

EPFSF Briefing: A Single Payments Area for Europe

The rationale behind the establishment of a SEPA

Establishing the Internal Market for Payments and a truly Single Euro Payments Area (SEPA) is a political objective for the Commission, the ECB and the banks. It is the view that harmonisation of essential rules on Euro payment services would facilitate a Single Euro Payment Area and promote efficiency of payments throughout Europe.

- ⇒ SEPA aims at a Pan-European Payments Area within which selected instruments for payments denominated in euro are based on common “scheme” rules. This requires consistent standards and legislation throughout the EU.
- ⇒ **SEPA means that European citizens would have to abandon¹ some of their existing national practices and to move towards a new way of paying their bills and of receiving their money.** This new pan European way of paying will apply both to “face to face” and to “remote” transactions, as well as national and cross border euro transactions within the EU.
- ⇒ As far as wholesale payments are concerned, a new pan-European market infrastructure being in place, SEPA will become a reality if corporates and public entities invest in order to migrate their flow of payments from national means of payments to the new set of pan-European schemes.

The industry stance

Regulation 2560/2001, which requires banks to handle domestic and cross-border euro transfers at the same price, constituted an important step towards the creation of an Internal Market for Payment services in the EU. In 2002, the EU credit sector associations and a group of large and smaller banks established the European Payment Council (EPC) as an industry initiative towards the creation of a Single Market for Payment in the EU. The EPC Roadmap 2004-2010 concentrates on three payment means: credit transfers, direct debits and debit cards.

The New Legal Framework

The New Legal Framework (NLF) for Payments aims to facilitate the creation of an Internal Market for Payments i.e. one big domestic market consisting of the 25 Member States. The NLF will cover all means of payment (except cash and cheques) under the same set of basics rules. It will focus on the payment provider-customer relationship and consumer protection rules.

The NLF is expected to introduce the concept of a Payment Institution in order to enhance competition in the market. Only Payment Institutions, Banks and E-money Institutions will be able to offer payment services to the public.

¹ Charlie Mc CREEVY, European Commissioner for Internal Market and Services, wants the migration to occur by 2010. The European Payment Council “EPC” is convinced that a critical mass of transactions will naturally migrate to these payment instruments by 2010 such that SEPA will be irreversible through the operation of market forces and network effects.

In general, it is difficult to give a meaningful short description of the content of the NLF as it is detailed and quite wide-ranging. It introduces detailed requirements on transparency prior to and post a payment, rules on how to authorise a payment, on liability, irrevocability; the principle of execution of the full amount of a payment, execution time and value dates. These specific requirements would apply to payments in general (except cash and cheques).

The industry has still many reservations mainly on the extended scope of the NLF: inclusion of SMEs in the scope of consumer protection rules, inclusion of transactions with one leg outside of the EU, inclusion of all currencies, even non-EU ones, inclusion of payments from and to a country outside the EU, on the light prudential regime for non-bank payment institutions to provide payment services; on extensive information and transparency requirements, on the introduction of strict liability of providers for the correct execution of payments. Furthermore, industry has concerns about the imbalance in liability between the payment service provider and payment service user, as well as about the NLF's intention to abolish value dating as a pricing instrument.

The draft proposal and a draft impact assessment are still under discussion, and the Commission is expected to adopt the final proposal by September 2005.

The EPC and the creation of three SEPA "schemes"

In a declaration issued on 17 March 2005, the EPC reaffirmed its commitment towards the three Pan-Euro Payment Schemes, i.e. on electronic credit transfers, on direct debits and on cards. We quote:

"We will deliver the two new Pan-Euro Payment Schemes for electronic credit transfer and for direct debits. We will also design a Cards Framework to define a single market for cards. The scheme rulebooks and the cards framework definition will be delivered by end 2005, and the services will be operational by January 2008.

We know from feedback from our community in the eurozone that by the beginning of 2008 the vast majority of banks will offer these new Pan-Euro services to their customers.

