



## SEPA: Changing times for payments

July 27, 2009

In the Single Euro Payments Area (SEPA) all euro payments are "domestic" payments – including those made between two EU countries. New SEPA schemes for credit transfers and direct debits as well as requirements for infrastructures and technical standards apply SEPA-wide. They are designed to enable cross-border euro payments to be handled as efficiently and inexpensively as transactions currently executed within national bulk payment systems.

The conditions for achieving a critical mass of SEPA-standard transactions have not yet been fulfilled. Only just under 2% of all credit transfers in the euro area are executed according to the SEPA standard, although SEPA credit transfers have been offered by banks and payment service providers since January 2008. It is important to inform particularly those users with large transaction volumes – corporates and the public sector – about the benefits and technical details of SEPA. The introduction of the SEPA direct debit in November 2009 will enable these users to streamline their IT-based payment processes: differing national standards can then be consolidated into a common SEPA standard for both credit transfers and direct debits.

Full migration to the SEPA schemes is necessary for the single market to yield efficiency gains. National legacy schemes must be discontinued after a manageable period of coexistence with SEPA so that the single European market for payments can actually become a reality. The retention of national standards would result in a "mini-SEPA" with legacy schemes being used for national payments and SEPA schemes being used for cross-border payments in the EU. Market participants, the European Commission and the ECB are involved in discussions on a potential end-date for the coexistence of payment schemes. Such an end-date should be agreed and come into force on an EU-wide basis.

SEPA is designed to foster competition. In the market for debit cards, however, the threat of an EU-wide duopoly looms. The existing debit card systems in Europe can only handle payments within individual national markets. SEPA, however, requires that card schemes can be used for cross-border payments. Either at least one European debit card scheme with at least regional coverage can successfully be created or the EU market will be dominated by a duopoly of the international card issuers Mastercard and VISA.

SEPA will intensify the restructuring and consolidation in the payment services segment. Shrinking margins will force providers to process large transaction volumes in order to remain competitive. Given the large investments for SEPA and increased competition banks will have to consider which payment-handling processes to perform inhouse and which ones to outsource. The first European link-ups have been established between national clearing organisations.

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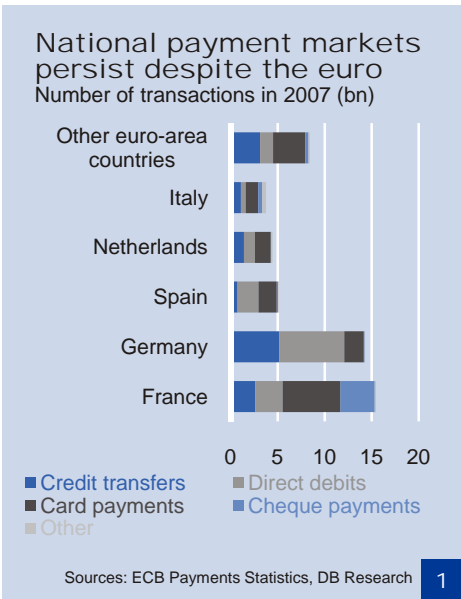
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Every euro payment – regardless of whether it is a cash or non-cash transaction – is a clearly visible sign of Europe’s economic integration. The introduction of the single currency did not, however, bring about any change to the national fragmentation of non-cash bulk payments, i.e. credit transfers, direct debits and card payments. These payments have been and are being automated within member states – and are thus handled much more efficiently and inexpensively than payments made from one member state to another. Since over 95% of retail payments are domestic payments the IT-based payment systems were originally set up on a national basis. Legal provisions, processes and technical standards therefore differ from country to country and are incompatible. Up until now this had meant that payments made outside national systems, for example credit transfers between Frankfurt and Madrid, could not be executed at a similarly low cost to credit transfers between Frankfurt and Hamburg.

EC Regulation 2560/2001<sup>1</sup> obliges the providers of payment services – under certain conditions – to charge their customers the same fees for cross-border payments within the EU as for domestic payments. The political pressure surrounding this issue was thus transformed into the economic pressure to create a European system for retail payments.<sup>2</sup>

**What is SEPA?**

The European banking industry, as the main provider of payment services, subsequently initiated the Single Euro Payments Area (SEPA) to devise the necessary common technical and organisational standards. The goal is to enable retail payments in euro between two accounts maintained in SEPA countries to be handled just as efficiently and inexpensively as payments within the current national payment systems. As things currently stand, the SEPA countries comprise the EU’s 27 member states as well as Iceland, Norway, Liechtenstein and Switzerland. For the euro-area countries the single euro payment area is attained when all domestic and intra-European retail payments comply with SEPA standards and the national systems have been replaced. In the euro area national markets will give way to a European market.

**Who’s behind SEPA?**

The European Payments Council (EPC) is the leading institution behind the development of SEPA. The EPC was established by the European banking industry. The members of the EPC’s committees and working groups are representatives of individual banks and the national banking associations. Corporates, consumers and infrastructure providers influence the shaping of standards via the stakeholder fora of the EPC. Its main priorities are to create common schemes for payment instruments and lay down SEPA-wide rules for the infrastructure and technical standards.

**SEPA: Payment schemes, infrastructures and technical standards**

**SEPA payment schemes**

Based on existing national schemes, rulebooks have been approved for SEPA credit transfers<sup>3</sup> and direct debits<sup>4</sup>. This means that for the whole of Europe there are common rules governing the design of

<sup>1</sup> EC Regulation No. 2560/2001 on cross-border payments in euro, December 19, 2001.  
<sup>2</sup> For a dynamic and innovative European payments market, prices must result from a market process balancing the supply and demand sides of payment services. Please see Mai, Heike (2005). Payments in Europe: Getting it right. p. 3-4.  
<sup>3</sup> EPC, SEPA Credit Transfer Scheme Rulebook – Version 3.2 Approved, June 2008.  
<sup>4</sup> EPC, SEPA Core Direct Debit Scheme Rulebook – Version 3.1 Approved, June 2008.

**Additional Optional Services can be offered**

payment instruments, for example with regard to procedures, execution times and data structure. All SEPA credit transfers and direct debits must strictly comply with these rules so that a barrier-free European payment market can actually be created. This is the only way to guarantee the seamless automated transfer of money from one account in country A to another account in country B. If one national banking sector deviates from the common standards, this market would be protected from European competitors within its national borders.

Nonetheless groups of banks can offer Additional Optional Services (AOS) – in strict adherence with the rules – in order to satisfy the specific user requirements. One example is the plan by Greek banks to support the use of Greek characters in the SEPA format in addition to the Latin alphabet. Additional Optional Services must be described in detail and their descriptions must be disclosed publicly.<sup>5</sup> Each SEPA bank can sign up to an agreement governing an AOS and then offer the service. Since Additional Optional Services are primarily geared towards country-specific user requirements, very close attention has to be paid that they do not compromise either the rules of the scheme or interoperability and thereby do not create barriers to competition. AOS should not be confused with VAS (Value Added Services). Individual banks can develop Value Added Services based on the SEPA schemes to provide greater benefits to their clients and to distinguish themselves from their competitors. One example would be supplementary services for handling SEPA direct debit mandates.

