

## INSTANT PAYMENTS AND EPI



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## SEPA reinforced: restart retail payments for the benefit of European society

The SEPA project has substantially transformed the European payment landscape over the last two decades. Cross-border euro payments have become faster, cheaper and more efficient. Such an extensive transformation has only been possible thanks to a coordinated effort on the part of both private and public players. With TARGET2, the Eurosystem created a reliable basic infrastructure that became essential for the settlement of individual payments across Europe in central bank money. Furthermore, the additional TIPS service now enables euro retail payments to occur within a matter of seconds.

The EPC, an association of payment service providers, developed basic SEPA instruments. Mandatory migration from previous national instruments to SEPA credit transfers and direct debits

accelerated adoption. Moreover, with PSD2, a uniform European regulatory framework was established.

While the SEPA approach has worked well for credit transfers and direct debits, national card schemes have not made it across borders. Only in combination with one of the international schemes are buyers able to pay with these cards outside of their home country.

Moreover, some domestic online, mobile and P2P payment schemes based on instruments such as cards or instant payments have emerged. While international bigtechs are either gaining an increasingly large market share or already enjoy a strong incumbent position, these domestic schemes will lack the scale to effectively compete in the medium term.

Given the experience gained with the SEPA project, the apparent shortage of viable European payment options and the increasing influence of international competitors, what can be done to reinforce SEPA and facilitate digital payments that both promote economic development in the EU and make it easier and safer for European citizens to pay?

One important decision has been already made: to update the basic European payments infrastructure. Not only will TIPS develop into a cross-currency instant payment platform – even more prominent is the launch of T2 in November 2022. It will replace and modernize TARGET2, which started in 2007.

With T2 and TIPS, a novel, reliable infrastructure that allows for efficient and secure payments in Europe will be in place. Now, appropriate payment instruments and solutions based on common standards are needed in order to take advantage of this.

The EPC's SEPA instant credit transfer scheme is one such instrument. Although it has been in place since November 2017, only about 70% of euro area PSPs have joined the scheme, and only 10% of credit transfers are instant at present.

SEPA instant credit transfers represent an opportunity for the European payment industry to jump into the digital age and support both individuals

and firms in meeting their daily payment needs. For payment service providers, instant payments can foster customer relationships by focusing on direct account-to-account transactions rather than being fragmented across proprietary solutions, card schemes and bigtech platforms.

For instant payments to become the new normal and for us to reap the benefits of this, mandatory measures similar to those implemented for the first SEPA instruments might be worth considering.

That being said, payment service providers must think beyond pure processing. But at the same time, they must recognize it as being the core of innovative payment solutions. New standards such as request-to-pay messages jointly developed within the EPC are building blocks towards reaching these ambitions. Common APIs based, amongst other things, on the rules of the PSD2, or, going beyond this, the development of premium API services, may also help to realize the vision of frictionless payments that are integrated into everyday life whilst also being easy to manage, safe and transparent.

A number European banks came together in the EPI to develop a European payment solution that would utilize the building blocks described. It intends to offer an EPI wallet based on instant payments and an EPI card based on European standards such as CPACE. At the end of the first quarter of 2022, the participants will decide whether to launch the market entry of these solutions.

Despite the tremendous progress made in the European payments market, another even more profound change is already on the doorstep. Bigtech firms have announced their intention to come up with their own stablecoins based on DLT, which may potentially be usable on a global scale. In response, central banks around the world are weighing up the option of issuing their own digital currencies. Since July 2021, the Eurosystem has also been exploring the possibility of implementing a digital euro. If this comes to fruition, it could complement the existing SEPA infrastructures and build upon European payment solutions for the benefit of European citizens and businesses alike.



## TUOMAS VÄLIMÄKI

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### Instant payments and standards to enable new pan- European payment methods

Single Euro Payments Area (SEPA) has benefitted us a great deal. With joint standards and rules, credit transfers are transmitted uniformly within a country or from one country to another, even with same fees. Technological developments and the fact that we, the consumers, expect everything to take place in real time are also reflected in our expectations for the next steps in the evolution of payments.

However, processing payments is much more than just instant messaging: a payment message means nothing if there is no embedded mechanism to transfer the associated credit. And there is much more. Risk management, authentication, KYC, AML and sanction screening are functions that need to be performed when conducting payments. Payments industry is responding to the growing expectations. Automated Clearing Houses have developed their cycles to transfer credit faster. Often this takes place within the same day. In addition, we have the instant payments, which in SEPA are implemented via the SEPA instant credit transfer scheme (SCTInst). Payments that are made

under the scheme are transferred from the payer to the payee immediately 24/7.

SEPA Instant payment scheme was introduced in November 2017 and its implementation still continues. A lot has been done, but we can see also many shortcomings. Not all SEPA countries yet meet the regulatory requirement for coverage. And fulfilling the regulation doesn't tell all about the actual situation. For example, in Finland, good progress has been made in general as banks have built capabilities to receive instant payments. Although this meets the requirement of the regulation, full benefits can only be gained when incoming and outgoing payments are treated the same way in all relevant participants. This development takes time, and it is understandable that banks are moving forward according to their own business decisions. There are numerous development streams that fight for the resources in banks.

