



SEPA BACK ON THE AGENDA

EQ magazine spoke with Gertrude Tumpel-Gugerell of the Executive Board of the European Central Bank. How has the crisis affected the implementation of SEPA? What will happen next? Gertrude Tumpel-Gugerell: "SEPA will bring more competition and pressure on revenues, but also more business opportunities and new sources of profit for retail payment service providers."

What are the lessons learned from the financial crisis?

There have been a number of lessons learned from the financial crisis. Let me just mention that it has illustrated the close interdependencies between financial markets, intermediaries and infrastructures. While public attention has been mainly on banks and the banking sector, the solidity of infrastructures, i.e. payment and securities clearing and settlement systems, has also been put to the test.

EU market infrastructures have supported the liquidity and stability of financial markets and proven resilient to more volatile market activity and peaking transaction volumes. Thanks to sound risk management frameworks, they have helped contain the systemic impact of the default of critical counterparties.

The financial industry, regulators and overseers have interacted successfully to weather the storm, and we have now established measures to reduce the likelihood of another similar crisis.

There is a need for enhanced crisis management arrangements across market infrastructures to improve the existing information sharing framework and the cooperation/coordination between oversight authorities. Furthermore, the Eurosystem is actively contributing to the review of existing international oversight standards for financial market infrastructures (including liquidity management standards), and to the

establishment of a sound infrastructure for OTC derivatives.

Another area that warrants particular attention is that of retail payments, given the importance of retail markets to the overall stability and efficiency of the financial system. The Eurosystem sees the need for a more integrated and harmonised retail payments infrastructure. This is why it strongly supports the realisation of SEPA.

In what way has the crisis influenced the importance of SEPA?

While it is certainly true that the crisis has claimed a lot of resources in the ECB, it has not diminished the importance attributed to SEPA. We have to be aware that retail payments represent the interface of the financial system with the day-to-day lives of almost every individual and every company in Europe. Therefore the retail payments market has a crucial function in preserving the public confidence in the financial system and, ultimately, the euro as the single currency. It is also worthy of note that the financial crisis has highlighted the importance of retail payment services to the banks' balance sheets. While retail payment services have certainly not been prominent in the public debate, retail business has successfully withstood the financial crisis and provided a steady and reliable source of revenue. Banks with a balanced business model have been best equipped to cope with the situation.

What changes will SEPA bring?

SEPA will result in more competition and pressure on revenues, but also more business opportunities and new sources of profit for retail payment service providers. Thus, it requires banks to change their business and revenue models. This is never easy – especially not in a period of limited growth and higher risks like we have now. But regardless of external conditions, banks need to invest in SEPA to position themselves strategically – the earlier, the better.

Will SEPA ever be realised if there is no end-date?

To avoid a lengthy, costly and confusing period of dual processes, and in order to make the SEPA benefits attainable, in 2008 the ECB stressed the importance of setting an end-date for the migration to SEPA payment instruments. In 2009, the financial sector and European institutions reached the consensus that the most viable option for determining a migration end-date is regulation by public authorities. The European Commission is currently investigating the possibility of a regulation to facilitate the migration to SEPA.

Which additional regulations do you expect with regard to SEPA?

It is in the interest of the banks to encourage their clients to embrace the SEPA payment instruments by providing good and accessible information to their customers.

Even more importantly, the banks need to convince their clients of the benefits of SEPA with attractive, high-quality product and service offerings.

At the same time, it has to be recognised that the self-regulatory powers of the banking community have their limits. In January 2010, i.e. two years after the product launch, SEPA credit transfers accounted for only 6.2% of the overall credit transfer volume. Although we expect to see an increase in this figure by the middle of the year – as public administrations in several countries have planned to migrate to the SEPA products – further action is needed. For instance, a regulation could facilitate the migration to SEPA. Furthermore, customer acceptance of SEPA products can be encouraged through further involvement of the users in the governance of the SEPA project. In addition to the EPC organising stakeholder involvement around the design of the SEPA products, a new governance body, known as the SEPA Council, will be established. The aim is to go beyond the interbank and inter-payment service provider domain, taking into account general welfare considerations and balancing the (sometimes conflicting) interests of the different stakeholders. Consequently, this governance body will also play a crucial role in the move towards SEPA.

Should public authorities take the lead?

When referring to bank customers, we usually think of individual retail clients and companies. However, it should not be forgotten that public administrations, e.g. tax authorities, benefits agencies, etc., generate a critical mass of retail payments. Migration of these payments to SEPA will bring substantial volumes. The European Commission established that in autumn 2009, the migration rate of public authorities to SEPA was still below the overall migration rate in the euro area. Despite some differences in the migration rates of public authorities in different countries, I think that the use of SEPA by public administrations could play a very prominent role in the overall migration to SEPA.



When do you think SEPA will be realised?

In my view, the realisation of SEPA will not be a steady state, but a process. It depends on the ability of the European retail payments market to both harmonise and modernise payments. The harmonisation of retail payment instruments and standards is a precondition for overcoming the current fragmentation and creating a competitive European retail payments market. At the same time, the harmonised retail payment instruments need to be complemented with innovative features to be able to keep up with user expectations and market realities. These user expectations and market realities are not stable, but governed by technological progress, as is SEPA. The chip, the internet and the mobile phone are three innovations that have had a profound impact on society over the last 20 years. They are undoubtedly having an impact on customers' payment needs and payment behaviour, too. This needs to be taken into account in the further development of SEPA.