**SEPA direct debit**

- Cross-border direct debits made possible for the first time
- Submission 2 banking days before due date (debtor's debit date) for recurring direct debits and 5 days for first time or one-off direct debits
- Debtor can return the direct debit up to 8 weeks after the payment has been debited from his account
- Returns by the debtor bank must be effected no later than 5 days after the due date
- International Bank Account Number (IBAN) and Bank Identification Code (BIC) instead of national account number and bank sort code
- Direct debit mandate: debtor gives a signed mandate to the creditor; when the direct debit is submitted the transaction data includes the mandate in digital form; the digital mandate data is forwarded by the clearing organisation to the debtor bank; the mandate expires 18 months after the last initiated direct debit
- New end-to-end data elements that simplify electronic processing by users' accounting departments: mandate number, creditor identifier
- Originator reference and remittance information (if supplied by creditor)
- Dedicated field to indicate "on-behalf-of" payments

**SEPA credit transfer**

- Bulk payments (non-urgent) in euro
- Maximum execution time of 1 banking day (max. of 3 banking days until 2012)
- The full amount credited to the beneficiary account with no deductions
- No cap on the value of the payment
- IBAN and BIC instead of national account number and bank sort code
- Full remittance information transmitted (max. 4 x 35 characters)
- Dedicated field for originator reference, if supplied by the originator
- Dedicated field to indicate "on-behalf-of" payments

<sup>5</sup> List of disclosed Additional Optional Services on the EPC homepage.

**Infrastructure**

In addition to the common payment schemes an infrastructure is required to execute the clearing and settlement of payments between the banks of the originator and the beneficiary. The infrastructure providers include Automated Clearing Houses (ACHs), card processors and other processors that process, forward and exchange payment data. The EPC has described the role and procedures to be performed by infrastructure providers in a separate rulebook<sup>6</sup>, based on the rules for SEPA credit transfers and direct debits. In this rulebook, the Clearing and Settlement Mechanisms (CSMs) are divided into five categories which are distinguished by, on the one hand, the number of banks reachable via this mechanism and, on the other, by the organisational requirements. A pan-European ACH (PE-ACH) must provide reachability to all SEPA banks. STEP2, the European Banking Association (EBA) clearing platform, enables the direct or indirect reachability of no less than 98% of all financial institutions that have signed up to the SEPA Credit Transfer Scheme.<sup>7</sup> EBA STEP2 is therefore frequently described as the only PE-ACH to date. A PE-ACH must meet the most exacting demands with regard to open and fair access in usage and governance. In the other CSM categories the reachability can be restricted to certain markets or the clearing and settlement can be performed on a decentralised basis between various banks without recourse to an ACH. Payment providers decide for themselves which CSMs they use to clear and settle payments. It is thus left to the market to decide which clearing and settlement structures will actually develop and become established. Clearing houses disclose their compliance with the provisions of the rulebook on the EPC website.

**SEPA Clearing and Settlement Mechanisms (CSMs)**

PE-ACH: Pan-European Automated Clearing House (ACH) that can settle SEPA payments with all banks in SEPA (full reachability) and that can be selected by all SEPA banks as a clearing house.

SEPA-compliant ACH that can process SEPA transactions within a defined market, i.e. does not (yet) provide reachability for all SEPA banks.

Multilateral and/or bilateral CSM: Decentralised, structured clearing and settlement of SEPA transactions between several participants in a defined market without using an ACH.

Bilateral: Decentralised clearing and settlement of SEPA transactions between two participants in a defined market (e.g. correspondent banking).

Intra-bank/intra-group: clearing and settlement of a payment in which the accounts of both the originator and the beneficiary are maintained by the same bank or group.

**Technical standards**

The EPC has defined the necessary technical standards to enable the automated processing of bulk payments between banks. The data that must be supplied for payment execution, such as the details of the originator and beneficiary, can be derived from the rulebooks for payment instruments. For SEPA transactions the accounts must be identified by IBAN and BIC; national account numbers and bank sort codes will no longer be used. These data elements are presented in the UNIFI (ISO 20022) XML message standard, i.e. the structure and format of the payment messages are uniquely defined and form the basis for the interoperability of

<sup>6</sup> EPC (2007). Framework for the Evolution of the Clearing and Settlement of Payments in SEPA. Version 1.1 Approved (for short: PE-ACH/CSM Framework). January 2007.

<sup>7</sup> EBA Clearing (2008). STEP2 SCT settlement migrated to TARGET. Press release on December 9, 2008.

payment infrastructures in the EU. These standards are compulsory in the interbank domain. They are also the basis for the standards developed for the communication between customers and banks.<sup>8</sup> If other standards are used for data exchange in the customer-to-bank domain, the bank has to convert them into the SEPA standard.

The XML-based ISO standard designated for SEPA payments is not a proprietary European standard, but is derived from a newly developed, universal ISO messaging standard for the financial sector. If this becomes the established standard for global payments, European banks could use the same basic standard for both SEPA and global foreign transactions.

### SEPA for card payments

#### SEPA Cards Framework

In the card payments segment SEPA is designed to enable European customers to use their “general purpose card” for euro payments or withdrawals from cash dispensers inside SEPA just as easily and conveniently as in their home country. To achieve this objective the EPC has not, however, developed a sole scheme for SEPA card payments, as was the case with the SEPA credit transfer and the SEPA direct debit. Instead it approved a framework of basic principles and guidelines (SCF – SEPA Cards Framework).<sup>9</sup> Providers of card schemes that meet these standards offer their competing schemes as SEPA card payments.

#### Payment cards

Payment cards are not always categorised according to the same criteria. The three basic criteria to be distinguished between are the debit amount, the point at which the amount is debited and the account from which the debit is made. Hitherto, most definitions have assumed that the account to be debited is the current account of the cardholder with the card-issuing bank. For credit cards special credit card accounts are also the norm. The definitions used below for debit and credit cards are based on the categorisations used by the European Commission and the BIS.

|  | Date                            | Amount                              |
|--|---------------------------------|-------------------------------------|
| Debit card   | Immediately                     | In full                             |
| Charge card<br>(also called delayed/deferred debit card) | At the end of the agreed period | In full                             |
| Credit card  | At the end of the agreed period | Part, remainder is revolving credit |

#### Objective: more competition in the card market

The framework is intended to remove the barriers to market entry and promote competition that boosts efficiency in the card payment market. Card systems can specialise in debit cards or credit cards or offer both. Girocard (which operated under the name electronic cash until 2007) is one example of a pure debit card provider; Mastercard and VISA offer both credit and debit cards. The players in the card market comprise card firms, that can have a variety of legal forms,

<sup>8</sup> EPC, SEPA Credit Transfer Scheme Customer-to-Bank Implementation Guidelines. Version 3.2 Approved. October 2008. EPC, SEPA Core Direct Debit Scheme Customer-to-Bank Implementation Guidelines. Version 3.2 Approved. December 2008. EPC, SEPA Business-to-Business Direct Debit Scheme Customer-to-Bank Implementation Guidelines. Version 1.1 Approved. December 2008.

<sup>9</sup> EPC, SEPA Cards Framework. Version 2.0 Approved. March 2006.

**Interoperability**

issuers and acquirers – often banks, data processing companies, software suppliers or hardware providers.<sup>10</sup>

Before market barriers can be removed there must be interoperability in the card market: cardholders, issuers, acquirers and merchants need to be able to choose between card schemes solely on business grounds and without technical or legal restrictions. The medium-term objective is that the technical infrastructure will allow every card scheme to be accepted at every card terminal, and that thus the consumer decides without technical preselection which of the cards accepted at a store or cash machine he wishes to use. The EPC is working on establishing the basis for interoperability and gradual harmonisation of technical standards.<sup>11</sup> The core business and functional requirements are to be developed for the interfaces: card – terminal, terminal – acquirer, acquirer – card issuer as well as the security standards and certification processes for cards and terminals.

