

SEPA – delivering benefits to the corporate.

Banks will look to e-Invoicing and supply chain financing as value-add services in the post-SEPA world.



When the Single Euro Payments Area (SEPA) came into being on 28 January this year, it was the culmination of six years of development by the European Payments Council (EPC), a representative body of the European banking industry. In June 2002, the EPC was charged with creating SEPA – a harmonised, open and interoperable ‘domestic’ payments market for the euro zone. Since that time the EPC has grown to 72 members in 30 countries, representing all sizes and sectors of credit institutions within Europe. It has developed Scheme Rulebooks for the SEPA Credit Transfer and SEPA Direct Debit payment instruments (which will be introduced in November 2009) and also a SEPA Cards Framework.

But now the SEPA foundations have been laid there is a new task ahead; financial institutions across Europe – not just those in the euro zone – are building new payments services offerings that will take advantage of the SEPA environment. Financial institutions have invested heavily in complying with SEPA; in 2006, Accenture forecast the top 100 banks in Europe would spend more than €3 billion in order to comply with the initiative. They would spend this on an initiative that would in fact reduce their payments revenues. SEPA provides the framework for the European Commission’s Regulation 2560/2001, which stipulates that the fees banks charge their customers for euro cross-border payments are the same as those charged for domestic transactions. Before the introduction of the Regulation, the average fee for a cross-border credit transfer of €100 was €24, after introduction it dropped to an average of €2.46 (World Payments Report, 2007).

Banks will be unable to make the same margins on the SEPA Credit Transfers and SEPA Direct Debits that they have on national payments instruments and cross-border services. How then, will they recoup their SEPA spend and also replace the lost payments revenues?

Adding value to SEPA

A CapGemini report, SEPA: potential benefits at stake, which was issued at the launch of SEPA, suggests that the initiative holds “a market potential” of up to €123 billion. The report identifies three trends in the payments market in Europe: rapidly growing transaction volumes, price convergence and little or no growth in operational costs. As a result of these trends, the total revenues for banks will increase, says the report, although fees per transaction will decrease.

The jewel in the crown of SEPA, however, will be the so-called value added services. CapGemini identifies electronic invoicing (e-invoicing) as perhaps the most promising. SEPA standardises and harmonises payments processing across borders, removing some of the obstacles that have prevented more widespread adoption of e-invoicing in Europe. Banks, which are well-positioned to offer e-invoicing services, said CapGemini, could create potential extra revenue flow of €0.4 billion–€3.4 billion per year. It could be argued that the business case for SEPA alone is not great, but add e-invoicing to the equation and it becomes astonishingly good.

But there is more to SEPA than e-invoicing; some of the more forward-thinking financial institutions operating in Europe are turning their attention to supply chain financing as another area where they can add value for their clients.

E-invoicing

There is no doubt that paper invoices have no future: invoices should be sent and received in the same way as the payments to which they are linked, i.e. electronically.

The European Commission estimates that the potential cost savings of e-invoicing in the business to business sector will be €238 billion per annum. The European Association for Corporate Treasurers puts the figure at €243 billion. These estimates are based mainly on process savings for organizations receiving invoices and do not take into account a wealth of other benefits e-invoicing delivers such as:

- Lower credit risk when more frequent invoicing lowers outstandings;
- Lower fraud risk when e-invoices sent via service providers provide authenticity and integrity;
- Better cash flow through faster payment;
- Lower IT costs when interfaces to service providers and software for invoicing, accounting, VAT and payments are standardised;
- Further automation when e-orders, e-statements etc in the procurement process use the same data elements and standards and are sent in the same channels;
- Lower cost for financing when invoice financing can be automated; and
- Much higher productivity when staff members are freed up from boring, badly paid routine work to customer service, sales and process improvements.

While SEPA has removed many of the obstacles to cross-border e-invoicing, it has not yet changed the mindset of a critical mass of actors in this field – enterprises and the public sector.

This is one of the tasks of the European Commission's Expert Group on e-Invoicing, which was set up in 2008 to establish a European Electronic Invoicing Framework by 2009. The Expert Group, chaired by **Bo Harald**, head of TietoEnator's Executive Advisors' Group, has three streams of work under way, which will result in the development of:

- A compelling set of high level Business Requirements, which will cover the needs of all users and market participants;
- Proposals to simplify and evolve the Legal and Regulatory framework for e-invoicing. This work is addressing the requirements set out in existing Value Added Tax legislation, as implemented across EU Member States. The group is also looking into the broader legal issues related to e-invoicing such as archiving, company legislation and intra-community rules; and
- A vision for how the market could better respond to user needs through network solutions supported by standards.

