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on
SEPA Incentives

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This document is prepared as a basis for consultation and discussion with all stakeholders. It does not prejudice the final form nor content of any decision or position to be taken by the Commission.

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1. INTRODUCTION

1.1. Aim of paper

The integration of the non-cash payments systems in Europe is the logical follow-up to the introduction of the euro. It is expected that the realisation of the Single Euro Payment Area will result in tremendous gains and potential savings for society and bring benefits to all stakeholders. An efficient single market for payment services will increase competition, facilitate new business opportunities, the realisation of economies of scale and foster specialisation and innovation. Because there are such large economic benefits, the realisation of the Single Euro Payment Area is also of political importance. SEPA was always seen as a market-led process which would be supported by regulatory action where necessary.

Without preconceived ideas, this paper explores ways to support, underpin and enhance the self-regulatory activities of industry. However, whilst the preference is for market-led solutions, regulatory action is not ruled out where there is a risk of market failure that could put the economy wide benefits of the project at risk.

Given the importance of the SEPA project and the role to be played by the European Commission and the European Central Bank in its successful development, at service level Commission and ECB staff are engaged in increasing co-operation and coordination of SEPA related work-streams. As a practical example of this cooperation, both institutions have undertaken close consultation in the preparation of the present paper as well as in the Eurosystem's Fourth Progress Report on SEPA. Both institutions have a shared vision for SEPA and have identified the same issues that could undermine its success.

The Single Euro Payment Area requires the removal of legal, commercial and technical barriers that keep national markets apart. The legal barriers are addressed in the proposal for a Directive for a New Legal Framework (NLF) for Payments in the Internal Market¹. This proposal has been adopted by the Commission on 1 December 2005 and is now in the hands of the Council and the European Parliament. In order to contribute to the realisation of SEPA according to deadlines that have been set for the project, it is of crucial importance that the NLF is approved by the end of 2006. This paper does not mean to interfere in any way with the adoption of the NLF. The focus of this paper is rather on the current self-regulatory initiatives of industry towards SEPA in order to ascertain whether those initiatives will be sufficient to realise the vision of the European Commission for SEPA (this vision is described in Section 2 of this paper).

After Regulation (EC) No 2560/2001 obliged bank to charge equal prices for cross-border and domestic payments, the banking industry reacted quickly by creating the European Payments Council in 2002. The banking industry has since then put considerable effort and resources into ensuring that SEPA will be realised through self-regulatory, market-led actions. The EPC work to date has been to design European schemes for interoperable payment solutions, with regard to both technical and commercial standards and infrastructures. The future work of the EPC will mainly be to finalise the design and to oversee the implementation of the solutions developed.

¹ http://europa.eu.int/comm/internal_market/payments/docs/framework/com_2005_603_en.pdf

The EPC work covers three fundamental areas of European payment products. It has developed a set of inter-bank arrangements (schemes) and contractual and technical arrangements to facilitate the development of European credit transfer and direct debit products by banks for the benefit of their customers. It has also developed framework principles which card schemes should follow. Additional follow-up work of the EPC is envisaged to ensure these schemes and framework are taken up by banks and users. These work streams are described in Section 3 of this paper.

Section 4 of this paper compares the objectives of the EPC work with the Commission vision of SEPA. This concludes that the Commission largely shares the overall objectives and market driven process of the EPC. However, it also examines the gaps between this vision and the EPC work. These occur in a number of areas. Firstly, within the definition of schemes and frameworks, that define the inter-bank arrangements for core and basic services to be offered by banks. The Commission is afraid that products based on the schemes as currently developed may not be persuasive to all end users.

This may be connected to the governance of the EPC which is exclusively by banks. It may also be connected to the late and relatively modest consultation of all end users and their requirements. This may result in a problem in the phase after the implementation of the products by banks: will users adopt these products? Unless users see advantages in these EPC products they will not adopt them and the current SEPA project will be a failure.

Section 5 of this paper examines the important role of the European Central Bank and its Eurosystem of National Central Banks in the SEPA-process.

Finally, Section 6 of this paper analyses areas where it is considered that regulators may be able to support, underpin and enhance the market-driven process of industry, particularly in relation to the gaps described in Section 4 between the Commission vision and the EPC work. Whilst no decision have been made at this stage, this section requests input from all stakeholders to determine whether any regulatory activity or other measures could help: guarantee the success of SEPA; ensure that where needed standards are set to create level playing field for competition; assure its full economic potential in realised; and minimise migration costs.

Whilst feedback on all parts of this paper is welcome from all stakeholders involved (banks, other payment providers, corporates, commerce, small and medium sized businesses, consumers, governments, infrastructure providers, processors, scheme owners, etc.), the Commission's services are particularly interested in replies to the questions posed in Section 6. Answers to these questions will help the Commission decide what, if any, further regulatory action may be needed to help ensure the success of SEPA.

1.2. Consultation process

It is important to stress that this first draft does not contain any fixed ideas. This consultation paper casts the net as wide as possible with the aim to generate maximum insight in all areas and looks for feedback on possible recommendations and suggested ways forward. As part of its commitment to the process of better regulation the Commission will extensively consult all stakeholders in the market in a second round by the summer of 2006. Stakeholders are particularly encouraged to answer the questions in Section 6.

A hearing is planned on SEPA incentives for 3 October 2006. This hearing will also provide a platform to publicly discuss the issues and recommendations with all parties involved.

In parallel to the consultation process the Commission continues to monitor market developments, maintain the dialogue with market parties in particular the EPC, and continues to analyse the issues at hand. The Commission also plans to launch an External Study on the costs and benefits of SEPA and possible problems and solutions during 2006. Together they will provide input for a Communication by the Commission tentatively before the end of this year. This Communication will outline progress on SEPA and highlight the areas where the Commission considers regulatory action could be needed. Any subsequent regulatory action proposed will, in line with better regulation, be accompanied by an impact assessment.

2. VISION OF THE EC

2.1. Vision of SEPA

SEPA is the integrated market for payment services which is subject to effective competition and where there is no distinction between cross-border and national payments within the euro area. This calls for the removal of all technical, legal and commercial barriers between the current national payment markets so that these become a single 'domestic' payments market for the whole euro area. The creation of a Single Euro Payment Area, providing European citizens and businesses with low-cost, efficient, modern and reliable payment services contributes significantly to the Lisbon Agenda to make the EU “the most competitive and dynamic knowledge-driven economy by 2010”.

In practice the Single Euro Payment Area means that consumers, SMEs and corporates can use payment services that meet their requirements and that can be used across Europe in a uniform way. Payment service users will then be able to choose to use the payment service provider with the most compelling offer independent of country of origin. In a SEPA environment, payment service providers can compete within the wider EU market on a level playing field.

Within SEPA, payment service providers will be entitled to access a number of infrastructure providers for payment processing in a competitive environment. For competition between payments processors to be possible on a level-playing field, there is a need for common formats, messaging and communication standards. SEPA will be based on open standards, and open governance arrangements for activities in the collaborative space between payment service providers. This will make it possible to leverage the possibilities offered by new technologies such as IP network, open standards, etc. It is expected that the processing market will experience consolidation in the years ahead, because of the potential for economies of scale and scope to be realised in that market. It is desirable, however, that the SEPA landscape will still feature a number of competing payments processors.

In SEPA, customers will be able to benefit from the end-to-end automation of the payment chain, so that they can also rationalise the internal processes linked to it. SEPA is a good opportunity to bring payment processing to the state-of-art level, making use of the most recent technologies and available market developments, e.g. mobile phone penetration approaching 100% in the EU and widespread use of internet.

SEPA should foster creativity by payment service providers in their product offerings through the introduction of SEPA-wide payment related services, in particular e-invoicing. The Commission attaches particular importance to SEPA providing a springboard to launch e-invoicing in view of the huge potential savings that this can generate for the whole EU economy and so contribute to the Lisbon process. Potential savings of dematerialisation of the wider transaction processing chain are conservatively estimated at EUR 50–100 billion. Banks could greatly benefit from this. Experience from Member States shows a compelling business case for banks to provide these value added services. (An initial assessment of the potential benefits of SEPA in general and e-invoicing in particular can be found in Annex 4).

Beyond and above the fact that SEPA payment products should be competitive with the current best of breed products², it is expected that payment service providers will actively create new business models, develop new value added products and services in order to retain competitive advantage and service their clients better. Pricing should be transparent and reflect costs so that users have an incentive to use the more efficient instruments. Through competition, costs and therefore the overall price level of payments should over time decline. It is to be expected that effective competition between payment service providers will as well play a role in eliminating differences between the prices currently seen across Europe.

Improving efficiency of all payments will also be enhanced in SEPA through a gradual repositioning of cash and other costly instruments such as cheques and their replacement by more efficient electronic payments with straight-through-processing.

By creating open standards that overcome technical and commercial barriers and by fostering effective competition, improved payments service levels will benefit the end-users of these services, namely, consumers, business and governments, with transparent and lower prices. SEPA will allow the payments industry to become more efficient, thereby providing significant savings and benefits to the wider European economy and facilitating the attainment of the full potential of the Single Market.

As the main goal of SEPA is economic, its overall success will be judged by the economies it delivers. It will be deemed a success when the full potential of economies of scale and scope and competition are realised with the euro-zone. This means savings for users and lower costs for providers. This vision does not allow for developments that will only take us half the way. A mini-SEPA that only delivers solutions for cross-border payments in Europe is not acceptable. This will only add an extra payment system on top of the 25 national systems that we already have and thus increase cost and not create great benefits, or realise economies of scale and scope. Competition on the European level will not be possible as all payment systems remain nationally fragmented. It will result in a situation where there are new SEPA products on offer, but very few users will adopt them for domestic transactions. A real SEPA will change substantially current domestic payment markets to the benefit of both users and providers.

² Best of breed means the economically most efficient product/service design taking into account all stakeholders' cost and benefits and also future development needs.

2.2. Vision on the self-regulatory process

The Commission supports to the greatest possible extent continued self-regulation by industry, but given the importance and size of the social and economic benefits of SEPA, the Commission reserves the right to introduce or propose necessary legislation to achieve it. However because payments are a network industry, self-regulation inevitably involves cooperation between all providers who are also competitors. An infrastructure needs to be developed which requires common investments and common standards. This need for competitors to cooperate in turn entails responsibilities in this process and of course the obligation to respect competition law. The self-regulatory process should also bring about a process for the continuous development of the infrastructure for end-to-end (sender to receiver) payments.

A market-driven and self-regulatory is the preferred approach, because it allows the decisions to be made by the parties that have to act and that have most relevant information. It also makes future developments easier to manage. This, however, requires that all sources of information have to be tapped into. The self-regulatory process cannot be considered successful if it does not include effective consultation of all stakeholders or at least a representative sample in both the design and implementation phase. Effective consultation also greatly promotes user adoption of the new products and improves legitimacy of the process. In all standardisation processes it is therefore essential that the interests of users as well as providers and other relevant stakeholders be appropriately represented in the governance structure which is responsible for standard setting.

Furthermore, governance of the self-regulatory process cannot be in the hands of an exclusive club. Non-bank payment service providers will have to be involved and allowed to participate on a non-discriminatory basis.

To sum up, for competition in network industries to succeed and deliver the expected huge savings for the EU economy three basic criteria must to be met:

- there must be common standards which are set in an open, transparent and accountable process which can also revise or adapt them in future as necessary;
- there must be infrastructure available that are collectively characterised by full technical and commercial interoperability, and
- there must be transparent cost-based pricing to encourage the use of efficient payment instruments to the detriment of expensive payment instruments.

While SEPA will increase competition, the Commission is convinced that there is a business case for banks to develop best of breed SEPA products and use these as a basis for developing value added services, such as real time payments and e-invoicing.