**SEPA Cards Framework**

The SEPA Cards Framework (SCF) applies exclusively to transactions with the following characteristics:

- Payments or withdrawals from cash dispensers within SEPA using cards issued by SEPA banks. Additional services offered by card issuers such as a credit line are not within the scope of the Framework.
- Euro used as the currency of the card transaction; euro used as clearing currency between acquirer and issuer.
- Transaction guaranteed to the merchant's acquirer in accordance with the terms and conditions of the relevant card scheme.
- EMV chips on cards and the option of PIN usage at terminals is obligatory from 2011.

The SEPA standards to be fulfilled by card schemes are designed to promote competition and transparency:

- Non-discriminatory and transparent criteria for the participation of SEPA banks in a card scheme.
- Licence always issued to a bank for the entire SEPA, not for individual countries; at a bank's discretion it may enter into only an issuing licence or only an acquiring licence.
- Transparent SEPA-wide pricing structure: no bundled prices but individual prices for different services.
- Separation of the card scheme's brand governance and management from the provision of other services like data processing (use of specific service providers for data processing, certification etc. may not be mandated; card scheme may however offer such services itself).
- Open instead of proprietary standards.
- Compliance with the SEPA Cards Framework is based on a voluntary commitment. A card scheme itself declares its implementation and compliance with the SCF criteria; there is no official body that attests to the compliance of a scheme.

**“Every card at every terminal“**

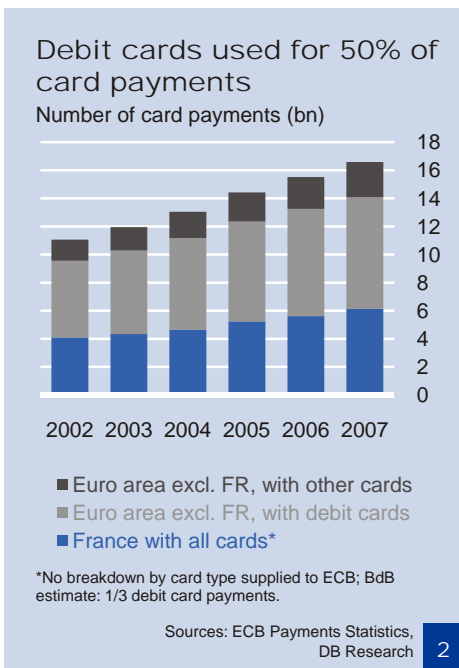
The slogan for card payments in Europe is “every card at every terminal”. The wording of the SEPA Cards Framework is, however, more modest. An SCF-compliant card is required to be usable throughout the territory of SEPA, i.e. the card must be capable of being issued and acquired on a SEPA-wide basis. As is already the case, however, each merchant makes the individual decision which cards to accept or decline. This can mean that despite a consumer's

<sup>10</sup> For an overview of card payments and card systems see Mai, Heike (2005). Payments in Europe: Getting it right. p. 22ff.

<sup>11</sup> EPC, SEPA Cards Standardisation „Volume“. Version 3.2 Approved. December 2008.

card being SEPA-compliant it cannot actually be used in all SEPA countries. The European Commission and the ECB expressly support this definition and point out that, for example, a legacy national card scheme is SCF-compliant with regard to its geographical coverage if it satisfies the technical and commercial conditions for admitting banks from other SEPA countries.<sup>12</sup> Geographical coverage is not an issue with credit cards or charge cards as they have long been usable throughout Europe as well as internationally. Mastercard and VISA dominate the European market. Among other providers, American Express and Diners Club offer credit and charge card services. In the SEPA context no changes are expected in this market.

**Status quo in the card market**



Debit cards are used for a little over half of all card payments in the euro area, according to available data.<sup>13</sup> The debit card segment is dominated by national schemes that serve the markets for domestic payments. The only means of using a debit card for foreign transactions up until recently was Mastercard’s Maestro scheme, which dominates the market for cross-border debit card payments. Maestro is often offered as a complement to the national scheme on one debit card (co-branding) to enable the cardholder make card payments in or to foreign countries. VISA is currently positioning its V-Pay European debit card with merchants and card issuers. Both schemes can make use of the respective credit card networks and offer Europe-wide acceptance.

Various strategies for the national debit card systems are conceivable in order to expand their geographical coverage beyond national borders and to enable them to be used as extensively as possible across Europe:

1. Replace the national card schemes with the international alternatives (Maestro, V-Pay),
2. Co-brand the national schemes with the international schemes for cross-border transactions, or
3. Create a European card scheme. The latter could be achieved by
  - (a) Establishing alliances between existing national systems,
  - (b) Expanding a national scheme to cover the whole of Europe, or
  - (c) Creating a completely new European scheme.

**National providers: SEPA strategies**

The market is showing the first signs of the SCF’s impact. The Euro Alliance of Payment Schemes (EAPS) is an alliance of national debit card systems (3a) that offers cross-border payments with the national systems being preserved but being interlinked. To date, the participants are operators of debit card and cash dispenser schemes from Italy (Bancomat, Pagobancomat), Spain (EURO 6000), the UK (LINK), Portugal (Multibanco), Germany (girocard) and the cash dispenser network of the savings banks in Europe (Eufiserv). Under the working title “Monnet Project” a group of German and French banks is currently assessing the feasibility of another alternative, namely of setting up of a completely new

<sup>12</sup> European Commission, European Central Bank, Payments: Commission and ECB welcome clarifications on a SEPA-wide payment cards market, IP/08/1268, August 21, 2008.

<sup>13</sup> The ECB payments statistics do contain a “card payments” reading for France, but it is not broken down according to the types of card payment, which is why France is not included in the analysis. In 2007 the total number of card payments made in France exceeded 6 billion, representing 37% of all card transactions in the euro area.

European debit card scheme with a common infrastructure (3c). If a decision is made to go ahead with the scheme, attracting more participants will be an important objective. PayFair, another initiative for a European debit card scheme, is being driven by the non-bank sector.

**Increased competition requires more providers**

As far as the competition situation is concerned, the creation of a European card scheme (3) is the only way to really break up the *de facto* duopoly of MasterCard and VISA, whose credit and debit cards can be used Europe-wide. However, this presupposes that the Maestro and V-Pay debit card products are available not only for international but also national transactions in all SEPA countries. The co-branding of national and international schemes (2) would leave the status quo unchanged with respect to competition, i.e. within national borders for national payments and complemented by Maestro or V-Pay for cross-border payments. The replacement of national schemes with international ones (1) would not boost competition either as the number of providers would fall.

**Greater efficiency requires uniform infrastructure**

If besides increased competition another objective is to generate efficiency gains from economies of scale, a card scheme must process more transactions than is currently the case in the national market.

