



PAYSYS **REPORT**

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1. **SEPA for cards: rising from the dead**

Once again, European regulators are demanding European payment solutions at the POS. But the political vision remains blurred. Regulators are not against international schemes but they want European solutions that can be used SEPA-wide. At the same time, they do not seem to want to touch national schemes which are often seen as particularly efficient. So, there are ideas of interlinking or interconnecting national schemes or even building a European scheme. Much emphasis is given to the potential of SCT Inst to provide a basis for European payments at the POS.

SEPA for cards: rising from the dead

(mk) "SEPA for cards" – is it "2.0", "3.0" or something higher? It is difficult to keep track. But, currently, the topic is definitely alive and kicking. In the October 2018 edition of this newsletter, we commented on a speech given by the ECB's Yves Mersch which put "SEPA for cards" back on the political agenda.¹ Meanwhile the topic has gathered momentum. The Eurosystem has extensively commented on SEPA for cards² and many central bankers have taken up the issue.³

The Eurosystem's report on "Card payments in Europe" contains some well-known facts:

- SEPA for cards has not been achieved.
- There is a lack of interoperability.
- Often players are promoting proprietary standards.
- National cards schemes are relatively low-cost.
- Pan-European acceptance is reliant on co-badging
- Attempts to create a European card scheme have failed.

However, there are some new elements. In particular, the implementation of Target Instant Payment Settlement (TIPS) is seen as a possible game changer.

"The use of this newly installed instant payments infrastructure could be a way to support the interlinking and interoperability of national card schemes and, if full pan-European coverage is ensured, would provide a possible alternative to establishing a European card scheme. To promote the use of such cards, it would be helpful to have a common European logo indicating the possibility of using the cards of national card schemes at EU level." (Card payments in Europe, p. 3).

The Eurosystem discusses three options that might advance SEPA for cards:

- interlinking of national schemes,
- a SEPA scheme and
- interconnection of national schemes.

A fourth option, co-badging among national card schemes, is ruled out as not workable. But as far as the other options are concerned, the Eurosystem wants to leave it to the market.

Subsequently, the Eurosystem describes current standardisation efforts in which a plethora of industry bodies is involved. For the moment, the Eurosystem sees its main role in monitoring and supporting such activities.

However, recent speeches of regulators also show that they want to see results. With respect to important areas of the payment market, inter alia the card market, the ECB's Yves Mersch said in February 2019: *"I look forward to proactive cooperation with the payment industry in these areas, based on joint standardisation and harmonisation."*⁴ The Bundesbank's Burkhard Balz has the same message, only expressed somewhat more directly: *"It must not happen – as frequently in the past – that discussions finally yield no results. There must be concrete actions. Quick results are necessary."*⁵ (Our translation.)

Our Comment:

There was a time when SEPA for Cards received a lot of attention by the authorities. Pushed by regulators, the European Payments Council (EPC) developed a SEPA Cards Framework (SCF) and the card industry pledged support for this idea. Finally, complete success was announced. Based on self-assessments, the industry declared itself SCF-compliant.⁶ Although this implied that, in many countries, domestic schemes continued to operate more or less than before, regulators did not complain. The topic of “European Card Scheme” somehow slipped off the agenda. But now the topic is back on the agenda, as the reports quoted above are demonstrating.

The Eurosystem’s report shows that a lot is going on at the moment and it has a message: more needs to be done. As far as current activities are concerned, the reader of the Eurosystem’s report has to handle many acronyms: ECPC (European Card Payment Cooperation), ECSG (European Cards Stakeholder Group), ECPA (European Card Payments Association), ERPB (Euro Retail Payments Board), ECPI (European Card Payment Interconnection). Did we forget anything?

Why not sell Cartes Bancaires acceptance in Germany, PagoBancomat in France and so on?

But what is the essence of the report? Going through it provides a kind of déjà vu. The report stresses that there are schemes that cover all of Europe, the large international schemes Mastercard and Visa. The Eurosystem sees nothing wrong with this but would like a European scheme. It has all kinds of suggestions but in the end it concludes that “SEPA for cards is market

driven” (p. 34). That sounds familiar. We have been there before. SEPA schemes were pressured to become SEPA compliant. Schemes adjusted their rules and some of the technology and then self-certified themselves as just that, “SEPA compliant”. All attempts to build a European scheme were unsuccessful.

The Status Quo



The Future?⁷



The Future with a Common Logo



Figure 1: SEPA for Cards via interoperability at the POS

But the Eurosystem also discusses some options for the road towards SEPA for cards. One way is technical interoperability on the acquiring side. This is what NEXO Standards (<https://www.nexo-standards.org>) tries to achieve. If terminals can cope not just with the domestic scheme and the international schemes but also with other European domestic schemes, acquirers can do the job. In the past decade, they have been successfully selling UnionPay, JCB, Discover and oth-

Interoperability on the acquiring side would still leave separate infrastructures for each domestic scheme in place.