The Commission believes that SEPA should remain primarily a market-led process. However, in view of very substantial potential economic gains that SEPA could deliver to society as a whole, the Commission reserves the right to take regulatory action and enforce competition law if these gains or effective competition are put at risk.

3. OVERVIEW OF THE RESULTS OF SELF-REGULATION TOWARD SEPA

3.1. EPC timing and milestones

The EPC has defined three phases in its project to realise the Single Euro Payment Area: a design, an implementation and a migration phase. At present the design phase is approaching its end. The schemes and frameworks and necessary standards are expected to be adopted by the EPC Plenary meeting of 8 March 2006. After that the banks and related institutions are expected to implement these schemes, frameworks and standards and to develop SEPA products on the basis of them. This phase should end by 1 January 2008 when SEPA products will first become available to customers. Then the migration phase will start in which adoption of SEPA products starts. This should lead to an irreversible uptake of the new SEPA products reaching critical mass by the end of 2010.

The Roadmap 2004–2010: "Realisation of the Single Euro Payments Area" (December 2004) confirmed the commitment of European banks to the EPC process to realise SEPA through self-regulation. In the Roadmap principles are laid down for the way the market is to be organised in SEPA. One of these principles is vigorous competition. In the Roadmap principles are laid down for the way the market is to be organised in SEPA. One of these principles is adequate competition.

One suggested way to comply with this principle is to require a separation of schemes from infrastructures. In the Roadmap the EPC has decided to separate scheme and infrastructure, at least as a matter of principle. For this separation it is necessary to establish a Scheme Management Entity. At national level there is often a historically developed bundling of processing and scheme management services under one bank-controlled collective institution. This bundling has been under pressure and criticism from competition authorities in some Member States. A split between scheme and infrastructure makes it possible to set objective requirements and create a level playing field and competitive market both for payment service providers and for processors/infrastructure providers.

The Scheme Management Entity will have a role in definition, change management and enforcement of scheme rules by all participants and arbitration. There can be one Scheme Management Entity for all schemes or there can be one management entity per scheme. What relationship a Scheme Management Entity will have with regard to EPC Frameworks is not clear. The ownership, governance and control over the Scheme Management Entity have to be decided upon.

In the Crowne Plaza Declaration of 17 March 2005 the EPC reiterated its commitment to building the Single Euro Payments Area (SEPA). The EPC declared that it will deliver a Pan-Euro Payment schemes for electronic credit transfer and for direct debits and that it will design a Cards Framework to define a single market for cards. Both were planned to be operational by January 2008 and offered by the vast majority of banks. It is expected that by 2010 a critical mass of transactions will naturally migrate to these payment instruments such that SEPA will be irreversible. "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."³

³ Crowne Plaza declaration by the European Payments Council, Brussels, 17 March 2005.

The EPC recognises that the deadlines for these milestones are tight. The design phase is soon to be concluded in order to allow the banking community to develop products complying with SEPA requirements in time. Once the products are made available by the banking communities, their adoption should be a market-driven process dependent on user interest.

3.2. Work to date: design and governance

The European Payments Council was established in 2002 by the different EU banking communities in order to realise the Single Euro Payment Area through self-regulation. In 2004 the EPC Charter was approved, which established the governance structure of the EPC. The decision making body in the EPC is the Plenary⁴.

The Plenary established several working groups to address specialised areas. The activities of all current working groups are governed by the Terms of Reference approved by the Plenary in October 2004. They will be operational until June 2006. The current working groups are:

- WG Electronic Credit Transfer
- WG Direct Debit
- WG Cards
- WG Cash
- WG OITS (Operational, infrastructure and technical standards)
- Legal Support Group
- Roll Out Committee

(In Annex 1 a brief description of the objective and deliverables of the different groups is given.) The WG Credit Transfer has two task forces one for e-payments and for m-payments. Under the OITS there are a number of task forces working on specific issues, such as security of payments.

3.2.1. Scheme rulebooks for credit transfers and direct debit

The Rulebooks define a complete set of business rules, practices and standards, which will govern the SEPA schemes for a core and basic, credit transfer and direct debit (CT and DD). The Rulebooks contain provisions on the scope of the scheme, the roles and responsibilities of the participants, business and operational rules and the legal and contractual framework. The Rulebooks are intended to ensure full interoperability in the bank-to-bank space and intend to leave room for competition in the bank-to-customer space, although obviously some elements in the customer to bank space have to be defined as well, e.g. required data to be submitted to the bank in a SEPA credit transfer

⁴ The Plenary is composed of representatives of member banks and three representatives of the ECSA's (FBE, EACB, EASB). The basis of seat allocation is based on transaction volumes per country, so that the market reality is reflected and a fair representation of all banking sectors, and types of banks is achieved. In total there are now 63 seats.

order. But apart from the requirements, in the customer-to-bank space, banks can develop their own competitive product offering as well as value added services.

The Rulebooks for Schemes Credit Transfer and Direct debit (version 1.0) were approved by the EPC Plenary in September 2005 for consultation among national banking communities. The process of national consultation (including stakeholders) was to be concluded by 11 November 2005. A number of improvements in the schemes have been identified through the consultation.

- (1) There is a need for an urgent or time-critical credit transfer scheme next to the core and basic scheme that ensures same-day settlement of an urgent payment.
- (2) There is a need for a business-to-business direct debit scheme (that allows for shorter refund periods as needed by corporate payment service users).
- (3) There is a need to develop a different additional routing process of the direct debit collection process (storing the mandates not with the creditor but with the debtor bank.) These issues emerged after the consultation of national banking communities and the EPC is currently addressing them.
- (4) Finally, a solution for e-signatures in relation to direct debit mandates was identified. The EPC is also working on these issues and aims to propose a solution by September 2006.

The dialogue with some stakeholders (EACT) is continuing.

3.2.2. *Adjacent issues*

There are a number of additional adjacent issues that need resolution to ensure Europe-wide interoperability once the Rulebooks are complemented.

Technical standards. In a collaborative effort with SWIFT, a SEPA data model is to be developed based on international, global open standards for the exchange of data. Standards and the SEPA Data Model incorporating the proposal to use UNIFI (ISO 20022) XML standards are ready for approval and national consultation. Expected completion is February 2006. (See Annex 2 for further elaboration of the current practice of standardisation in the financial services industry.)

The EPC also developed a framework for clearing and settlement mechanisms processing infrastructure. This framework has been reviewed by EPC Roll-Out Committee (see below). The expected completion is before the March 2006 Plenary.

A legal review on competition issues and initial legal review by external legal counsel was completed by end-November in readiness for possible amendments and next steps e.g. dialogue with DG Competition. Completion is end November 2005

Adherence Agreements will have to be signed by banks if they want to participate in a SEPA Scheme and commit banks to abide by the rules of the scheme. These agreements are currently being drafted. These Adherence Agreements will be discussed in the Legal Support Group and the EPC Roll-Out Committee and submitted to EPC Plenary. Completion is expected mid-January 2006.

A project for *Interchange Fees for Direct Debit* project was initiated in late 2005 by the Plenary. It has been agreed to develop a possible model for interchange by end February 2006.

The Working Groups active in these adjacent issues are scheduled to finalise their recommendations by end-January 2006, including those points resulting from the external legal review. New drafts of the Rulebooks on CT and DD (version 2.0) are to be sent out to EPC members and Communities in early February 2006. It is on the basis of these Rulebooks for CT and DD and the adjacent issues that individual banks and/or national banking communities will develop the SEPA products to be commercially launched by 1 January 2008. The Rulebooks and adjacent deliverables are scheduled to be approved as a 'package' at the EPC Plenary on 8 March 2006. Approval by that date is regarded by the EPC as necessary in order to allow the banks sufficient time to develop products and introduce them timely.

3.2.3. *SEPA Cards Framework (SCF)*

For cards, the EPC does not envisage developing a European scheme because there are already a number of schemes available. The framework thus sets general principles for the market which should be sufficient to allow the development of SEPA by market forces.

Therefore, the SCF spells out high level principles and rules which, when implemented by banks, schemes, and other stakeholders, will enable European customers to use general purpose cards to make payments and cash withdrawals in euro throughout the SEPA area with the same ease and convenience as they do in their home country. There should be no differences whether they use their card(s) in their home country or anywhere else within SEPA whether it is at an ATM, POS or a 'card-not-present' transaction (e.g. using a card to pay for a purchase over internet or telephone orders).

Banks have to commit to the SCF as issuers: i.e. offer SCF compliant cards (with EMV) from 1 January 2008 onwards, phase out non-compliant cards by end 2010. As acquirers, banks must offer to merchants from 1 January 2008 onwards the option to acquire SCF compliant card transactions from one or more compliant schemes. Banks also have to ensure that the payment scheme(s) of which they are member(s) are SCF compliant by 1 January 2008. More importantly, the SCF seeks commitments from card schemes to make an effort to become compliant with the Framework. They have to commit and submit an implementation plan to the EPC and adjust their scheme according to the requirements laid down in the Framework (see Annex 1).

The Cards Framework identifies the need for open standards to be defined for card payments. Currently these standards are proprietary, but in SEPA they should be open and provide the basis for effective competition in processing. To date, the standardised interface is the card to terminal interface (EMV-standard). Terminal to acquiring-processor (switching and authorisation), acquiring-processor (switch) to bank and acquiring-processor to clearing and settlement are yet to be developed. A common terminal certification process for SEPA cards could reduce the cost of terminals considerably.

A legal review (in particular as regards competition aspects) was completed in early 2006. Commitment and implementation plans by national banking communities were expected to be prepared by end December 2005. By February 2006 a majority of

communities has done this and a report will be delivered to the Plenary on 8 March 2006. The EPC will monitor deployments (but it will neither certify nor qualify schemes).

3.2.4. Roll Out Committee (ROC)

Implementation and migration issues are now under close review by the EPC Roll-Out Committee which convened for the first time on 21 November 2005. The purpose of the Roll Out Committee is to prepare and support the successful roll-out phase of the SEPA CT & DD Schemes, by coordinating and guiding national communities steering EPC implementation activities. Its deliverables are to ensure:

- a consistent implementation of SEPA schemes and framework across the board,
- compatibility with the Adherence Agreement (with the Legal Support Group),
- the relationship with infrastructure providers,
- a framework for the development of processing on the European level (Pan European Automated Clearinghouse, PE-ACH)
- a framework for the evolution of clearing and settlement mechanisms (CSM).
- proposals for (a) Scheme Management Entity(ies) (see below).

On 21 November 2005 the ROC approved the CSM Framework for national consultation and reported on the status of implementation organisations in EU12 countries (including links to Eurosystem). It also launched a study into Scheme Management Models.

4. COMPARISON OF VISION AND EPC WORK

4.1. Overall support for the EPC and its work

The Commission services welcome the creation of the EPC by the European banking communities. It shares its overall objectives, process and timing. In particular, it shares the views on

- The vision of SEPA (making euro zone equivalent to a domestic payment space)
- The process being as far as possible market-driven and self-regulatory
- The timing with the key dates of 2008 (availability of products by all providers) and 2010 (critical mass and irreversibility)

The Commission services also recognise the substantial progress made by the EPC, after initial set-backs and delays, and the enormity and complexity of the task. Therefore the Commission services wish to strongly help and encourage the EPC to complete its ambitious programme in a timely manner. The potential gains to the EU economy are too great for this to fail.

However, even though the Commission services fully support the EPC's work, there are a number of areas where there seems a gap between the vision of the Commission for SEPA and the current work of the EPC and the banking communities. These gaps are of such a nature that they should be addressed lest they prejudice the successful realisation

of SEPA and its gains to the EU economy. This section describes these gaps and Section 6 of this paper explores ways how these gaps could be filled to ensure a successful SEPA.⁵

This note does not directly address the competition law compliance of the EPC's initiatives, on which the Commission is required to reserve judgement, and falls under the competence of the Competition Directorate General.

