



EUROPEAN CENTRAL BANK

EUROSYSTEM

DIRECTORATE GENERAL PAYMENT SYSTEMS AND
MARKET INFRASTRUCTURE

2 February 2007

SUMMARY OF THE 13TH MEETING OF THE CONTACT GROUP ON EURO PAYMENTS STRATEGY

(Retail and large value payments issues)

Frankfurt, 21 November 2006

1. Approval of COGEPS minutes from previous meeting

The Chairman, Mr. Gerard Hartsink, welcomed the members of the COGEPS. After a few preliminary remarks of the Chairman, the group approved the minutes for publication.

2. Preliminary remarks of the co-Chair

Due to the tight agenda there was no reporting on this point.

3. COGEPS co-operation model

The Chairman presented the evolution of the EPC structure and of its dialogue with the European Public authorities. He concluded that COGEPS created trust between the banks and the Eurosystem, and that this co-operation allows monitoring, stimulating and being a catalyst in order for the payment industry to be in line with the decisions taken both in the retail and large value fields.

The Co-Chair, Mr. Godeffroy, presented the current co-operation model and confirmed that the Eurosystem is currently satisfied with it. He underlined that in the future more efforts will have to be made to increase the awareness on SEPA among corporates and public administrations. He further clarified the difference between the co-operation model and the oversight framework, by stating that the final goal of the co-operation model is to foster European integration, while the oversight framework is aimed at maintaining financial stability for which the ECB Governing Council is the decision making body. He agreed that clarification will be needed about the envisaged overall regime of the schemes, scheme owner and scheme management entity.

4. SEPA Direct Debit and Credit Transfer

a) Progress report on the SEPA Direct Debit

Christian Westerhaus, Chair of EDD WG, clarified that Rulebook v2.2 has been updated and that in order to deal with direct debit (DD) implementation issues a task force will be established. He reported that the EPC in September had approved the principles for developing an alternative channel for mandate submission, the so called debtor mandate flow (DMF) channel. The underlying principles are: i) mandate from debtor via debtor bank and creditor bank to creditor; ii) availability of debtor bank e-banking channels to ensure full electronic submission (although paper submission will still be possible); and iii) optionality for all actors. A common mandate layout is being developed, and the Storyboard will be updated to align the communication. In the second quarter of 2007 a new ISO standard should be established to carry the mandate related information for the DMF.

Mr. Westerhaus also stated that the Business-to-Business direct debit (B2B) will be an optional feature. There will be no refund rights after the settlement date; therefore, the debtor bank will have to check the existence of the mandate. The collection cycle will be shorter when compared to the Business-to-Consumer direct debt (B2C). All services will be fully described in the Rulebook to be delivered for national consultation, for a sound check of the banking community at large and for a legal verification.

He highlighted that two issues will not be included in the Rulebook v3.0. Firstly, e-signature adoption will be included in a later version of the Rulebook and a workshop in December will clarify the technical issues. Secondly, the risk mitigation annex will not be made public and therefore will be separated from the rest of the Rulebook v3.0.

The Eurosystem pointed out that it is important to clarify how the two mandate flows will co-exist, and how they will be explained to the users (corporates or individuals). It is also important to make sure that the users do not face a situation where the choice is only apparent, i.e. they choose options which in the end are not available.

The EPC clarified that CMF will be mandatory as of 1st January 2008 although its practical implementation will depend on the availability of the PSD. The DMF is still considered as an optional service and the EPC has planned to initiate a consultation process to its members and their communities to decide whether DMF should be made mandatory. The final decision will be taken by the EPC plenary in March 2007.

b) Common solution for Direct Debit creditor mandates and SEPA (non-Mastercard and non-Visa) cards

Harry Leinonen, Bank of Finland, presented the issue for information of the COGEPS. He pointed out that there are synergies between direct debits and debit cards (i.e. debit pull technology). Thereby existing solutions could be re-used without putting in place new infrastructures.