Economies of scale at the European level are, however, only possible within a SEPA-wide common technical and organisational infrastructure – assuming such a system has a commensurate share of the EU card market. A new European scheme with a common infrastructure and governance would fulfil this condition (3c), as would the expansion of a national scheme (3b) with the appropriate standards to other countries. Linking up existing national schemes (3a) via “switching stations” for cross-border transactions would, by contrast, set national markets more firmly in stone. Such a “mini-SEPA” would not enable the optimum economies of scale to be achieved in the volume-driven payments market. The banks would only be making investments for cross-border transactions that make up a very small proportion of all card payments (an estimated 1-2% of the total). These investments are unlikely to yield unit cost reductions on account of the low number of transactions. Innovations would also be difficult to implement in a scheme comprising different technical standards and governance structures. The European Central Bank (ECB) would accept such a formal SEPA compliance at best as an interim solution.<sup>14</sup>

**ECB and EU...**

Both the ECB and the European Commission are exercising their clout with regard to shaping the market conditions in the European card business. The ECB derives its competencies in the payments segment from its statutes which charge it with promoting the smooth operation of payment schemes. It also draws up standards for supervision of payment schemes. This is the background to the ECB's support for SEPA. With regard to the card payments segment, the ECB issued early warnings that SEPA could bring price increases for cardholders and merchants if national debit card schemes were to be replaced by Mastercard and VISA. The combination of less competition, the profit-oriented type of company, the business models and cost structures of Mastercard and VISA raised concerns of upward pressure on pricing.<sup>15</sup> The national card

**... for competition...**

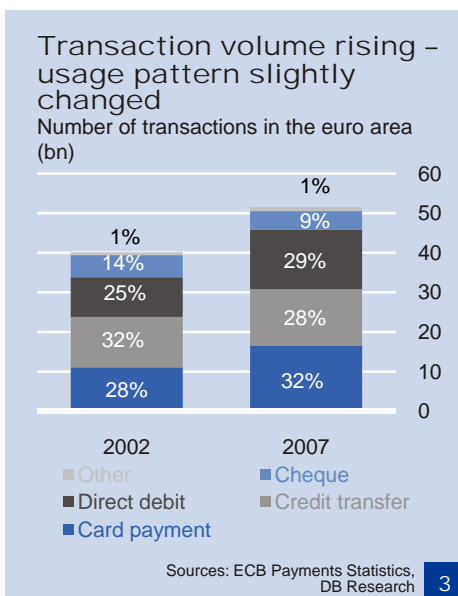
**... against higher prices...**

<sup>14</sup> Gertrude Tumpel-Gugerell, Member of the Executive Board of the ECB (2008). Do you SEPA? The ECB's point of view. Keynote speech at the third International Payments Summit in Milan. October 27, 2008.

<sup>15</sup> ECB (2006). The Eurosystem's view of a “SEPA for cards”. November 2006.

**... for the creation of a European card system**

**EU providers: strategic positioning**



schemes in Europe have traditionally been owned by the banks in their national markets. Although the interbank alliances in the oligopolistic markets for infrastructure do raise competition concerns, the situation could be a great deal worse for end-users with listed, shareholder value-driven card companies, according to the ECB.<sup>16</sup> The European Commission is also determined that SEPA should not be misused to replace inexpensive national debit card systems with more expensive schemes, as happened in the United Kingdom and Austria when they changed over to international systems.<sup>17</sup>

It is a political objective of the ECB to promote the creation of a European card system whose rules could be made or decisively influenced in Europe by European market participants. A new European card system could bring greater diversity to the business models and governance structures in the market. It should be operated under EU law and thus personal information should be processed in accordance with EU data protection rules.<sup>18</sup> The ECB and the European Commission are both pushing for the EPC and the European banks to redouble their efforts to set up a SEPA for cards and create at least one new European card system.<sup>19</sup>

For banks, data processors and also merchants in the EU the question whether and how to create a European card system will impact their strategic positioning in the European card market. A third European debit card system can only strengthen their negotiating position vis-à-vis the international card organisations. The key factor in the decision for or against such an investment is, however, the expected profitability of a new card scheme for the supply side. The market is interesting, as card payments already make up 32% of non-cash payments in the euro area or 37% in the entire EU. Moreover, the market is expanding; card payments are the convenient alternative to cash payments in many purchasing situations. In the period 2002-2007 card usage in the euro area increased by an average of 10% per year, and by 12% in the EU as a whole. Only direct debits have posted similarly vigorous growth, but they lag behind card payments in absolute terms, accounting for 30% of non-cash payments in the euro area or 28% in the EU as a whole.<sup>20</sup>

On the cost side, profitability is highly dependent on the number of transactions executed and economies of scale achieved. On the revenue side the decision by the European Commission on the multilateral interchange fee (MIF) will influence the potential shape and the business case of new debit card systems. At present the multilateral interchange fee is observed and monitored by the European Commission's Competition Directorate-General and the corresponding national authorities in order to ensure competition is not impaired.

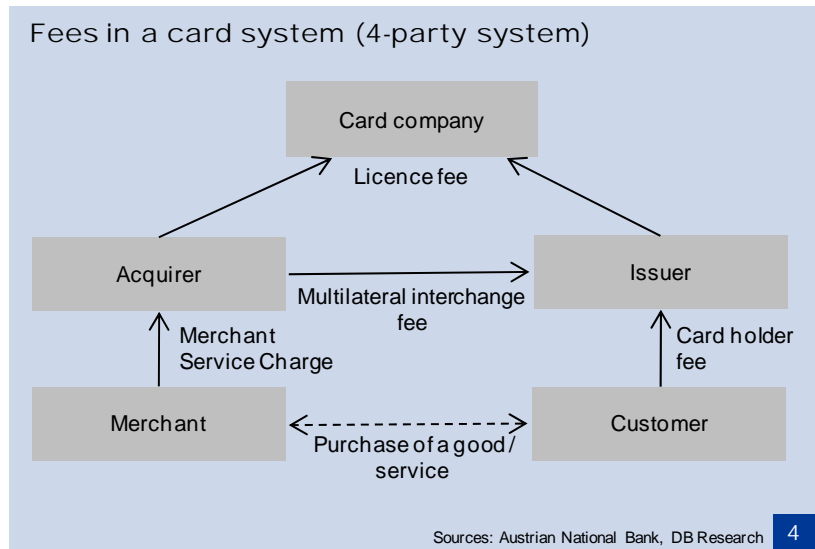
<sup>16</sup> Jean-Michel Godeffroy, Director General Payment Systems and Market Infrastructure, ECB (2007). New card schemes for Europe. Speech at the Télécom Paris conference in Paris, October 26, 2007.

<sup>17</sup> Neelie Kroes, European Commissioner for Competition (2008). Europe's payment systems after the MasterCard decision. Speech on the occasion of the ERRT (European Retail Round Table) Conference in Brussels, January 14, 2008.

<sup>18</sup> ECB (2007). Single Euro Payments Area (SEPA). From concept to reality. Fifth progress report, July 2007.

<sup>19</sup> ECB (2008). Single Euro Payments Area (SEPA). Sixth progress report, November 2008. European Commission, European Central Bank, Payments: Commission and ECB welcome clarifications on a SEPA-wide payment cards market, IP/08/1268, August 21, 2008.

<sup>20</sup> ECB Payments Statistics. 2007 data, i.e. the latest available figures, DB Research calculations.



### Multilateral Interchange Fee – definition and debate

The multilateral interchange fee is remitted by the bank of the card-accepting merchant (the acquirer) to the card-issuing bank (the issuer) for the issuer's services (e.g. authorisation, payment guarantee). This fee is levied as part of the mostly turnover-based fee that a merchant has to pay to the acquirer for each card payment transaction (also referred to as the Merchant Service Charge). Ultimately merchants will pass on this fee to their customers if possible. The size of the multilateral interchange fee can be negotiated bilaterally or multilaterally. If no agreement has been made between the issuer and the acquirer, the "Fall Back Rate" of the respective card organisation is applied. Acquirer and issuer pay a licence fee to the card organisation.