The Eurosystem sees TIPS as a potential facilitator towards interconnected European card schemes.

ers to merchants. So why not sell Cartes Bancaires acceptance in Germany, PagoBancomat in France and so on?

Accepting one additional brand is not all that much of a hassle for a merchant, in particular when it means only another tick in the acquiring contract. However, as the number of logos increases that have to be displayed at the POS, space might be a problem and card holders might easily be confused. Thus, there is a case of having a common logo.

Underneath, there would still be the national schemes. If, for instance, a French CB card is used in Italy, it would be a CB transaction. Once technical hurdles have been overcome, such a solution would probably be easy to implement. Only the integration of the German girocard would be more challenging because it does not adhere to the standard 4-party model.

While relatively easy to implement, interoperability on the acquiring side would still leave separate infrastructures for each domestic scheme in place. Thus economies of scale would not be fully exploited. One step further would be a common infrastructure with common rules. The Berlin Group has been working in this direction for many years. It aims at creating a common clearing & settlement (C&S), based on SEPA Direct Debit (SDD) adjusted for card payments. While this idea is still "in the cards", another idea has gained momentum: using TIPS to clear and settle European card transactions.

This concept is currently being promoted by ECPA (European Card Payment Association) under the name ECPI (European Card Payment Interconnection). The Eurosystem sees TIPS as a potential facilitator towards interconnected European card schemes. But the idea of using TIPS remains vague. National schemes are assumed to persist but there also should be a "separate legal entity responsible for managing the scheme's rules".⁸ So, there would be national schemes and a European scheme for cross-border transac-

tions?⁹

Standardisation of C&S coupled with a plethora of interoperability provisions seems to be a bit of a half-way house between interoperability on the acquiring side and the establishment of a proper European scheme. If there is standardisation on the technology side and if there is a common C&S mechanism plus separate legal identity to manage interoperability, why not move to a common scheme? In the long term, the ECPI project could be the nucleus of a real European card scheme.

Without interchange fees it is difficult to see a business case for issuers

Should European banks really move closer towards a common scheme, one important issue would necessarily pop up: multilateral interchange fees. Setting up a common European card scheme would be greatly facilitated if the authorities allowed banks to set a common interchange fee.¹⁰ Without interchange fees it is difficult to see a business case for issuers. Card holders are unlikely to tolerate transaction fees. The case of Scandinavian P2P payment systems is a case in point.

So far, the politically intended vision of a European card scheme has proved unrealistic. All attempts have failed. Some expect that the POS payment instrument

“cards” have had their best time.

Forget cards and existing card-based infrastructure. Why not set up a new POS system as a greenfield solution based on instant credit transfers via smartphone? This is the great vision that is repeatedly shining through in connection with the new quest for a European system.

It is difficult to predict how such a shift from cards to instant payments would affect acquirers.

There are still no widespread solutions for instant POS-payments at the national level. A European patchwork could be avoided right from the start. The payment instrument used at the POS would again access the banks' current accounts directly (without intermediation through competing international systems such as Visa, Mastercard, Facebook, Google, Paypal, etc.). For the banks it would be an enticing

vision to regain the threatened dominance in payment transactions at the POS. However, the banks would have to abandon their national card systems, which continue to be successful.

This scenario is difficult to digest and therefore currently unrealistic. Card payments would be substituted by the payment instrument "credit transfers" and replaced in the longer term. However, without an interchange fee for credit transfers, the business case still stands on clay feet. It would have serious consequences for the acquiring industry. It is difficult to predict how such a shift would affect acquirers. Theoretically, it is conceivable that the system works without acquirers. But how well would a system function in which each merchant could simply self-acquire, be it Carrefour or a small games shop around the corner?

Although we are not in a position to make a proper judgement about the technical pros and cons of the various options, we would like to suggest that “faster” is not always “better”. As our EPCA partner, Peter Jones has repeatedly pointed out, real-time may have its drawbacks in terms of security, in particular security of the cardholder. This point can probably be extended. Whatever Europe comes up with, there still will be the international schemes which offer highly convenient products with a rich functionality. “Real time” may be a factor leading towards “plain vanilla” products. Batch processing provides processors with more time to carry out multiple processes.

