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Accompanying document to the

Report from the Commission to the European Parliament and the Council

of […]

**on the application of Regulation (EC) No 2560/2001
on cross-border payments in euro**

Annex to the Report

{COM(2008) 64 final}

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1. INTRODUCTION

Concerns about the functioning of the European cross-border payments existed well before the 1 January 1999, day of the introduction of a single currency, the euro.[1] Nonetheless, the inefficiencies and high costs of cross-border payments became apparent only after the introduction of the euro and the disappearance of exchange rates between the euro area countries. In 2001 the Commission realised that initiatives undertaken to facilitate the integration of fragmented European financial markets[2] would not lead to a reduction of costs and improvement of service standards in the field of cross-border payments. This constituted an obstacle to the proper functioning of the Internal Market and was seen as unacceptable by both consumers and businesses, for an area which operated with one, common currency.

Against such background, on 25 July 2001[3], the Commission made a proposal for Regulation (EC) No 2560/2001 of the European Parliament and of the Council on cross-border payments in euro (hereinafter referred to as the 'Regulation 2560'). It was adopted on 19 December 2001 and entered into force on 31 December 2001.

The objectives of Regulation 2560 were the following:

– to reduce the charges levied for cross-border payments to the level of domestic (national) payments;

– to encourage the financial services industry to make the necessary changes in existing cross-border payment infrastructures, as part of the integration of European financial markets;

– to apply the principle of transparent charges in order to allow customers to assess easily the cost of a cross-border payment;

– to lower costs and improve speed and quality of cross-border payments in euro by eliminating barriers to automated processing of payments (Straight-Through Processing or STP);

– to facilitate the execution of cross-border payments through the use of the International Bank Account Number (IBAN) and Bank Identifier Code (BIC);

– to remove all national reporting obligations for balance-of-payment statistics for cross-border payments up to EUR 12 500 and as to the minimum information to be provided concerning the beneficiary which may prevent automation of payment execution.

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1 See for example *Making payments in the Internal Market*, COM(1990) 447; *Credit Transfers in the EU*, COM(1994) 436; *Green Paper on Practical Arrangements for the Introduction of the Single Currency*, COM(1995) 333.

2 For example, *Financial Services Action Plan*, COM(1999) 232; *Communication on payments of small amounts in the internal market*, COM(2000) 36.

3 http://ec.europa.eu/internal_market/payments/crossborder/archive_en.htm#draft

Regulation 2560 equalises the price of cross-border payments (credit transfers, ATM cash withdrawals and card payments) made in euro up to EUR 50 000[4] and the price of corresponding national payments in euro within the same Member State (Article 3). It applies to both electronic payments[5] (since 1 July 2002) and credit transfers[6] (since 1 July 2003).

At the same time it should be clearly stated that Regulation 2560 stops short of a direct price setting and of making prices for cross-border payment services uniform within all Member States. It does not affect the possibility for institutions to offer a broad range of fees for different payment services, provided that this does not discriminate between cross-border and national euro payments.

2. REVIEW CLAUSE

Article 8 (Review Clause) of Regulation 2560 states that:

Not later than 1 July 2004, the Commission shall submit to the European Parliament and to the Council a report on the application of this Regulation, in particular on:

– changes in cross-border payment system infrastructures;

– the advisability of improving consumer services by strengthening the conditions of competition in the provision of cross-border payment services;

– the impact of the application of this Regulation on charges levied for payments made within a Member State;

– the advisability of increasing the amount provided for in Article 6(1) to EUR 50 000 as from 1 January 2006, taking into account any consequences for undertakings.

This report shall be accompanied, where appropriate, by proposals for amendments.

The review process of Regulation 2560 has involved a number of different elements. It started in 2004, when the Commission launched a tender and awarded a contract to an independent consultant, Retail Banking Research Ltd. (RBR), to study two aspects: the impact on charges levied for payments made within a Member State and a more general analysis on competition for cross-border payment services.[7] Both studies were published in September 2005 on the Internal Market and Services DG internet site.

4 From 1 January 2006, when the Regulation entered into force, this threshold was set at EUR 12 500 level.

5 Defined as 'Cross-border electronic payment transactions being the cross-border transfers of funds effected by means of an electronic payment instrument, other than those ordered and executed by institutions; cross-border cash withdrawals by means of an electronic payment instrument and the loading (and unloading) of an electronic money instrument at cash dispensing machines and ATMs at the premises of the issuer or an institution under contract to accept the payment instrument.'

6 Defined as 'Cross-border credit transfers being transaction carried out on the initiative of an originator via an institution or its branch in one Member State, with a view to making an amount of money available to a beneficiary at an institution or its branch in another Member State; the originator and the beneficiary may be one and the same person.'

