

# Sándor Dávid: The Single Euro Payments Area

*The objective of the pan-European regulatory and self-regulatory work related to the creation of the Single Euro Payments Area (SEPA) is to improve the efficiency of low-value payments (i.e. retail payments) by establishing a common legal framework and the application of standards. Among the elements of the SEPA project, our focus will be on schemes, in particular the SEPA Credit Transfer Scheme (SCT) already essentially implemented in the EU and Hungary, which we will discuss in detail,<sup>1</sup> stressing the fact that SEPA is not a concrete payments system, but rather a set of procedural and legal rules regulating payment methods, in addition to the entire infrastructure supporting the clearing and settlement of transactions. In the longer term, the broad implementation of the schemes can potentially lead to a substantial reduction in costs for banks, which may ultimately be passed on to customers. We will present the practical experience gained in connection with the Credit Transfer Scheme, in light of the information compiled in the course of the central bank's informative meetings conducted at the affected Hungarian banks.<sup>2</sup> Currently, 12 banks now apply the Credit Transfer Scheme in Hungary. Due to the lack of a domestic euro infrastructure, domestic euro payments are carried out through international channels. Consequently, a much larger portion of euro transfers made by Hungarian banks have already shifted to the new SEPA format than what has been characteristic of retail payments within the euro area thus far. This phenomenon stems from the fact that initially, the SEPA Credit Transfer Scheme offered a competitive alternative most simply from the perspective of cross-border transaction fees.*

## INTRODUCTION

The acronym SEPA is used in the payments industry to refer to several notions:

- On the one hand, the term SEPA represents the vision, the targeted state for the euro area in 2010, and over the longer term, the entire European Union when users of payment services no longer experience any difference between the basic payments services provided by any service provider within the territory of the European Union.<sup>3</sup>
- On the other hand, the term SEPA also refers to a geographical concept, comprising all the countries within the SEPA area (the 27 EU member states, as well as Iceland, Norway, Lichtenstein and Switzerland).
- Thirdly, the expression SEPA is most frequently used within the professional vernacular to indicate the self-organisation coordinated by the European Payments Council (EPC,<sup>4</sup> henceforth: Council), the pan-European SEPA project in a narrower sense, striving to promote the realisation of the SEPA vision by introducing (creating

and propagating) standard payment schemes and frameworks.

Regarding the interpretation of SEPA, it is important to stress that SEPA is not a payments system: one of the fundamental elements of even its narrowest definition is that SEPA is not restricted to being a payments system or mechanism.

## THE CONDITIONS, REASON AND OBJECTIVE BEHIND THE CREATION OF THE SEPA PROJECT

The introduction of the single currency, the euro, did not lead to the automatic unification of the entire volume of payments and clearing, contrary to regulators' expectations. While this change has taken place in the domain of large-value payments as the fruit of cooperation between the ECB and the central banks, in the domain of low-value (i.e. retail payments), it has not. The fragmentation of the market among nations and the diverging national legal frameworks regulating payments have remained unchanged. Varying national payment customs have been upheld, financial institutions have not modified their payment services

<sup>1</sup> For readers who are interested in further detail on the subject, a separate publication will soon be available on the MNB website under a similar title.

<sup>2</sup> We would like to express our gratitude to the banks which provided indispensable data and other information for this article: OTP, K&H, WestLB, ING, BB, Deutsche Bank, Commerzbank, KDB, CITI, Erstebank, and Unicredit.

<sup>3</sup> The terms 'euro' and 'European' are easily exchangeable in the SEPA acronym. This error is not a grave one, as the Single European Payments Area is also a fitting expression, expressing the harmonisation of payment frameworks and rules within the European Union, and that companies will be able to provide payment services with identical conditions in any of the community's currencies on the entire territory of the EU.

<sup>4</sup> The European Payments Council is a professional association specialising in the domain of payments, established in 2002 by the major European banks and in charge of coordinating self-organisation. The SEPA payment methods are implemented under the auspices of the Council.

fulfilling the same function, but of varying standards and pricing. Substantial differences have remained in the fees and processing time of domestic payments and cross-border payments among participating states.

It is in reaction to this situation that European authorities came up with the vision for a Single Euro Payments Area (SEPA), a state in which bank customers will be able to perform euro transactions – credit transfers, direct debits and card payments – within the EU from the same bank account, and in which all euro payments within the EU, including cross-border payment transactions, will be no different from domestic payments.

