Gertrude Tumpel-Gugerell: Implementing SEPA – our expedition to a fully integrated euro retail payment market

Keynote speech by Ms Gertrude Tumpel-Gugerell, Member of the Executive Board of the European Central Bank, at the IEA & Marketforce's 2nd Annual Conference "The Future of Cards and Payments", London, 6 July 2009.

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Ladies and gentlemen,

It gives me great pleasure today to update you on where we stand in our expedition to a fully integrated euro retail payment market – the Single Euro Payments Area (SEPA). A successful expedition calls for a good combination of exploratory spirit, a sense of orientation and determination. Sometimes just one single person can possess this combination of qualities. Take Captain James Cook, for example: not far from our venue, in front of Admiralty Arch, you will find a statue in memory of this famous British explorer, navigator and cartographer, who died 230 years ago.

Captain Cook undertook three major journeys; likewise, the SEPA challenge comprises three stages: the SEPA Credit Transfer (SCT) scheme, the SEPA Direct Debit (SDD) scheme and SEPA for cards.

The players in the European banking industry have joined forces to establish SEPA and successfully reached the first stage of this demanding but very promising journey – the introduction of the SEPA Credit Transfer scheme. We cannot, of course, hide the fact that a lot of stakeholders – including the Eurosystem – would have appreciated a faster adoption of SEPA by both providers and customers.

The adoption of the SCT scheme has started, but progress remained slow throughout 2008. However, recent figures give reason to hope that the dead calm is coming to an end and that a fresh breeze is ahead. The latest figures give a clear indication that SEPA has reached the tipping point: it is now being used for more than just cross-border payments. Therefore, there is a confident hope that the adoption rate might accelerate further in the near future, especially when we take into consideration the plans of the respective public authorities to adhere to the SCT scheme later this year.

This momentum will be further accelerated by the introduction of the SDD scheme. Forward-looking and European-thinking banks and infrastructures will already be offering SDD by November 2009 while others have up to a year in which to sign up to the scheme. Thanks to the reviewed regulation on cross-border payments, banks offering legacy direct debits in euro will definitely be introducing SDD by November 2010 at the latest. This will motivate a lot of companies to finally set sail and start implementing SEPA.

The outcome of the third stage of the SEPA journey, SEPA for cards, is perhaps the most uncertain. The Eurosystem continues to encourage market participants to introduce a European card scheme. Joint research by the European Central Bank (ECB) and De Nederlandsche Bank shows that the launch of a new European card scheme could provide the impetus for solving the problem of interoperability and overcoming the costly fragmentation of the European card market. Consumers and merchants are likely to benefit most from SEPA when sufficient competition in the card payment market alleviates any potential monopolistic tendencies. The ECB appreciates, therefore, the different initiatives that have a European card scheme as their destination and welcomes the travel preparations made by them. That said, we should not lose sight of our objective by starting even more initiatives. Instead, the projects that have already taken off are invited to get down to business and perhaps combine forces. Now is the time to come up with concrete travel plans, including defining and committing to milestones.

Perhaps it is not by chance that the British Prime Minister's Strategy Unit is located in Admiralty Arch, with the statue of Captain Cook in front of it. With everything that we hope to achieve for SEPA in the short and medium term, we must not lose sight of the broad SEPA strategy and our long-term objectives.

The objectives of greater harmonisation and increased innovation

In the past, the main reasons for exploration at sea were political as well as commercial, such as the discovery of new trade routes. However, Captain Cook's voyages in particular had an explicitly scientific purpose, too. The aim of his first journey, for example, was to observe and record the transit of Venus across the Sun.

SEPA is a project driven by business as well as politics and is also gaining more and more academic attention. A research conference held recently at the ECB found that a fundamental relationship exists between the retail payment business and overall banking performance. There is academic evidence that, in countries with more developed retail payment markets, the banks perform better. This relationship is stronger in countries which have adopted a relatively high number of technologies for retail payment transactions.

Starting in the 15th century, the Age of Discovery was characterised by increased competition among explorers in order to be the first to discover the last remaining uncharted waters. A by-product of this was that innovations in sailing ship technologies, the creation of new maps and advances in astronomy were achieved. In the same way, competition is an important contributor to innovation and efficiency in the field of retail payments, too. According to academic research, consumers in a very competitive retail payment market benefit from more choice, quicker execution of payments and greater efficiency. Competition among retail payment instruments fosters innovation and may also encourage retail payment providers to improve their services. As a result, banks also perform better in such a market. Furthermore, greater use of electronic retail payment instruments seems to stimulate banking business. At a time when banks are having to reconsider their business models in light of the current financial market developments, these are promising results and should even motivate us to strengthen our joint efforts to achieve a real Single Euro Payments Area. Retail payments could well prove to be the banks' trade route out of the rough sea that they are currently having to navigate. Therefore, the SEPA objective of harmonisation is of sustained importance and the European Payments Council (EPC) is encouraged to proceed with its efforts in realising this goal.