7 *Study of the Impact of Regulation 2560/2001 on bank charges for national payments* and *Regulation 2560/2001: Study of Competition for Cross-border Payment Services*. Both studies were

In order to collect information on the impact of Regulation 2560 directly from stakeholders, a questionnaire was distributed in June 2005 to Member State authorities, financial institutions, merchant associations as well as consumer organisations in all EU Member States. The main results of the RBR studies and of the questionnaire were incorporated into the *Consultative Document to contribute to the Preparation of a Report on the Application of Regulation (EC) No 2560/2001 on Cross-border Payments in Euro*, which was published and opened for consultation on 19 October 2005. The Consultative Document was discussed in the Commission's two existing consultative committees on retail payments, PSGEG[8] and PSMG[9]. The results of these consultations were subsequently analysed by the Commission. All written contributions which were not indicated as confidential were published on the Internal Market and Services DG website.

3. DIFFICULTIES ENCOUNTERED IN APPLICATION OF REGULATION 2560

3.1. Geographic scope of application

In order to clarify issues relating to the extension of Regulation 2560 to SEK, the Commission issued an interpretative note.[10] It is useful to emphasise that there is no link between charges applied to euro payments and SEK payments; they can be subject to very different fees. It is the principle of non-discrimination between cross-border and domestic payments which is maintained: e.g. a Swedish bank executing a payment in SEK between Stockholm and Brussels should apply the same charges as for a corresponding SEK payment from Stockholm to Gothenburg.

Table 1: Scope of Regulation (EC) No 2560/2001 on cross-border payments in euro (as of 30 June 2007)

Countries or territories	Euro coins and notes	Regulation 2560/2001 (text with EEA relevance)
Belgium, Germany, Ireland, Greece, Spain, France, Italy, Luxembourg, Netherlands, Austria, Portugal, Slovenia, Finland	Yes	Yes
Bulgaria, Czech Republic, Denmark, Estonia, Cyprus, Latvia, Lithuania, Hungary, Malta, Poland, Romania, Slovakia, Sweden, United Kingdom	No	Yes, for the euro Optional (Article 9) for national currencies; by decision of the Swedish authorities applies to Swedish kronor (SEK)

published in September 2005 on the European Commission Internal Market and Services DG internet site.

8 Payment Systems Government Expert Group.

9 Payment Systems Market Group.

10 http://ec.europa.eu/internal_market/payments/docs/reg-2001-2560/reg-2001-2560-article9_en.pdf

Countries or territories	Euro coins and notes	Regulation 2560/2001 (text with EEA relevance)
Monaco, San Marino, Holy See (Vatican City State)	Yes (special coins)	No
Andorra, Montenegro, Kosovo	Yes	No
French overseas departments (French Guiana, Guadeloupe, Martinique, Réunion), Saint Martin, Saint-Barthélemy	Yes	Yes
Azores, Canary Islands, Madeira	Yes	Yes
Overseas territories (listed in Annex II to the EC Treaty)	Depends on decisions in country to which they are attached	No
Channel Islands, Isle of Man	No	No
Guernsey, Jersey	No	No
Gibraltar	No	Yes, for the euro
Faeroe Islands	No	No
Iceland, Liechtenstein, Norway	No	Yes, for the euro
Switzerland	No	No

Source: European Commission

3.2. Credit transfers

Credit transfers are by far the most disputed category of payments under Regulation 2560. The difficulties related to the pricing and execution of transfers are also reflected in the answers to the Consultative Document from 19 October 2005 and often indicated by consumer organisations, e.g. BEUC. Many enquiries result from common misunderstandings surrounding the Regulation.[11] Nevertheless, from 1 July 2003 a number of genuine problems have emerged, too.

It should be noted that the use of all three cost options ('OUR', 'BEN', 'SHARE') is covered by Regulation 2560. There is no rule in Community law giving preference to one over the other. However, the principle of equality of charges in Regulation 2560 states that charges at both ends of the credit transfer (i.e. for the originator and for the beneficiary) have to be the same as for corresponding national payments. Domestic (national) transfers in euro area countries are generally executed by default as SHARE, with no other cost options available. In most situations cross-border transfers within the euro area should be therefore also executed by

[11] Section 4 of the report and of this Annex briefly describe the impact of the Regulation on the consumer awareness.

default as SHARE (no other cost option should be proposed to customers). The situation is usually different in non-euro area countries, where OUR, SHARE and BEN cost options are frequently offered for domestic euro transfers. In this case charges for cross-border payments in euro should correspond to the prices for domestic transfers in euro, accordingly for each cost option.

Turning to more specific country issues, there was a particular difficulty in Spain, where national credit transfers were executed as 'OUR', i.e. a bank of the sender paid a fee to the recipient's bank to 'remunerate' it for its service. When a transfer was sent by a bank from another Member State, the receiving bank in Spain, which could not receive a fee from the sending bank, took its remuneration from the beneficiary. This discriminated against customers who received transfers from other Member States, and was considered an incorrect implementation of the Regulation. The Commission and the Bank of Spain held several meetings to find a solution to this problem. In April 2005, the Bank of Spain distributed a circular indicating to Spanish banks that they were not permitted to take different fees for national transfers and cross-border transfers in euro and, since October 2006, credit transfers in Spain are executed as 'SHARE'.

