

# New regulations on fund transfer business in Japan

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ON JUNE 24, 2009, THE PAYMENT SERVICES ACT OF JAPAN (ACT NO. 59 OF 2009; THE PSA) WAS PROMULGATED. THE PSA WILL COME INTO EFFECT NO LATER THAN JUNE 23, 2010; AT WHICH POINT, THE REGULATORY FRAMEWORK FOR THE FUND TRANSFER BUSINESS IN JAPAN WILL CHANGE DRASTICALLY. THIS CHAPTER OUTLINES SOME OF THE FUNDAMENTAL ASPECTS OF THE NEW REGULATIONS, DISCUSSES CERTAIN DEFERRED ISSUES WITH RESPECT TO SUCH REGULATIONS AND PRESENTS OTHER SUBSTANTIAL REGULATORY CHANGES WHICH WILL BE INTRODUCED BY THE PSA.

## Background of the new regulations

Only banks licensed under the Banking Act of Japan (Act No. 59 of 1981, as amended) and certain other financial institutions handling deposits licensed under other applicable laws (collectively, the Banks) are permitted to engage in 'money remittance transactions'. According to a Supreme Court precedent (decision of the Third Petty Bench of the Supreme Court of Japan on March 12, 2001), engaging in 'money remittance transactions' means "to undertake the task of transferring funds requested by customers utilising the systems of fund transfer without transporting cash between distant parties, and/or to carry out such task". As standard fund transfer services fall under the definition of 'money remittance transactions', aside from Banks, no persons/entities are permitted to conduct fund transfer business in Japan.

However, due to the innovation of information-communication technology, persons/entities other than Banks can easily conduct services that are similar to the traditional fund transfer business conducted by Banks. This, therefore, means that the line between permitted and

prohibited services is blurred and it has been argued that, by considering customer protection, it is necessary to sort this issue out and set new regulations on fund transfer services by permitting certain entities other than the Banks to engage in the business of such services.



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## Outline of the new regulations

The PSA will allow companies that are not licensed Banks to engage in the business of ‘money remittance transactions’ in Japan provided that: (i) they are registered as ‘fund transfer business operators’ (operators); and (ii) they are able to engage in services to the extent that such transactions fall under the category of a ‘certain small amount of transactions’. Details of the ‘certain small amount’ mentioned in (ii) above will be provided for in the cabinet order. However, in light of discussions at the National Diet of Japan, such amount is expected to be between JPY500,000 and JPY1,000,000 or less.

An entity which intends to be an operator will be subject to a registration requirement and certain regulations including the security of its assets and other customer protection measures, supervision and measures against money laundering. In order to avoid over-regulation and enhance convenience to users, the PSA and related laws and regulations intend to set out the minimum regulations to ensure customer protection and the sound development of fund transfer business; therefore, certain regulations that are imposed on the Banks will not be imposed on operators.

Further details of such are as follows:

### Registration requirements

In order to be registered as an operator under the PSA, an applicant must satisfy certain requirements, such as the applicant must be a stock company (*kabushiki kaisha*) or a foreign entity which has the equivalent registration in its home country and has an office(s) and representative in Japan; the applicant must have sufficient financial standing to conduct business appropriately and properly; the applicant must have a satisfactory organisational structure to conduct business appropriately and properly; and the applicant must have a compliance system to ensure observance with the relevant laws and regulations.

With regard to the above, details of the meanings of ‘sufficient financial standing’, ‘satisfactory organisational structure’ and ‘compliance system’ are expected to be clarified in the cabinet office ordinances or guidelines which will be published in the future.

Although, generally speaking, banks are not permitted to engage in other business or own more than 5% voting rights in an ordinary company under the Banking Act, such restrictions will not be placed on operators.

The PSA also clarified that a foreign entity is generally prohibited from soliciting money remittance transactions in Japan without registration as described previously.

### Security of assets

The PSA will impose an obligation on an operator to secure the assets in amounts equal to or more than the total amount of: (i) funds which an operator is transmitting; and (ii) procedural costs in relation to reimbursement of such funds as set out in (i), so that the transferred funds can reach the recipient even in the event of an operator’s insolvency. Such total amount must be at least the prescribed minimum amount (as provided in the cabinet order), in order to ensure the security of its assets. Details of the methods for calculating (i) and (ii) will be clarified in the cabinet office ordinances.