Regarding the instruments for putting the SEPA vision into practice, a significant conceptual change has emerged in the attitude of authorities since the beginning of this millennium. The authorities initially believed that the simple enactment of regulations (Regulation [EC] No 2560/2001,<sup>5</sup> henceforth: Regulation) could create the process which would lead to the unification of the payments market and the standardisation of payment services. However, the Regulation did not generate the expected results, and the unification of bank fees and costs of cross-border payments only led to imbalances between them, as well as increased domestic fees in several cases, due to the fact that the required conditions – identical standards and an adequate infrastructure – were not in place.

This effect could only be countered if cross-border payments and their most important components – processing, clearing and settlement – were reorganised by making them as inexpensive as domestic payments. In order to achieve this, authorities and service providers had to recognise the fact that fees can only be reduced if service production and unit costs are significantly lowered. In other words, banks and infrastructure providers had to first make investments, allowing innovations to emerge which would allow production costs of services to be reduced, and had to strive to find solutions which fully exploit economies of scale and network effects. It was therefore evident that standardised payment services and models had to be created and implemented. Regarding common payment schemes, it must be mentioned that the cost of their development and introduction will primarily be borne by the European banking community and providers of clearing and settlement services, while their benefits will be reaped by the users of payments services. A study commissioned by the European Commission<sup>6</sup> analysed the social costs and benefits of the SEPA project, broken down according to the main

stakeholder groups for the period 2006-2012. Besides the beneficial reduction of fees for customers, the analysis also takes into account the value of necessary investments and operation costs. The analysis examines four scenarios from the perspective of the pace of migration, made up of the combination of the two possible demand side and the two possible supply side SEPA strategies.

Based on the cost-benefit calculation, the study established that a rapid, broad shift from the credit transfer and direct debit methods currently in use to SEPA schemes at the pan-European level could lead to savings of EUR 123 billion in the period 2006-2012. This amount could increase by EUR 238 billion if the use of SEPA schemes is implemented not only in the inter-bank, but also in the entire customer-to-customer payment chain. At the same time, if migration happens slowly and fails to reach the critical volume by 2012 at the latest, a loss of up to EUR 43 billion may ensue on a social level.

According to regulators, the legal framework they have created complements self-regulation well, as the development of services and products which adhere to regulations and are based on customer knowledge and relations can be most effectively done by the banks themselves. The development of payments, however, is not a short-term process, and thus requires the long-term, coordinated cooperation of the banking community and other institutions. Therefore, in order for this process – which requires substantial investment by banks – to begin and to yield results over the short term, regulatory cooperation and even political pressure were needed.

The main mechanism for implementing SEPA is therefore self-organisation by banks, a catalyser and instrument of pressure supported by authorities, instead of the enactment of regulations. This self-organisation is the SEPA project taken in the narrower sense, striving to achieve the aforementioned vision in this manner.

The organisational frameworks required for bank cooperation were established by the EU's banking community in the form of the Council. The Council elaborated the SEPA project and its components with the involvement of customers and various service providers, including a single set of pan-European payment instruments – SEPA Credit Transfer and Direct Debit Schemes, card payments, clearing and settlement mechanisms to be employed and the framework regulations for cash handling. In the domain of

<sup>5</sup> Regulation (EC) No 2560/2001 sets forth the equality of fees applying to euro transfers within and between participating states, meaning that fees applying to cross-border payments cannot be higher than the fees applying to the same domestic payments.

<sup>6</sup> Caggemini analysis (2007): 'SEPA: potential benefits at stake' (Researching the impact of SEPA on the payments market and its stakeholders).

legal regulation, the authorities have elaborated general EU-level framework regulations applying to payment services which strongly support integration. Accordingly, the European Parliament and the European Council issued Directive 2007/64/EC on payment services in the internal market (Payment Services Directive – PSD) at the end of 2007, which clearly aims to lay down the legal frameworks for the EU’s single payments.

**STAKEHOLDERS OF THE SEPA PROJECT**

Those affected by the project can be classified into three main groups. Regulators and the Council, the latter representing self-regulation, responsible for elaborating SEPA’s set of instruments, thereby creating the opportunity for single payment services. Banks and the infrastructures supporting clearing and settlement tasks, ensuring the supply side of payment services which are based on the SEPA schemes and framework rules – credit transfer, direct debit and card payments. Finally, the end-users of services, comprising private individuals, companies, merchants and institutions affected by payments, as consumers representing the demand side. In order to reap the benefits offered by SEPA, substantial adaptation – as well as investment – is required, in particular from service providers, as well as consumers.

