

# **The Legal Nature of Electronic Money**

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*Three electronic purse projects are currently under consideration and could be introduced in France before the end of the year<sup>1</sup>. The three systems are based on the same principle: an issuer loads electronic units into the micro-chip of an electronic purse in exchange for a sum of money from the holder. Electronic purses use micro-chip card technologies in the same way as conventional payment cards, with the difference that electronic purse holders have previously paid for the units they spend. Examples already exist of so-called "single card" systems, such as the phone cards used in payphones or mobiles, in which prepaid cards are used to pay for goods or services provided by the card issuer. The future projects, however, are due to be rolled out nationwide in a diversified retailer network.*

*The term "electronic money" refers to the electronic units issued by the issuer and recorded in the electronic purse micro-chip. To make a payment using an electronic purse, holders transfer electronic units from their card to the seller's card. This transaction does not generate any debit/credit movement on the buyer's or seller's bank account<sup>2</sup>. Electronic units are converted into currency units at a later stage and the funds are transferred to the seller's account by bank transfer. Purseholders' accounts are debited when they buy the electronic units, if the transaction is carried out using bank money.*

*The electronic purse is the device which incorporates the electronic money and allows it to circulate. The purpose of this study is not to define what an electronic purse is, as a medium for "electronic money", but to attempt to define the legal nature of electronic money.*

*"Electronic money" is in fact a genuine "payment system", comprising an issuer, purseholders/consumers, and a network of merchants. There can be no doubt that this system introduces a new means of payment, in the form of an electronic purse loaded with electronic units which can be used to transfer funds and fulfil a money obligation. However, describing an electronic purse as a means of payment is not sufficient in itself, bearing in mind that means of payment such as bank notes and coin, cashless payment media like cheques and payment cards, and even debt securities do not have a uniform status and are not governed by a uniform set of rules.*

*The choice of the term "electronic money" suggests that, because of similarities with fiduciary or bank money in the way it is used, this new*

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<sup>1</sup> "En France, trois porte-monnaie électroniques, trois technologies", *Technologies Bancaires Magazine* n° 72, January-February 1999.

<sup>2</sup> There will not actually be any real transfer of units but transfer of a coded message which will generate an increase in the number of units in the seller's micro-chip and a corresponding and equal reduction in the number of units in the buyer's micro-chip.

*means of payment displays the characteristics of a new legal form of money. Before determining whether this is indeed the case (Section 2), it is important to recapitulate the defining characteristics of money and the reasons why bank notes and bank money have been termed "money" (Section 1).*

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## I. MONEY AND MONETARY INSTRUMENTS

In order to meet the definition of money<sup>4</sup>, a means of payment must display all the characteristics of money (Section 1.1). In particular, it must be a monetary instrument (Section 1.2).

### 1.1. The Characteristics of Money

While some commentators predict the future disappearance of money following the introduction of new technologies<sup>5</sup>, legal experts point out that even now it is an unknown quantity in law: "Money is omnipresent in social relations, but entirely absent from legal theory"<sup>6</sup>. The few legal definitions that exist<sup>7</sup> define money mainly by its function as a unit of account or means of payment, without drawing a distinction between the different functions of money.

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<sup>3</sup> This study has been carried out as part of an on-going research programme into means of payment using new technologies under the direction of Prof. Thierry Bonneau.

<sup>4</sup> For the purposes of this study, money corresponds to the M1 monetary aggregate, which comprises banknotes, subsidiary coins and sight deposits issued and managed by credit institutions and the Treasury. Cf. Didier Bruneel, "La monnaie", *Banque*, ed. 1992.

<sup>5</sup> Richard W. Rahn, *The End of Money and the Struggle for Financial Privacy*, Seattle, Discovery Institute Press, 1999.

<sup>6</sup> Rémy Libchaber, *Recherche sur la monnaie en droit privé*, Bibliothèque de droit privé, Tome 225, Librairie générale de droit et de jurisprudence (LGDJ).

<sup>7</sup> "Un instrument légal de paiement, pouvant avoir, suivant les systèmes monétaires, une base métallique ou une base fiduciaire, le plus souvent par combinaison des deux [A legal payment instrument which, depending on the monetary system, may have a metal basis or a fiduciary basis or, most often, a combination of both]", Gérard Cornu, *Vocabulaire juridique*, Association Henri Capitant.

### 1.1.1. The three functions of money

According to one writer, "jurists approach money from the standpoint of the rights and obligations arising from its use, which leads them to define what is money and what is not"<sup>8</sup>. But as Jean Carbonnier<sup>9</sup> has pointed out, "money is a means of payment, but not every means of payment is money". Money therefore has other characteristics than that of extinguishing a claim to a sum of money.

Economists, on the other hand, are more interested in the monetary functions of money and its effects in the economy. This leads to the distinction between the unit of account, which can be used to measure the value of dissimilar goods; the means of payment, which can be used to acquire any good; and the store of value, which is an asset that can be kept while remaining perfectly liquid, meaning that it can be used immediately in an exchange without the need for risky and possibly costly conversion<sup>10</sup>.

And yet there are not necessarily any great differences between the definition of money in economics and what the law seeks to identify as its defining characteristics. Money also has a threefold legal function<sup>11</sup>. It is an instrument of valuation: that is its function as a currency unit; it is an instrument of payment; and it is a good that can be saved in the form of monetary instruments<sup>12</sup>. The *currency unit* (unit of account) is an ideal unit essentially defined by a name (franc, euro, dollar) that serves as a reference within the framework of a monetary system. A collection of currency units constitutes a sum of money. But this ideal unit requires a medium in which it can be embodied for the purposes of exchange and storage: that is the *monetary instrument* (store of value)<sup>13</sup>. Monetary instruments, which embody currency units, are banknotes, coins and bank money. *Means of payment* – cheques, bank cards and credit transfers – are used to transfer funds either by delivery or by way of book entries. Banknotes combine the functions of monetary instrument and means of payment.