SEPA Direct Debit: achievement or overregulation?

First of all, we should not forget that SEPA Direct Debit (SDD), which was launched in November 2009, is the first direct debit instrument ever that can be used for both national and cross-border collection of payments throughout the 32 SEPA countries. The creation of such a scheme is a great achievement, as it is geared towards achieving consensus among representatives from 32 countries, all of whom have had very different experiences with legacy instruments and payment habits.

In my view, SEPA Direct Debit is not over-regulated. First of all, the respective SEPA Direct Debit Rulebooks are the product of a market-driven, decision-making process of the EPC. Furthermore, the public statements and subsequent references to direct debit interchange fees in the new regulation on cross-border payments in euros stemmed from banks needing clarity regarding the

long-term business model for SDD.

It is clear that the rollout of SEPA Direct Debit will not be a 'big bang'-style event. Instead, it will be a gradual process, since reachability for direct debit transactions will only be guaranteed as of 1 November 2010. Furthermore, it is evident that the SEPA Direct Debit schemes are basic models to which extra features can be added as required as additional optional services. I think a lot of the reservations regarding SEPA Direct Debit stem from the fact that customers are not sufficiently informed. Obviously, this is an area for improvement. More importantly, they need to be convinced of the benefits of SEPA Direct Debit with attractive, high-quality product and service offerings.

Is the ECB in favour of a third card scheme besides V PAY and Maestro?

The Eurosystem has always been in favour of banks setting up at least one additional European card scheme. The rationale behind this is that it would first of all enhance competition between card schemes and give cardholders, merchants and banks more options. Secondly, it would allow for diversity in card scheme governance and scheme ownership models.

In the EU, card payments have been the strongest driver for cashless payments. This proves the potential of this means of payment to generate revenue for the financial industry through growth, even at a time when interchange fees are under pressure. Card payments can be strategically positioned as a real alternative to cash. I expect that, based on these strong arguments, banks will look carefully into their cards business strategy.

What major effects has SEPA had on infrastructure to date?

It is interesting to note that the effects of SEPA have so far been most visible at the infrastructure level. Most infrastructures have been processing SEPA credit transfers since their launch in 2008, and a large number are also SEPA Direct Debit scheme



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compliant. Several infrastructures have taken the step from being purely national operations to become pan-European service providers. There is also a choice between core clearing and settlement service providers and those who offer additional payment processing-related services. A number of infrastructures have also established interoperability links for the exchange of SEPA transactions across infrastructures, thus creating wider reach.

Will the card processing market benefit from standardisation?

In the medium term, the ECB expects that card processing will benefit from use of the same standards and infrastructures utilised for credit transfers and direct debits. The integration of a new card processing framework in the existing PEACH/CSM framework by the EPC will represent an important contribution to this development. Some European infrastructures are already being used for card processing. In the long run (and in a market-driven process), the ECB also expects that the harmonisation and modernisation of the infrastructures will pave the way for a more integrated and consolidated market in order to utilise economies of scale and scope.

Do you foresee the need for a standardised payment area larger than SEPA?

In the course of 2009, it became apparent that the international financial community considers SEPA one of the world's most important payment harmonisation projects. In fact, SEPA has become a point of reference for other payment harmonisation projects. One example of this is the International Payments Framework (IPF), an association that plans to improve non-urgent multi-currency cross-border credit transfers.

The ECB welcomes the fact that initiatives such as the IPF take the SEPA Rulebooks and the SEPA standards as an example when designing their framework for cross-border and cross-currency payments. In terms of governance, these payments need to remain clearly separate from SEPA payments to provide the necessary legal clarity to customers, payment service providers and governance bodies. Overall, I believe that more standardisation will also lead to greater efficiency in the payments market at a global level. However, we should not forget that the harmonised legal framework for payments at the SEPA level is not available across countries globally. It is therefore difficult to envisage a time frame for such harmonisation activities to come to fruition.

ECB, ESCB and the Eurosystem

Since 1 January 1999, the European Central Bank (ECB) has been responsible for conducting monetary policy for the euro area – the world's largest economy after the United States. The euro area came into being when responsibility for monetary policy was transferred from the national central banks of eleven EU Member States to the ECB in January 1999. Greece joined in 2001, Slovenia in 2007, Cyprus and Malta in 2008, and Slovakia in 2009. The creation of the euro area and a new supranational institution, the ECB, was a milestone in the long and complex process of European integration.

European Central Bank

The legal basis for the single monetary policy is the Treaty establishing the European Community and the Statute of the European System of Central Banks and of the European Central Bank. The Statute established both the ECB and the European System of Central Banks (ESCB) as from 1 June 1998. The ECB was established as the core of the Eurosystem and the ESCB. The ECB and the national central banks together perform the tasks they have been entrusted with. The ECB has legal personality under public international law.

European System of Central Banks (ESCB)

The ESCB comprises the ECB and the national central banks (NCBs) of all EU Member States (Article 107.1 of the Treaty) whether they have adopted the euro or not.

Eurosystem

The Eurosystem comprises the ECB and the NCBs of those countries that have adopted the euro. The Eurosystem and the ESCB will co-exist for as long as there are EU Member States outside the euro area (comprising the EU countries that have adopted the euro).

