Topics of this issue:

1. Interoperability in the world of cards?

In its Green Paper on card, internet and mobile payments[1] the EU Commission stresses the benefits of standardization and interoperability. It points to the positive results reached with respect to credit transfers and direct debits and criticizes the lack of interoperability in the field of card payments.

"In line with the Commission's proposal for credit transfers and direct debits, the principle of interoperability could be applied in the cards market" (p. 17).

The Commission's statements on e- and m-payments suggest that it also contemplates action in these fields.

The meaning of the term "interoperability" is defined in the following paragraph:

"To ensure that any payment can reach any beneficiary without detriment to the actors and intermediaries involved, a higher level of coordination is desirable in the form of full interoperability." (p. 17)

So, "full interoperability" is the aim, implying "any payments" should reach "any beneficiary".

Our comment

We have already looked at the Green Paper and what it says about interoperability in our January edition of this Newsletter. But we would like to come back to this issue because it took us some time to grasp the enormous importance of the Commission's suggestions with respect to "full interoperability".

First let's go back to the definition cited above. What does that mean in practical terms?

- *Any holder of a Skrill (Moneybookers) account can pay any holder of a PayPal account?*

[1] European Commission, GREEN PAPER. Towards an integrated European market for card, internet and mobile payments, COM(2011) 941 final, Brussels, 11.1.2012 (http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2011:0941:FIN:EN:PDF)

- *Any holder of a Visa card can pay any MasterCard merchant?*
- *Any holder of an Amex card can pay any Visa or MasterCard merchant?*
- *Any holder of a Cartes Bancaires card can pay any ec cash merchant?*

In the field of credit transfers and direct debits the Commission has mandated just that.[2] Payees with a payment account that allows acceptance of direct debits or credit transfers must be reachable from any other SEPA account that allows the account holder to make credit transfers or initiate direct debits. Ultimately, interoperability is gained through consolidation of legacy schemes to a common SEPA scheme rather than through linking of different schemes with each other. It is instructive to recall that early SEPA ideas started in the 1990s, in those days it was discussed how to interface schemes with each other rather than how to consolidate schemes. As it turned out the differences in terms and rules between the schemes hampered the interlinking approach.

It seems that the Commission is contemplating such an interlinking approach for card payments and e/m-payments. To be sure, there are some card schemes that would not suffer a great deal from such an approach. Indeed, the participants of EAPS (Euro Alliance of Payment Schemes) are trying to achieve just that. However, the EAPS approach works only as rules and regulations of participating schemes are fairly similar or nearly interchangeable. EAPS rules accordingly are concise compared with rules of the international schemes. So, issuers and cardholders as well as acquirers and merchants need not seriously care about differences between schemes. By contrast, the rules of the international schemes vary in many details. So there is no straightforward way to interlink these systems with each other. Also from a business perspective for the large international 4-party schemes and proprietary e/m-payment schemes such a regulation would be a no-go. Imagine Visa having to obtain agreement from MasterCard for a chip-only product like V PAY. More generally, any innovations would have to be shared automatically with rival schemes. The same would apply to e/m-payment schemes. This would basically mean that innovation would be slowed down enormously.

A cooperative approach, relying on ex ante standardisation, may have some merits in markets for "commodity products". A case in point is the credit transfer and – to a lesser

[2] For direct debits, see Article 9 in the REGULATION (EC) No 924/2009 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 16 September 2009 on cross-border payments in the Community and repealing Regulation (EC) No 2560/2001. For credit transfers, see Article 3 in the REGULATION (EU) No 260/2012 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 14 March 2012 establishing technical and business requirements for credit transfers and direct debits in euro and amending Regulation (EC) No 924/2009 ("end-date regulation").

degree – the direct debit. In many countries, such products have, indeed, been supplied cooperatively by the whole banking community. The same applies for debit card payments and cash withdrawals. In this way, reachability and economies of scale have been achieved. However, in many cases, another implication has been almost zero innovation. Does the EU Commission really want such a result for card payments and e/m-payments?

2. M-payments: Head: you win; tail: I lose

Once again, m-payments are all the rage. After the bursting of the first m-payment bubble more than ten years ago it took the industry some time to recover. However, the spread of NFC (near field communication) and the increasing use of smart phones have triggered new enthusiasm.

Initiatives of Apple and Google have shaken up the market and telcos and PSPs are struggling to come up with their own solutions. In Germany, Telekom has joined mpass the m-payment scheme of Vodafone and O2. In Holland, banks and Telcos have teamed up to roll out NFC-based m-payments. The so-called “Sixpack” initiative hopes to get the approval of European anti-trust authorities soon. Time will tell whether such hopes are realistic. The UK-based “Project Oscar” of Telefónica, Vodafone and Everything Everywhere had to give up hope of a fast clearance by DG Competition. On April 13, the European anti-trust watchdog announced that an in-depth investigation of the British initiative would be opened.[3]

Meanwhile, the EPC produces White Papers on m-payments and the EU Commission complains in its Green Paper that the European development in e-/m-payments is not fast enough.

Our Comment

It is a familiar picture, by now: one branch of the EU Commission is pushing market participants to come up with interoperable solutions, the other is quick to intervene and suspect restrictions of competitions – even in markets that still have to be developed.

