered losses. Information on the key annual and quarterly performance indicators of each [EMI](#) and [PI](#) as well as on their compliance with prudential requirements is available on the Bank of Lithuania website.

Chart 7. EMI and PI capital ratio



Source: Bank of Lithuania.

Supervision of the EMI/PI sector. In terms of supervision of the EMI/PI market, the Bank of Lithuania uses a risk-based supervision model – therefore, taking into account the risks posed by certain EMIs and PIs, some of them may attract closer supervisory attention than others. The Bank of Lithuania is currently

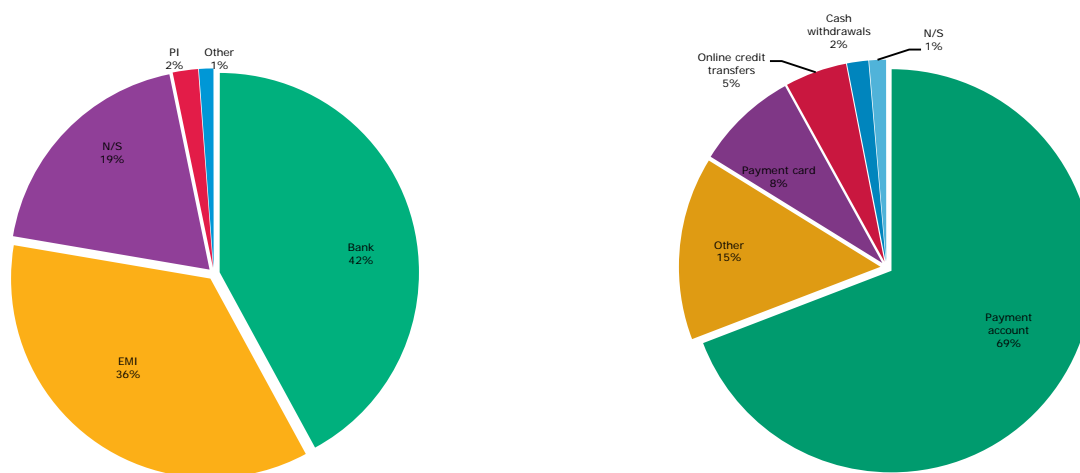
improving the model for assessing the risk level of EMIs and PIs, which will enable assigning EMIs and PIs to risk groups according to various aspects, including AML/CTF, financial (customer fund protection, solvency, sustainability) and other indicators. Moreover, in order to reduce the administrative burden on EMIs and PIs involved in reporting for supervisory purposes, the Bank of Lithuania is looking for an innovative solution that would allow obtaining the necessary data from EMIs and PIs and automatically generating respective reports. To this end, the Bank of Lithuania joined the GovTech² Lab in 2019. As part of the GovTech Lab, the Bank of Lithuania proposed to develop a RegTech solution, which would streamline reporting procedures, thus allowing financial market participant to submit reports to the Bank of Lithuania in a more efficient manner. The Bank of Lithuania continues its work on this solution in 2020.

In 2019, within its supervisory mandate, the Bank of Lithuania mainly focused on compliance with AML, own capital and customer fund protection requirements, as well as examined whether EMIs and PIs provide services only within the scope of their licences. Since the beginning of 2019, the Bank of Lithuania conducted inspections of five EMIs and PIs (checks on AML/CTF risks), an analysis of AML/CTF risk management controls provided in documents of five EMIs and PIs, an analysis of adequate separation and protection of customer funds of 13 EMIs and PIs, and one investigation regarding delays in payment transactions. Three new analyses of adequate separation and protection of customer funds as well as two analyses of the scope of the services provided were started in 2020. Moreover, the Bank of Lithuania conducted an analysis of over 20 EMIs and PIs that have failed to commence their licensed activities. Since the beginning of 2019, due to irregularities detected in these areas, the Bank of Lithuania revoked two PI (for AML/CTF violations, activities beyond the scope of their licence, improper implementation of customer fund protection requirements) and one EMI (for breaches of own capital requirements, failure to commence licenced activities) licences, imposed 11 fines (for AML/CTF violations, breaches of customer fund protection requirements and delays in payment transactions) totalling €538.6 thousand, two activity restrictions (for AML/CTF violations, internal control failures, late submission of supervisory reports), as well as issued one warning and three public notices on breaches of legislation due to failure to comply with own capital requirements. The Bank of Lithuania's supervisory priorities for 2020 remain the same.