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<sup>8</sup> Jean-Michel Servet, "La monnaie contre l'État ou la fable du troc", in *Droit et Monnaie*, Litec 1988.

<sup>9</sup> Jean Carbonnier, Conclusions générales du colloque "Droit et Monnaie", in *Droit et Monnaie*, Litec 1988.

<sup>10</sup> Monique Béziade, *La monnaie et ses mécanismes*, ed. La Découverte, 1993.

<sup>11</sup> Jean-Louis Rives-Lange, "La monnaie scripturale" (contribution to a legal study), *Études de droit commercial à la mémoire de Henri Cabrillac*, Litec, 1968.

<sup>12</sup> Anne-Marie Moulin, "Le droit monétaire français et les paiements en écus", *Bulletin trimestriel de la Banque de France*, December 1992.

<sup>13</sup> Jean Carbonnier, *Les biens*, Thémis, PUF, p. 36.

### 1.1.2. Currency unit

The currency unit is sometimes held to be the sole characteristic of money<sup>14</sup>. According to this view, money is a unit of account that is used to determine the value of the services and goods we need<sup>15</sup>, whether or not it is given material form through embodiment in a medium<sup>16</sup>. Thus, the franc was created by Article 5 of the Act of 18 Germinal Year III (April 1795), in which it was defined as 5 grams of silver to a standard of 900/1000 (Act of 17 Germinal Year XI), then as 65.5 mg of gold to a standard of 900/1000 (Poincaré franc, Act of 25 June 1928). This definition was repealed, without being immediately replaced, by Article 2 of the Act of 1 October 1936. The Legislative Decree of 30 June 1937, which in turn amended the 1936 Act, stated that the new gold content of the franc would be determined by decree at a later stage, but no such decree was ever published.

Article 34 of the 1958 Constitution states that "legislation shall establish the rules concerning ... the issuance of currency". A new currency unit, called the "new franc" was instituted as of 1 January 1960 (Ordinance of 27 December 1958 and Decree of 22 December 1959) under the transitional measures provided for by Article 92 of the Constitution. The new franc thus became a multiple of the old franc without any substantive change and with no attachment to any standard. Since 1 January 1999, the euro has replaced the franc as the currency unit of the euro zone, to which France belongs. The new currency unit is defined by Regulation (EC) 974/98 of 3 May 1998, Article 2 of which states that "as from 1 January 1999 the currency of the participating Member States shall be the euro. The currency unit shall be one euro"<sup>17</sup>. Any money obligation must henceforth be paid in France in euros or, until the end of the transition period on 31 December 2001, in the currency unit of the former national currency having the status of a temporary subdivision of the euro.

But an approach which reduces money to a unit of account overlooks its function as a medium of exchange. This presupposes that money is given material form in a monetary instrument and circulates from one holder to another via means of payment.

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<sup>14</sup> J. Hamel, "Réflexion sur la théorie juridique de la monnaie", Mélanges dédiés à M. le professeur Sugiyama, 1940.

<sup>15</sup> Christine Lassalas, *L'inscription en compte des valeurs : la notion de propriété scripturale*, Thesis, LGDJ, 1997.

<sup>16</sup> J. Hamel, *op. cit.*

<sup>17</sup> *Official Journal of the European Communities* (OJEC) L 139 of 11 May 1998.

## 1.2. Monetary Instruments and Means of Payment

Payment is generally defined as the discharge of an obligation by the satisfaction of the creditor. With regard to a money obligation, the debt is discharged by delivery of the sum, either in the form of cash that is legal tender and inconvertible currency (banknotes and coins), or by *entering the amount of the sum of money owed in the creditor's bank account*. Payment is made on transfer of the currency units<sup>18</sup> from the debtor to the creditor.

These currency units, embodied in monetary instruments, circulate with the help of means of payment. Under the terms of Article 4 of the Banking Act of 24 January 1984, "means of payment shall be understood to comprise all instruments which, irrespective of the medium or technical procedure used, enable any person to transfer funds"<sup>19</sup>.

Notes and coins (fiduciary money), like bank accounts (bank money) are therefore three monetary instruments that contain currency units. In the case of fiduciary money, the means of payment and the monetary instrument are one and the same. Payment is made by delivery of notes or coins (see Section 1.2.1). In the case of bank money, the bank account assumes the role of monetary instrument: the means of payment, also called cashless payment medium, will trigger the payment by giving an order to the bank that holds the account to transfer funds to the creditor's account<sup>20</sup>, through a dual transaction: a debit entry on one account (the payer's) and a credit entry on another account (the payee's)<sup>21</sup>.

A study of the various monetary instruments shows that none of them except for fiduciary money causes currency units to circulate<sup>22</sup>. As Thierry Bonneau has pointed out: "Whereas specie and fiduciary money are means of payment, bank money is simply money and is not a means of payment"<sup>23</sup>. The term bank money therefore refers to bank account balances and not to

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<sup>18</sup> Rémy Libchaber, *op. cit.*

<sup>19</sup> *Journal officiel* of 25 January 1985. "The term medium does indeed refer to the instrument and probably designates the fact that the medium for the instrument may be paper or a magnetic strip", cf. on this point Éric Froment, "L'innovation dans les paiements", *Banque* n° 471, 1987.

<sup>20</sup> Payment may also be made by novation, whereby the creditor is paid by a third party.

<sup>21</sup> Thierry Bonneau, *Droit bancaire*, 2<sup>nd</sup> ed., n° 420.