The current situation is not optimal for the users, i.e. consumers and businesses. How to promote instant payments, if there is no certainty of the relevant parties' capability to treat payment instructions according to the same rule book? Achieving full benefits of instant payments requires both the payer and the payee to be aware and trust when they can expect the funds transferred to be available to the payee.

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**We need a common  
real time electronic  
retail payment method  
that is available all  
around Europe.**

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There can be many rails for instant payment and not everything has to be transferred along the same channel. Still, standardization facilitates expansion. The Eurosystem has set full deployment of instant payments as one of the main goals in its retail payment strategy. We see real benefits in instant payments. To support implementation, the Eurosystem also launched the TARGET Instant Payment Settlement (TIPS) system. With the recent changes in TIPS, the Eurosystem facilitates pan-European reachability of instant payments by enabling also ACHs as clearing members.

Instant payment infrastructure will be of particular importance in the future as it can be used as a foundation for new payment services to end customers. When money can be transferred in real-time across the Europe, new innovative solutions can be built on top of it.

According to the Bank of Finland's annual consumer survey, card payments have grown strongly over the years at the expense of cash. However, the use of mobile payments is becoming more and more popular and the summit of card payments may already be behind us. Mobile payments still often involve the use of card payment rails. But it doesn't have to stay like that. Smartphone applications can be developed to link the payer to payee and the established connection can be utilized to send instant payment transactions to banks for settlement. This development would create competition in the payments market and benefit payers and payees both with enhanced service level and with reduced costs.

Before this will be reality, there are challenges that need to be overcome. Banks' interfaces via which the new payment apps could send and receive transactions, are inconsistent and non-standardised. New services need to have uniform rules and a business logic which benefits all parties in the payment chain. To overcome these hurdles and to enable pan-European development, we need European coordination and joint efforts. Payments is a business where economies of scale are significant, and it naturally leads to market concentration. These efficiencies may not trickle down to end users if market concentration means non-existing competition.

The euro area deserves more than facilitating the interoperability of some aging technology based national payment methods to complement the role of cash as a true European retail payment method. That is, we need a common, real time or instant electronic retail payment method that is based on the latest technology and could be used everywhere in Europe, both in physical stores and in e-commerce.



## PIERO CIPOLLONE

Deputy Governor -  
Banca d'Italia

### Connecting fast payments system to improve cross- border payments

Advancing the G20 Agenda on cross-border payments was a priority of the Italian G-20 Presidency.

There are many ways to address the current difficulties in retail cross-border payments but the current state of development of the CBDC and the trends observed in the corresponding banking models suggest that the most promising way forward is to tap into what we already have and put interoperability of the fast payments system at the centre of our considerations.

To move money smoothly across jurisdictions, we need to address the three dimensions of interoperability – technical, semantic and business-related. Despite the fact that central banks command only some of the levers needed to reach effective solutions, much can be done by orchestrating a well coordinated common effort among all the actors involved, namely governments and private-sector operators.

Central banks have much experience with retail and wholesale payment systems, and have all the technical

skills not only to set up brand new interoperable payment systems but also to figure out solutions for connecting existing infrastructures.

The Bank of Italy, in coordination with the Eurosystem, has spent a lot of time studying both how to enlarge the scope of a payments' platform and how to connect fast payment systems in different jurisdictions. It might be useful to reflect on a couple of experiences.

The first case refers to the use of TIPS by Sveriges Riksbank, which is planned to start in 2022 for the execution of instant payments in Swedish krona. In addition, a solution to the problem of cross-currency settlement, i.e. where euro and krona are both present in the same transaction, is now being investigated. From an engineering perspective, sharing the same platform allows us to exploit common technical and semantic elements. From a legal viewpoint, the Eurosystem concluded a Currency Participation Agreement (CPA) with Riksbank in which mutual rights and obligations are defined. Our common European Union membership has minimized the need for adaptation, thanks to comparable legal backgrounds.

Other European jurisdictions, some not belonging to the EU, are working with the Bank of Italy and with the ECB to explore the possibility of replicating this model, and TIPS is a recognized benchmark for those countries aiming to join the EU.

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As members of the Eurosystem, we should be bolder in engaging with neighbouring jurisdictions, especially - but not only - those belonging to the EU, in order to replicate this model.

The second case refers to the successful experiment of a connection between Fast Payment Systems (FPSs), namely Buna and TIPS. BUNA IPS is the system corresponding to TIPS operated by ARPCSO, an independent entity owned by the Arab Monetary Fund (AMF). During the experiment, a number of cross-currency transactions were settled in both TIPS and BUNA IPS, by debiting a bank's TIPS account in EUR

and crediting another bank's account in BUNA in Jordanian dinar (JOD). The average end-to-end response time for these transactions was approximately 15 seconds.

This second experience goes beyond what has been done in other cases of FPSs between two interconnected jurisdictions, since with a single link we were able to connect the 19 TIPS countries with the 16 Buna jurisdictions.

