The European payment landscape: TARGET2 and SEPA

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THE EUROPEAN PAYMENT LANDSCAPE: TARGET2 AND SEPA

AGENDA

- TARGET2: The integration process of large value payment systems in euro
- SEPA: The integration process of retail payment systems in euro
  - Initial thoughts
  - The building of SEPA
  - SEPA: a two-step approach – 2008 Milestones
  - SEPA: a two-step approach – 2010 Milestones
  - Final issues
TARGET2: THE INTEGRATION PROCESS OF LARGE VALUE PAYMENT SYSTEMS IN EURO

CONCLUSIONS

- The TARGET System is a successful precedent in the integration of large value payment systems in euro.

- The technical decentralization supporting the current TARGET functioning makes necessary to strengthen the integration process.

- TARGET2 tackles the shortcomings associated to the possibilities of TARGET to develop the integration process while will be able to provide a modern system with state of the art functionalities.
The current TARGET system

- Real-Time Gross Settlement System (RTGS) for euro large value payments
- TARGET is the result of the interlinking of the 15 national RTGS systems of the European Union member States plus the RTGS system operated by the European Central Bank
- TARGET went live in January 1999, at the same time as the start of the European Monetary Union

TARGET Objectives

- To serve the needs of the execution of the ESCB monetary policy
- To provide a safe and reliable channel for the processing of interbank and customer payments
- To contribute to the integration of the euro area money market

TARGET fulfils its objectives

- **Efficiency** – Together with the Fedwire system, is the biggest RTGS system in the world
  - 2004 Daily average value of payments processed: 1,7 bill €
  - Daily average number of transactions: 267.000 ops
- **Solid legal framework** – Immediate finality in central bank money
- **Operational reliability** – 99.81 % of availability in 2004
- **Integration of euro area money market** – Wide participation
- **High availability of liquidity** for participants
The current TARGET system
Has difficulties to face some challenges due to its design:

TARGET Challenges
- Decentralize system.
- Different technical solutions
- Not harmonized users interface in different countries
- Lack of efficiency in terms of costs
- Different price structure
- Differentiation between cross-border and domestic payments
- National peculiarities in the provision of payment services
- European Union enlargement

Project evolution

<table>
<thead>
<tr>
<th>Date</th>
<th>Event</th>
<th>Description</th>
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<tbody>
<tr>
<td>24/10/02</td>
<td>ECB Governing council’s decision on the long term strategy on TARGET</td>
<td>Multiple-platform decentralised system</td>
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<td>16/12/02</td>
<td>Users Public consultation</td>
<td>Deadline April 2003</td>
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<td>28/07/03</td>
<td>Joint offer of the central banks of France, Germany and Italy (3CB)</td>
<td>Consolidation of the idea of single shared platform</td>
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<td>31/12/03</td>
<td>The rest of central banks express their willingness to joint the shared</td>
<td>Confirmation of the idea of single shared platform</td>
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<td>platform proposed by the 3CB</td>
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<td>22/07/04</td>
<td>ECB Governing Council approval of the General Functional Specifications</td>
<td>The drafting of the User’s Detailed Functional Specifications starts</td>
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<td>Dic. 2004</td>
<td>The ECB Governing Council accepts that TARGET2 will consist on a</td>
<td>The ECB Governing Council accepts that TARGET2 will consist on a single</td>
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<td>single shared platform based on the 3CB proposal</td>
<td>shared platform based on the 3CB proposal</td>
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The integration process of large value payment systems in euro

**TARGET2 RESPONSES**
- Technically centralised system
- Common environment and interface for all users irrespective of their country
- Efficiency in terms of costs
- Common price structure
- No differentiation between cross-border and domestic payments
- Common set of core services
- Easy incorporation of new member states (EU enlargement)

**TARGET2 OVERVIEW**
1. TARGET2 ≠ SSP
2. Mandatory modules
3. Optional modules
4. Dual account structure
5. Customer relationship at domestic level
6. “Building blocks” concepts

**BCNs**
- Collateral Management
- Monetary Policy
- Reserve Management

**TARGET2**
- PHA – Home Accounts
- Customer Relationships Management
- Statistics

**SSP**
- Payments Module
- Contingency Mod.
- ICM
- HAM
- CRM
- DW
- Standing Facilities
- Reserve Management

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The integration process of large value payment systems in euro

- Dual account structure
- Wide range of operations
- Direct and indirect participation

Improved Liquidity management

SLBE liquidity management
- RTGS with FIFO-by pass queue mechanism
- Priority assignment for one specific payment order
- Bilateral and multilateral optimisation procedures
- Intraday credit (repo+pledge)
- Liquidity reserves

TARGET2 incorporates:
- Active queue management
- 3 possible priority levels for each payment order (MU/U/N)
- Improved optimisation procedures (4 algorithms with continuous processing)
- Sending limits
- Definition of execution time and warehouse functionality
- LIQUIDITY POOLING
The integration process of large value payment systems in euro

The integration of ancillary systems settlement procedures

From TARGET to TARGET2

Wide range of ancillary systems (110), typologies and settlement timetables

A single harmonised interface for all ancillary systems supporting all settlement modalities

The integration process of large value payment systems in euro

2003

DEFINITION

General
Functional
Specific

Detailed
Technical
Specific

DEVELOPMENT

TESTING

Technical
Implementation

Customer migration process

# country window

2004

2005

2006

2007

BANCO DE ESPAÑA
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SEPA: THE INTEGRATION PROCESS OF RETAIL PAYMENT SYSTEMS IN EURO

SINGLE EURO PAYMENTS AREA (SEPA)

**Goal**

“To establish a single payment market in euro that ensures that any European citizen can make her or his payments throughout the euro area from a single bank account, using a single set of payment instruments as easily, costly and safely as in her or his national context”

Fragmentation

- Instruments
- Infrastructures
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SINGLE EURO PAYMENTS AREA (SEPA)

The building of SEPA

Building blocks

White Paper (May 2002)

European Payments Council EPC (June 2002)

Roadmaps (2002 and 2004)

Progress Reports

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SINGLE EURO PAYMENTS AREA (SEPA)

SEPA for citizens – 2008

“To offer citizens and commercial enterprises the chance to optionally use pan-European instruments also for their national payments.”

Credit Transfers

Direct Debits

Cards

Cash

Credeuro

ICP

Prieuro

PEDD

Fees

Fraud

Competition

Costs

Counterfeit
SINGLE EURO PAYMENTS AREA (SEPA)

SEPA: a two-step approach II

Standardisation
- Common standards, rules and conventions: essential for providing efficient pan-European instruments
  - Sound governance structure
  - Implementation follow-up

Major goals
- Strong co-operative links between different bodies (EPC, ECBS, ISO, SWIFT, etc.)
- Streamlining of the work plan (contribution to final goals)
  - Basic payment instructions (credit transfers)
  - Value-added services
  - End-to-end services
  - IBAN, STP, simplification

SEPA for infrastructures – 2010
- Pan-European Automated Clearing House - (PE-ACH)
- Multiple service providers - (competition)
- Larger volume of transactions - (wider range of services)
- Finalise the process of consolidation of national infrastructures in Europe – (adaptation)
SINGLE EURO PAYMENTS AREA (SEPA)

Some problems

- Lack of support and/or opposition by some agents to the SEPA project
- No clear link between high-level objectives and their implementation at domestic level
- EU, EEA and euro area: different speed / different goals

Some proposals

- Public Administration
- EU legislator
- Inform and educate end-customers

Dialog / Regulation
Monitoring / Collaboration
Differentiation

Thanks for your attention