So far the EPC has been focusing mainly on core and basic payment instruments. This approach was necessary in order to establish a SEPA-wide framework within a reasonable amount of time. The final service offered should, of course, go beyond these basic products, since customers will set the benchmark at the level of service of the legacy instruments. However, this should not prevent providers and users from making a thorough analysis of their business processes and adapting them to suit their new SEPA environment. In addition, the EPC should also pay increased attention to the standardisation of the customer-bank interface.

The basic SEPA instruments that the European banking industry has delivered so far should provide the foundations on which to build a more innovative retail payment market. I expect more innovative products based on the core SEPA instruments, such as e-payments or m-payments, to emerge onto the market sooner rather than later. Flexible and innovative service providers are the most likely to succeed. Banks and infrastructures have to be open to new payment instruments in the electronic and mobile environment. Otherwise, as we can already see happening, third parties will step in and fill the gap. The EPC is encouraged, therefore, to intensify its work on mobile and electronic payments, and banks are encouraged to adopt the solutions developed by the EPC. We must start preparing now for the future and think beyond the borders of our current payment behaviour.

All these efforts to foster harmonisation and innovation will contribute to reducing the persistent fragmentation of the European payment market. History has indicated that a tendency towards national retrenchment may increase in times of uncertainty and the recent crisis has indeed confirmed this. Currently the state of our financial integration shows some signs of segmentation along national borders, particularly with regard to the interbank market.

Thus, it is important not to forget that integrated financial markets can help financial stability. They offer their participants a more efficient environment than a market divided by national borders ever could. Integrated markets are more liquid and offer better opportunities for risk diversification, thereby reinforcing the system's capacity to absorb shocks. Therefore, financial integration is directly linked to our objective of improving market resilience and also contributes to financial stability in the long term. As cross-border financial risks are becoming more and more important in Europe, we need to remain firmly committed to financial integration. For this, the further integration of the retail payment market is crucial. However, a persistent debate surrounds this integration process: who is the navigator on our SEPA journey?

Barriers to self-regulation – regulatory needs

Retail payments have traditionally been off the radar screen of most of the central banks, except from the perspective of pure oversight. Now, however, not only in Europe, but also in other regions, the crucial role of retail banking and payments in an efficient overall economy has been recognised. Therefore, central banks have decided to strengthen their role as a catalyst for change and the fostering of integration and innovation in this field.

I have persistently emphasised that SEPA continues to be a mainly self-regulated project. However, we must not underestimate the limitations of self-regulation and the thin line between cooperative and competitive space. There are elements which the market will not be able to accomplish on its own and which need more regulatory involvement. That is why the ECB has been increasingly involved as a moderator for the past few months in order to keep SEPA successfully on course.

Take, for example, the discussion on the multilateral interchange fee for direct debits. After intensive discussions with market participants, the European Commission, together with the ECB, has provided clarity on this controversial issue. The transitional provisions published by the ECB and the European Commission in September 2008 have been integrated into the amended regulation on cross-border payments.

Beyond these transitional provisions, banks requested additional guidance regarding the long-term business model for SDD. Consequently, in March 2009 the European Commission and the ECB published a joint statement providing further clarification. In particular, it has been made clear that, for reasons of efficiency, a general per transaction multilateral interchange fee for national and SEPA direct debit transactions does not seem justified, nor would it be compatible with EU antitrust rules.

Another example of where self-regulation might not be the best solution is the question of the migration end-date. Although we have successfully started out on our journey to SEPA, we have not yet determined our date of arrival. The Eurosystem has emphasised that an ambitious and yet realistic end-date for migration to SCT and SDD is necessary. Recent experiences with cash support the need to set a migration end-date. Despite several attempts to make dollar coins popular, customer acceptance has been limited. One of the major reasons given is that the 1 dollar bill was not simultaneously phased out with the introduction of the 1 dollar coin. The UK has been successful in introducing the 1 £ coin several years ago. When the first 12 European countries introduced euro cash each country defined a transitional period for the parallel use of the euro and the national currency, based on the maximum time frame set by the EU legislator.