There are two obvious ways towards SEPA for Cards that have not been discussed, at all: the mergers & acquisitions (M&A) path and expansion across region-

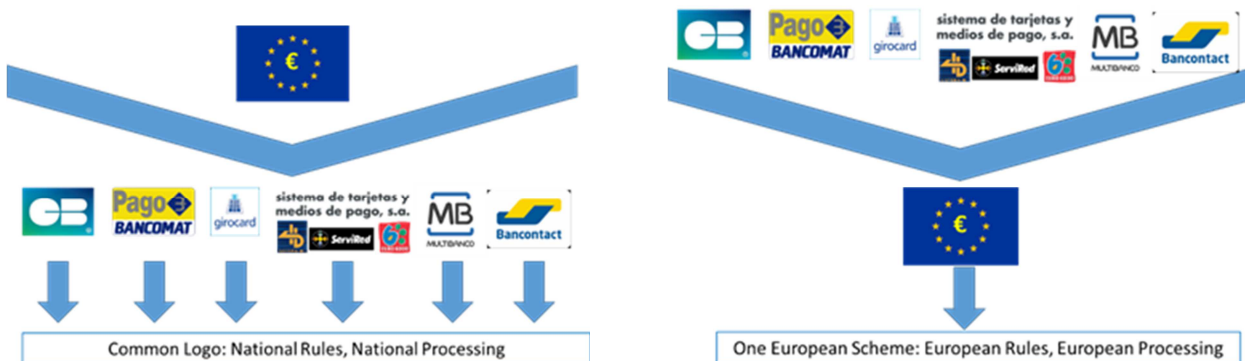


Figure 2 Common Logo or Common Scheme?

al/national borders. In a truly integrated economic area, one should expect M&A to happen. For instance, this was the case in the US where the PIN debit systems started out regionally dispersed and then integrated via M&A. Similarly, US PIN-debit systems extended their regional reach over time.

One might argue that in Europe things are different because domestic debit card schemes are run by national banking clubs. But that shows precisely, how far Europe is still away from full integration. Banking clubs are organised across national lines. We have European associations, say of the savings banks, but the German savings banks are in a boat with the other German banks and the Spanish savings banks are

currently integrating their card scheme with the two other Spanish schemes. So, before pushing banks and PSPs into European solutions, regulators might ponder the question what inhibits organic integration of European card payments.

Appendix

	ECPI-Initiative (ECPA)	Instant Payment Vision
Main characteristics	interoperability of domestic card schemes	new POS-payment scheme beside cash and cards
Payment device	card or mobile	mobile
Legal payment instrument	card-based	credit transfer
European-wide acceptance logo	additional logo is considered	unified acceptance logo would be useful
Scheme relevance	Additional scheme regarding cross-border clearing & settlement	System is based on SCT-scheme; new scheme is obsolete
Clearing & Settlement	based on SCT Inst	
Interchange	yes	no
Acquirer	traditional role	superfluous?

Blueprints of a European POS payment scheme

Notes

- 1 "Donald Trump – Father of the European Card Scheme?", Issue 7/2018.
- 2 See European Central Bank: Card payments in Europe. Current landscape and future prospects: a Eurosystem perspective, April 2019.
https://www.ecb.europa.eu/pub/pubbydate/2019/html/ecb.cardpaymentsineu_currentlandscapeandfutureprospects201904~30d4de2fc4.en.html#toc1
- 3 See, for instance, Burkhard Balz, Der Zahlungsverkehr der Zukunft – wohin bewegen sich Deutschland und Europa?, SAFE Policy Lecture, Goethe-Universität Frankfurt, 07.02.2019. <https://www.bundesbank.de/de/presse/reden/der-zahlungsverkehr-der-zukunft-wohin-bewegen-sich-deutschland-und-europa--776224>
- 4 "Promoting innovation and integration in retail payments to achieve tangible benefits for people and businesses." Speech by Yves Mersch, Member of the Executive Board of the ECB, at the American European Community Association, Brussels, 7 February 2019.
- 5 Burkhard Balz, Der Zahlungsverkehr der Zukunft – wohin bewegen sich Deutschland und Europa?, SAFE Policy Lecture, Goethe-Universität Frankfurt, 07.02.2019.
- 6 Repeatedly, SEPA for Cards has been a topic in this newsletter. See, for instance, "SEPA-compliant or SCF-compliant: to be or not to be?", in the March 2013 edition. The EPC saw SCF as a "remarkable success". See "EPC Blog: The SEPA Cards Framework Bows Out After Ten Years of Good and Faithful Service," 17 November 2015.
- 7 Recently, the three Spanish schemes have merged. But they do not seem to have a common logo, yet.
- 8 Card payments in Europe, p. 13.
- 9 Such parallel existence of national and European schemes also appears in the speech of the Bundesbank's Burkhard Balz (cited above). He proposes a common logo for the national schemes and a "European brand" for those countries without national schemes. But he leaves it open whether the European brand would cover card payments or rather a mobile P2P system.
- 10 Unlike ordinary cartel prices that are meant to prevent prices from falling below a certain level, multilateral interchange fees set a ceiling to prices. Therefore, they must not be compared with ordinary cartel prices. See Malte Krueger: Multilateral interchange fees: Don't throw the baby out with the bathwater, Journal of Payments Strategy & Systems, Volume 13, Number 2 (forthcoming).

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