

AIB GLOBAL TREASURY SERVICES

## Topic of the Day

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### SINGLE EURO PAYMENTS AREA (SEPA)

*TIME TO WAKE UP !*

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# Single Euro Payments Area (SEPA)

## *Time To Wake Up!*

### What is SEPA ?

**S**EPA is a project designed to significantly increase competition for goods and services within the European Union internal market by providing businesses and consumers with access to faster, more efficient and cheaper euro payment services.

The EU Commission is convinced that the ability of the EU internal market to grow and become more competitive is hindered by a fragmented payment services industry. They believe that competitiveness within the EU economy will only improve when, in Ireland for example, businesses and consumers can make a payment between Dublin and Madrid as easily as from Dublin to Mallow.

The Commissioner for the EU Internal Market, Mr. Charles McCreevy, is on record as expressing his frustration at the fact that goods can be physically moved across Europe in one or two days but that the payment in relation to these goods can take between 3 and 5 days.

The SEPA project can simply be described as the creation of a payments market that enables businesses and consumers to make and receive euro payments within the EU as cost effectively and efficiently as they make their current national payments. The intention is that the new payment services will emulate the best national payment systems.

The SEPA project envisages that national banking communities in Europe will move away from their current national payment systems and replace them with a single pan-European system.

### How Big is the SEPA Project?

The SEPA project has been described as the biggest financial industry project ever undertaken. It will have a bigger impact on European businesses than the Y2K project or the introduction of Euro notes and coins in 2002.

In 1999 the project to create the euro mainly impacted on the banking industry in 12 countries. The banking industry in these countries had to bear the cost of integrating their systems to facilitate the settlement of euro transaction at the wholesale interbank level.

The launch of euro notes and coins and the introduction of the euro as the domestic currency in 12 EU countries in 2002 was a project, the impact of which, was largely borne by the banking and retail industry.

The availability of euro notes and coins facilitated the settlement of euro transactions at the retail level in these countries.

The scale of the SEPA project is much bigger as it seeks to establish a Single Euro Payments Area in the 25 EU member states, 3 EEA states (Iceland, Liechtenstein and Norway) and Switzerland. The project is the final stage of the EU's overall euro project as it will create an infrastructure that will facilitate the settlement of commercial euro transactions, both national and cross border, in the above detailed 29 countries.

The project envisages that businesses and consumers will be able to use euro payment instruments such as credit transfers, direct debits and debit/credit cards as easily within the SEPA countries as they can currently in their national market.

The SEPA project envisages that national banking communities will move away from their current national payment standards and replace them with pan-European standards. In Ireland, for credit transfer and direct debit transactions, this would involve a move from the current national standard based on National Sort Code (6 digits for bank identification) and Account Number (8 digits) to the new pan-European standard. The new standard is based on SWIFT Bank Identifier Codes (BIC – 8/11 character alpha-numeric code) and International Bank Account Identifier (IBAN – 22 character alpha-numeric combination in Ireland).

The scale of the change, envisaged by the SEPA project, should not be underestimated either by the banking industry or their customers.

## How is the SEPA Project Progressing in Ireland?

Ireland, a country whose base currency is the euro, has already been impacted by the SEPA project.

Many Irish banking customers are already experiencing some of the benefits of the SEPA project, as they are able to transfer amounts up to €50,000 across Europe for the same price as an equivalent domestic transfer.

The Irish banking industry is now embarking on the next stage of the project. This will involve the development of pan-European credit transfer and direct debit schemes for delivery on the 1<sup>st</sup> January, 2008. These schemes will enable banking customers to initiate transactions both nationally and cross border within SEPA based on the IBAN and BIC standards.

In addition, the banks are working to ensure that the debit and credit card services they provide will be acceptable across all the SEPA countries.

In the move to the new environment, many Irish banks have started to invest in technology and systems that will position them for the future. For instance, AIB Capital Markets recently became the first Irish bank to directly join Europe's only pan-European Automated Clearing House (PEACH) – the Euro Banking Association's STEP 2 clearing system. STEP 2 is the only pan-European clearing and settlement infrastructure that facilitates the easy settlement of routine euro payments with Europe.

Once the pan-European payment schemes are introduced, the next stage of the project will be to replace the existing national banking payment infrastructure with the new pan-European system. This will require increased investment from the banks but will also involve investment and change by most Irish businesses.