3.3. Cash withdrawals in ATMs

A problem of euro withdrawals in non-euro area countries appeared when one UK ATM operator started offering withdrawals of euro notes through cash machines in the UK. The question arouse whether the new service offered by this ATM operator to UK cardholders with sterling accounts – i.e. the possibility for these customers to withdraw euro notes from cash machines in the UK – would be subject to the Regulation.

3.4. Card payments

As confirmed in the *Note on practical implementation of Article 3 of the Regulation No 2560/2001 on cross-border payments in euro*[12], the principle of equality of charges introduced by the Regulation is also applicable to the Merchant Service Charges (MSC). MSC is a fee paid usually for each transaction by a merchant to an acquirer, who processes the merchant's transaction through the network and obtains the funds from the cardholder's bank. Though no difficulty was encountered when applying the Regulation to MSC, the structure of fees for card payments and characteristics of the supply side (merchant-acquirer relations) in some Member States raise concerns about the degree of competition in the provision of card payments services (see Section 9 of the report and Section 7 of the Annex).

3.5. Competent authorities and out-of-court redress bodies

Though Recital 13 illustrates that there should be procedures for the treatment of complaints and the resolution of disputes ("…the Member States should ensure that there are adequate and effective procedures for lodging complaints or appeals for settling any disputes between the originator and his institution or between the beneficiary and his institution, where applicable using existing procedures…"), the recital alone, not being accompanied by an article, does not involve any real obligation for Member States.

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12 MARKT 2902/2002; http://ec.europa.eu/internal_market/payments/docs/reg-2001-2560/reg-2001-2560-article3_en.pdf.

The review process and received complaints revealed wide discrepancies as regards powers and practices of existing schemes, questioning in some cases their ability to effectively solve Regulation-related cross-border disputes. This included e.g.:

- Complaints accepted only in the official language (e.g. France, Netherlands, Poland)
- Low maximum limits of the disputed amounts (e.g. Poland, Portugal)
- Conciliation bodies that cannot take binding decisions (e.g. Finland, France, Sweden, Spain) or charge substantial amounts for their services (e.g. Poland, Latvia).
- Fragmented and/or not transparent out-of-court redress system making it difficult and time-consuming to lodge a complaint (e.g. Portugal, France, Germany);
- Lack of alternative dispute resolution bodies specialised in financial services (e.g. Portugal, Lithuania, Estonia);

Member States were also asked to indicate whether they have decided to establish or appoint competent authorities for the purposes of the Regulation. Based on these responses, in a number of cases when it appeared that a general problem of erroneous application of the regulation was emerging, the Commission informed the complainant about the details of the supposed national competent authority and contacted them itself. Even then, some competent authorities indicated that they do not deal directly with disputes, even if it appears that there was an infringement of the Regulation.

4. CONSUMER AWARENESS OF REGULATION 2560

Customers appear to receive the necessary information about any modification in the applicable charges, too. The same distribution channels (as for the provision of original information) are used for this purpose. Nonetheless rules surrounding the date when any modification takes effect differ considerably between countries. In Italy and in Germany, for example, in some specific cases the information on modification of charges may be available only when the change has already taken effect. In Sweden customers should be informed about any modification of charges at least 14 days prior to the modification taking effect or 'in reasonable time' where cards and ATM charges are concerned. In contrast, in France the information should be communicated to the customer three months in advance of the scheduled date.

As demonstrated by the surveys (i.e. Flash Eurobarometer 193 of September 2006 and upcoming Flash Eurobarometer 216)[13] the knowledge of the Regulation existence and rules among the general population is low. Only around 25% of the surveyed consumers (euro area Member States except Slovenia) answered that they are no additional fees applied for cross-border transfers, ATM withdrawals and card payments in comparison to corresponding national operations. In contrast, over 50% of those surveyed expressed their total ignorance as regards charges for cross-border payments. It seems that only those groups of consumers directly interested in cross-border payment services (e.g. people working or studying in other Member States) may have a better awareness of the Regulation.

[13] http://ec.europa.eu/public_opinion/flash/fl193_en.pdf

This low level of consumer awareness has its reflection in the misunderstandings and confusion that occur, particularly when cross-border credit transfers are concerned. Some typical issues may be identified:

- Use of other cross-border payments instruments and payments in other EEA currencies. Some consumers are convinced that the provisions of Regulation 2560 cover all EEA currencies and apply to all cross-border payment instruments in use (e.g. cheques).

- Free of charge cross-border credit transfer. In some Member States of the euro area sending a domestic credit transfer is free of charge (or, in fact, the cost is included in the account service fees paid monthly, quarterly or yearly). By analogy some consumers are expecting that the same situation takes place in every Member State and argue that their cross-border transfers executed in these countries should be free of charge, too.

- Transfer from euro to non-euro Member States. In contrast to the euro area, where charges on incoming transfers are rare, incoming transfers in the non-euro area Member States are usually charged. The misunderstanding stems then from the false beneficiary interpretation of the 'full amount transferred' principle (understood as no charges should be applied even in the separate transaction) and from the payer belief, that the amount will be received free of charge. Currency conversion fees usually add to the confusion.[14] Furthermore, in many cases consumers from non-euro countries compare the cost of cross-border euro transfers to the cost of domestic transfers in their national currency.