**COMPONENTS OF THE SEPA VISION AND THE SEPA PROJECT**

The creation of SEPA is currently founded on three main mechanisms. The first is the common, broad legal framework which is compulsory for all and is contained in the Payment Services Directive (PSD) with the aim of harmonising the legal framework for payments in all participating states. The second element is the set of high-level requirements expected from the banking community,

formulated by the authorities, which form a certain requirement of principle and deadlines for cooperation between banks. The third is the SEPA project taken in the narrower sense, coordinated by the Council, of which the main achievement has been the elaboration and management of SEPA payment schemes and standards.

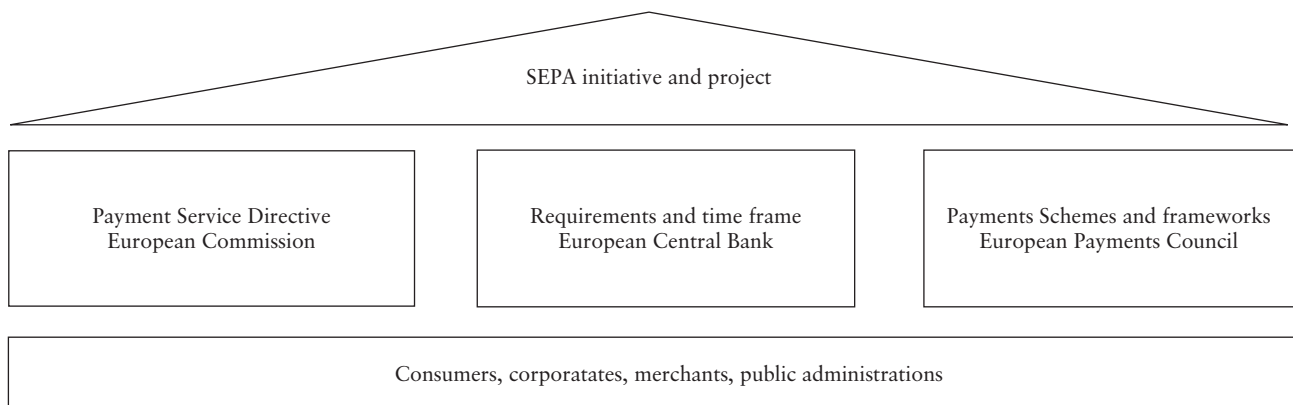
The Directive establishes general, common legal frameworks for every participating state and currency, in other words not just for the euro area and the euro. The rules set forth by it must be applied to payment products and services accepted in existing national payments, in other words not only payments taking place within the SEPA scheme. Regarding the relation between the Directive and SEPA, it is clear that the Directive applies to a much wider range of operations, rather than just transactions executed through the SEPA schemes. Taken the other way around, the Council had to elaborate SEPA schemes so that they would comply with the rules applying to payment operations set forth by the Directive. Neither the Directive nor the Regulation contain concrete provisions on transaction fees, or on the level or value thereof. They only contain compulsory principles on the mode of defrayment fees, and their division between the originator and the beneficiary. In other words, fees will continue to form the subject of agreement between the service provider and the customer, and as such, continue to stimulate competition between service providers.

Consequently, the fees applying to SEPA payments will lead to a reduction in fees as a result of stronger competition among service providers targeted by the Directive, via the innovation which they will seek to reduce their costs, instead of price regulation.

It is the Eurosystem’s duty to assist the payments system’s smooth operation, thereby contributing to the maintenance of financial stability. Accordingly, it supports the SEPA

**Chart 1**

**Components of the SEPA initiative and channels of implementation**



project in order to assist the implementation of SEPA. It offers guidance to infrastructure providers in the execution of the SEPA project and cooperates with public sector institutions affected by payments to enable them to use SEPA products as soon as possible.

The Council, a self-regulating professional organisation, is responsible not only for creating new payment schemes and frameworks, but also for introducing them by 2010, as well as managing, controlling and monitoring the process. In other words, the Council is responsible for the SEPA project's elaboration and implementation.

The components of the SEPA project in the narrower sense are:

- single payment instruments based on the euro; credit transfer and direct debit schemes, as well as the frameworks for card payments and clearing and settlement mechanisms,
- common technical standards,
- common business models,
- common legal foundations and contractual frameworks,
- efficient, competing clearing and settlement infrastructures capable of handling the common schemes,
- competing services capable of satisfying consumer expectations, continuously improved and developed in the future.

## METHODS FOLLOWED IN THE COURSE OF DEVELOPING SEPA'S PAYMENTS INSTRUMENTS

The development of schemes and frameworks took place based on two different methods. For the schemes, a replacement strategy was employed, while for the frameworks, an adaptation strategy of existing systems. The rules and standards devised for the schemes were compiled in Rulebooks (RB).

