

SEPA - the Single Euro Payments Area

SEPA involves the creation of a zone for the euro in which all electronic payments are considered domestic effectively removing the barriers to movement of cross-border payments. The programme is sponsored by the European Commission and European Payments Council.

The primary goal of SEPA is to enable customers by November 2012 to make cashless euro payments to anyone located anywhere in the area using only a single bank account and a single set of payment instructions.

SEPA includes the development of a new infrastructure, common financial instruments and new standards and procedures. It is hoped that the high costs to the European economy associated with cross-border transfers should be significantly reduced through economies of scale.

Payment Services Directive (PSD) is the key piece of enabling legislation that will provide the legal foundation for the creation of an EU single market for payments.

The Directive will licence banks and payment services providers and support the three pan-European SEPA payment initiatives covering credit transfers, direct debits and certain credit card payments. The PSD must be implemented on 1 November 2009.

SEPA & The Eurozone

The Eurozone (officially the Euro Area) should not be confused with SEPA which covers the 31 Member States of the EU/EEA. The Eurozone is a currency union of 16 EU states which have adopted the euro as their sole legal tender. A further eight other states are obliged to adopt the zone once they fulfill the strict entry criteria. Monetary policy of the zone is the responsibility of the European Central Bank (ECB). Microstates Monaco, San Marino and Vatican City will all be part of SEPA although interestingly Andorra, despite adopting the euro, will not.

Short History of SEPA

The first of the SEPA compliant cross-border schemes - the SEPA Credit Transfer - was introduced in January 2008 with a deadline for full compliance currently set at 31 December 2010. Uptake to date has been very poor.

It should be noted that by December 2008 only 1.5% of credit transfers within Europe were executed to SEPA standards. The delay in introduction of the legal framework provided by the PSD is also likely to have a knock-on effect for the SEPA Direct Debit scheme. French banks have recently pushed back the date for implementation of the SEPA Direct Debit scheme by a year to November 2010, setting the stage for a confrontation with the ECB and the European Commission

Overall, advancement with SEPA has been long and tortuous. Many have deduced that the main November 2012 deadline for SEPA is unlikely to be achieved.

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What is a SEPA Credit Transfer?

The SEPA Credit Transfer is a cross-border, non-urgent euro payment scheme. It allows transfer payments to be made between any SEPA country including euro payments within the UK. The person being paid will receive the monies within three working days of the bank receiving the instruction from the payer.

What is a SEPA Direct Debit?

The SEPA Direct Debit scheme should be available from late 2009 onwards and will enable Direct Debit originators to collect euro payments in any of the SEPA countries including their own domestic DD, using a single Direct Debit service rather than having to use the country specific Direct Debit services that currently exist.

Main Objectives of SEPA

- Fundamentally, the standardisation of euro payments: common time limits and processes, all-electronic straight-thru-processing (ISO 20022) with no differences between national and international payments across the SEPA area.
- Greater reliability in pan-European payments thereby strengthening consumer trust in payment services.
- Increasing competition with fewer niche players made possible through SEPA standardisation.
- Reduction in the costs of electronic money and of payment transactions in general driven by greater market competition amongst payment providers and banks
- Reduction in the number of cash transactions through the use of more cost-effective e-money.
- Increasing surveillance of the flow of e-money particularly regarding money laundering and terrorism

How will SEPA work?

With regard to euro payments there will be a range of options available to organisations including:

- through their banks,
- directly to SEPA compliant Clearing Settlement Mechanisms (or CSMs),
- through a SWIFT Closed User Group of SCORE
- web based secure products
- via the European Credit and Debit Card networks.

At present, most commentators believe that there will be just a single Pan-European Automated Clearing House (PE-ACH) for processing all the euro transactions. Additionally, we are also seeing several SEPA compliant regional Automated Clearing Houses (or ACHs) and Clearing Settlement Mechanisms (or CSMs) such as Vo-calLink which will operate alongside PE-ACH. The latter has been purpose built by the Euro Banking Association (EBA)

In addition, banks have 'bilateral file exchange arrangements' in place with partner banks to handle particular payment concentrations. These so-called 'super CSMs' should have competitive advantage in terms of pricing, efficiency and additional functionality such as direct corporate access.