Finally, one source of confusion is related to the already discussed problem of a cost option (OUR, SHARE and BEN). It should be noted that, when different charging options are proposed to the consumer, lack of information on charges faced by the beneficiary when using SHARE cost option may be seen as an incentive to choose a more expensive OUR option.[15]

5. IMPACT OF REGULATION 2560 ON CHARGES FOR CROSS-BORDER PAYMENTS

The costs of cross-border credit transfers in the euro area have fallen significantly since the entry into force of the provisions of Article 3(2) of the Regulation. The costs of a EUR 100 transfer in the twelve euro area Member States (Slovenia excluded) have decreased from average EUR 23.60 in 2001 to average EUR 2.46 in 2005.[16] In four Member States – Austria, Belgium, Germany and the Netherlands – regulated cross-border credit transfers do not incur any fees. In contrast, banks in Greece, Spain, Italy and France charge fees in excess of the euro area average.[17]

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[14] When the account of the originator (or of the recipient) is not in euro, the bank of the originator (or of the recipient) may charge an exchange fee (currency conversion) in addition to the service fee for the transfer. Exchange fee operations are not covered by this Regulation and the banks are free to determine the charges for such operations.

[15] Banks are logically obliged to provide information on their own tariffs and not on those used by other institutions.

[16] For more information please refer to the *Commission Staff Working Document addressed to the European Parliament and to the Council on the impact of Regulation (EC) No 2560/2001 on bank charges for national payments*, SEC(2006) 1783: http://ec.europa.eu/internal_market/payments/docs/reg-2001-2560/report-2007_01_11_en.pdf

[17] Spanish banks typically charge 'ad valorem' fees, which means that regulated transfers of EUR 50 000 could well cost around EUR 200. The same price policy is applied by some Greek banks.

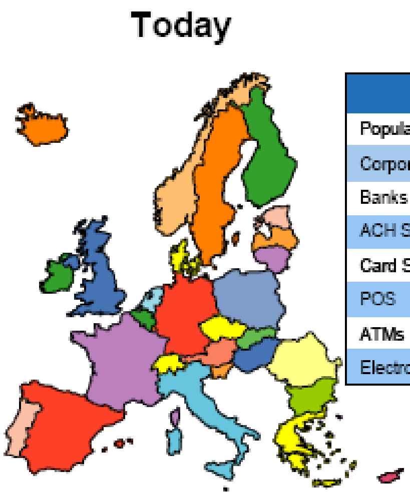
The costs of cross-border card payments have not changed since the introduction of Regulation 2560. Cardholders are not charged any fees per transaction in 19 of the 25 EU countries (credit and charge cards), including all euro area Member States.[18] Where a fee is charged, it varies from 0.1% to 0.7% in the MasterCard network and from 0.5% to 0.7% in the Visa network.[19]

In addition, Merchant Service Charges followed a slight downward trend, though this development cannot be attributed to the Regulation. The issue of surcharging, discussed before, does not fall within the scope of this Regulation.

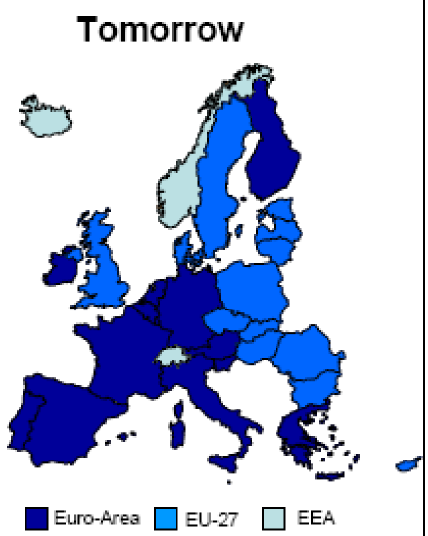
6. CHANGES IN CROSS-BORDER PAYMENT SYSTEM INFRASTRUCTURES

6.1. Single Euro Payments Area (SEPA)

Graph 1: The scope of SEPA



	13 euro	31
Population	315m	504m
Corporates	17m	25m
Banks	6-7k	9k
ACH Schemes	11	20+
Card Schemes	14+	18+
POS	4.6m	6.7m
ATMs	240k	339k
Electronic transactions	50bn	73bn*



Today – Different Country Implementations	Tomorrow – Harmonised SEPA
• National / local solutions	• Common solutions with additional optional services
• Different schemes, experiences, standards, consumer protection laws	• Common core payment instruments and experiences, consistent standards, application of harmonised consumer protection laws
• No interoperability of national schemes	• Improved interoperability
• Different country implementations	• Harmonisation and consolidation
• Cross-border complexity and risk	• Reduced complexity, improved efficiency

* Not all euro transactions

Source: *Making SEPA a Reality. Implementing the Single Euro Payments Area*, EPC, April 2007.

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18 Annual fees for cards were discussed in the report on bank charges for national payments.