The PSA provides for three methods to secure the assets, that is, deposit of such at a deposit office; the conclusion of a guarantee agreement with certain financial institutions such as banks (subject to filing a notification with the relevant authority); and the placing of such on trust (subject to the approval of the relevant authority).

In the event of an operator’s insolvency, users have rights to recover their assets from the above secured assets in priority to an operator’s general creditors, pursuant to the procedures provided in the PSA.

### Other regulations for an operator’s customer protection

In the PSA, there are certain regulations relating to an operator’s customer protection other than the asset security obligation described above.

An operator will be required to take certain measures for the safe management of information relating to its fund transfer business (such as measures to prevent the divulgence of such information). Also, where an operator delegates its fund transfer business to a third party, it will be required to take certain measures to ensure the

adequate performance of such business (such as the supervision of delegates). In addition, an operator will be required to provide its customers with explanations so that they do not falsely believe that the operator is a Bank and will also be required to inform its customers of the details of the fund transfer agreement.

Details of those regulations will be provided for in the cabinet office ordinances.

### Supervision

The PSA provides certain supervisory functions of the relevant authority in relation to an operator's business, including an obligation to maintain records and book keep; an obligation to prepare and file an annual report on its fund transfer business and other periodical reports on the

security of its assets; an on-site inspection; a business improvement order; cancellation of registration; and a business suspension order.

In addition, if a self-censorship organisation is established under the PSA, the organisation shall implement rules which its members shall abide by. An operator may be required or expected to become a member of such organisation.

### Measures against money laundering

Akin to the Banks, an operator must verify the identity of a customer when it conducts business with such customer. It also has an obligation to file a suspicious activity report in certain situations, pursuant to the Act on Protection of Transfer of Criminal Proceeds (Act No. 22 of 2007, as

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amended) and/or the Foreign Exchange and Foreign Trade Act (Act No. 228 of 1949, as amended).

## Deferred issues

Aside from the fund transfer services, it has been argued that certain other services may theoretically fall under the definition of ‘money remittance transactions’, those are fee collection services and cash-on-delivery services.

Fee collection services means services where agents (e.g., convenience stores) collect cash over-the-counter on behalf of the providers of goods and services (e.g., collection of fees for public utilities). Cash-on-delivery services means services where delivery agents (e.g., home delivery companies) deliver goods or services to customers for payment of the price of such goods or services.

Both fee collection services and cash-on-delivery services have been conducted without any specific regulations. However, there is an argument that some measures to protect customers’ funds should be taken to prepare for the insolvency of the providers as well as to prevent fraudulent acts by providers.

The Japanese government took into consideration the strong criticism that there has never been any material issue for these services in terms of consumer protection and that the regulation of these services may harm the convenience of customers. At the Diet, the Japanese government advised that the PSA is not intended to be applied to such services. However, the Japanese government has not expressed a clear view as to whether or not these services fall under the category of ‘money remittance transactions’.

## Other regulatory changes by the PSA

The PSA will also bring about certain regulatory changes to other related fields.

### Regulations on pre-paid payment instruments

Pre-payment services where certain values including electronic moneys are recorded on certificates (e.g., papers or cards with IC chips) are regulated; whereas services where the record management is conducted only on a computer server are not specifically regulated. As both services are pre-payment measures, this discrepancy has

been said to be problematic in relation to consumer protection. Once the PSA comes into effect, the PSA will regulate both services.

### Regulations on fund settlement of interbank payment systems

The PSA will also introduce new regulations regarding fund settlement of the Japanese interbank payment systems. Settlement of interbank payment is made through the payment system operated by a private incorporated body whose members are banks. To ensure the function of clearing through such system, the PSA defines an organisation operating such system as a ‘fund clearing organisation’ and requires such organisation to acquire a licence from the relevant authority.

## Conclusion

Although there is certain ambiguity on the law’s position over the fee collection services and cash-on-delivery services, the new regulations on the fund transfer business are a significant step toward expanding business opportunities for those relevant entities that are not Banks and enhancing the convenience of the users. Practitioners and market participants must pay close attention to the further developments of the new regulations by reviewing the forthcoming relevant cabinet order and the cabinet office ordinances and guidelines which will complete the outline of the regulations provided in the PSA.

#### Note:

As we finished writing this chapter on November 26, 2009, we have not been able to reflect the contents of the drafts of the relevant cabinet order and cabinet office ordinances (published on December 7, 2009) in this chapter.

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