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**TOWARDS A SINGLE EURO PAYMENTS AREA -  
THIRD PROGRESS REPORT**

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*Previous publications:*

- *Improving cross-border retail payment services - The Eurosystem's view, September 1999*
- *Improving cross-border retail payment services - Progress report, September 2000*
- *Towards an integrated infrastructure for credit transfers in euro, November 2001*
- *Towards a Single Euro Payments Area – (2<sup>nd</sup>) Progress report, June 2003*

## **EXECUTIVE SUMMARY**

This report explains the Eurosystem's interest in, and work towards the establishment of, the Single Euro Payments Area (SEPA). It compares the objectives of the SEPA with today's situation, and highlights what has been done, notably by the European banking industry, and what remains to be done to meet the expectations of the euro area citizens. The report takes as a basis the long-term view of the SEPA project's ultimate objective, as defined by the European banks: to transform the euro area into a fully integrated domestic payments area.

### **The SEPA objectives**

For citizens in the euro area, a real SEPA will be achieved when they can make payments throughout the whole area from a single bank account, using a single set of payment instruments, as easily and safely as in the national context today. For the customer, it should not make any difference where or with which bank in the euro area this account is held. The Eurosystem's vision for the SEPA, hence, is that all euro area payments should become domestic and reach a level of safety and efficiency at least on par with the best performing national payment systems today.

In the White Paper of May 2002, 42 European banks and the European credit sector associations clearly expressed a similar vision. They want everyone's payments within the SEPA to be as easy and inexpensive as in his or her hometown. Therefore, the Eurosystem welcomed banks' creation of a European Payments Council (EPC) in June 2002 to implement their political commitment to make the SEPA a reality by 2010.

Early in 2004, the Eurosystem received signals from several bankers indicating that support for the SEPA project and its objective had weakened. According to these critics, the SEPA goal of a domestic payment area would have to be revisited in view of the transition costs. Some bankers wished to limit the project to cross-border payments in order to avoid having to change national payment systems into a pan-European system. While the Eurosystem is open to a discussion of implementation problems, it cannot compromise on the final objective. Payment systems have to conform to the European people's desire for a single currency. If the EPC proves unable to deliver on the SEPA, alternative solutions will have to be explored. Therefore, in order to ensure European citizens the full benefits of the SEPA, the EPC is invited to reconfirm its commitment to the SEPA White Paper and to present a convincing project plan with realistic milestones.

The Eurosystem understands that, in line with the objectives of the White paper, a fully-fledged SEPA infrastructure will be available by end-2010 at the latest. Therefore, it is desirable that a SEPA for citizens should be achieved in January 2008 by offering citizens and commercial enterprises the chance to use pan-European instruments for national payments also.

Thus, in a first phase banks would be able to offer to customers pan-European instruments, services and standards in parallel to national services, standards and instruments. The pan-European services would

allow customers to make all their euro payments – national and cross-border – in one format from one account. In a second phase, once national instruments, services and standards have been gradually phased out and replaced by pan-European ones, national infrastructures would be either abolished or transformed into pan-European ones.

Defining the SEPA objectives is clearly the EPC's responsibility. However, the project may be implemented differently across countries, depending on local conditions. In order to drive national implementation, the Eurosystem expects the respective national banking communities to translate the pan-European SEPA objectives into national migration plans that allow each bank and infrastructure provider to adapt its strategies and solutions to move progressively into the SEPA. National central banks stand ready to contribute to the local implementation of the SEPA objectives. The EPC should monitor each national banking community's contribution to SEPA. The Eurosystem intends to monitor progress regularly.

## **Payment instruments**

From a customer perspective, achieving a SEPA requires in practice that the different payment instruments become pan-European. Concerning credit transfers, there is currently a clear difference between national and cross-border credit transfers. The challenge is to transform Credeuro from a cross-border service only for payments up to € 12,500 into a basic credit transfer service functioning for all retail payments in euro in the euro area. In addition, there is a need to complement Credeuro with a service for same-day value payments (labelled "Prieuro" in the EPC terminology) in order to achieve a service offer at least on par with the best performing national markets today. Therefore, the Eurosystem proposes the following two intermediary steps towards establishing pan-European standards for all euro-denominated credit transfers in the euro area by 2010:

First, the Eurosystem would like to see Credeuro (and the supporting interbank charging convention ICP) become the compulsory minimum standard for retail cross-border credit transfers in the euro area falling under the Regulation on cross-border payments in euro (2560/2001) by 1 January 2006.

Second, euro area citizens should have Credeuro and Prieuro as optional standards for national credit transfers from 1 January 2008.

At present, direct debits are not even available at a pan-European level. For the pan-European direct debit (PEDD), the challenge for the EPC is to make up for initial delays on the project. Therefore, the Eurosystem urges the EPC to pursue the PEDD project without further delay in order to achieve the euro area-wide use of the PEDD by 2010. In order to ensure a SEPA for all citizens, the Eurosystem recommends that the PEDD be made an optional standard available for all euro area customers' national direct debits from 1 January 2008.

Prior to the introduction of the euro, there was already a well-developed service offer for using cards in cross-border transactions. However, the market is strongly segmented into national and international card solutions. Thus, we are still far from a SEPA in which any cardholder would be able to use his/her card in

any ATM or EFT-POS, at reasonable cost, with no differentiation within the euro area based on country of origin. Interoperability among card schemes will need to be achieved so that cardholders who request it will be able to use their cards the same way nationally and within the SEPA well in advance of the 2010 deadline. This will require a transformation strategy for both national and international card schemes to respond to the creation of the new domestic payment area. Moreover, in order to combat fraud, it is important that a sufficiently high share of cards and terminals be migrated to the EMV by 1 January 2005 (date on which Visa and Mastercard will apply a liability shift in Europe). As soon as possible, there should only be one harmonised way of implementing the EMV standard, including the use of PIN or other possible anti-fraud measures.

## **Standards**

Standardisation is one of the cornerstones for achieving a SEPA. Therefore, the Eurosystem emphasises the importance of having both 1) a sound governance for the definition, adoption and implementation of standards and 2) a well-defined work programme including relevant milestones. Standards are key to implementing end-to-end straight through processing (STP) in Europe. Therefore, the Eurosystem invites the EPC to complete the work of defining, adopting and implementing standards and business practices for an end-to-end STP payment processing. If needed, available standards and business practices should be reviewed and simplified. The EPC is also invited to reinforce its co-operation with other stakeholders and customers in order to ensure that the standards and solutions identified are suitable for and, to the maximum extent possible, compatible with the entire business chain.

Notably, in the field of credit transfers, the Eurosystem invites the EPC and national banking communities to implement a common account identifier (IBAN) for both national and cross-border credit transfers and direct debits in the SEPA. In addition, the Eurosystem also recommends that the EPC define and implement further common standards and business practises enabling full end-to-end STP for credit transfers in the SEPA, including a unique standard for electronic payment initiation and automated reconciliation. The Eurosystem then expects that similar steps should be developed for other payment instruments as well.

The Eurosystem invites the EPC along with the European Committee of Banking Standards (ECBS) to respond to the seven High Level Recommendations for Standards made in this report. Moreover, there is a need for the standardisation activities to address the specific needs of the SEPA. In this sense, the EPC should become the body guiding the work of the ECBS.

## **Infrastructure**

In previous reports, the Eurosystem concluded that the banking industry's choice for a pan-European automated Clearing House-concept (PEACHes) is a realistic approach to creating a more efficient infrastructure, and therefore welcomed the EPC decision to favour PEACHes based on one agreed model. However, only one PEACH provider currently exists. This development alone has so far not contributed

to the desired consolidation of too many fragmented infrastructures currently operating at a national level. Therefore, in order to stimulate the transformation of the current infrastructures and to achieve increased overall efficiency due to economies of scale and scope, the Eurosystem recommends that a SEPA for the infrastructure be completed by end-2010 by ensuring the development of national SEPA migration strategies. Decisions related to the next generation of national systems should be made from a pan-European perspective to ensure compliance with SEPA instruments and standards and the overall SEPA infrastructure.

### **Governance of the process**

The Eurosystem acknowledged in previous reports that the European banking industry has made progress in terms of co-operation by setting up the European Payments Council (EPC). Banks needed a lot of time to define properly the governance of their SEPA project. Moreover, banks from 28 countries are now associated with the work on the SEPA, although only the 12 euro countries are directly concerned for the moment. This could jeopardise the SEPA's 2010 target date, because the commitment could be different within and outside the euro area. Given that the SEPA is primarily a euro area project, the project's governance should also reflect the distinction between the euro area and the EU/EEA.

Generally, the EPC's ability to deliver on all the SEPA milestones it has set itself would be proof of good governance of the European banking industry. This will require effective project management, as well as an enforcement process for agreed decisions.

In this context, the Eurosystem urges the EPC to:

- make sure that the decisions which primarily concern the euro area are made by euro-area banks, and that they cannot be overruled by a coalition of non-euro area banks and a minority of the euro area based banks;
- ensure that the EPC Secretariat is equipped with the resources it needs to manage the project effectively;
- finalise the integration of the ECBS within the EPC governance in 2004 as promised.

In addition, the Eurosystem invites the national banking communities in the euro area to:

- present convincing arrangements for the implementation of EPC decisions at the domestic level (by 6 months after their adoption at EPC level at the latest);
- present the EPC with a national migration plan during 2005 for the gradual transition to a SEPA before end-2010.

In addition, upon request from several market participants who claim that SEPA cannot be achieved on a voluntary basis only, the Eurosystem might offer the support of an ECB Regulation if and when this could be useful. This would help the SEPA (for the citizens and the infrastructure) become a reality even where banks have difficulties in implementing pan-European payment instruments or fail to deliver a convincing transition plan from national to SEPA infrastructures.

### **Other stakeholders**

The Eurosystem, as the central banking system of the euro area, primarily focuses on the initiatives of the banking industry to achieve a SEPA. However, the Eurosystem is aware of the importance of other stakeholders like Community legislators, governments, merchants, consumers, and corporates. Achievements for customers, including notably corporate customers, are welfare gains for the society as a whole. Moreover, central and local governments sending and receiving a substantial volume of payments play a vital role in encouraging pan-European standards. They have the ability to make pan-European standards compulsory for certain types of payments. Therefore, the Eurosystem encourages respective stakeholders to actively assume their role in making the SEPA a reality. A more harmonised legal framework is an indispensable precondition for achieving a SEPA. The European Commission is currently working on a New Legal Framework for the payment industry. It will be of the utmost importance for the New Legal Framework to be consistent with the SEPA objectives, clear and equally implemented in all Member States.

## INTRODUCTION

The launching of the euro as the single currency in 1999 and the introduction of euro banknotes and coins on 1 January 2002 provided banks the chance to make a quantum leap in transforming still largely fragmented national retail payment systems and diverse instruments into a single euro payments area (SEPA). The objective and benefits of a SEPA are clear. The creation of the euro area will allow the establishment of a modernised, more efficient and sound retail payment network that will be superior to the existing fragmented retail payment infrastructure. The transformation will have to take place from quite a diversity of starting points. It concerns many components and stakeholders. As such, it constitutes a major challenge requiring a profound transformation of the existing infrastructure.

In December 2001, the European Parliament and the EU Council adopted a Regulation<sup>1</sup> on cross-border payments in euro obliging banks to charge equal fees for national and (comparable) cross-border payments. The most obvious discrepancy for many customers was the high charges for cross-border payments compared with national payments.

In June 2002, the European Banking industry, having established the European Payments Council (EPC) as its main co-ordinating and decision-making body for this matter, took up this challenge. The EPC adopted<sup>2</sup> a roadmap with milestones leading up to a SEPA by end 2010 (see Annex 1). While the European banking industry has made real progress, it has also faced obstacles in the elaboration and implementation of its strategy.

The Eurosystem, in pursuit of its mandate to promote the smooth operation of payment systems, has worked intensively with the banking industry, and other relevant stakeholders, to help overcome the obstacles faced in the creation of the SEPA. In that spirit, the ECB has regularly published reports analysing progress for retail payments.

This third progress report covers SEPA objectives (chapter 1), pan-European payment instruments (chapter 2), pan-European standards (chapter 3), pan-European infrastructure (chapter 4), and governance (chapter 5). Finally, Chapter 6 addresses the role that other stakeholders should play to support and complement the efforts currently undertaken by the banking industry.