19 DG Competition *Report on the retail banking sector inquiry*, p. 108–109: http://ec.europa.eu/comm/competition/antitrust/others/sector_inquiries/financial_services/retail.html.

The SEPA project is a set of interbank rules, practices and standards. The relationship between banks and their customers is, for competition reasons, left to individual credit institutions and/or banking communities.

The EPC has planned its timeline for the SEPA project around three main phases: a design phase (2002–2006), an implementation phase (2006–2007) and a migration phase (from 2008 onwards).[20]

The first tasks of the EPC related to the immediate need of cost-effective processing, clearing and settlement of Regulation 2560 compliant credit transfers. In April 2003 EPC adopted two inter-bank agreements, Credeuro and Interbank Convention on Payments (ICP)[21], setting standards for the execution of basic cross-border credit transfers in euro. The adherence to the conventions is voluntary, but they were widely adopted by the EU banks. The Credeuro Convention is a low cost, end-to-end scheme for basic STP (Straight Through Processed i.e. fully automated, including IBAN and BIC codes) credit transfers up to EUR 50 000, where the beneficiary is credited within three business days and the cost option used is SHARE. The IPC Convention sets rules for interbank charging for Credeuro-specified transfers, suppressing beneficiary deduction practices and replacing them by interbank charges.

At the same time the EPC has selected STEP2 as a first PE-ACH (Pan-European Automated Clearing House) operator. STEP2 is a network for clearing and settlement[22] of credit transfers in euro compliant with Credeuro criteria. It was developed by the Euro Banking Association (member of the EPC) and is run by an autonomous company, EBA Clearing.

The proper design phase for SEPA started in 2004 and is now close to being finalised. This phase involved the design of the new, pan-European credit transfer and direct debit schemes and the adaptation of existing schemes for card payments to a new set of business and technical standards – the SEPA Card Framework. A framework for clearing and settlement infrastructure providers, based on principles of reachability of all euro area banks and a separation of schemes and infrastructures, has also been developed. The separation will allow infrastructure providers to compete and offer their processing services to any bank or card scheme provider, situated not only in the euro area, but also within other EU/EEA Member States.

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20 The following paragraphs are based mostly on the brochures *The Single Euro Payments Area (SEPA): An Integrated Retail Payments Market*, ECB, February 2007 and *Making SEPA a Reality. Implementing the Single Euro Payments Area*, EPC, April 2007.

21 Known also as Interbank Charging Principles Convention.

22 Settlement takes place in EURO1 system.

SEPA CREDIT TRANSFERS

The SEPA credit transfer (SCT) scheme defines a common set of rules and processes for credit transfers denominated in euro. The scheme defines a common service level and a time frame under which financial institutions participating in the scheme must as a minimum conduct SCTs.

Features of the SCT scheme

- There is SEPA-wide reachability – any customer should be able to receive and send SCT transactions;
- There is no limit on the value of the payment;
- The maximum execution time is three business days;
- The scheme is separated from the processing infrastructure;
- IBAN and BIC are used as account identifiers;
- There is a comprehensive set of rules for rejected and returned payments.

SEPA DIRECT DEBIT

The SEPA direct debit (SDD) scheme defines a common set of rules and processes for direct debits denominated in euro. The scheme defines a common service level and a time frame stating when financial institutions participating in the scheme must as a minimum be able to act in their role as debtor (sending) banks.

Features of the SDD scheme

- It offers full SEPA-wide reach on the debtor side – any debtor can sign up for SDD participation
- It covers both recurrent and one-off payments in euro;
- Mandates are handled by creditors;
- The maximum execution time is five business days for the first payment, and two business days for recurring payments;
- It offers a separation of scheme and processing infrastructure;
- IBAN and BIC are used as account identifiers;
- It ensures a comprehensive set of rules for rejected and returned payments;
- A solution for an electronic mandate is under development.

SEPA CARD FRAMEWORK

SEPA card payments will take place according to a set of high-level principles which issuers, acquirers, card schemes and operators will have to adapt to.

Features of SEPA card payments

- Cardholders can pay with one card all over the euro area (limited only by brand acceptance by merchants);
- Merchants can accept any card compliant with the SEPA Card Framework;
- Payment card processors and other service providers will be able to compete with each other and offer their services throughout the euro area, making card market more competitive and cost-efficient.

Source: *The Single Euro Payments Area (SEPA): An Integrated Retail Payments Market*, ECB, February 2007.

The second phase, the implementation phase, started in mid-2006 and will continue until end-2007.This phase of the project concentrates on preparation for the roll-out of the new SEPA instruments, standards and infrastructures. National implementation/migration bodies that have now been established in each euro area country will assist by monitoring the different stakeholders' preparations for SEPA roll-out. These stakeholders are very diverse, consisting of a number of parties such as banks, infrastructure operators, public administrations, companies and other users.

The final phase will be a migration period, in which national payment schemes will coexist with the new SEPA schemes. Customers will be offered both 'old' national and new SEPA instruments, and the clearing and settlement infrastructures will be able to process payments made using both types of instruments. The goal is to achieve a gradual market driven migration to SEPA, so that by end-2010, a critical mass of transactions has migrated.