4.2. Comparison of the vision and the EPC governance and standard setting

The payments industry is a network industry par excellence. Payment services can only be provided and competition function if all participants/competitors adhere to certain common technical standards and common (commercial and legal) scheme rules. These standards and scheme rules are being developed and implemented by cooperation between competitors. However, this right for competitors to cooperate carries responsibilities.

First, it goes without saying that such cooperation and outcomes must be consistent with competition law. Secondly, it implies a responsibility for banks under their governance arrangements, to ensure a proper consultation of other stakeholders in the payment system, in particular end users, as also stated by the EPC in the Crowne Plaza declaration, and also (independent) infrastructure providers. Thirdly, non-bank payment service providers should not be excluded from the EPC and its governance. Nor should it unduly favour a particular infrastructure provider while excluding others. Any measures taken which have a restrictive effect on the market need to be justified by efficiencies and limited to what is necessary to achieve such efficiencies, in accordance with competition law.

The principles of openness must be adhered to in this process, because otherwise the cooperative process could lead to solutions that are sub-optimal from a wider economy perspective and skewed in favour of the cooperating banks. The question of governance and the involvement of all stakeholders is therefore a fundamental principle for the Commission that needs to be resolved urgently.

The EPC, whose members are drawn from European banks and three of the European Credit Sector Associations, represents most banks in Europe. The Commission acknowledges that it has been a very considerable achievement for the EPC to manage such a change programme impacting in different ways on all banks in Europe. But it means that the current self-regulatory process is largely and exclusively a bank-led process. Other stakeholders have been involved only to a limited extent in the EPC processes. This leads to the identification of four gaps.

4.2.1. Lack of effective and timely involvement of end users

It has come to the attention of the Commission that a number of stakeholders feel there is to date a lack of effective and timely involvement of end users in the process to develop the schemes. Although the schemes are not final product offerings, on which end users

⁵ This analysis is based on the comparison between the EC vision and the EPC achievements so far. This is based on the version 1.0 of the rulebooks and frameworks for consultation. Definitive deliverables are expected from the EPC Plenary meeting on 8 March 2006. Inevitably, this assessment must be a snapshot of work in progress and the EPC is already addressing some of the gaps identified.

will experience, the schemes do define the customer space for service offering and also draw a line between what is core and basic and what will be value added. The self-regulatory process may not lead to satisfactory outcomes, if it does not include effective consultation of all stakeholders to establish their user requirements. Improving user involvement in the process not only enhances legitimacy of this process, it may also contribute to user adoption of the new products. The EPC has started consultation at the EU level with corporates (European Association of Corporate Treasurers). The Commission services understand that consultation of Eurocommerce on the SEPA Cards Framework will start in February 2006.

It has been argued that the development of the schemes concentrate on the required inter-bank rules, procedures and other arrangements that are of no importance to end users. According to that line of reasoning the users will have to wait until the banks offer SEPA products to judge and give their comments or 'vote with their feet'. This is unacceptable, because the schemes do set limits for what kind of products can be offered at a European level and draw a line between what is core and basic and what will be left to the competitive space of 'value added' services. It is, therefore, preferable to involve users at an early stage of scheme development to ensure user requirements are met.

The consultation of most stakeholders has been left to national banking communities. There were no guidelines or standards for this consultation and that has led to very different levels of involvement of different national stakeholders. The EPC documents for consultation were not published. This meant national banking communities could judge the need for input from end users and some thought it unnecessary.

This late consultation on version 1.0 of the EPC rulebooks has not yet finished. It is not clear how end-users concerns will be taken into account in version 2.0 or whether this version will be made public and open for further comment. Since consultation on version 1.0 was not "open" but largely left to national banking communities, there are no consistent standards for this consultation and the level of consultation of end users varies considerably between countries.

Hopefully version 2.0 of the Rulebooks (to be approved by the EPC Plenary in March 2006) will have benefited sufficiently from stakeholder consultation and input. If there are major outstanding issues, further consultation may be needed. The Commission services consider that ways will have to be found to make the consultation more open and transparent, both now and in the future.

4.2.2. Non bank payment service providers

Non bank payment service providers, such as the new Payment Institutions envisaged in the proposal for a Directive on payments, have not been included in the design of the new SEPA schemes and frameworks. They are currently excluded from participation in the schemes. This may be incompatible with Article 23 of the New Legal Framework as well as with competition law.

4.2.3. Lack of direct involvement of infrastructure providers and processors

Infrastructure providers and processors have to adjust to SEPA. EPC has declared that it aims at separating schemes from infrastructures and this may entail major changes for processors. They are, nevertheless, not directly involved in the EPC⁶, because they are not banks and they are therefore not always optimally informed. The majority of processors in Europe are bank-owned and as such have an advantage over independent processors. In consequence the issue of technical and commercial interoperability in processing may have to be further analysed in order to make sure that all possible routes to SEPA are being kept open and migration costs minimised.

4.2.4. Need for users cost-benefit analysis

Any assessment of economic efficiencies from introducing SEPA products in a given form must of necessity consider the benefits and costs for users.

4.3. Comparison of schemes for CT and DD with the Commission vision

The current version of the schemes provides a major building block for interoperability in the European market. The schemes define the rules; practices and technical standards to be used by all banks adhering to the scheme. The services of the Commission believe that room should be left for banks to develop value added services on the basis of the SEPA CT and DD. This opportunity is the best way to stimulate innovation and ensure that the payment industry in the EU is capable of responding to the Lisbon challenge by unleashing creative competition.

While the schemes are a very important achievement, the Commission understands that these are defined on the basis of the existing available services nationally, rather than being forward looking and ambitious. Mass payment services in many Member States has to a large extent become a commodity, which means that price is low and processing more or less a collective utility. The Commission is concerned that in markets where the 'best of breed' products are currently "commoditised", banks that migrate to SEPA will have to reintroduce value added services to bring the SEPA-scheme based products on a par with the existing national products.

SEPA payment services should be as good as or, preferably, better than what is current available in national markets. They must be forward looking to the situation after 2010 in order to best serve the mass payments market and so increase the overall efficiency of the EU economy. Only if the SEPA CT and DD products are best of breed will they have a chance of being adopted on a large scale by users to replace existing national products. If SEPA products are not adopted massively by users for domestic payments but become merely used for cross-border payments, SEPA will be a failure and the expected economies of scale and scope will go unrealised.

The Commission services have concerns that the schemes, as currently defined in the CT and DD rulebooks (version 1.0), aim at core and basic service levels only and could lead to a shift to a low common denominator of all existing schemes in Europe. It does not

⁶ With the exception of the (bank-owned) Euro Banking Association (EBA). This may put other infrastructure/processors at a disadvantage, since the EBA will have been able to participate fully in the EPC process.

ensure that the future SEPA products to be offered on the basis of these schemes are going to be 'best of breed.' On the contrary, there is a risk of product performance regression and continued national fragmentation of the market. Banks in countries that have a higher service level than the EPC scheme defines or requires, are free to continue offering the existing national service level as a value added service (with possible consequences for pricing) whereas currently this is a commodity.

It is, however, not the preferred approach for public authorities to establish what level should be considered as the minimum service level to be provided. In principle, this should be left to a competitive market through an open and transparent process of standard setting. It is doubtful whether the current level of EPC schemes will allow cross-border competition to make itself felt, nor will it necessarily force communities with a relatively low service level to improve it to remain competitive.

Instead of commenting itself in detail on the content of the rulebooks, frameworks and schemes, the Commission Services think that end users should be consulted in an open and transparent way as in effect the EPC rulebooks represent de facto EU standards.

4.4. SEPA Cards Framework (SCF)

The SCF raises concerns, because of the possible effects on competition resulting from the open approach chosen. In particular, there are concerns that application of the SCF entails a risk that the fragmented market will integrate and remove barriers but only at the cost of moving to a highly concentrated market in Europe.

Without prejudging the outcome of the sectoral enquiry that DG Competition is currently undertaking into the market for card payments⁷, it is clear that at the national level there is currently a high concentration as well, with only one national debit card scheme. While this may not have necessarily negatively impacted on efficiency, it may have done so in a number of cases. It is too early to tell how many competing card schemes an integrated European market will be able to support. However, migration that leads to decreasing service levels or increasing price levels is not acceptable.

The second issue with the Cards Framework is that it does not address two conditions for effective competition in the European market for card processing. Firstly, there are several standards to be defined in the processing chain of card payments. These standards should not be proprietary, because that may eliminate competition. It is not clear how the EPC envisages to deliver these standards, or, alternatively, why it believes that these standards can be left to the market to define.

Secondly, there has been little discussion with regard to the international card schemes on the principle of separation between schemes and infrastructure. The question how this can be enforced, in particular with regard to the international card schemes, has not been addressed by the EPC.

⁷ Consultation Document of DG Competition expected in March, hearing planned for summer 2006, with a final report following that.

A third, but more general consideration, is that competition in relation to the multi-lateral interchange fee paid by retailers, may operate in a perverse manner, for example competition between card systems can lead to a bidding up of the multi-lateral interchange fee.⁸

4.5. SEPA Infrastructure/processing

The EPC needs provide technical standards that will deliver interoperability at the European level. But on infrastructural issues and processing the EPC has so far provided only the framework for clearing and settlement mechanisms. The EPC has decided on the principle of separating scheme from infrastructure. This is welcome in that it may have the potential to enhance competition in the area of processing by objectively defining the requirements that processors have to meet to process payments of a given scheme. However, the role of the Scheme Management Entity is at this stage, still very unclear. And the objective requirements for processors have so far not been elaborated.

In addition, it is unclear whether separation alone provides sufficient guarantees for effective competition for processing, as there may be other commercial or legal barriers to effective competition that need to be addressed. Indeed, a number of the criteria currently proposed by the EPC itself for providing processing and clearing services seem to preclude competition on grounds which are neither self-evidently necessary nor proportionate.

4.6. Concerns with regard to milestones and adoption by banks

The activities of the EPC aim to overcome the fragmentation in the European market have so far been mainly in the design of solutions and the development of standards (on different levels). This design or standardisation process has taken place on all the issues where banks have to be able to work together efficiently; i.e. at the level of business practices and technical standards. There are, however, few guarantees that the standards developed will also be implemented by payment services providers and processors.

One issue is that the design has been executed mainly by bank payment experts which often have an exclusive focus on solving operational problems in the back-office. It is not clear that banks at the highest level have bought into the process and look open SEPA as a business opportunity. High-level commitment and co-ordination of the diverse interests of the banking industry is essential to avoid the risk of weakening commitment to change. All payment service providers will have to strategically define their position in the new SEPA environment and may have to develop new business models for this new reality. In the absence of business models banks may have strong incentives not to push forward SEPA. This may put into doubt the first key milestone of SEPA: the offer by all banks of SEPA products by 1 January 2008. In fact, the national banking communities have not mandated the EPC to act in this process which is left primarily to the national banking communities themselves.

Whilst the EPC has set up the Roll Out Committee for the purpose of monitoring and providing guidance to the national implementation processes, there are no other methods in place for ensuring take up of the SEPA schemes by payment service providers. There

⁸ See Gresham's Law of Payments: Talk by Mr. I.J. MacFarlane, Governor of the Reserve Bank of Australia, Sydney, 23 March 2005.

would seem to be a need for a tighter definition of deadlines and deliverables. For instance, it is not clear by when or how many banks should have adherence agreements, or when it will be checked whether banks/schemes are actually going to market SEPA products (after 1 January 2008). A credible adoption and implementation plan with sufficiently concrete details may be needed. The available national migration plans may not be sufficient.

