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SEPA

Plus ça change...

UK payments landscape to see significant changes

Dubai hosts inaugural ATM conference

Iran to dominate ATM market in Middle East and Africa?

Global smart card shipments to reach 4.8 billion in 2008

Country profile: Portugal



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How important is 28th January for SEPA?

The first SEPA-compliant payment instruments come into operation on 28th January 2008. In

many ways this date is only symbolic, as it is not the deadline for withdrawing existing services but a start date for offering new services that meet the requirements of the EPC's Rulebooks; banks that sign-up to these rulebooks must as a minimum be able to accept SEPA Credit Transfers (SCTs) by 28th January 2008 and make SEPA Direct Debits (SDDs) available by no later than 1st January 2009.

As detailed in our lead article (page 2), substantial progress towards SEPA has been made. The reality, however, is that most payments are still national – for example, industry estimates suggest that only 3% of credit transfers are cross-border. Is this because making cross-border credit transfers up to now has been difficult or expensive? Or is it because demand for such services is still relatively low? The answer is a bit of the first, but much more of the second.

This places banks in a dilemma. It is expensive to run parallel systems that offer national and SEPA-compliant payments, but while most demand is for existing services, it is also expensive to migrate customers. In the case of SDDs, for example, industry experts estimate it will cost €50 per direct debit to migrate from existing mandates – a total of at least €1 billion for mandate conversion alone.

In practice, national and SEPA-compliant payment instruments will continue to be offered in parallel for some time. As demand for SEPA-compliant payments slowly grows, and banks become ever more concerned about the costs of running parallel systems, pressure will increase to withdraw national legacy systems. The European Commission correctly points out that the benefits of SEPA will only be fully realised once this happens.

The Eurosystem's target is that a critical mass of payments within the euro area will be migrated to SEPA by the end of 2010, but this looks extremely unlikely. Exactly when this will happen is unknown, but it is the date that national payment systems are decommissioned, and not 28th January 2008, which will go down as the defining moment for SEPA.

Dominic Hirsch, Editor

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Annual subscription (12 issues):

£600 (€900/\$1,200) printed

£950 (€1,400/\$1,900) electronic and printed

ISSN 1748-5304



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SEPA

Plus ça change...

Significant progress has been made in the last eighteen months towards designing and developing the infrastructure needed to implement SEPA

EBA Clearing has developed a Priority Payment Scheme, which provides end-to-end processing of single credit transfers in euros within four hours

With the first milestones for the implementation of the Single Euro Payments Area (SEPA) now imminent, we thought it timely to review the current status of the SEPA project. How, if at all, will the European payments market change in January? Will corporates, small and medium-sized enterprises (SMEs) and consumers notice any difference in the products and services they are offered or in their utility or pricing? And what needs to be done urgently to move the project forward?

Significant infrastructural progress

There is little doubt that significant progress has been made in the last eighteen months towards designing and developing the infrastructure needed to implement SEPA. This results from the praiseworthy efforts, not to mention an aggregate investment of billions of euros, by the European Payments Council (EPC), EBA Clearing, SWIFT (the financial messaging network), individual banks, processors, Clearing and Settlement Mechanisms (CSMs) and others. Key activities have been:

- The approval and publication by the EPC of (updated) versions of the SEPA Credit Transfer (SCT) and SEPA Direct Debit (SDD) Rulebooks and Implementation Guidelines; the SEPA Data Model; the UNIFI (ISO 20022) XML standards; the SEPA CSM/PEACH (Pan-European Automated Clearing House) Framework and the SEPA Testing Framework. Adherence to the Rulebooks means that banks must at a minimum be able to accept SCTs from 28th January 2008 and make SDDs available no later than 1st January 2009.
- The publication in August 2007 by the European Automated Clearing House Association (EACHA) of version 3.0 of its Technical Interoperability Framework (TIF), which defines the requirements for interoperability between European CSMs as well as between banks and CSMs.
- The fifth SEPA progress report of the Eurosystem – the European Central Bank (ECB) and the national central banks within the euro area – defined its requirements for SEPA-compliance for payments infrastructures. These include compliance with the EPC's specifications and the adoption of interoperability rules and procedures for the exchange of SCT and SDD payments between banks and infrastructures.
- EBA Clearing and SIA-SSB, the Italian infrastructure company, have designed and implemented a SCT service which utilises EBA Clearing's STEP2 platform and is based upon the EPC Rulebook and ISO 20022 XML schema. The basic STEP2 Credeuro credit transfer service has been enhanced by additional functionality.
- EBA Clearing and SIA-SSB have also developed a Multi-purpose Pan-European Direct Debit (M-PEDD) service, again based upon the STEP2 platform and ISO 20022 XML standard messages. This has debit requests, cancellations and reversals, a single daily clearing and settlement cycle and payment warehousing up to S-14 (14 days before settlement).
- EBA Clearing has completed the acceptance testing of its SCT and M-PEDD services, which involved 103 and 12 banks respectively. The SCT service will be able to receive SCT payments from 25th January 2008, with the first settlement on 28th January.
- EBA Clearing has developed a Priority Payment Scheme, which provides end-to-end processing of single credit transfers in euros within four hours. This is due to be operational in the first half of 2008.
- As at November 2007, STEP2 had 1,747 direct and indirect participants, which in aggregate allow credit transfers to be sent from and to all bank accounts in the 30 EEA countries (the EU27, Iceland, Liechtenstein and Norway) plus Switzerland.
- As at November 2007, 15 technical facilitators (including Deutsche Bank, Equens, Iberpay and Seceti) were linked to EBA Clearing's STEP2 to allow their customer banks to exchange SEPA payments with other banks in 31 European countries.

- There are now more than 1,500 approved adherents to the EPC's SEPA Credit Transfer Scheme.
- STEP2 cross-border credit transfers grew 19% by volume and 22% by value in the year to November 2007, to over 350,000 transactions on average per day with a value of €1.48 billion.
- In October 2007, five CSMs – Equens, Iberpay, Seceti, Stet and VocaLink – announced that they had agreed to establish interoperability by January 2008 to enable the exchange of SEPA payments, the first implementation of EACHA's TIF. Together these CSMs processed over 18 billion direct debits and credit transfers in 2006.
- VocaLink, the transaction processing company that operates the UK's BACS service for direct credits, direct debits and standing orders, set up a €CSM partnership with around 20 banks (including ABN-Amro, Bank of America, Citibank, Dexia Bank, Fortis, Lloyds TSB, the Royal Bank of Scotland and Santander) in July 2007. This provides a pan-European clearing service for SEPA payments and the worldwide clearing of non-SEPA payments.
- In November 2007 the Euro Alliance of Payment Scheme (EAPS) was formally established as a scheme of schemes, with the objective of enabling its members' cards to be accepted in other members' ATMs and POS terminals. Its founder members are COGEBAN¹, European Payment Card Solution², Eufiserv³, Euro 6000⁴, LINK⁵ and SIBS⁶.
- VPay, the European debit card scheme that is based upon EMV chip and PIN technology, has started to gain some traction. The first VPay transactions have taken place in countries such as the Netherlands and Switzerland. In December 2007, Visa Europe announced that 22 banks from eight countries (Austria, Belgium, Bulgaria, France, Germany, Italy, the Netherlands and Switzerland) had committed to issuing an aggregate of 20 million VPay cards. Visa claimed this represented 12% of the debit card market in these countries, although the real figure is closer to 9%.

Recent EU events underpin SEPA

There is little doubt that significant impetus has been given to SEPA by two key events in Brussels and Strasbourg in 2007.

First, nearly seven years after it was initiated by the

European Commission, the European Parliament agreed the Payment Services Directive (PSD) in April 2007. This was subsequently ratified by the Council of Ministers.

The PSD provides a common legal framework for defined payment services in the EU irrespective of their currency – including credit transfers, direct debits and card payments. It defines the new concept of a 'payment institution' and covers pre- and post-transaction information requirements, execution times, value dating and so forth. It mandates that payments must be executed by no later than D+1, with a waiver of D+3 to 1st January 2012 only if a bank has explicitly agreed this with its customers⁷.

The PSD was published in the Official Journal of the European Union on 5th December 2007 and must be enacted into national law in the 27 Member States by 1st November 2009.

Second, on 19th December 2007 the European Commission's Competition Directorate finally made a ruling on MasterCard Europe's intra-EEA fallback multilateral interchange fees (MIFs) for POS transactions on consumer debit, charge and credit cards, which it has been investigating since 2002. The fees are used for virtually all cross-border transactions on Maestro and MasterCard-branded consumer cards within the MasterCard Europe region, and also for domestic purchase transactions in eight EEA countries including Belgium, the Czech Republic, Greece, Ireland and Italy.