6.2. Payment Services Directive (PSD)

The Directive has two main objectives:

The first objective is to generate more competition in payment markets by removing market entry barriers and guaranteeing fair market access. Currently, the diverging legal rules in 27 different Member States represent a significant impediment to new payment service providers (such as supermarkets, money remitters or, in some cases, telecom or IT providers), and effectively block them from competing and offering their services throughout the Internal Market.

The second objective is to provide a simplified and fully harmonised set of rules with regard to the information requirements and the rights and obligations linked to the provision and use of payment services.

Some of the most important rules in the PSD cover:

- Execution time: all credit transfers without any currency conversion must mandatorily be carried out at the latest by the end of the next business day (i.e. the so-called 'D+1' basis).

- Liability of a payment service provider in case of non-execution or defective execution of a payment transaction.

- Liability of payment service user in case of misuse of a payment instrument (limited to EUR 150). This amount may be reduced by Member States and there is no liability for unauthorised payments occurring after the user has properly notified his/her payment service provider.

- Introduction of the full amount principle according to which the full amount specified in a payment order shall be credited without any deduction to the beneficiary.

- Conditions for refunding.

- Irrevocability of payment orders (e.g. the ability of the payer to stop the execution of a payment after it has been received by the payment service provider).

6.3. The impact of SEPA and PSD on the Internal Market

Consumers should be able to benefit from increased simplicity and convenience of making payments (the effect of SEPA), as well as from price and information transparency (as a result of PSD). Due to increased competition, arrival of the new payment institutions and thanks to market transparency, charges for standard payment services in a number of high-cost euro area countries are likely to gradually decrease.[23] Furthermore, as quoted earlier, consumers would be able to use their debit cards anywhere in the euro area[24] as conveniently as in their residence country and to draw on cross-border direct debits to pay their bills.

Banks will be able to lower their costs of processing payments, thanks to the efficient pan-European infrastructures and effects of scale as well as owing to improved access to all national markets. They would have the possibilities of additional income generation on optional services like e-invoicing. Corporates would be able to consolidate their payments and handle them cost effectively from one single European location. Furthermore use of optional services, like e-invoicing and e-reconciliation, could lead to substantial savings for them. For smaller businesses (SME) simplified processing will most likely improve cash flow management and reduce costs. It should enable them to receive or make payments anywhere within euro area as easily as within their own country. Further on, as said before, SEPA and PSD are together expected to increase competition among the providers of payment services. This would mean more choice, lower costs and better service for merchants. Finally, for governments and public administrations, the common schemes will enable the delivery of improved services to citizens at home and abroad.

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23 The Commission will closely monitor the SEPA-related price developments in all EU countries.

24 Technical ability, as card acceptance would depend on the individual merchants' decisions.

Table 2: Scope of the SEPA, PSD and Regulation 2560 (as of 30 June 2007)

	Currency	Geographical Area
SEPA	Euro	EU 13; EU 14, EEA 3, EFTA 1 (for euro payments)
PSD	All EU currencies	EU 27 Possibly EEA 3 (pending the decision of the EEA Joint Committee)
Regulation 2560	Euro and Swedish kronor; optional for other EU currencies	EU 13; EU 14, EEA 3 (for euro and SEK payments)

Explanations:
EU 27 – all EU Member States, EU 13 – euro area Member States, EU 14 – non-euro area Member States, EEA 3 – Iceland, Liechtenstein and Norway, EFTA 1 – Switzerland
Source: European Commission

6.4. SEPA, PSD and Regulation 2560: the direct debit issue

Direct debits constitute around 25% of all non-cash payments in the EU.[25] This instrument may become very useful for all European citizens paying regular bills in another EU country, e.g. those possessing secondary residences or holiday apartments.

[25] EU-25. For comparison: credit transfers 28%, card payments 32%, cheques 13%, other instruments around 2%. Source: ECB Blue Book 2006, http://www.ecb.int/pub/pdf/other/bluebook200612addenden.pdf.

7. ADVISABILITY OF IMPROVING CONSUMER SERVICES BY STRENGTHENING THE CONDITIONS OF COMPETITION

7.1. Results of the inquiry into the European retail banking sector[26]

Barriers to entry into the payments market. Payment systems in the EU are still in the phase of transition towards modern infrastructures and new SEPA rules and procedures. This means that banks and other institutions offering cross-border payment services in different Member States have to join various national systems, adapt to different standards and face different costs. In most EU Member States there is one national clearing infrastructure, which is operated either by the central bank or by a membership association controlled by the main banks in the country. Operators of the established infrastructures are potentially in a position to create entry barriers which may take a variety of forms. In particular some membership rules (e.g. local presence requirement or 'need to be a bank') and the way the fee system is structured (e.g. high level of joining fees, per transaction fees based on the volume of payments) may raise barriers to entry for new or small players. Furthermore, in Member States where interchange fees for credit transfers and direct debits are agreed upon, such fees may distort competition between different means of payment and competition in the provision of payment services to customers, as banks have an incentive to promote the use of payment means with high interchange fees.