In essence, schemes are a set of rules applying to the execution of a specific payment method (e.g. credit transfer), regulating the major orders of procedure, data content and data format.

Three layers of activity can be distinguished within the scheme.

The first layer represents the relation between banks and their customers. Banks now have the opportunity to offer their products and services in a context of ample competition. Banks can compete for customers with an array of products and services based on the scheme. In the area of basic services, they can compete in prices and the level of service, while optional value-added products leave even more room for competition.

On the second layer, the replacement strategy transpires in the inter-bank area, and represents the introduction of common procedures and standards which completely substitute the procedures and standards used in given countries, regions or customer groups. These elements are underpinned by supporting and processing infrastructure – separate from the payment scheme – which serves for the processing, clearing and settlement of transactions (Clearing and Settlement Mechanism,<sup>7</sup> or CSM). Rules applying to the schemes and infrastructure are also elaborated, in the sense that the scheme's general rules (e.g. applying to data formats) must also be adhered to by them (e.g. a clearing house cannot change the compulsory data content in the course of processing if it wants to participate in carrying out transactions according to the SEPA schemes). At the same time, one of the fundamental principles when elaborating SEPA schemes was the separation of the scheme and the infrastructure, to allow any infrastructure to be able to adapt to the requirements; in other words, enabling payments based on the scheme to be performed through any clearing and settlement mechanism. The scope of necessary data and the standards applied were compiled in Rulebooks. Regarding specific message standards, the Council decided that the UNIFI (ISO 20022) XML message standards would be applied in inter-bank message traffic. It also recommends them for bank-customer relations. The International Bank Account Number (IBAN) and the Bank Identifier Code (BIC) form an integral part of the message.

The third layer is the level of infrastructure, where the schemes – i.e. the rules applying to the various payment methods – were separated from the infrastructures, i.e. the infrastructure providers offering clearing and settlement services to payment service providers. A further objective at this level is to enable interoperability between the various infrastructures within the euro area, allowing all euro payment orders to be executed within any infrastructure,

<sup>7</sup>The terms Clearing and Settlement Mechanism, CSM, Clearing and Settlement Infrastructure, or simply infrastructure are used as synonyms in the article.

regardless of the location of the originator's or the beneficiary bank account or bank within the euro area.

In the following section, only the schemes, and more specifically the SEPA Credit Transfer Scheme, will be examined due to the limitations on the length of this article, as the Direct Debit Scheme will only be initiated from November 2009.

### THE SEPA CREDIT TRANSFER SCHEME (SCT)

The SEPA Credit Transfer Scheme is a payment method which defines a common set of rules and procedures for euro-denominated credit transfers – single, bulk and/or one-off or recurring. It includes a common level and timeframe of service, to which the financial institutions participating in the scheme must adhere to a minimum extent when carrying out transfers. Participants of the scheme are banks and payment service providers which have committed to adhering to the scheme's rules by signing the multilateral contract with the Council. Participants can choose between performing the procedures of the scheme themselves, and partially or entirely delegating them to a third party.

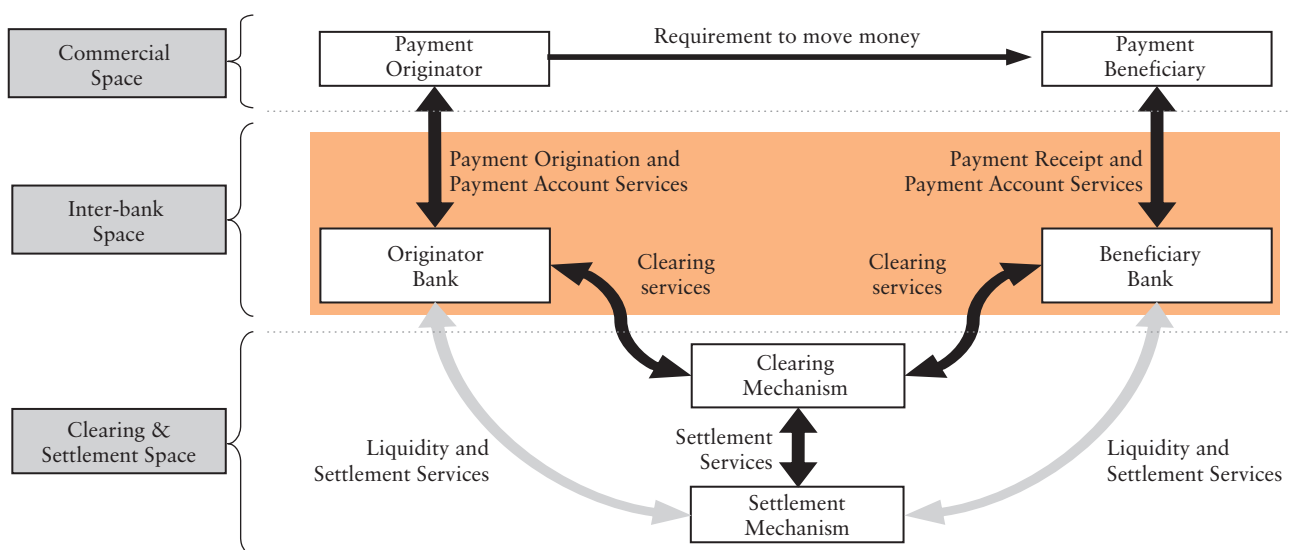
Payment is initiated by the originator in the course of the credit transfer. At the originator's order, the originator bank forwards the payment order to the beneficiary bank via other payment institutions and the infrastructure involved in the intermediation (Chart 2).

