

A short introduction on SEPA



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1. Introduction

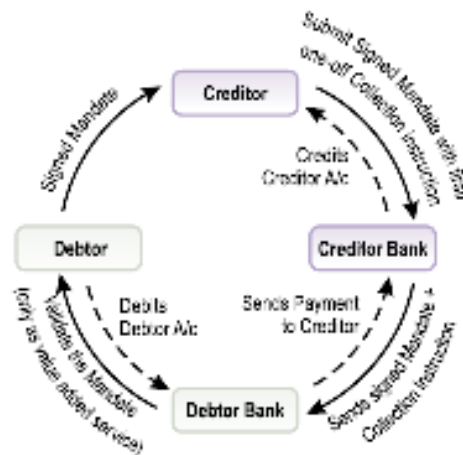
“The SEPA project is fully part of the setting up of a single market for Europe, and requires the full support of all stakeholders, particularly the entire banking community.”¹ 31 countries fall under the SEPA agreement, though not only EU countries, but also Iceland, Liechtenstein, Switzerland and Norway. Even more countries are interested in joining the agreement. Till the 28th of January the countries used their national payment system – which was problematic, because cross border transactions were cost intensive. With SEPA technical, legal and commercial barriers shall be taken down and customers shall feel more secure doing their payments from a single account.

The following paragraphs shall introduce the most important aspects of SEPA.

2. What is SEPA?

SEPA is a framework of rights and obligations and includes rules to standardise transfers on the one side and to dissolve national payment systems in a medium term on the other. The reason: Transactions in the EU often caused problems because of national payment systems. The amount sometimes didn't reach its destination account or the required time was very long. Due to these problems the cross border financial infrastructure needed standardisation. SEPA tries to tackle these problems, so that in the future customers can easily and safely make transfers within an international payment system. Starting from January 2008 with a few restrictions – but definitely completely in a few years - customers can make cashless payments within the whole payments area from a single account as easy as domestic ones today.

So the main aim of SEPA is to improve payment procedures. One is the PECT or Pan European Credit transfer, which covers all credit transfers from one account to another within the whole area. As already in practise the International Bank Account Number (IBAN) and the Bank Identifier Code (BIC) will be the basic identifiers for both sides.



¹ European Central Bank, p. 5

SEPA also addresses direct debit, which is named PEDD or Pan European Direct Debit. It applies if an authorised collection on an account has to be made. The figure below illustrates the whole process. In short the debtor authorises the creditor to charge his account by signing a mandate. Finally the creditor's bank sends the signed mandate and the collection authorisation to the debtor's bank.

Also cross-border card payments shall become more efficient and safe. EMV and PIN represent hereby the common principles. EMV is well known as the international standard developed by Europay, Mastercard and VISA to make smart card terminals operate together more efficiently.²

3. Payment Service Directive

In 2007 the European parliament approved the *Payment Service Directive* (PSD), which deals with a number of issues which are not part of SEPA. The PSD introduces rights and obligations for users and providers of payment services and rights to provide payment services to the public. The PSD deals also with requirements for transparency and information. Member states must transfer these rights into national law till 2009. At the moment 25 different sets of national applicable regulations exist. Within the new payment area banks and investment firms must acquire a license and therefore fulfil certain criteria such as good repute, adequate system controls and minimum capital requirements. Cash and cash transactions, cash and cheque payments and payments under a voucher or points system are exempted from the licensed rights. To keep all information transparent a number of requirements have also been set up: Besides general information providers must offer pre-contract information which applies for the payment order, the time of execution or charges applicable. Also post contract information – information after the transaction - must be provided like the references for identifying parties or the amount and currency of payment. Liability must be provided in case of an unwanted transaction. Payment orders must be executed within one business day, in special cases also within three. All the rights just mentioned shall support a fluent operation between service providers and user.³

4. The European Payment Council

The *European Payment Council* (EPC) represents “the decision making and the coordinating body of the European banking industry in relation to payments.” The EPC was established in 2002 and shall provide strategic guidance for standardisation to formulate best practises and to monitor the implementations of decisions taken. Momentarily the EPC consists of 69 members, there under banks and banking

² Cognicant, White Paper, no Year, p. 4,5

³ Freshfields Bruckhaus Deringer, 2007, p. 2,3

associations throughout Europe. Moreover 300 professionals of the banking industry are involved in the work programme of the EPC.⁴

5. History of development

With the 28th January 2008 the first big step was taken to harmonise European payment processes. From now on the standards for the Credit Transfer and Direct Debit are binding – the one of the Direct Debit latest in November 2009. The EPC also opened a customer stakeholder forum, so that customers can help to develop the two schemes.