Opponents of the multilateral interchange fee call it an unjustified markup that card-accepting merchants are forced to pay. Supporters of the multilateral interchange fee regard it as a payment to the card issuing institution which would otherwise not get the opportunity to be paid for the services it provides during the card payment process. Charging the cardholder a transaction-based fee is regarded as unrealistic as the customer can choose to pay cash instead, for which the merchant cannot demand a direct fee from the customer.

### More competition in an attractive market

The hitherto unclarified legal situation and the debate surrounding the central issue of the multilateral interchange fee make it difficult to forecast how the card market will develop and whether new providers will enter the market. The market must remain free to allow supply and demand to constantly set new prices. Only if the market remains attractive to providers – issuers, acquirers, card systems, data processors – and it is possible to make a profit will new suppliers enter the market and invigorate competition with their own pricing and service concepts. This will in turn expand the range of options open to merchants and increase their market clout. Only in cases of anti-competitive behaviour is there a need for state intervention by the competent antitrust authorities.

### Migration

#### SEPA: Status quo

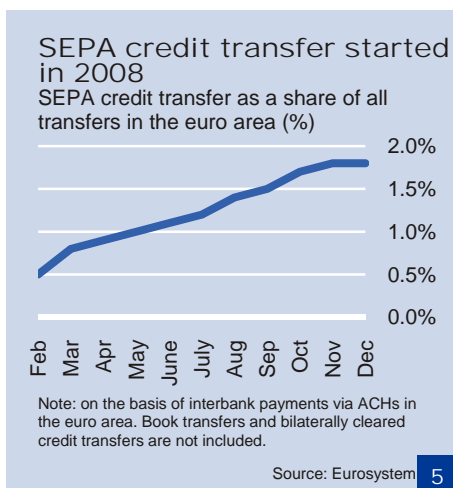
The changeover from the legacy national payment systems to the new SEPA scheme requires adjustments to be made by both providers and users. The banking industry has made SEPA credit transfers available to its customers since 2008. There are now 4,472 banks participating in the SEPA Credit Transfer Scheme which process the vast majority of all payments in the SEPA territory. Experience to date shows that SEPA credit transfers are executed efficiently and with a very low error rate. According to a report covering 16 European countries on the quality of the SEPA credit transfer in the start-up phase there were a few shortcomings in the reproduction of the remittance information and with returns. Two-

thirds of test transfers were, however, credited after one banking day, while the maximum execution time of three days was overrun in only 2% of transactions.<sup>21</sup> The SEPA direct debit will only be available to customers after the transposition of the Payment Services Directive (PSD) into national law, i.e. from November 2009 at the latest. During an interim period from early 2008 until late 2010 an SCF-compliant payment card is defined as a card that is branded with at least one SCF-compliant card scheme. After that date, only SCF-compliant schemes will be allowed on the SEPA payment card. The efforts to achieve technical standardisation in the card payment segment are to be completed by the end of 2010.

**Critical mass of SEPA transactions**

The superseding of the old schemes by the new ones is to be made irreversible by 2010, according to the EPC, by achieving a critical mass of SEPA transactions, and ultimately this is to result in the discontinuation of the national systems. Given the migration plans published by the euro area banking industries<sup>22</sup> this date does seem very ambitious, though. Critical mass is not expected to be achieved until after 2010 and is more likely to be attained for SEPA credit transfers than for SEPA direct debits as the latter will not be available until after the implementation of the PSD from November 2009. The aim is to keep as brief as possible the period in which SEPA and the national systems operate side by side in order to minimise the costs of duplication for users and suppliers.

**High-volume users are key**



In order to achieve critical mass it is primarily the high-volume transaction users – corporates and the public sector – that need to be convinced of the benefits of the SEPA schemes. To date, bank customers use SEPA payments almost exclusively for cross-border intra-European transfers. In September 2008 the SEPA scheme was used to execute 1.5% of all credit transfers in the eurozone, which corresponded to around 7 million transactions.<sup>23</sup> Using SEPA for domestic payments will be made much more attractive by the introduction of the SEPA direct debit in November 2009, as the entire payment-processing IT can then be reconfigured. According to the ECB, the changeover to SEPA direct debit should be facilitated by making as effortless as possible the conversion of existing direct debit mandates – known as *Einzugsermächtigungen* in Germany – into SEPA mandates, for example as part of the transposition of the PSD into national law.<sup>24</sup>

**Corporates and SEPA**

A survey in September 2008 revealed that a large majority of the 182 companies that responded (82%) were convinced that they could boost their efficiency with the help of SEPA. Nevertheless most respondents (61%) were only in the planning phase for SEPA. And more than one-third (35%) of respondents did not have any migration plans for SEPA. The main reason cited for this discrepancy between expected positive effects and hitherto hesitant adoption of SEPA was the cost of IT modifications for SEPA schemes, but the dearth of information about SEPA, BIC and IBAN and the lack of prioritisation of the project were also mentioned. Some of the respondents saw SEPA as not yielding any clear economic benefits.<sup>25</sup>

<sup>21</sup> ABK Systeme / eFIS Financial Solutions und ibi research an der Universität Regensburg, SEPA – Ready for take-off?, May 2008.

<sup>22</sup> Overview at <http://www.ecb.int/paym/sepa/timeline/html/index.en.html>.

<sup>23</sup> ECB, Single Euro Payments Area, Sixth progress report, November 2008, p. 13.

<sup>24</sup> ECB, Single Euro Payments Area, Sixth progress report, November 2008, p. 13.

<sup>25</sup> gtnews, October 28, 2008.

Companies named the following obstacles to the implementation of SEPA schemes...

|   | %  |
|---|----|
| Systems development requirement               | 45 |
| Lack of demand from business partners         | 30 |
| Low priority of SEPA project                  | 29 |
| Unclear business case                         | 27 |
| Insufficient information about SEPA solutions | 22 |
| Insufficient advice on BIC and IBAN           | 19 |
| No senior management buy-in                   | 14 |
| No cross-border business                      | 8  |
| Other   | 11 |

Sources: gtnews, Taking Stock of SEPA, Survey of 182 companies in September 2008.

6

For these migration hurdles to be cleared providers need to offer customers attractive products and beef up their active communication on the topic of SEPA. Solutions to potential migration obstacles are currently being developed. To facilitate the changeover from account numbers and sort codes to IBAN/BIC the German banking industry is already offering its customers an automated conversion.<sup>26</sup> In other countries, too, transformation aids have been made available.

#### The benefits of SEPA

SEPA enables companies and public administrations with Europe-wide operations to reduce their payment transaction costs: by further centralising and streamlining their account structure, IT systems and related management in the individual countries. Moreover, European standards for payment data will enable greater automation in the field of account reconciliation. Users are also provided with new data fields which will make it easier to assign payments. For example, dedicated fields can be used to enter information on "on-behalf-of" payments and originator references. Greater centralisation of payment management also makes the control and risk management tasks in cash management easier to perform. The bundling of national payment volumes into one provides customers with a stronger position when negotiating on price with potential transaction banks. In the medium term EU-wide competition can be expected to bring about convergence between local price levels and lower fees in high-price national markets.