The present report is aimed at meeting the same goals as previous reports, but focuses more on the customer perspective than previous reports. Therefore, each chapter starts by analysing the objective from a customer perspective (section 1), continues with a gap analysis comparing the objective with the present situation (section 2), and concludes with a proposal for the way forward (section 3).

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<sup>1</sup> EC/2560/2001 requiring banks to apply for (comparable) cross-border payments in euro up to EUR 12,500 the same charges as for national payments

<sup>2</sup> White Paper, "Euroland – Our Single Payment Area", May 2002.  
For further information see [www.europeanpaymentscouncil.org](http://www.europeanpaymentscouncil.org).

## **1 MOVING TOWARDS A SINGLE EURO PAYMENTS AREA 2010: MILESTONES AND OBJECTIVES**

### **1.1 The vision of SEPA as a domestic payments area**

For euro area citizens, the vision of SEPA as a domestic payments area implies that a customer (private or corporate) should be able to execute any payment within the euro area as easily and inexpensively as in his or her hometown. A customer should only need one bank account and one card to make any payment in the euro area safely and efficiently. The Eurosystem realised that due to its complexity, this long-term vision for the SEPA could not realistically be achieved with a big bang, and that only a gradual transformation was possible.

Transforming the euro area's present situation, with 12 different national environments as well as a cross-border environment, into a payment organisation similar to that of a single country should provide considerable welfare benefits. These benefits are illustrated with examples in Annex 2 that show the concrete advantages for corporate and private customers compared with today's situation. When the SEPA is fully achieved, and meets the requirements of corporate treasurers, a corporation will only need one electronic link to its chosen bank. Through that link, it will be able to send payment files to and receive bank statements from all its other banks in one standardised format, regardless of where the bank is located in the euro area.

In addition, the project of transforming the euro area into a SEPA will lead the way for integration throughout the EU. Countries that have not yet adopted the euro will receive clear guidance on what will be expected when they join the EMU. Thus, the SEPA project contributes to the Lisbon Agenda<sup>3</sup> (EU to become the world's most competitive and dynamic economy by 2010).

In the EPC White Paper adopted in May 2002, 42 European banks, the Euro Banking Association (EBA) and three European (credit sector) associations subscribe to the same vision that all payments in the euro area should become domestic, declaring that a full migration to SEPA will be achieved by end of 2010. This implies that today's relatively inefficient cross-border transactions will become a relic of the past, to the benefit of European consumers, industries and banks. Thus, the Eurosystem fully subscribes to the EPC's idea of the SEPA becoming a domestic payment area, achieving levels of service and automation above the best national performance today, by 2010.

### **1.2 Assessment of results**

If the euro area's current retail payment system were assessed as if it was a single country's payment system, it would be rated woefully inefficient. Although there are highly efficient regions, the overall structure is very fragmented and lacks common standards. While recognising some initial tangible results in the area of pan-European credit transfers, the Eurosystem is concerned that the EPC has been significantly delayed in implementing its objectives, especially for standardisation and pan-European Direct Debits (PEDD).

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<sup>3</sup> The Lisbon Agenda explicitly mention integrating financial markets and facilitating the continued consolidation of the financial sector as high priorities requiring the full and consistent implementation and effective enforcement.

### **1.3 The way forward**

Given the risk of a growing perception that the SEPA project might not receive the widespread support and commitment it needs within the banking industry, **the Eurosystem expects the EPC to reconfirm its commitment to the SEPA White Paper and to update it with realistic milestones in the form of a convincing project plan.**

The Eurosystem understands that that, in line with the objectives of the White Paper, a fully-fledged SEPA infrastructure will be available by end-2010 at the latest. Therefore, it is desirable that **a SEPA for citizens be achieved in January 2008 by offering citizens and commercial enterprises the chance to use pan-European instruments also for national payments.**

The Eurosystem takes on a regular monitoring role. This monitoring has been made easier by the fact that the EPC has agreed to provide the ECB with a quarterly status report on progress made in different areas (the “SEPA indicators”). The Eurosystem has received quarterly reports on SEPA indicators concentrating on credit transfers and containing some elements on cards and cash. This progress report is based on the information received up to end-September 2004 (see Annex 3). The EPC has agreed to improve gradually the quality of the reporting in co-operation with the Eurosystem when the scope and the main milestones become clearer. In other words, the SEPA indicator report is a tool for tracking the gradual moves to pan-European standards, business practices, infrastructure and payment instruments until 2010.

In addition, as concrete implementation of the SEPA takes place at the national level, **the Eurosystem also expects the national banking communities in the euro area to translate pan-European SEPA objectives into national migration plans.** This would allow banks and other stakeholders to plan their moves and contributions to the SEPA. National central banks stand ready to contribute to the local implementation of the SEPA objectives. The Eurosystem will monitor each national banking community’s progress towards the SEPA with the assistance of the EPC.

## **2 PAN-EUROPEAN PAYMENT INSTRUMENTS**

### **2.1 Credit transfers**

Bank customers’ and the Eurosystem’s expectations for the Single Euro Payments Area, combined with the Regulation on cross-border payments, have put pressure on banks to develop efficient cross-border credit transfers. In November 2002, the EPC adopted the Credeuro, which is a standard for a “basic” pan-European bank-to-bank credit transfer that guarantees a bank customer charges at the level of a domestic transfer and a maximum execution time of three days. However, even though the European banking sector has made substantial progress in the area of cross-border credit transfers in euro, there is still a way to go until there is a true SEPA without borders.

## **2.1.1 Traditional credit transfers (Credeuro)**

### **Objectives**

Customers have very clear expectations for a SEPA in credit transfers (see examples in Annex 2). Corporate customers would like to see a single standard for electronic payment initiation, enabling them to send all payments in one file and one format regardless of where the beneficiary is situated in the euro area. Similarly, corporate customers also expect to receive all incoming payments in one file and one format, regardless of where they were initiated, allowing for automated reconciliation. As the service level currently differs a lot between different euro area countries, the benchmark must of course be the most efficient national practice. Every customer must be better off than, or at least as well off as, today.

### **Assessment of results**

In its second progress report, the Eurosystem asked the EPC to publish a quarterly list of banks in each country that have adopted the Credeuro. The Eurosystem also asked the EPC to provide information on the share of Credeuro-compliant credit transfers, processed by the banks adhering to the Credeuro convention, as a percentage of total payment volumes.

The report on SEPA indicators as at 30 September 2004 shows that the banks that have subscribed to Credeuro represent a majority of the market in 13 countries. The number of banks subscribing to Credeuro shows a widespread acceptance and awareness of the advantages of pan-European standards.

A high implementation rate for Credeuro among banks does not necessarily mean that the customers are aware of, and use, the Credeuro, since it is banks that choose which services to promote actively and offer to their customers. The EPC has so far not been able to provide information on Credeuro transfers' share of all cross-border credit transfers due to a lack of information on the total volume of cross-border payments. Therefore, the EPC has agreed to conduct a sampling exercise of the major players involved in cross-border payments. The EPC has stated that this exercise could be carried out before end of 2004. The results of the sampling exercise will give guidance as to the need for a campaign to raise customer awareness of the Credeuro.

The EPC adopted the Interbank Convention on Payments – ICP convention – in April 2003 to support the Credeuro and to harmonise the interbank charging practices for cross-border credit transfers. The convention applies to basic STP (straight through processed) cross-border payments falling under the Regulation on cross-border payments. The default charging option under the convention is SHARE, meaning that the payer pays the sending bank's fees and the payee pays the receiving bank's fees. Due to the EC Regulation (2560/2001) on cross-border payments in euro, the charges for both the originator (payer) and the beneficiary (payee) have to be the same as for corresponding national credit transfers. The convention also states that the practice of beneficiary deduction by intermediary banks is no longer acceptable and should be replaced by interbank charges. Four countries (DE, FR, NL and SE) have transcribed the ICP convention into their national banking industry agreements. For the remaining

countries, the number of banks subscribing to the ICP convention is approximately at the same level as the number subscribing to Credeuro.

However, the EPC has so far made very little visible progress in meeting the expectations of euro area citizens, who want all credit transfers in the euro area to be domestic, implying that national schemes, standards and business practices must be replaced by pan-European ones. Thus, Credeuro is still a cross-border standard only and significantly different domestic business practices and standards continue to prevail within countries.

### **The way forward**

The Eurosystem encourages the EPC to survey regularly the share of Credeuro transfers in all cross-border credit transfers. This would facilitate insight into the actual use of Credeuro compared with other payment solutions. Since many customers' choices are restricted to the services provided and promoted by their own bank, it is important that the banks not only implement Credeuro, but also actively promote its use.

The Eurosystem would also like to see the ICP convention implemented in all euro area banks. This should preferably involve its incorporation into the national banking industry agreements. Alternatively, more banks should subscribe to the convention individually. A high take-up rate will help achieve a more transparent charging regime for cross-border credit transfers in euro. The goal is a main charging option for cross-border payments in euro **that ensures that the principal amount is always transferred in full**. Charges on the beneficiary side should only be allowed if beneficiaries are charged when receiving national payments.

The biggest challenge is, however, to develop the Credeuro into the basic pan-European credit transfer service covering all domestic retail payments by 2010. In this context, same-day value is a prerequisite for Credeuro to be able to compete with existing national credit transfer instruments. Therefore, the Eurosystem underlines the importance of following through with the EPC's stated ambition of complementing Credeuro with same-day settlement (Prieuro). Thus, in order to ensure a SEPA for all citizens, the Eurosystem proposes the following two intermediary steps towards establishing pan-European standards only for all domestic credit transfers in the euro area by 2010:

**First, the Eurosystem recommends that Credeuro (and the supporting interbank charging convention ICP) become the compulsory minimum standard for retail<sup>4</sup> cross-border credit transfers in the euro area falling under the Regulation for cross-border credit transfers (2560/2001) by 1 January 2006. Showing its support for this initiative, the Eurosystem has decided that the national central banks of the Eurosystem – in the few instances where they process retail payments – will offer Credeuro and ICP for non-urgent retail payments as of 1 April 2005.**

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<sup>4</sup> Currently up to €12,500.

**Second, euro area citizens should have Credeuro and Prieuro as optional standards for national credit transfers from 1 January 2008.**

### **2.1.2 Innovative payments (e-/m-payments)**

The EPC Task Force on e- and m-payments has met regularly since February 2003, with ECB and ECBS representatives as observers. Its tasks are to analyse the market for electronic and mobile payments and develop a pan-European vision for banks' activities in this field. The work so far has included fact-finding, scope definition and identification of business scenarios. However, Task Force members still have divergent expectations on the future demand for e-payment services. In contrast to the banking sector's slow progress in developing widely accepted e- and m-payment solutions at both the national level and the pan-European level, non-bank competitors have been more active in this field.<sup>5</sup> However, their success also depends on the interfaces and co-operation with the banking sector. **The Eurosystem encourages the market participants from the banking and non-banking sector to enter into a constructive dialogue in order to promote pan-European standards for e- and m-payments.**

## **2.2 Pan-European Direct Debit (PEDD)**

### **Objectives and milestones**

A pan-European direct debit (PEDD) would be very beneficial to corporate customers active in different countries, but it would also be a great improvement for a citizen who, say, pays utilities in more than one euro area country (see Annex 2, example 2 and 3). This is often a main reason for keeping accounts in different countries.

The Eurosystem has encouraged the EPC to devote significant attention to direct debits, since this is one of the most important payment instruments in the euro area. A well-functioning PEDD is also a crucial success factor for any PEACH, as it would provide a critical mass of payments that would make it viable. The EPC had expressed a desire to define a PEDD scheme by 1 July 2003, and concluded that the SEPA's needs would best be served by building a brand new PEDD scheme instead of seeking to harmonise existing national direct debit schemes. The EPC's intention, as stated in the White Paper, is to have the first PEDD transactions processed by 1 July 2005 and to have all direct debit transactions processed as PEDDs by the end of 2010.

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<sup>5</sup> The ESCB is monitoring developments in the market for innovative payments, playing its role as a catalyst. Since 2003 the ECB has been operating the electronic Payment System Observatory (ePSO), an information-sharing Internet platform (see [www.e-psos.info](http://www.e-psos.info)). The ESCB has initiated a survey amongst suppliers offering innovative solutions for e- and m-payments between merchants / consumers and between private consumers. The results of this survey reveal that a substantial number of e-payment initiatives exist, but banks only originate a few of these, and even fewer initiatives are aiming to be pan-European.

