

# Changes ahead for electronic payment instruments in Japan

Yasuyuki Kuribayashi and Takashi Saito of City-Yuwa Partners explore the new regulations concerning electronic payment instruments in Japan

Currently, there are payment methods by credit card, prepaid payment instruments, and digital money, etc. as electronic payment instruments used for daily payment for goods and services.

Under Japanese laws, business operators who provide these electronic payment services are regulated by the Installment Sales Act or the Payment Services Act (PSA) both of which stipulate the necessary licenses (i.e. registration or notification) and various regulations on the conduct of such business operators depending on the business or the contents of the services provided.

The Act on Prevention of Transfer of Criminal Proceeds (APTCP) is the law that lays out AML/CFT regulations in Japan and imposes on financial institutions, etc. obligations, among others, to verify the identity of customers upon conducting certain transactions and report suspicious transactions to authorities.

Under the current APTCP, credit card companies and funds transfer service providers are regulated by the APTCP, however, issuers of prepaid payment instruments are not regulated by it as refund to the users is prohibited in principle with regard to prepaid payment instruments and therefore the risks of money laundering can be considered to be low.

## Background of the amendment

In Japan, considering the recent developments of digitisation of financial services and sophistication of method of money laundering, etc. the Financial System Council's working group on payment system discussed toward amendment to the PSA, etc. from a viewpoint of handling the digitisation of finance and implementation of the necessary regulations since October 2021.

With regard to the transactions by using stablecoins that have been rapidly increasing, in particular in the US, the



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Financial Action Task Force (FATF) has pointed out that the risks of money laundering is high.

As for prepaid payment instruments, issuers of prepaid payment instruments are currently not regulated by the APTCP as stated above, however, recently, prepaid payment instruments that can be transferred electronically have appeared and provided as new financial services, and consequently

these new type of prepaid payment instruments increase the risk of money laundering.

On the other hand, it is also possible that stablecoins are used as a remittance and payment method in various areas in future, and prepaid payment instruments have already been used as one of the convenient payment services and have contributed towards the development of a cashless system.

## Enactment and promulgation

On March 4 2022, the series of amendment bills, including the amendments to the PSA, the Banking Act and the APTCP, were submitted by the Financials Services Agency to the National Diet of Japan with the aim of the government handling the risk of money laundering appropriately, accelerating the business effort toward financial innovation and establishing a stable and efficient payment system.

After the discussion in the National Diet, the amendments to the PSA, the Banking Act and the APTCP, etc. (the amendments) were enacted on June 3 2022 and promulgated on June 10 2022.

## Major new regulations

Under the amendments, among others, 'electronic payment instruments' corresponding to stablecoins are newly defined and regulations on issuers of stablecoins and intermediaries of transactions regarding stablecoins are newly implemented.

In addition, the regulations for issuers of prepaid payment instruments the charge amount of which can be high and can be transferred electronically (the 'electronically transferable large sum type prepaid payment instruments') are strengthened by imposing the regulations under the APTCP, etc. since the risk of money laundering is particularly high in the transactions by using this type of prepaid payment instrument.

## New regulations on stablecoins

### Definition

Under the amendment to the PSA, among others, 'electronic payment instruments' corresponding to stablecoins are newly defined as follows (Article 2, paragraph 5 of the amended PSA):

1. Property value (limited to currency-denominated assets which is recorded on an electronic device or any other object by electronic means, and excluding securities, electronically recorded monetary claims, prepaid payment instruments and any other items specified by the Cabinet Office Order as similar thereto (excluding items specified by the Cabinet Office Order taking into consideration a degree of distribution and any other circumstances)) which can be used in relation to unspecified persons for the purpose of paying consideration for the purchase or leasing of goods, etc.

## *“On March 4 2022, amendment bills were submitted to the National Diet of Japan”*

or the receipt of provision of services and can also be purchased from and sold to unspecified persons acting as counterparties, and which can be transferred by means of an electronic data processing system;

2. Property value which can be mutually exchanged with what is set forth in 1. above with unspecified persons acting as counterparties, and which can be transferred by means of an electronic data processing system;
3. ‘specified trust beneficiary interests’;
4. Any other items specified by the Cabinet Office Order as similar to 1. to 3. above.

The definition of the electronic payment instruments is similar to the cryptoassets definition under the PSA, however, they are different on the point that the electronic payment instruments are required to be currency-denominated assets. The more detailed contents of the electronic payment instruments will be stipulated in the Cabinet Office Order to be amended going forward.

### **Outline of new regulations**

#### *Issuers of the electronic payment instruments*

As issuance and redemption of the electronic payment instruments fall under the category of exchange transactions under Japanese law, only a bank and a funds transfer service provider are allowed to issue

the electronic payment instruments in principle.

