

# The Single Euro Payments Area : SEPA

H. Maillard  
J. Vermeulen

## Introduction

In the course of the entire process of economic integration which began in Europe half a century ago, several steps have been taken with the aim of unifying the various national financial markets and creating a genuinely integrated market. Undeniably the most dramatic stage was the advent of the euro on 1 January 1999 and the launch of the euro notes and coins three years later. At the same time, Target – the real time gross settlement system for large payments in euro – was established in 1999, creating a vital instrument for the implementation of the single monetary policy.

Today, all consumers can easily effect [cash] payments anywhere in the euro area, using the same unit of account. However, in the case of small cashless payments (retail payments), each country still has its own specific features (infrastructures, instruments and regulations) so that cross-border payments are more complex than domestic payments, and economic transactions between countries are more complex than those within national borders.

As part of the Lisbon Agenda, which aims to boost the competitiveness of the European economy, the SEPA (Single Euro Payments Area) project represents a major new step forward. It is intended to enable the economic players to effect cashless payments throughout Europe via a harmonised set of instruments, so that there is no longer any difference between a national payment and a cross-border payment. Thus, the establishment of SEPA will create an innovative, efficient and competitive retail payments market, giving the euro its true dimension as a single currency and permitting full use to be made of the

opportunities offered by the single market, since the payment systems work by “oiling the wheels” of the single market.

In the coming years, the traditional Belgian instruments – credit transfers, direct debits and card payments – will be replaced by European payment instruments. This revolutionary development requires the implementation of a complex process of harmonisation aimed at abolishing all the legal, technical and practical obstacles, and entailing the commitment of all the players concerned, ranging from the financial sector to the consumer and including businesses and public authorities.

In this article we describe the various phases in the creation of the single euro payments area, the European context in which it is taking place and the Belgian approach to the migration to the new payment instruments.

## 1. The concept of the Single Euro Payments Area (SEPA)

### 1.1 SEPA: definition and objectives

SEPA is “an area in which consumers, companies and other economic actors will be able to make and receive payments in euro, whether within or between national boundaries, under the same basic conditions, rights and obligations, regardless of their location”<sup>(1)</sup>.

(1) Towards a Single Euro Payments Area, the ECB's 4th SEPA progress report, February 2006.

Starting from a fragmented framework in which each country has developed a national payments system with its own characteristics (legal framework, consumer protection, payment practices, infrastructure, charging policy, etc.), SEPA aims to foster European integration via a competitive and innovative retail payments market in the euro area, capable of providing better services, more efficient products and less expensive payment solutions.

Once SEPA is in place, the advantages will be as follows:

- everyone will have the use of a set of common European payment instruments which will operate in the same legal framework and according to the same technical and operational standards. A Belgian consumer will thus pay his water bill for his home in Belgium in the same way as he pays for his holiday apartment on the Spanish coast, via the new European direct debit system. Similarly, a company will be able to pay its expatriate employees via one and the same bank regardless of the SEPA country in which it is based;
- competition between payment system suppliers will develop at all levels, which should, in principle augment their efficiency and lead to more advantageous pricing;
- firms operating at European level will be able to achieve substantial economies of scale by rationalising their payments: they will be able to handle all their payments via a single European centre for the entire group;
- SEPA will also help to eliminate some major obstacles to the free movement of products and services in the single market.

## 1.2 The SEPA area

The document “SEPA Countries and SEPA Transactions” (EPC<sup>(1)</sup> – 27 February 2007) identifies the countries which make up SEPA, namely:

- the thirteen countries which have adopted the euro;
- the fourteen other European Union (EU) countries;
- the three other countries in the European Economic Area (Iceland, Liechtenstein and Norway);
- Switzerland: even though EU legislation has not been transposed into Swiss law, the Swiss banks can join in the SEPA project by taking the necessary measures (Resolution EPC 040/06).

A number of territories are considered to form part of the EU (under Article 299 of the Treaty of Rome). They are the French overseas departments (Martinique, Guadeloupe,

Guyana and Réunion), Gibraltar (United Kingdom), the Azores and Madeira (Portugal), the Canary Islands (Spain) and the Åland islands (Finland).

Five of these territories have their own ISO country code. Altogether, therefore, thirty-six ISO country codes are possible in SEPA.

A transaction is only regarded as a SEPA transaction if it takes place between two banks with a Bank Identifier Code (BIC) comprising one of these thirty-six ISO country codes.

## 1.3 The European actors in SEPA

### 1.3.1 The Council and the European Parliament

Ever since the early 1990s, the European Commission has been examining the question of cross-border payments in the EU, in the light of the high charges, lengthy execution times and lack of transparency associated with this type of transaction. It therefore set the tone with Regulation 2560/2001<sup>(2)</sup> which obliged banks to cease differentiating at European level between charges for cross-border payments and charges for national payments.

SEPA aims to improve the operation of the single market and meet the targets defined by the Lisbon Agenda. The existing legal frameworks relating to payments are largely based on national regulations, causing fragmentation of the single market.

For some years now, the European Commission has been working on a draft European Payment Services Directive – PSD<sup>(3)</sup>. Adopted by the European Parliament on 24 April 2007, the PSD is to be transposed by no later than November 2009 into the law of each country making up the SEPA area. The European authorities thus wish to establish a single European legal framework, an essential prerequisite for implementing SEPA.

The directive is based on three main pillars:

- first, to permit stronger competition on the national markets, it regulates the right to provide payment services for the public by harmonising the market access conditions applicable to payment service providers other than credit institutions. A stumbling block which held up the directive for a long time was market access for payments institutions, new players offering payment services, and the status to be accorded to them;
- in order to strengthen consumer protection, the directive aims to improve transparency and to guarantee efficient payment systems. New information obligations

(1) EPC is the abbreviation for the European Payments Council, see 1.3.3.

(2) Regulation (EC) No 2560/2001 of the European Parliament and of the Council of 19 December 2001 on cross-border payments in euro.

(3) Directive of the European Parliament and of the Council on payment services in the internal market and amending Directives 97/7/EC, 2000/12/EC and 2002/65/EC.

will be imposed on payment service providers<sup>(1)</sup>: for instance, the payer will have to receive information on the charges payable, if any, on the payment transaction, and on their breakdown, the debit value date or the date of receipt of the payment instruction. The payee will have to be informed of all the charges applied to the payment transaction and their breakdown, and the credit value date;

- definition of the rights and duties of all the parties involved, be they consumers or payment service providers.