## **Assessment of results**

The EPC adopted its definition of PEDD in June 2004 (see PEDD Resolutions in Annex 6), one year behind schedule. Most of the difficulties in reaching an agreement regarding the design of the PEDD stemmed from diverging views regarding the options for the interchange fee structure and the minimum security level required. Furthermore, the EPC has declared that it needs another full year – until mid-2005 – to hammer out the details of the PEDD scheme. Therefore, the first transactions may not be processed until end-2006.

## **The way forward**

The Eurosystem welcomes the fact that the EPC has finally agreed on the PEDD principles. However, the Eurosystem also stresses that from now on the PEDD project must be pursued without further delay. Therefore, in order to ensure a SEPA for euro area citizens, **the Eurosystem recommends the EPC and the national banking communities to make PEDD available as an option for national payments in the euro area from 1 January 2008**. This would be an important milestone towards the endgame of achieving Europe-wide use of the PEDD by 2010. The Eurosystem is prepared to assist the banking industry in the creation of a PEDD, for instance by offering its legal assistance and technical support in addressing relevant issues, in order to keep up progress in this important work.

## **2.3 Cards**

### **Objectives**

Cards are the payment instrument that traditionally has functioned best for cross-border payments within the EU. However, national and cross-border payments within the euro area do not take place under the same conditions. This affects all stakeholders involved (cardholders, card acceptors, card issuers, card acquirers, processors). The differences in fees and efficiency between national and cross-border payments are incompatible with the SEPA concept. They are the consequence of the fragmentation into national markets. National standards, rules, procedures, practices and processors still dominate today. For the cardholder, the SEPA objective is quite clear: he/she expects to be able to use his/her card in any part of the euro area as efficiently as in his/her hometown. This process of transformation will require adaptations from national and international card schemes.

## **Assessment of results**

In order to address the SEPA issues, the EPC plenary endorsed eight recommendations for card schemes in March 2003 (see Annex 6). The recommendations cover, among others, issues related to anti-fraud activities, consistent tariff schemes across the SEPA and the amendment of card scheme rules and conventions to promote the SEPA. According to the EPC calendar, all eight recommendations should be implemented by 1 January 2006 at the latest.

## **The way forward**

The usage of card payments is growing, and the growth is expected to continue with the SEPA, since cards are an easy and efficient vehicle for making payments. The Eurosystem attaches great importance to this payment instrument and organised on 25 March 2004 an ECB *Payment Cards Roundtable* of policy makers and market players in order to discuss the contribution of cards to SEPA.

Moreover, the Eurosystem is currently working together with the banking industry to define a statistical data collection and distribution process that provides an overview of the cards market's evolution in the SEPA.

Although Regulation EC 2560/2001 has already forced banks to apply the same customer fee for domestic and cross-border payments, many hurdles will have to be eliminated before customers can use their payment card in all euro area countries as easily as in their hometown. National and cross-border transactions should be treated identically in order to comply with the SEPA. Ideally, this equivalence should be in place for a large part of the market well in advance of the 2010 deadline, at least as an option for any cardholder who requests it. This encompasses issues like fees, the use of PIN or signature, merchant acceptance rates for cards Europe-wide and the levels of fraud that influence customer trust and confidence in cards, processing and clearing arrangements.

The card industry has to make progress in interoperability in order to meet the SEPA objectives. Cardholders should be able to use their card in the euro area even if the issuing bank and the acquiring bank are based in different countries.

For this purpose, some kind of European interoperability logo might be necessary to distinguish cards that meet SEPA standards and can be processed according to SEPA conventions.

To a large extent, international card schemes already establish the bridge between countries. However, they do this in a similar way within the euro area and outside, i.e. with a relatively high interchange fee which leads banks to levy higher fees on the merchants for cross-border transactions. This result is inconsistent with the SEPA.

There are two complementary approaches the EPC could take in order to achieve the SEPA for cards. On the one hand, they could work with national (and international) card schemes to define standards which would make card schemes interoperable in the euro area. On the other hand, they could discuss with international card schemes what steps are needed to make sure that the financial conditions applied in the euro area do not distinguish between domestic and cross-border transactions. The Eurosystem advises the EPC to pursue both approaches simultaneously.

The EPC's decisions need to be consistent with those made by the card schemes' decision-making bodies to achieve the SEPA for cards.

The most urgent field of action is preventing and combating fraud, which is very high in the euro area cross-border context compared with the national context. Initiatives undertaken in this context should be

made in such a way that they facilitate the SEPA instead of creating obstacles to it. The migration to chip cards, usually using the EuropayMastercardVisa standard (EMV), is one major step towards fraud prevention. However, the EPC reporting on SEPA indicators at 30 September 2004 shows that most countries still have a long way to go before all cards, EFT-POS-terminals and ATMs are EMV compatible. One source of great concern is that the implementation of EMV is not harmonised inside the SEPA, which limits interoperability. This could hamper the EU-wide usability of cards and hinder progress towards one common way of using cards in the euro area. The beneficial effects of EMV in terms of fraud reduction can only materialise if there is a substantial migration of the card infrastructure (in the banking sector) and of the EFT-POS terminals (on the merchants side). On 1 January 2005, Visa and Mastercard will apply a liability shift in Europe. This liability shift stipulates that if a cross-border counterfeit fraud transaction takes place and one of the parties (card or terminal) is EMV-enabled, then the party which is not EMV-enabled is liable for the fraudulent transaction. In this context, the Eurosystem would like to emphasise that it is **important for a sufficiently high share of cards and terminals to be migrated to the EMV by then**. As soon as possible, there should only be **one harmonised way of implementing the EMV standard, including the use of PIN or other possible anti-fraud measures** and the gradual abolition of fallback solutions, etc. In addition, other fraud types (e.g. for card-not-present transactions) should be targeted, as incidents are expected to increase after card-counterfeiting has become more difficult.

Moreover, the EPC is currently analysing the feasibility of creating a European anti-fraud database that includes consolidated information from all card schemes and operators. In its second progress report, the Eurosystem highlighted that fraud is a major concern for consumers, merchants and providers and therefore welcomes any work in this field. The Eurosystem stands ready, if needed, to assist the EPC in implementing this anti-fraud database.

## 2.4 Cash

Euro area citizens have had a SEPA for cash, i.e. using the same banknotes and coins, since 1 January 2002, even though there is still work to be done on the supply side. The Eurosystem has been in the process of defining common principles and objectives regarding its role in the cash cycle. The Governing Council of the ECB has underlined on various occasions the importance of a “level playing field” for NCB cash services. A number of measures have already been undertaken with a view to contributing to a fair competitive environment in this respect and they have been the basis and starting point in this process.

In addition, as underlined in the EPC’s resolution of 10 December 2003 (see Annex 6), the banking industry and other commercial parties concerned (e.g. cash-in-transit companies) have repeatedly asked the Eurosystem to offer a level playing field for euro cash services. This would help individuals and enterprises reap the benefits of the Economic and Monetary Union (EMU) and of the SEPA in general.

In view of the Eurosystem’s prominent role in the cash cycle, it should provide continuity and stability to facilitate the planning of the partners in the cash cycle (i.e. banks, CIT-companies). To this end, the Eurosystem has liaised and met with the EPC’s Cash Working Group and other stakeholders to discuss

questions related to a more efficient cash supply system, including the notable recent discussions regarding the framework for counterfeit detection and fitness sorting by credit institutions and other professional cash handlers.

### **3 PAN-EUROPEAN STANDARDS**

#### **3.1 Objectives in the field of standardisation**

The main reasons for the difference in service for cross-border retail payments and national payments are a failure to use agreed pan-European standards and the low level of automation. This problem, underlined by the Eurosystem for many years, is now well recognized by the European banking industry. Consequently, in May 2002 the European banking industry pledged to develop a common set of pan-European standards, rules, and conventions for basic payment instructions by 1 July 2003 and then implement them. This would allow banks to achieve levels of service and automation across Europe at least equal to the best national performance. The industry also agreed to define an additional set of standards, rules and conventions enabling the provision of value-added or local usage services offering STP and set a timetable for implementation by 31 December 2004.

In its second progress report (June 2003) the Eurosystem underlined that the above-mentioned commitments were encouraging steps towards the objective of defining, implementing and governing all standards needed to turn the SEPA into an effective domestic payments area. In that perspective, the Eurosystem stressed that standardised message formats and bank and customer identification codes, allowing all payments to be fully automated, are important prerequisites for efficient interbank infrastructures. In addition, the Eurosystem emphasised the crucial importance of strong co-operative links first between the EPC and the ECBS, and between those groups and other international standardisation bodies (e.g. SWIFT, ISO) for the setting up of standards. It also emphasised the need for a convincing arrangement for enforcing pan-European standards decided by the EPC.

#### **3.2 Assessment of results**

Work has progressed on the definition, implementation and governance of the standards needed for the SEPA. The Eurosystem recognises that this field of work is perhaps the most challenging of the entire project since it concerns a variety of aspects and since there are strong incentives not to proceed and to stick to well-functioning national, local or even proprietary solutions.

Concerning the **definition of standards**, a number of standards have been fully defined and documented, notably in the field of **credit transfers**. The Eurosystem also acknowledges the EPC's resolution on the Format Rules for Basic Cross-Border Credit Transfers denominated in euro. This is an additional step towards making payments processing fully automated.

However, work on **Pan-European Direct Debit, including the definition of standards, is seriously behind**. Hence, the EPC goal of defining an additional set of standards, rules and conventions enabling the provision of **end-to-end STP** and setting a timetable for implementation by 31 December 2004 is no longer realistic.

The Eurosystem observes serious shortcomings in the **implementation and governance** of agreed standards. These are well recognised by the banking industry. The issue of a governance structure is still not finally settled. In particular, the working structure of the ECBS and the EPC, as well as their interrelations, should be better clarified and streamlined in order to speed up the processes of defining and implementing standards<sup>6</sup>.

There are still problems with implementing agreed standards. As an example, the Eurosystem acknowledges that IBAN has been made available to customers (see Annex 3). However, this does not imply that it is largely used in the payment practice. Hence, more needs to be done, including by stakeholders other than just the banks, if the industry is to progress towards a pan-European account identification that is used in practice.

With regard to **end-to-end STP**, corporate customers are still not able to submit payment orders in a common electronic format across the euro area, as the ECBS's electronic payment initiator has not yet been used as a building block to define SEPA schemes for end-to-end services (such as, for example, e-invoicing, e-payment, and reconciliation services). The e-PI notably supports end-to-end e-services, as the beneficiary can capture all relevant information in an electronic data container, which can be used by the ordering customer to transmit all relevant data to the ordering bank electronically. For the Eurosystem, a unique standard allowing for automated payment initiation and reconciliation (including a standardised payment reference) is a necessary SEPA requirement.

### 3.3 The way forward

Significant work has been done on the **definition of standards**. Progress is also noted on the **implementation and the establishment of effective governance**. This is promising, but far more needs to be done in this field. The expectations of the Eurosystem in the governance of standards are further developed in section 5. Moreover, the Eurosystem has undertaken an in-depth analysis of the standardisation process and developed high-level recommendations (see Annex 5). The dialogue on these has started between the Eurosystem and the EPC. The ECB will, in addition, organise ad hoc workshops in order to foster dialogue with the banking industry and to discuss standards and business practices that are relevant for the SEPA where the banking industry does not have a common view. A first workshop on the e-PI was organised in June 2004. The banking industry should define clearly pan-European basic and value added services. A detailed action plan, based on the roadmap set out in the White Paper, should also define milestones and the timing of when these services will be implemented. The plan should adhere to the approach currently followed in the roadmap, i.e. defining clear milestones in a short-, medium- and long-term view. It should be updated when necessary in order to consider the current status of the work, with, if appropriate, the involvement of other relevant bodies. It is important that the efforts to design standards fit into an overall strategic banking industry action plan. They must respond to a business need

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<sup>6</sup> These processes can be summarised as: 1) assessing the business case and defining the scope; 2) developing and designing the standard; 3) deploying the standard.

(from a SEPA perspective, not necessarily from a cross-border perspective alone) and must be embedded in a widely accepted business model.