High variations in card fees across the EU. As mentioned already in Section 5, the structure of fees for card payments raises competition concerns. There is a substantial discrepancy in merchant[27] (including multilateral interchange fees, MIF) and cardholder fees across the Member States and card schemes. In 2004, the interchange fees on Visa and MasterCard credit cards in some Member States amounted to 1.5% of the transaction value or over two-and-a-half times more than in some other Member States. For MasterCard and Visa debit cards (Maestro and V-Pay/Visa Electron) average interchange fees in some Member States could be three to four times higher than in other Member States. Evidence shows that in contrast to Visa and MasterCard most domestic card networks set very low or zero interchange fees on debit card transactions, resulting in generally low merchant fees.

Following the pattern of interchange fees, merchant fees for Visa/MasterCard credit cards in some Member States were more than three times the level of fees in others. Moreover, small merchants paid on average 70% more for card acceptance than large merchants. A comparison of price differentials between large and small merchants in the international schemes (MasterCard/Visa: 70% on average) with those in domestic debit systems (7% on average) suggests that scale may not be the decisive factor in such pricing policies. It could be that smaller merchants pay a premium for accepting MasterCard and Visa cards. If that were true, the differentiation of prices according to the size of the merchant could be a measure for the exercise of market power by banks within a given system.

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[26] The report is available at: http://ec.europa.eu/comm/competition/antitrust/others/sector_inquiries/financial_services/retail.html.

[27] Merchant Service Charges (MSC) or merchant fees consist of two elements, Multilateral Interchange Fees (MIF) and Acquirer Bank Fees. MIF for credit card payments in international networks of Visa and MasterCard could constitute as much as over 80% of MSC.

Although payment markets in Member States show very different degrees of maturity, fee differences of such magnitude could be explained by the presence of competition barriers.

As far as cardholder fees were concerned, average levels of cardholder fees charged by Visa and MasterCard in a particular Member State tended to be similar, though levels could vary substantially across Member States. Average annual fee for MC and Visa credit cards amounted to EUR 23 and EUR 24, respectively, but could reach over EUR 50 in some countries and below EUR 10 in others. For debit cards, average fees for national debit schemes amounted to EUR 9, for Maestro EUR 10 and for Visa Electron EUR 11. In addition, there was no strong relationship between the level of the cardholder fee and the level of the interchange fee in the markets. An econometric estimation made by DG Competition showed that if the interchange fee increases by EUR 1, typically only 25 cents are passed on to consumers in lower fees. These findings challenged the hypothesis that an increase in interchange fees is fully offset by reductions in cardholder fees.

Network rules, membership fees, preferential bilateral interchange fee agreements. Card acquirers in a number of Member States (e.g. France, Belgium, Denmark, Hungary, Ireland and Portugal) apply blending[28] to competing products both in domestic and international card payment systems. The results of the inquiry suggest that blending of prices may weaken inter-network price competition, which in turn leads to retailers paying higher fees.

Both Visa and MasterCard prohibit co-branding[29] with networks which are deemed competitors. This may deter national debit card payment systems from entering into competition with MasterCard and Visa or impede retailers and other operators from entering into competition with the incumbent card issuer.

By concluding and acting on a basis of 'preferential bilateral interchange agreements', institutions in some Member States, involved in both card issuing and acquiring activities, may indirectly obstruct new entries into the acquiring market by not applying the same favourable conditions to newcomers, usually cross-border acquirers. Preferential bilateral interchange agreements ('on-us' interchange fees)[30] existed at least in Portugal, Belgium, Austria, Spain and United Kingdom.

Similarly, the prohibition for merchants to charge customers a usage fee, 'surcharging', in many networks may hinder the development of more efficient payment instruments as the true costs are hidden to the consumers via cross-subsidisation. The surcharging prohibition may constitute a barrier to entry for alternative non-cash payment instruments, such as mobile phones or e-money.

[28] Blending is a practice of charging merchants a global price for accepting cards of different types (debit/credit) and/or issued by different networks, without distinction between interchange fee levels.

[29] The definition of 'co-branding' may vary across card networks. It generally refers to the presence of the logo of the card network and a second logo (of another network or a non-bank) on the face of the card.

[30] Transactions under preferential fees or 'on-us' transactions have place where the issuer and acquirer are the same or belong to the same group.

7.2. Way forward

It must be highlighted that many of the competition barriers that the sector inquiry has found should be remedied through the establishment of SEPA and thanks to the implementation of the Payment Services Directive. For example, payment card networks and clearing and settlement systems should not be able to distort competition by imposing discriminatory rules and governance arrangements in the SEPA/PSD environment. The SEPA framework for payment cards should provide retailers with greater choice of suppliers for acquiring services, opening up greater competition in this highly concentrated market.

The Payment Services Directive prohibits access restrictions to payment systems and infrastructures based on institutional status.[31] As the PSD introduces a harmonised set of rules for payment providers throughout the EU, it will reduce legal compliance costs for payment service providers and foster competition between payment services, as well as allow payment service users to shop around on the basis of an informed choice. Its implementation will enable citizens to benefit from more competitive and efficient payment services.

