

SEPA in need of more competition

Opinion of PaySys Consultancy GmbH on the SEPA Migration End-date Hearing of the European Commission scheduled for November 17, 2010

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SEPA and SEPA objectives

- **SEPA is the Single Euro Payments Area**
- **The European Commission defines SEPA as follows: „SEPA is the integrated market for payment services which is subject to effective competition and where there is no distinction between cross-border and national payments within the Euro area.“ (EU Commission: Consultative Paper on SEPA Incentives, 13.2.2006)**
- **The creation of a Single Euro Payments Area is meant to contribute significantly to the Lisbon Agenda to make the EU “the most competitive and dynamic knowledge-driven economy by 2010”.**
- **For the moment, SEPA covers**
 - **credit transfers**
 - **direct debits**
 - **card payments**

What has been done to achieve the SEPA objectives

- **European banks have founded the European Payments Council (EPC), which has developed the new SEPA schemes „SEPA credit transfer“ (SCT) and „SEPA direct debit“ (SDD).**
- **For the area of card payments, the EPC has published a framework for SEPA-compliant card schemes (SEPA Cards Framework). European banks have declared their commitment only to issue cards of SEPA-compliant schemes.**
- **The European Commission has passed the Payment Services Directive (PSD), thus harmonising the legal framework for payments in the EU and has regulated the reachability of all payment institutions for direct debits (EC No 924/2009).**
- **The EPC and other bodies have promoted the use of common technical standards (for instance EMV for cards, ISO20022 for giro payments) to replace current national standards.**
- **The European Central Bank has published „Terms of Reference“ for various actors in the payments industry.**
- **Processing infrastructures that used to be run by national banking communities as „closed shops“ have been opened up. As a result, multi-national processing companies such as Equens or VocaLink have emerged, offering their services throughout Europe.**

SEPA at crossroads

- In spite of substantial efforts, SCT and SDD have gained only a small market share. SDD, in particular, faces many criticisms.
- Therefore, the EU Commission contemplates the introduction of a binding end-date for non SEPA-compliant payment schemes. The EPC and the ECB are strongly endorsing such an idea.
- Such a move would imply the shut-down of all national credit transfer and direct debit schemes which are currently used.
- The EU Commission hesitates, however, with the publication of a concrete proposal for the implementation of such an end-date. As it points out, such a move „de facto grants a private monopoly to the EPC“. (European Commission: SEPA Migration End-date. Discussion paper, 15.3.2010).
- As an alternative to a de jure shut-down of legacy schemes, the EU Commission has proposed the definition of „essential requirements“.
- In principle, such an „essential requirements approach“ would make scheme competition possible.
- In the area of giro payments (credit transfers, direct debits), scheme competition would be an innovation. In the past, in individual countries, giro payments have usually been based on national interbank solutions.
- There is no reason, however, why giro payments should be kept out of the competitive space. In the area of card payments, the authorities also have opted for a competitive solution. The same is true for other network services, such as telecommunications and postal services.

„Essential requirements“ as de facto end-date regulation

- We strongly endorse the use of an „essential requirements“ approach because it opens more space for competition. „Old“ methods which, up to now, are operating only nationally, are also given the possibility to become SEPA-compliant.
- However, the approach suggested by the EU Commission (in the "Working Paper on SEPA Migration End-Date“, 2.6.2010, not yet an official proposal), goes far beyond defining essential requirements. The Commission proposal contains long and detailed lists of requirements that basically imply that SDD and SCT have to be used. Thus, it is an end-date mandate in disguise.
- The European Commission has scheduled a public hearing on the topic of migration end-dates for November 17th. As the published agenda shows, the Commission is not prepared to restrict itself to setting broadly defined „essential requirements“. Rather, it only wants to discuss ways how to make the EPC schemes (SDD and SCT) mandatory.
- Such an approach is highly objectionable. If competition is desired, the Commission should restrict itself to defining truly „essential“ requirements, which are indispensable for reaching the SEPA-target. The EPC's "SEPA Cards Framework“ and the „Terms of Reference for the SEPA Compliance of Card Schemes“ of the ECB could serve as an example.

Options

- **The Commission recognised that directly mandating the EPC-schemes gives rise to anti-trust concerns. Therefore, the Commission now has to answer the question, which conclusions to draw. Can SEPA objectives of a single payments area, of efficiency and innovation only be achieved via (directly or indirectly) mandating EPC schemes or should competition between payment schemes be allowed? Accordingly, the options are either to**
 1. mandate the exclusive use of EPC schemes or
 2. introduce a framework for the SEPA-compliance of direct debit and credit transfer schemes and interoperability as well as reachability of such schemes.
- **If the Commission chooses the first option,**
 - the legacy schemes will be replaced by the new SEPA schemes,
 - competition between payment schemes, as considered by the Commission will not take place,
 - it remains to be seen whether these schemes will meet the requirements of the market.
- **If the second option is chosen:**
 - A framework for giro payments must be defined along the lines of the Sepa Card Framework. Such a „Giro Payments Framework“ would define SEPA-compliance for credit transfer and direct debit schemes. Moreover, the ECB could issue complementing "Terms of Reference for the SEPA Compliance of Giro Payment Schemes“.
 - The Commission could mandate the full interoperability and reachability for direct debits and credit transfers, if it is considered necessary. By which means this will be achieved can be left to the payment industry and to competition without the need for detailed technical requirements. Fears that a less restricted approach will yield to a fragmented payments landscape are unsubstantiated,
 - The Commission could set end-dates for achieving SEPA-compliance.

Results & recommendations

- As is evident from the agenda of the hearing, the Commission has chosen the first option. The only question to be discussed is the way to best achieve this option: by mandating detailed technical requirements or through direct mandating of the EPC schemes.
- The example of payment card systems and of many other network industries demonstrate that there is room for competition even in network industries with strong economies of scale and scope. Although the topic of competition between giro payment schemes has come up relatively late, it is not too late to evaluate the second option instead of rejecting it prematurely.
- "Given that the European cards market is big enough to combine competition with consolidation and economies of scale [...]". This statement about cards comes from the ECB's 7th progress report. Why does this insight not apply in an equal manner to direct debit and credit transfer schemes?
- The Commission is at a crossroad: A breach of anti-trust principles without convincing reasons could prove a severe mistake at the beginning of SEPA. Even if the Commission is under pressure to act, it should take the time to explore the second option.

***"He who says A need not necessarily say B. He may realise that A was wrong."
(Bertolt Brecht)***

The EU Commission should have the courage to allow for and to foster competition between giro payment schemes.