EU RETAIL PAYMENT LANSCAPE

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A pan-European retail payment solution – Challenges and a potential way forward

1. Call for a pan-European retail payment solution

The Eurosystem has been constantly calling – at least since November 2019 – for a pan-European payment solution. The arguments as to why such a solution is needed are even more convincing now given the

- progress made by large non-EU technology platforms in digitalising and embedding payments,
- persisting fragmentation with a plethora of various digital payment solutions, as well as
- growing global risks that reiterate the need for independent European solutions.

The Eurosystem believes that consumers, merchants, companies and public authorities will benefit from a genuine European solution that delivers a unified payment experience throughout the EU across a large range of payment situations, such as online, offline or mobile as well as among private persons. It should enable easy, user-friendly, safe and frictionless payments. For merchants, such a solution should be cost-efficient, and convenient to take up and integrate into existing check-out systems. Moreover, this solution should be offered by European private players under a transparent European governance structure. A common brand would ensure that it is easy to recognise, also internationally once acceptance has been established in the EU.

2. Progress made so far and challenges faced

The most ambitious private project that aims at meeting these objectives is the European Payments Initiative, EPI. Initially, it was supported by 31 banks and two acquirers operating in seven markets. A number of shareholders withdrew during the first quarter of 2022. However, eleven banks and two acquirers in three markets (Belgium, France and Germany) are still participating. The scope of the proposed solution was scaled back to an instant payment-based wallet solution, abandoning EPI cards. However, the shareholders envisage a comprehensive package of features for all kinds of use cases and payment situations, including those usually associated with cards. They also see the possibility of integrating a European digital identity and, if realised, the digital euro as well as launching enhanced value-added services.

But even with the potential creation of an EPI Target Holding Company and the development of a concrete payment solution, a number of challenges remain. Why does it seem so difficult to agree on a common solution? Several issues are crucial:

First, most European banking communities invested in a mobile or e-commerce payment solution years ago. Some of these are quite successful in their home markets. Consequently, the owners are often interested in retaining the client relationships and some of the (im)material assets. The same often holds true for banking communities that own national card schemes.

Second, in countries that rely on international card schemes instead of national ones, banks might be bound by long-term contracts with the former, which they cannot terminate easily. This influences their future strategy in payments more generally.

Third, while most banks are convinced of the long-term strategic imperative of a pan-European payment solution, in the short-term each would need to invest a substantial amount of money. Depending on the internal assessment of this investment and their own financial situation, some do not want to take the risk.

Fourth, despite strong political support from the Eurosystem and the European Commission (coupled with a strong call for a pan-European payment solution), the new solution still needs to be sold to merchants, which requires considerable financial efforts. Without a sufficiently large acceptance network, consumers cannot pay with the solution.

Last but not least, the shareholders might also have felt a sense of uncertainty about the role the digital euro could play and about the need for a large coverage of instant payments.

3. Potential way forward

In short, the EPI project faces typical coordination problems combined with uncertainty. Although it has come a long way, shareholders still have much work to do. However, it is obvious that a pan-European solution would be in the interest of all European players. If they do not move forwards, the European payments market might soon be dominated by an international oligopoly. To put it bluntly, shareholders may risk losing direct client relationships and room for commercial manoeuvre as they are forced to act in accordance with the oligopoly's rules. Moreover, the sovereignty of the European payments market could be at stake. Should the Eurosystem intervene and propose its own solution?

In my opinion, private shareholders are best placed to offer a pan-European payment solution. They have the necessary expertise as well as the relationships and skills to do so. The Eurosystem, the European legislator and national authorities should support these activities even more.

If all forces – private and public – are pulled together, the European payments market can develop according to the goals announced by the Eurosystem and the European Commission.

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MEP & Vice-Chair, Committee on Economic and Monetary Affairs - European Parliament

Addressing the challenge of digital (instant) payments: a matter of sovereignty

The EU retail payment landscape has significantly changed over the recent years as the result of the rise of new entrants and solutions on the market. European regulators have worked on innovative European legislations on open finance, to empower consumers in the digital age and make them access to a variety of online services at a reasonable cost.

Instant payments are at the forefront of these changes, providing consumers with the ability to transfer money within a few seconds no matter what time or day of the year it is. Instant payments can also be used together with other innovations within the payment ecosystem such as the SEPA Request to Pay Scheme, a messaging functionality to request a payment initiation. Instant payments have also proven to be a valuable solution in the context of the Covid 19 pandemic, in Europe but also in other countries, as we see a global development of instant payments in the United States or in a number of Asian countries.

The benefits of instant payments are numerous; from allowing easier cross border transfers to reducing the use of cash and the associated risks of fraud or anti-money laundering.

Instant payments can be used in different cases. While peer-to-peer payments allowing an easier split of expenses between friends, family or colleagues tend to increase, other use cases remain underdeveloped because of limitations preventing their wider spread, in particular in-store payments to a retailer.