<sup>22</sup> For example, the bills of exchange issued in the Middle Ages against a money deposit or because of a debt on the issuer did not contain currency units, but merely enabled the circulation of a claim on money units which were themselves contained in gold or silver coins held by the issuer. Rémy Libchaber, *op. cit.*, n° 85.

<sup>23</sup> Thierry Bonneau, *op. cit.*, n° 418, p. 260.

the various instruments (cheques, bank cards, credit transfers) which enable bank money to circulate (Section 1.2.2).

### **1.2.1. Fiduciary money: the banknote**

#### **1.2.1.1. Legal nature of fiduciary money**

*Whereas banknotes used to represent a claim on the issuer, nowadays they are regarded as movables of a particular type<sup>24</sup>.*

Originally, banknotes denominated in francs, which the Banque de France alone has been authorised to issue since the Act of 24 Germinal Year XI, displayed similarities with promissory notes. The note was an acknowledgment of debt which the issuer undertook to exchange for gold. Gradually, all the restrictions inscribed in writing were abandoned, such as the name of the beneficiary, the subscriber's signature, the maturity and a nominal amount which differed each time.

In a convertible currency system, a banknote was merely a claim on the issuing bank's gold and silver reserves and portfolio of bills. In this respect, Article 17 of the Act of 22 April 1806 stated that the Conseil Général of the Banque de France should "decide on the creation and issuance of banknotes, payable to the bearer on sight". A person receiving a banknote accepted the issuing bank as debtor in place of the person delivering the banknote. The banknote was regarded as a negotiable instrument or debt instrument transmissible from hand to hand, bearing in mind that the bearer could demand payment on sight of a certain quantity of specie. In this system the banknote represented a pecuniary right in personam, and hence a chose in action.

In an inconvertible currency system, the system in effect in France since the Act of 1 October 1936<sup>25</sup>, the currency can no longer be converted into gold. The Banque de France is released from the obligation to reimburse banknotes in specie. Consequently, banknotes ceased to represent a chose in action as of that date and were treated as movables. In a judgment of 4 June 1975, the Court of Cassation refused to apply Article 439 of the Penal Code, which

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<sup>24</sup> "Le statut juridique du billet de banque", article published in the February 1976 issue of the *Bulletin trimestriel de la Banque de France*.

<sup>25</sup> An inconvertible currency system has been imposed, for more or less lengthy periods, on several occasions: from 1848 to 1850, from 1870 to 1875 and from 1914 to 1928.

makes the destruction of securities an offence, to a case involving the destruction of banknotes<sup>26</sup>.

Moreover, the value of banknotes is determined by statute. Banknotes were made legal tender by the Act of 12 August 1870, which stated that banknotes issued by the Banque de France "shall be accepted as legal currency by public deposit-takers and by private individuals". Before that date, the value of banknotes issued by the Banque de France depended entirely on the confidence placed in the issuer. Thus the Court of Cassation, in a judgment of 7 April 1856, held that "a banknote of the Banque de France is pure confidence"<sup>27</sup>. Today, Article 5 of the Act of 4 August 1993 as amended states that the Banque de France is the sole authorised issuer of banknotes accepted as legal tender. Any person owing a sum of money can therefore discharge the debt by paying, in banknotes, an amount equal to the sum owed to the creditor, who is obliged to accept them as a means of payment.

Legal tender is the corollary of an inconvertible currency system: once it is decided that banknotes will be inconvertible, the holders of banknotes must be protected by ensuring that payment by means of banknotes may not be refused. Creditors will accept a monetary symbol for its face value only if they can be certain that it will in turn be accepted from them for the same value.

*In a convertible currency system, therefore, a banknote derives its power exclusively from the confidence placed in the issuer; in a legal tender and inconvertible currency system, it derives its power from statute and from the confidence placed in the state.*

Unlike all other corporeal movables, banknotes – a true paper currency – have no intrinsic value other than as collectibles.

For many years, statutory measures have been taken to restrict payments made with banknotes, without infringing their status as legal tender. For example, the Act of 12 October 1940 as amended instituted an obligation to use cashless media to make certain payments, and the 1999 Budget Act prohibits the use of cash for payments between individuals, or from individuals to merchants, in excess of 50 000 francs. Fiduciary money has the drawback of being an anonymous means of payment, leading parliament to prohibit its use in certain cases for reasons of transparency and as a weapon in the fight against crime.

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<sup>26</sup> *Bulletin de criminologie*, 1975, n° 143.

<sup>27</sup> Nicole Catala, *La nature juridique du paiement*, Thesis 1961.

### 1.2.1.2. The protection of fiduciary money

*Law-makers have always been very much on guard against any private initiative to replace fiduciary money with another medium having the same features and advantages.*

Thus, the decree of 25 Thermidor Year III authorised the issuance of bearer notes<sup>28</sup>, except when the purpose of the notes was to "replace or stand in for the currency". The law-makers at the time feared the appearance of notes, drawn on debtors whose solvency could not be verified, that might compete with banknotes.

Today, this vigilance takes the form of according fiduciary money specific legal protection.

Article 442-4 of the new Penal Code states that "introducing into circulation any unauthorised monetary symbol with the purpose of replacing coins or banknotes that are legal tender in France shall be punishable by five years' imprisonment and a 500 000 franc fine"<sup>29</sup>.

The introduction and utilisation of monetary tokens in competition with fiduciary money are therefore prohibited; fiduciary money is accorded specific protection in criminal law. In addition, infringements of legal tender constitute a criminal offence under Article R 642-3 of the new Penal Code, which punishes "those who refuse to accept coins or banknotes that are legal tender in France at the value for which they are in circulation."

Banknotes are also given special legal treatment under the terms of Article 5 of the Act of 4 August 1993, according to which "the rules applicable to lost or stolen bearer instruments shall not apply to banknotes that are legal tender". The loss or theft of banknotes is governed by Article 2279 of the Civil Code<sup>30</sup>.