Main characteristics of the SCT:

- All customers can use it within the SEPA territory, and can reach all beneficiaries – and their bank accounts – located within this territory.
- The full original amount must be credited to the beneficiary's account, in other words neither the originator bank nor the beneficiary bank may deduct a transaction fee from the amount of the transfer. Banks may only deduct fees from their own customers – the initiator bank from the originator, the receiving bank from the beneficiary – cleared independently from the transaction. These fees are determined based on the agreement between the bank and its customer.
- No limit on the amount of the credit transfer is determined by the scheme. There is only a technical limit of EUR 999,999,999.99 on the amount of the credit transfer.
- Execution of the credit transfer (from the order of the originator to crediting on the recipient's account) must take place within three banking business days.
- The scheme and processing of payments are separate; in other words any financial service provider which has joined the SCT scheme can clear its credit transfers within SEPA through any infrastructure capable of handling SEPA credit transfers to which the partner bank in the given transaction has been connected.

Chart 2

#### Actors and process of SEPA credit transfers in the three-layer model



- Use of IBAN (International Bank Account Number) and BIC (Bank Identifier Code) are compulsory. As the nationally used bank account and identifiers vary, they have been changed to unified codes in the scheme.
- Comprehensive rules apply to the rejection and return of credit transfers (this is necessary, for example, in the event that the beneficiary's bank account number is provided incorrectly or the infrastructure rejects the order).
- The UNIFI (ISO20022) XML standard is used as the message standard, considering the advantages stemming from its already widespread use.
- The XML standard is suitable for transmitting remittance information needed for identifying the transaction for the parties, contained in 140 characters (called the comment section in Hungary).
- The scheme enables banks providing the transfer service directly or indirectly, i.e. via an intermediary – a direct participant of the scheme – to join.

## SEPA SCHEMES AND HUNGARY

### Hungarian aspects and expectations from Hungary

Hungary is not yet a participant of the Eurosystem, but it is one of the 27 EU member states. In case of Hungary, EU membership means that it has made a commitment to introduce the euro as soon as it becomes possible from the perspective of economic policy. As described above, the introduction and use of SEPA schemes is not a legal requirement for stakeholders, even in the euro area. Their motivation is rather based on expectations from the authorities, as well as the self-organisation of their own industry and the long-term benefits offered by SEPA. Although there is also an expectation from SEPA countries not yet having introduced the euro (more specifically their payment actors), this is obviously less concrete than from their euro area counterparts. It can therefore be stated that there are no strict legal or other requirements applying to stakeholders in euro payments in Hungary formulated by the authorities regarding rapid migration. i.e. the implementation and use of SEPA schemes. Nevertheless, Hungarian stakeholders are in a similar position as the main

actors and other stakeholders of the euro area regarding the final state aimed for, as the future introduction of the euro will most likely demand that Hungary integrate itself into the euro area's payments in a state founded fully on SEPA payment schemes, according to the Council's current plans. As a result, it is the fundamental interest of Hungarian stakeholders to create and maintain SEPA compatibility, and furthermore to continuously follow and also contribute to new deliberations on SEPA.<sup>8</sup>

The clearing and settlement of Hungary's domestic payments is based on the forint, although the law does not prohibit the settlement of domestic transactions in other currencies, such as in euro, if both parties come to an agreement. A significant portion of international – cross-border – payments of domestic (resident) customers is processed in euro. Hungarian banks therefore had to prepare their international relations for the actual use of the SEPA Credit Transfer Scheme by over 4,000 payment service providers located in the euro area as of 28 January 2008, the date when the SCT scheme went live. Therefore, as of this date, Hungarian financial institutions with a clientele potentially including beneficiaries of such credit transfers had to (it was advisable) be prepared, at least in case of in-coming, cross-border payments in the direction of Hungary.

