Towards the Single Euro Payments Area

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Marianne Palva
Adviser
Financial Markets and Statistics

The primary objective of the Lisbon Strategy adopted by the European Council in March 2000 is to make the European Union by 2010 'the most competitive and dynamic knowledge-based economy in the world, capable of sustaining growth with more and better jobs and greater social cohesion'. The Single Euro Payments Area is one of the prerequisites for achieving this objective. The European Commission estimates that its establishment could bring the EU savings of EUR 50–100 billion every year.

Efforts to create the Single Euro Payments Area have been considerably stepped up over the past year. The first steps towards a more efficient system of payments in the EU were, however, already taken shortly after work began on creating the Single Market[1]. The European Commission discussed payments harmonisation and increasing competition in several publications, and in 1997 it issued a Directive on cross-border credit transfers[2], the aim of which was to harmonise certain aspects of payments transmission within the EU and improve cross-border credit transfer services for both private individuals and small and medium-sized enterprises.

The first concrete step towards an EU-wide single payments area was the commencement of the third phase of European Economic and Monetary Union at the beginning of 1999. The euro was introduced as an accounting currency at this time. Also introduced at this time was the EU central banks' TARGET system, which enabled the real-time transmission of euro-denominated payments throughout the EU. The private EURO 1 payments system[3] also began operating at this time. However, TARGET and EURO 1 handle mainly large-value payments, and their introduction therefore did nothing to improve payment services for small customers.

Despite growing pressure from the European Central Bank and the Commission, no significant progress was made in the transmission of small-value payments until December 2001, when the Commission issued a regulation under which banks were to levy the same charges for small-value credit transfers and card transactions to and from other EU countries as for similar transactions within their domestic market. This led the banks to begin practical work on creating a

1 The Single European Act came into force on 1 July 1987. Therein, the Single Market is defined as 'an area without internal frontiers in which the free movement of goods, persons, services and capital is ensured in accordance with the provisions of this Treaty [= Treaty establishing the European Community]'. The Single Market was to be in operation by 1 January 1993.

2 European Parliament and Council Directive 97/5/EC of 27 January 1997 on cross-border credit transfers.

3 For more information on EURO 1 see the Euro Banking Association website at: http://www.abe.org/.

Single Euro Payments Area (SEPA), leading in 2002 to the establishment of the European Payments Council (EPC)[4]. This is a cooperative body with representation from European bankers' associations and large banks operating in the EU.

The introduction of euro cash at the beginning of 2002 removed in practice the obstacles to cash payments within the euro area, but differences still remained in payment transmission. Only for cross-border small-value payments and the use of payment cards in foreign ATMs did charges come down to the same level as domestic charges as a result of the regulation. A great deal of effort is still required before the transmission of payments throughout the euro area is as efficient as, for example, domestic payments are at present in Finland. The Commission has now increased the pressure for harmonisation by publishing a proposal for a Directive on payment services in the Single Market[5] and a consultation document[6].

In taking this action, the Commission seeks to promote the creation of an advanced and efficient euro payments area as part of the implementation of the Lisbon Strategy. It also wants to improve consumer protection, strengthen consumer confidence in all means of payment and ensure a level competitive playing field. The Directive on payment services is currently being worked on and should be ready during the coming Finnish EU Presidency. The ECB and national central banks are also seeking to foster the emergence of a Single Euro Payments Area and have been involved in close cooperation with the banking sector to this end. In February, the ECB published its fourth progress report[7] on the topic, and, in May, the ECB and the Commission released a joint statement to the press to promote realisation of SEPA[8].

Besides cash, the common means of payment within the Single Euro Payments Area will be credit transfer, direct debit and card payment.

The Single Euro Payments Area: timetable and means of payment

Working through the EPC, the European banking sector has drawn up a timetable for introduction of the Single Euro Payments Area and specified the common means of payment for inclusion within it. In addition to cash, these are credit transfer, direct debit and card payment. The terms 'SEPA credit

[4] Further information on the European Payments Council is available at: http://www.europeanpaymentscouncil.org/.

[5] Proposal for a Directive of the European Parliament and of the Council on payment services in the internal market and amending Directives 97/7/EC, 2000/12/EC and 2002/65/EC. Presented by the Commission on 1 December 2005.