Finally, the scope of this directive is not confined to the new payment instruments defined by the SEPA project, and the directive will therefore apply in the same way to existing national payment instruments, both those for euro payments and those in any other national currency.

### 1.3.2 The European Central Bank and the Eurosystem

The European Central Bank (ECB) and the Eurosystem play a key role in the implementation of the SEPA project. The tasks of the Eurosystem include promoting the smooth operation of payment systems while ensuring their efficiency and security. In that context the Eurosystem therefore has to be an important player in the process, fulfilling the role of a catalyst.

The Eurosystem took the introduction of the euro as an opportunity for highlighting the need for a European payments area. It was invited to participate in the meetings of the EPC (European Payments Council) and most of the working groups as an observer, in order to put its own point of view on the strategy of the banks. That role also enables it to express the expectations of all the economic actors. It keeps a close eye on the progress of the work of defining the components of the future single payments area at European level.

The Eurosystem formulates recommendations for a retail payments system meeting the needs of a unified market, encourages governments to adopt the SEPA products as soon as possible in order to act as a driving force in putting SEPA in place, and collaborates in publicity measures at both European and national level, via the national central banks.

Having presented its vision of an international retail payments system in September 1999, the ECB published a number of progress reports<sup>(2)</sup> in September 2000, June 2003, December 2004 and February 2006 on progress towards the establishment of SEPA. The fifth version of that report is currently in preparation.

The national central banks of the euro area are closely involved in the preparation of European policy within the Eurosystem. At national level, each of them provides active support for the country's financial community, and assists its migration in order to foster the successful local implementation of the SEPA objectives.

### 1.3.3 The European Payments Council

The European banking community understood the signal sent out by the authorities, and in June 2002 it decided to set up a new pan-European body, the European Payments Council (EPC), with representatives from banks and associations of financial institutions from the thirty-one SEPA countries.

Via the EPC, which is based in Brussels, the European banking sector unequivocally affirmed its intention to create a single payments area by 2010, and to do so primarily by a process of self-regulation (interbank agreements concluded at European level).

The EPC is an international non-profit organisation governed by the Belgian legislation on international non-profit organisations (law of 2 May 2002). It currently comprises 67 members and encompasses the banks and European credit sector associations, namely the European Banking Federation (EBF), the European Savings Banks Group (ESBG) and the European Association of Cooperative Banks (EACB).

The EPC Plenary<sup>(3)</sup>, comprising representatives of all types of European banks, takes decisions on strategic questions prepared by a number of working groups dealing with key topics relating to the establishment of SEPA.

## 1.4 The SEPA components

Apart from the legal framework mentioned earlier, the project is based on a number of components intended to permit the eventual establishment of a totally automated chain for processing all euro payment transactions in accordance with SEPA.

Definition of the standards is an essential prerequisite for establishing an efficient payments system: the existence of common standards is the only means of achieving the automation of the entire payment processing chain. In

(1) Articles 36 and 37 of the Directive on payment services in the internal market.

(2) Towards a single euro payments area – Objectives and deadlines – Progress report.

(3) The current governance structure dates from 2004. The Plenary is the EPC decision-making body. It is assisted by the Coordination Committee.

SEPA, interoperability can therefore only be ensured if all the actors adopt common standards so that payments can be automated.

The EPC thus defined an interoperability framework for card payment systems (SEPA Cards Framework) and drew up practical rules (Rulebooks) for the new payment instruments (credit transfer and direct debit), namely the SEPA Credit Transfer (SCT) and the SEPA Direct Debit (SDD)<sup>(1)</sup>. The EPC defined these schemes, the rules applicable to the processing of payment orders, and the data necessary for their exchange. The aim is to establish end-to-end automation of the processing of payment instructions in order to execute them more speedily while also reducing the costs. All the schemes and the Rulebooks will be implemented on the basis of technical standardisation of the data exchange (XML language – ISO 20022 international standards).

In an initial phase which is currently nearing completion, the EPC concentrated on defining the basic components necessary for the creation of a genuinely unified market. Subsequently, the work will probably focus on the creation of added value services (AOS – additional optional services) permitting the progressive automation of the processing of payment transactions, e.g. via the dematerialisation of certain stages in the process. Thus, electronic invoicing (e-invoicing), the electronic reconciliation of invoices (e-reconciliation) and the European electronic direct debit mandate (e-mandate) are subjects to be addressed in more detail.

#### 1.4.1 Payment instruments

The EPC is using three main categories of instruments to provide payment solutions for future SEPA users: the European credit transfer, the European direct debit and the card payment.

These instruments have been developed to meet the everyday needs of European users by providing them with payment instruments which are both simple and economical. For more specific payment transactions, the market players will be able to develop additional optional services, based in particular on the specifications relating to the European credit transfer and the European direct debit. These “enhanced services” must not under any circumstances hamper the smooth operation of the basic service, restrict competition or cause renewed fragmentation of the market.

During the design phase of the various SEPA payment instruments, the EPC adopted two different but complementary approaches:

- a strategy for replacing the European credit transfer and the European direct debit by offering totally new instruments: it soon became apparent that it was unrealistic to try to harmonise the various different but similar existing payment instruments, in view of their great diversity. The EPC therefore opted for the definition of new instruments developed from the start for cross-border use. This resulted in two Rulebooks describing the schemes (rules, practices and standards) ensuring interoperability for the processing of SEPA payment transactions at interbank level;
- a strategy for adapting card payments. Since this type of payment is far more complex than the other two means of payment adopted, the EPC considered it preferable to adapt the existing schemes in line with a new series of technical and commercial processes and standards. For cards, the EPC produced a reference framework (Framework) setting out the main principles which card systems must satisfy in order to eliminate the technical, legal and commercial barriers impeding the interoperability of card transactions.

The “Rulebooks” define the standards to be respected for interbank exchanges, but the EPC also issues recommendations for relations between banks and their customers (*bank to customer B2C* and *customer to bank C2B*).

##### 1.4.1.1 The European credit transfer

The credit transfer is a payment order issued by a debtor to his bank instructing the bank to transfer funds to the payee’s bank.

The new European credit transfer operates according to basic principles similar to those of the current Belgian credit transfer, the work of the EPC having focused mainly on greater standardisation in order to automate the interbank payments (UNIFI (ISO 20022) XML).