The actual problem is to find a secure and efficient way for electronic direct debit mandate presentment by the payer to the creditor and a network and framework/schema for transferring European (non-branded) card payments. The proposed solution would rely on two points: i) use EMV cards to convey the mandates to the creditors; and ii) use the direct debit interbank infrastructure to transport card payments. This would imply that in direct debit cases based on mandates given to creditors, the transactions at POS would technically resemble debit card transactions without a payment guarantee and that non-Visa/non-Mastercard SEPA debit card payments would be routed technically as direct debits but with a payment guarantee as an option where available.

The EPC agreed to further analyse this proposal.

c) Multilateral balancing fee

Claude Brun, EPC Vice Chair, reported that the EPC conducted a study on a SEPA direct debit multilateral balancing fee. By analysing the costs on the two banks involved in a direct debit transaction, the study was aimed at clarifying the need for a balancing fee and at defining its maximum level. Claude Brun indicated that the underlying methodology has already been explained to the European Commission and to national competition authorities, who did not raise competition concerns, so far. The default maximum multilateral balancing fee has been identified in the amount of 0.093 euro per transaction from the creditor bank to the debtor bank. This unique fee, in which all return costs are included, is going to be implemented as part of the SEPA Direct Debit rulebook.

d) Additional Optional Services (AOS)

Charles Bryant, EPC Secretary General, clarified that AOS equally apply to any of the SEPA schemes, and that they fall into two categories 1) AOS provided by individual institutions as value added services to the basic schemes. These are considered to be outside the scope of the EPC's work, as they are part of the competitive domain; 2) community AOS, on which the EPC will soon publish a positioning paper. Community AOS are classified into 3 groups: a) data-based AOS, namely the available fields and data characteristics which can be mobilised on top of the core schemes to take the full scope of the UNIFI ISO 20022 XML standards; b) delivery-channel AOS, between banks and customers; 3) other AOS. AOS stem from the need to cope with innovation and regional, national or group specificities which may be based on the way data are carried or described, therefore outside the mere scope of the payment environment.

On the Eurosystem side it was pointed out that there is no reservation against AOS as such, but it was stressed that community AOS should not be misused to keep regional or national fragmentation, but

rather to facilitate the transition from national to European solutions. Therefore, regional or national community solutions in the form of AOS should either be phased out at some stage or offered to all users in the EU.

It was further stressed by the Eurosystem that transparency must be mandatory for community AOS, as the clear danger is that it becomes a platform for overprotection of the national differentiations. The EPC confirmed that transparency will also be mandatory for usage rules for optional fields in the core schemes (e.g. remittance code, which cannot be defined as AOS). The EPC will address the transparency issue in their positioning paper.

It was agreed to request all national communities to provide their list of AOS in order to verify what is going to be in common and what will remain as mere national specificities.

e) Progress report on the SEPA Credit Transfer

Mark Hale, Chair of ECT WG in EPC, reported that the progress of the Credit Transfer Scheme is aligned to the EPC document release schedule. He pointed out that since the last COGEPS close co-operation with EACT has taken place to enhance existing core and basic schemes and to take into account comments received. EACT is reviewing a proposal on how to structure the 140 character field and the options for using that field for remittance advice reference. He also underlined that FAQ will be published before the end of the year to provide a sort of guideline for the Rulebook implementation.

f) Presentation on the Scheme Management Entity

Charles Bryant, EPC, stated that the Scheme Management Entity (SME) is an evolving function of the EPC for managing and governing the Rulebooks. The SME creation will require changes to the current EPC's charter and the definition of a set of detailed internal rules (to be approved by March 2007). The EPC will own the Schemes, and two main pillars of activities are identified in the scheme management. The first pillar concerns the development and evolution of the Schemes, which will take place via a structured dialogue with the stakeholders to gather input in a transparent and systematic way at national and European level, gathering input in different forums (i.e. with heavy users, light users, vendors/service providers). The final decision regarding the changes in the Rulebooks will remain with the EPC Plenary. The second pillar is related to the administration and compliance of the Schemes, which is aimed at ensuring that the Rulebooks are enforced and administered properly and that any dispute is dealt with in a consistent way. The SME will be in charge of the second pillar, and from a legal viewpoint it will be part of the EPC AISBL.