With the advent of SEPA, companies will also have access to completely new products: for the first time it will be possible to collect cross-border direct debits. In addition, a special direct debit for inter-company payments has already been approved by the EPC and can be implemented by payment providers if they wish. The EPC is working on concepts to support online payments: the SEPA credit transfer is to be augmented with online authorisation and a real-time payment guarantee ("SEPA online payment"). The SEPA direct debit scheme offers the option to handle the mandate electronically i.e. issuance, validation and exchange in a four-party system ("SEPA eMandate"). In the SEPA environment there are also initiatives to develop more products like payment execution by mobile phone, same day value payments or e-invoicing.

### The public sector and SEPA

The public sector is responsible for some 20% of all payments in the euro area, which means that the migration of public-sector payments onto SEPA schemes is of key importance.<sup>27</sup> Despite the political will to integrate the European payment markets many public administrations have hitherto been hesitant about migrating their own payments onto SEPA. Solving the above-mentioned difficulties should, however, make it easier for the public sector to adopt a key role in the single European market for payments, so that the efficiency gains and economies of scale slated by policymakers do materialise. The EU institutions plan to complete the migration to SEPA credit transfers by mid-2009.<sup>28</sup>

### Objective: SEPA replaces legacy schemes

SEPA is not to be understood as a supplementary payment service offering, but will replace the national payment schemes in the medium term since national systems run counter to the principle of the single European market. The continued existence of national payment schemes for domestic transactions and the use of SEPA for foreign transactions only would lead to a "mini-SEPA" and would satisfy the demands of neither the European Commission nor the ECB.<sup>29</sup> If the old schemes and SEPA were to operate side by side for an unnecessarily long period this would reduce the cost savings

<sup>26</sup> <http://www.bv-zahlungssysteme.de>.

<sup>27</sup> European Commission (2009). Annual Progress Report on the State of SEPA Migration in 2008, March 2009.

<sup>28</sup> *ibid.*

<sup>29</sup> European Commission (2006). Consultative Paper on SEPA Incentives. February 2006. ECB (2008). Single Euro Payments Area (SEPA). Sixth progress report. November 2008.

**Debate about end-date for co-existence of schemes**

for users and the synergies for providers that SEPA is expected to yield. Europe-wide competition and the expected efficiency gains can only materialise in a legally and technically harmonised Europe-wide market.

This is the reason for the debate about setting an end-date for the old schemes. There could be different end-dates for credit transfers and direct debits. Such a fixed timetable, communicated well in advance, would give users with high transaction volumes a reliable planning horizon for their budgeting and the implementation of the measures required for the changeover to the SEPA schemes. The European Association of Corporate Treasurers (EACT) supports a fixed end-date for national schemes to be replaced by the SEPA Credit Transfer – subject to a number of product enhancements – and has proposed a procedure for a smooth transitional phase.<sup>30</sup> However, there are market participants – both users and providers of payment services – who have reservations about an end-date or would like to see the national schemes continue to operate alongside SEPA. The reasons for these reservations could be, for example, that their business is focused on the national market or the concern that the changeover to SEPA schemes could jeopardise existing business practices that are based on the traditional national systems.

**ECB and EU favour an end-date**

As the debate is conducted throughout the ranks of market participants it must not be forgotten that both the ECB and the European Commission unequivocally demand that SEPA be implemented. In its Sixth Progress Report the ECB called on providers to work harder to offer an attractive and broad range of SEPA products. It also strongly advocates a realistic, but ambitious end-date to the co-existence of national schemes and SEPA.<sup>31</sup> In June 2009, the European Commission has launched a public consultation on a possible end-date for migrating legacy payment instruments to SEPA products. Stakeholders are invited to give their opinion on actual end dates and on related details like implementation by self-regulation or legislation.<sup>32</sup> At the same time it has repeatedly stressed that the SEPA schemes must offer price/performance characteristics that are at least as good as those of the national schemes.<sup>33</sup> In August 2008 the Directorate-General Health and Consumer Affairs published a comprehensive report on payment services and prices in the various European countries in order to provide a benchmark for future reports monitoring the impact of SEPA and the PSD on consumers.<sup>34</sup>

**End-date must be the same throughout the EU**

In order to guarantee fair competition conditions an end-date should be agreed and come into force on an EU-wide basis. Otherwise, individual national markets could keep out European competitors for longer by choosing distant end-dates.

<sup>30</sup> EACT(2008). Press release Single Euro Payments Area: EACT favours setting an end-date for SEPA Credit Transfer. October 15, 2008.

<sup>31</sup> European Commission. Commission launches consultation on possible end-date for SEPA migration. IP/09/884. June 8, 2009.

<sup>32</sup> European Commission (2009). Commission launches consultation on possible end-date for SEPA migration. Press release IP/09/884. June 2009.

<sup>33</sup> E.g. Charlie McCreevy, European Commissioner for the Internal Market, (2008). Single Euro Payments Area (SEPA). Speech at the 7th International EPCA Conference "Releasing the power of payments". La Hulpe, April 1, 2008.

<sup>34</sup> Directorate General Consumer Protection (2008). Preparing the Monitoring of the Impact of the Single Euro Payment Area (SEPA) on Consumers. August 18, 2008.

## Directive on payment services in the internal market 2007/64/EC

### Scope

After five years of debate and consultation between the European Commission, banks, consumer organisations and sector associations, the Council of the European Union and the European Parliament passed the Directive on payment services in the internal market (PSD) in November 2007. The transposition of the directive into national law by November 1, 2009 at the latest will thus create a common legal framework for payment services within the EU. Iceland, Liechtenstein and Norway will also transpose the PSD into national law, which will mean that the directive applies to the whole of the European Economic Area (EEA). The directive constitutes an important legal basis for SEPA, but has a wider scope: the PSD applies not only to SEPA schemes but also to the existing national payment services, i.e. for payments in all EU/EEA currencies within the EU/EEA by credit transfer, direct debit or card. Other areas also covered include the paying of cash into an account, cash withdrawals and the issuing, acceptance and settlement of payment instruments.

### Boost competition – strengthen consumer protection

The objective of the PSD is to foster competition in the EU payments market. Both the European Commission and the ECB expect that this will in turn boost cost efficiency and innovation in the payments segment. Furthermore, it is intended to boost the rights of payment service users with special attention being paid to consumer protection.<sup>35</sup> The European Commission in particular expects competition to intensify and thus the prices of payment services to fall.

### New: payment institutions

As the EU-wide legal basis for payments the PSD is the necessary precursor and complement to SEPA and makes a vital contribution to enabling the single market for payment services to become a reality at all. Alone the breaking up of hitherto national payment markets by SEPA will intensify competition among the providers – mainly banks up until now. In addition, the introduction of the newly created “payment institution” category is designed to make the market more competitive. After being licensed in one member state payment institutes can, under certain conditions, offer payment services and related ancillary services and operate payment systems in all member states. Besides the explicitly mentioned payment services, e.g. the execution of payments against credit balances or credit lines, payment institutions can at the same time conduct other business operations. For example, telecommunication companies or retail groups might like to provide payment services to their own customers or to an alternative clientele. In addition to banks and payment institutions the PSD also permits e-money institutions, post giro offices, central banks and member states or their different levels of government to operate as payment service providers.

### Rights and obligations of payment service users and providers

The rights and obligations of users and payment service providers are specified in detail in the PSD. Providers are obliged to furnish users with the terms and conditions of the contract, in particular with regard to fees and execution times. The same applies to transaction-related information. Rules on transparent pricing are intended to make it easier for customers to compare services. The PSD also regulates the execution of a payment, e.g. with regard to

<sup>35</sup> Joint Declaration by the European Commission and the European Central Bank on the occasion of the passing of the Directive on payment services by the European Parliament. Brussels, April 24, 2007.