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<sup>28</sup> Issuance of bearer notes had been prohibited by a decree of 9 November 1792.

<sup>29</sup> Article R 642-2 of the new Penal Code further provides that "accepting, holding or using any unauthorised monetary symbol whose purpose is to replace coins or banknotes that are legal tender in France shall be punishable by the fine applicable to second class summary offences".

<sup>30</sup> Article 2279 of the Civil Code states that "with regard to movables, possession is equivalent to title". This also applies to bearer instruments, even if they are incorporeal movables. Cf.

1<sup>re</sup> Chambre civile, 2 May 1990 unpublished, concerning interest bearing notes.

### 1.2.2. Bank money

Fiduciary money is not the only medium for currency units. For years, economists have considered that bank balances also constitute money, because they function like money. M. Ansiaux<sup>31</sup>, a Belgian economist who coined the French term "*monnaie scripturale*", or bank money, defines it as a new type of money, different from coins or banknotes, "which passes from account to account instead of circulating from hand to hand".

The balance on a bank account represents a sum of money, ie, a certain quantity of currency units (100,000 francs, for example) "which exists independently of the monetary instruments of which it is the sum (eg, two hundred 500-franc notes), or of the claim which serves as a vehicle for it in commerce (eg, a cheque)"<sup>32</sup>. Thus, bank money may be defined as a sum of money entered in a bank account which circulates from one account to another by means of cashless payment media like cheques, credit transfers and bank cards. These media, like bank cards which were originally described as "electronic money", merely serve to transmit an order to a credit institution to transfer funds to another bank account<sup>33</sup>.

The legal classification of a depositor's right to his bank account traditionally applied in case law and legal theory is that of a claim on the institution that holds the account<sup>34</sup>. This classification is based on the general deposit theory, which holds that as the funds are fungible, depositing them in an account entails transfer of property to the banker. The banker is under an obligation to return, not the specific currency units which constituted the deposit, but the value of the deposited units (Article 1927 of the Civil Code). For that reason, the depositary may make use of the funds he has received. In this

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<sup>31</sup> *Revue d'économie politique*, September-October 1912.

<sup>32</sup> Jean Carbonnier, *Les biens*, Thémis, PUF, p. 36.

<sup>33</sup> Elie Alfandari, "Le droit et la monnaie de l'instrument à la politique", in *Droit et Monnaie*, Litec, 1988.

<sup>34</sup> Some commentators reject this approach in favour of a right in rem over a bank account. According to this view, the holder of a bank account has not only a pecuniary right in personam on the bank but also a genuine right of ownership on the account and the sums on it. This argument, which springs perhaps from confusion between the ownership of the currency units recorded on the bank account and the nature of the contractual relations between the depositor and the bank, cannot call into question the definition of bank "money", endorsed by both case law and legal theory, because currency units can perfectly well be embodied in this medium.

Cf. on this point: *L'inscription en compte des valeurs : la notion de propriété scripturale*, Christine Lassalas, Thesis 1997, LGDJ, *contra cf.* : *Le dépôt de monnaie en banque*, François Grua, D. 1998, Chronique ; Elie Alfandari, *Les droits des créanciers et des déposants d'un établissement de crédit en difficulté*, D. 1996, 33<sup>e</sup> Cahier, Chronique.

regard, Article 2 of the 1984 Banking Act states that "funds received from the public shall be understood to be funds which a person accepts from a third party, especially in the form of deposits, *with the right to make use of them for his own account*, but subject to an obligation to repay them".

The bank may make use of the funds only insofar as it has not received an order to repay them or transfer them to another account. Some commentators consider that payment in bank money is precarious, because "it depends solely on the availability of the funds that the banker holds"<sup>35</sup>.

Cashless payment media serve merely to transmit an order to the debtor's depository bank to transfer funds to the bank of the beneficiary of the payment. Thus, when a cheque is issued, even if it is guaranteed by the bank, no transfer of funds takes place but merely the transfer of a claim to a sum of money. The beneficiary of the cheque must present it to the issuer's bank so that the issuer's bank can transfer the sum of money. In case law, issuing a cheque constitutes payment only if the cheque is paid by the drawer's bank<sup>36</sup>. In contrast, when the debtor's bank transfers funds to another bank account, it transfers not a claim but a sum of money (the currency units) that will be entered in the beneficiary's account. Bank money is indeed a form of money, since it is a store of value (of currency units) that can be circulated from one account to another.

## II. ELECTRONIC MONEY

New means of payment such as electronic money, which entirely eliminate paper in fund transfers, are becoming increasingly prevalent. Mario Giovanoli paints an interesting picture of how means of payment may develop in a recent article in which he argues that greater transformations have taken place in the monetary sphere in the 20th century than at any other time<sup>37</sup>. Traditionally, a distinction is drawn between three stages in the development of money: coins – gold or silver –, fiduciary money and bank money. By this yardstick, the question is whether electronic money, as a new means of payment, is a new legal form of money (Section 2.1) or whether it proves to be just another way of managing bank money (Section 2.2).

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<sup>35</sup> François Grua, *Qu'est-ce qu'un compte en banque ?*, D. 1999, 24<sup>e</sup> Cahier, Chronique, p. 24.

<sup>36</sup> Cassation civile, 17 December 1927, S. 1925, I, p. 19.

<sup>37</sup> Mario Giovanoli, "Virtual Money and Global Financial Market: Challenges for Lawyers", *Yearbook of International Financial and Economic Law*, 1998.

## 2.1. Electronic "money" is not a new legal form of money

If electronic money were a new legal form of money, it would have to fulfil the three defining criteria of money: it would have to be a unit of account (Section 2.1.1), used as a means of payment (Section 2.1.2) and embodied in a monetary instrument (Section 2.1.3).