It was clarified that the Eurosystem in its oversight function will have the right to act as an overseer towards the scheme owner, the scheme themselves and the scheme management entity. However, its concrete role remains to be further discussed.

g) Priority payments: next steps

Gilbert Lichter, EBA Association, briefly summarised the discussion held during the SIBOS meeting, and stated that the issue was presented to the TWG for clarification. Currently discussions are ongoing with SWIFT to create a database where the name of banks adherent to the protocol could be published. At present, 28 banks are in the pilot and they should be ready by June to offer such a service. EBA clarified that the EBA priority services will be open to any bank (EBA member or not). Any infrastructure will be able to use this protocol for priority payments. EBA Association also confirmed that they have no intention to register the ownership of the usage of the protocol as there will be no proprietary standards.

5. SEPA clearing and settlement infrastructure: next steps

Charles Bryant, EPC, clarified that the scope of the discussion did not include cards' processing infrastructures. He stated that the EPC has separated the infrastructure environment from the payment product schemes, for which the EPC is fully responsible. The EPC approach to the CSMs was therefore to opt for a framework instead of a rulebook (the PE-ACH/CSM Framework). The framework sets some principles for the market and specifies modalities of clearing and settlement. The first modality is the PE-ACH, which is scheme-compliant and in addition provides reach for all participants. The second one is the scheme-compliant ACH, (may include some of the current national ACHs), which processes the SEPA-products, but does not grant reach to all participants. The third one is any other form of organised but decentralised CSM. The EPC expects these three modalities to comply with the above-mentioned Framework, and it was underlined that interoperability is granted by the Scheme Rulebooks and the adoption of the ISO 20022 (XML) standard.

Wiebe Ruttenberg, ECB, highlighted that standardisation, interoperability and consolidation are essential to promote an efficient payment market in euro. Infrastructures in a first step should become SEPA-compliant. However, in order for infrastructures to be interoperable throughout the euro area more has to be achieved in terms of clearing and settlement standards, routing, security, opening hours, contractual issues (technical and business interoperability). Open standards, not only in the inter infrastructure domain, but also in the interbank domain, are crucial for banks to freely choose the infrastructure to connect to. Interoperability is conducive to a market driven process of consolidation. To achieve economies of scale, the consolidation process could lead to 4-6 ACHs. Any risks of continued or renewed fragmentation within SEPA should be eliminated. Looking further ahead, a code of conduct might be contemplated for the SEPA infrastructures, as was recently agreed by the securities industry aiming at interoperability, unbundling of services and transparency of prices and services.

On the EPC side it was stated that the interoperability issues clearly have an impact on the definition of the timeframe for testing, and it was recognised that the current testing work will be based on the CSMs specifications available at this stage.

EBA pointed out that they are widely interlinked with ACHs, in particular the ones which are operated by NCBs, and interoperability is ensured by the use of common standards. EBA is active in organising

information sessions and in distributing specifications, and is committed to achieve full reachability within the EU-13 by the end of 2007.

The Eurosystem sees the infrastructure for SEPA not by definition solely based on one or more PEACHs, but reachability for all banks is the most important issue. This can happen via STEP 2 which is currently the only PE-ACH. However, it is expected that EBA Clearing Company does not abuse its position by overcharging market participants.

EPC sees the infrastructure as a competitive environment. To meet the deadline of 1 January 2008 it seems that there are solutions available in the market. Regarding the problem of overcharging it was pointed out that also double charging should be avoided when using a PE-ACH combined with a SEPA-compliant ACH.

6. Cash

Leonor Machado, Chair of the EPC Cash WG, reported on the steps taken to present the SECA Framework to the Eurosystem and praised the decision of the latter to propose a Roadmap for actions contributing to more convergence of Eurosystem NCB cash services. As regards National Cash Plans she reported that the second round has been initiated. For the standardisation activities high-level specifications were delivered to the Eurosystem. They are aimed at spreading common a Eurosystem standard for Euro banknote packaging.

Antti Heinonen, ECB, also reported on the good progress after having received the SECA Framework from the EPC, which is the first document where a structured approach and priorities are clearly shown. As regards the roadmap for more convergence of NCB cash services, he clarified that this will be delivered by spring 2007. He also underlined that the timetable for SEPA and SECA are not aligned. Furthermore, all relevant stakeholders (including CIT-industry) have to be involved. On the specific content of some of the topics the Eurosystem will consult the EPC.