## Provisions of the EU Payment Services Directive (PSD)

### Preamble

- I Subject Matter, Scope and Definitions
- II Payment service providers
  - Payment institutions: Authorisation, Capital requirements, Activities, Supervision
  - Access to payment systems
- III Transparency of conditions and information requirements for payment services
  - Single payment transactions
  - Framework contracts
- IV Rights and obligations in relation to the provision and use of payment services
  - Authorisation of payment transactions, liability
  - Execution of payment transactions, execution time and value date
  - Data protection
  - Out-of-court complaint and redress procedures for the settlement of disputes
- V Implementing measures and Payments committee
- VI Final provisions
  - Obligation on member states to transpose directive in full
  - Review of PSD in November 2012

payment authorisation, irrevocability of the payment and liability for unauthorised or incorrectly executed transactions. Several provisions of the PSD on transparency and usage of payment services can be waived in the contracts between companies and payment service providers and alternative agreements can be reached. In dealings with consumers, by contrast, no deviations from the directive are permissible. There is no contractual freedom with regard to maximum execution periods and the value date as these are the means by which the lawmakers aim to guarantee the efficiency of payment services and the transparency of pricing. For example, the PSD stipulates for payment transactions in euro that the payment must have been credited to the account of the user's payment provider by the end of the business day following receipt of the payment order at the latest. Until January 1, 2012 a maximum execution time of 3 business days can be agreed between provider and user. These periods can be extended by one more day for payments that are initiated in paper form. For incoming payments the credit and value date for the payee's account must be the day on which the payee's payment provider receives the funds. For outgoing payments the value debit date for the payer's account is no earlier than the point in time when the funds leave his account.

The transposition of the EU Payment Services Directive into national law has to be as harmonised as possible to enable the creation of a single market for payments. The European Commission is actively shaping this process. At the start of 2008 the Commission set up a working group consisting of representatives from all member states to preclude differing interpretations of the PSD's rules and definitions. However, the PSD does explicitly provide national parliaments with freedom of choice in implementation in a number of areas.

## Outlook

SEPA and the PSD offer payment providers new opportunities and framework conditions that will lead to consolidation in the market. Insourcing, outsourcing and also offshoring will restructure the payment processing market. All banks will of course continue to provide payment services to their customers in order to be able to manage their accounts. The question is, however, whether the banks will continue to perform those process tasks that are invisible to the customer inhouse or to outsource them.

Differing estimates of the investments that the banks need to make for SEPA are made in various reports published by management consultancies. Despite their differing methodologies these reports do nevertheless suggest that the banking sector will have to make investments totalling several billions of euros.<sup>36</sup> So every bank will thus have to face the strategic question of "make-or-buy?". In 2007 a survey of big banks in Europe revealed that 58% of respondents did not want to perform a large proportion of their payment processing themselves or wanted to outsource it in the following five years. 68% of these banks were also planning to offshore. A small group of banks – 15% – have decided to adopt the opposite strategy: they already process the payments of other banks or plan to become insourcers.<sup>37</sup>

## Investments for SEPA

<sup>36</sup> Overview provided by Schmiedel, Heiko (2007). The Economic Impact of the Single Euro Payments Area, ECB Occasional Paper Series No 71. August 2007, p. 10.

<sup>37</sup> Capgemini, ABN AMRO, EFMA, World Payments Report 2007, p. 48.

## High transaction volumes essential

This development is, however, not only being driven by the initial investments in new IT and processes; an even more significant factor is the need to process larger transaction volumes in order to achieve competitive unit costs. Winning a large share of the EU market as well as efficient work processes are the decisive factors. Banks that already possess Europe-wide expertise and market presence in the payments segment find themselves in a privileged starting position. As an alternative to seeking economies of scale smaller providers could also select a strategy of specialisation, offering additional services tailored to selected client groups. Large providers can also pursue a twin-track strategy: they can satisfy clients' demands both by handling large volumes of payments at competitive prices as well as by offering special additional services.

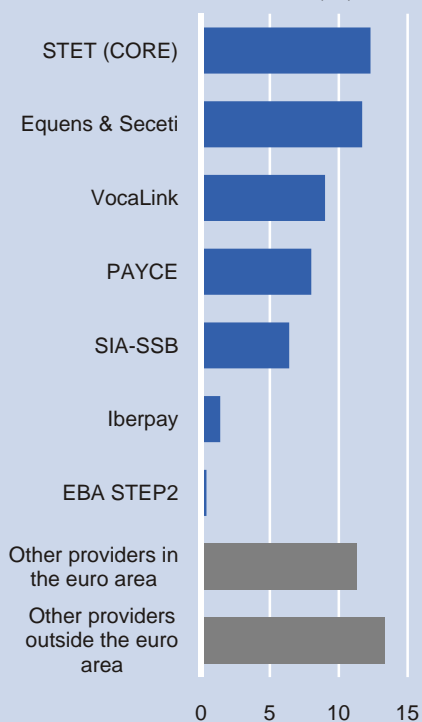
## Consolidation has commenced

In the market for clearing and settlement of payments the imperative to process large volumes of transactions is already leading to the first consolidations. Taking SEPA into account, a number of national ACHs or their operating companies are positioning themselves for the coming Europe-wide payment market. Volumes exceeding 10 billion payments need to be processed each year in order to achieve unit costs in SEPA that are the same as those already being achieved in countries with high transaction volumes. Given the roughly 51 billion payments per year in the euro area<sup>38</sup> this would leave enough room for a handful of clearing houses for bulk euro payments.

To date, ACHs have only provided national coverage on account of the technical and legal obstacles. In a number of countries one dominant clearing centre has developed – for example in France and in the Netherlands. In other countries there are several clearing houses: for example, for different payment instruments – as in the UK or Spain – or subsystems of a central clearing and settlement system as in Italy. In Germany, in contrast to other countries with high transaction volumes, around 85% of bulk payments are cleared in a decentralised system called “garage clearing”; i.e. most payments are cleared bilaterally between the banks or banking groups. The existing clearing systems are thus starting from very different positions with regard to transaction volumes and the range of payment instruments processed. A number of clearing providers are aggressively increasing their capacity via mergers and insourcing: Equens S.E. – the product of the merger between ACH Interpay of the Netherlands and the German cooperative banks' Transaktionsinstitut für Zahlungsverkehrsdienstleistungen AG – will also soon command a major share of the Italian market after commencing a joint venture with the clearing company Seceti S.p.A.<sup>39</sup> Britain's VocaLink Ltd. not only operates the UK clearing houses BACS and Faster Payments, but will also do this for the leading Swedish clearing house Bankgirocentralen BGC AB.<sup>40</sup> Germany's savings banks are offering other banks the insourcing of SEPA payments – processing and clearing – branded as PAYCE. Even before SEPA has been completely implemented and clearing houses can seek to win banks throughout Europe as participants the data processors are attempting to secure sufficient volumes in the market via consolidation. In the segment for processing card

A few providers dominate clearing and processing in the EU

Number of transactions in 2007 (bn)



Sources: ECB Payments Statistics, company data, DB Research

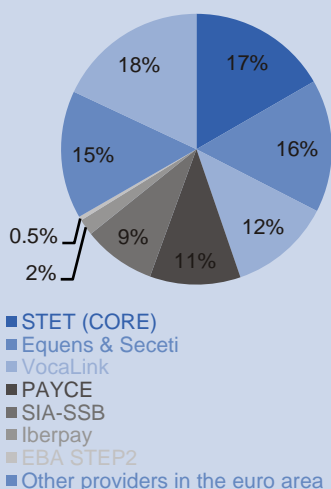
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<sup>38</sup> ECB Payments Statistics. Total number of payments in the euro area in 2007.