In the following section, we will summarise the experiences which were compiled by central bank experts in the course of interviews with the payment executives and experts from Hungarian SEPA banks regarding the banks' membership, the infrastructure used, the products and services based on the SCT, related customer information and sales experience. We will furthermore present their answers regarding future plans related to SEPA, which reflect the possible implementation of new schemes and SEPA schemes in the domain of forint payments.

### Joining the SEPA Credit Transfer Scheme

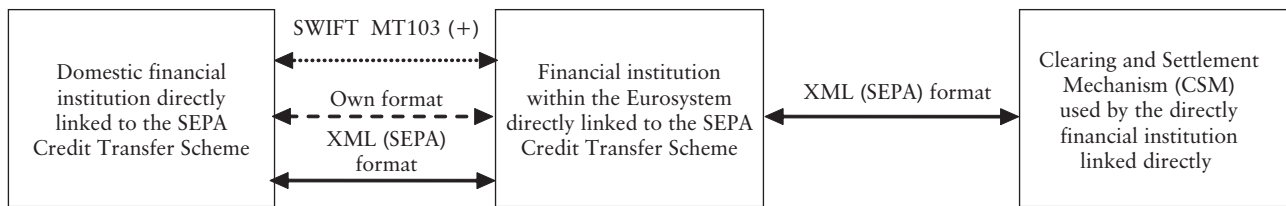
So far, 12 Hungarian financial institutions have joined the SEPA Credit Transfer Scheme. By voluntarily submitting joining documents,<sup>9</sup> all of the banks have undertaken a commitment to act as receiver banks at the disposal of their customers for SEPA credit transfers as of 28 January 2008, the date when the scheme went live, or subsequently, from the date of their membership. As sending banks, they will

<sup>8</sup> The first pillar of the SEPA initiative taken in the wider sense – the Directive – creates a general, common legal framework for all participating states and currencies, in other words, not only for members of the euro area and for the euro. Its rules must be applied by November 2009 at the latest regarding payment products and services accepted in the domain of existing national payments as well, and not only to payments carried out through SEPA schemes. This element of the SEPA initiative is therefore mandatory for Hungarian actors, regardless of the date of introduction of the euro.

<sup>9</sup> The NASO (National Adherence Support Organisation) provides support for the joining process in Hungary as well. This organisational unit, operating within the Hungarian SEPA Association, provides support for banks wishing to join in submitting the so-called adherence package to the Council in time and in due form.

## Chart 3

## Communication between banks connected indirectly, and those connected directly to the SCT



enable customers to initiate SEPA credit transfers by the end of 2008 at the latest, in accordance with the expectations of the European Council, the Commission and the ECB.<sup>10</sup>

All of the twelve Hungarian banks have in common the fact that they joined the scheme indirectly, rather than directly, either through their parent bank or through a correspondent bank.

In practice, this form of adherence means that Hungarian banks must transmit payment messages to correspondent banks participating directly in the SEPA Credit Transfer Scheme in the agreed data format, which is then transmitted from the correspondent bank to the recipient's correspondent bank in XML format. According to the SEPA Credit Transfer Scheme's rules applying to data standards, the rules affecting customers set forth in the scheme (such as settlement within 3 banking business days) must be adhered to by all members.

Hungarian banks usually use SWIFT (MT103 or MT103+) messages – generally used for this purpose – or the parent institution's own internal communication system to send and receive payment messages related to SEPA transactions. These are transformed or reverted to the data format prescribed by the XML standard by the correspondent bank (which is generally the parent bank), then forwarded to the suitable clearing and settlement infrastructure depending on the recipient, or received by it in case of incoming items.<sup>11</sup> However, several Hungarian banks already transform data into the XML format complying with the SCT scheme, and then forward the payment message in this form to their correspondent bank (Chart 3).

The clearing and settlement of credit transfers takes place with the help of the banks adhering directly to the scheme, through the service provider(s) operating the infrastructure selected by them. These are generally pan-European clearing

houses or SEPA-compliant, local or regional clearing houses. In some cases, the central units of large European multinational banks operate intra-group clearing and settlement mechanisms. Only messages in XML format may be exchanged between the banks adhering directly and the clearing and settlement infrastructures used by them when making SCT credit transfers.