The main innovations introduced by the EPC are:

- reachability throughout the SEPA area: it must be possible to arrange a payment in favour of any payee;
- compulsory use of the BIC<sup>(2)</sup> and the IBAN<sup>(3)</sup>, as is already normal practice for cross-border transfers;
- extended message information.

(1) The European credit transfer and the European direct debit are the terms adopted by the Belgian financial community to designate the two new payment instruments, the *SEPA Credit Transfer* and the *SEPA Direct Debit*. Their names may vary from one country to another: thus, in France, the preferred term is *prélèvement* (take out) rather than direct debit. In the rest of this text we shall use only the terms adopted in Belgium.

(2) BIC (Bank Identifier Code) – this code permits identification of the financial institution operating an account.

(3) The IBAN (International Bank Account Number) is an account number with a uniform, international structure. It is made up of the code for the country in which the account is held, a two-number check digit and the national account number (the traditional account number).

The EPC will probably adapt the content of its “Rulebook” to the more stringent requirements defined by the PSD when it becomes officially applicable, particularly as regards the time allowed for executing a payment<sup>(1)</sup>.

#### 1.4.1.2 The European direct debit

The direct debit is a transfer initiated by the creditor via his bank under an agreement concluded between the creditor and the debtor by means of a mandate.

For this instrument, too, the EPC has defined a set of common rules and procedures and specified a common service level, and processing times to be respected. Here, too, the use of the UNIFI standards (ISO 20022) XML is intended to standardise the messages exchanged.

The EPC opted for a European direct debit system based on the CMF model (Creditor Mandate Flow – the mandate is administered by the creditor), different from the current Belgian system which is based on the DMF model (Debtor Mandate Flow – the mandate is administered by the debtor's bank)<sup>(2)</sup>.

The main characteristics of the European direct debit are:

- reachability throughout the SEPA area: a European direct debit can be effected in favour of any payee;
- the mandate can be issued in paper form or electronically;
- compulsory use of the BIC and the IBAN;
- as well as the recurring direct debit, there is now the option of a one-off direct debit (which did not previously exist in Belgium);
- the debtor can ask his bank<sup>(3)</sup> to reverse a debit which has already been effected:
  - within eight weeks;
  - within 13 months if the mandate was invalid or had expired;

(1) The PSD sets a deadline of three working days. That will be cut to one day from 1 January 2010. For a payment between a Belgian payer and a Belgian payee, the deadline is still fixed by the Poty law at one working day.

(2) The current Belgian system of direct debits (DOM 80) is based on the DMF model: the debtor sends the mandate to his bank or to his creditor, but it is the debtor's bank that keeps the mandate and pays the creditor's request for payment after checking the mandate. The SEPA Direct Debit is based on the CMF model in which the creditor keeps the mandate and requests payment on that basis from the debtor's bank. The main difference between the two systems therefore concerns the party keeping and administering the mandate.

(3) The bank is then obliged to make the refund; the validity of the request has to be examined in the context of the debtor/creditor relationship.

(4) This concerns both credit cards and debit cards. However, special cards are excluded, e.g. cards issued by private companies, fuel cards, “Proton” type electronic purses, etc.

(5) EMV (Europay, MasterCard, Visa) is an international standard for chip cards. The abandonment of magnetic strips in favour of chips is justified by the ever-increasing security requirements. Interoperability was also at the centre of the development of the EMV card, which offers other functions in addition to cash withdrawals and payments.

(6) Framework for the evolution of the clearing and settlement of payments in Sepa, EPC, January 2007.

- The EPC is currently working on the preparation of a special European instrument for direct debits between businesses (B2B).

Meanwhile, these specifications are no longer entirely in line with the requirements of the European authorities. As in the case of the European credit transfer, the EPC will have to adapt the content of the “Rulebook” according to the obligations defined in the PSD, particularly as regards the deadlines for requesting reversal.

#### 1.4.1.3 The SEPA card payment

In the case of card payments, the EPC has been far less radical: it has confined itself to defining the SEPA Card Framework (SCF), setting out the general principles which issuers, holders, card systems and operators must satisfy.

The main characteristics of a SEPA card payment are:

- every card<sup>(4)</sup> issued by a credit institution must be capable of being used on any terminal throughout the SEPA area;
- competition is possible between payment card processing service providers: the opening up of the entire SEPA market will make the market competitive and reduce the costs to users;
- technical interoperability based on the use of chip cards meeting the EMV standard<sup>(5)</sup>.

### 1.4.2 The infrastructures

The SEPA clearing and settlement framework<sup>(6)</sup> is intended to guarantee access for all banks in the SEPA area (“reachability”). One of the basic principles is the clear segregation (unbundling) of roles and responsibilities between the payment instruments and the infrastructures (the whole set of procedures and systems used by financial intermediaries to clear and settle payment orders).

The infrastructures will play a key role in the success of SEPA by permitting efficient and secure transfers between debtors and creditors via the financial intermediaries. They will have to be capable of managing the migration of a critical mass of retail transactions to the new European payment instruments.

At present, the infrastructures are fragmented at European level: each country has developed its own (in some cases multiple) clearing systems, which may or may not be automated (ACH – Automated Clearing House) to meet national requirements. This has led to the coexistence of dozens of different infrastructures operating primarily at national level, generally with their own specific standards.

It is these national systems that exchange the very great majority of payments, which are predominantly domestic. The diversity of systems also engenders wide variations in service levels, not only between different countries but also between national and cross-border payments.

The clearing of cross-border transactions is currently based mainly on two types of solutions: multilateral systems or bilateral mechanisms in the form of correspondent banking. The future will decide whether these two types of solutions continue to operate in parallel, or whether one will come to dominate on the European payments market.

The SEPA project sets ambitious goals for infrastructures: they will have to ensure the interoperability required for the project to work, while respecting the constraints set by the SEPA framework for infrastructures and the PSD; in particular, it will be necessary to make major reductions not only in costs but also in the time taken to process international transactions in the SEPA area.

Interoperability will probably lead to consolidation of the payment infrastructures at European level, certainly in the case of multilateral systems, via one or more central structures managing all national and cross-border transactions (a central PE-ACH – Pan-European ACH).

So far, the EBA (Euro Banking Association) has developed STEP2, the first pan-European automated clearing house, which can clear both domestic and cross-border retail payments in euro. This is the first infrastructure to satisfy the criteria for a PE-ACH as defined by the EPC. However, up to now the volumes handled have been fairly marginal, and few national transactions are transferred to this European system. Other companies (Equens/Netherlands, STET/France, Voca/Britain, etc.) have announced that, in the future, they intend to offer a solution for clearing transactions in SEPA.

