

SEPA will make Europe more competitive and provide better services for bank customers. **Gerard Hartsink**, chairman of the European Payments Council, says developments are gathering steam ahead of the 2008 deadline.

- Most banks will meet the 2008 deadline, and by 2010 market forces will ensure the rest are SEPA-compliant.
- The process can only be realised through the involvement of all players.
- SEPA will bring economic benefits to Europe as a whole, including banks and their clients.

THE ROAD TO SEPA

| 2002 | 2004 | 2005 | 2006 |
|--|---|---|--|
| European Payments Council (EPC) formed by payments industry as a self-regulatory initiative, supported by European authorities | December: EPC approves Roadmap 2004–10 | 17 March: EPC Crown Plaza Declaration – EPC approves roadmap | December: European Commission proposes Payment Services Directive (PSD) and European Parliament later reviews 642 amendments |
| | | | EPC proposes pan-euro payment schemes for electronic credit transfer and direct debits, and a cards framework defining a single market for cards |
| | | | March: EPC approves SEPA cards framework and single euro cash area framework |
| | | | 4 May: ECB and European Commission state that public administrations should become launching customers for the new SEPA payments services |

The Single Euro Payments Area (SEPA) is an essential component of the Lisbon Accord of 2000, which aims to make the EU 'the most competitive and knowledge-driven economy by 2010'.

The European authorities are encouraging self-regulation from the payments industry, which formed the European Payments Council (EPC) in 2002. This initiative was also a consequence of Regulation 2560/2001 on Cross Border Charges, which removed the differences in charges for cross-border payments in the EU.

The payments industry's vision was released in 2002 and was subsequently incorporated into the preamble of the EPC charter. It states that the members will: 'share the common vision that Euroland payments are domestic payments; join forces to implement this vision for the benefit of customers, industry and banks and accordingly launch our single payments area.'

The EPC has continuously met its commitments, delivering the frameworks, business rules and standards for SEPA. It is now time for banks to honour their commitment and make it a reality.

Driving the roadmap

In December 2004 the EPC plenary approved its Roadmap 2004–10, which agreed that: 'SEPA will be the area where citizens, companies and other economic actors will be able to make and receive payments in euros within Europe, whether between or within national boundaries under the same basic conditions, rights and obligations, regardless of their location.'

The roadmap was reviewed in the first quarter of 2005 by all EPC members and banking communities, in particular those in the euro area. The roadmap was also reviewed by new and national banking communities to ensure that the entire banking community supported its objectives, scope, deliverables, timelines and roles.

The EPC plenary concluded that the roadmap was supported and approved in the EPC Crown Plaza Declaration of 17 March 2005, with the focus on the primary EPC deliverables. The plenary said: 'We will

'It is up to banks and their national communities to take the lead for the implementation and migration plans.'

About the EPC

The European Payments Council (EPC) is the decision-making and coordination body of the European banking industry in relation to payments.

It was established in June 2002 and adopted its current governance structure in mid-2004. Its purpose is to support and promote the creation of a single euro payments area. It defines common positions for core payment services within a competitive market, provides strategic guidance for standardisation, formulates best practices and supports and monitors implementation.

The EPC has 66 members, comprising banks and banking associations. Over 300 professionals from 27 countries are directly engaged in the EPC's work programme.

deliver the two new pan-euro payment schemes for electronic credit transfer and 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 the end of 2005, and the services will be operational by January 2008.

'We know from feedback from the 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.

'SEPA will be delivered by the banking industry in close conjunction with all stakeholder communities (consumers, SMEs, merchants, corporates and government bodies) and supportive public authorities.

The community of European banks is strongly committed to this ambitious programme of action, based on self-regulation and a full recognition of the role of market forces and competition.'

The EPC plenary has met the regulators' expectations for the January 2008 deliverables for credit transfers, direct debits and cards while the Euro Banking Association is handling the value added service priority payments. Complementary deliverables for cash, e-payments and mobile payments have also been approved.

It is up to banks and their national communities to take the lead for the implementation and migration plans.

Improving credit transfers and direct debits

The EPC aims to replace the current euro credit transfer and direct debit instruments with SEPA instruments. The business rules and standards are set

| | 2007 | 2008 | 2010 |
|--|---|---|---|
| September: Proposal for second-mandate flow option (mandate flow of the debtor to the debtor bank) and business-to-business direct debit scheme approved | January 2007: EP and European Council pass PSD proposal | November 2007 – January 2008: Eurosystem platform to be implemented | 2010: A critical mass of transactions will naturally migrate to SEPA payment instruments |
| September: European Associations of Corporate Treasurers reiterates its support for SEPA | December: EPC plenary receives proposal on borderless solutions for m- and e-payments | January 2008: Deadline for banks to start delivering SEPA payments services | |

out in Version 2.1 of the Rulebooks issued in September 2006 and are complemented by the Implementation Guidelines, version 2.1, issued in September 2006.