7. SEPA Cards Framework agreed principles and next steps

Wiebe Ruttenberg, ECB, shortly presented the report on the Eurosystem's view of a "SEPA for Cards". The report was only published the day before on the ECB website and for this reason it was not discussed in length. In the report, the Eurosystem explains that there is a risk that SEPA migration might not entail optimal results concerning the interchange fee and general fees level, governance of card schemes and achievement of a greater degree of market integration. Against this background, the Eurosystem sees the need for at least a third initiative, whether it takes the form of an alliance, it is a national scheme expanding or a brand new scheme which will moderate those risks and ensure a higher degree of competition. With the report the Eurosystem intends to clarify a series of public policy provisions that need to be taken into consideration by banks and their card schemes, in addition to the requirements of the SCF, in order to operate within SEPA. These include the need for each card scheme to define and publicly disclose a medium to long-term strategy which is consistent with the objectives of SEPA; to

protect confidentiality of personal data; to contribute to the design of standards with a clear commitment to achieve full interoperability and timely implementation; to have a strategy on how to reduce fraud, and especially cross-border fraud; and to foster competition. In the report the Eurosystem requests the EU Commission to announce as soon as possible an interchange fee policy providing clear guidance, and to clarify its position with respect to some acquiring and acceptance practices. In addition, the EU Commission and the national competition authorities are requested to align their decisions on particular interchange fee cases.

Claude Brun, as Chair of the EPC Cards WG, reminded the participants that the implementation of the Framework is the responsibility of banks. He also reported on the progress made in terms of fraud prevention by the implementation of EMV technology and highlighted the need for detailed work plans for developing and implementing standards for every phase of the card payment transaction and for combating fraud types other than those covered by EMV, as also requested by the Eurosystem. Mr. Brun also reported on the work undertaken in the field of standardisation and summarised the existing standardisation initiatives. He concluded by presenting the next steps which will be taken by the EPC.

Concerning the alignment of decisions of national and European competition authorities, Eva King, European Commission, mentioned that the European Competition Network (ECN) with sub-groups is already dealing with SEPA, MIFs etc. However, she added that past court cases cannot be overruled, as this would affect legal certainty. Of course, there are some landmark decisions such as the Visa decision which expires in 2007 and will be reviewed, and the expected MasterCard decision. As a result, more alignment is desirable but there will still be differences as there will always be a case-by-case approach. Due to this approach, DG-Competition will not establish any general framework but there is the possibility of future regulation. In addition, the first draft of the sector inquiry identifies some problematic practices and will provide some guidance to the market. Concerning the monitoring of prices, the EU Commission is in favour of a reactive stance, and shares the ECB's views on fraud and data protection.

The Eurosystem clarified that the report is for consultation and that feedback is expected from the banking community. For this reason, an ad hoc COGEPS on Cards will take place early in 2007 and the card meeting planned for 1 December in Strasbourg will be used to get also the feedback from the card schemes. On the risk of price increase, it was further highlighted that it should be avoided to feed the general perception of price increase due to the introduction of SEPA. Therefore, it was suggested to have an observatory to monitor the process, but it was also pointed out that the Eurosystem is not the natural candidate for that.

On the EPC side it was highlighted that there are a limited number of options that schemes can follow in order to migrate to SEPA and the industry should not be blamed in case of subsequent price increases. In general, moderation and caution was suggested on the price issue as different prices correspond to different services. As regards interchange fees in particular, the idea of a code of conduct and business rules was discussed, as it does seem not possible to build SEPA without a clear guidance on the interchange fee issue. The Alliance scenario was criticised by some participants on the grounds that it

presents the risk of preserving market fragmentation, and the acceptability of the interlinking was questioned.