Another route is that followed by the EACHA (European Automated Clearing House Association) which links together the national clearing houses. This association is examining the possibility of interconnecting the national infrastructures within a vast payment exchange system.

By the end of 2010, all infrastructures will have to be capable of handling the critical mass of euro payments in the SEPA format, while ensuring that, until that time, the current payment operations exist alongside the SEPA instruments. Another challenge is to increase transparency in regard to the services offered and the rates charged by the infrastructure providers.

## 1.5 The European timetable for SEPA<sup>(1)</sup>

The preparations for SEPA are divided into a number of phases, most of them determined by the EPC. In 2002, the EPC proposed a timetable for SEPA, and so far that has been the guideline for the project. We can now present the progress of the SEPA project in the form of this diagram.

During an initial design phase (2004-2006), the EPC defined the general standards which lay down the rules and the main characteristics of the new payment instruments, also referred to as payment schemes. Between mid 2006 and the end of 2007, more detailed standards were derived from these general standards, defining the interpretation of the general standards and the concrete data formats in precise instructions for implementation and IT development.

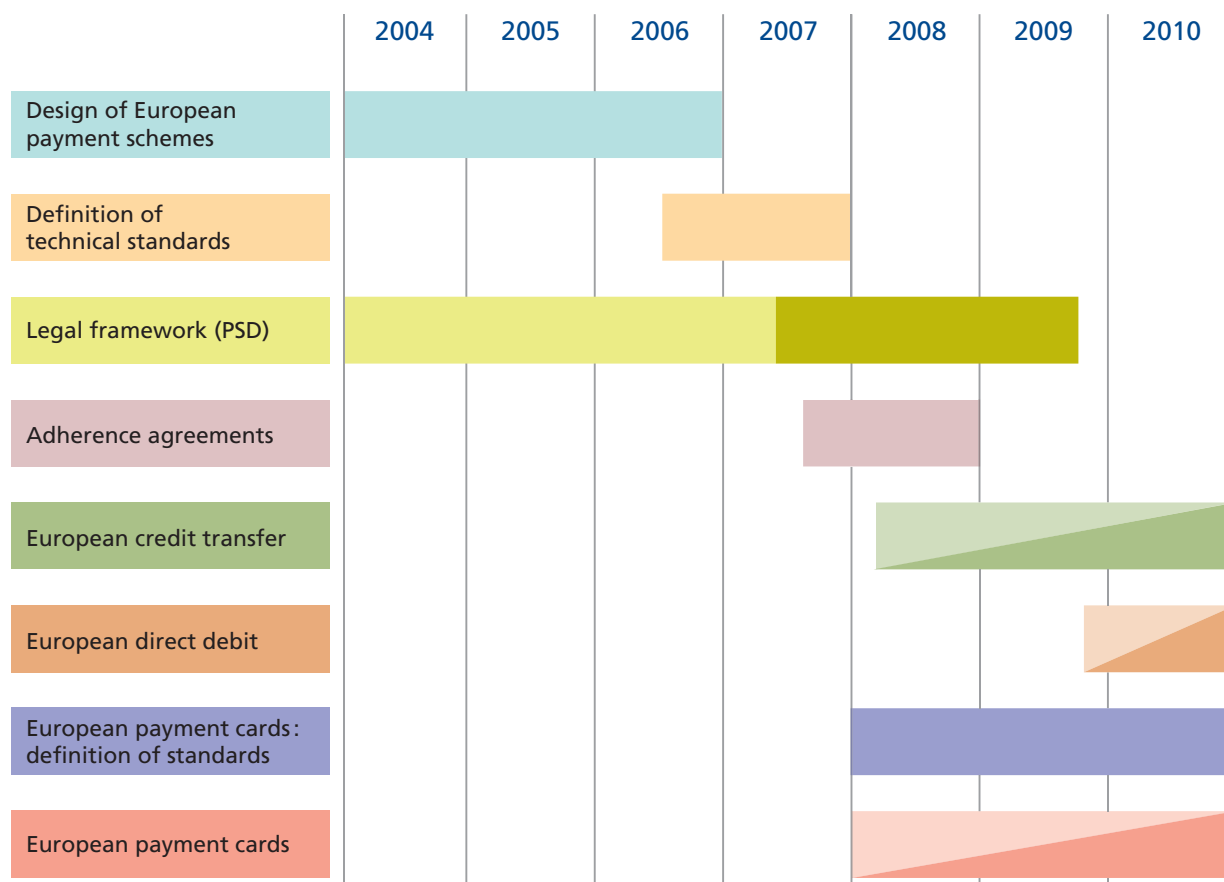
At the same time, the European Commission, the European Parliament and the Council were working on a new directive.

The next stage in the transition to SEPA will begin in September 2007. From then on, all banks are expected to undertake to use the new European payment schemes for their customers' payment transactions. For that purpose, each bank is expected to sign an "adherence agreement" with the EPC. These are statements of intent in line with the self-regulatory character of the EPC, without any legally binding measures. It is hoped that the maximum number of banks will sign these adherence agreements on a voluntary basis, so that the new payment instruments can be launched on time, namely on 28 January 2008. On that date, the banks are to offer their customers the European credit transfer as a new payment instrument. The old national credit transfers will, of course, continue to be processed. The aim is to discourage the use of national credit transfers gradually between now and the end of 2010. No specific plan for abandoning them has yet been drawn up in most countries, which suggests that they will not actually be dropped until after 2010.

In principle, the scenario for abandoning national direct debits should be much shorter, since the launch of the European direct debit is scheduled for 1 November 2009, the date on which the European directive is to be finally transposed into national law, even though the initial EPC project still sets the deadline at 2010. However, there are still as yet no plans for abandoning national direct debits. It is therefore even more likely than in the case of European credit transfers that they will not actually disappear in the majority of countries until after 2010.

(1) The actual plan for Belgium is explained in section 2.2.





In the case of card payments, the EPC hopes to be able to establish standards by the end of 2010. Each country has its own card payment infrastructure, accompanied by specific protocols and technical solutions, and harmonising them at European level will be a lengthy process. From 2011 onwards, the banks will issue SEPA cards only.

In contrast to the introduction of the euro notes and coins, where there was a compulsory schedule for the various phases, the establishment of SEPA is a process being managed mainly by the market. With the support of the ECB and the European authorities, the EPC has defined the general framework. The market (banks, businesses and public authorities) are now expected to commit themselves to making the necessary changes to establish SEPA. The Belgian example, described below, shows the form which that process may take in practice.