This experiment points to a key dimension of cross-border payments: the role and local importance of regional systems. Developing regional fast payment systems among countries whose legal and technical frameworks have many commonalities can preserve local customer relationships and banks' internal procedures and preferences, thereby facilitating broad political consensus for the interlinking. At the same time, these interlinked systems could represent an intermediate step on the path to a common platform able to connect everybody by means of a single link.

The Nexus project, which the Banca d'Italia has recently joined, is one such example. It aims to connect national payment systems to improve the speed, cost and transparency of cross-border payments. A single connection to the Nexus platform should allow a fast payments system to reach all the other countries participating in Nexus.

To leverage this technical expertise, central banks should assign the highest priority to projects where technical interoperability would per se permit the smooth flow of funds between different jurisdictions. In terms of priorities, the next one should be our efforts to connect regional fast payment systems as they maximize the returns for both citizens and firms that both stand to benefit from the interoperability of payment systems, while limiting the number of links needed to ensure their interoperability.

As for business interoperability, we must accept that our mandate falls short of this need, since the government and the private sector occupy the driver's seat in this process. But we should also be cognizant of our power of advocacy and stand ready to use it.



## ERIC TAK

Global head of the Payments Centre - ING Group

### Paving the way for EPI - a Dutch perspective

While the EU continues to strive for a single market, payments remain a largely national affair. Fragmentation caused by regulatory differences, national payment solutions and local culture and payment habits continue to make the EU payment landscape complex. As most national cards and alternative payment methods still do not work across borders, a truly European payment solution is missing. When you add dependencies on foreign players and the increase of Bigtech entering the market, the importance to start working together on a unified pan-European solution becomes clear. This is needed to have sufficient scale to invest, to stay relevant and to ensure usage across borders.

For many years, the Dutch payment system has been among the most efficient and advanced in the world. At the end of 2020 85% of all Dutch payments with Debit and Credit cards were contactless, predominantly with contactless payment cards and increasingly with a smartphone or wearable.<sup>1</sup> For e-commerce purchases, iDEAL is the market leader in the Netherlands. iDEAL is an online payment method developed by Dutch banks that enables consumers to pay online through their own bank. In addition to webshops, other organisations that are not part of the

e-commerce market, like utilities or public use-cases, also accept iDEAL. Almost 70% of Dutch consumers use this method to pay for their online purchases,<sup>2</sup> of which 85% is handled through a mobile device.<sup>3</sup> In order for such a market to switch to a European alternative, it would have to be at least as convenient and safe as already existing methods. Not an easy task, but nevertheless we believe it to be an important one.

The European Payment Initiative (EPI) aims to create this truly European payment scheme (covering P2P, Point of Sale and e-commerce/m-commerce) for the EU to regain sovereignty in payments, push the single market further and provide a European choice to its citizens. For banks such a scheme can mean a more scalable solution that is focused on innovation and better facilitates cross-border usage and ultimately global acceptance.

For the Netherlands specifically there are a few obstacles. Currently the local Interchange Fee for Debit cards is capped at € 0,02 while the EU cap lies at 0,20% of the transaction value. The proposed scheme fees for EPI will reflect the real costs of processing transactions and are based on de European interchange levels. Therefore it is less attractive for Dutch players to use the EPI card-scheme. For a truly European approach it would be important to eliminate the Member State options for the Interchange Fee that are already distorting cross-border acquiring but now also complicate the participation in EPI. Also the emergence of Debit cards that can be used for e-commerce necessitate a rethink of IFR caps in Member States.

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This is especially important as processing costs for e-commerce purchases are generally higher due to fraud mitigation and the need for 3DS security. As we see more e-commerce Debit card solutions coming up, an interchange fee of € 0.02 would not be sufficient to cover the costs. Furthermore, while we believe that EPI is an important step in strengthening Europe's payments landscape, we would encourage that this is developed leveraging existing best practices. We believe iDEAL is such a best practice and can provide a good basis for an EPI solution.

The challenges that have led to the creation of EPI go beyond payments and also touch upon the future and relevance of banks. Such a trustworthy interoperable EU-wide architecture, together with initiatives like the EU electronic identity wallet are important stepping stones for regulatory developments like a much needed Open Data framework to facilitate a data driven economy. Therefore it would be important to keep the lessons learned from PSD2 in mind: i) safeguard real technical standards; ii) ensure supervisory harmonization; iii) make sure the system is trustworthy and privacy sensitive e.g. think about data minimization and the use of consent dashboards.

The challenges of today's payment landscape require an holistic approach and cooperation among all the different actors involved, but getting it right would mean a future-proof solution that would reclaim the EU's sovereignty in this field.

[1] Betaalvereniging Nederland - <https://factsheet.betalvereniging.nl/>

[2] Betaalvereniging Nederland - [https://www.betalvereniging.nl/wp-content/uploads/Infographic\\_Thuiswinkel\\_Markt\\_Monitor\\_2020.pdf](https://www.betalvereniging.nl/wp-content/uploads/Infographic_Thuiswinkel_Markt_Monitor_2020.pdf)

[3] iDeal - <https://www.ideal.nl/actueel/nieuws/explosieve-groei-van-ideal-in-coronajaar-2020/>