8. Proposed directive on payment services

Eva King, European Commission, reported on the process which is currently undertaken to approve the Payment systems directive (PSD) in first reading. Parties seem to be heading in direction of a compromise. Sensitive issues remain, namely: i) payment institutions and their supervisory regime, where parties are coming closer to a compromise; ii) time for execution of payments (D+1 or D+2); and ii) scope of application of the PSD, where the tendency seems to be that the PSD will not apply to payments which are arriving from (or are sent to) third countries. The transposition time will be left to 18 months, due to Titles III and IV, which touch upon civil law of the Member States. It was stressed that it will be vital to co-ordinate transposition among the Member States to ensure that when banks send out the new terms and conditions to customers, they are valid throughout the euro area and EU-27. In terms of migration, it should be made transparent how legacy contracts (e.g. old mandates in the case of direct debit) could be transformed into the SEPA mandates. The Commission shares the Eurosystem's view that even if PSD is not adopted yet there is no need to delay SEPA.

The EPC will soon formalise a position on how to proceed in case the PSD is not in place, but there seem to be general agreement that the main problem will be for the SEPA Direct Debit and not for Credit transfers and Cards.

The Eurosystem confirmed that independently to the adoption of PSD banks should continue with the implementation of the SEPA products. It will be further investigated what implications have to take into consideration in case the PSD is not adopted on time.

9. SEPA implementation

9.1 National implementation and migration plans

Gerard Hartsink, EPC Chair, reported that in terms of implementation four work areas are very important for the implementation process:

- i) Communication: the EPC issued a document "Making SEPA a reality", which is going to be used by banks during the communication campaign;
- ii) Testing: Charles Bryant (EPC) explained the preparation process for the testing phase (i.e. Testing Framework, preparation and experts recruitment) and clarified that although the EPC will define testing scenarios, the actual organisation of testing will be left to communities. Testing documentation will be released to the banking community early in 2007.
- iii) Directory operational readiness, which is a practical guide for the banking community with a description of the implementation organisations and contact.

- iv) Sharing national experiences, as there are lessons to be learned from the national implementation plans which could be shared with other communities. Currently this is done in the Roll-Out Committee which will be transformed in an Implementation Managers Forum.

The EPC developed a document describing the current level of preparation for SEPA. This includes among others, single banks, banking communities at national levels, operators, and public sector. It represents a self-assessment exercise and shows that public administrations are not well advanced. The document will be soon shared with the Eurosystem.

Eva King, EC, reported that the EC is organising high level political support for the implementation of SEPA (e.g. ECOFIN SEPA resolution). In addition, she announced that the EC will publish its strategy on SEPA next steps, which will include the work on cards and the review of the Regulation 2560/2001. The Regulation will be reviewed to reflect the current status and also to clarify the requirements on prices, and on statistical reporting. She reported that the Regulation review might also be done with the aim of facilitating SEPA migration thus reducing duality periods.

Wiebe Ruttenberg, ECB, reported that on national implementation and migration plans a discussion has taken place in the Governing Council on the current status in the different countries. Next year an update will be done. He invited the EPC to share their assessment with the Eurosystem, in order to align the monitoring tools. The Eurosystem also stressed the need of having concrete information on the migration process is crucial to monitor the implementation of SEPA.

To the question whether the EPC has already a global view of the migration plans, the EPC answered that as soon as the schemes are implemented it is expected that all countries have consequent migration plans in place and this is considered to be a country-level issue and a market-driven approach. The Eurosystem encouraged the EPC to take a collective responsibility on this issue.

9.2 Involvement of Public Administration, Corporates and SMEs

Gerard Hartsink, EPC Chair, stated that it is important to involve high level decision makers in corporates in order to obtain a clearer commitment to adopt SEPA products. Communication with SMEs should be improved, and NCBs have a very important role as the main part of the work should be done at national level. As concerns public administrations he highlighted the complexity in mapping such sector as the boundaries between public and non-public is not always easy to define. He also pointed out that the banking sector will clarify what is available to public administrations in terms of SEPA products.

Eva King, European Commission, reported that EC treasury service will invite the EPC to explain the SEPA products. The EC will compile a list of public administration entities to contact, and plans to hold a forum for public administrations to explain the business case for SEPA. The EC will also organise forums in which corporates will be able to express their expectations and clarified that further developments are needed in the area of e-invoicing and value added services. They are considered as key for corporates to have a clear interest in SEPA products.