Even if the SEPA products are successfully adopted by all banks in 2008, the plans for mass and irreversible migration by users from current domestic schemes to SEPA products by 2010 remain vague. The Commission agrees that this should be a market-led process. However, it is not clear how these can be monitored to ensure slippage is avoided or more importantly, what efforts banks and national banking communities will make to persuade users to adopt the new products or minimise the cost of migration to themselves and users (see point 4.7 below). The market-led process implies a convincing business case which does not seem to have been developed either from the cost or benefits side. In view of the potential overall gains of SEPA to the EU economy the Commission is convinced there is a macro-business case but there is a need to examine this at the micro level, if migration and mass take up are to be successful.

This then leads to the question what will happen to the EPC after it has delivered most (if not all) of its deliverables in the course of 2006. It may be given a role in the Scheme Management Entity which will manage the rulebooks and update them where necessary. The EPC lacks executive power to pursue the change process, which could risk delaying the introduction of SEPA. In order to keep the self-regulatory process going in the right direction in accordance with the agreed timetable, the banking community owners of the EPC may have to reconsider their position and methods.

4.7. Minimising cost of adoption/migration for users

For successful migration to the new SEPA schemes and frameworks, first and foremost, certainty is required about the deadlines and about the fact that all providers will have adhered to the schemes and offer the products on that basis. To minimise the cost of migration it is also necessary to look at the migration, or take up, processes that all different stakeholders will have to go through. Not all stakeholders have so far received guidance. This is unlikely to remain outside the remit of the EPC, which is developing a communication strategy to that effect.

For card schemes and clearing and settlement mechanism providers there are frameworks available that give some guidance. One important aspect in those frameworks, however, is a separation between scheme and infrastructure. This point may still require a lot of attention with regard to a number of detailed issues (technical and commercial) that might still render a 'visible' separation ineffective.

For end users, the picture is much more unclear. Corporates are now involved in the EPC-process with the consultation on the Rulebooks. This is important because they will have to invest in order to adjust their internal processes to match the new SEPA payment requirements. The Commission understands that SMEs and merchants have not been extensively consulted. This is particularly pressing for merchants as they will have to offer terminals that are able to acquire at least one SEPA card compliant scheme. Merchants may have difficulty adjusting, however, because they may not be sufficiently aware what will happen and what is expected of them. The Commission understands that consumers have also only been consulted at a national level in different ways. It is,

nevertheless, important that they are properly consulted and informed. They may have to adjust and must understand why and how. Consumers for instance, will have to start using IBAN and BIC for credit transfers. This will directly impact on their user experience. For the latter categories of end users, however, the scope of change may be rather limited as is their payment business.

As far as the Commission's services are aware, national banking communities have not devoted much attention to the issue of user adoption and have not analysed ways to reduce migration costs for users. Whilst some responsibility must be on users themselves, national banking communities need to take the lead and show convincing strategies to bring about change.

There is therefore a threefold risk to a successful SEPA take-up. First, SEPA products may not be compelling because of their service level (see 4.3). Secondly, stakeholders are not well-informed about the imminent changes and what is expected of them in terms of consultation and adoption. Therefore, there is a severe risk of non-adoption by users. Thirdly, banks or banking communities need to develop business models and convincing strategies for take-up.

Unless these problems are solved there is a risk that SEPA schemes may provide the basis only for cross-border payment solutions. This would lead to a situation in which national markets remain separated, competition will not improve, and savings cannot be realised. In other words, a mini-SEPA and failure.

4.8. Future orientation of SEPA schemes

SEPA is not a one-off process with the launch of the scheme currently under development. First, ways will have to be found how to ensure that these schemes are effectively managed. Secondly, the schemes will have to be modified to sort out teething problems. Thirdly, ways will have to be found to update and improve them over time in order to keep them up-to-date with technological progress and commercial expectations e.g. real time payments may become a normal standard product in the future. These roles seem to fall to the Scheme Management Entity.

However, there is as yet no clarity about construction of the Scheme Management Entity as envisaged in the Rulebooks for credit transfer and direct debit. There are apparently different schools of thought with regard to the role and design of the Scheme Management Entity. There is a risk that the Scheme Management Entity will not have an open and independent governance structure and that it is forced to move at the pace of its slowest participant. It is particularly important that the governance of and consultation by the Scheme Management Entity reflects the highest standards particularly for the updating and improvement of the schemes. There must be substantial changes from the closed, non-public process used in drawing up versions 1.0 and 2.0 of the current rulebooks.

Finally, SEPA generates a lot of momentum to improve payment systems. It opens a great window of opportunity for a technology leap. We should use this opportunity, be visionary and look beyond the borders of the traditional payment services sector. At least we should aim to reposition cash and cheques in payments. It is also important to point out the need for a long-term strategy for the harmonisation of bank account numbers. Currently IBAN and BIC are necessary for automating payments in Europe as much as possible. In the long run, however, a way should be found to harmonise account number across Europe in such a way that also facilitates customer mobility and ease of use.

Finally, e-invoicing is a major issue for the Commission. E-invoicing is sending invoices through an electronic medium, like internet or e-mail. E-invoicing will allow integration of the processing of payments and the administrative processes related to it. It is part of a wider development of dematerialisation in supply chain management. This issue, however, is not touched on by the EPC at the moment⁹.

E-invoicing can contribute to a major leap in productivity and efficiency going beyond just payments. Through enhanced application of information technology, invoicing is the link between internal company processes and the payment system. The potential economic gains are so large that they could make a significant and genuine contribution to the Lisbon process to make the EU a more competitive economy. Promoting e-invoicing and identifying the standards needed for it requires the commitment of a variety of parties to a common vision. Currently there is no such shared vision within the EPC. This means that new business opportunities for banks and payment institutions to provide value added services may be lost or their advent delayed. More importantly, large economies to society as a whole may not be realised. The Commission's services and the ECB attach the utmost importance to the development of SEPA in a way that is compatible and facilitating significant progress in this area. At a minimum SEPA should provide a springboard for e-invoicing; but ideally SEPA should be able to deliver at an early date a fully-fledged product capable of swift launch. (Annex 5 is a memorandum of Bank of Finland which contains an initial description of e-invoicing).

5. ROLE OF ECB AND NCB'S

According to the Treaty, one of the Eurosystem basic tasks is to promote the smooth operation of payment systems. To achieve this mandate the ECB fulfils three main roles in relation to payment systems: a catalyst role, an oversight role and an operational role. The Eurosystem actively monitors the work undertaken by the EPC to develop the SEPA and assists the banking sector by providing reports, speeches, interviews etc. In 2005 the Eurosystem organized high-level meetings with various stakeholders to work towards a common understanding of the goals of the SEPA and to obtain greater commitment from the banking industry in delivering the SEPA.

In its role as catalyst the Eurosystem is prepared to assist the banking industry in its creation of the SEPA to secure safety and efficiency. In this process the Eurosystem offers its expert and legal assistance and technical support in addressing relevant issues.

The Eurosystem, which in its oversight capacity actively monitor the SEPA migration, expects that national migration roadmaps are available during 2006 and considers playing a more active role if this is not achieved.

In principle, the ECB prefers to leave the development of SEPA to the banking industry. Consequently, the operational side of SEPA i.e. the processing of retail payments should also be handled by the banking industry. However, there are two scenarios in which the Central Banks may consider a more active operational role:

⁹ However a preliminary dialogue of e-invoicing issues is scheduled to start between the EPC and EACT.

- i) In the case that the banking industry fails in delivering such an infrastructure or
- ii) In the case that the banking industry only delivers basic services that have to be complemented by the individual players effectively leaving the smaller players out of the game.

6. POSSIBLE RECOMMENDATIONS FOR DISCUSSION

A number of issues are identified below which are crucial for the success of SEPA. For each issue identified, questions are raised on how the issue can be overcome and possible recommendations for remedies put forward. The intention of consultation on these recommendations is to trigger discussion in order to develop at a later stage possible regulatory or other intervention, provided this can be shown to be appropriate, proportionate and cost effective. In general, the issues are derived from the preceding sections and are therefore their description kept as short as possible. For supporting analysis we refer to the Annexes.

There is inevitably some overlap between the different recommendations and they are interrelated in the sense that they all deal with improving the way the market functions. This means that governance issues, user involvement, pricing and innovation issues may appear in different places. In order to cast the net as wide as possible, we prefer to have overlaps rather than miss the point.

If there are areas not mentioned in this consultative paper, but that nevertheless appear relevant to the SEPA project, please do not hesitate to also communicate these and comment as best seems. Stakeholders are therefore asked to identify any issues or problems provide whose omission of which could damage the success of SEPA. Stakeholders are also encouraged to suggest appropriate remedies.

Most of the following questions are linked to the vision as set out in Chapter 2 and the gaps as identified in Section 4.

Questions:

- (1) Do stakeholders have any comments on the vision in Section 2?
- (2) Do stakeholders have any comments on the gap analysis in Section 4?

6.1. Governance and consultation

Issue

The EPC is an organisation that comprises banks and banking associations. Limited and non-open consultation of end users has taken place, but even then this was only in the last stages of the design the SEPA schemes and frameworks. Although the schemes describe mainly the inter bank processes, several key aspects directly concern the end users (e.g. time cycles for clearing and settlement, return capabilities, mandate management, capability of the defined schemes as regards the remittance information size, etc.).

Questions

- (3) How can governance be improved?
- (4) Do stakeholders feel they have been involved enough in consultation in the SEPA/EPC process so far?
- (5) How can non-bank payment service providers contribute to the self-regulatory development of SEPA?
- (6) Could membership of the EPC (or any of the institutions it envisages, like the Scheme Management Entity) be opened up for all payment service providers? What conditions would have to be met?
- (7) How can other stakeholders, most importantly end users (consumers, SMEs, merchants, corporates, public bodies, but also processors, infrastructure providers) be better involved in the consultation process? (E.g. open public consultation, feedback through nominated representatives) what is the preferred channel for consultation (e.g. through the EPC directly, through an independent channel, through their financial institutions, national associations)? Please elaborate.
- (8) What are the best practices for user involvement and consultation available in Member States?

6.2. How can we ensure that product themselves to meet the vision?

Issue

A market-driven migration from existing products used mostly in national schemes to the new and euro area-wide SEPA products will be a difficult process if the new products are not 'best of breed'. No products have as yet been developed on the basis of the schemes and frameworks designed by the EPC. However, the currently available schemes for credit transfer and direct debit (version 1.0) may not rise above the lowest common denominator of existing national service levels.

However, these schemes are under revision after consultation at national level and some additional work has already been started by the EPC. Nevertheless, one issue still deserves attention, because of its potentially great benefits. A number of stakeholders have mentioned that the development of a standard for structured remittance information in the payment instruction, would allow for enormous savings because it would facilitate end-to-end automation and automated reconciliation in the internal administrative process of companies. Another feature that some stakeholders think would create benefits, is standardised customer interfaces for payment initiation (e.g. forms for credit transfers).

Regulatory intervention is a last resort if consultation fails to ensure that these schemes are not best of breed to match the markets and Commission vision for payments for 2010 and beyond.