### 2.1.1. Unit of account

Like all forms of money, electronic money must and can serve as a currency unit. A merchant will not accept payment in electronic money unless he is convinced that the quantity of electronic units received from the bearer represents the equivalent of the sum of money that he would have received if he had been paid by means of bank money or fiduciary money. The merchant must be able to claim a sum from the issuer that exactly represents the amount of the sale.

Users of electronic money will have confidence in it as long as its value is identical to the value of bank or fiduciary money. The emergence of an exchange rate between electronic money and bank or fiduciary money should therefore be avoided, because that could call into question electronic money's function as a unit of account<sup>38</sup>.

Similarly, electronic money may not be denominated in a currency unit other than the one determined by the State in which it is used, or expressed in currency units that do not have their origin in statute. As mentioned in Section 1.1.2, the euro is the currency unit in France as defined by Regulation (EC) no. 974/98 of 3 May 1998. A merchant applying this rule in conjunction with the rule relating to legal tender may refuse any payment proposed in another currency. However, that does not mean that a merchant may not under any circumstances accept payment in another currency by agreement.

But according to Court of Cassation case law, expressed in a judgment of 17 February 1937, "as a matter of principle (...) any payment made in France, for whatever reason, must be made in French currency"<sup>39</sup>. Under the terms of a Court of Cassation judgment of 17 May 1927, known as the "Matter"

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<sup>38</sup> Jean-Michel Godeffroy and Philippe Moutot, "Monnaie électronique : enjeux prudentiels et impact sur la politique monétaire", *Revue d'économie financière*, n° 53.

<sup>39</sup> Cassation Chambre des requêtes, 17 February 1937, S. 1938, p. 140.

judgment, this case law is limited to domestic payments and does not extend to international payments<sup>40</sup>.

The electronic information recorded on the micro-chip of an electronic purse must represent in France the currency unit in use in France (ie, the euro). A holder could not use an electronic purse whose electronic values are denominated in another currency unit to extinguish a debt denominated in euros (during the transition period, of course, the franc can also be used).

### **2.1.2. A novel means of payment**

**2.1.2.1.** The electronic money payment system constitutes a new generation of means of payment which displays novel features in relation to cashless payment media.

The system works as follows.

- Electronic units are loaded into the micro-chip of an electronic purse in exchange for a sum of money paid to the issuer.
- Payment is made by transferring units from the holder/consumer's electronic purse to the merchant's card, generating a debit from the former and a credit to the latter.
- The balance recorded on the medium represents the amount of the sum of money that the holder may claim from the issuer, the issuer having undertaken to convert the balance into bank or fiduciary money at the holder's or merchant's request.
- The system is attractive to the issuer because it enables him to capture and invest funds paid into an account whose credit balance results from the time lag between the payment of funds by the holders and the payment or repayment of the electronic money to merchants or holders<sup>41</sup>.

This payment system has several unusual features in relation to conventional systems.

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<sup>40</sup> Cassation, 1<sup>re</sup> Chambre civile, 17 May 1927, S. 1928 p. 25.

<sup>41</sup> Jean-Michel Godeffroy and Philippe Moutot, *op. cit.*

First, for the issuer, the funds received are not recorded in the name of the consumer/holder of the medium, nor are they payable to an identified merchant. Thus, *the issuer's debt does not have the same characteristics as a depositary's debt towards the depositor.*

Second, *payment entails an immediate alteration to the balances of the electronic purses.* Unlike the situation with cheques or bank cards, it is not the issuer who makes the alteration. When a customer pays a merchant by cheque or bank card, the amount is not immediately transferred to the beneficiary's account. The instrument has to be presented to the debtor's banker before the beneficiary's account can be credited.

Third, payment by means of bank money takes the form of a transfer of funds whereby the debtor's account is debited and the creditor's account is credited<sup>42</sup>. With an electronic purse, however, payment in electronic money does not involve a transfer of funds. The funds have already been paid to the issuer by a debit from the debtor's account or a payment in fiduciary money in return for units loaded into the debtor's card. The issuer repays the funds by crediting the creditor's account or by paying cash after the creditor has asked for the electronic units received in payment to be converted.

The merchant has a claim on the issuer for the conversion of the electronic units recorded on his card (or point of sale terminal – POST). Hence there is no uncertainty as to settlement arising from the consumer's solvency. With regard to the consumer, the merchant has received final payment. Electronic units are therefore a payment instrument, since they extinguish the debt between the merchant and the consumer. The novel feature, resulting from the fact that the units are prepaid, lies in the certainty of provision for the payment

**2.1.2.2.** Because of these features, electronic money is sometimes presented as an alternative to fiduciary money: it is transmitted from hand to hand (albeit electronically); it enables payment to be made in accordance with the conditions required by law for the discharge of the debtor; and it does not require any link with a bank account. It is as though electronic money, by agreement rather than by statute, had been given a legal framework identical to that of fiduciary money.

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<sup>42</sup> In case law, the creditor is paid when the sum is entered in the account. Cassation 1<sup>re</sup> Chambre civile 23 June 1993, *Revue trimestrielle de droit commercial* 1993, p. 694, obs. Henri Cabrillac and Bernard Teyssié.

However, this approach pays little attention to the legal rules that govern fiduciary money and its protection, which prohibit the issuance of any monetary token intended to replace fiduciary money. Fiduciary money has one specific feature, originating in statute, which cannot by definition belong to electronic money as the law stands at present. Furthermore, as we shall see, electronic money is above all a right to a sum of money. In contrast, banknotes issued by the Banque de France, being classified as corporeal movables since the inconvertible currency system was introduced, represent much more than a mere claim to a sum of money. From a legal standpoint, therefore, electronic money cannot possibly be assimilated to fiduciary money.