Wiebe Ruttenberg reported that the ECB will send messages at very high level stressing the importance of early adoption of SEPA products, in particular on the side of public authorities. Regarding SMEs he encouraged banks to increase their efforts at local level to approach the vast number of small firms which need clear and simple information on how SEPA will translate into concrete steps for them. He announced that early next year the ECB will hold the regular meeting with users on SEPA, and that later in the year the ECB also intends to hold a conference for end users like corporates and public authorities. He also stressed the need to progress further in the field of e-invoicing and other value added services.

9.3 Communication strategy

Charles Bryant, stated that in this field the main function of the EPC towards its membership and the other stakeholders is to produce relevant material, and it is up to the communities to communicate with their client base. He reported that the EPC website has been upgraded, and that after the publication of the document “Making SEPA a reality”, a whole series of fact sheets will be published. He also indicated that the EPC is working on a guide for banks on how to inform public administration.

Wiebe Ruttenberg stated that the ECB has also upgraded its SEPA webpage, where it had published two brochures on SEPA (short and extended version). The extended brochure will be translated in all EU languages. He also reported that in addition to the regular meetings with end- users, a SEPA summit was organised in November, with an intense media exposure.

It was reported that a trilateral dialogue between EPC, EC, and ECB has been initiated to work together on the communication issue. As a concrete first example, before publishing its extended brochure the ECB requested the EPC and EC to comment on it, with the view that communication messages should be as aligned as possible. The EPC reported that the brochure is seen as a very fair and reasonable summary of what is the SEPA project about, and that it represents a good example of the good level of collaboration in this field. In January next year further joint work will be undertaken.

On the Eurosystem side, it was stressed that currently corporates represent the most important target group for SEPA communication and therefore it is expected that the joint efforts move in this direction. As a concrete example, a list of investment items for corporates (and eventually for public administrations) could be built.

10. TARGET2 issues

Patrick Poncelet, TARGET Working Group Secretary, presented the current state of the work. He highlighted that during the summer two joint task forces have been established to solve the remaining issues and to enhance the preparation for testing and migration:

- 1) The operational task force has so far dealt with issues related to contingency procedures, flexibility for banks, multi-addressee access, and settlement of ancillary systems.

2) the testing and migration task force has dealt with TARGET2 directory issues, balance of payment reporting, TARGET2 user testing guide for migration, national migration profiles, ancillary systems profiles, and migration of multi-country banks to facilitate testing.

He underlined that the release of UDFS version 2.2 announced for 15 December 2006, was essential for the work of programmers, and therefore advocated for an earlier release. He also pointed out that more effectiveness was needed in answering questions posed by banks', although most of them are now solved with the recent release of the third progress report on TARGET2.

Carlo Martens, ECB, clarified that the reason for not distributing the UDFS version 2.2 earlier was that it has gone through a thorough revision process within the Eurosystem, which has taken more time than expected. However, he reassured that no new business features will be added, and accepted that clarifications on banks' open questions that have an impact on banks' software developments open are needed. He therefore proposed to publish this specific information via a separate document, so-called "advance technical release notes". The first issue of this type of documents would be published as soon as possible and whenever future changes to the UDFS may have an impact on banks' software development, the Eurosystem intends to notify the banks as quickly as possible by means of such advance technical release notes.

11. Others

Heiko Schmiedel, ECB, presented the preliminary results of the SEPA economic impact study conducted by the ECB. He mentioned that the aim of the study was to obtain a balanced picture of the SEPA economic impact and of its related opportunities for banks. As a pilot, data has been collected from a small group of major European banks. In describing the main findings he pointed out that the overall average impact seems to be broadly moderate. He indicated that in the short-term there will be higher costs mainly due to coexistence, (setting-up and running SEPA schemes in parallel), total payments business revenue will be neutral, and cross-border competition will be minor. In the long-term, banks expect some downward pressure on revenues due to increased cross-border competition. However, banks are likely to benefit potential cost savings, e.g. economies of scale in the long-run. The ECB might consider enlarging the sample of participating banks.

Jean-Michel Godeffroy, ECB, briefly reported on the topics recently discussed by the CPSS.

Harry Leinonen, Bank of Finland, circulated a paper on the Helsinki Manifesto: "We have to move fast, before it is too late". He particularly stressed the need for the creation of EU-wide standardised and harmonised banking and financial eServices.