Apart from the mandatory data standards and data content details, the execution structure of SEPA credit transfers sent and received by Hungarian banks does not differ much from that of 'simple' euro transfers used thus far. Several Hungarian banks mentioned that they were already in compliance with the customer-level requirements set forth by the SEPA Credit Transfer Scheme (such as settlement within 3 banking business days) in the field of simple euro transfers. For this reason, customers will not be able to perceive any real difference, even in transactions carried out according to the SEPA Credit Transfer Scheme.

### SEPA products and services

Over half of the twelve adhering Hungarian banks are already at the disposal of customers on both sides – as receiving and originating banks. By the end of 2008, all banks currently acting as 'receiving' banks only must comply with requirements applying to originating banks.

The banks involved and their parent banks have chosen different SEPA strategies based on their own judgement. As a result, Hungarian subsidiary banks have elaborated and adopted SEPA credit transfers among their range of products and services offered. It is important to stress once again that the SEPA Credit Transfer Scheme's Rulebook does not contain any expectations requiring products based on the SEPA scheme to be advertised as separate products to customers.

<sup>10</sup> At the time the SCT model was launched, the banks who were about to join – who had a low turnover compared with the rest of Europe – could simply declare that they will reorganise their originator capacity. The reason for this partial 'waiver' was to enable that the largest number of payments services providers to join the model as soon as possible, thereby helping to reach the critical mass of transactions necessary for an irreversible migration process.

<sup>11</sup> This may be a pan-European or national clearing house, clearing within the bank group, or even a further relation with a correspondent bank. The EBA STEP2 pan-European clearing house is used in most cases.

For this reason, the business conditions or list of conditions of some banks clearly name SEPA credit transfers among their foreign exchange and related account management services, while others do not make a distinction, and do not mention or name SEPA credit transfers as a separate product at all. Some banks have founded payment products on the SEPA scheme and advertise them separately, but call them a (brand)name of their choice rather than ‘SEPA credit transfers’.

Adhering banks which have not announced SEPA credit transfers as a separate product are free to decide whether or not they wish to execute transactions based on the scheme. Generally, this decision depends on the satisfaction of all conditions (such as whether a beneficiary holds an account at a bank adhering to the SEPA Credit Transfer Scheme, or whether a foreign customer has provided the BIC, in addition to the IBAN, etc.) required for execution according to the SEPA Credit Transfer Scheme.

### Informing customers

Several Hungarian banks have prepared informational material for the public on the introduction of new SEPA products, which provide adequately detailed information to customers. Informing customers generally takes place through bank notifications and statements, in which SEPA items are indicated separately.

### Fees

Fees related to SEPA credit transfers vary from one bank to the next, regardless of whether they have been announced in their terms and conditions or list of conditions. They are usually identical or lower than the transaction fees applying to general foreign exchange or non-SEPA euro transactions. This observation holds true for fees applying to both crediting and debiting accounts.

### Level of customer information

The banks interviewed unanimously agree that for the time being, customers are unfamiliar with the SEPA schemes (in particular credit transfer, currently). The majority have not heard about it, or do not perceive any difference between payments executed according to the scheme and other payments.<sup>12</sup>

Banks highlighted their experience related to the data content of SEPA credit transfers whereby the mandatory use of the

IBAN and BIC codes in the role of initiator – necessary to carry out SEPA credit transfers – was not a novelty to customers, as they have been in use in international transactions since 2002. The role and the necessity of these two codes are therefore familiar to customers.

### Hungarian SEPA credit transfer volume in the first half of 2008

There is still relatively little data on Hungarian and international SEPA credit transfer volumes. The estimates of participating banks, data compiled by the ECB from euro area member states and data pertaining to EBA STEP2 system are available to the MNB.

Based on the ECB’s data, the number of transactions complying with the SCT scheme in the months of April, May and June amounted to 0.4%, 0.6% and 0.9% respectively of the total volume of euro transfers of euro area banks. The estimates received from the 12 Hungarian banks suggest that this number is substantially higher in case of Hungarian banks, at approximately 10%-20%. The ECB’s estimate of the Hungarian volume is also available, reflecting the number of transactions performed through the EBA STEP2 payments system, most widely used for international credit transfers. Based on this estimate, the proportion of SEPA credit transfers initiated from or received in Hungary cleared in STEP2 compared to the total volume of euro transactions initiated from Hungary and carried out through STEP2 in the months of April, May and June amounted to 32%, 47% and 44% respectively. However, this estimate presumably strongly distorts figures upwards, as not even the simple STEP2 euro transfers used as the denominator are all included, moreover it does not contain simple euro, nor SEPA credit transfers carried out through other infrastructures. Consequently, the closest current approximation is the proportion of 10%-20% provided by Hungarian banks.