First, a lack of integration of the instant payment market, with only 61% of payment service providers part of the EU wide "SEPA Instant Credit Transfer Scheme", and only 12% of the SEPA Credit Transfer Transactions being instant payments. Second, a lack of standardisation of QR codes on which a growing number of instant payments rely on. Third, a lack of transparency and proper information on costs, disincentivising the use of instant payments, which remain on average more expensive for consumers compared to traditional payments (close to €1 on average).

The payment regulatory framework needs to be fit for purpose to empower and protect consumers while supporting the rise of European payment solutions and providers.

There is room for improvement to unlock the full potential of instant payments for the benefit of consumers, merchants and businesses. The upcoming European initiative on Instant Payments will be instrumental to further empower, protect consumers against fraud, and ensure their proper information on the associated costs. It represents the last missing piece of the Digital Finance Strategy, following the adoption of landmark pieces of legislation on the use of distributed ledger technology for markets infrastructures, digital operational resilience or activities and services related to crypto-assets. Together with a potential review of the Payment Services Directive (PSD2), a fit for the future Instant Payments initiative should make instants payments the new norm for fast, safe and transparent payments in Europe for a variety of use cases.

Similarly to what we have done for crypto-assets with the Markets and Crypto Assets Regulation (MiCA), and beyond financial services with the recently adopted Digital Services Act (DSA), the payment regulatory framework needs to be fit for purpose to empower and protect consumers while supporting the rise of European payment solutions and providers.

In practice, this means:

- Strengthening the integration into the single market of existing pan European initiatives to reduce the current market fragmentation and allow cross border real-time payments;
- Developing innovative and user-friendly solutions for online and mobile applications as well as QR codes to provide consumers but also retailers with a real choice on the payment method they want to use for each purchase or sale, alongside credit cards, regular banking transfers or cash payments;
- Improving transparency and information on the different features, value, functionalities and costs of each payment method; and
- Increasing the guarantees associated with instant payments, to foster trust and reliability for the consumer and the retailer, when it comes to safety features or reimbursement options, while preserving innovation and sound competition on the payment market.

2022 and 2023 will be important years for creating a unified EU payment system, with beyond legislative initiatives already on the table, concrete outcomes of the European Payments Initiative (EPI), a coalition of major European financial services players supported by the European Commission and the European Central Bank, which will also conclude its preliminary work for the creation of a digital euro.

What is at stake is the European sovereignty in the field of payments, and the ability of European players to provide adequate solutions, including through instant payments, to European citizens.

The future of payments will be European and instant or will not be.

MASSIMILIANO ALVISINI

Chief Executive Officer Europe - Western Union

How the PSD2 Review can unleash innovation and growth for the European payments sector

For decades now, the payments sector across the world, and in Europe, has been serving economies and communities by delivering financial, and more widely, social growth and development – quite frequently, to those that need it the most. The pandemic showed, yet again, how the payments sector has the ability to innovate in order to deliver for millions of people, providing them with a true lifeline.

We now, slowly, emerge from the pandemic to a totally new economic environment. Our societies are facing challenges, such as the double threat of inflation and lack of economic growth that haven't been seen since the 1970s. The cost-of-living crisis threatens to throw millions into poverty – a development that previously would be unheard of in Europe. Our new challenges demand new responses. As European-wide economy and society, we cannot collectively afford to lose opportunities to further unleash innovation, and growth.

The payments sector did rise to the pandemic challenge and is ready to rise to the challenge of delivering innovation and growth once more, as it has always done. To do that, as in every industry, our sector needs legal certainty and predictability to have the ability to innovate and grow. The Payment Services Directive (PSD) does precisely that: it has been at the forefront of providing much needed certainty within the European Union. However, a lot more needs to be done: to begin with, it is essential that we harmonize the rules across the EU, ensure that Anti-Money Laundering and data privacy rules work in sync with the PSD, and of course recognize the specific nature of the non-bank payment sector. All of that, while we continue to respond to the needs and reflect the needs of our customers, always fostering financial inclusion – a cause that lies at the center of Western Union's history through the years, and one I am personally committed to.

I believe that the upcoming PSD2 review initiated by the European Commission does serve these goals and is indeed a truly welcome step in the right direction, that has the potential to deliver for our economies and societies. As the stakeholder dialogue commences, I would like to offer my thoughts on how the current framework could be enhanced:

- In the interest of building a genuine Single Market for payment services in the EU, the rulebook for payment services in the EU should be further harmonized, establishing a real level playing field for all payment service providers. Presently, national fragmentation prevents the payments industry from leveraging the real benefits of the Single Market. Western Union believes that at least parts of the PSD should be converted into a Regulation and thereby apply directly across the Union. Examples include the complaints handling procedures, rules related to central contact points, and the supervision and division of responsibilities when payment services providers use agents.
- It is important that there is better alignment between the rules of the PSD2, the EU's Anti-Money Laundering regime (AML) and data privacy regulations. We welcome the truly game-changing plans for a common e-identification mechanism.
- Member States and financial supervisors should do more to address the de-risking practices of the banking sector. The PSD provides the framework on which authorized and regulated payment service providers have to follow strict requirements in line with their business model and the level of associated risks. Despite this, non-bank payment service providers have often experienced the unilateral closure of their bank accounts across various jurisdictions. Bank refusal to offer banking services to payment service providers is, in our view against the spirit of the PSD. It is also inconsistent with the risk-based approach in the EU's AML regime. These de-risking practices by banks could potentially drive non-bank payment service providers out of the market, resulting in millions of customers resorting to unlicensed alternative channels to cover their financial needs.
- In this context, we welcome the EBA Opinion of January 2022; we believe it would be greatly beneficial for our sector should the PSD2 review were to give the EBA a formal mandate to clarify the interrelationship between legitimate AML concerns and unwarranted de-risking practices.