Credit transfers and a pan-European direct debit scheme are identified as key drivers for change towards SEPA, and the use of Credeuro and PEDD standards should become obligatory in interbank processing (i.e. each bank in the euro area would have to support the corresponding core data sets). The following action points are therefore suggested:

- the implementation of IBAN<sup>7</sup> as the banking industry's accepted standard for both national and cross-border credit transfers and direct debits in the SEPA. The banking industry is invited to develop a plan to migrate national and cross-border transactions towards this objective and to translate this plan into an **EPC resolution on IBAN implementation**;
- **the definition and consolidation of STP end-to-end credit transfer standards and business practices for the SEPA.** The banking industry is invited to complete the work of defining related standards and business practices, including a unique standard for electronic payment initiation and automated reconciliation. In addition, the EPC should develop a plan to migrate towards this objective and to translate this plan into an **EPC resolution on a single end-to-end STP credit transfer for the SEPA**;
- a further objective could be to simplify pan-European Standards and business practices to make them easier for banks and customers to use. For example, the EPC may consider defining a long-term plan to phase out the use of BIC for customers (in addition to IBAN) and to simplify further the charging options;
- Similar steps should be developed for other instruments.

## 4 PAN-EUROPEAN RETAIL PAYMENT INFRASTRUCTURE

### 4.1 Objectives and milestones agreed

The interbank clearing and settlement infrastructure for retail payments in euro is currently fragmented and lacks efficient automated clearing houses with a pan-European reach. In an industry where fixed costs are high, there is little doubt that the present situation is highly inefficient. In that context, the Eurosystem's second progress report welcomed the EPC's adoption of a concept for the European retail infrastructure (the pan-European automated clearing house -PEACH- concept). Provided that the level of service for national payments does not deteriorate, the adoption of this concept must be seen as a positive development. Its implementation may increase competition, foster consolidation of payment instruments in euro and of the euro retail infrastructure, and pave the way for a reduction of processing costs for all payments. The PEACH concept was adopted together with the definition of two major milestones for its implementation. The first one was to have a first PEACH-compliant service provider operational for

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<sup>7</sup> According to the ECBS version that is more restrictive than, but complies with, the ISO version. Work is ongoing to align these two versions.

credit transfers by mid-2003. The second one is the launch of the next wave of innovations, starting with the processing of the first transactions of the new pan-European direct debit instrument.

According to the Eurosystem's definition, a PEACH could only be truly pan-European if all euro area and EU banks are reachable. For this reason the Eurosystem asked (Second Progress Report) the EPC to ensure that by end of 2003, all EU banks (prior to enlargement) would be reachable via the PEACH. In addition, the Eurosystem supported the EPC's resolution that banks from the New Member States should be reachable by the end of 2004. Moreover, the Eurosystem asked the EPC to confirm that it will work towards processing national payments via PEACH, which would encourage the consolidation into a limited number of infrastructures at the pan-European level by 2010.

## **4.2 Assessment of results**

The Eurosystem is pleased to note that the first PEACH service provider, the EBA Clearing Company, which uses the STEP2 system, has become operational according to plan. In addition, the goal of attaining 100% receiver capability in the first PEACH by end-2003 was almost fully met on time (except for Ireland, where there is still no country entry point). The EBA has actively approached banking communities in the New Member States to try to arrange solutions by the end of 2004. Whether this objective will be fully met is still unclear, especially considering the short implementation time given to these countries after joining the EU in May 2004<sup>8</sup>. In some cases, good long-term solutions might not be realistically implemented until the beginning of 2005. The Eurosystem is also pleased that the EPC has adopted a number of Resolutions that, together with an impact paper, clarify the PEACH concept (see Annex 6).

However, so far the EBA Clearing Company, using STEP 2, is the only PEACH operator. In this regard, the Eurosystem would welcome additional PEACH providers to create the necessary competition. Moreover, the EBA has recognised that in order to be competitive with existing infrastructures and attract also the substantial volume potential in national traffic, it needs to become a full-service provider. To become a competitive alternative for processing national volumes, PEACH service providers need to be able to offer, in addition to credit transfers, a wider range of services including direct debits. For this reason, the EBA has started to analyse the settlement of direct debit transactions, as this is an important payment instrument at the national level.

It must also be noted that even for credit transfers, the present service level requirements (e.g. value limitation to maximum € 12,500, full information to customers, clear roles/responsibilities among stakeholders, 3-day execution time, etc.) are not sufficient to match what is offered at national level. Therefore, at this stage, little national traffic has transferred to the only PEACH that exists.

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<sup>8</sup> As of 15 September 2004, there are 67 STEP2 indirect participants in the eleven countries where there is no entry point. The number of banks per country is: Ireland 6, Estonia 3, Lithuania 4, Slovakia 8, Cyprus 6, Hungary 7, Malta 5, Slovenia 5, Czech Republic 8, Latvia 9 and Poland 6

### **4.3 The way forward**

It is clear that the euro area banks will, in the end, benefit from a consolidation of the infrastructure for retail payments if the final objective is to reduce costs and increase efficiency to at least the level of the most efficient national systems today. However, this process entails adjustment risks and costs that the private sector is reluctant to bear.

In the case of TARGET, a successful example of market infrastructure consolidation, the adjustment costs and risks were born by the Eurosystem. However, the Eurosystem and the banks have already agreed that the private sector should find their own solutions for the SEPA.

Now that the PEACH concept has been defined at the EPC level, the migration path to consolidation is in the hands of the national banking communities. In line with the White Paper, the Eurosystem understands that the PEACH scheme-compliant pan-European infrastructure is to be put in place by 2010. As a next step, the EPC should further clarify the procedure for PEACH assessment. It is expected that during the years 2004-2010, all retail payment systems will have to reinvest. Therefore, at this critical moment, **the Eurosystem expects that banks, as users or as shareholders of the existing systems will impose a SEPA choice. This may include the decision to close the system and to move to another infrastructure or to transform proven and efficient national arrangements into a PEACH-compliant system.**

## **5 GOVERNANCE**

### **5.1 Objectives for SEPA governance**

In its previous progress report in June 2003, the Eurosystem welcomed the fact that European banks had responded to its call for pan-European interbank co-operation by creating the EPC. At the same time, the Eurosystem stressed that the success of the EPC would ultimately be determined by the results it has committed to deliver. The Eurosystem emphasised a need to clarify the decision-making process and the methods for implementing and adhering to decisions. In addition, there was a need to rearrange the working group structure, especially to increase the efficiency of the work on standards.

The Eurosystem has not elaborated formal criteria to assess the SEPA project's governance. As long as the EPC meets its milestones in a timely manner and is able to deliver a SEPA for citizens in 2008 ahead of a full implementation of SEPA by 2010, all while balancing the interest of different stakeholders, the governance will have proven effective. Good project management requires that the high-level SEPA objectives from the White Paper be translated into concrete deadlines and milestones that are regularly and continuously met. The Eurosystem has emphasised particularly the need for good governance regarding the development and implementation of standards, which requires a high degree of co-operation among banks and an efficient co-ordination among the different bodies working on standards. An efficient governance of the SEPA includes the ability to define a coherent and efficient strategy for the implementation of EPC resolutions on pan-European payment instruments, standards and business practices.

## 5.2 Assessment of results

Since last summer, the EPC has already achieved a lot in formalising a governance structure at the pan-European level. The EPC has adopted a Charter and a new structure (see Annex 4) which took effect in June 2004. This is an important step forward.

In its new structure, the EPC has become a legal body under Belgian law with its own dedicated resources and staff. The EPC Plenary is the decision-making body and the Co-ordination Committee determines if proposals are mature enough for the Plenary. Four specific Working Groups focus on payment instruments (Cards, Cash, Direct Debit and Credit Transfers). Two horizontal support groups (Legal and Operations Infrastructure Technology & Standards (OITS)) have been set up. In addition, a Nomination and Governance Committee (NGC) has been formed as an advisory body to the Plenary to oversee the structure, and to propose changes when necessary. The EPC also aspires to a stronger role in creating standards by becoming the leading body with the integration of ECBS. Details and timing of the integration of ECBS into the EPC structure are still unclear. This is still an ongoing process. The Eurosystem is concerned about stakeholders' commitment to solving the governance issue for standardisation. In addition, to facilitate integration of New Member State banks into the SEPA project, the EPC is currently integrating banks from those countries in its bodies.

The Eurosystem welcomes this new governance structure. It allows for a better project focus. Work on standards should benefit in particular from an enhanced and accepted structure. At this point in time, it is still too early for the Eurosystem to assess how the new EPC structure will work.

It should, however, be noted that the voting weight of euro area banks in the EPC Plenary is limited to 59%. The EPC Charter stipulates a 2/3 majority to pass Resolutions. This implies a risk of euro area banks being outvoted despite the fact that the core of the project is highly relevant for the euro area, much more than for other EU countries. Currently, achieving the SEPA by 2010 is a primary concern for 12 countries. In an EPC with 28 countries potentially represented, it is entirely possible that commitment to achieve results in the euro area will weaken. For example, the effort to make IBAN compulsory in the euro area should not be subject to potential disagreement from one or several non-euro area banking communities.

In addition, the Eurosystem considers that the new EPC structure should have sufficient dedicated resources to provide a **professional project management of the SEPA**, something that has so far been insufficient regarding work on standards and pan-European direct debits. In that respect, the resources attributed to the secretariat should be carefully considered. The **main open question**, which is not sufficiently explained in the EPC Charter, is **how the EPC will implement and enforce its decisions for all EU banks**. The EPC Charter refers to the national communities only in very vague terms<sup>9</sup>. As there is not yet a formal link making EPC decisions binding at the national level, a crucial question is how to establish a link from EPC to different national banking associations and communities. The EPC itself has recognised that the involvement of national banking associations in the process is a key element.

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<sup>9</sup> “the national communities shall in particular: promote at local level the realisation of the EPC vision and mission, ... take due care of implementing and monitoring EPC decisions.”

### **5.3 The way forward**

Following the outcome of an EPC strategy meeting on 6-8 September 2004 and the EPC Plenary on 6 October 2004, the EPC is currently considering how to deliver the schemes, standards, rules and conventions necessary to support pan-European credit transfers, direct debits and (debit) cards. However, for the enforcement of these schemes, and for the subsequent consolidation of infrastructures (SEPA for infrastructures by 2010), the EPC puts the responsibility on the national banking communities. The Eurosystem recognises that for the time being the most important delivery that could be expected from the EPC is the definition of pan-European payment instruments, and this needs to be achieved within the next two years to facilitate the Eurosystem's objective of SEPA for citizens by 2008. The subsequent step of implementation is the responsibility of national banking communities in co-ordination with their national central banks. To achieve this implementation in an efficient and harmonised way, the role of the EPC will be to monitor closely national progress. In this context, in order to improve banks' governance of the SEPA project, **the Eurosystem invites the EPC to:**

- **ensure that the decisions which primarily concern the euro area cannot be made by a coalition of non-euro area banks and a minority of the euro area based banks;**
- **ensure that the EPC Secretariat is equipped with the necessary resources for a professional project management to develop pan-European payment instruments.** In this respect, the Eurosystem would also welcome the EPC starting to include **reporting on working group milestones in the quarterly report to the ECB** on SEPA indicators;
- **ensure that the ECBS is integrated within the EPC governance before the end of 2004.**

In addition, **the Eurosystem invites the national banking communities in the euro area to:**

- **present a convincing arrangement for the implementation of EPC decisions at domestic level (at the latest 6 months after their adoption at EPC level);**
- **present to the EPC during 2005 a national migration plan for the gradual transition to the SEPA before end-2010.**

## **6 FURTHER WORK INVOLVING ALL STAKEHOLDERS**

The benefits of common pan-European payments can only be achieved if a critical mass of stakeholders uses them. It is therefore important to create awareness among users of payment services about the benefits and added value those services could generate, thereby creating a widespread demand for pan-European payment services.

### **6.1 Consumers**

Banks will have to work out how to inform and educate their customers in this major and long-term industry-wide migration project. Customers will have to be informed about changes in procedures and

services. The banking industry is the body best suited to provide such information because of its close relationship with customers and in-depth knowledge of services provided. This process can also be viewed as a good opportunity to convey to the consumers the greater possibilities and wider economic and financial network created with the euro.

In its second progress report, the Eurosystem pointed out the benefits of consumer organisations establishing an observatory to monitor banks' payment charges and charging principles and publishing the results. An observatory could enhance transparency tangibly and thus improve competition among banks. Although the Regulation on cross-border payments in euro requires equal prices for national and comparable cross-border payments in euro, the need for an observatory remains. As various price studies by the European Commission have shown, bank charges and charging principles differ significantly among individual banks and different Member States. Since the Regulation on cross-border payments in euro came into force in July 2003, the ECB and the national central banks have received a number of customer complaints regarding banks' charging principles for cross-border credit transfers. Some of these complaints show that not all banks yet apply the Regulation correctly. An observatory would greatly facilitate the comparison of bank services for customers. Consumer organisations are likely to be best suited to establishing and managing such observatories. At a national level, they could compile relevant data that would be fed into a euro area wide database, accessible by the public and managed according to an agreed methodology.