A common migration end-date across Europe should, however, give national communities the possibility of setting earlier dates at the national level. Setting an end-date for SEPA migration would facilitate communication and provide more certainty for all stakeholders. The most viable option for determining a migration end-date is through regulation by public authorities, for instance by way of an EU regulation. The Eurosystem appreciates the fact that the European Commission has launched a public consultation on this matter.

Some people are of the opinion that, with the guidance given by the European Commission and the ECB on multilateral interchange fees for direct debits and the possible regulation of an end-date for SEPA migration, there is no room for self-regulation any more. Or, in other words, that there is no reason for the EPC to exist any more. I could not disagree more! The guidance provided on the multilateral interchange fees for direct debits and the possible setting of a migration end-date are necessary in order to allow the EPC's self-regulation to function. In other words, without this well-targeted public intervention, the SEPA project could have come to a halt. Therefore, for the Eurosystem, it is not a case of either self-regulation or outside regulation; rather, both should exist in parallel.

The question of governance

Amid all our ambitions to foster a more integrated and innovative market, we must focus on the customer even more. Both policy-makers and the financial services industry should be focusing on the customers' needs and benefits. After all, the financial industry has a legitimate interest in its products being used and accepted by its customers.

In its Sixth Progress Report on SEPA in November 2008, the Eurosystem emphasised that the success of SEPA depends greatly on adequate governance of the project and stressed that such good governance arrangements should aim to involve different stakeholders and provide transparency.

In more concrete terms, there is a difference between the governance of the EPC and the governance of the overall European retail payment market. Although the EPC plays an important – even crucial – role in the emergence of SEPA, it cannot be held accountable for the European retail payment market in general.

Let us first discuss the governance of the EPC. So far the EPC has done a good job, by publishing its rulebooks and recently also providing summaries of its industry discussions. However, more information could be provided on the EPC's planning and how it deals with changes requested by stakeholders.

Let me be clear: without a credible and decisive EPC, an integrated European retail payment market is hardly imaginable. Therefore, in my view, the EPC should continue to play a central role. As an executive body of payment service providers, it should define the common rules and standards for the European market. In such a way, and in line with our statements in our progress reports, the EPC should continue to work on improving its own governance arrangements. The EPC has the power to involve stakeholders and consult them on its deliverables. The recently launched Cards Stakeholder Forum is a step in the right direction, even if the exact structure of the group warrants further discussion.

There are lessons to be learned from what happens at the national level when attention is paid to the needs of the general public. The governance of payment systems requires transparent processes. Major changes to payment schemes should be subject to transparent evaluation, weighing up the costs and benefits to the banking industry and to society as a whole.

This leads me directly from the governance of the EPC to the governance of the overall European retail payment market. To put it in the context of Captain Cook: we need a captain; and we need to make the tasks of this captain clear before the end of 2009. We can learn from the experience of the Payments Council in the UK.

The governance of the European retail payment market also entails a more social, strategic and political dimension to retail payments, which, by definition, cannot be handled by a self-regulating body of banks or payment service providers alone. In some countries, best practices have emerged in the past few years. In addition to the coordination on the "supply side", which is the role that the EPC plays at the European level, national fora have emerged. These fora deal with the more social and political elements of the retail payment market, and we need to represent this to a certain extent at the European level.

A new European forum could promote the goals of SEPA in the context of the evolving landscape of the European retail payment market by:

1. firstly, ensuring appropriate coordination and dialogue with national structures during the migration process;
2. secondly, promoting innovative solutions in line with the objectives of the Lisbon agenda; and
3. finally, being transparent as regards end-users and all relevant stakeholders and involving them as market partners.

The creation of a European forum does not, however, dilute the continued importance of the EPC, now or in the future. The European retail payment market will benefit considerably from a strong EPC *and* an additional European forum dealing with the social, strategic and political aspects of the retail payment market.

Conclusion

In conclusion, allow me to re-emphasise that the SEPA ship has left the harbour destined for a fully integrated market for euro retail payments. The compass is set for a full Single Euro Payments Area.

The Eurosystem appreciates the efforts of those banks that are committed to launching SDD in November 2009 and we encourage all the others to follow suit as soon as possible. The projects for the introduction of an additional European card scheme are invited to increase their efforts and publish their concrete itineraries.

Payment services have stood solid as a rock throughout the turbulence of the recent months and it has been widely acknowledged that retail payments will be a cornerstone of banks' business in the years to come.

Therefore, it is even more important that our journey to SEPA will succeed – despite the periods of nearly stand still and turbulences. Competition, standardisation, innovation and the right level of regulation are the key factors contributing to a favourable outcome.