## 2. SEPA in Belgium

Although SEPA is a project involving 31 countries in a unified payments area, each of those countries is to organise its own migration to SEPA starting from its own national

situation, typified by its own payment practices, instruments and specific infrastructures.

### 2.1 The Belgian implementation arrangements

SEPA is not just a banking project, but concerns all the economic actors. While the banks are the ones most involved in the preparations, sooner or later the other participants in economic life, namely companies, public authorities and consumers, will be confronted by the switch to the new European payment instruments. This is therefore a project which affects the community as a whole, and will require a commitment by all the parties concerned.

In order to ensure that the migration to this new environment is organised efficiently, a dual structure has been set up in Belgium :

- an interbank structure, called the SEPA Forum, which deals with all aspects relating to the banking world;
- a broad community consultation structure which also involves the non-bank players via the creation of a third working group called "Implementation of SEPA in the community", which comes under the "Steering Committee on the future of means of payment".

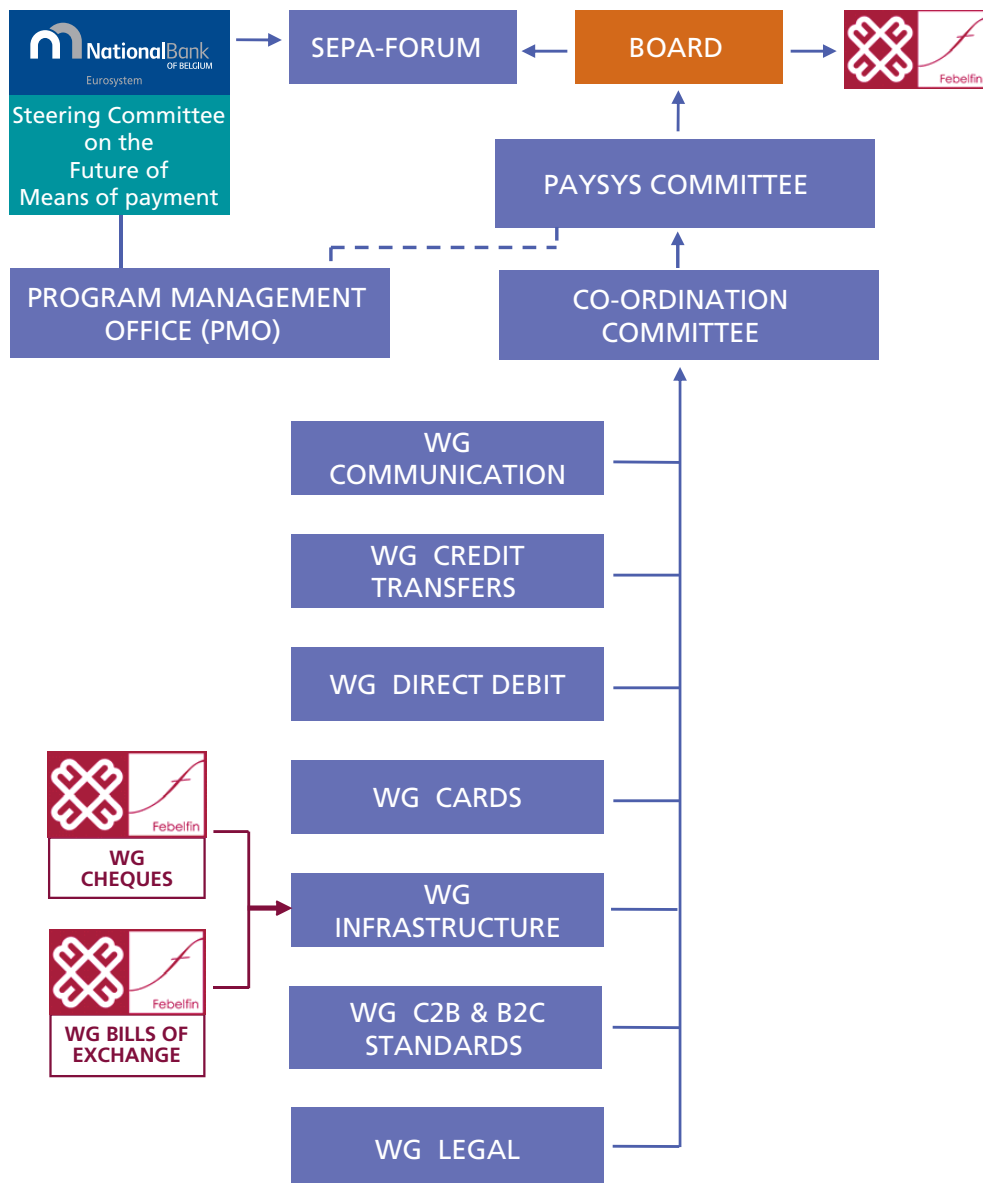
### 2.1.1 The SEPA Forum

The SEPA Forum was set up in 2005 as a platform for consultation between the Belgian banking sector, the Post Office and the National Bank of Belgium. It is a consultative body without any legal form. Its organisational structure is based on that of the EPC and comprises a number of levels:

- at the lowest level, various working groups and task forces are examining the impact in Belgium of decisions taken by the EPC. All the financial institutions are represented in these working groups;
- on the basis of the findings of these working groups, the Co-ordination Committee (Cocom) coordinates the work, prepares proposals and monitors the overall cohesion;

- The Payment Systems Committee (Paysys) is a consultative body existing at the level of the Belgian financial community, which defines the policy and the strategy for all questions relating to payment systems in Belgium. This body submits proposals to the SEPA Forum which has to pronounce its opinion on them;
- at the highest level, the Governor of the Bank chairs the SEPA Forum and, with the top management of the banks, he endorses the proposals issued by the specific working groups. The banking sector then undertakes to implement those decisions.

Belgium is represented in the various European working groups active at EPC level by the chairmen of the corresponding Belgian working groups. They defend the Belgian viewpoint in the discussions and ensure consistency and direct communication between the Belgian and European levels.





### 2.1.2 The social dialogue

The migration to the SEPA environment affects the whole community since, ultimately, all the economic actors will use the new payment instruments. It is therefore clearly essential to involve all the parties in the implementation of SEPA in Belgium. The aim is to introduce SEPA in the optimum way in order to make it a genuine success for the Belgian economy as a whole. Consultation of all the parties concerned is therefore an essential pre-condition for the successful implementation of SEPA.