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It should be noted that under the SEPA scheme the use of Bank Identification Codes (BICs) and International Bank Account Numbers (IBANS) is now mandatory for cross-border euro payments. Banks can reject payments that do not include valid BIC and IBAN data and there is a need for cross-border validation at an early stage of the fund transfer process.

In summary, the key benefits of the SEPA Schemes are that they provide customers with common rules, predictable execution time cycles for both one-off and recurrent transactions and the certainty that payments will be received by the payee without fees being deducted from the principal sum.

How are UK Banks Involved?

The UK is, of course, a non-euro country and the number of cross-border euro payments to and from the UK is relatively small. However, the UK banking industry can see the benefits of SEPA (albeit at a cost) and most major banks have a SEPA credit transfer capability for their euro-based accounts.

Inevitably, the creation of SEPA will not be visible to the vast majority of UK customers making sterling payments as existing sterling schemes will continue to operation alongside SEPA. Only over time will UK business and individuals who make or receive payments in euro be affected by SEPA as its geographical scope extends beyond the Euro-zone. The existing BACS direct debiting scheme will continue in the UK after the implementation of the PSD.

Strategists in multinational businesses and banks will be very mindful that they do have with SEPA the opportunity to consolidate their payments processing onto common platforms across the Eurozone. All should benefit from substantial economies and efficiencies by selecting an appropriate provider although the cost and potential risks are major barriers to early progress.

ea Consulting Group Commentary

SEPA seems beset by problems. Even the ECB has expressed its extreme frustration at the lack of clarity on many aspects of the SEPA. The main ECB criticism concerns the SEPA governance process which by European standards is poorly resourced. It is also very keen on the development of a European credit card scheme that languishes behind expectations. Against this background the ECB has implored the banks, regulators and the IT software industry to simply get on with the job and it will help resolve the outstanding issues. Progress, however, continues to be pitifully slow especially in light of a worldwide banking crisis.

It is clear across Europe that, irrespective of SEPA, banks are facing major challenges with their payments services as we are witnessing a trend of reduced margins with a steady decline in revenue per transaction.

BCG (Boston Consulting Group) in their latest survey entitled 'Weathering the Storm: Global Payments 2009' reflected the mood of the industry and concluded that European banks should avoid any substantial SEPA-related investment whilst the future remains so unclear. In particular, they are critical of European policymakers forcing payments providers into unnecessary expenditure. More cost-effective focus is required on other initiatives such as setting industry standards for electronic and mobile-payment instruments, and improving payment inefficiencies within specific countries.

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Very importantly, BCG recommends that the large automated clearing houses (ACHs) in Europe should wait until it is confirmed whether full SEPA will actually be achieved before consolidating into one platform. Strategically, ACHs will wish to secure volume but should delay full migration.

Significant change is forecast:

'Since most banks serve both wholesale and retail payments customers, one operating model has traditionally been used to deliver products to both segments. Yet rising customer demands have put pressure on banks. Transaction banking units must thus confront the dilemma of whether to continue using one comprehensive operating model - in order to help achieve scale and cost efficiency - or to split their operating model into wholesale and retail components in order to provide more customised solutions (at the expense of economies of scale and at structurally higher costs). Global banking giants may end up having to forge a completely separate, end-to-end business model for their wholesale transaction banking activities.'
BCG 'Weathering the Storm: Global Payments 2009'

News that the French banks are to delay implementation of the SEPA Direct Debit scheme by a year to November 2010 will also be greatly upsetting to the ECB. Irrespective of the potential benefits of SEPA, the slow transposition of the PSD text into Member State law (with only the UK and Bulgaria on track) appears to suggest a lukewarm approach on the Continent to greater regulation governing payment services combined with a hint of protectionism?

The main SEPA deadline of November 2012 looks pie-in-the-sky and very wishful thinking. Substantial progress will require significant drive from within the EU/EEA political process to re-engage cross-border enthusiasm for SEPA.

Despite the best intentions, SEPA has drowned under the complexity of rival and viable national payment systems with few seeking to invest in an area likely to guarantee only ever diminishing returns and market consolidation.

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