<sup>39</sup> Equens SE, Gruppo ICBPI. Press release on September 15, 2008.

<sup>40</sup> VocaLink Ltd. Press release on May 15, 2008.

Oligopoly foreseeable in the SEPA market for clearing and processing  
Share of transactions in the EU, 2007 (%)



Sources: ECB Payments Statistics, company data, DB Research

8

**Competition in payment processing**

**SEPA to reduce bank profits**

According to an ECB survey, Europe's big banks expect their profits to shrink as a consequence of more intense competition once migration to SEPA has been completed. Even though a number of banks associate SEPA with new areas of business, the report's respondents generally assume that the long-term decline in unit costs will not fully offset the decline in revenues. The report comes to the conclusion that the industry as a whole expects profits to be lower than in a scenario without SEPA.

The impact assessment conducted at the behest of the European Commission also forecasts that with full SEPA implementation banking industry profits will be lower than in a world without SEPA. However, what is also being considered in this case is the sector's absolute profits over several years: even with SEPA, the banking sector will make bigger absolute profits from payment business than in the base year for the report (2006). The rising number of non-cash transactions – a trend that has nothing to do with SEPA – would more than compensate for the narrowing of margins and thus prevent a decline in absolute profits compared with 2006.

payments, too, SEPA-driven market concentration can be observed in the form of takeovers.<sup>41</sup>

As detailed in the SEPA Rulebook for Clearing and Settlement Mechanisms, besides the use of a PE-ACH – currently only EBA STEP2 for SEPA credit transfers – there are alternative methods of clearing and settling payments. Existing national ACHs believe that SEPA necessitates an expansion in their coverage and they want to offer their clients not only a link with EBA Clearing but also their own channels: they have united to form the European ACH Association (EACHA) and agreed on standards for reciprocal links.<sup>42</sup> On this basis Equens already has functioning links with Iberpay (Spain), VocaLink, Seceti and DIAS (Greece).<sup>43</sup> VocaLink signed a cooperation arrangement for SEPA payments with WestLB as part of the German savings banks' joint clearing network PAYCE.<sup>44</sup> In addition to clearing payments via clearing houses that provide differing levels of coverage banks can of course also choose bilateral clearing within SEPA. For big European banks in particular this is an alternative to centralised CSMs operated by third parties. It is only once national restrictions disappear, i.e. when SEPA has been fully implemented, that it will become apparent which clearing routes and providers will establish themselves in the market by merging with other entities or poaching clients from competitors.

The market for payment clearing is closely linked with the offering of payment processing services. Apart from performing "plain-vanilla" clearing many providers also act as insourcers, offering back-office solutions for banks that range from individual process steps right through to end-to-end payment handling. Other players in this market are banks that regard payment handling as their core business and act as insourcers, offering processing and clearing services to other payment providers. To date, only banks have had direct contact with the users of payment services as the account maintaining institutions for private individuals, companies and public administrations. Licensed as payment institutions, ACHs and data processors will soon have the opportunity to maintain end-consumers' accounts themselves and offer their payment services directly.

Market consolidation is being driven not only from the cost side, but also by the downtrend in prices. Cross-border competition can be expected to bring down prices, although depending on the current national price level. Potentially greater economies of scale in the EU market will be passed on to consumers via falling prices. Despite all the difficulties involved in predicting market developments the assumption is that the banks' profit margins on payments will shrink considerably due to SEPA. Market share must therefore be increased so that a larger number of transactions can offset lower unit profits.

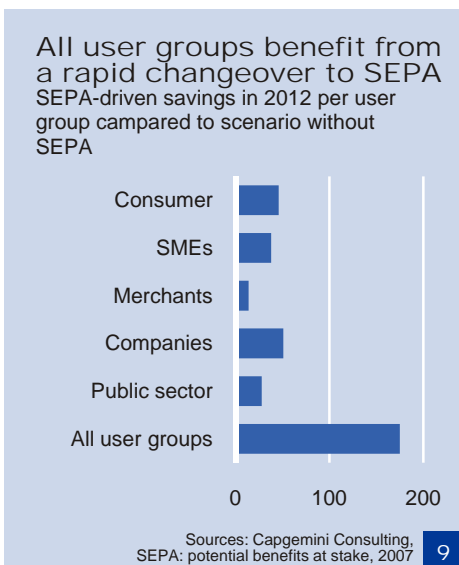
Regardless of whether they are banks, payment institutions or data processors, payment processors have to generate very large volumes of transactions in order to prevail in European competition despite margins being squeezed even tighter. SEPA will speed up

<sup>41</sup> European Commission (2009). Annual Progress Report on the State of SEPA Migration in 2008, March 2009.

<sup>42</sup> Equens SE, Sociedad Española de Sistema de Pagos S.A. Iberpay, Seceti S.p.A., STET, VocaLink Ltd., Press release October 2, 2007.

<sup>43</sup> Equens SE, Self-assessment based on the terms of reference for SEPA compliance of infrastructures established by the European Central Bank, September 2008.

<sup>44</sup> PAYCE, Press Release October 2, 2008.



### Single market requires full implementation of SEPA and PSD

consolidation; the number of processing centres in the single European market will be much smaller than in the existing nationally fragmented payments business.

How the restructuring on the supply side will take shape in the newly created single market for payments hinges on how intensively corporates, public administrations and consumers will utilise the opportunities presented by SEPA and the PSD. The sooner and the more vigorously that especially high-volume users select providers on a cross-border basis, the greater the pressure on providers to offer the corresponding services. The EU-wide harmonisation of internal processes and the bundling of order volumes will strengthen the negotiating position of companies vis-à-vis potential providers of payment services. In shaping products and standards the users of payment services also have a direct impact on market developments, for example, in the Customer Stakeholder Forum of the EPC.

According to the European Commission's impact assessment<sup>45</sup>, consumers along with large and small businesses will benefit from having to spend less on payment processing within SEPA. SEPA will also bring significant cost savings for public administrations and merchants. This applies both to the demand and supply sides, as long as SEPA is implemented swiftly and the period of coexistence of national schemes and SEPA schemes is kept brief ("SEPA Big Time"). This scenario would be the best fulfilment of the objectives of the Payment Services Directive and of SEPA. Without full migration, but with a large number of customers calling for SEPA products from their banks, the savings would be lower but also tangible for all user groups ("Demand Pull").

SEPA and the EU's Payment Services Directive are already showing an impact on the supply side: SEPA credit transfers have been available to users since January 2008 and the first SEPA-driven mergers and alliances have materialised in the payment-processing segment. The expected efficiency gains for the economy as a whole can, however, only be achieved if the PSD and SEPA are fully implemented across the entire SEPA territory and are also taken up by users. Only under identical EU-wide competition conditions can payment providers throughout the single market compete for customers with their respective price/performance offers. And only under uniform SEPA-wide standards can economies of scale in the European payments market be achieved via consolidation among suppliers. The long-term retention of national payment schemes – alongside SEPA – would prevent the single market for payments from becoming a reality.

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<sup>45</sup> Capgemini Consulting (2007). SEPA: potential benefits at stake.

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