What can we expect from the implementation of the PSD Directive for the users of payment services?

by Gerardo Coppola

I would like to give you an additional perspective of the topic of today's meeting on *"economic development and immigration"*.

I would choose a financial approach to analyse and discuss with you some improvements that the retail payment industry can offer to migrants when they decide to perform the simple act to send a small amount of money to their families.

The financial needs of foreign workers provide a convenient angle from which to get a clear view of the complexity of migration issues.
The task is not complicate because European countries are going to experience a very fast and radical transformation of payment services thanks to the entry into force of the Payment Services Directive – PSD - and the forthcoming realisation of the Single Euro Payments Area –SEPA - through the end date Regulation which will deeply affect the sector of remittances and money transfers' activity as well as other payment services.
With regard to the macroeconomic impact of remittances flows they have become a major source of external finance for poor countries. Even if the recent financial crisis has undermined the growth of money transfers the value of worldwide remittances is still very high up to $ 300 billion in 2010 the same amount of Switzerland' s GDP. High or exorbitant fees charged by financial agents are a drain on the value of money sent home by workers. These fees especially affect the poor. Reducing remittance fees by five percentage points could increase annual remittance flows to developing countries by several billions and this is the goal policymakers are trying to pursue.
On the positive side, remittances are believed to reduce poverty, as it is the poor who migrate and send back remittances.
Policymakers need to reach much more consensus on how to increase the efficiency of the monetary channels used by migrants to transfer money to their families abroad so they can positively contribute to migrants' home communities and countries.

It may sound like a paradox but even if emerging markets have very limited banking infrastructures, mobile payments are growing faster and faster because the low level of access to banking facilities has triggered the development of services through the popular and widespread use of mobile phones.

From another point of view, we need to think that migrants are becoming more and more integrated in the receiving countries so that policymakers have to guarantee them the same service levels in the market of financial services. An important manifestation of this integration is now represented by the admission of thousands of migrants to the next local government elections in Spain.

Therefore, my speech will focus on the developments which have taken place in the last few years in Europe in the retail payment services and which set the conditions for the future evolution with expected benefits for all users, included migrants who live and work in Europe.

The area of cashless payment instruments is traditionally dominated by commercial banks. They are well positioned in as trusted providers to both merchants and consumers, especially in developed markets where they have long-standing transactions and account based relationships.

So far, non banking providers still account for a small percentage of total worldwide non cash transactions volumes, less than 1 per cent.

Furthermore, the amount of transactions in cash in the Euro area – where the role of banking sector is likewise prominent - is still high. One of the conclusions of a recent work of the ECB *(see the April Monthly Bulletin)* is that the value of euro cash payments remains high about 2 times the value of electronic payments at point of sales.

The survey also shows that cash usage varies from country to country: Italy, Spain and Austria were among the most intensive users of banknotes whereas France and the Netherlands were found to use banknotes the least.

The landscape of payments will change dramatically thanks to the coming in force of Payment Services Directive in all the countries of European Union plus other three Nordic countries.

So far few financial intermediaries have seen the opportunities disclosed by the PSD as a transformation driver unlike many payment service providers who are investing heavily in IT systems to handle incoming new payment services.

I want to highlight **FOUR** legal provisions of the PSD - revolutionary in my view - that are changing the payments industry in Italy and in Europe and that can bring in economic advantages for citizens as well as for migrants in terms of competition, efficiency and openness of markets.

1)MARKET ENLARGEMENT

The wide use of cash in Europe can allow payment service providers – different from banks - to enter the industry and achieve huge profits provided they develop safe and convenient means of payments for companies and households.

In fact, in order to remove legal barriers to market entry, a single license has been established for all providers of payment services and a new category of payment service providers has been introduced subject to a set of strict and comprehensive conditions to provide payment services throughout the Community.

The new legal framework ensures for the first time that the provision of payment services to users can be executed also by non-banking entities such as Payment Institutions which can be created also by telecommunication, information technology or network operators, or large retailers which can run Hybrid Payment Institutions (they can carry out mixed business). (Electronic Money Institutions were introduced by the electronic money directive but did not take off because of the heavy burdens imposed by the legislation and hopefully will have a new impetus with the revision of the e-money directive)

In terms of market perspectives, Payment Institutions can act in partnership with banks exploiting economies of scale arising from the volume of transactions processed. Or they can act in competition with banks and postal offices focusing on electronic payments thus exploiting the benefits of new electronic payments which rely mainly on the efficiency and resilience of the IT.

2) MARKET ACCESS

It is essential for any payment service provider to be able to access the services of technical infrastructures of payment systems. Such access will, however, be subject to appropriate requirements in order to ensure the integrity and stability of those systems.

In order to ensure equality of treatment throughout the Community as between the different categories of payment service providers, the rules concerning access to the provision of payment services and access to payment systems have been clarified.

Provisions have been established for the non-discriminatory treatment of authorized payment institutions and credit institutions so that any payment service provider competing in the internal market is able to use the services of the technical infrastructures of these payment systems under the same conditions.

As I said before, the PSD has identified six types of organisations that can offer payment services: credit institutions, e-money institutions, payment institutions, post office giro institutions, central banks and various government organisations.

As a consequence, a company or organisation that falls within these six categories, and which is authorised and supervised as appropriate, can apply to become a principal member of Visa or other payment cards systems.

Such members can then issue cards or offer an acquiring service, allowing their customers to accept debit and credit cards payments.

More complicated is the issue of access to payment systems.

3) MARKET REGULATION

A general rule has been set by the PSD in order to promote transparency and competition in the market of payment cards.

The payment service provider cannot prevent the payee from requesting a charge from the payer for using a specific payment instrument.

However, Member States may decide whether they forbid or limit any such practice where, in their view, this may be warranted in view of abusive pricing or pricing which may have a negative impact on the use of a certain payment instrument taking into account the need to encourage competition and the use of efficient payment instruments.

As in the majority of European countries, in Italy the surcharge fee on payments instruments has been prohibited (article 3, 4. The payee shall not charge the payer for the use of a given payment instrument. The Bank of Italy may establish, with own regulation, derogations taking into account the need to encourage the use of most efficient and reliable payment instruments.).

Therefore, the Italian Antitrust Authority has recently forbidden credit and debit card surcharges which are standard practice among some retailers, including airline companies operating in my country. This month we expect other similar decisions against the major Italian flight carrier, Alitalia, which sets such expenses as high as up 5 euro per capita and per flight.

Such achievements have been possible because the transposition of the PSD in Italy - having taken into account the need to encourage competition and promote the use of efficient payment instruments - forbids payment service providers to request charges harming the interest of consumers especially when the surcharge is not proportionate to the cost incurred by the business for processing the payment.

I have also heard that on the 30 March 2011 *Which?* - a British consumer association - issued a surcharge complaint to the Office of Fair Trading over the fees retailers charge consumers for paying by credit or debit card claiming that low cost airlines are among the worst offenders.

They asked for upfront costs, fair charges and for retailers to absorb the cost of the fee to process a debit card payment.
The principle is gaining ground that it is not good enough for some businesses to generate profit by imposing inflated surcharges when their actual card processing costs are substantially lower.

4) EXPLOITING MARKET ADVANTAGES

Finally, unlike banks, Payment Institutions don't need to realize the expensive changeover from the old standards and requirements of payment services and instruments to the new ones required by the SEPA framework.

They can easily rely on the new arrangements for credit transfers, direct debits, cards, mobile and electronic payments that will be carried out according to the same standards and conditions no matter where payment service providers are located with enormous benefits in terms of cost and security.