In 2004, a "Steering Committee on the future of means of payment" was set up in order to consider the future of means of payment jointly with the parties involved. It was therefore logical for a special working group, dealing with aspects relating to the implementation of SEPA in Belgium, to be set up under the Steering Committee.

The Steering Committee comprises representatives of the banks, public authorities, the Post Office, consumers, corporates, small firms and the self-employed. The NBB chairs the committee, and provides administrative and organisational support. Three sub working groups have been set up to consider the specific questions concerning consumers, businesses and public authorities.

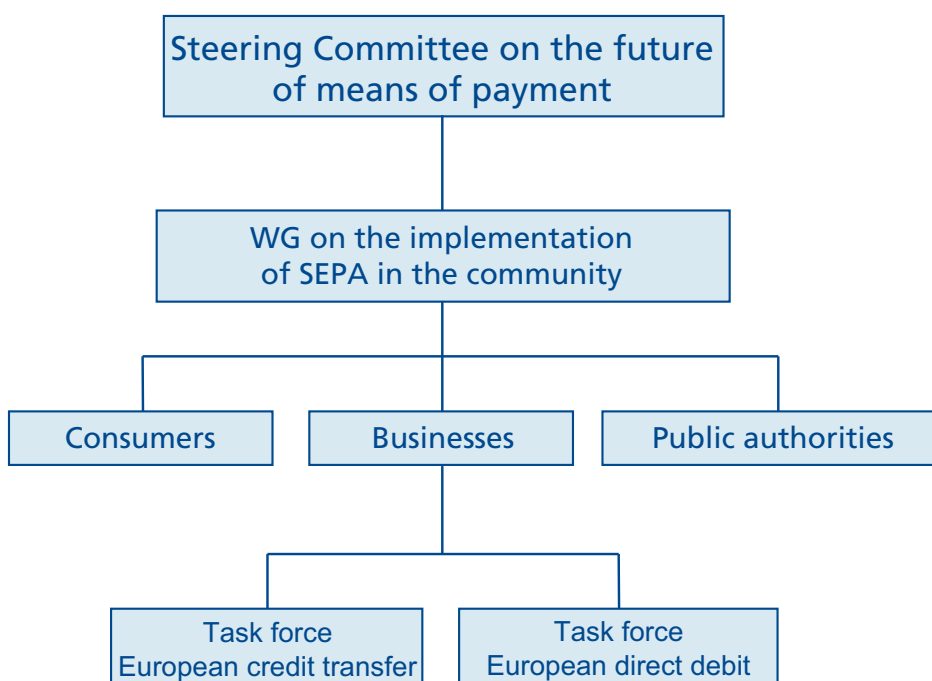
Initially, the aim is to raise the awareness of the economic actors, to exchange information on the progress of the SEPA project in Belgian society and to identify the points

requiring special consideration. At a later stage, a concrete plan for migration to SEPA will have to be drawn up for each of the main sectors.

In the sub-group on public authorities, the federal authorities – wishing to present themselves as early adopters – have set up their own Steering Committee. That move is also entirely in line with the recommendations of the European authorities<sup>(1)</sup>: the adoption of the new payment instruments by the public authorities will speed up the attainment of the critical mass of payments necessary for the SEPA project, and will set an example for the other actors.

In the subgroup on businesses, two task forces have also been set up to coordinate the migration and the transition, one for the European credit transfer and the other for European direct debit, the ultimate aim being to avoid disruption for consumers. The latter task force comprises the main Belgian issuers of direct debits. The banks are also largely dealing with the preparations concerning enterprises. Suppliers of banking solutions such as Isabel (computerised interfaces between enterprises and banks) are in the process of developing software dedicated to SEPA transactions.

(1) In the view of the European authorities, the national public authorities which originate or receive large volumes of payments (wages, taxes, etc.) should act as a driving force and set an example in the introduction of the new payment instruments, by committing themselves to the SEPA project as soon as possible.







The timetable for the introduction of the European credit transfer in Belgium centres on two dates:

- launch of the product on the Belgian market on 28 January 2008;
- migration period with gradual switch to the European credit transfer<sup>(1)</sup>;
- 31 December 2010: abandonment of the current Belgian credit transfer form.

2.2.2 The European direct debit

The new European direct debit system is fundamentally different from the current Belgian system. However, the Belgian banks decided to migrate as swiftly as possible to the new common standard and abandon the current system. Maintaining two very different systems in tandem would entail substantial costs, would probably delay the conversion and would make it necessary to adapt a system already destined for abolition to the new rules laid down by the PSD.

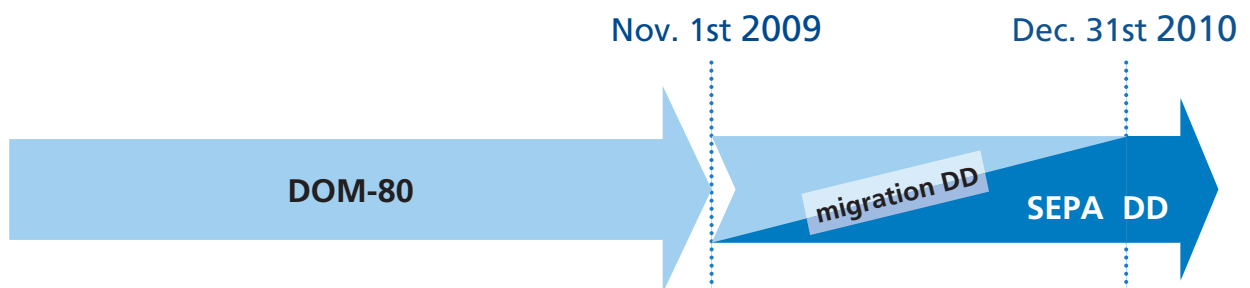
For users, both businesses and individuals, the main changes will concern the following points:

- bank identification via the combination of the IBAN and the BIC in the same way as for the European credit transfer;
- administration of the mandate: all direct debits are based on the grant of a mandate by the debtor in favour of the creditor. In the case of the European direct debit, the mandate will be retained by the creditor and not by the debtor's bank, as in the case of the Belgian direct debit;

- the request for repayment by the debtor: subject to compliance with the conditions laid down in Article 52 of the PSD, the debtor has eight weeks in which he can reclaim from his own bank the whole of the amount debited, or even thirteen months if the mandate had expired or was invalid;
- a new variant of the direct debit will be offered to users via the introduction of a one-off European direct debit which enables the debtor to issue a mandate authorising the creditor to initiate a single debit from his account.