If electronic money is a novel means of payment and a unit of account, in order to constitute a new legal form of money it must also be a new monetary instrument in the same way as a banknote or bank account.

### **2.1.3. A new monetary instrument?**

Until now, money (in the sense of currency units) has been embodied in three monetary instruments: coins, banknotes (fiduciary money) and bank accounts (bank money). Banknotes were regarded as a genuine currency from the time they were made legal tender, meaning that they were no longer convertible into gold and derived their value from their face value alone. Bank account balances were classified as "bank money" from the time when it was realised that they could be transferred from one account to another without being converted into fiduciary money. If electronic money is to be considered a new legal form of money, it must also fulfil this function and serve as a monetary instrument.

**2.1.3.1.** This means that the electronic units exchanged between electronic purse holders and merchants must also represent a store of value equivalent to the store of value represented by coins, banknotes and bank balances.

Electronic units can be classified in only one of two ways: they are either corporeal or incorporeal movables.

Electronic units cannot be classified as corporeal movables because they do not have material form. They must therefore be classified as incorporeal movables. Traditionally, a distinction is drawn within this category between rights in rem, such as ownership, which attach to a thing and are binding on all – these are the intangible "properties" – and rights in personam or choses

in action, which are effective only with regard to persons bound to one another by such rights<sup>43</sup>.

On the basis of this distinction, electronic money is either an intangible "property" or else it is a chose in action.

Given that electronic money does not fall within the legal tender or inconvertible currency system, the holder of electronic money must always have the right to ask the issuer to convert electronic units contained in an electronic purse into fiduciary or bank money. No merchant would agree to be paid using this system of payment if he were not sure of being able to change the electronic units at the issuing institution or, in other words, if a claim on the issuer did not attach to electronic money. Thus, a claim on the issuer always attaches to electronic money.

Ultimately, therefore, the question is whether electronic money is an intangible "property" to which an incidental claim is attached or whether it is merely a claim on the issuer.

But electronic money has no autonomous value apart from the value of the claim on a sum of money that it represents.

The proof of this assertion is that if the issuer could no longer convert these electronic units into bank or fiduciary money, merchants would no longer accept them. Electronic units derive their value solely from the existence of the claim on the issuer. The sole effect of payment in electronic money is to transfer a right to a sum of money from the debtor (consumer) to the creditor (merchant).

**2.1.3.2.** Furthermore, from the issuer's standpoint, no transfer of a sum of money takes place between the consumer and the merchant at the time of payment.

An issuer of electronic money holds on a single overall account the entire sum of money received in exchange for the electronic units he has issued. When a consumer uses electronic units to pay a merchant for a purchase, this does not generate a transfer of the above-mentioned sum of money from the issuer. The situation is the same as with a transfer between two bank accounts in the same branch. The branch still holds the same sum of money after the transfer has been completed. Only the creditor of the sum has

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<sup>43</sup> René Savatier, "Essai d'une présentation nouvelle des biens incorporels", *Revue trimestrielle de droit commercial*, 1958, p. 331.

changed. The only difference between such a transfer and a payment using electronic units is that the issuer does not know who the new creditor is until the creditor asks for the electronic units to be converted.

In an electronic money payment system, a transfer of a sum of money takes place:

- between the merchant and the issuer when the merchant asks for the electronic units he has accepted in payment to be converted;
- between the issuer and the consumer when the card is loaded or reloaded;
- should the case arise, between the issuer and the holder (consumer) if the latter asks for repayment of the electronic units recorded on his card.

In conclusion, the issuer's overall account acts as the store of value. Electronic units represent only a claim on this account, and hence a claim on bank money. They are not a new form of monetary instrument but merely a new means of payment. In this respect, they may be classified as debt instruments.

Note that there is no reason for the legal nature of electronic money to change according to the characteristics of different systems. Some systems provide that electronic money should move up the chain to the issuer as soon as it has been used to pay a merchant before passing into the payment circuit again; others allow electronic units to circulate several times in the system before moving up the chain to the issuer<sup>44</sup>. Some commentators consider that electronic money in these systems is a true currency because users consider it to have a value in itself. But even if the units circulate several times, they still represent only a claim on the issuer. Moreover, because of the risk of fraud or counterfeit, issuers will have to maintain a permanent comparison between the amount of electronic units present in the system and the amount issued. This implies regularly moving electronic units up the chain to the issuer. Electronic money is not about to circulate in a perfectly closed system, entirely independent of the payment system using bank or fiduciary money.

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<sup>44</sup> In particular, these are the systems that allow for the transfer of electronic units between electronic purses belonging to holder/consumers. To the best of our knowledge, there is no system that allows merchants to reuse electronic units to pay other merchants or individuals.

## 2.2 Electronic money is a new debt instrument

As we have seen, electronic money is a claim to a sum of money. This claim circulates from medium to medium (from one electronic purse to another) until it is converted by the issuer. Electronic units seem to fulfil a dual function: they establish a right with regard to the issuer, and they furnish proof that the holder of the electronic purse on which the electronic units are recorded is indeed the holder of the claim<sup>45</sup>. Electronic units are thus more than mere claims and should be classified as bearer instruments, which French legal opinion now agrees should be called anonymous instruments as opposed to registered securities. Electronic units display all the characteristics of anonymous instruments embodied in an electronic medium, circulation of which effects a payment in full discharge.