We are also convinced that a critical mass of transactions will naturally migrate to these payment instruments by 2010 such that SEPA will be irreversible through the operation of market forces and network effects."

Regarding **credit transfers**, the objective is that Credeuro will become really a pan-European standard. The ECB also expects industry to define pan-European standards for payment initiation by Corporates. However, a lot of these requirements are already in practice today, e.g. for urgent payments. Many industry stakeholders believe that these fundamental changes to the operating model will force banks to reconsider the current model of national parallel infrastructures. Through the provision of STEP2, the Euro Banking Association (EBA) has established a first PEACH. However, national payments are still cleared through the national incumbents, resulting in EBA processing small numbers of cross-border transactions. Next to other industry factors like banking consolidation and increased focus on cost reduction, SEPA will be an additional catalyst to encourage industry to consider the various options for consolidation of the payments processing and clearing infrastructure.

In the area of **direct debits**, the challenge is to create a scheme that is not available today. For example, European citizens are not able to pay their utility bills from one bank account to

payees in different countries via direct debit scheme. In June 2004, the EPC agreed on a set of high level PEDD scheme principles. Work is now underway to define the detailed rule book of the new PEDD scheme. Target live date of PEDD (pilot) will be 2008. In order for the scheme to be viable to the payee (the collecting company), 100% reachability is required on the payer side. In other words, all banks have to be able to process PEDD debit transactions. It is expected that this will be a challenge for the industry.

Cards have been the fastest growing retail payment means in Europe. It distinguishes itself from credit transfers and direct debit in the fact that it is a branded product that is offered in a very competitive environment. Across the debit and credit card segment, two card scheme types can be distinguished. The first type consists of schemes that have been created nationally and are governed and processed by national players. More recently, most of these local debit schemes have been enhanced with an international cash and payment functionality like Maestro or Visa Electron. The second type are cards issued only under an international payment scheme brand (like MasterCard or Visa), and which by their nature have global utility. Whereas one could claim that therefore SEPA is already a fact for cards, the ECB and the Commission would argue that this is not entirely the case. Areas that need to be addressed include the need to enhance the acceptance proposition in some markets, the legal environment (see NLF), the general adoption of the highest security standards (e.g. Chip and PIN), the removal of any remaining national market entry hurdles for card issuers or acquirers, the rationalisation of processing infrastructures and the alignment of inter-bank fees to the SEPA vision. Above all of this, industry's main objective is to ensure that cards remain a commercial business and do not become a public utility, potentially resulting in lack of innovation and investment, to the detriment of cardholders and merchants.

Final remarks

The financial services industry is firmly committed to creating pan-European payment schemes. These will provide a major contribution to achieving the Single Euro Payments Market. The banking industry fully supports the Commission's objective to create the appropriate level of legislation that will accompany and facilitate these market developments. It also welcomes the intention of the Commission to leave the rules and practices applying to the inter-bank (inter-payment service provider) environment up to the market. Nevertheless, the anticipation of the NLF provisions in the absence of a thorough and serious economic assessment of the potential advantages and disadvantages of a Directive and prior to the full design phase of the pan-European schemes may be counterproductive. Furthermore, creating a framework covering all payments may also not be workable in practice. The considerations and justification for regulating the various means of payments are different and what applies to a particular means of payment may not be applicable to other means of payment or payments as a whole. More time and coordination are needed between the banking sector and the Commission, also given the complexity and difficulty of reaching agreements across 25 Member States and a large number of financial institutions. In addition, the draft directive may not successfully achieve the necessary modernization and simplification of the regulatory framework applying to retail payment services because of the room it will leave for Member State's interpretation. In our view, the only way to move towards an Internal Market for retail payments and a level playing field between payment providers is to achieve full harmonisation of national payment rules and practices but in a single market framework based on market competition principles.

Briefing notes are prepared by the Financial Industry Committee to the European Parliamentary Financial Services Forum. For further information on the subjects raised in the briefs please contact the Chairman, Members or Secretariat of the Financial Industry Committee.

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