Questions

- (9) Will the products based on the current SEPA schemes and framework (version 2.0) be sufficiently attractive
 - (a) to be offered by payment service providers and
 - (b) to be taken up by users¹⁰?
- (10) Do stakeholders think the products based on the current SEPA schemes and framework (version 2.0) will be of sufficient quality to encourage users to migrate from existing national products? (Full answers to these questions may have to wait until version 2.0 is available). Responses should specify the scheme details considered deficient and the improvement deemed necessary. E.g. are there features missing in the SEPA schemes that are available in the current domestic schemes and that are particularly important to users?
- (11) Should the development of common SEPA customer standards and interfaces also be addressed?
- (12) What are the topics where end users' believe improvement would be valuable (Remittance information, time cycles, consumer protection, other?) Do stakeholders think there is a need for the development of a standard for structured remittance information in SEPA payments?
- (13) Is there a need to develop common SEPA credit transfer forms, direct debit (mandate) forms, both paper and electronic such as currently exist at the national level?
- (14) Are there products at the national level that cannot be based on the SEPA schemes/frameworks? What will happen to existing domestic products that cannot be provided within the scope of the SEPA schemes and framework?
- (15) Could there be a role for the regulator to mandate a minimum service level?

6.3. Adoption and offer by banks and card schemes of SEPA products

Issue

It is important that all payment service providers and card schemes offer SEPA products. Because of the network externalities present in the market for payment services it is necessary to generate critical mass for the new payment instruments and to ensure reachability (in the case of direct debit). Availability of SEPA products by ALL providers, should ideally start on the SAME date, 1 January 2008 in order to avoid first mover disadvantage.

It is, however, unclear how take-up and implementation by banks and card schemes can be guaranteed in a self-regulatory framework on the same date. Regulation could be limited to ensuring that the products are available.

¹⁰ This assumes that EPC will publish version 2.0 after approval by the March 2006 Plenary – this point is not clear.

Questions

- (16) Can we rely on self-regulation in the take-up and implementation of SEPA products and standards by 2008?
- (17) Do we have to make the SEPA schemes and frameworks mandatory and if so, to whom? To all banks? What would be the cost of this and would the cost be proportionate to the gains?
- (18) How can we be sure that SEPA products will be available from all providers by January 2008? Would more detailed monitoring and milestones be helpful?
- (19) Should we make adherence to EPC DD and CT rulebooks mandatory for all payment service providers by the same date i.e. 2008?
- (20) Should we make compliance with the Cards Framework mandatory for all payment service providers by the same date i.e. 2008?
- (21) Should the scope of regulating SEPA compliance be limited to payment service providers that are already domestically offering corresponding national products? (i.e. if a bank currently offers direct debit services domestically to its customers, the bank has to offer the SEPA Direct Debit product by 1 January 2008) Would this regulation solve the reachability problem and ensure a successful launch of SEPA in 2008?

6.4. How can public authorities contribute to the standard setting process?

Issue

If standard regulation is shown necessary, the question arises how this should be organised. Standards here include not necessarily only technical standards. In fact standards comprise the whole set of arrangements (commercial and legal) needed to facilitate the necessary exchanges between competing providers of payment services. Schemes can therefore also be considered as standards.

Different models for establishing standards and making them mandatory exist. There is a range of alternative models for this available in Europe. Standard setting can be done by dedicated standardisation bodies at the European level (e.g. ETSI/CEN), which develop standards requested by the Commission. Another approach can be found in the Giovannini process of integration of securities clearing and settlement. A group of dedicated experts coming from, but operating independently of, their different stakeholder and national backgrounds, develops standards. Finally, there are other possibilities in which the Commission involving the Member States and the Parliament in accordance with the so-called Lamfalussy approach formally endorses the developed standard by means of a Comitology procedure. (see Annex 3 for further elaboration of three models)

A principle underlying all these standard setting processes is that the definition of the standard (to be interpreted in a wider sense than just technical standards and also including schemes) is left to the parties with the required expertise and best placed to develop the standard. Then enforcement of the standard can if necessary be required by regulation, but this would require as a minimum that the processes of developing the standard was open, transparent and accountable, that users were consulted on their needs

and requirements. If these principles of legitimacy are adhered to, legal endorsement could perhaps be given. Both the EPC and possible future institutions (Scheme Management Entities) should build on these principles.

Questions

- (22) If it is shown necessary, what is the optimal way to regulate standards for SEPA (legally, recommended)?
- (23) What are/were best practices for standard setting in payments at the national level?

6.5. How can we ensure effective competition in the processing of payments?

Issue

The European market for infrastructure solutions for processing payments in SEPA has to be competitive. The EPC has developed a number of principles to realise this, such as developing open standards (SEPA data model based on UNIFI) and aiming for a separation of infrastructure and scheme. It is not clear whether these are sufficient. There are, however, technical and commercial barriers still remaining that prevent a competitive processing market.

The separation of scheme and infrastructure may have to be complemented by the separation of activities (unbundling) and increasing transparency of pricing with regard to all distinct activities to ensure that service levels are maintained and that entry barriers do not prevent market entry in the longer run. Particularly, the cards processing industry deserves attention in this respect.

Questions

- (24) How can effective competition be ensured in all aspects of processing payments? These questions are preferably answered separately for
 - (a) credit transfers/direct debits and
 - (b) for card payments.
- (25) Will open standards and the separation between infrastructure and scheme allow for effective competition in processing? If so, should a separation between scheme and infrastructure be made mandatory?
- (26) Do we need a mandated list of technical requirements to facilitate interoperability between SEPA infrastructures/processors?
- (27) Will open standards and the separation between infrastructure and scheme allow for effective competition in processing of card payments? Is there a need to require card processors and networks to process neutrally all SEPA-standardised card transactions irrespective of brand and national background? Do we need additional rules on top of technical interoperability requirements to facilitate technical and commercial interoperability between processors?
- (28) Should the (rules for) POS card-terminal certification/accreditation be harmonised throughout Europe? How should this be done?

6.6. How to ensure adoption of SEPA products by users?

Issue

For SEPA to deliver the expected economies not only will SEPA products have to be offered by providers (6.3), but there will also of scale and scope, have to be a migration of a critical mass of users to these products by end 2010. The adoption of SEPA products by users will have to be a market-driven process, customers should freely choose based on service level and price. Mass take up of SEPA products is vital for providers as this is the basis of the business case to justify the investment needed.

Governments can play an important role in the adoption process. Government payments have a significant market share¹¹ that would contribute to realising critical mass. The role for governments could be to:

- (a) Get actively involved in the standard setting process as an important user.
- (b) To find ways to minimise migration cost and to provide input on user requirements that will help to make the new products acceptable and attractive.
- (c) "Kick-start" SEPA as early adopters of the new SEPA products.

Questions

- (29) How can adoption of SEPA products by end users be ensured?
- (30) Can stakeholders identify problems that would prevent migration by end users for domestic products to the SEPA schemes based products?
- (31) Is there a role for governments to be earlier adopters of SEPA products? What role can governments play in the design and consultation of SEPA products? What have been the experiences at national level with government involvement in promoting new payment services?
- (32) What is needed for big non-government users (corporates, SMEs, merchants) to ensure mass take-up? These stakeholders are particularly requested to give their views on what would facilitate their use of SEPA products.
- (33) Is consumer (i.e. private individuals) education necessary to facilitate adoption? How can this be organised best? Who should take the lead in these activities? When and how should education/communication on SEPA to end users take place?

6.7. How to minimise the cost of migration

Issue

The investment costs for migration to the new SEPA products for different stakeholders should be kept as low as possible. In order to reduce migration cost it is necessary to

¹¹ Payments by public authorities (tax, social security, procurement) may exceed 10% of all payments and therefore may contribute significantly to attaining critical mass.

create certainty about deadlines and objectives. To a large extent these costs are adjusting internal systems of (corporate) users and banks. These costs are not only in the inter-bank and in the bank-to-customer domains, but to a large extent in the adjustment of internal processes of all stakeholders.

It may be possible to mitigate these costs through the implementation of adequate conversion software, e.g. conversion of national message formats to SEPA formats or conversion of national bank account numbers to European bank account numbers. This may allow changes for SEPA to be made in pace with the natural investment cycle, rather than forcing all stakeholders to migrate before one date (2008 or 2010).

Questions

- (34) How can migration cost be minimised?
- (35) How do banks estimate their migration cost? Please explain the basis for the estimate.
- (36) How do other stakeholders perceive the adjustment cost of the transition to SEPA?
- (37) What ways can be identified to minimise migration cost for users?
- (38) Should IBAN and BIC be made mandatory for all users, for all euro-domestic credit transfers and direct debit transactions?
- (39) In what areas does uncertainty hinder migration? Would certainty over product availability and timing reduce migration cost?
- (40) Which kind of migration services could facilitate the migration process? (E.g. would it help if national banking communities were to publish conversion tables from national data formats to SEPA formats to provide a unique source of reference for the developers of conversion software? Can national banking associations publish these conversion tables? Will this allow software-providers to develop and deliver their conversion products on time and competitively?)
- (41) How much time would be needed for an efficient migration process and how much earlier should specifications/requirements on mandatory changes and conversion services be available?
- (42) Do software-providers and other stakeholders see other measures that would facilitate the introduction of products that could reduce migration cost?
- (43) How can we ensure that migration coincides with the 'natural investment cycles' of stakeholders?

6.8. How can we ensure that SEPA products can be improved over time?

Issue

The current development of schemes by the EPC aims at meeting the 2008 deadline for introducing SEPA products and mass take-up by 2010. While that is a very important goal, it is an intermediate objective. It is also important to allow for further improvement of products (and schemes) over time. The development and introduction of schemes

should, therefore, not be considered as a one-off exercise, and should be seen in a dynamic perspective. The governance of the schemes should be such that after the introduction of the new products there is room for and incentives in place to ensure that schemes develop and improve further over time in order to meet changing user preferences and new technological opportunities. In addition to what has already been discussed above about developing a structure for involving stakeholders in the design and implementation phases, it is important to organise a governance structure that foresees the future improvement of the schemes/products as well.

The EPC aims to establish one or more Scheme Management Entity for credit transfer and direct debit. This entity may facilitate developing a process aimed at 'continuous improvement' of the Scheme it manages. It is important the incentives are set so that the Scheme Management Entity can indeed realise this objective. There may also be other ways to ensure flexible scheme design able to provide for new user requirements and preferences as well as upgrading products in the light of new technological opportunities.

Questions

- (44) How can we ensure that SEPA schemes and SEPA products will be improved over time?
- (45) What kind of governance arrangements should be made?
- (46) What other measures or policies are available to ensure that SEPA products are improved over time?
- (47) What arrangements currently exist at national level for ensuring that products and schemes can be improved over time to take into account changing user preferences or new technological opportunities?
- (48) How can the development of value added services be arranged, which initially may be only provided by a smaller group of banks? How can interoperability be ensured?

6.9. How can we ensure effective competition in SEPA?

Issue

There are three particular areas of concern. SEPA may lead to dysfunctional outcomes from the perspective of ensuring effective competition: cards¹², direct debit and processing/infrastructure.

Cards

In cards there are concerns that the SEPA process might lead to the disappearance of efficient national schemes, without achieving corresponding efficiencies at the EU level,

¹² The cards industry is subject to a sectoral investigation by DG Competition. Several individual card cases are being or have recently been examined by DG Competition and national competition authorities. This process may lead to changes in the rules governing cards and have a major impact on the conditions of competition. Any final conclusions on cards for the process described in this paper will not be drawn until the sectoral investigation is finalised and any policy conclusions reached.

as a result of which at least some national user communities may experience a loss in functionality and/or unreasonable switching costs.

It has been argued in Section 6.5 that open standards and effective separation between scheme and infrastructure is necessary. How this will be organised, is, however, unclear.

Additional measures may be necessary to overcome fragmentation between national markets. It has been argued by banks that it is necessary to develop arrangements for cost recovery of inter-bank services (interchange fees). Cross-border processing currently is restricted under the rules of some international schemes and there may be other barriers to integration and competition.

Direct debit

In direct debits there is a concern about the welfare implications of introducing a multilateral interchange fee and what the European Direct Debit will mean for the pricing and use of this payment instrument. Direct debits are considered efficient and hence deservedly popular with corporates in a number of member states.