The decision, which was allegedly the subject of fierce debate between the Commission's Competition and Internal Market and Services Directorates, was that MasterCard's MIFs violated EC Treaty rules on restrictive business practices under Article 81(1) and did not fulfil the exemption conditions in Article 81(3). The Commission said that MasterCard's MIFs restrict "price competition between acquiring banks by artificially inflating the basis on which these banks set their charges to merchants", which is harmful to businesses and their customers, and that they do "not lead to objective efficiencies that could balance the negative effects on price competition between its member banks". MasterCard was directed to withdraw its intra-EEA fallback MIF arrangements, and was given six months to comply fully with the decision.

The Commission's ruling states that MIFs per se are not illegal and that other MIF arrangements, adopted by MasterCard or other payment card

There is little doubt that significant impetus has been given to SEPA by two key events in Brussels and Strasbourg in 2007

The Payment Service Directive provides a common legal framework for defined payment services in the EU



Despite the advances in the SEPA project's infrastructure and legal framework, it is likely that few consumers, SMEs or corporates will notice that anything has changed on 28th January

- schemes, may obtain Article 81 (3) exemption. It is clear that MasterCard Europe did not persuade the Commission that its interchange fee methodology is reasonable, did not provide sufficient empirical evidence to demonstrate the positive effects of its MIFs, and failed to convince the Commission that its interchange fee levels were acceptable.

The Commission's decision is welcome and illuminates the legality of interchange fees. However, it does not provide a benchmark that can be used for the whole European payments card industry. Nor does it provide the level of certainty on interchange fees that payment card organisations and banks have been requesting for several years, to enable them to change their business models and plan strategically.

Little change expected in January 2008

Despite the marked advances in the SEPA project's infrastructure and legal framework, and some increased clarity regarding payment card interchange fees, it is likely that few consumers, SMEs or corporates will notice that anything has changed on 28th January.

For credit transfers, where the greatest advances have been made, it is not expected that the introduction of SCTs will result in any significant change in the short term in the products offered or their pricing, European reach or the information shown on bank statements.

Only around 150 to 200 banks in the EEA and Switzerland will be direct members of the STEP2 PEACH. These banks almost certainly already offer credit transfer services that enable fund transfers to be sent to and received from all '31 SEPA countries'. Although there are around 1,600 indirect participants, some of these may not have completed their interface testing with direct participants, and the Eurosystem has stated that 'smaller banks' that do not handle a 'critical mass' of payments just need the ability to receive SCTs from January 2008. Many of these, and probably the majority of the remaining 6,000 European banks, will therefore not be offering enhanced credit transfer services in January, or indeed for some months.

Prices for cross-border credit transfers in euros are also likely to remain unchanged, as they have already been reduced dramatically since July 2003 as the result of EU Regulation 2560/2001. It mandated that the same price must be charged for ATM cash withdrawals, payment card purchases and credit transfers in euros that occur within Member States (national transactions) and between Member States (cross-border transactions).

Neither consumers nor businesses will see any change in the direct debit services offered in 2008, although Jean-Michel Godeffroy of the ECB stated in October 2007 that some banking communities may offer SDDs from July 2008. Most banks, however, will probably not start offering them until 2009.

Finally, neither consumer nor business cardholders will see any change to the acceptance or functionality of their payment cards. Many argue that little change is required anyway, because all bank-issued European charge or credit cards have international branding; 94% of debit cards in the Eurozone are co-branded with an international scheme such as Maestro, MasterCard, Visa or Visa Electron (see table); and merchant acceptance of both national and international payment cards is more than adequate.

Although the EAPS claims that it is now fully operational, there is little evidence of substantive, transaction volume-generating inter-scheme links

Debit cards in the eurozone

End-2006 (millions)¹

Country	National debit only ²	(Co-) branded with international card scheme ³	Private label	Total
Austria	-	7.0	-	7.0
Belgium	0.4	11.0	0.1	11.5
Finland	3.2 ^{4,5}	1.7	1.3	6.2
France	1.5 ⁵	30.6	-	32.1
Germany	-	92.0	-	92.0
Greece	-	5.9	-	5.9
Ireland	0.6 ⁶	1.0	-	1.6
Italy	4.1	31.3	-	35.4
Netherlands	4.0	18.8	-	22.8
Portugal	0.3	10.4	-	10.7
Slovenia ⁷	-	2.3	-	2.3
Spain	0.1	33.5	-	33.6
Eurozone	14.2	245.5	1.4	261.2
% of total	5.4%	94.0%	0.5%	100%

Source: RBR analysis

Notes: ¹ All figures are rounded.