Protection of consumer rights. In 2019, 587 complaints (comprising more than one third, or 35.7%, of all complaints) received by the Bank of Lithuania concerned payment services provided by credit institutions and other payment service providers. 38% of all complaints were related to services provided by EMIs and PIs (see Chart 8). In most cases (69% of all complaints regarding payment services), payment service users complained about payment accounts opened on their behalf with credit institutions and other payment service providers, which are used for the execution of payment transactions. These complaints were mainly related to the application of AML/CTF requirements (blocked payment accounts, requests to provide certain KYC information, restricted access to funds in the payment account, non-communication with the customer, unilateral termination of contracts with legal persons holding payment accounts or refusal to open a payment account). Some complaints were related to fees applied for payment services.

² GovTech is a technology infrastructure aimed at strengthening the public sector and improving public services.

Chart 8. Complaints by payment service providers and payment services



Source: Bank of Lithuania.

Regulatory changes. A number of [amendments](#) to the Republic of Lithuania Law on Payments (hereinafter – the Law) entered into force in 2019: amendment to Article 3(5)(16), requiring payment service providers to ensure that consumers can make payments at least via payment cards (or other means, if cards are not issued), where the account is restricted but a certain amount of funds is secured for the customer to be freely disposed of in accordance with the procedure laid down by legislation; provisions of Article 58 concerning the application of more secure authentication procedures; and the requirement to provide payment initiation and account information services via dedicated application programming interfaces (API).

[Regulation \(EU\) 2019/518](#) amending Regulation (EC) No 924/2009 as regards certain charges on cross-border payments in the Union and currency conversion charges entered into force on 15 December 2019, while some of its provisions setting out new obligations relating to the disclosure of information on the applied currency exchange mark-up to the payer who is offered a currency conversion service became (will become) applicable from 2020 and 2021 respectively.

Commission Delegated [Regulation \(EU\) 2018/389](#) with regard to regulatory technical standards for strong customer authentication and common and secure open standards of communication became effective on 14 September 2019. At the end of 2019, the European Commission prepared an information document on consumer rights, as provided for in Article 106(1) of the Second Payment Services Directive (PSD2) and Article 28 of the Law. It can be found on the European Commission [website](#) and must be made available on the websites of all payment service providers.

[Resolution No 03-10](#) of the Board of the Bank of Lithuania on the approval of the rules regarding operational or security incident reporting to the Bank of Lithuania and of notification templates came into force on 1 April 2019. It approved the procedure for providing information specified in the Resolution to the Bank of Lithuania and the procedure for submitting REJECT, BLOCK and FRAUD reports and notifications, respectively implementing the requirements of Articles 10, 33 and 38 of the Law.

On the basis of [Resolution No 03-165](#) of the Board of the Bank of Lithuania on fraudulent payments statistical reporting, implementing the provisions of Article 56(6) of the Law, statistical reporting on payment fraud was launched in 2019.

By [Resolution No 03-90](#) of 25 April 2019, the Bank of Lithuania approved the assessment criteria for dedicated APIs and the questionnaire used where an account servicing payment service provider applies to the Bank of Lithuania for the authorisation referred to in Article 33(6) of Regulation (EU) 2018/389 (the exemption from the obligation to set up the contingency mechanism).

Pursuant to [Resolution No 03-66](#) of the Board of the Bank of Lithuania on the approval of the rules for establishing and managing the list of the most representative services linked to a payment account and of the requirements for the fee information document and the statement of fees, implementing Article 62 of the Law, as of 2019, payment service providers must provide their customers with statements of fees paid on the payment account by the customer to the payment service provider during the previous calendar year.

In 2020, the Bank of Lithuania prepared [draft amendments](#) to legal acts of the Bank of Lithuania and submitted them for EMIs' and PIs' consideration: regulations for the calculation of initial capital and own funds, the procedure detailing the preparation of supervisory reports and the provision of information to the Bank of Lithuania, as well as requirements on internal control, risk management and customer funds protection. These drafts will be adopted in 2020. Information on EMI and PI reports as well as the reporting calendar are available [here](#).

In 2019, the Bank of Lithuania prepared several [positions and guidelines](#) with respect to the EMI/PI sector. On 25 March 2019, the Bank of Lithuania took a decision to comply with the provisions of the Guidelines of the European Banking Authority on the Conditions to Benefit from an Exemption from the Contingency Mechanism under Article 33(6) of Regulation (EU) 2018/389 (RTS on SCA & CSC); on 7 October 2019, the Guidelines for Advertising Financial Services and Guidelines on Security Token Offering were drawn up; on 25 May 2020, the Bank of Lithuania prepared its position on the right of EMIs and PIs to access bank accounts opened with credit institutions, identifying types of bank accounts to be opened for EMIs and PIs and aimed at improving possibilities for EMIs and PIs to open bank accounts for holding customer funds.