In the EPC plenary of December 2006, Version 2.2 was approved, adding an upgraded chapter 6 regarding the scheme management functions. Version 2.2 will be the basis for the January 2008 bank deliverables, as committed to in the EPC declaration of 17 March 2005.

The EPC plenary decided in December 2005 to formulate an additional proposal for a second-mandate flow option (mandate flow of the debtor to the debtor bank) and for a business-to-business direct debit scheme.

These were approved in September 2006 and will be included in Version 3.0 of the SEPA Direct Debit Rulebook and in the Implementation Guidelines, which will be approved in March 2007.

The Rulebooks mainly cover the business rules and standards for the bank-to-bank space with the data standards from customer to customer, and are the basis for banks' value propositions for their customers. Banks compete with their value propositions for core and for added value-payments services.

The SEPA credit transfer and direct debits legal models are based on adherence agreements between banks and payments institutions and the scheme management entity. The EPC plenary supports a legal model making the scheme management entity a function of the EPC AISBL (a Belgian legal entity).

Making cards work across SEPA area

The EPC strategy for cards is an adaptation strategy. The SEPA cards framework will be developed with high-level principles and rules for banks, card schemes and card processors. This will enable European customers to use general-purpose cards to make and receive payments and cash withdrawals in euros throughout the SEPA area with the same ease and convenience as they do in their home country. Banks are expected to deliver these services from January 2008 to their customers (consumers and merchants).

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The European Central Bank (ECB): eurosystem made it clear in February 2006 that more standardisation is expected for the card payments process. The EPC responded by approving a document for further standardisation of the process in September 2006. In November 2006, the ECB: eurosystem published its 'SEPA for cards', with ten provisions for the cards business in the euro area.

While banks, card schemes and processors are considering their options, the ECB: eurosystem is reviewing these dialogues. The European Commission and the ECB are concerned that there might not be enough scheme competition left in the end game. DG Competition and the Commission have set up an inquiry into competition in the current cards payments market, and a position paper from the Commission, focusing on interchange arrangements is expected.

Efficient clearing and settlement mechanisms

The SEPA credit transfers, direct debits and cards transactions need to be cleared and settled efficiently. The settlements will be executed in central bank money via Target 2. The new eurosystem platform should be implemented in all euro markets between November 2007 and the beginning of 2008.

The EPC has developed a clearing and settlement framework – the pan-European automatic clearing house (PE-ACH), allowing for five clearing venues. While some banks prefer to continue with their bilateral clearing, others support the PE-ACH model, which offers pan-European reachability for euro-clearing services to all banks.

Cheaper cash

The EPC strategy regarding cash is twofold, reducing the costs of cash processing and repositioning the payments instrument for cash. The single euro cash area (SECA) framework was approved by the EPC in March 2006 and is focused on reducing cash processing costs.

In the European Payment Profit Pool Analysis of June 2005, McKinsey made it clear that banks are losing at least €21 billion on cash in nine of the EU25 markets. In response, the EPC has published options to reduce this based on the lessons learned about the repositioning of cash in some European markets.

Standardising m- and e-payments

Limited progress has been made on m- and e-payments because the market is fragmented by numerous proprietary solutions from non-banking companies. Banks need to agree on the business rules and standards before progress can be made. The number of users and the services delivered by mobiles and e-commerce is growing fast.

Borderless solutions are required to meet the needs of consumers and merchants. The EPC plenary approved a proposal in December 2006 for the next steps of these payment channels.

Communicating success

Communicating SEPA's benefits for all stakeholders and society is essential for a successful migration. The Commission and the ECB: eurosystem intend to intensify the communication in close cooperation with the banking industry.

The EPC has developed a communication document, Making SEPA a reality, for marketing purposes and to facilitate dialogue. The EPC does not have a specific communication role for national communities, which are handled by national public authorities and banking associations.

The importance of payments

- At least 24% of banking revenues, 34% of banking costs and 9% of profits are related to payments.
- Banks are losing €21 billion on cash in nine of the EU25 markets.

