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1. SCF 2.1: A new version of the SEPA Cards Framework

In December 2010, the EPC Plenary approved version 2.1 of the SEPA Cards Framework (SCF).[1] The new version updates version 2.0 which was published in 2006. The update was necessary in order to take important developments such as the passing of the Payment Systems Directive and the formulation of the ECB's view of a SEPA for Cards into account. There are many changes but, on the whole, the framework has not changed much.

Where-ever necessary, the framework now refers to "banks and payment institutions" rather than only to banks.

It is explicitly stated that issuers will be allowed after 2010 to decline non chip based transactions and that issuers decide whether they want to accept magnetic stripe as fallback (SCF2.1, p.8).

The requirement for schemes to carry out a self-assessment exercise and to publish the result is included (SCF2.1, p.13).

As regards schemes' pricing principles, cross-subsidisations are explicitly ruled out (SCF2.1, p.14).

SCF scheme rules include a right of merchants to surcharge (SCF2.1, p.15).

Finally, there are a number of paragraphs defining SEPA rules for three-party systems (SCF2.1, p.15-16).

- Generally, the SCF also applies to three-party systems if they offer services, that fall into the scope of the SCF. However, three-party systems are exempted from a number of provisions. When defining the exemptions the SCF distinguishes between three-party systems with licensees and without licensees.

[1] http://www.europeanpaymentscouncil.eu/documents/Cards%20SCF%20006%2009%20v%202%201.pdf

- Schemes without licensees basically have to adhere only to the technical standards defined by the SCF.
- Schemes with licensees have to regard the principle of transparency, they have to offer SEPA wide licences,[2] they have to grant free processor choice and they have to adhere to technical standards defined by the EPC. They may, however, keep governance, managment and processing together and they may restrict authorisation, clearing and settlement to themselves.
- Finally, the EPC proposes that a National Central Bank or another “relevant regulatory body” could exempt smaller three-party systems from the requirement to comply with the SCF.[3]

Comment

The new version of the SCF does not come up with any surprises. As required by the PSD, the “payment institution” appears alongside of banks. Given earlier statements of the EPC or the ECB, the inclusion of three-party scheme also was to be expected. So, in a way, it is more interesting to note what has not changed and what has not been said explicitly.

First, the EPC sticks to its guns and does not follow the advice of the ECB to contemplate designing a European card scheme. The SCF remains a set of high-level rules supplemented by a few more concrete security and standardisation provisions.

Second, the EPC does not say a word about a potential role of SDD for card clearing, which is a straightforward consequence of the above.

Third, the EPC does not want to become a regulator in its own right. It sees its task in formulating rules and monitoring them. Thus, in the end it is the responsibility of individual institutions to comply with SEPA (and other) rules.

*Fourth, the EPC maintains that application choice should reside on the issuing side of the market. The EPC states: “*cardholders will have through their cardholder agreement with their card issuer the choice of which payment application they will use provided the merchant accepts it and its POS equipment supports it. The agreement between the cardholder and the issuer will define the choices available to the cardholder*” (SCF 2.1, p. 17). This is not in*

[2] Existing exclusive national licences must be transformed into SEPA licences by end 2013.
[3] This is an interesting concept: The EPC as a private body defines rules as part of self-regulation and the ECB, a public body, can exempt institutions from the requirement to comply with these rules.

line with the wording in the ECB's Terms of Reference where it is stated: "cardholders and merchants will have the choice of which payment application they will use"[4].

Fifth, at least for us as outsiders, it still remains not entirely clear what it implies for a card or a transactions to be „in scope" or „out of scope". Clearly, when it is said that non-Euro transactions do not fall under the SCF " (SCF 2.1, p. 7), this simply means that SCF rules do not have to be applied. It seems reasonable to think that issuing members will nonetheless be allowed to issue cards that may be used for non-Euro transactions and also that SCF compliant cards may be capable of handling transactions in EUROs as well as in other currencies. Obviously, non-EURO-transactions regularly are covered by payment schemes' rules with no effect on the SCF-compliance of the scheme. So „out of scope" with regard to the currency of a transaction means that SCF rules do not have to be applied to this particular sort of transactions.