## 6.2 Corporates

The importance of incorporating industry in the development and implementation of the SEPA should not be underestimated. Enterprises of all kinds frequently use payment services and would gain from a more standardised and open structure. Increased international trade and companies with branches in many countries require efficient and smooth cross-border payment services in euro (see also Annex 2).

In May 2003, the ECB arranged a meeting with the EPC and the Euro Associations of Corporate Treasurers<sup>10</sup> (EACT). The subject for the meeting was to understand better corporate treasurers' expectations for SEPA. The main message from EACT was that all parties involved must adopt common standards and end-to-end STP to improve efficiency and to reduce costs. The current situation of diverging national standards and payment information requirements should be abandoned as quickly as possible. The EACT also pointed out that development in this area has so far to a large extent been carried out by banking business, without participation from the final users of payments or banking services. This might be one explanation why banks have not yet been able to meet corporate customers' requests for a common electronic payment initiation standard that enables customers to switch their payment traffic between different banks easily. The initial meeting between the banking industry and the EACT has been the starting point for a regular exchange of information, which would benefit all parties.

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<sup>10</sup> EACT represents over 3,500 treasurers and financial professionals in 10 euro area countries see [www.eact-group.com](http://www.eact-group.com)

### **6.3 Merchants**

Merchants in their role as card acceptors play an important role in achieving an efficient and safe SEPA regarding acceptance of international cards and EMV migration on all their EFT-POS terminals.

The low level of acceptance of international cards at national level is an obstacle to a SEPA because it restricts card usage for the European citizen and limits competition between national and international card schemes. At the root of this problem is the relatively higher level of interchange fees for cross-border transactions. The enhancement of card acceptance internationally is a crucial step towards promoting the SEPA and requires closing the gap between national and euro-area interchange fees.

The co-operation of card acceptors for the EMV migration of terminals is essential because fraud will migrate to non-EMV compliant card acceptors. Only when a critical mass of the market migrates to EMV will EMV make a significant contribution to fraud prevention. In addition, card acceptors should contribute to the gradual abolishment of fallback solutions (i.e. use of magnetic stripe and signature under certain circumstances), which could undermine the benefits of EMV migration.

### **6.4 Governments**

**Governments are important actors in the financial arena, both in their role of setting the future agenda and in their role as a participant, performing financial transactions. Their commitment and involvement should therefore be sought and enhanced.**

The implementation of common standards by organisations with large flows of payments is crucial for establishing a critical mass of users. Some entities among the governmental bodies are transferring or receiving considerable numbers of payment transactions i.e. taxation authorities, customs, health care and transfers to and from social security systems. These entities should be encouraged to start using and requesting common standards (BIC and IBAN) regularly, increasing the awareness of those standards. It would also show the interest and importance the Member States place in this development.

### **6.5 Community legislator**

The European Commission is currently working on a New Legal Framework for Payments in the Internal Market (NLF) as a step towards creating a “Single Payments Area” in the EU. The aim is to make pan-European payments as easy, cheap and secure as national payments are today and to further enhance the single market for payment services by providing a comprehensive legal framework. This is considered essential to maximise the efficiency of the European economy, and in particular electronic commerce. The legislation aims to improve consumer protection and to increase the efficiency and security of payments by removing technical and legal barriers.

The Eurosystem welcomes the objectives of the European Commission’s initiative as a major step towards realising the single market for payment services for the EU.

The aim of the NLF should be to enhance the single market for payment services by implementing the same legislation in all Member States. The SEPA project is, on the other hand, focused on the euro area.

The two projects should reinforce each other. The Eurosystem is providing actively its advice on the legislative project. For its part, it will continue to focus its efforts primarily on achieving the SEPA in the euro area. It will thereby involve the stakeholders of the other Member States and aim for a smooth transition into an enlarged SEPA. In this way, the countries that have not yet adopted the euro as their currency will receive a clear indication of what is expected from them once they join the EMU.

## SEPA OBJECTIVES ACCORDING TO THE WHITE PAPER

### EXTRACT FROM THE EPC'S WHITE PAPER ON A SEPA

#### CHAPTER 6

#### ROADMAP 2002 – 2010

Over the last 5-10 years Europe has achieved a major step forward by agreeing to the introduction of a single currency – the Euro – and by converting accounts, banknotes and coins to this currency. Time has come now to launch the next wave that will ensure that the economic benefits of this conversion accrue to all actors: consumers, SMEs, corporates, retailers and banks. In the previous chapters, the key recommendations for achieving these benefits were laid out. This chapter combines the proposed actions and milestones into an overall roadmap.

- **By December 31, 2002:** *a substantiated, syndicated and detailed roadmap* achieved by:
  - (1) launching a strong governance structure and the five working groups by July 1, 2002;
  - (2) reviewing and substantiating the choice for a Pan-European ACH (e.g., review of existing options, business rationale, business requirements); (3) systematically analyzing standards, rules, business practices and conventions required for STP; (4) conducting a detailed investigation of the specific networks and switching fees for cards and proposing options to allow efficient cash handling within the euro area (the last three actions by the end of 2002). These efforts will lay the foundation for a concerted course of action over the next 5-10 years.
- **By July 1, 2003:** *the first tangible results* achieved by: (1) having an operational pan-European ACH; (2) defining a pan-European direct debit product (e.g., value proposition, requirements, migration timetable); and (3) agreeing to the basic standards, rules and conventions for credit transfers and cards, leveraging the existing standards (e.g., IBAN, BIC, MT103+). These targets are ambitious, but necessary to create the right momentum and make efforts credible to the other stakeholders.
- **By December 31, 2004:** *ramp up activity* by: (1) having 50% of cross-border payments volumes on the pan-European ACH infrastructure; and (2) agreeing to the value added services standards and their implementation plan (including incentive measures and cut-off point). By this time the industry should be in the acceleration phase, provided there is a real will to move forward.
- **By July 1, 2005:** *the next wave of innovations*, starting with the processing of the first transaction of the new pan-European direct debit instrument. By this time the governance structure should be able to demonstrate that it can respond to the continuing changes in the environment by launching new initiatives.

- **By December 31, 2007:** *achieve target service levels* for the pan-European infrastructure, so that banks will be able to reap the full benefits from the migration in their own back-offices.
- **By December 31, 2010:** *achieve a full migration* for banks and their customers to the Single Euro Payments Area, with realization of all economic benefits and a clear shift in mindset from “Migration towards SEPA” to “Managing SEPA on a going concern basis”. Although this time horizon might seem long, it is actually quite ambitious given the changes that will have to take place in legislation, in the activities of thousands of banks and in the habits of millions of customers.

Achieving these milestones will require significant work from the banks but also from all other key stakeholders (e.g., customers, ECB, EC, technology providers). The ability of this initiative to meet its milestones will therefore depend upon every stakeholder’s willingness and commitment towards SEPA.

Clear decisions, actions and milestones are the key ingredients to truly turn the euro area into a Single Euro Payments Area. The next chapter deals with the final building block required making this happen: a strong governance structure.

## SEPA SUCCESS POTENTIAL

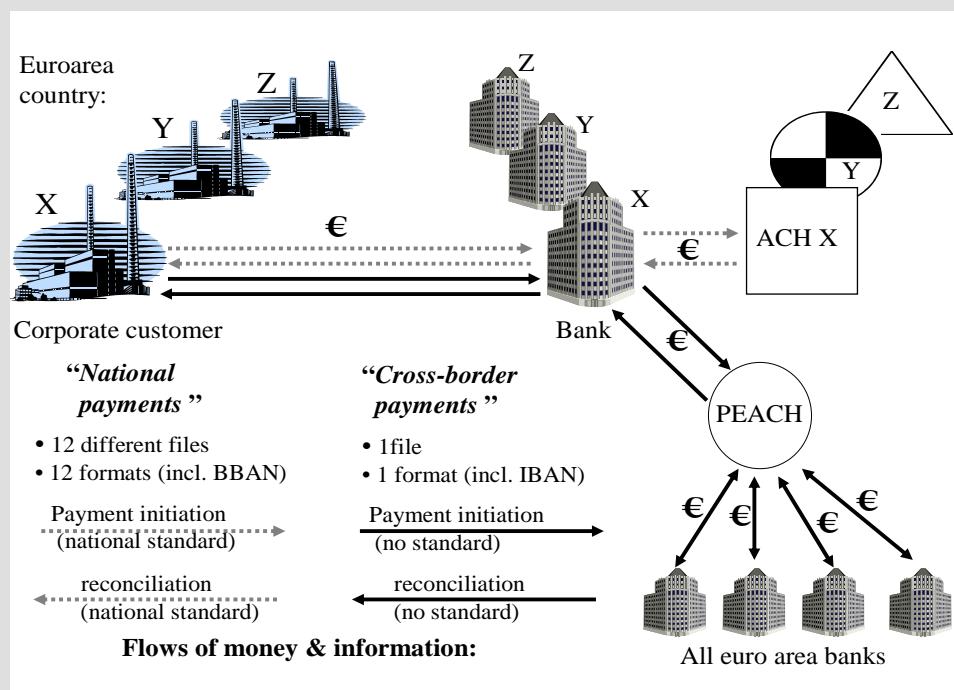
### SEPA potential success story 1: the benefit of SEPA to a large corporate customer

In our example (see figure 1), we have a corporate customer with payment traffic to and from all 12 euro area countries. In his home country X, there is a well-defined national standard for payment initiation and reconciliation enabling a very high degree of automation. In addition, his payments are processed very efficiently through a national automated clearinghouse (ACH), which is based on economies of scale deriving from millions of daily payments. However, this customer has a problem achieving the same degree of efficiency for his payment traffic involving other euro area countries.

In neighbouring country Y, this customer has substantial purchases generating outgoing cross-border payments, as well as sales generating incoming cross-border payments.

Unfortunately, the vendors in country Y need to be treated differently from competing vendors in the corporates home country X despite being in the same currency area. In the same way, it is less efficient to receive payments from customers in another part of the currency area than from customers situated in the home country. The customer's bank X treats the payments to country Y as cross-border payments, and demands that the customer submit payment initiation as a separate file based on the bank's own proprietary standards. Moreover, for the incoming payments from country Y, there is no standard allowing automatic reconciliation, so extra staff has been hired to be able to track these payments manually.

Figure 1. SEPA not achieved for a corporate customer



Since a pan-European ACH (PEACH) was created for cross-border credit transfers, this customer expected a level of service similar to that of the national ACH (i.e. a pan-European standard for payment initiation and reconciliation). Therefore, it was a negative surprise to find out that, from his point of view, the cross-border payments were processed as inefficiently as before. The customer considered changing banks to try to obtain a better solution, but abandoned this idea when he found out that it would imply costly system changes (having to change from one proprietary standard for payment initiation to another).

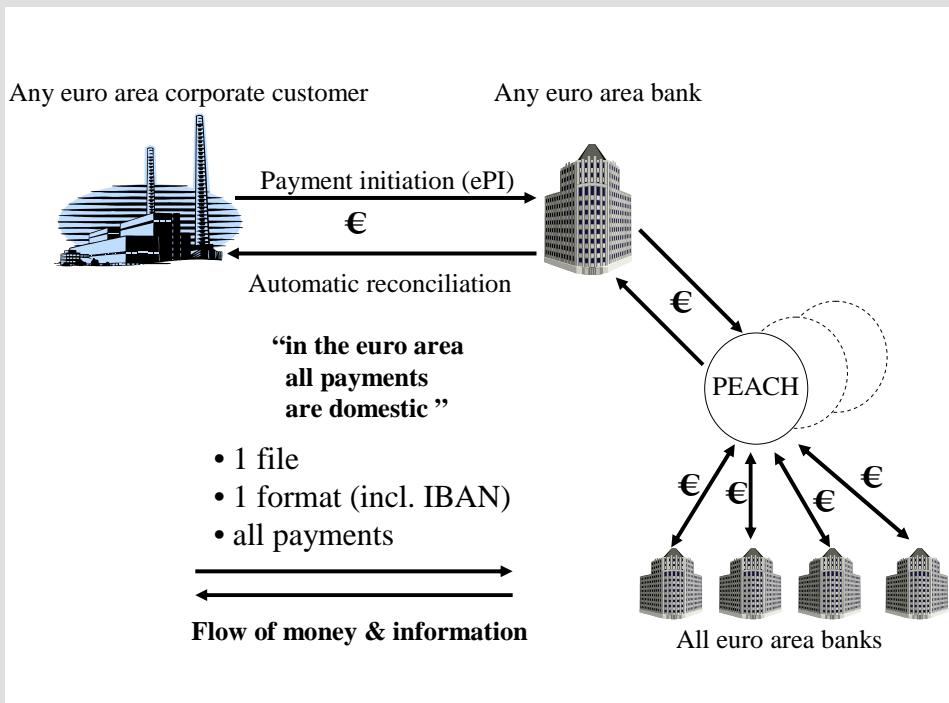
In second neighbouring country Z, the customer has bought another company since the introduction of the euro. His initial idea was to cut costs by pooling the subsidiary's financial functions with those of the parent company. However, this was easier said than done. The country Z subsidiary's national payments were already completely automated and just as efficient as those of the parent company, but used completely different and incompatible national standards. Therefore, the company concluded that the cost of adapting the central treasury's systems to a new set of national standards would be greater than the savings it could generate. The company also ruled out the possibility of instead treating all country Z payments as cross-border payments to be sent from the mother-company for processing through the PEACH when it learned that this would seriously decrease its automation rate. Moreover, the company learned that the PEACH covers only one payment instrument (credit transfers), so the huge amount of national direct debits in country Z would have had to be processed locally anyhow.