The Irish banking industry through the Irish Payment Services Organisation (IPSO) is working on developing a plan to facilitate the smooth transition from the existing national payment instruments to the new pan-European ones. At this stage, it is envisaged that existing national payment instruments will be retired in late 2009 at the earliest.

### What are the Practical Benefits of SEPA?

Some of the major benefits for bank customers are likely to be lower payment costs, faster execution times, no charges deducted directly from the payment and consistent payment initiation standards across Europe. In addition SEPA will deliver additional services not available currently e.g. cross border direct debits within the EU.

Another impact of the SEPA project is likely to be the withdrawal of cheques and other paper based products as a payment option. The European banking industry has clearly indicated that they have no intention, in this technological age, to develop a pan-European paper based clearing system. The Irish Payment Services Organisation (IPSO) has recently indicated its intention to stop providing cheques as a payment option to customers by 2010. Ireland remains a high user of cheques in Europe, whilst other countries have already moved to more efficient and lower cost electronic payment services.

In order to consider the impact of SEPA on customers it might be useful to look at some practical examples of the potential benefits:

Example 1

*An Irish bank customer goes to work for a German company in Munich. The customer no longer needs to move his bank account to a German bank. They can request that their German employer pay their salary to their bank account in Ireland by providing the employer with the BIC and IBAN details of their Irish bank account. They can provide a direct debit mandate to their German electricity utility enabling the utility company to collect their bill directly from the customer's account in Ireland. The debit card supplied by their Irish bank will be accepted by German retailers for purchases.*

Example 2

*A European health insurance company wishes to offer insurance products from a European base to consumers in Ireland. The company can obtain direct debit mandates from the Irish consumers for the insurance premium. The company can settle any claims directly and cheaply to the consumer's Irish bank account once they obtain the BIC and IBAN details of the account.*

Example 3

*An Irish company sets up a sales office in Paris. The company will no longer need to obtain a local bank account as sales invoiced from the office can be paid directly to the head office bank account in Ireland. In addition the company can pay its local staff and other expenses directly from their Irish head office bank account.*

These examples are, of course, hypothetical and may be impacted by other European legislation. However, they do demonstrate the ability of an integrated and efficient European payments industry, combined with other legal initiatives, to increase competition and efficiency in the EU internal market.

## How Should I Prepare for SEPA?

Firstly, businesses and consumers need to understand what the SEPA project is about. Secondly, they need to accept that this project will have an impact on them. Thirdly, they need to gain an understanding of the changes they need to make in order to benefit from the project.

The following checklist may assist;

Exporters/Sellers	Importers/Buyers
Do I sell in euro to any SEPA countries?	Do I buy in euro from any SEPA countries?
Do I have the IBAN and BIC details of all my bank accounts?	Do I have the IBAN and BIC details of my suppliers?
Do I include my IBAN and BIC details on all my invoices in accordance with EU legislation?	Have I updated my accounting and banking systems with the IBAN and BIC details of my suppliers?

**N.B.** Businesses sending or receiving any cross border euro payments within the EU will be required to provide the IBAN and BIC details of the receiver's account from the 1<sup>st</sup> January 2007.

Businesses that fail to provide these details will not be able to send payments to their European suppliers. Businesses that export into Europe will need to ensure that their customers are supplied with the BIC and IBAN details of their account (available on their bank account statement). Failure to do so is likely to delay payment with a negative impact on cashflow.

At some date before 31<sup>st</sup> December, 2010 the Irish banking community will have to adopt the BIC and IBAN standard for national payments. This will have an impact on every bank account holder in the country.

### What Help Can I Expect from My Bank in Relation to SPEA?

Banks will provide customers with advice on the impact of the SEPA project on their business. Banks will also assist customers to understand how SEPA offers opportunity for business growth and cost reduction.

Customers will experience an increasing level of communication from their bank in relation to SEPA in the coming months.. Initially this is likely to focus on increasing awareness of the need to supply the IBAN and BIC details of the receiver's account for all euro payments within SEPA.

Banks will update their customer interfaces to help customer's adopt to the new environment. For instance, AIB is planning to enhance its iBusiness Banking internet channel so that customers can easily update the existing account information they hold for the receiver of their payments to the new IBAN and BIC standards.

In the coming years, the banks will be actively promoting the new SEPA payment instruments and assisting customers in transitioning from the current national systems.

SEPA is a big challenge for the banks and their customers. However, the successful implementation of this project should provide opportunities for the banks and their customers to conduct business in an internal market of nearly 400 million people.

It really is time to wake up to SEPA.

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