Regardless of whether the bank account of the recipient of a euro transfer initiated from Hungary is led by a Hungarian or a foreign bank (the former is considered a domestic, while the latter is considered a cross-border transaction from a legal perspective), the procedures involved in its execution are the same, as there is no euro clearing and settlement in Hungary among domestic banks. Hungarian banks therefore carry out all euro transfers via foreign correspondent banks. From the perspective of its content, all Hungarian euro transfers thus qualify as cross-border transfers. As the SEPA Credit Transfer Scheme primarily brings substantial benefits to banks in the

<sup>12</sup> This experience generally applies to the entire euro area. Due to the fact that the schemes essentially set forth rules for the inter-bank area, SEPA awareness is low. The Council, the European Commission and the Eurosystem are striving to improve the level of information with the help of a separate communication strategy.



case of cross-border payments, its use is spreading at the fastest pace in this segment.

## CONCLUSIONS

The introduction of the euro has not yet brought any significant changes in the domain of retail payments. The nationally distinct payment services and infrastructures have remained in place.

SEPA is an initiative essentially aiming at common legal frameworks from the perspective of the European Commission and the ECB, and for the elaboration of common standards from the perspective of the Council, with the objective of improving the efficiency of euro-denominated retail payments within the EU. The Directive developed by the Commission lays down a common and mandatory legal framework and rules for all payment services and products within the EU, effective from 2009, regardless of whether payments are carried out in euro or another currency.

European banks have organised among themselves, and created the SEPA schemes and frameworks in accordance with the Directive, under the auspices of the Council: these are the SEPA credit transfer, direct debit and card payment frameworks. These frameworks are based on the use of common procedures, standards, bank account and bank identifiers, in other words the SEPA project is composed of multiple elements. Thus far, the SEPA Credit Transfer Scheme has practical significance, which has already been implemented across the entire EU, including Hungary.

Contrary to common belief, the SEPA scheme is not a payments system, but rather a set of procedural and legal rules pertaining to a specific euro payment method, which can potentially lead to substantial cost efficiencies over the longer term for banks, and thereby customers as well.

According to a study<sup>13</sup> commissioned by the European Commission, rapid and broad transition from the credit transfer and direct debit methods currently in use to SEPA schemes at the pan-European level may lead to savings on a social level of EUR 123 billion compared to the currently used payment methods over the period 2006-2012. This amount could be further increased by EUR 238 billion, if the benefits offered by electronic invoicing are included in the calculation.

Here, it should be noted that neither the Directive, nor the SEPA Credit Transfer Scheme contain specific stipulations on

transaction fees, or their level or value. The defrayment of fees, however, is regulated, as well as their division between the originator and the beneficiary.

Twelve banks already use the SEPA Credit Transfer Scheme in Hungary. Based on the data available to the MNB, it can be stated that Hungarian banks have thus far implemented the SEPA Credit Transfer Scheme at a faster pace than euro area banks. This is due to fact that the procedures used in both domestic and cross-border euro transfers are the same, as there is no euro clearing and settlement in Hungary among domestic banks. Regardless of whether the bank account of the recipient of a euro transfer initiated from Hungary is led by a Hungarian or a foreign bank, the former is considered a domestic, while the latter is considered a cross-border transaction from a legal perspective. Hungarian banks therefore carry out all euro transfers via foreign correspondent banks. From the perspective of its content, all Hungarian euro transfers thus qualify as cross-border transfers. As the SEPA Credit Transfer Scheme primarily brings substantial benefits to banks in case of cross-border payments, its use is spreading at the fastest pace in this segment.

## APPENDIX

The abbreviations used in the article are explained below:

SEPA: Single Euro Payments Area

SCT scheme: SEPA Credit Transfer Scheme

SCT: SEPA Credit Transfer

EPC: European Payments Council

PSD: Payment Services Directive – Directive 2007/64/EC of the European Parliament and of the Council of 13 November 2007 on payment services

PE-ACH: pan-European automated clearing house

ACH: automated clearing house

TC: Terms and Conditions

LC: list of conditions

CSM: Clearing and Settlement Mechanism

<sup>13</sup> Capgemini analysis (2007): *SEPA: potential benefits at stake (Researching the impact of SEPA on the payments market and its stakeholders)*.