### 2.2.1. Issuance of electronic units

Issuance has its origin in the contract between the issuer of a debt instrument and the holder. An anonymous instrument is an instrument making no mention of the creditor by which the debtor undertakes to pay the material holder of the instrument at maturity<sup>46</sup>. The validity of such "instruments" is recognised by the decree of 25 Thermidor Year III (12 August 1795)<sup>47</sup> and their issuance is permitted even in the absence of any express statutory provision<sup>48</sup>. The issuance of a debt instrument is neither a loan nor a deposit. It is a specific operation<sup>49</sup> which takes place, as far as electronic money is concerned, when funds are paid in exchange for recording electronic units in an electronic purse.

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<sup>45</sup> Cf. Philippe Goutay, "La dématérialisation des valeurs mobilières", *Bulletin Joly Sociétés*, April 1999, n° 4.

<sup>46</sup> Christian Gavalda and Jean Stoufflet, *Droit du crédit 2*; 3rd ed., p. 177.

<sup>47</sup> A decree which allowed the subscription and circulation by mutual agreement of bearer instruments

(I, *Bulletin* 172, n° 1028, B. 57, 140) "The National Convention decrees that the ban introduced by Article 22 of the decree of 8 November 1793 on subscribing and putting into circulation bearer notes and bills does not include a ban on issuing them when their purpose is not to replace or stand in for the currency [...]."

<sup>48</sup> As the Act of 15 June 1976 merely banned the issuance of *grosses notariées* (instruments drawn by a notary incorporating an authority to execute), it may be deduced that civil bearer instruments are lawful.

<sup>49</sup> Concerning traveller's cheques, which are similar instruments, a Paris Appeal Court judgment of 27 November 1991 held that "an organisation issuing traveller's cheques acquires the status of issuer only when a customer buys the traveller's cheques, either from its own offices or from those of an issuing agent, or from those of a money changer approved by one of the foregoing, since only this act of purchase, which implies payment of a sum equal to the nominal value of the instrument, gives rise to obligations, in particular on the person who has become the issuer".

### 2.2.2. Rules governing the circulation of electronic units

If electronic money were nothing more than a claim on the issuer, an assignment of claim would be effective against third parties only by due service on the debtor or by acceptance in an authentic deed according to the provisions of Article 1690 of the Civil Code<sup>50</sup>, which sets out the general rules governing assignment of choses in action. If such a formality were not carried out, the debtor (ie, the issuer) could therefore refuse to discharge his debt to holders, whether merchants or not, thus rendering the system inoperable. Case law seems to favour the solution whereby the debtor, by agreement, accepts the assignment by private instrument, but this would still be ineffective against third parties<sup>51</sup>.

But if the claim, embodied in an instrument which establishes it, includes a negotiability clause, it allows the creditor to transfer his rights to a third party by way of assignment. As Didier Martin has said, negotiability is "the capacity for an instrument to be transferred by a simplified procedure under commercial law, namely delivery with or without endorsement"<sup>52</sup>.

The legal rules governing this new anonymous instrument will be determined to a great extent by the contracts signed by holders and merchants with intermediary banks and/or the issuer. They are not covered by any specific provision of the Commercial Code, nor could they be brought under the regulations governing bills of exchange or promissory notes<sup>53</sup>.

Furthermore, classification as an anonymous instrument means that the issuer cannot assert exceptions since he has undertaken to pay any holder. This principle results from a Court of Cassation judgment of 31 October 1906, which holds that "in bearer certificates, the debtor accepts in advance as his direct creditors all those who successively become bearers; it follows that the bearer is vested in a right in personam which, if he is in good faith, allows only exceptions in personam or exceptions that result from the essential content of the deed"<sup>54</sup>.

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<sup>50</sup> This article states that "the assignee is put into possession with regard to third parties only by due service of assignment on the debtor. Nevertheless, the assignee may also be put into possession by acceptance of the assignment given by the debtor in an authentic deed".

<sup>51</sup> Christine Lassalas, Thesis, prec.

<sup>52</sup> Didier R. Martin, *Du titre et de la négociabilité* (concerning pseudo-negotiable debt instruments), D. 1993, Chroniques.

<sup>53</sup> Rouen, 14 juin 1963, D. 1963, J, p. 636.

<sup>54</sup> Chambre civile, 31 October 1906; D.P. 1908, I. 497 ; S. 1908, 305, note Lyon-Caen.

### 2.2.3. Payment constituting full and final discharge of the obligation

The fact that the transactions involved in these systems are for small amounts and that it is difficult to know the identity of the holders is sufficient reason for merchants who accept payment in electronic money also to accept that by delivering electronic money, holders/consumers discharge their obligation. This type of full and final payment is possible provided that it fulfils the conditions of delegation<sup>55</sup>.

Payment by the mere assignment of a money claim does not "in itself extinguish the assignor's debt to the assignee"<sup>56</sup>. In order for payment to constitute full and final discharge of the obligation, the creditor must agree to discharge his first debtor. This results from the provisions of Article 1275 of the Civil Code, which states that "delegation, whereby a debtor gives the creditor another debtor who obligates himself to the creditor, does not constitute novation unless the creditor has expressly stated that he intended to discharge his debtor who made the delegation". The only remaining uncertainty is the way in which the merchant must express his intention of discharging the holder/consumer. Some commentators, like Malaurie and Aynes, recommend that this intention should be expressly stated and not presumed. Others consider that there is no justification for such a formalistic requirement and that a tacit intention should be regarded as sufficient provided that it is certain<sup>57</sup>. If the contracts concluded between the issuer and the merchants contained provisions relating to full and final discharge of the obligation, this could therefore constitute sufficient evidence of the acceptor's intention to discharge the holder.

### 2.2.4. A new debt instrument?

**2.2.4.1.** The novelty of electronic units as anonymous instruments should not be exaggerated, since they bear a strong similarity to traveller's cheques, for the following reasons:

- neither means of payment is linked to the debtor's bank account and are hence not cashless payment media. The holders of these instruments do not open an account with the issuer;

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<sup>55</sup> Delegation is a species of novation whereby a debtor (the delegator) causes a delegated third party, generally his own debtor, to obligate himself to the creditor (the delegatee), who correspondingly discharges the delegator of his own obligation.