Infrastructure

In processing/infrastructure there are concerns that the outcome will be a single European monopolist processor/clearinghouse, which could be able to extract rents from the payment value chain, even though other processors exist. In addition to financial rents, this may bring costs to society in terms of rigidity vis-à-vis innovation, poor service levels, inadequate investment incentives and poor accountability to users.

This section asks what can be done to avoid any unfavourable outcome in these three areas.

Questions

6.9.1. Cards

- (49) What obstacles hinder effective competition in card payments in SEPA? What can be done to ensure greater competition in card payments in SEPA?
- (50) Do we need interchange fees in card payments? Could not both sides to the payment directly charge the payment service provider according to the principle of shared cost?
- (51) Should card scheme rules which prevent price discrimination between payment instruments at the point of sale (e.g. no surcharge rules) be banned?
- (52) Should scheme rules that limit cross-border issuing and acquiring be banned?

6.9.2. Direct Debit

- (53) Is a MIF necessary for the SEPA Direct Debit? If so why? Why can't both sides to the payment be directly priced by their payment service provider according to the principle of shared cost? What alternatives are available?

6.9.3. *Infrastructure*

- (54) What barriers exist for competition in processing? What measures are necessary to ensure commercial interoperability of processors/infrastructure providers and create a level playing field for competition?

6.10. How to ensure the repositioning of cash and cheques?

Issue

The efficiency of the payment system can be further improved by an increased use of electronic payments. This change is difficult because clear pricing signals (i.e. prices based on cost and effective competition) to users are largely absent. The repositioning of cash and cheques does not therefore result from the current market process. In addition, the use of relatively expensive payment instruments such as cash and cheques can also be stimulated or even mandated through existing legislation at the level of Member States.

Questions

- (55) How can efficient payment instruments be promoted and cash and cheques be repositioned? How can the price signalling mechanism be improved to promote the use of the most efficient instruments?
- (56) What legislation can be identified that encourages or makes the use of cash/cheques mandatory? What can be done to remove or diminish the effect of legislation identified above?
- (57) What legislation can be identified that distorts price signals in the use of cash and cheques? What can be done to remove or diminish the effect of the legislation identified above?
- (58) Are there other rules or market practices that favour the use of cash/cheques? Are there examples of best practice to reduce consumer reliance on cash without provoking consumer organisations?
- (59) Are there any rules/regulations and market practices that hinder transparent and cost based pricing and use of electronic payment instruments?
- (60) What practical problems exist that hinder the introduction of pricing of cash (deposits/withdrawals) and/or cheques?

6.11. Customer choice and mobility

Issue

The benefits of competition can only be reaped by payment service users if they have choice and can easily exercise this choice. Choice should be supported by transparent pricing, allowing customers to make informed decisions. Transparent pricing is an important element in the proposed Directive on payment services (New Legal Framework).

In payments there seems to be a high degree of lock-in for users to payment service providers once chosen. Partly, this may be related to the fact that making payments requires a user to hold an account with a payment service provider. The Commission has

set up a Forum Group on bank accounts to study whether barriers to customer mobility can be identified and to formulate recommendations to remove these barriers.

Questions

- (61) What are stakeholders' views on customer mobility and choice?
- (62) To which extent would common and open customer-to-bank standards (e.g. e-banking standard, direct debit message standards, credit transfer form standards) contribute to reducing customer lock-in?
- (63) Apart from the transparent pricing of payment services under the proposed directive on payment services and the initiative to set up an Expert Group on customer mobility in relation to bank accounts, are there any other initiatives that need to be undertaken now?
- (64) Is there a need for bank account number portability? Should account numbers in Europe be harmonised? Can other identifiers be developed for directing payments?

6.12. E-invoicing

Issue

E-invoicing may contribute to a technology leap in a wider area than just payments, as invoicing is the link between internal processes of companies and the payment system. It could become an important part of the Lisbon process to make the EU a more competitive economy. Promoting e-invoicing and identifying the standards needed for it requires commitment of a variety of parties to a common vision. Currently there is no such shared vision and that may well mean that new business opportunities and gains, but more importantly large economies to society as a whole, may not be realised. The Commission's services attach the utmost importance to significant progress in this area.

Questions

- (65) How can e-invoicing be promoted?
- (66) What are stakeholders views on the potential for e-invoicing with near universal reach to most business and consumers in the EU who are increasingly using e-banking?
- (67) The Nordic countries have experienced exponential growth of e-invoicing. Users have experienced considerable savings and banks developed a convincing business case. Are there any reasons why a similar model could not be adopted to the rest of the EU?
- (68) What standards are needed for the realisation of e-invoicing throughout Europe? Is it sufficient to define standards for structured remittance data or are more complete schemes needed? Could one scheme and standard be developed that meets the needs of all potential users and ensure near universal reach?
- (69) Can the EPC in cooperation with the relevant stakeholders set standards for e-invoicing? Should they be mandated to do this by a certain date?

- (70) What would be the role of different stakeholders in the process of promoting e-invoicing?
- (71) Should e-invoicing be part of or form the core of a larger separate and more ambitious project to dematerialise the supply chain?
- (72) Is there a role for governments/EC in promoting e-invoicing? (For example mandating their use. Or governments only admitting e-invoicing or charging supplements for paper invoices?)

7. CONCLUSIONS AND NEXT STEPS

This consultative paper is aimed at raising questions and gathering input from all market parties. This consultation paper will be distributed among all market participants, payment service providers, payment service users and infrastructure providers and will be posted on Internal Market and Services DG website in order to encourage the collection of views from the widest possible community.

The deadline for response to this consultative paper is 21 March 2006. Replies can be sent to markt-h3@cec.eu.int In parallel, the Commission will engage in bilateral discussions with stakeholders.

In light of the analysis of the responses received¹³ to this consultation and the bilateral discussions, the Commission will prepare a second consultative paper. This paper will aim to identify more concretely, possible recommendations that could be submitted to the College for further action to ensure that the full economic potential of SEPA is attained. This second paper will be published for consultation before the summer of 2006.

The results of these consultations will be used to prepare a major conference on SEPA to be held on 3 October 2006.¹⁴ The intention is to follow this up with the first adoption by the Commission of a Communication on additional measures to ensure the creation of a Single Euro Payment Area further to the Commission proposed COM(2005)603 (i.e. New Legal Framework for payments in the internal market) and industry self-regulation.

¹³ All contributions to the consultations will be published on the Commission website (http://europa.eu.int/comm/internal_market/payments/sepa/index_en.htm) unless a contribuant indicates the wish not to have (part of) his contribution published.

¹⁴ Invitation and programme will be posted on the website of the Commission (http://europa.eu.int/comm/internal_market/payments/sepa/index_en.htm) in spring 2006

Annex 1: Overview of working groups and activities of the EPC

All working groups received a mandate from the EPC Plenary of October 2004. They are operational under Terms of Reference valid until June 2006.

WG Electronic Credit Transfer

This group has developed the Rulebook for the SEPA credit transfer. (Version 2.0 to be approved by the Plenary in March 2006). Two task forces are in place for focussing on e-payments (internet) and m-payments (mobile phone).

WG Direct Debit

This group has developed the rulebook for the SEPA direct debit. (Version 2.0 to be approved by the Plenary in March 2006).

WG Cash

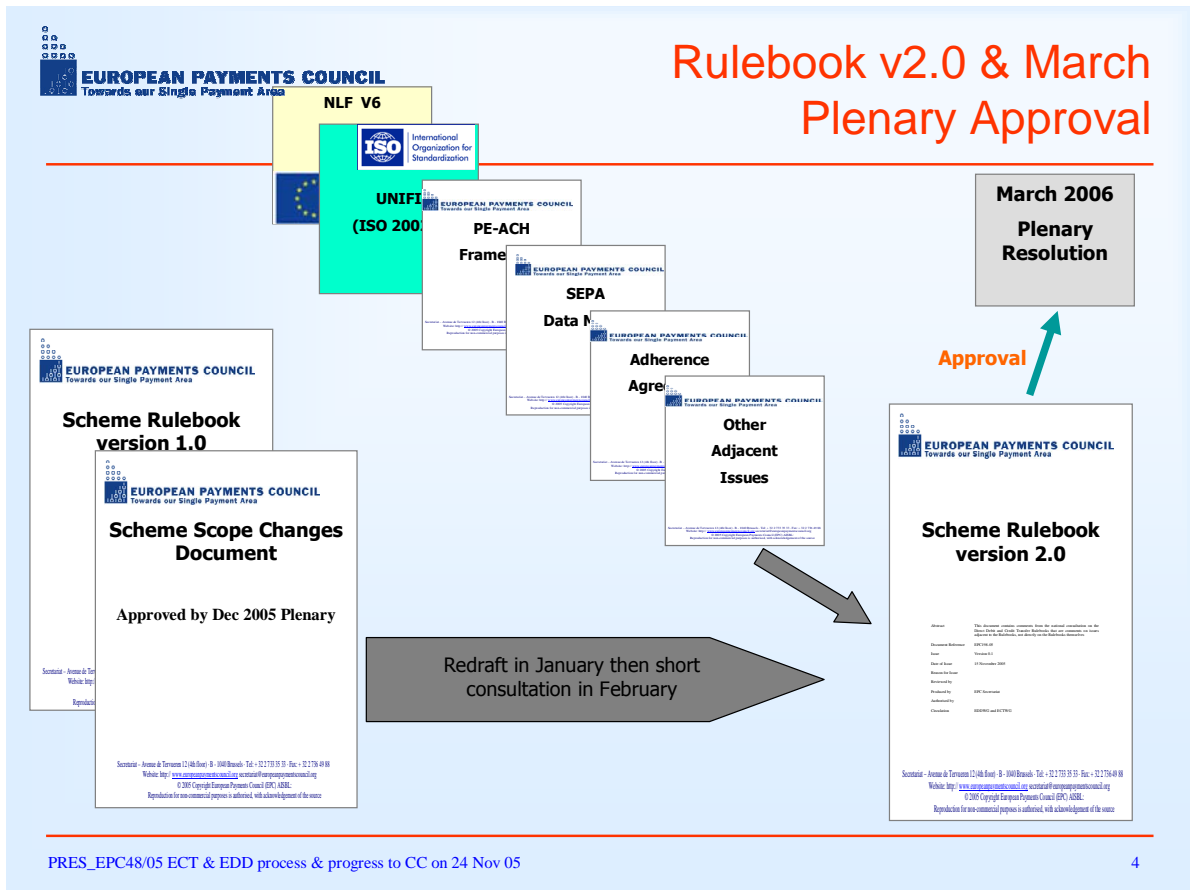
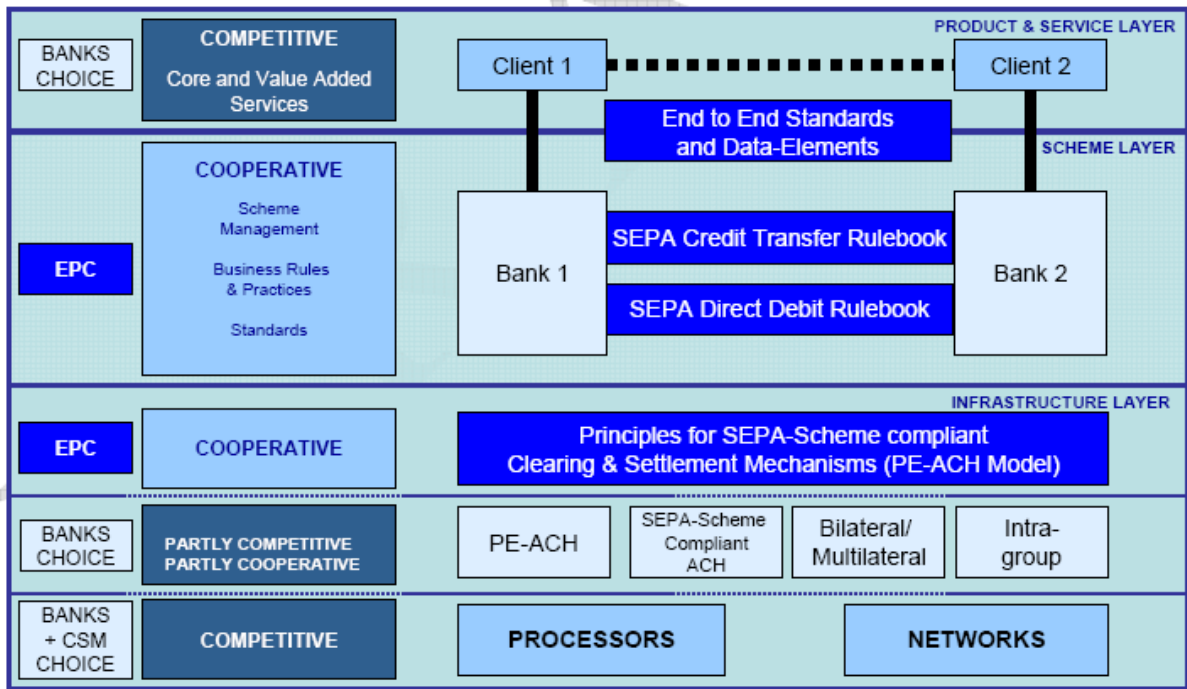
This group focuses on improving the efficiency of the cash handling and processing in SEPA and has developed the Cash Framework (version 1.0 to be approved by the Plenary in March 2006)