Definition of ‘electronic payment instrument, etc. business’

The amended PSA newly defines the electronic payment instrument, etc. business as intermediary business between an issuer of electronic payment instruments and users thereof (Article 2, paragraph 10 of the amended PSA) and imposes regulations on a business operator thereof. The following acts fall under the definition of ‘electronic payment instrument, etc. business’:

1. Purchase and sale of an electronic payment instrument or exchange with another electronic payment instrument;
2. Intermediary, brokerage or agency services for the act shown in 1. above;
3. Management of electronic payment instruments on behalf of another person (excluding the cases specified by the Cabinet Office Order as being less likely to weaken the protection of users); and
4. Entering into a contract with an user (limited to an user who made a contract with the funds transfer service provider the content of which is conducting exchange transactions continuously or repeatedly) to conduct either of the following matters by means of an electronic data processing system on entrustment from the funds transfer service provider and on behalf of the funds transfer service provider, and

increase or decrease the amount of claims corresponding to obligations under exchange transactions based on the agreement:

- a) Having funds transferred based on the agreement and decreasing the amount of claims corresponding to obligations under exchange transactions to the extent equivalent to the amount of the funds; or
- b) Increasing the amount of claims corresponding to obligations under exchange transactions to the extent equivalent to the amount of the funds received under the exchange transactions.

A business operator who intends to conduct the ‘electronic payment instrument, etc. business’ must be registered as the ‘electronic payment instrument, etc. business operator’ in advance (Article 62-3 of the amended PSA). The main grounds for refusal of the registration are as follows:

1. The business operator is not a Japanese stock company or a foreign company with a business office in Japan and it conducts an ‘electronic payment instrument, etc. business’ in a foreign country with an equivalent registration from the authority of the foreign country (i.e. it is a ‘foreign electronic payment instrument, etc. business operator’);
2. The ‘foreign electronic payment instrument, etc. business operator’ does

## “Under the amendments, ‘electronic payment instruments’ corresponding to stablecoins are newly defined”

- not appoint a representative in Japan (who has an address in Japan);
3. The business operator does not have the sufficient financial foundation that is necessary for the provision of the ‘electronic payment instrument, etc. business’ in a proper and steady manner;
  4. The business operator has not established or maintained an internal structure that ensures the proper and steady performance of the ‘electronic payment instrument, etc. business’ and the compliance with the PSA.

### *New regulations on the ‘electronic payment instrument, etc. business operator’*

The PSA also imposes various restrictions on the ‘electronic payment instrument, etc. business operator’. The main restrictions include five aspects.

First is the obligation to take necessary measures for security management over the information relating to the ‘electronic payment instrument, etc. business’.

Second is the obligation to take necessary measures to protect users and ensure the proper and steady performance of the ‘electronic payment instrument, etc. Business’, which includes providing users with information relating to the contents of

contracts concerning the ‘electronic payment instrument, etc. business’.

Third is the obligation not to receive deposits of money or any other assets from a user in relation to the ‘electronic payment instrument, etc. business’ in principle.

Fourth is the obligation to segregate users’ electronic payment instruments from the ‘electronic payment instrument, etc. business operator’s’ own electronic payment instruments and to conduct periodic audits on the status of the segregated management by a certified public accountant or audit corporation.

Lastly, there is the obligation to enter into an agreement concerning the ‘electronic payment instrument, etc. business’ with the issuer of the electronic payment instruments, etc. that stipulates the sharing between the issuer of the electronic payment instruments, etc. and the ‘electronic payment instrument, etc. business operator’ of the liability to compensate users for any loss or damage sustained thereby and conduct the ‘electronic payment instrument, etc. business’ in relation to the issuer based on the agreement.

### *Definition of ‘electronic payment, etc. dealing business’*

Keeping digital money type stablecoins issued by a bank in mind, the amended PSA

newly defines the ‘electronic payment, etc. dealing business’ (Article 2, paragraph 17 of the amended Banking Act) and imposes regulations on a business operator thereof. The following acts fall under the definition of ‘electronic payment, etc. dealing business’:

1. Entering into a contract with a depositor that has opened an account for deposits with a bank to conduct either of the following matters by means of an electronic data processing system on entrustment from the bank and on behalf of the bank, and increase or decrease the amount of claims under the deposit agreement based on the agreement:
  - a) Having funds in the account transferred and decreasing the amount of the deposit claims to the extent equivalent to the amount of the funds; or
  - b) Increasing the amount of the deposit claims to the extent equivalent to the amount of the funds received under the exchange transactions.
2. Intermediary services for entering into contracts that concern the acceptance of deposits on behalf of the bank shown in 1. above in relation to the act shown in 1. above.
 