*But what about non-guaranteed payments? The SCF (2.1. p. 7) states "*For removal of any doubt, the Framework is founded on the reality that card-present card transactions are guaranteed transactions, i.e. the payment is guaranteed to the merchant's acquirer according to the relevant scheme's terms and conditions. Such card payments are distinct from direct debit transactions, which are not guaranteed and are outside the scope of this Framework.*"*

But there are cards in the market that can be used for direct debit payments (without formal consent of the issuer - so called „ELV" in Germany and Austria). According to the above condition, these transactions would be out of scope. But what does this mean? Does it force issuers to prevent this use of SCF-compliant cards for „out of scope"-payments? Or, does it mean, that the ELV transactions and other non-guaranteed transactions are „out of scope" in the sense that banks may issue such cards and do not need to observe SCF principles? The latter interpretation would give the opportunity to keep a national ELV-like scheme alive whereas the former interpretation would rule out ELV. More general, by the logic applied to non-Euro transactions, „out of scope" for non guaranteed transactions would imply that EPC members could issue SCF-compliant cards in schemes which relevant rules allow for non-guaranteed payments and that SCF-rules would simply not have to be applied to these transactions.

This is an important topic, because the idea of unbundling of payment and guarantee has been put forward as one possible way to deal with the anti-trust problems of multi-lateral

[4] European Central Bank: Terms of Reference for the SEPA compliance of card schemes, 4 March 2009, p. 7. At the EPSM meeting 26 January 2009, Jean Allix made clear that DG Competition supports the ECB's view.

interchange fees.[5] *PayFair, the new European scheme, wants to implement a choice between guaranteed and non-guaranteed payment (see our December 2009 newsletter). Also other new scheme builders do have the option of non-guranteed card-present transactions in their blue-print concepts. The ECB, however seems to support an „guaranteed-only“ approach. In a recent speech, Gertrude Tumpel-Gugerell (Member of the Executive Board of the ECB) stated that* "In essence, for SEPA for Cards to become a success, card payments need to be positioned as a real alternative to cash: efficient, fast and guaranteed."[6] *Thus, there seems to be a tension between, anti-trust requirements (and ideas in the market how to fulfil these) on the one hand, and security concerns on the other hand – with the EPC somewhere between the ECB and DG Competition. We are curious what the outcome will be. For the moment, Gerard Hartsink has already announced that there will be a version 3.0 of the SCF in 2010. Perhaps that will provide some further guidance on the topic of guaranteed versus non-guaranteed payments. A revised version 3 would be highly welcome because SCF 2.1still contains many points that are open for interpretation.*

2. Atos, SIA-SSB and the meaning of SEPA

SIA-SSB, an Italian payment processor has been put up for sale in 2008. The bidding process has been protracted and the advent of the financial crisis has further slowed down things. However, in the end of 2009 Atos Origin seemed to be the front runner in the group of bidders. According to press reports the Banca d'Italia has vetoed the deal on the grounds that SIA-SBB as provider of vital payment ionfrastructure should not fall into foreign hands.[7]

Comment:

Reading the news about the blocking of the Atos-SIA-SSB deal one cannot help scratching one's head. Did not "SEPA" stand for "Single Euro Payments Area"? Had not central banks joined the EU Commission pressuring banks and PSPs day and night to move forward on the road to SEPA? Has it not been explained to us, time and again, that within SEPA borders

[5] See „An extra charge for the payment guarantee?“ in our November 2009 newsletter and Peter Jones: The tourist test: time for change?, in: Payments Cards and Mobile Sept./Oct. 2009.
[6] The Progress of Migration to SEPA, 7th Annual Payments Conference, British Bankers' Association, London, 23 November 2009. http://www.ecb.int/press/key/date/2009/html/sp091123.en.html
[7] See: All change at the processors, Cards International, 9 December 2009, p. 1 or: Colpo di scena: SIA-SSB non si vende. Bankitalia: è troppo strategica, http://www.cwi.it/notizia/19241/2009-11-05/Colpo-di-scena-SIA-SSB-non-si-vende-Bankitalia-e-troppo-strategica.html

should not have any significance with respect to payments? Payment processors are one of the groups that have been most vigurously moved towards SEPA: opening up of ownership, mergers and acquisitions in large numbers have taken place already. All players are driven by the perception that size is essential for success or even mere survival in a large payment area as SEPA. Indeed, SIA-SSB itself has been active in x-border acquisitions – buying GBC, a Hungarian processor, in 2007. while the SIA-SSB sales' process drags on the market environment keeps evolving. At the end of November 2009, two heavy weights have announced that they are planning a merger: Equens (itself the outcome of a number of mergers) and Cedicam (Crédit Agricole's payments subsidiary).[8] So while consolidation preceeds in the rest of Europe (unless regulators also block this deal) SIA-SSB remains in the uneasy position of a bride without bridegroom.