The Belgian financial community has opted for a scenario in which the current Belgian system is replaced by the new European standard. Although direct debits do not have as large a share of the market in Belgium as in other countries, the number of direct debits is considerable, as is the number of mandates currently held by the debtor banks (around 30 million). In order to avoid the need for enterprises to get their customers to sign new mandates when changing their current direct debits to the European direct debit system, the Belgian banks have developed a mandate migration process<sup>(2)</sup> which will permit their exchange via a central mandate database containing data supplied by the banks currently holding the mandates; creditors will consult the database via their own banks. This exchange of mandates will be effected by an application developed by the NBB.

(1) The fact that some public authorities intend to use the new European credit transfer form from 2008 will certainly mean that the critical mass can be attained quickly during the migration period.  
 (2) This process allows the mandates to remain legally valid. The need to inform the parties about their new rights and obligations is under examination.



The Belgian financial community had initially planned to introduce the new type of European direct debit on 1 January 2008, in accordance with the recommendations of the European authorities and keeping to the same timetable as the European credit transfer. At the end of 2006, owing to the delayed adoption of the PSD it was decided to postpone the launch date, because harmonisation of the legal framework throughout the SEPA area is essential for this product. Otherwise it would be impossible for a firm to administer its direct debits with customers in different countries, and thus to deal with varying repayment application times.

The recent adoption of the PSD and its expected transposition into the various national laws by November 2009 at the latest prompted a further postponement of the actual launch date for the European direct debit in Belgium. Thus, the launch date has been set at 1 November 2009, and the period in which the current system and the European direct debit coexist will be kept as short as possible. The probable obligation to apply the PSD to the current direct debit is likely to encourage enterprises to migrate to the new system. The choice of one or more migration scenarios is one of the subjects being discussed with the main users of this means of payment in the task force on the European direct debit.

In any case, the main Belgian corporate users of the product are already making preparations for the migration.

### 2.2.3 Card payments

Belgium has always had a pioneering role in the field of debit card payments. There is currently only one system in Belgium, namely the Bancontact/Mistercash scheme applied by Belgian banks. Bancontact/Mistercash has been managing the whole card payment processing chain: relations with card issuers, relations with traders, transaction processing, sale and maintenance of payment terminals, etc.

In regard to card payments and the planned process of migration to the SEPA framework, there were four possible scenarios for the Belgian banks:

- convert the present Bancontact/Mistercash scheme into a SEPA-compliant scheme enabling any card to be used on any terminal in the SEPA area: the banks felt that this scenario was unrealistic for a “small” system in view of the size of the SEPA area;
- conclude alliances with other systems to cover the whole of Europe: the banks also considered this option to be unrealistic, since no other system has ever succeeded in concluding such an alliance;

- maintain the national card system and add an international card scheme with co-branding: that is already the case for over 95 p.c. of Bancontact/Mistercash cards which also have the Maestro international function (Mastercard). However, that solution is not in line with the long-term philosophy of the SEPA project since it maintains the fragmentation of the national markets;
- abandon the Belgian system and adopt an international scheme which meets the requirements of the SEPA framework.

The last scenario is the one favoured by the Belgian banks. In the future, Belgian banks will be able to offer other card schemes which conform to SEPA. In the view of the Belgian banks, switching to an international system has another advantage, namely the possibility of incorporating new technical developments, which is not feasible in the case of the Belgian scheme that is reaching the end of its life.

The chosen solution also offers the opportunity to split the card payment processing chain, certainly following the sale of Banksys and Bank Card Company by the Belgian banks. Competition would thus become possible at every stage in the chain: choice of the card scheme which banks offer their customers, choice for traders, choice of the operator for the card processing, etc.

The solution chosen by the Belgian banks means that, on Belgian cards, the Bancontact/Mistercash standard will be replaced by an international standard for domestic Belgian transactions.

The traders’ representatives were vigorously opposed to this solution for a number of reasons:

- the Bancontact/Mistercash system has proved to be not only efficient but also secure, relatively cheap, and easy to use. Traders fear that the new system will not achieve the same level of quality as the present system, and that it will be expensive to update the terminals and the software;
- the main objection raised by distributors concerns the charges for payment transactions. The new scale of charges would lead to a substantial increase in the cost per transaction for traders. A key element in the debate is the introduction of an interchange fee. Under the Belgian Bancontact/Mistercash system, Banksys is in direct control of relations between the card holder and the trader via his bank. In contrast, international schemes are based on four-part models with the payment of an interchange fee by the trader’s bank (acquirer) to the card holder’s bank (issuer), to compensate for the higher costs which the latter incurs (security, guaranteeing the payment to the trader, etc.).

There is nothing certain as yet about these interchange fees, so that the various parties still cannot in any case make the strategic choices which are necessary in the process of migration to SEPA<sup>(1)</sup>.

More generally, there are fears that the predominantly national card payment systems currently used in the different countries may be replaced by one or two international systems owned by Mastercard and/or Visa, reputed to be more expensive. Establishing a duopoly for this type of payment is not, in principle, likely to encourage more competition.

The Eurosystem has drawn the actors' attention to this question<sup>(2)</sup> and expressed certain fears regarding the SEPA framework for card payments as adopted by the EPC. The Eurosystem has listed a number of general policy principles intended to supplement the framework:

- the existence of consumer choice between the various competing card payment systems, with no predefined priority;
- the existence of a competitive, reliable and cost effective market comprising service providers and infrastructure suppliers;
- the elimination of all technical, contractual and operational barriers forming the basis of the existing national segmentation.

The major sources of concern for the Eurosystem relate to a possible increase in usage costs associated with the replacement of the national systems by international systems (Visa or Mastercard), which generally involve higher interbank fees than the national systems. Nor does it favour co-branding, since – by maintaining the majority of the existing situations and limiting the use of international standards to cross-border transactions only – that does not offer economies of scale or strengthen competition.

The Eurosystem is therefore encouraging the emergence of a European card system based on the second option of the "SEPA framework for cards", namely extension of a national system to all SEPA countries by the conclusion of alliances via agreements between systems which continue to operate independently. That is the Eurosystem's preferred way of boosting competition on the market and making use of the experience of national card systems.