In general countries must adopt the general methodology of identification (IBAN / BIC) now and a pan European clearing structure was established. Entities, customers, institutions shall have access to the complete SEPA infrastructure in 201x, because the whole procedure shall be finished some time after 2010.

Plans for a pan-European financial system started much earlier. The overall basis for a harmonised financial market was the introduction of the Euro-currency by 11 countries in 1999 followed by 12 other states in 2002. The introduction of the 2560/2001 regulation meant another step towards SEPA, which limited bank charges regarding card payments, ATM withdrawals and credit transfers. Consultation between banks started in 2002 within the so called SEPA workshop. As a result in 2002 the EPC was found by 42 banks, three European Credit Sector Associations and the Euro banking association, which had been attending the workshop. The actual negotiating finished in December 2005, after the EU adopted “a proposal for a directive on a New Legal Framework for payments in the internal market”. January 2007 for cross border transactions the identification numbers IBAN and BIC became compulsory.⁵ The development and launch of SEPA is divided into three phases. The design phase began in 2004, where schemes for credit transfer and direct debit were developed. Moreover a framework for cards was developed. Within the implementation phase SEPA was launched and the developed standards were tested. In the last phase – the migration phase – the instruments have been migrated and are coexisting to the existent ones.⁶

6. Expected economical impact

The question arises, which economical impact SEPA will have on the banking industry. The banking industry is looking forward to SEPA. Within a survey 74% of the banks assumed, that it will enhance business opportunities, because of geographical changes. Also substantial cost savings are expected. It is estimated that a doubling of the payment value will result only in an increase of the costs of 22%. In

⁴ European Payments Council, 2008

⁵ Sepa.ie

⁶ European Central Bank, p. 14

fact improved cash handling might result in decreasing costs up to 25%. Another study concluded that the European standardisation will effect economies of scale in payment services. It is also possible that banks earn revenues of about 8 billion Euros by 2010 if they work on their policy to replace cash with non-cash transactions. However the introduction of SEPA might be more expensive then expected. Banks will need to invest three to eight billion Euros over the next year.⁷

7. SEPA in Malta

Malta's roadmap to SEPA is the Maltese Implementation Plan, which contains details on how SEPA compliance will be achieved in Malta. Since January 2008 SEPA credit transfer (SCT) is implemented in the banking community.⁸ The payment systems used in 2006 are SWIFT for Credit Transfers and for direct debit no established clearing system existed. ATM and EPOS were used for card transactions. For the next years the task for the Malta Banker's association is to coordinate and migrate SEPA into national level to align them with European standards.⁹ By November 2009 the Payment Service Directive will be put into national law and SEPA Direct Debits will be supported.¹⁰

8. Hopes and benefits

Hopefully SEPA will heighten competition and new innovative products will enter the market. Cost compensation shall be one particular aim, because the new system supports especially the use of electronic cash and payments in cash are in general more expensive.¹¹

How can enterprises benefit from SEPA? Enterprises can handle their payments only with one bank account, which will become more easy and quicker. The same applies for end consumers, so that payments in a foreign country won't differ from domestic ones. Incoming as well as outgoing payments will be transacted in the same format, so that the whole process is more transparent regarding the identification of both parties. Additionally to value added services, e-invoicing and e-reconciliation will be offered for the whole SEPA market.¹² Hopefully the standardized format heightens the trust of the customers in electronic payments. Especially card holders benefit, because they can offer there services throughout the whole Euro area.

⁷ Schmiedel, Heiko, 2007, p. 7 - 8

⁸ Central Bank of Malta

⁹ Malta Banker's Association p. 2

¹⁰ Central Bank of Malta

¹¹ European Central Bank, p. 17

¹² Irish Payment Services Organisation

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