Harald says e-invoicing in Europe will be driven by the public sector because government authorities are the largest senders and receivers of invoices. "The Expert Group is very proud of the countries that have made a move to e-invoicing, but is also disappointed that not more countries have made such a commitment," he says. Five countries – Denmark, Sweden, Italy, Spain and Finland – have stated they will no longer accept paper invoices in the public sector. These countries see it as an important method of saving tax payers' money – always a popular move by any government.

Supply Chain Financing

E-invoicing is an important step along the way to end-to-end straight-through processing for corporates and myriad services that can be developed from this base. Once e-invoicing is established, an institution can attach remittance information to a payment, thus enabling faster reconciliation and settlement. This greater element of transparency will also increase the ability to automate the financial supply chain and in turn enable banks to offer supply chain financing services. Automating the financial supply chain begins at the purchase order and continues through to reconciliation of the payment and final settlement. Once the supply chain is automated, corporates gain greater visibility of their cash and liquidity positions, while banks gain a clearer understanding of their corporates' finances and cash flows. Armed with this understanding, banks will be able to extend credit to their corporate clients, thus building revenues.

There is €800 billion of surplus cash in working capital across Europe; if banks can offer services that identify that cash, they can securitise it and offer services around it.

Once the invoicing process is automated, everything around it can also be automated, providing greater transparency of the payment transaction from start to finish. Cash flow forecasting becomes more accurate, cash can be drawn down at better rates, and excess cash can be used to fund other parts of the business.

As corporates globalise they are increasingly dealing with a broad range of suppliers around the world. The development of 'Just in Time' techniques in manufacture means that both the physical and financial supply chains are critical – if a small supplier cannot deliver its component on time, it could ultimately lead to the corporate missing its sales and revenue targets. Being able to finance suppliers along the chain, to ensure they can continue to supply will help to prevent such a situation.

Corporates want a single channel by which to connect to all of their bank partners, but a lack of standardisation has proved to be a significant challenge. A bank in China will operate on different standards and require different formats from their corporate customers from a bank in the UK, for example. As corporates globalise this too, presents a problem.

To overcome these problems, TietoEnator has been active both in ISO20022 standardization and implementation of corporate-to-bank service together with leading edge banks. TietoEnator's on-demand B2B integration services exchanging more than 500 million transactions annually include also online conversion services. This "any format in – any format out" approach makes it easy for corporates to join the service, without having a need for large IT investments."

The role of banks

A changing regulatory environment, globalisation of banking and increased international trading by corporates are driving banks to change their payments models. Competition is intensifying in the banking industry and the implementation of the European Commission's Payment Services Directive in November 2009 will further intensify this competition by opening up the payments market to a new category of player, the Payment Institution.

Moreover, the credit crunch and ensuing economic downturn in many countries have resulted in financial institutions struggling to make money; indeed the one bright light has been the transaction banking space.

SEPA has created both opportunities and challenges for banks in the payments space. It is still early days but some patterns are emerging – the larger transaction banks are positioning themselves to be insourcers of payments processing, believing that by building scale they can make money out of SEPA. Regional and smaller banks are contemplating outsourcing or specialisation in order to survive in the payments world. The commoditisation of payments brought about by SEPA, the economic downturn and advances in technology and standardisation have all posed a fundamental question for banks – "Do we stay in the payments business or do we get out?" For many years payments was considered to be what banking was all about; the fact that is now being questioned highlights the profound changes that are taking place in the wake of SEPA in the payments industry.

CASE STUDY

The Royal Bank of Scotland

As a global transaction bank, The Royal Bank of Scotland (RBS) supports its customers with cash and liquidity management capabilities as they move money globally, says **Gary Wright**, Head of International Cash Management Products and Development at the bank. RBS must do this in a challenging environment, where payments are commoditised and competition and regulatory demands are increasing.

The introduction of SEPA Credit Transfers has been a further step in enabling corporates to move money more efficiently across borders in Europe and already, says Wright, corporates are asking their banks "What is next?"

In the immediate future is the PSD, which will ultimately require banks to provide their corporate customers with full transparency and stated finality of payment. The PSD has generated heightened activity in the payments space, says Wright, as banks consider their strategies and whether to insource or outsource payments processing.

"We now have in Europe a legal framework and a series of initiatives that are designed to move money around more effectively and to provide greater transparency for corporates in managing cash," he says. "There are also potential developments that will be driven by the evolution in technology and particularly the move to real-time information."