Corporate treasurers have long dreamed of being able to send all payments in 1 file and with 1 format to any bank for execution, regardless of destination (national or cross-border). In our example (see figure 2), this would mean that a corporate customer with payment obligations in all 12 euro area countries could end the present need of having to rely on 12 different banks requesting 12 different files.

However, in the SEPA, the ability to serve this specific corporate customer would be opened up to all banks regardless of size, which would enhance the service level and boost competition. Moreover, as an additional benefit, any bank would also be in a position to offer information about all incoming payments from any of the 12 countries in 1 file and with 1 format, enabling automatic reconciliation for the corporate customer. In short, the SEPA would boost end-to-end straight through processing tremendously for companies active in two or more countries by facilitating automation of the customer-bank relationship. An additional benefit for the corporate customer that would enhance competition between banks is that the customer could easily redirect his payments to be executed by any bank in the euro area without making any changes to the format. In the previous situation, there were 12 different national infrastructures and one PEACH (covering only cross-border payments for one payment instrument). In a scenario in which SEPA is fully achieved, we have a lower number of pan-European infrastructures. In this example (example 3), competing PEACHes, based on the same standards and business practices, take care of all types of payments for all euro area countries.

From a processing point of view, figure 1 represents the current situation in which national payments are processed at economies of scale (millions of payments) in national ACHes, whereas cross-border payments are processed in a PEACH with only few transactions (thousand of payments). However, in figure 2, cross-border payments can equally benefit from economies of scale, which are even greater than before, as the previous volume from 12 national infrastructures is concentrated into a few remaining PEACHes.

Figure 2. SEPA fully achieved for a corporate customer



### **SEPA potential success story 2: The benefit of SEPA to a small corporate customer**

This example considers the case of a small corporate customer of a bank. The company makes shoes in country X and has so far only sold its products on the national level. One of its reasons for not expanding sales outside its home country was the problem of secure payments. In the company's previous set-up, small national shoe shops agreed to pay against a direct debit procedure. In this way, our manufacturer could sell without undue risk resulting from the payment angle, and its clients agreed to pay according to a well-established and cheap national procedure. However, the same payment instrument was not available to customers in other countries. Therefore, our manufacturer proposed payments against a documentary credit (also called letter of credit and mainly used to secure payments from risky countries outside EU) as an alternative to avoid risk, but in most cases potential customers refused this payment instrument as too costly.

With a pan-European Direct Debit (PEDD), this shoe maker would be able to offer the same payment conditions to any potential customer in the euro area. Thus, in this case, the PEDD enables the manufacturer to treat the euro area as a domestic payment area offering his customers an efficient and cheap payment instrument similar to the national practices his national customers had been used to before. For the manufacturer, this substantial extension of his domestic market meant increasing sales without incurring the additional risk previously entailed in crossing payment borders.

### **SEPA potential success story 3: The benefit of SEPA to a private citizen**

In this example, we have a private citizen who resides with his family in euro area country X but works in euro area country Y, where he lives during the workweek. In order to obtain basic utilities (electricity, water, gas, telephone etc.) for his two homes, he is required to have a national bank account in each of the respective countries and to accept local direct debits. He notices that credit transfers initiated within each country are normally executed in one day, compared with three days when sent between two countries. In addition, he is annoyed that he needs a specific national debit card for each country. Each works very well in the country of issuance, but is basically useless across the border as it is not accepted for payments and cash withdrawals are very expensive if not impossible. Due to limitations in the banking infrastructure, the introduction of the euro banknotes and coins in 2002 did not change the situation.

However, the situation changes when the pan-European ACH launches, in addition to credit transfers, pan-European Direct Debits. This shift enables utility providers in the euro area to establish direct debit procedures with any euro area bank, eliminating the need for a national bank account. For our citizen, this simplifies matters greatly by allowing him to use only one bank for all his banking services. He first decides to pit his banks in country X and Y against each other and decide which offers the best service/price relation. However, to his surprise, he finally decides that the best offer is that of an Internet bank in a third euro area country Z. In addition to the PEDD offer, this bank also offers two credit transfer options with the same service level regardless of where the beneficiary is situated within the euro area.

However, for urgent payments it is possible to pay for a value-added service to get same day settlement. Lastly, he is able to replace his national debit cards with a pan-European one that he can use with no problem in many shops and vending machines in the entire euro area. In addition, this card allows him to withdraw cash from any ATM at a reasonable cost. The experience teaches him that the SEPA has opened up a completely new dimension to competition, with possibilities that he did not even dream about before.

**SUMMARY OF THE 4<sup>TH</sup> EPC REPORT TO THE ECB ON SEPA INDICATORS**  
**(30/09/2004)**

Country	No. of banks subscribing to:		Implementation of:		
	Credeuro	ICP	IBAN **	BIC **	PEACH***
AT	235	234	100%	100%	100%
BE	39	37	100%	100%	100%
DK	24	18	100%	100%	100%
DE *	1549	2524	100%	100%	100%
ES	169	166	99%	99%	100%
FI	331	331	100%	100%	100%
FR *	7 <sup>11</sup>	591	100%	100%	100%
GR	21	21	100%	100%	100%
IE	5	4	100%	100%	****
IT	98	167	100%	100%	100%
LU	40	40	100%	100%	100%
NL *	103	103	100%	100%	100%
PT	16	16	100%	100%	100%
SE *	17	145	95%	95%	100%
UK	18	13	71%	79%	100%
Sum	2672	4410			

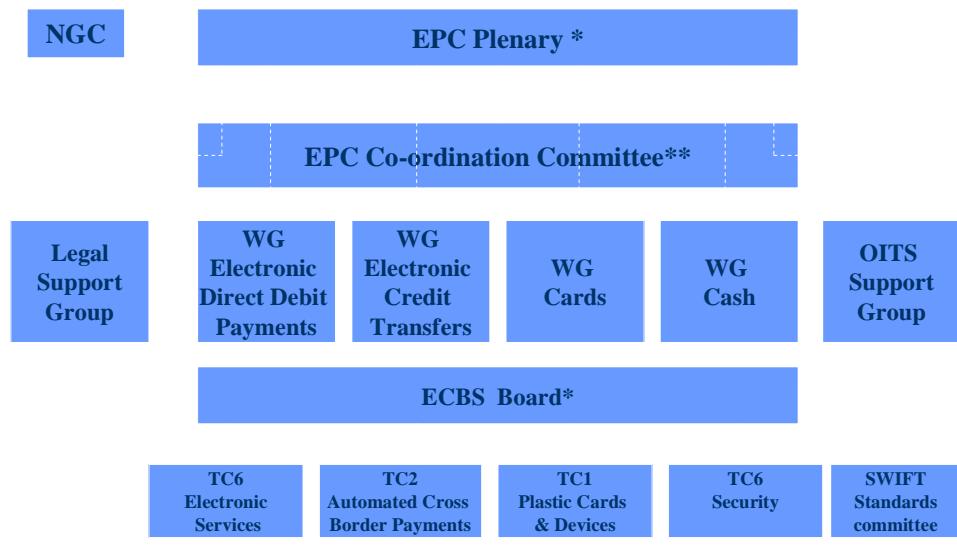
- \* Notice in DE, FR, NL and SE, all banks have adopted ICP nationally. Thus, the figures indicated are the total number of credit institutions 2002 according to the Blue Book, April 2004.
- \*\* Percentage of financial institutions that make available to their customers IBAN and BIC automatically and on a permanent basis, via their account statements.
- \*\*\* Percentage of credit institutions that could be reached through the PEACH.
- \*\*\*\* Ireland currently has no direct participants in STEP2. However, some Irish banks are indirect participants, and payments can be made to the accounts of customers of these banks via STEP2. This will continue to be the case until such time as a STEP2 entry point has been established.

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<sup>11</sup> Representing approximately 70% of cross-border volume.

## **EPC ORGANISATION**

Proposed basic EPC structure and alignment to ECBS and SWIFT Standards



\* Decision Making Body

\*\* Process Decision Making Body

**NB 1) The EPC Co-ordination Committee will become the ECBS Board**

**NB 2) The structure of the EPC task forces and ECBS working groups will be realigned**

## SEVEN HIGH-LEVEL RECOMMENDATIONS FOR STANDARDS

The Eurosystem has been following the standardisation work of the banking industry and, as result of this monitoring, has defined a set of high-level recommendations. In February 2004, it presented this set of recommendations to the banking industry. Since then, the recommendations have been the basis for a closer collaboration and have been revised, in co-operation with the banking industry.

**Recommendation 1 (strategic vision):** The EPC should formulate and regularly review the **strategic vision** of what standards (business and technical) are necessary to support the achievement of the SEPA endgame for each payment instrument (credit transfer, direct debit, cards).

The strategic vision should be driven by customer demand and respond to the challenges and chances offered by the integration of the euro area and by technological advancement. The vision should:

- be steered at the highest strategic level (i.e. the level of Chief Executive Officers);
- be complemented by a detailed overall action plan (short-, medium- and long-term) to be developed and consolidated by the various involved bodies in accordance with their mandates;
- ensure that SEPA offers to the banking industry the opportunity to define and implement safe, efficient and fully automated payment services that make use of the best available technology.

**Recommendation 2 (business model):** Standardisation work should be triggered by a positive assessment of the business needs and of a **business model** that could be deployed Europe-wide in pan-European payment schemes. In particular, this procedure should foresee that, to the maximum extent possible, national bodies are well informed and that both national interests and the interests of all credit institutions are also considered.

The business model(s) should be developed for all SEPA services, including end-to-end core datasets for payment services.

**Recommendation 3 (procedures):** **Clear and efficient procedures** need to be established for the process of standardisation. This shall include the handing over of business requirements for pan-European payment schemes for subsequent definition and development of supporting standards.

Special attention should be devoted to support, facilitate and promote adoption and implementation of pan-European standards.

The procedure should be streamlined to guarantee that consultation and assessment are done efficiently and in a timely manner.

**Recommendation 4 (roles):** Different parties' respective **roles** and responsibilities need to be clarified, including those of a) European banking standards bodies, b) other standard bodies, and c) other stakeholders.

- The overall organisation (modus operandi) of the bodies in charge should be streamlined to ensure efficient standard setting and adoption;
- where appropriate, a Memorandum of Understanding (MoU) shall be signed among the bodies involved (e.g. EPC, ECBS, SWIFT, etc.) defining separation of competencies and division of tasks;
- the EPC should have a stronger role on standards by asserting itself as the leading body guiding the ECBS's work for the SEPA and the formal integration of ECBS into the EPC structure. A model of seamless, integrated co-operation between the EPC and the ECBS should be agreed and put in place as soon as possible and be operational by the end of 2004 at the latest.