If the news should be correct that the Banca d'Italia has indeed blocked the deal, the credibility of European regulators would be damaged. Banks and others have invested heavily in SEPA – not always completely voluntarily. And now they find that one of the very regulators that pushed them forward is blocking the road. It will be interesting to see how the European Commission, the ECB and the other central banks with in the ESCB (European System of Central Banks) will react.

3. The "market road" to SEPA: A small example

In late 2009 Postbank and Deutsche Bank announced that Postbank customers would be able to use ATMs of Deutsche Bank in other countries (Spain, Italy, Portugal Poland, China, India) without a charge.[9] Just a few days later, in early 2010, Santander announced that its UK customer will be able to withdraw cash for free from its Spanish ATMs.

Our comment:

For a long time, retail banking was strictly a national business. There were few cross-border merges and acquisitions and even if a bank manged to buy a foreign retail bank it usually ran the foreign part as a distinct entity. So, even if brands crossed border, as for instance the

[8] See Press release. http://nl.sitestat.com/interpay/equens/s?en.pdf.press_release_cedicam_-_equens&ns_type=pdf&ns_url=http://www.equens.com/Images/press%20release%20CEDICAM%20-%20Equens.pdf

[9] In fact, for Deutsche Bank customers, this has been possible for quite some time. Deutsche Bank also has an agreement with 5 other international banks about the mutual free use of ATMs.

brand of Deutsche Bank, for retail customers this did not mean much. They were treated by the foreign subsidiary of their bank just like anyone else. This is changing. For one, it becomes easier to buy a foreign bank. Witness the course of events in Italy, for instance, where the Banca d'Italy used to oppose any attempt of foreign banks to buy an Italian bank. Thus, the Dutch Bank ABN Amro was able to buy Banca Antonveneta in 2005 only after the president of the Banca d'Italia had to resign. Overall, the common market and SEPA have made cross-border expansion easier. Second, banks with cross-border business increasingly try to position themselves as European player – rather than as a national player with some cross-border business. As the examples above show, this attitude now becomes more visible for retail customers. The "fee frontier" is no longer along national frontier but along company frontiers. Such an approach which might be called "integration by mergers and acquisitions", could also be envisaged with respect to payment systems. A case in point is the U.S. where regional payment networks have been integrating over the years. To some extend, this is also taking place in Europe. SEPA has opened access and slashed anti-competitive practises. But regulators do not seem to trust such a truely market driven process towards a Single European Payments Area. Therefore, in parallel, they follow an approach that has more in common with central planning: device products at a central level and then force people to use them.

4. Kroes' farewell gift for Visa

According to press reports, Nellie Kroes the outgoing competition commissioner wants to make a decision in the Visa case before she hands over her portfolio to the new commissioner, Joaquín Almunia (Spain). If the press reports are correct, Visa will basically face the same ruling as MasterCard. Kroes is quoted as stating: "I will not allow Visa to benefit at the expense of MasterCard".[10]

[10] Kroes to clamp down on payment. See http://www.euractiv.com/en/financial-services/kroes-clamp-payment-cards/article-189260

Our comment

It has never been clear why Visa representatives thought that they might get a better deal than MasterCard. What ever hope there was, Nellie Kroes seems determined to crush it. This seems fair enough. After the controversial and protracted proceedings against MasterCard the EU Commission came out not only with a verdict but also with general ideas regarding the proper conduct of 4-party payment schemes. This point has also been stressed by commissioner Kroes who is reported saying that the fees and the methodology adopted by MasterCard could be used as a kind of benchmark for others in the sector.[11] *So, unless the European Court of Justice decides against the Commission or the new commissioner Joaquín Almunia changes course, the MasterCard decision (plus the subsequent agreement from April 2009) broadly define the rules of the game for the coming years.*

Should you have any questions or comments please contact

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[11] See footnote above.