[6] European Commission: Consultative paper on SEPA Incentives, 13 February 2006, available at: http://europa.eu.int/comm/internal_market/payments/docs/sepa/sepa-2006_02_13.pdf.

[7] ECB publication: Towards a Single Euro Payments Area – Objectives and deadlines (Fourth progress report), 17 February 2006, available at: http://www.ecb.int/pub/pub/paym/html/index.en.html.

[8] Statement available at: http://www.ecb.int/press/pr/date/2006/html/pr060504_1.en.html.

The aim for the end of 2010 is for the various SEPA means of payment to be adopted throughout the Single Euro Payments Area.

transfer', 'SEPA direct debit' and 'SEPA card' are used for means of payment that comply with the EPC specifications.

The Single Euro Payments Area covers the EU and EEA countries plus Switzerland. SEPA services apply only to payments in euro. The EPC timetable envisages the common means of payment in euro being introduced alongside the present national means of payment at the beginning of 2008. The aim is to dispense almost entirely with national means of payment by the end of 2010, with the Single Euro Payments Area adopting the various SEPA means of payment instead. If they so choose, banks will be free to offer additional supplementary services as well.

With the introduction of SEPA, all banks operating within the euro area will be expected to provide their customers with SEPA means of payment and also be equipped to receive payments made with them. It will be left for each bank to decide for itself how to arrange its transmission of SEPA payments. At the time of writing, these decisions have for the most part still to be taken. At present, there is one EU-wide clearing house for small-value payments (STEP 2) through which euro-denominated credit transfers can be made to all banks in the EU. STEP 2 is also developing the capability for handling common direct debits. At present, some national payment centres (eg Interpay[9] and VOCA[10]) have stated their intention to provide banks with SEPA payment services. To date, there are no confirmed plans for new, competing payment centres covering the whole of the EU. For the sake of competition it would be good if there were more service providers on the market.

There are already international payment cards that can be used not just in the euro area, but worldwide, while every country also has national card systems for use solely on the domestic market. These will have to be withdrawn unless they are developed to comply with the SEPA Cards Framework (SCF). All SEPA cards must comply with the SCF standards. The use of common standards will enable all SEPA cards to be used in the same payment terminals. The SCF also defines the standards for communication between merchants and the acquirers of payment transactions.

The reason for common standards is to enable merchants to freely choose an acquirer for their payment transactions from all the service providers operating within the euro payments area. At present, choice is generally restricted to, at best, service providers within a merchant's own country. This is because different countries observe

[9] Further information on Interpay is available at: http://www.interpay.nl/eng/Publications/SEPA_services_at_Interpay.asp.

[10] Further information on VOCA is available at: http://www.voca.co.uk/home/index.php.

different standards between the point of sale and the bank or other service provider acting as acquirer of a payment transaction. Some countries do not have any sort of common standards in use. At the time of writing we are not aware of any concrete plans for the launch of new cards aimed specifically at the euro payments area, but the Berlin Group[11] is exploring the possibility of linking together the present national card systems.

Finland's SEPA implementation and migration plan

The ECB requires each country involved in SEPA to prepare by the end of June 2006 a national plan setting out the transition to common means of payment in euro. In March, the Finnish Bankers' Association and the Bank of Finland published Finland's national SEPA implementation and migration plan[12]. The Finnish Bankers' Association held primary responsibility for preparing the plan, with the Bank of Finland contributing in its role as oversight authority and a developer of payment systems. The plan has been approved by the Payment Systems Steering Group (MJO), an umbrella organisation for cooperation on payment issues between the Bank of Finland, the Finnish Bankers' Association and banks offering payment services in Finland. The MJO will monitor implementation of the plan and adjust it as required.