<sup>56</sup> Cassation commerciale, 23 juin 1992, *Bulletin civ.* IV, n° 245.

<sup>57</sup> Marc Billau, *La délégation de créance*, Bibliothèque de droit privé, Vol. 207; and *Juris-classeur civil*, fascicule 104, *Contrats et obligations-délégation*, by Philippe Simler.

- the issuance system is the same: a sum of money is paid to an issuer, who in exchange issues instruments which may be used to pay for goods bought from merchants;
- in addition, traveller's cheques generally include an order clause which means that they can circulate freely, without having to fulfil the formal requirements for assignment of claim.

In a judgment of 16 January 1963<sup>58</sup>, the Court of Cassation classified traveller's cheques as follows: "Traveller's cheques, which express an undertaking to pay contracted by the issuing bank, constitute not banknotes but sight or short-term debt instruments".

An earlier judgment of the Criminal Division dated 8 November 1950<sup>59</sup> held that traveller's cheques "though they may have the aspect of cheques, do not correspond to the legal definition of cheques and express not a payment order but merely an undertaking to pay contracted by the issuing bank".

Traveller's cheques, transferable by endorsement, fulfil the definition of an instrument establishing a right that it is supposed to embody intrinsically<sup>60</sup>. Legal theory prefers to reserve opinion on whether or not blank traveller's cheques can circulate: if that were the case, they could be assimilated to banknotes. This would make them an unlawful means of payment in France because of the legal rules mentioned earlier, especially those in the Penal Code that prohibit putting into circulation unauthorised monetary tokens whose purpose is to replace banknotes that are legal tender (Article 442-4 of the new Penal Code, prec.)<sup>61</sup>.

**2.2.4.2.** Unlike traveller's cheques, however, electronic money is an anonymous instrument embodied in a micro-chip and not on a paper medium. This would not be the first time that the law recognised the embodiment of a

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<sup>58</sup> D. 1963, p. 517, note Despax ; *Banque*, 1964, p. 115, obs. Xavier Marin

<sup>59</sup> *Revue trimestrielle de droit civil*, 1956, p. 91; *Banque*, 1956, p. 41, obs. Xavier Marin.

<sup>60</sup> If a traveller's cheque does not include an order clause, it can circulate only by way of assignment of claim. However, almost all traveller's cheques include an order clause whereby they can be endorsed. Endorsement is effected by the payee appending a second signature; the comparison between that signature and the one appended on the instrument at its creation is intended to forestall the circulation of stolen traveller's cheques. Although the problem has never arisen, this endorsement must be assumed to produce all the effects of endorsement of a promissory note. The beneficiary of the endorsement then benefits from the disqualification of personal exceptions and the endorser becomes the guarantor in solidum of payment of the instrument.

<sup>61</sup> This study does not seek to consider whether or not this type of traveller's cheque is lawful, any more than it seeks to consider whether or not electronic money is lawful.

right in an electronic record, since Article 1 of the decree of 2 May 1983 on the rules governing transferable securities states that "transferable securities are henceforth materialised solely by an entry in the account of their owner"<sup>62</sup>. Consequently, the dematerialisation of transferable securities does not seem to have led to the disappearance of anonymous instruments, which remain unconditionally effective<sup>63</sup>.

Electronic money seems to be a new "dematerialised" form of debt instrument. However, a very full report of the *Conseil National du Crédit et du Titre* (National Credit and Securities Council) published in 1997<sup>64</sup> defined dematerialisation as "quite simply the process by which the handling of paper is abolished". But electronic money is indeed an instrument having a specific legal nature, created as such, and not the dematerialisation of a classic form of pre-existing paper instrument. That is why we would argue that electronic money is a debt instrument not dematerialised but "embodied in an electronic instrument", whose circulation effects full and final payment.

Electronic money is not therefore a new form of money but a debt instrument that facilitates the circulation of bank money. The electronic money payment system is a new way of managing bank money in which the means of payment is a card loaded with electronic units. From a legal standpoint, each electronic unit is thus *a claim embodied in an electronic instrument and accepted as a means of payment by third parties other than the issuer*.

The success of electronic money projects will depend to a very large extent on users' confidence in the effectiveness of this new means of payment and in the solvency of the issuer. In this respect the issuer, as an intermediary in fund transfers, manages a means of payment and, under Article 1 of the Banking Act, must have the status of credit institution<sup>65</sup>. Likewise, at European level, the European Parliament and Council directive proposal "concerning access to the activity of electronic money institutions and its exercise, as well as the prudential supervision of these institutions" could classify issuers as credit institutions so that, as well as being governed by the

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<sup>62</sup> Decree 83-359 of 2 May 1983, *Journal officiel* of 3 May 1983, p. 1359. Cf. also Didier R. Martin, "De la monnaie", *Mélanges en l'honneur de Henry Blaise*. However, there does not seem to be any need for dematerialisation to be given the sanction of statute.

<sup>63</sup> Philippe Goutay, "Titre négociable et opposabilité", *Mélanges Association européenne pour le droit bancaire et financier (AEDBF)*, 1997

<sup>64</sup> *Rapport du CNCT*, "Problèmes juridiques liés à la dématérialisation des moyens de paiement et des titres", May 1997.

<sup>65</sup> Article 1 of the 1984 Banking Act states that "credit institutions are legal persons carrying out banking operations as their regular business. Banking operations comprise the receipt of funds from the public, credit operations and making available to customers or managing means of payment".

1977 and 1989 banking directives and the 1991 money laundering directive, they will also be subject to prudential supervision.