² Cards branded just with a national debit card scheme logo that may only be used nationally.

³ Cards branded (or co-branded with) Maestro, MasterCard, Visa or Visa Electron.

⁴ These cards are being re-issued with an international debit card logo.

⁵ Around 1.8 million of these cards are combination debit/charge or debit/credit cards co-branded with MasterCard or Visa for international charge/credit card usage.

⁶ AIB announced in July 2007 that all its Laser national debit cards will be co-branded with Maestro - this will mean that less than 300 thousand Irish debit cards will be Laser only.

⁷ End of 2004.

between members, based upon new cross-border acceptance arrangements. Neither is there any sign of the emergence of a third European debit card scheme nor of the Falkensteiner Group of major banks showing its hand and setting-up bilateral or multilateral acceptance arrangements.

This stasis is notwithstanding the repeated and increasingly assertive campaigning by the ECB and the European Commission for an alternative debit card scheme, with co-branding being seen as a possible interim approach while a long-term strategy is developed. The authorities state that such a scheme should focus on the euro area, but possibly have wider coverage in the remainder of the EU. It could be completely new, created via a national card scheme evolving to cover the whole euro area, or emerge via an alliance between existing national schemes. In all cases, however, the new scheme should be bank-owned, be based upon a four-party model, have a clear separation between scheme management and processing services, and have low or no interchange fees.

Ten New Year's resolutions

The various stakeholders involved in the SEPA project should make the following New Year's resolutions to accelerate the implementation of SEPA in 2008:

1. Public administrations and governments throughout the euro area must commit to adopting SEPA-compliant payments, transforming their political support of the project into concrete action by becoming operationally ready to send and receive such payments as soon as possible. (*The World Payments Report – 2007* said that these organisations are key catalysts in the migration to SEPA payment instruments, with transaction volumes that account for 15% of credit transfer and direct debit transactions in the eurozone and 29% of the volumes required for SEPA to attain critical mass.)
2. National banking associations or equivalent bodies, responsible for defining and coordinating SEPA implementation at a national level, must finalise and publicise their migration plans. They must communicate the move to SEPA to local stakeholders as part of an enhanced SEPA communications programme aimed at all end-users.

3. National banking associations or equivalent bodies must set end dates for the termination of legacy national payment instruments.
4. The European Commission should provide greater clarity on the acceptable multilateral interchange fee arrangements and levels of interchange fees for payment card transactions, for both consumer and commercial cards. It should commit to changing its current apparent insistence (as illustrated in the recent MasterCard decision) on looking at the issue on a case-by-case basis, and should provide better benchmarks and guidance for the whole European payment cards industry.
5. The European Commission should reach a speedy decision on Visa's intra-regional interchange fees, following the ending of Visa's current exemption on 31st December 2007.
6. The European Commission should give guidance on the acceptability of interchange fees for direct debits.
7. The European Commission should complete its review of Regulation 2560/2001 and raise the threshold for balance of payments reporting to €50,000.
8. The EPC and any other parties involved in producing payment card standards within the four domains (card-terminal, terminal-acquirer, acquirer-issuer and terminal certification), with the objective of removing national standards and ensuring inter-operability, flexibility and independence in the choice of service provider, should commit to finalising these standards by the end of 2008.
9. The EPC must clarify precisely which additional features will be offered within the SDD scheme.
10. Payees/originators and corporates should start collecting BIC and IBAN information from their customers and suppliers. ■

Notes:

- ¹ Manager of the Italian PagoBancomat national debit card and Bancomat ATM schemes
- ² Licensees for the German Electronic Cash national debit card and Deutsches Geldautomatensystem ATM schemes
- ³ Pan-European ATM network
- ⁴ Spanish payment scheme
- ⁵ Operators of the UK's ATM-sharing network
- ⁶ Responsible for the Portuguese Multibanco debit card scheme
- ⁷ An extra day is allowed for transactions initiated by paper

Public administrations throughout the euro area must commit to adopting SEPA-compliant payments, transforming their political support into concrete action

The European Commission should give guidance on the acceptability of interchange fees for direct debits

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