OITS

This group focuses on Operational, Infrastructure and Technical Standards. This group has in close co-operation with SWIFT developed the SEPA data model based on the UNIFI & XML standards that are going to be open ISO 20022 standards (more details in ANNEX 2). Four work blocks underpin the work of the OITS, which focuses on different aspects (e.g. routing, data formats and security). Also a “Framework for the evolution of clearing and settlement of payments in SEPA” has been developed.

Legal Support Group

The Legal Support Group provides support to all EPC bodies in relation to legal and regulatory issues and in particular to develop, on behalf of EPC, common positions with respect to the New Legal Framework and its implementation. LSG operates under ToR approved by the EPC Plenary of October 2004 for two years, ending June 2006.



source: EPC

Annex 2: Current practice of standardisation in the financial services industry

Introduction

Most standards in the financial industry focus on a part of a business process (such as the clearing of instructions) or on a particular domain (e.g. simple, non-time critical or "plain vanilla" payments compared to payments originating as opposed to securities transactions) in the financial industry without taking into account what's happening outside their focus area. This results in a "silo approach" which doesn't offer end-to-end interoperability and puts the burden of linking the various standards on the financial institutions. A concrete example can be found in the securities industry where the FIX standards support pre-trade and trade and the ISO 15022 standards support post-trade and beyond. The impact of this approach is increased by the fact that individual messages are often developed in isolation without considering the actual business processes that they need to support.

Even within their focus area, standards insufficiently take into account diversity, such as market practices, forcing industry to spend time and energy to define the ways(s) to link the use of standards in various concrete situations. Furthermore, standards documentation usually leaves much room for interpretation, often leading to differences in the implementation of these standards. This will of course create problems and errors when these standards are used between financial institutions. All of the above reduces the level of STP (Straight Through Processing) that can be achieved, resulting in additional costs for the industry.

Requirements setting

The standard setting process needs to address the above problems by consciously focusing on the requirements of end-to-end business processes and by involving industry experts to define and validate requirements and solutions. The standard setting process also needs to use a formal business process modelling approach to reduce ambiguity and risk of misinterpretation of the developed standards. The standard setting process needs to base itself on a dictionary with reusable components. This dictionary facilitates industry-wide agreement on the definition of the reuse of multiple components in different messages.

Way forward selected by the financial industry for payments

The financial industry at both international and European levels is supporting and adopting the UNIFI (ISO 20022) standards development methodology and outcome.

The UNIFI standards development methodology is a three-layered approach, based on business process modelling. The first two layers are technology independent and use UML (a modelling notation) to describe all aspects in a formal way.

The first layer (the business layer) focuses on the business process. It starts with a business analysis to get a correct and complete understanding of the end-to-end business process. All relevant business activities and business roles are identified and for each business activity the used information is identified. The business analysis is followed by a requirements analysis to identify all communication needs, i.e. which information needs to be sent between which roles at what moment and under which conditions.

The second layer (the logical layer) focuses on the solution. During the logical analysis the main components of the solution will be identified. This includes the definition of the required messages and the description of the business transaction, i.e., the way the messages must be used to support the business process. This activity is followed by the logical design to define the detailed structure of the messages and to formalise the description of the business transaction.

The third layer (the technical layer) focuses on the physical realisation of the defined solution. During the technical design technology specific information, such as XML-tags, will be added and during the physical implementation the logical solution will be converted into a physical solution. This means for instance that the defined message structures are converted into XML Schemas.

The main advantage of this approach is the decoupling of the physical representation from the business standard. It also allows to involve the business experts at the right time and for the right reasons, namely to discuss the business aspects of the standard and it results in an implementation-neutral and representation-neutral definition of the standard.

ISO has a pre-defined process to approve standards. In the frame of UNIFI (ISO 20022) standard, a series of experts groups are defined for the endorsement and registration of various standards produced by the financial industry. This mainly relies on a Registration Management Group, specific Standards Evaluation Groups per business area and a Registration Authority. Any financial industry group, community in the financial industry or standards body can submit a business justification for a project to develop standards in a particular domain of the financial industry to the Registration Management Group.

UNIFI (ISO 20022) Compliance of the development undertaken by the submitter is performed both by the Registration Authority and the relevant Standard Evaluation Group. Strict checks are applied throughout the process. The development of standards is resource intensive and time consuming. The investment in the ISO 20022 process therefore necessitates a strong commitment of the submitting organisation and developments are often granted to specialised, established standards bodies, or to alliances of standard bodies. The ability to gather the necessary expertise, the commercial neutrality of the submitting body, and its ability to enforce and maintain over time the produced standards are also elements taken into account when the Registration Management Group assesses a business justification.

Applicability to the SEPA context

The European Financial Industry, through the EPC, has been heavily supporting the developments of the UNIFI Credit Transfer and Direct debit standards. Business justifications to ISO 20022 RMG for these two standards were submitted by SWIFT in the name of its community. SWIFT has also been nominated as Registration Authority for the UNIFI (ISO 20022) standard by the ISO Central Secretariat.

The initial development of standards has been described above. The ISO 20022 RMG is setting rules for organising the maintenance of already created and registered standards. These rules will be similar to the ones set up for the creation of new standards. It is therefore advisable to follow the maintenance process that is currently being designed in the frame of the ISO 20022 standards development methodology.

Annex 3: Alternative models for regulating standards

Introduction

At the level of the European Union, there are different approaches for regulating standards:

1. The Giovannini approach
2. The CEN, CENELEC, ETSI approach
3. The Accounting approach

These summaries are intended to give an indication of the key features of different standardisation approaches without seeking to be complete.

1. Cross-border Clearing and Settlement of Securities: Giovannini Barrier 1

General Approach: The creation of a single EU market in the area of cross-border clearing and settlement, that is both efficient and safe, raises many of the same issues in relation to the need for common standards as does the single payments market¹⁵. One problem is the diversity of IT platforms and interfaces existing at the national level used by clearing and settlement providers in securities markets.

In its 2001 report, prepared in response to a request from the European Commission, the Giovannini Group¹⁶ published a report identifying 15 barriers to efficient EU cross-border clearing and settlement. This was followed by a second report in 2003 suggesting a strategy for removing the 15 barriers. Inter alia, the Giovannini Group stated that national differences in the information technology and interfaces used by clearing and settlement providers (the so-called Giovannini Barrier 1) should be eliminated via an EU wide protocol to be prepared by SWIFT.

Nature of the standards: SWIFT is developing a recommendation for a single protocol for European Clearing and settlement on the basis of open access ISO standards (e.g. 15022 & 200222 with an XML internet protocol approach) which facilitates STP (straight through processing). N.B. The reference to SWIFT is to the standard-setting side of the co-operative's work and does not imply any requirement to use SWIFT as the communication provider. However, the use of the common protocol cannot be imposed (by SWIFT or other entities), thus implementation is to be ensured via adoption by the ESCB, the Securities Market Practice Group (SMPG) and recommendation by other industry bodies/associations.

Governance: The draft common protocol recommended by SWIFT is subject to discussion within an Independent Advisory Group (IAG) established by SWIFT, whose

¹⁵ Although there are a smaller number of market players, the situation in securities is further complicated by the large number of different securities traded.

¹⁶ The Giovannini Group is composed of financial-sector experts of the private and public sectors of the EU securities industry (e.g. from the European Commission, (investment) banks, asset managers, brokers, exchanges, central counterparties (CCPs), International and domestic central securities depositaries (I/CSDs), central banks, consultants and other industry bodies and associations.

role is to review the output of the Barrier 1 consultation process. For more information on the IAG (members, tasks etc.) see: http://www.swift.com/index.cfm?item_id=43429. The CESAME group regularly discusses the development of the draft common protocol and implementation issues. Since there is no directive on C&S or any other EU legal provision obliging industry to develop and use the common protocol, there is nothing like "oversight" or "adoption" or "ratification" of the protocol.

Implementation: Once defined, the standard protocol should be implemented by all European industry participants, e.g. banks, CSD's and CCP's¹⁷ central banks, intermediaries etc. However, there is no EU legal basis to impose mandatory standard application, which therefore remains voluntary.

2. CEN, CENELEC, ETSI Approach

General Approach: The Commission can seek the preparation of standards in the field of Information Communications and Technology by making a request to one of the three European Standardisation Organisations (ESO); namely CEN (general standards), CENELEC (standards for safety of electrical goods); and ETSI (telecomm standards). The required standard is included in the ICT standardisation work programmes managed by DG Enterprise and Industry.

Nature of the standards: as required in the specific ICT area. Apparently, there is some experience with the adoption of standards in the financial services area (e.g. for the operation of ATMs).

Governance: All three ESO's are well-established standard setting bodies operating in an open and transparent manner and subject to appropriate governance arrangements. Membership is in principle open to all interested parties.

Implementation: Implementation of standards is voluntary. The underlying idea is that if standards are truly useful to industry, industry will adopt them of its own accord. Nevertheless, it should be noted that once a standard is adopted by an ESO, a Member State is bound to withdraw any conflicting national standard. However, in to give a standard a kind of EU seal of approval, a reference (not the standard itself) may be published in the Official Journal.

3. Accounting Approach

General Approach: Under Regulation (EC) No 1606/2002 all EU listed companies are required to prepare their annual consolidated accounts using International Financial Reporting Standards as endorsed at EU level. Standards are formally adopted by the Commission in accordance with a Lamfalussy-type procedure whereby Parliament must not object and Member States vote on a weighted majority basis in the Accounting Regulatory Committee. IFRS standards may only be adopted if they meet certain specific conditions set out in the Regulation. Before the Commission proposes the formal adoption of an IFRS, an accounting technical committee (EFRAG) must be consulted and its opinion provided. See Recital 10 of Regulation (EC) No 1606/2002.

Nature of the standards: Accounting standards.

¹⁷ Central Securities Depositories and Central Counterparties.