Source: European Payment Profit Pool Analysis, June 2005, McKinsey

The printed word

- EPC Roadmap 2004–2010 (December 2004)
- EPC Crown Plaza Declaration (March 2005)
- SEPA Credit Transfer Rulebook, version 2.1 (2006) and Implementation Guidelines, version 2.1 (September 2006)
- SEPA Direct Debit Rulebook, version 2.1 (2006) and the Implementation Guidelines, version 2.1 (September 2006)
- SEPA Datamodel, version 2.1 (September 2006)
- EPC CSM/PE-ACH Framework (July 2006)
- UNIFI (ISO 20022) XML standards approved by ISO; see www.ISO20022.org (July 2006)
- SEPA Cards Framework (March 2006)
- SECA (Cash) Framework (March 2006)

Involvement of end users

The EPC's design deliverables, such as the SEPA Credit Transfer Rulebook and SEPA Direct Debit Rulebook, were approved by corporates and their national and European associations, such as the European Associations of Corporate Treasurers (EACT).

EACT supports the Rulebooks, but expects more functionality for direct debits to be made available.

The EPC has given the Commission and the ECB: eurosystem the opportunity to provide feedback and additional requirements for public administrations.

'Bankers should not underestimate the impact of the Payment Services Directive.'

Economic benefits of SEPA

Over time, all customers, corporates, public administrations and consumers are expected to benefit from SEPA. So far, a convincing analysis of the macro, meso (for corporates and banks) and micro study is not yet available.

The McKinsey report of June 2005 clarified the importance of payments for suppliers. At least 24% of banking revenues, 34% of banking costs and 9% of profits are related to payments. The analysis also clarified that

there are structural differences in the revenue models and for the instrument mix in the euro area. In some markets, customers pay more than others; in others, consumers are paying more than corporates and vice versa.

The EPC will not take a position on banks' revenue models because this is beyond its mandate and in conflict with competition rules.

The interest revenues and interchange commission will likely be put under more pressure, requiring banks to refine their fee structure. Several regulators are in favour because it creates more transparency for customers and reduces the volatility of the profits, and thus the risks, for banks.

To realise the economic benefits of SEPA, banks and their customers (corporates, merchants, public administrations) must invest in their organisations and infrastructures. This has to be planned carefully, and should be aligned with national implementation and migration plans.

Banks are fully committed to SEPA and have empowered the EPC to make it happen. Now, in unison, we must turn our SEPA vision into reality. FBA

Implementation: January 2008 deliverables

The ECB and the European Commission expect banks to deliver SEPA payments services from January 2008, and the EPC plenary has made it clear that banks are committed to deliver these services. Ultimately, banks are designing these value propositions for their customers.

Banks and national communities are leading the implementation process, while the EPC is supplying the support and tools to monitor this implementation. The EPC has undertaken several initiatives to reduce coordination risks, including a testing framework and a directory for operational readiness. A national implementation managers' forum is also being planned.

SEPA and our customers

The ECB and the European Commission made it clear in their joint statement of 4 May 2006 that public administrations should become launching customers for the new SEPA payments services.

However, several bankers and banking associations have expressed concern about the speed of customers' acceptance of SEPA.

After its September 2006 board meeting, EACT reiterated its support for the introduction of SEPA in line with the timetable agreed by the European authorities and the EPC. While corporates and merchant organisations have confirmed that they appreciate SEPA's economic benefits, the position of public administrations is not yet clear.

Several consumer organisations support the SEPA payment instruments, provided they are as easy to use, safe and efficient as what they are used to. The change for consumers is limited. The new SEPA payment instruments are generally an upgrade of the current payment instruments, with the additional feature of reachability to all bank accounts in the euro area. The introduction of mobile telephones, the internet and the euro was of far greater significance for consumers than SEPA payment instruments.

Harmonisation: the payment services directive

SEPA requires the harmonisation of legislation by public authorities and the harmonisation of business rules and standards by the industry. In December 2005, the European Commission published a proposal on the Payment Services Directive (PSD). Many market participants, including the EPC, commented on this proposal, and the European Parliament reviewed 642 amendments. The EP and the European Council are expected to pass the proposal before April 2007.

Bankers should not underestimate the impact of the PSD. Not all banks realise that it will apply to their payments services for all currencies in the European Community (EU25) and not only to the new SEPA payments services.

Gerard Hartsink

Gerard Hartsink is chairman of the EPC and a senior executive vice president at ABN AMRO Bank, where he is responsible for European affairs and market infrastructures in the securities, payments and cards industry and relations with European institutions.