**Recommendation 5 (enhanced co-operation):** Also, particularly with a view to integrating the standardisation work needed for the SEPA into the wider international context, the EPC is invited to make proposals in order to:

1. Enhance co-operation with:
  - SWIFT and the European Standards Organisations (ESOs), with the aim of ensuring the proper level of co-ordination for the definition of relevant standards;
  - the European authorities with the aim of supporting the implementation of SEPA standards (Such proposals should foresee the involvement of important representative bodies and banking industry players, such as the EPC, ECSAs and EBA, to ensure a proper level of promotion and support).
2. Support the deployment of European standards world-wide throughout important international standardisation organisations (e.g. ISO and SWIFT);
3. Reconsider the role of the national and European banking associations to ensure both that their roles do not conflict and that the European banking industry is efficiently represented, especially with regard to standardisation work. In addition, it is recommended that, whenever a common decision is taken at the European level (e.g. definition of a pan-European standard, etc.), the national banking associations will lead national implementation by spreading information to their national member banks.

**Recommendation 6 (security):** The EPC should define a minimum common level of **security** offered across Europe, as well as a clear message vis-à-vis the users that security concerns are clearly and duly considered. In particular, the banking industry is invited to:

1. consider, in co-operation with the Eurosystem, the possibility of establishing a Product Certification Program to address security challenges. This programme may allow for the certification of products

- used in the provision of payment systems (and may also be extended to other important financial applications) on the basis of a number of security criteria to be defined;
2. elaborate further possible actions and initiatives aimed at enforcing the security of payment services and at combating fraud (e.g. electronic identification/authentication of banks' customer, etc.).

**Recommendation 7 (communication):** Implementation of standards should be accompanied by a coherent **communication strategy** involving all concerned parties and including end customers.

**SUMMARY OF IMPORTANT EPC RESOLUTIONS****EPC resolutions****Resolutions on the Pan-European Direct Debit, 17 June 2004**

In consideration of the expectation from customers to be provided with a limited set of convenient, cheap, reliable and predictable pan-European instruments to cover their most important payment needs, and the fact that direct debits respond to a real need for processing recurring and non-recurring payments, the EPC endorsed the creation of a new electronic PEDD Scheme that can be used for Intra EU

(i.e. both cross-border and national) transactions, considering that:

- (1) a new instrument can coexist in parallel with unchanged national schemes during a transitional period and is the fastest way to launch the implementation of PEDD;
- (2) the new instrument to process both cross-border and national direct debit transactions, future-oriented and secure for intra-EU transactions, should gradually lead the parties to use it for national transactions and will lay the basis for a sound business case.

The EPC defined the Pan-European Direct Debit (PEDD) as:

“The instrument governed by the rules of the PEDD scheme for making payments in euro throughout the SEPA from bank accounts allowed to support Direct Debits.

Transactions for the collection of money from a debtor’s bank account are initiated by a creditor via its bank (creditor’s bank) as agreed between debtor and creditor and based on an authorisation given to the creditor by the debtor to have its bank account debited (mandate)”.

The EPC, on behalf of the European banking community, is accountable for the scheme and is responsible for the management of the scheme rules. In order to ensure the soundness of the scheme and consumer confidence in PEDD, banks are responsible for major processes, e.g. setting up PEDD and processing transactions. Consumer protection rules in line with industry best practice, including a dispute and redress procedure based on Alternative Dispute Resolution, will be defined.

The creditor’s banks must be able to reach debtor’s banks and debtor’s banks must accept PEDD so that each creditor authorised to issue PEDD must be able to reach each debtor willing to pay via PEDD within SEPA. Debtors can refuse that their account be debited with PEDD transactions.

PEDD should gradually cover all market sectors. Government agencies and utilities should adopt PEDD to make the scheme viable and to support banks in their investments. The migration of the payment flows will be market driven. Interbank data and payment flows will respect PEDD scheme rules. Any migration of national direct debit schemes to PEDD will occur according to progressive migration paths to be defined at national level by banks together with their customers.

Regarding development and implementation of PEDD, the main principle is to begin with a basic scheme which could evolve to best cover the various market needs. There must be the same scheme in terms of

means and processing for recurrent and one-off direct debit transactions. The timeframe will be organised in two phases following the agreement of the model to be voted in June 2004:

- a first phase to finalise the scheme and produce a high-level project plan to be delivered by June 2005;
- a second phase dedicated to development and implementation, which will be subject to the coming into force of a robust legal framework and the removal of all national and EU legal and regulatory barriers to the full implementation of the PEDD scheme. This second phase will begin with a pilot targeted by end 2006, to process the first transactions. After successful completion of the pilot phase, implementation and evolution of the scheme will be able to start.

#### **PEACH impact paper endorsed by the EPC in February 2004**

When reviewing the different architectural models that can be identified to process mass payments, the European Banking industry opted for the creation of a Pan-European Automated Clearing House (“PEACH”) addressing the needs of banks operating in the European Union and potentially substituting some of the domestic ACHs.

The PEACH model as defined by the EPC was selected because of six key criteria:

- *speed and reliability of payment processing*: a centralised model provides similar inter- and intra-state payment processes, removing service level differentiation, and enabling lean and efficient operations. Such a model would also be more suited for future adaptations of its systems (quicker time-to-market, more flexibility);
- *liquidity efficiency*: a centralised model enables financial institutions to optimise their liquidity use;
- *level of operating costs*: a centralised model allows for the lowest costs achieved through the highest economies of scale;
- *investment level and ease of implementation*: the PEACH model is expected to be the cheapest, given its low complexity, and can be implemented in a short time-frame;
- *integration capabilities*: the PEACH model can best facilitate progressive integration of existing domestic systems into a common future-oriented structure, while preserving large investments already carried out on national ACHs;
- *degree of openness*: a proper approach to corporate governance ensures open and fair access to all financial institutions across the EU.

Whilst in the short-term STEP2 will co-exist with multiple national ACHs, the long-term PEACH vision is for a pan-European clearing service processing both traditional local payments and intra-EU payments. A smooth migration from the current multiple systems to this new infrastructure therefore has been proposed. As this migration proceeds, the organisational distinction between ‘local’ and ‘intra EU’ payments within financial institutions shall disappear along with the technical distinction.

PEACH is focusing on mass payments in euro, which include both:

- cross-border payments within EU (“in this paper, intra-EU payments”);
- domestic payments within EU countries (“in this paper, local payments”).

It is essential that a critical mass of payment instructions is processed by the PEACH, including local volumes, in order to match the low unit costs of large national ACHs. It needs to be considered that the bulk of the costs for processing intra-EU payments lies within the financial institutions (client order/reporting automation, back office automation). Significant back-office cost reductions are possible through various measures.

The core requirements for the PEACH were outlined as follows. The PEACH is a pan-European framework. PEACH-compliant service providers must:

- offer fair and open access to any financial institution in the EU (or the geographical area defined);
- be “country-neutral”, understood as European-driven, i.e. satisfying the market practices at the European level;
- be able to deliver payment instructions to any bank operating in the EU (or the geographical area defined);
- help minimise bank internal costs related to processing of customer payments;
- be highly automated, simple to use, based on broadly accepted industry standards;
- design their product/service in a way that allows progressive integration of local traffic;
- be ready to allow the processing of pan-European instruments as defined by the EPC, i.e. in a first stage CREDEURO and pan-European direct debits, and take the necessary steps to act in compliance with the relevant EPC Resolutions referring to these instruments;
- act as a gatekeeper to ensure full automation of interbank payment instructions processing and settlement;
- enable settlement in existing pan-European settlement systems.

### **Resolution on the PEACH, 28 January 2003**

At its 28 January 2003 Plenary meeting, the EPC proposed a new model for euro retail payments clearing to cut away the current costs and complexity of intra-EU transfers and create progressively a domestic market for Europe. This model, the pan-European ACH (PEACH), has found support within the banking industry as the preferred model for credit and debit transfers in line with the recommendations of the White Paper, "Euroland – Our Single Payment Area".

The EPC defines the Pan-European ACH (PEACH) as: "A business platform for the provision of euro retail payment instruments and basic related services, made up of governance rules and payments practices and supported by the necessary technical platform(s)."

The EPC takes note that amongst the available options and initiatives, the STEP2 project of the EBA is the most likely to satisfy by July 2003 the business needs of the industry with regard to credit transfers falling under Regulation 2560/2001 of the EU. The EPC recommends that efforts of the industry and of the banks individually are focused on the implementation of STEP2 and a rapid connectivity and usage by the largest possible number of financial institutions, both on the sending and receiving sides.

The EPC endorses the principle that competition should take place amongst banks and possibly amongst service providers. Banks should co-operate to find the best infrastructure and the best access mode to this infrastructure. It is recognised that it is important to differentiate between the infrastructure and competition issues. The PEACH is one entity, one infrastructure but not necessarily a single system (hence, in the longer term, service providers might be more than one).

### **Resolution on Receiver Capability, 4 June 2003**

The 4<sup>th</sup> Plenary meeting of the EPC adopted the following principles for the receiver capability within the PEACH framework:

The EPC declares that the collective responsibility of the European banking industry implies that each national banking community ensures that all its member financial institutions can be reachable by PEACH in order to create a level playing field in the SEPA.

- Each national banking community in the EU shall make sure that all financial institutions in the community are reachable by PEACH;
- all financial institutions in a national banking community may become direct or indirect participants of PEACH;
- any direct participant can act as an entry point to forward credit transfers to non-participants;
- the national banking communities shall ensure that the entry point arrangements do not infringe national competition laws;

- each national banking community shall set up business practices and procedures in order to preserve for incoming intra-EU credit transfers the STP character necessary to maintain the low cost/low revenue structure of the payments processed;
- the cost of “receiver capability” will be borne by the receiving banking community; each community is free to define its rules and procedures regarding the sharing of charges.

The EPC agrees to take all the necessary actions, through the ECSAs and National Banking Associations, to ensure that receiver capability be put in place for credit transfers by 31 December 2003 at the latest.

### **Resolution on PEACH governance guiding principles, 17 September 2003**

On recommendation from the Infrastructure Working Group, the EPC agreed on a set of governance criteria which are intended to give broad guidance on what could constitute best practice for good governance of the PEACH operator(s) in the framework of PEACH. The selected criteria complement the regulatory principles issued by the overseers and supervisors of payment systems: the 10 Core Principles issued by the Committee on Payments and Settlement Systems of the BIS that are part of the oversight principles of the Eurosystem.

The EPC confirms its endorsement of the high level governance principles as spelled out by the Working Group in the revised section “Formulation of best practice for governance of PE -ACH operators” of its initial “Findings and Recommendations Report” dated 9 January 2003. The EPC sets out hereby the industry’s core requirements with respect to minimum governance criteria that any PEACH system operator should meet.

These good governance criteria are the following:

- profit model - there is a preference for a not-for-profit model;
- membership - the participants shall be individual financial institutions only;
- ownership - ownership and control should be in the hands of financial institutions. There should be fair and open access to the system’s ownership. The ownership principles must be acceptable to competition and regulatory authorities;
- control - the interests of all classes and sizes of financial institutions must be represented;
- governing structure and representation - every bank or grouping of banks should have a chance to become participant of the governance structure and be fairly represented. PEACH is to be country neutral. Transparency and a clear definition of the responsibilities and liabilities of each category of participating financial institutions, be they owners or users, should be established;
- decision-making process - PEACH operators must have an effective, workable, clear and unambiguous decision-making process. A mechanism should be put in place to make and enforce decisions and to ensure commitment from their participants to apply the rules. Governance arrangements should ensure that owners and users have appropriate representation on the decision making body(ies);

- access criteria - the principle of fair and open access should be guaranteed. Objective and transparent access criteria should be established;
- pricing model - pricing should be fair, transparent and non-discriminatory. Pricing should respect competition rules, not be a barrier to access and help the PEACH operator(s) to remain economically viable;
- risk bearing, audit and oversight, legal form and operating rules - the PEACH operator(s) should only bear an acceptable level of risks and have the appropriate legal form and audit functions in place to support its objectives. As a general principle, the PEACH should provide industry utility type services and not enter into competition with financial institutions and users of the system;
- dispute resolution (a mechanism for dispute resolution should be put in place).

The EPC resolves that on the basis of the high-level Governance Principles as set forth above, any PEACH operator should be able to perform a public self-assessment according to a checklist provided by the EPC. In the future, the EPC may decide that additional measures are needed to ensure compliance with PEACH Governance Principles.

### **Resolution regarding cards, 7 March 2003**

On 7<sup>th</sup> March, the EPC endorsed the following Recommendations formulated and unanimously agreed by the Cards Working Group:

#### **Recommendation 1:**

The banking industry should reinforce actions to prevent and combat fraud through active co-operation between banks, card schemes, retailers, the Eurosystem, the European Commission, law enforcement authorities, governments, and other stakeholders. Minimum security standards (including EMV chip) and a common approach for tackling fraud will be defined, and their implementation monitored.