In its Green Paper, the EU Commission quotes estimates of the m-payment volume in 2014 totaling more than USD 1 trillion (of which USD 350 billion in Europe). Thus, it does not come as a surprise that the EU Commission sees a big potential market for European payment providers. But at the same time the Commission is concerned that European providers might

[3] Commission opens in-depth investigation into the creation of a mobile commerce joint venture by UK mobile operators Telefónica, Vodafone and Everything Everywhere, IP/12/367, 13/04/2012.

miss a big opportunity. It points out that Asia/Pacific has already far more m-payment users than Europe. What are the reasons? According to the EU Commission

"One of the key reasons for the slower market take-up in Europe is the highly fragmented mobile payment market. The key market actors (mobile network operators, payment service providers, mobile phone manufacturers) have not yet agreed on a viable business model enabling inter-operable payment solutions." (Green Paper, p. 6)

Thus, it sees interoperability as sine qua non of a European m-payment success. The world viewed with the eyes of DG Competition looks a little different:

"The Commission's initial investigation revealed that the joint venture and its three parent companies may have the technical and commercial ability and incentive to block future competitors from offering their own mobile wallet services to customers in the UK, or to degrade the quality of these competing mobile wallets so that they become less attractive."[4]

Somehow, one cannot help the impression that whatever the industry does, it is always wrong: non-cooperation is bad for interoperability, cooperation is bad for competition.

On the whole, there is a strong sense of "déjà vu". When the Spanish bank BBVA teamed up with Telefonica Moviles in 2000 to come up with a joint m-payment scheme (Movilpago) they were instantly scrutinized by the Spanish competition watch dog.[5] Anti-trust authorities demanded that other banks and telcos were allowed to participate. Obviously, this slowed down the whole project and then the m-payment wave burst and everything surrounding m-payments became much more difficult. The same may happen again. Or, this time, others may be faster and grab the market.

3. Canadian Task Force for the Payments System Review

In December 2011, the Task Force for the Payments System Review published its final report.[6] The Task Force finds that the Canadian payment system is "remarkably antiquated" (p. 5) and diagnoses the need for radical modernization. According to the Task Force, such modernization might bring huge benefits: *"a thoroughly modernized payments system could save the Canadian economy as much as two per cent of GDP in productivity gains,*

[4] See: Commission opens in-depth investigation into the creation of a mobile commerce joint venture by UK mobile operators Telefónica, Vodafone and Everything Everywhere, IP/12/367, 13/04/2012.
[5] See Malte Krueger, The Future of M-payments – Business Options and Policy Issues -, Background Paper No. 2, Electronic Payment Systems Observatory, Institute for Prospective Technological Studies, Sevilla 2001. http://www.h-ab.de/fileadmin/dokumente/krueger/2001_M-Payments_ePSO%20Background%20Paper%202.pdf
[6] Task Force for the Payments System Review, Moving Canada into the Digital Age, December 2011.

equivalent to $32 billion in annual savings for Canada." (p. 4) In order to reach this goal, the Task Force wants the Canadian Government to take the initiative. In its final report, the Task Force recommends the following actions (p. 10):

- "Implement electronic invoicing and payments (EIP) for all government suppliers and benefit recipients.
- Partner with the private sector to create a mobile ecosystem.
- Propel the build of a digital identification and authentication (DIA) regime to underpin a modernized payments system and protect Canadians' privacy."

Furthermore, the Task Force proposes the following legislation (p. 10):

"- Define a discrete payments industry and require payments service providers to become members.

- Create a new public oversight body for the payments industry.

- Encourage industry to create a broad-based, collaborative, self-governance organization including both providers and users to develop and implement strategy and standards for the payments industry.

- Reinvent the objects, governance, powers, business model and funding of the Canadian Payments Association (CPA)."

Having studied the report, the Canadian Minster of Finance has welcomed the recommendations of the Task Force.[7] For the moment it seems unclear, however, to what extent the proposals of the Task Force will be implemented. The Canadian government plans to establish a senior-level advisory committee made up of public and private sector stakeholders to discuss emerging payments system issues. Furthermore, Department of Finance officials will review, in close consultation with stakeholders, the application of the Code of Conduct for the Credit and Debit Card Industry in Canada to emerging mobile payment products. Finally, the Government will also review the governance framework for the payments sector, including the Canadian Payments Association.

Our Comment

"Modernization", "participation", "interoperability", "billions of dollars of efficiency gains" - to those readers that have followed closely what has been written about SEPA this must sound familiar. But judging from the European perspective, it is not easy achieve these goals. In particular, realising the efficiency gains is a hard act.

[7] Minister of Finance Welcomes Findings of the Task Force for the Payments System Review, March 23, 2012 (http://www.fin.gc.ca/n12/12-030-eng.asp).

Obviously, it is easier to modernize the payment system of a single country. Thus, Canadians may find it easier to reap the hoped for benefits. However, given that they also want participation and interoperability they may have a long and rocky road ahead of them.

What remains is the impression that payments are increasingly treated like an essential infrastructure. Wherever regulators studied the working of the payment system they came up with ideas like participation of stake holders, interoperability, etc.. Whatever participants in the payment system think of it – the payment industry is likely to be treated more and more like a public utility. Whether this is the right approach to foster innovation is at least questionable.

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