Governance: IASB standards should be prepared transparently and after broad-ranging consultation of interested parties. The IASB is subject to oversight exercised by the Trustees of the IASC Foundation. In general the governance arrangements have been recently improved subsequent to the IASC Constitution Review conducted in 2005, although the Commission considers that there is still scope for further improvement. EU parties will participate upstream in the discussions leading to the preparation of an IFRS standard.

Implementation: Implementation of IFRS standards formally adopted by the Commission is mandatory for listed companies annual consolidated accounts. The underlying idea is that mandatory standards will facilitate investor transparency and promote EU capital market integration and thereby reduce the cost of capital for listed companies.

Concluding remarks

All of the models discussed above for standard setting have developed a formal approach, relying upon expertise from committed members, and a series of consultations with stakeholders to refine and endorse the outcome of the standardisation phase.

European Standards Organisations also maintain tight links with the International Standards setting organisations by means of affiliations or conventions. These links are to ensure that the respective work programmes are being exchanged with a view to avoid duplication and ensure standardisation work is not replicated in different bodies which would potentially result in divergent standards at the International and European level. The conventions also foresee the adoption of mutual standards if adequate. Therefore, whichever level the standardisation work is done at, the ultimate goal is to obtain general internationally recognised standards.

Annex 4: Estimated benefits of SEPA and e-invoicing

Below some preliminary and rough calculations of the benefits of SEPA and the potential savings possible from e-invoicing are outlined.

The economic costs of the non-single payments market

The absence of scale and scope economies, as well as a lack of effective competition in SPM, leads to costs for business and consumers running into tens of billions of euros. These are well documented in the Commission Impact Assessment¹⁸ which estimates these costs as follows:

	Cost in billion EUR
Payment accounts prices ¹⁹ (varies by factor 1:8)	6.7
Product standardisation & infrastructure consolidation ²⁰	10.0
Increased use of electronic payments instead of cash/cheques ²¹	5.3
	22.0

In addition the fees paid by retailers for debit and credit cards in some Member States would be much lower- as much as 20 times lower for debit cards and 9 times less for credit cards. This is primarily caused by a lack of effective competition rather than an absence of scale and scope economies.

Substantial gains if SEPA used as a launch pad for e-invoicing

Even more substantial gains arise if SEPA is used as a catalyst to launch e-invoicing by providing an IT platform to rationalize internal business processes linked to the payment chain. Revolutionary productivity gains in transaction are available from straight-through-processing (STP) and are widely recognized by the corporate sector²². These gains are not theoretical. The real experience gained in some Member States conclusively demonstrates that SEPA can become the foundation essential to facilitating end-to-end automation of the payment chain. A conservative estimate of the saving easily exceeds EUR 100 billion, every year, calculated as follows:

¹⁸ SEC(2005) 1535, 1.12.2005.

¹⁹ If the current price differences, of a factor 1:8 in Member States converged around the present European average, users in more expensive countries would gain substantially, e.g. users in the two most expensive countries would see savings of respectively EUR 5.4 billion and EUR 1.3 billion.

²⁰ Product standardisation and consolidation of payment infrastructures will maximise economies of scale. For example if unit cost levels were to decrease to 20% above the best practice level in Europe, this would generate EUR 10 billion additional profits for banks.

²¹ If all countries would reduce the use of cash, for example by using debit cards up to the level of the three countries with the lowest share of cash payments, this would mean savings for banks of EUR 5.3 billion.

²² EACT: European Association of Corporate Treasurers.

Total annual EU invoices ²³	Exceeds 20 billion
Percentage of invoices which are B2B or B2G ²⁴	Exceeds 50%
Current cost to manually process an invoice ²⁵	EUR 30–80
Cost saving from electronic processing ²⁶	60–90%
Conservative estimate of minimum saving per invoice ²⁷	EUR 25
Conservative estimate ²⁸ of total annual saving ²⁹	>EUR 100 billion p.a.

For a variety of reasons³⁰ banks are ideally placed to make these SEPA generated savings a reality. SEPA has thus clearly the potential to make a substantial and genuine contribution to the achievement of the Lisbon Agenda. Given its importance, the ECB and the Commission have established close cooperation and are coordinating their SEPA-related work streams.

²³ EACT estimates the total number of European invoices exceeds 27 billion.

²⁴ B2B: Business to business; B2G: business to government.

²⁵ Finnish State Treasury and private sector estimates.

²⁶ EACT estimate.

²⁷ In an electronic system there is no need to re-key in details of transactions, they need only be approved. Order and invoice reconciliation could be automated and book-keeping and accounting records electronically updated.

²⁸ The EACT estimates a saving potential of EUR 243 billion. The above estimate assumes only half of the B2B and B2G invoices (i.e. 5 billion invoices) each produce a minimum saving of EUR 25.

²⁹ Automation also results in better cash flow and lower risk as senders can invoice more frequently without causing costs to their customers; Both gain from increased improved security as invoicing is executed by banks using bank identification.

³⁰ Banks can provide a ready payment road, high security (through bank user identification) and common data interfaces (although presentation could be tailored nationally, regionally, or by bank). Through their advantages of trust, strong brands, customer relationship and distribution power, banks have the capacity to drive mass-market application. In short, e-invoicing provides tremendous societal benefits.

Annex 5: Memorandum on e-invoicing



Financial Markets and Statistics

Harry Leinonen

MEMORANDUM

9 December 2005

Unrestricted

1 (3)

Bank provided e-invoicing structures and benefits

The interest in and use of e-invoicing is growing at an extraordinarily rapid pace. Large scale implementation could generate annual cost savings in the EU in the range of EUR 100 billion, compared to paper-based invoicing. Banks play an important role in providing e-invoicing services.

Background

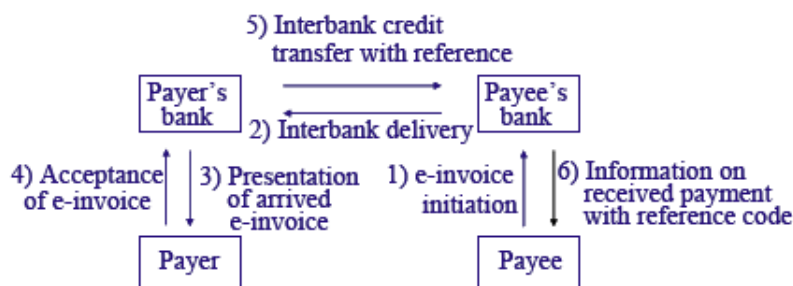
Most customers use PCs or larger processors and wish to receive and send all their payment data in electronic form via telecommunication. Corporate customers in particular would wish to exchange invoice information in electronic form using common standards in order to process invoicing information more efficiently and with less manual processing errors. In near future, private customers will most probably also have the same interests as this will help them to save time and manage their personal economics better.

Most payments made via banks are connected to an invoice or receipt, which contains the information on why the payment is made. Due to capacity restrictions in paper-based and early electronic payment systems, the data content attached to payments was considerably restricted. Invoicing data was transported separately between the payee and payer. The separate payment data contained at best only a reference number for automatic reconciliation of payment and invoicing data. IC storage and communication capacity and costs have currently reached such low levels that invoice information can easily be attached to payment information and thereby completely new benefits can be achieved.

The basic bank-provided e-invoice service

In the basic e-invoice service provided by the banks, eg in the Nordic countries, the invoicer/payee/creditor just needs to send the e-invoice information to its bank and the e-invoice information is routed via the interbank network to the payer's bank, where it is accepted by the payer and transformed into an accepted payment using the straight-through-processing mode. Generally, it processed as credit (reference) transfer after acceptance (see figure 1).

Figure 1: The basic e-invoice process





Harry Leinonen

9 December 2005

Unrestricted

For the customers it is important that the e-invoice standard is common to all banks, enabling them to reach all their customers via one route and interface (see below). Corporate customers in particular need to be able to import the data into their accounting systems for additional processing without re-inputting any data.

Corporate customers use two general options for processing the received e-invoices

- a) accepting the e-invoices via the e-banking web-service, whereby they are transformed into payment instructions, which are executed directly or wait in the bank's payment system until the due date
- b) importing the e-invoices into the payables or other accounting system of the company in which they are accepted and from which they are later presented to the banks as payment instructions.

Generally, smaller companies and private persons (and more so in the future) employ alternative (a) for invoice acceptance and use the monthly electronic account statement for accounting purposes. The large companies employ generally alternative (b).

The benefits of e-invoicing

A proper e-invoice scheme provides benefits in three legs of the traditional four-box payment model ie in the payee-to-payer leg, in the payer-to-bank leg and in the bank-to-payee leg.

In the payee-to-payer leg the e-invoice information flows automatically in STP mode and following costs can be avoided

- printing a paper invoice and putting it in the envelope
- the mailing costs of the paper invoice
- opening the invoice letter and archiving the paper invoice
- manually inputting the invoice data to the payables/accounting system at the payer.

In the payer-to-bank leg the e-invoice information is entered directly in electronic format and

- manual input from paper giros/invoices can be avoided in bank branches or by customers when using e-banking or ATM services

In the bank-to-payee leg the received payment information will be transferred in electronic format with proper remittance/reconciling/reference codes and therefore

- manual re-inputting of data can be avoided
- receivables files can be updated automatically based on the reconciling/reference codes.

The total benefits of e-invoicing depend on the current automation level in the different legs, but already a moderate estimation of the payee-to-payer leg benefits result in cost savings in the extent of EUR 10-20 per invoice. As there are about 60 billion non-cash transactions in the EU each year, the total benefits, even by cautious estimation, will be over EUR 100 billion per year. Considerable cost savings will also be found in the bank-to-customer legs due to automation.

Sending all outgoing e-invoices to the own bank and receiving all incoming e-invoices from the same site is the simplest e-invoice routing mechanism for customers, which provides both benefits via automatic STP-linkage between invoices and payments as well as a good shield against fake invoices. Ultimately the competition will determine if other alternatives such as emailing e-invoices or e-invoice hotels will survive.



The quest for common standards

Efficient implementation requires a common international XML-based e-invoice standard, preferably an ISO-standard. Currently there are several competing proposals and it is important to combine these into one common master standard. The data content of invoices varies, but XML provides the opportunity to develop a schema that includes all necessary data fields, where everybody selects the ones necessary for their specific purpose. In order to operate on a worldwide basis it has, for example, to be able to contain different VAT data structures. However, it is essential that the XML tags and attributes are standardised so that the e-invoice messages are interpreted in the same way by all users/applications. The same XML schema for a financial transfer message (FTM) can then be used by all the different bank and customer applications, which process payment or invoice messages. (See for standardisation details in separate detailed paper on e-invoicing.)

Important development possibilities

E-invoicing has started off between large corporate customers and in connection with credit transfer based payments. However, e-invoice services can and should be expanded to other customers (SMEs and private customers) and to all payment methods. The interest among SMEs is on the increase in all Nordic countries. In Norway, private customers already use e-invoicing and marketing has started in Finland.

Connecting e-invoices to direct debits would mean that the advance direct debits information could be sent to customers as e-invoices and paper notices would become obsolete. Attaching e-invoice information to card payments would especially benefit corporate customers as they would receive corporate card transaction details directly into their accounting systems. Also private customer would benefit from expanded information on card payments.

One essential result, when all payment transactions include invoicing details, is that the payment account and its account statements would become an electronic archive for all payments made. All the details on the payment receipts would be available in the electronic archive. Customers could easily browse their accounts, similarly to browsing email accounts, for special payments and their details eg when did I buy the camera and is the guarantee still in force.

The way forward

A common thrust by banks and corporate customers is needed to develop a common and comprehensive e-invoice standard, which would become an essential part of the payment messages of all payment methods. Introduce this as part of the SEPA changes would bring clear customer benefits within the SEPA process.