Furthermore, in some markets steps have already been taken by the industry to modify the structures and the rules and remove entry barriers. For example, Austrian banks have agreed to review arrangements for setting interchange fees and announced that a reduction can be expected. They will also take steps to foster genuine competition in acquiring. In Portugal issuers and acquirers have met some of the Commission's concerns by reducing domestic interchange fees and removing preferential bilateral domestic interchange fees. These initiatives in Austria and Portugal are welcomed first steps.

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[31] However, this does not apply to payment systems designated under the Settlement Finality Directive, to three party card schemes and to three party card schemes with licensees as long as the licensees do not have any right to negotiate fees between or among themselves.

8. NATIONAL REPORTING OBLIGATIONS FOR BALANCE OF PAYMENTS STATISTICS

8.1. Regulation 2560 vs. balance of payments statistics

Under the Regulation (EC) No 184/2005 on Community statistics and according to the subsidiarity principle, national authorities of the Member States are completely free as to the choice of the compilation method.[32] The techniques used for the compilation of these statistics must however strike the right balance between cost of data collection to all respondents and the required quality and timeliness of the statistics[33].

8.2. Balance of payments collection systems in the Member States

Data collected through bank settlements systems are the most vulnerable to the level of the exemption threshold provided in the Regulation. This vulnerability decreases as the relative share of the transactions directly collected from non-banks (including enterprises) increases, because the threshold is not meant to be applied to them.

At the end of 2006 ten Member States operated a full survey system (i.e. without the use of any bank settlement data). In addition, six countries operated mixed systems in which at least 50% of the BoP items were collected by surveys complemented with bank settlements reports. In contrast, only four countries collected BoP data mainly through bank settlements. One of those Member States expected to launch a full survey system in 2008, whereas another decided to reconsider the future of its collection system once the decision to raise or remove the exemption threshold is reached. Finally seven Member States were running direct reporting systems relying partially on bank settlements. All of them were planning to progressively widen the scope of direct reporting by enterprises and surveys and limit the use of bank settlements data.[34]

It should be noted that the introduction of the Regulation may have already influenced the quality of balance of payment reporting in those Member States that still strongly rely on bank settlements for the compilation of payments statistics. Many of the banks participating in the Regulation 2560 review process shared a belief that the Regulation had an impact on transfer patterns i.e. confirmed that splitting of payments takes place in order to keep the amounts below the threshold. Consumer associations were also encouraging the public to split large transfers in order to save money.

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32 Article 3(1) of Regulation (EC) No 184/2005: 'Member States shall collect the information required pursuant to this Regulation using all the sources they consider relevant and appropriate. These may include administrative data sources such as business registers.'

33 When moving to a survey system for data collection, the respondent costs are shifted from the banks to the corporations surveyed. Companies only report on their own business, while banks are reporting on a very large number of transactions passing through their systems. Conversely, in a settlement system a limited number of banks provide the information that otherwise may have to be collected from a very large population of companies, which would have to adapt their individual information systems.

34 All the above data are based on a confidential report of the Committee on Monetary, Financial and Balance of Payments Statistics (CMFB). References to the individual Member States have been removed.

8.3. Reporting obligations and the Single Euro Payments Area

As said before, a number of EU countries still collects balance of payments statistics (at least partially) from bank settlements. In such reporting systems, all or most payments that imply movements in accounts abroad need to be reported to the National Central Bank by the banks providing payment services. Reported data usually include all information on the incoming and outgoing payments above the reporting threshold. Such information includes the identification of the person/company ordering the transaction, economic classification of the transaction, currency of denomination, and the country of the beneficiary. The cost of the reporting for the banks is usually higher for incoming payments because the recipient must be contacted to know the nature of the payment (e.g. goods or services). According to some estimates from credit institutions, this work accounts for at least 25% of the cost of an international payment.[35]

The European Payment Council and banks have on numerous occasions expressed deep concerns that continued BoP reporting requirements would perpetuate a distinction between today's domestic and cross-border transactions and require costly statistical arrangements to be retained. In fact, it is difficult to imagine how such system would work without putting on hold the whole SEPA project.

It is important to indicate that further investigations (unrelated to the Regulation) on other existing national reporting obligations (e.g. for tax purposes or with respect to the detection of money laundering) seem necessary to assess the extent to which these reporting requirements are affected by SEPA. It is also practical to verify to what extent other reporting obligations should be adapted, or could be a supportive, new source for BoP information.

8.4. Advisability of increasing or removing the reporting threshold

An assessment of how other national reporting obligations (e.g. related to tax obligations or anti-money laundering policies) may be met in the context of SEPA will be undertaken by the Joint Task Force on the Use of Payments Data for Balance of Payments Statistics (PBOP-TF), organised by the European Central Bank.

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[35] A study on the Regulatory burden in Germany, produced in 2006 by Institut der deutschen Wirtschaft, Köln, estimates that the yearly costs of all statistical reporting by German banks reach the level of EUR 250 million.