According to the plan, the customer of a bank offering payment services in Finland will be able to make and receive payments by SEPA credit transfer throughout the entire euro payment area. The identifier information in such transactions will be the International Bank Account Number (IBAN) and Bank Identifier Code (BIC) already in use in cross-border payments. In this respect there will be no real change from the present situation. However, the new standard in respect of SEPA credit transfers that will come into force at the beginning of 2008 differs from the national standard currently in force in Finland, and its introduction will therefore involve changes in both banks' and customers' systems. Moreover, SEPA credit transfers do not include all the information required by the services currently provided in Finland, which means that some aspects of existing services will not be extended to cover the entire euro payments area. For example, the reference number standard and the transmission procedures for payment of wages and pensions are not included in their present form within the SEPA credit transfer framework. However, Finnish banks are keen to maintain their present level of service and help

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[11] Further information on the Berlin Group is available at: http://www.berlin-group.org/.

[12] Further information on Finland's SEPA implementation and migration plan is available at: http://www.pankkiyhdistys.fi/english/index.html.

The Payment Services Directive will increase the transparency of payment services pricing.

in the formation of a European reference number standard.

SEPA direct debits differ considerably from the system currently in use in Finland, which is based on payment authorisation given by the payer to his bank. In a SEPA direct debit, the payer will directly authorise the invoicer to debit his account without a control check by their banks. Authorisation can cover either regularly repeated or one-off debits. As proposed, however, the debit will not be final, as it is in the existing Finnish system; the payer will be able to cancel the debit for a period of six weeks from the date of debit. Finnish banks are doubtful there will be much interest in SEPA direct debits in Finland, but will seek to offer this service from the beginning of 2008 and supplement it with additional services to maintain their present level of service and safeguard the management of risk. The banks believe the present Finnish direct debit will give way over time to more advanced forms of payment such as, for example, e-invoicing. The framework does not preclude the use of systems more advanced than the SEPA objectives.

All international payment cards issued by Finnish banks (Visa and MasterCard) already fulfil the requirements for SEPA cards. They can already be used to withdraw cash and make payments both throughout the euro payments area and worldwide. In addition, before the launch of SEPA, general payment cards must already be equipped with the EMV chip payment capability required of SEPA cards.

In contrast, existing Finnish bank cards issued for use domestically are not SEPA-compliant. Under the SEPA implementation and migration plan, the issuing of new bank cards will cease at the latest by the end of 2007, and already issued cards will be usable at the latest until the end of 2010. At the time of writing we are unaware of any plans for the introduction of new, SEPA-compliant cards in addition to the existing international cards. The usability in Finland of SEPA cards based on EMV chip payment technology will depend on the speed with which merchants introduce machines capable of accepting such cards. The aim is for comprehensive coverage in the Finnish market by the end of 2010.

SEPA challenges in the long term

Implementation of SEPA to the extent and in the form agreed to date in the EPC will not bring any significant added value to payments from a Finnish perspective, nor will it improve the efficiency of payments transmission in Finland. The Payment Services Directive will, however, increase the transparency of payment services pricing. This could lead to higher prices for some services, but will on the other hand reduce hidden cross-subsidies, making it easier to compare prices between different service providers.

Finnish banks and the Bank of Finland have in different contexts emphasised the need for completely automated payment processing (STP)[13] through the entire payment chain, or at least from the payer to the payer's bank, from there to the payee's bank, and finally to the payee. In a more developed STP chain, the process begins with the payee electronically sending the payer an e-invoice. Completely automated processing requires the use of standardised reference data, but also standardised communication between banks and their customers. The latter is also essential in order to improve customer choice and increase competition between banks.

In the joint statement referred to at the beginning of this article, the ECB and the Commission point out that SEPA must be a forward-looking process involving the continuous development of payment services by exploiting the opportunities provided by new technology. They point to the example of e-invoicing, which raises the degree of automation and the efficiency of payments.

Estimates vary as to how much can be saved by automation of the entire payment process and increased efficiency, but over the euro payments area as a whole the final figure will be considerable. We mentioned above the Commission's savings estimate of EUR 50–100 billion per annum. Still larger sums have been quoted in reference to automation of the invoicing process as a whole.

The objectives that have now been agreed for 2008 and 2010 will establish the Single Euro Payments Area. There will nevertheless still be many challenges ahead before the Lisbon Strategy in respect of SEPA is fully implemented and efficiency achieved across the payment process as a whole so that the full benefits can accrue to consumers, businesses and the public sector.

Keywords: Single Euro Payment Area, SEPA, European Payments Council, SEPA implementation and migration plan, payment services

[13] STP = straight-through processing.