I mentioned above how financial inclusion is a cause that Western Union serves in Europe and across the world. Let me point out here that, the issue of de-risking is intrinsically associated with the question of financial inclusion. While technology is important, payment services providers need to cater to the needs of all their customers - including to those who prefer to transact with cash and are not a negligible part of the economy. With migrant populations in Europe a significant percentage of the total, this is particularly important.

Furthermore, should the PSD2 review deliver a more effective and innovative compliance framework across the Union, while of course not compromising on financial stability, consumer protection and crime prevention, this would allow the sector to further invest in innovation, and lower costs for consumers, making cross border payments even more affordable. This will also foster financial inclusion.

We at Western Union, with our experience of serving millions across the world, for more than 170 years now, stand ready to contribute substantially and creatively to the review, aiming at building a European payments sector that is fit for purpose and to respond to the challenges faced by our economies and societies. This is the time to truly unleash innovation and growth and put customers across the Union at the center of everything we, governments, regulators, providers, do.

BRETT LOPER
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Driving competition in payments through policy change

The second half of 2022 will usher in an acceleration of the work by the European Commission to review one of the key pillars of the European payments market: the Second Payment Services Directive (PSD2). More than four years after its entry into force, it is an opportune time for policymakers and industry to take stock of both its achievements thus far and the policy changes necessary to achieve the principal goal from 2015: a true pan-European single market for payments.

PSD2 aimed to enhance consumer protection, promote competition, and improve the security of payment services. While the Directive has been revolutionary in bringing about an open banking framework – which is being replicated globally – the goal of achieving more competition in the European market has proven elusive. There are valuable lessons in each of these areas.

Chief among these is the need to widen access to data, for all market players. While banks had historically guarded access to customer data, the open banking mandate in PSD2 finally enabled consumers and businesses to take more ownership of it. Importantly, this enabled new entrants to join the European payments market and – for some – to grow into highly successful pan-European fintechs. Take for instance the rapid rise of Swedish fintech Klarna, which effectively developed its own in-house Account Information Service Provider to power Buy Now Pay Later products. N26, the Berlin based neobank, is another example which leveraged open banking APIs to facilitate account switching, enabling it to grow to over 7 million customers. Based on these, PSD2 has undoubtedly led to more competition and greater choice for consumers and businesses.

However, given that only financial data is shared, open banking has become a one-way street with data flowing from financial providers to Big Tech players, with little or no data sharing reciprocity. The financial services industry, therefore, faces the threat of unfair competition by non-financial companies. To combat this, the industry is urgently calling on policymakers to expand the industries covered by data sharing obligations. As such, data portability should become the norm all sectors.

A competition focused "PSD3" will be key to driving competition against dominant players in the EU.

To boost the adoption of open banking, more guidance on the rules from the competent authorities is also needed and, critically, it needs to be consistent. Notably, API standardization could be the solution to avoid inconsistent customer experiences that differ wildly across products and providers. We consequently call on the European Commission to mandate the development of API standards by supervisory authorities. The Open Banking Implementation Entity, which developed such standards for the UK, is a successful example of a standardization effort that we believe can be replicated on the European market. Ideally, the European API standards would also align with international standardization efforts to ensure global interoperability.

Evolving open banking towards open data is not the only way that the review of PSD2 can promote more competition. Combining the review with the mandatory roll-out of instant payments in the EU would enable healthier competition to the two dominant card schemes, Visa and Mastercard. Already, American Express has launched an instant payments-based service in the UK, leveraging the Faster Payments Service. Bringing the European equivalent – SEPA Instant Credit Transfer – to all European banks would allow similar services to be across the EU.

A fully integrated instant payment system would not only allow companies such as American Express to provide further payment options to consumers and merchants but also help the EU achieve its goal of open strategic autonomy, while at the same time making sure EU and non-EU companies can build innovative payment services on top of it. This would improve competition and highlight the EU's openness.

A competition focused "PSD3", as well as a strong instant payments framework, will be key to driving competition against dominant players in the EU retail payment space over the next five years. The review of PSD2 should, therefore, also focus on rules that discourage fair competition. This includes rules on open access, co-brand cards, and licensee arrangements of three-party schemes, which have harmed competition by introducing unwarranted regulatory burdens on smaller card schemes seeking to compete with the dominant duopoly of Visa and Mastercard in Europe.

Overall, we are encouraged by the European Commission's initial statements on the PSD2 review and look forward to further engaging in order to foster real competition on the European market. Ultimately, this will mean better outcomes for citizens, businesses, and society as a whole.