Corporates are centralising their treasuries, taking advantage of developments in technology and standardisation, but in doing so, says Wright, they are often constrained by IT budgets. This provides a great opportunity for banks to deliver services that will help corporates to more effectively manage their cash and liquidity and also mitigate risk.

"Banks must put clients at the forefront of any of their SEPA developments," he says. "The banking industry must raise the bar and conduct more consultative discussions with their corporates in order to understand how to develop services that will benefit their business."

Banks have spent years decoupling remittance information from transaction data, says Wright and it is now time to converge the two again. If money can be moved with such information using standard formats – through the deployment of e-invoicing – then banks will be able to offer end-to-end STP, rapidly delivering information to where the corporate wants it. This, says Wright, is where value can be added in the payments process.

SEPA, SWIFT connectivity and e-invoicing can collectively deliver value and provide the framework for further initiatives. Automating the financial supply chain will optimise how Accounts Receivable and Accounts Payable departments manage cash. Corporates want more streamlined AR and AP processes, and are under regulatory pressure to be more efficient and transparent.

One of RBS' solutions for corporates is based on a SWIFT service bureau, giving users a single point of contact, service, pricing and standards development. "Corporates like the idea of using a bureau that can take in data in any format, convert it into a SWIFT standard message and send it on to banks," says Wright. "They like the idea of using the SWIFT network and the efficiencies it delivers, but they don't want to maintain an inhouse application to do that."

The bureau service is not solely about communicating SWIFT messages to banks; Wright says corporates will be able to maximise their SWIFT connectivity to aggregate data and better manage cash and liquidity. Going forward, more services will be built on to the offering, including AML controls, for example.

"As SEPA begins to have more of an impact on the payments space, banks will have to decide how they position themselves," says Wright. "RBS believes payments are the lifeblood of transactional banking and there is a great deal we can do to support our customers' trading activities."

Swedbank

Nordic banks have stolen a march on their counterparts elsewhere in Europe when it comes to e-invoicing. The collaborative nature of many developments in the region has enabled financial institutions to pool their resources and come to market much faster with services than their European counterparts.

Swedbank, for example, is offering a business-to-business, e-invoicing solution that covers all corporates from the very large through to small businesses. The service ranges from a Web portal up to solutions that can integrate invoice information into corporates' ERP systems. "We are not big countries in the Nordic region, and by working together we can reduce development costs. When you work together, developments are always much easier," says **Elisabeth Johnson**, Head of Clearing and Settlement at Swedbank.

Swedbank's B2B e-invoicing offering is based on white labelled on-demand service from TietoEnator, with received the IDC EMEA Award for ICT Innovation in 2007.

The bank has implemented a central SWIFT messaging hub, ProSwitch, across seven banks in the Nordic and Baltic regions. "This is the first common project done at a group level within Swedbank and it was a huge undertaking," says Johnson. "Cultural and system differences presented a real challenge, but we were able to overcome these and create an infrastructure that was ready in time for the introduction of SEPA."

Swedbank had, in fact, begun development on the common hub for SWIFT MT messages before SEPA was under way. The bank was able to include the SEPA requirements within the hub, using the XML ISO 20022 standard.

"We now have a common messaging hub for the Swedbank group, which handles external transactions for SEPA as well as internal transactions, where, say, a customer in Estonia wants to send a euro payment to one of its suppliers in Stockholm it can send the message through the hub without going into the SWIFT world," she says.

The infrastructure will enable Swedbank to develop products and services that will help the bank to compete in the SEPA world. "SEPA makes the payments space much more competitive, but it also enables banks to do things that we couldn't do in the past," she says. "ACHs can make payments clearing faster and smarter – already Swedbank is able to clear payments more times a day than previously."

The payments space will continue to change for the next few years, says Johnson, as ACHs consolidate and corporates begin to adopt XML standards. "PSD will also increase competition. In this environment, the services banks are able to offer will become very important for survival. Banks will need smart solutions that are cost efficient."

Conclusion

The initial focus on SEPA was cost, but as banks seek to recoup the investment they have made in complying with SEPA, attention has turned to revenues. Europe's banks are at the start of a road that will take them towards e-invoicing, supply chain finance, real-time information and the ability to compete in a rapidly changing environment.



TietoEnator is a professional service company providing IT, R&D and consulting services. With approximately 16 000 experts, we are among the leading IT service companies in Northern Europe and the global leader in selected segments. We specialize in areas where we have the deepest understanding of our customers' businesses and needs. Our superior customer centricity and Nordic expertise set us apart from our competitors.

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