A business operator who intends to conduct ‘electronic payment, etc. dealing

business' must be registered as the Electronic Payment, etc. Dealing Business Operator in advance (Article 52-60-3 of the amended Banking Act). The main grounds for refusal of the registration are as follows:

1. The business operator is not a Japanese stock company or a foreign company with a business office in Japan and it conducts an electronic payment, etc. dealing business in a foreign country with an equivalent registration from the authority of the foreign country (i.e. it is a 'foreign electronic payment, etc. dealing business operator');
2. The 'foreign electronic payment, etc. dealing business operator' does not appoint a representative in Japan (who has an address in Japan);
3. The business operator does not have the sufficient financial foundation that is necessary for the provision of the electronic payment, etc. dealing business in a proper and steady manner;
4. The business operator has not established or maintained an internal structure that ensures the proper and steady performance of the 'electronic payment, etc. dealing business'.

### **New regulations on electronic payment, etc. dealing business operator**

The PSA also imposes various restrictions on the 'electronic payment, etc. dealing business operator'. The main restrictions include four aspects.

First is the obligation to make a necessary explanation to customers concerning the Electronic Payment, etc. Dealing Business, take necessary measures for security management over the information of customers, and take necessary measures to ensure the appropriate performance and sound and proper management of the Electronic Payment, etc. Dealing Business.

Second is the obligation to perform its services for its customers in good faith.

Third is the obligation not to receive deposits of money or any other assets from a customer in relation to the electronic payment, etc. dealing business in principle.

Lastly, there is the obligation to enter into an agreement concerning the electronic payment, etc. Dealing Business with the bank that stipulates the sharing between the bank and the electronic payment, etc. dealing business operator of the liability to compensate customers for any loss or

damage sustained thereby and conduct the electronic payment, etc. dealing business in relation to the bank based on the agreement.

### **Regulations under the APTCP**

Under the amended APTCP, regulations thereunder (i.e. obligations to verify the identity of customers upon conducting certain transactions and report suspicious transactions to authorities, etc.) are also applicable to and imposed on the electronic payment instrument, etc. business operator and the electronic payment, etc. dealing business operator.

### **Electronically transferable large sum type prepaid payment instruments**

#### **Definitions**

Under the amended PSA, regulations only on issuers of prepaid payment instruments the charge amount of which can be high and that can be transferred electronically (the 'electronically transferable large sum type prepaid payment instruments') in which the risks of money laundering are particularly high are strengthened.

Under the amended PSA, the electronically transferable large sum type prepaid payment instruments are defined as third party type prepaid payment instruments (limited to those the amount of unused balance of which are recorded in record account for prepaid payment instruments) that can be transferred by means of an electronic data processing system (limited to those on which the amount of transferable unused balance per transfer or the aggregate amount of transferable unused balance during a specific period is high and that satisfy any other requirements specified by the Cabinet Office Order as those that are likely to weaken the protection of users of prepaid payment instruments or hinder the sound and proper management of the business concerning issuing prepaid payment instruments) and any others specified by the Cabinet Office Order as similar thereto (Article 3, paragraph 8 of the amended PSA).

In addition, under the amended PSA, record account for prepaid payment instruments is defined as the account that the issuer of the prepaid payment instruments itself records the contents of the prepaid payment instruments as for each of the prepaid payment instruments (limited to

those which the maximum amount of unused balance to be recorded in the account exceeds the amount specified by the Cabinet Office Order as high amount and that satisfy any other requirements specified by the Cabinet Office Order) (Article 3, Paragraph 9 of the amended PSA). It can be expected that a 'wallet' falls under the definition of record account for prepaid payment instruments.

The contents of the electronically transferable large sum type prepaid payment instruments in more detail, including the amount of threshold, are going to be stipulated in the Cabinet Office Order to be amended from now on.

### **Outline of new regulations**

#### **Notification of business implementation plan**

When a service provider intends to issue electronically transferable large sum type prepaid payment instruments, the service provider must file a business implementation plan with the prime minister in advance (Article 11-2, paragraph 1 of the amended PSA).

In the business implementation plan, the service provider is required to state (i) if the service provider sets the maximum amount of unused balance to be recorded in the record account for prepaid payment instruments, that maximum amount; (ii) the method of the management of an electronic data processing system to be used for its business; and (iii) other particulars specified by the Cabinet Office Order to be amended from now on.

#### **Regulations under the APTCP**

Under the amended APTCP, regulations thereunder (i.e. obligations to verify the identity of customers upon conducting certain transactions and report suspicious transactions to authorities, etc.) are also applicable to and imposed on the issuer of the electronically transferable large sum type prepaid payment instruments.

### **Looking ahead**

The relevant Cabinet Office Order is going to be amended from now on, and the amendments together with the amended Cabinet Office Order are scheduled to come into force within one year after the promulgation date of the amendments (i.e. first half of 2023 at the earliest).