#### **Recommendation 2:**

Domestic and international card schemes should present their scheme tariffs to member banks in a transparent manner fully consistent with the objectives of SEPA, in order to differentiate between the various functions provided and facilitate banks' business planning.

#### **Recommendation 3:**

Domestic and international card schemes should be encouraged to speedily complete amendments underway to their rules and conventions, in order to enable any bank or banking group to operate throughout SEPA.

#### **Recommendation 4:**

Whilst restating their preference for self-regulation as expressed in the vision, banks should co-operate with legislators and regulators (including the Eurosystem and the European Commission) to identify and

remove where necessary legislative and/or regulatory obstacles and discrepancies that prevent delivering the banking industry vision for card payments in SEPA.

**Recommendation 5:**

Collectively, banks should ensure that, with effective bank input, they achieve greater levels of technical standardization that fully support the banks' business objectives defined in the vision statement. This effort will be undertaken within existing standardization (including card schemes) organizations.

**Recommendation 6:**

In order to implement the agreed vision, banks should ensure that they fully exert their responsibilities as stakeholders in domestic and international card schemes at all times.

**Recommendation 7:**

In order to effectively support the implementation of this industry vision, the banking industry and the Eurosystem should jointly define an aggregated high-level statistical data collection and distribution process that provides a timely view on the intra-SEPA market evolution. It will be implemented by the ECB (and enhance the process presently used for the production of the ECB Blue Book statistics). As much as possible, existing data feeds will be used, new structures and costs minimized, and card schemes involved. This statistical data collection and distribution process should be implemented and managed in such a way as to fully respect data protection rules and business secrets principles.

**Recommendation 8:**

The banking industry should establish the Cards Working Group as the body under the auspices of the European Payments Council (in co-ordination with the appropriate banking bodies and schemes) with the specific mission to regularly and at least annually report to the EPC on the status of the above Recommendations, with propositions for action and, when appropriate, organise a debate on new issues and make additional recommendations. The EPC Cards Working Group will meet as required to deliver these objectives. The Cards Working Group will also ensure continued liaison with authorities through existing structures as required.

**Resolution on preventing and fighting card fraud across Europe, 10 December 2003**

Following a recommendation from the Cards Working Group, the EPC Plenary concluded as follows:

1. The EPC Plenary formally expressed its support for the positions presented by the Working Group, namely:
  - card fraud, and in particular cross-border card fraud within Europe, is costly for the European banking industry and consequently for its customers;
  - the development and persistence of card fraud damages the image of the European banking industry and may slow down public acceptance of electronic payment means;
  - the European banking industry, through card schemes, already has a long experience in card fraud prevention, yet should still exploit to the fullest opportunities for knowledge sharing in this field;

- as part of its Fraud Prevention Action Plan, the European Commission (EC) established a liaison group representing all interested parties (the Fraud Prevention Experts Group) and set up an EU-wide fraud prevention website with information on initiatives and links to all relevant organisations;<sup>12</sup>
- the non-uniform implementation of European data protection rules is still a major concern for the European banking industry in the fight against fraud.

The EMV migration shall be completed throughout Europe as soon as possible as per the EPC Resolution Doc EPC-0262 of 4 June 2003, and the EMV liability shift occur, as scheduled, on 1 January 2005.

2. The EPC Plenary gave the Cards Working Group a mandate to:

- study (from respectively a structural, a governance, a legal, as well as a cost/benefits perspective) the possibility and feasibility of creating a European anti-fraud database, hosted on a trusted third-party website (such as that of the ECB), consolidating data from all card schemes and operators and make a recommendation to the next EPC Plenary;
- capitalise as much as possible on existing solutions and taking into account recent progress in the field of card fraud prevention (chip/PIN, CV2 checking...), consolidate security standards and procedures to be promoted by the European banking industry, including the schemes, and the key stakeholders collectively;
- strengthen EPC involvement in the EC Fraud Prevention Experts Group (with an initial emphasis on building bridges with law enforcement liaisons across the EU) by creating an “advisory group” (which will include representatives from the Cards Working Group) that prepares the Experts Group’s deliberations and gives guidance on its work, in cooperation with other stakeholders involved;
- propose to the European Commission that it add to its fraud prevention website a section dedicated to the exchange of best practices within the European banking industry (with restricted access).

**Resolution on National Central Banks’ core functions as regards cash, 14 October 2003**

On recommendation from the Cash Working Group, the EPC Plenary meeting of 10 December 2003 approved a Resolution addressing the definition of core responsibilities for national central banks as regards cash.

1. The EPC formally expressed its support for the positions presented by the Cash Working Group.
2. The EPC gave the Cash Working Group a mandate to dialogue with the ECB in order to:
  - a) define the core responsibilities of the national central banks on the basis of the guiding principles and parameters described in the recommendations below;
  - b) seek commitment from the ECB and national central banks to ensure the continuity of their responsibilities, services and operational conditions as regards cash (any major modification

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<sup>12</sup> [http://europa.eu.int/comm/internal\\_market/payments/fraud/index\\_en.htm#2001\\_2003](http://europa.eu.int/comm/internal_market/payments/fraud/index_en.htm#2001_2003)

- with an impact on the amortisation and recovery period relative to each investment made will be reflected in the industry's pricing propositions);
- c) establish formal processes through which banks at the national level can be genuinely involved in the relevant parts of the national central banks' decision-making process as regards cash, with a view to creating real forms of partnership.

The EPC agreed on the following recommendations:

**Recommendation 1:**

Recognising that cash and card strategies are intertwined, banks must develop joint cards and cash strategies, including the development of strategies for reducing the costs related to cash products and processes, that address the reduction of the cash they handle. To implement the foregoing, each market should be required to put in place a plan to reduce cash handled. For the remaining cash, the industry will strive to implement cost-efficient solutions.

The Eurosystem should agree and implement a long-term policy for cash that fully reconciles macro-economic monetary and "public good" objectives on one side, and operational necessities on the other, from the perspective of both national central banks and the banking industry as such. Such a policy should always consider the banknotes and the coins composition of cash.

After a wide consultation process, this long-term policy should encompass all stakeholders in the economy, and aim at ensuring overall coherence with regards to cash (e.g. defining "best practice" guidelines for government disbursements, avoiding disruptive actions from e.g. tax authorities, aiming at complementarity with anti-money laundering objectives...).

This long-term policy will include measurable objectives as regards cash in circulation and maximum pay-outs by the banking industry (possibly on the basis of initial "bands" within which national economies will be invited to converge over time).

**Recommendation 2:**

Collectively (of course in full compliance with competition legislation) and individually, banks will formulate and implement policies and programmes that allow customers, both retailers and consumers, to make more informed choices regarding the payment instruments they accept and use. Such programmes should include, but would not be limited to, education of retailers and consumers and promotion of non-cash instruments (such as payment cards, e-purses and mobile payments). The relevant work will be coordinated with the work of the EPC Cash Working Group.

**Recommendation 3:**

The banking industry should establish, under the auspices of the European Payments Council, the Cash Working Group as the body with the specific mission to – in coordination with the appropriate national banking bodies - a) oversee the implementation of the above recommendations, b) consolidate information on policy, technology, legal and regulatory developments concerning cash and cash handling,

c) act as a catalyst and coordinator for standardization, and d) report to the EPC regularly and at least annually with propositions for action. This body will also ensure continued liaison with authorities as required.

**Recommendation 4:**

In order to address structural costs, make handling as safe as possible and enhance quality, the banking industry should collectively develop processes, means, and control mechanisms that enable an effective standardisation Europe-wide of requirements for equipment - both hardware and software - involved in the support of cash services (e.g. ATM cash recycling machines, cash counting machines...). Where necessary, standardisation and qualification processes will be undertaken in concert with the Eurosystem.

**Recommendation 5:**

Banks individually have responsibility for enabling enhancements at the industry level: the “network” principle applies here too. The banking industry shall formulate at the European level a set of best practices (in full respect of European and national competition law) that will guide individual banks, in cooperation with other stakeholders, in enhancing their cash service operations, thus enabling them to reduce their cost basis whilst providing adequate services to their customers. Of course, individual banks will retain full responsibility for implementing and pricing cash services to their customers.

**Recommendation 6:**

The banking industry and the Eurosystem should engage in the evaluation of the pros and cons of establishing a Europe-wide wholesale infrastructure for cash handling in the Single European Payments Area based on the concept described in Chapter 3.3. The consideration that at present the banking industry supports a very significant share of the total costs of cash at an economy level is an important dimension in this necessary discussion.

**Recommendation 7:**

In order effectively to support the implementation of this long-term policy and to assist the banking industry in making timely and informed decisions, the Eurosystem should endeavour to define and implement a data collection and distribution process that provides (almost) real-time feedback on market evolution. Such data must include information on Euro counterfeiting. Salient aggregates and periodicity of publication should be agreed with the banking industry.

**Recommendation 8:**

The Eurosystem will as required seek agreement with stakeholders regarding optimum conditions for the introduction of legislative and regulatory changes, also as regards e.g. transportation issues, in order to ensure that the above strategy can be effectively implemented. The guiding principle in this respect should be “harmonisation” that respects the subsidiarity principle yet allows for establishing a genuine level playing field for banks.

**Recommendation 9:**

The Eurosystem will harmonize its operating conditions for cash (i.e. banknotes and coins). This will include restating the core responsibility of national central banks in the distribution of cash (still allowing them to offer value added services as they deem suitable).

As a matter of priority, the Eurosystem will, in cooperation with the banking industry, identify and remove the barriers that currently prevent the provision of cash services cross-border.

### **Resolution on facilitating cross-border cash transport in the Eurozone, 10 December 2003**

On advice from the Cash Working Group, the EPC approved at its 10 December 2003 Plenary meeting the following recommendations:

- harmonisation of national laws and regulations may be a lengthy process. Specific “cross-border transportation” licence and rules should be defined, provided they do not generate undue costs compared with prevailing national conditions and are as far as possible compatible with national laws and regulations. Furthermore it must be ensured that national legislators will be willing to adjust their laws and regulations as appropriate;
- in particular, harmonised rules for the acceptance and use of “smart boxes” should be defined, and cooperation among the key players in this field (European Central Bank, manufacturers, law enforcement authorities) should be fostered;
- a contingency plan (“minimum cash transport service”) should be developed in order to ensure continuity of service at the appropriate security levels in case of extraordinary circumstances.

### **Resolution on use of payment alternatives to cross-border cheques, 10 December 2003**

On advice from the Cheque Task Force, the EPC adopted the following recommendations:

- banks should encourage beneficiaries to accept alternative means of payment instead of cross border cheques, based on an adequate sales policy in which the real value offered to customers is incorporated;
- banks should further promote existing or future alternative payment instruments in line with the interest of customers for cross-border payments;
- the banking industry should actively pursue the removal of barriers that exist at national level. The banking industry should also try to avoid the emergence of any future obstacles.

## LIST OF ABBREVIATIONS

ACH	automated clearing house
ATM	automated teller machine
BBAN	Basic Bank Account Number (IBAN – country code and control digit)
BIC	Bank Identifier Code
CIT	cash in transit
Credeuro	a basic cross-border credit transfer service for payments up to €12,500
CV2	card security code (Visual Cryptogram for customer verification and validation)
EACT	Euro Association of Corporate Treasurers
EBA	Euro Banking Association
ECB	European Central Bank
ECBS	European Committee for Banking Standards
EEA	European Economic Area (EU plus Iceland, Liechtenstein and Norway)
EFT-POS	electronic funds transfer at point of sale
EPC	European Payments Council
EMU	Economic and Monetary Union
EMV	Europay International, MasterCard International, Visa International
ESCB	European System of Central Banks
IBAN	International Bank Account Number (BBAN + country code and control digit)
ICP	Interbank Convention on Payments (Interbank Charging Convention)
MT 103+	SWIFT message format 103+
NCB	national central bank
NGC	Nomination and Governance Committee (of EPC)
NLF	New Legal Framework (of the European Commission)
OITS	Operations, Infrastructure and Technology Standards Support Group (of EPC)
PEACH	pan-European automated clearing house
PEDD	pan-European direct debit
PIN	personal identification number
SEPA	Single Euro Payments Area
SHARE	Interbank charging option where the payer pays the sending bank's fee, and the payee pays the receiving banks fee
STEP2	a pan-European ACH solution for processing bulk payments
STP	straight-through processing
SWIFT	Society for Worldwide Interbank Financial Telecommunication