A number of initiatives of this type have apparently been launched. For instance, the Berlin Group, which held its first meeting in October 2004 and comprises 22 of the leading players in the field of card payments, is trying to develop a solution based on national debit card schemes. A more recent initiative by eight major European banks aims to develop<sup>(3)</sup> an alternative debit card system which

will eventually compete with the Mastercard and Visa systems. However, it is too soon to assess the feasibility of these initiatives.

#### 2.2.4 The exchange and clearing infrastructures in Belgium

In June 2006 it was decided that the Belgian centre for exchange and clearing (CEC) would not be converted into a PE-ACH. Ultimately, therefore, the processing of national payment transactions will have to be transferred to a PE-ACH, depending on the offers available on the market. The reason is the same as in the case of the card scheme, namely that the Belgian system is too small to consider developing it at European level.

The Belgian banks did not wish to act as the first mover in the process of migrating payment exchanges to a PE-ACH. At present, there is no pan-European system capable of handling the transactions with the same level of service and at similar cost. Meanwhile, it was therefore decided to establish a provisional scenario by making the CEC SEPA-compliant, i.e. capable of handling the payment transactions effected between Belgian banks via the new SEPA payment instruments. Thus, by the beginning of 2008 when the European credit transfer is expected to be launched on the Belgian market, the Belgian banks will already be able to exchange payments in the new European formats.

For that purpose, the CEC participants and sub-participants have undertaken to:

- continue exchanging their national transactions in the current format via the CEC until the abandonment of the products specific to Belgium (scheduled for the end of 2010);
- use the new SEPA payment instruments as soon as they are launched:
  - for transactions between Belgian banks: exchange via the CEC or a PE-ACH;
  - for cross-border transactions: exchange via a PE-ACH.

Eventually, when the "Belgian" means of payment are replaced by SEPA instruments, the CEC will have to terminate its activities. However, that is not expected before the end of the migration period, namely 2010.

(1) Since the question of charges is a complex one, care should be exercised when comparing the current situation with the one resulting from SEPA. Thus, the obligation imposed by SEPA to "uncouple" the services will ensure greater transparency of pricing and will guarantee competition at the level of each service. In the future, this uncoupling will prevent the internal "cross-subsidising" of certain services, a practice which Banksys was previously able to apply. There also seem to be some signs that this increased competition and transparency have already led to lower prices, particularly at the level of the terminals.

(2) *The Eurosystem's view of a SEPA for cards*, European Central Bank, November 2006.

(3) *De Tijd*, "Banken werken aan nieuw Europees betaalkaartsysteem", 12 May 2007.

## Conclusion

SEPA is unquestionably the missing link which will make it possible to create a genuinely integrated, single payments market. This project aims to replace a set of national systems and standards with European ones, to eliminate all differences between domestic payments and cross-border payments within an area comprising thirty-one countries. SEPA will provide the whole of that community with retail payment instruments which are faster, more efficient, cheaper and more secure than those currently available on the national markets.

SEPA is the result of the efforts of various European actors. The European authorities set up a regulatory framework for all payment services, providing the essential legal basis for SEPA. The ECB and the Eurosystem, which guarantee the smooth operation of the payment systems, advise, assist and encourage all the parties concerned. Finally, the banking community coming together in the EPC is playing a proactive role and – principally via self-regulation – is working on the definition of a harmonised payment environment based on three common payment instruments and on European infrastructures. The ultimate aim is to establish a fully automated chain for processing euro payments, with competition possible at every stage.

Between January 2008 and December 2010, users will gradually have to change their payment practices and switch to the new pan-European instruments. Each country will have to organise this migration according to its own specific situation. Without wishing to act as a pioneer, Belgium is probably one of the countries which has made the most progress in organising that migration. A long tradition of interbank consultation – forming the basis of the current Belgian payments system which is universally acknowledged as efficient – permits the speedy translation of the SEPA standards in accordance with Belgium's particular needs and characteristics, and the definition of a migration plan governing the transition which will end with the disappearance of the current Belgian instruments, replacing them with the new SEPA means of payment. The social dialogue which has been established will mean that all the players concerned can be involved in the migration process: if all the needs and concerns are taken into account, that will facilitate a smooth and harmonious transition.

In the short term, the switch to SEPA will doubtless entail considerable efforts for all the parties concerned, but in the medium and long term it will bring benefits by offering banks, enterprises, public authorities and consumers a retail payments market which is innovative, unified, modern and efficient, enabling the initial objectives to be achieved.

## Bibliography

Beau D., G. Chabassol and B. Colles (2006), "La marche vers l'Europe des moyens de paiement scripturaux: le projet SEPA", *Bulletin de la Banque de France*, 147, March.

De Tijd, "Banken werken aan nieuw Europees betaalkaartstelsel", 12 May 2007.

ECB (2006), *The Eurosystem's view of a SEPA for cards*, November.

ECB (2006), *The Single Euro Payments Area (SEPA): an integrated retail payments market*.

ECB (2006), *Towards a single euro payments area: objectives and deadlines – 4th progress report*, February.

European Payments Council (2007), *Framework for the evolution of the clearing and settlement of payments in Sepa*, January 2007.

European Payments Council (2007), *Making SEPA a Reality*, 9 January 2007.

European Payments Council (2007), *SEPA Countries and SEPA Transactions*, 27 February 2007.

Febelfin/National Bank of Belgium (2007), *The Belgian SEPA Migration Plan – Version 3*, January.

## Internet sites

Bank information for Belgian consumers:

<http://bank.startpagina.be/>

Europese Centrale Bank:

<http://www.ecb.int/paym/pol/sepa/html/index.en.html>

European Commission:

[http://ec.europa.eu/internal\\_market/payments/sepa/index\\_fr.htm](http://ec.europa.eu/internal_market/payments/sepa/index_fr.htm)

European Payments Council:

[http://www.europeanpaymentscouncil.eu/content.cfm?page=sepa\\_vision](http://www.europeanpaymentscouncil.eu/content.cfm?page=sepa_vision)

Febelfin:

<http://www.sepabelgium.be>

Government of the Flemish Community:

<http://www2.vlaanderen.be/ned/sites/financien/>

National Bank of Belgium:

[http://www.nbb.be/pub/07\\_00\\_00\\_00/07\\_01\\_00\\_00/07\\_01\\_06\\_00\\_00.htm?l=fr&t=ho](http://www.nbb.be/pub/07_00_00_00/07_01_00_00/07_01_06_00_00.htm?l=fr&t=ho)