

Nonbanks in the Payments System: Innovation, Competition, and Risk

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General Discussion

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Moderator: Thomas M. Hoenig, President and Chief Executive Officer, Federal Reserve Bank of Kansas City

Mr. Hoenig:

Thank you very much, Gertrude.

I have a question. Would it, in your mind, facilitate the advance of payments and the new technologies if there was an ability to put a standard for identity authentication and protection in place across international or even national payments systems, so that people then know they have one standard, they know what the level of protection is, and what the requirements are? Or are payments in too much of a dynamic state to be able to set a standard at this point? Do you have an opinion?

Ms. Tumpel-Gugerell:

I am not sufficiently expert on these issues, but the fear and resistance against using new technologies are very often linked to psychological issues and also maybe fear of losing privacy. Therefore I think standardization is good. But in the best standardized system,

you never can exclude that somebody misuses it. This is always possible, even if it is a small likelihood. There are always crooks around.

Mr. Peter Burns, Vice President, Federal Reserve Bank of Philadelphia:

As we move from national payments systems in Europe to the single European payment area, do you sense there is sufficient network competition? Or is there a need for additional new network competition to enter into the mix of this expanded marketplace?

Ms. Tumpel-Gugerell:

The first step is to open the national contractual arrangements we have at the moment, which means very different arrangements, different levels of pricing, of interchange fees, different organizations, etc. So, the first step is to create the conditions for competition.

In the network field, the first concern would be to have more consolidation, then to look if there is still sufficient competition. At the moment, consolidation is in the focus because of the potential for cost reduction. But there are competition cases going on, debates with the Commission on MasterCard fees, etc.; reporting is expected soon. Both processes are happening in parallel.

Mr. Burns:

So there is, let's call it, a central banking safety and soundness dimension of this concern and there is maybe a political concern at the ministries of finance who may have different interests?

Ms. Tumpel-Gugerell:

Efficiencies are our focus at the moment. Competition is the competence of the national authorities and the European Commission.

Ms. Bronwyn Hall, Professor, University of California, Berkeley and Maastrich:

On the ATM interchange fees, I have noticed that each country has its own rules. I am careful to use a card from a county that forbids them (fees). I had a question because I didn't quite understand about SWIFT, about the reluctance. I have been receiving payments via SWIFT for quite a few years now, with no apparent problems. It is a commonly used technique. IBAN numbers, SWIFT, no fees, etc., that kind of thing. Where is the concern? Is this with the United States, is that what it is? Because, within Europe, it is not a problem.

Ms. Tumpel-Gugerell:

No, no, it is not a technical problem. The concern is about the transfer of data, which took place because of the antiterrorist financing campaign.

Ms. Hall: The airlines seem to have managed to negotiate a standstill agreement.

Ms. Tumpel-Gugerell:

They found an agreement. There is no political agreement on the SWIFT case, but SWIFT is now going in the direction of separating geographically data centers. They have announced that.

Ms. Hall:

I also noticed that many of the websites that do sales, because I operate in multiple jurisdictions, I am very aware of the cross-border purchasing opportunities. There are a large number of websites out there where they don't care where you come from. Airline tickets, for example: You frequently buy them in a different country from the one in which your card is located. It is delivered to a third country. They seem to be ahead of the regulatory scheme, as far as I can see.

Ms. Tumpel-Gugerell:

What is required now is that there are no higher charges for cross-border payments than for domestic payments. This was a Commission regulation issued five years ago, so the customer does not see it, but behind it, we still have differences. We have different standards and systems and therefore the idea is not to have parallel systems for

international payments and domestic payments but to have just one standard. This would be the change.

Mr. Wilko Bolt, Economist, De Nederlandsche Bank:

You just mentioned in your talk that there is a difference in profitability in payments between the United States and Europe, that the profits are higher in the United States in the payments services sector. I was wondering, where does this difference come from? Is it because in the United States the infrastructure is consolidated to a higher degree? Or is it that they charge more directly than often is the case in Europe? If the last case is true, then it is very difficult to compare those two.

Ms. Tumpel-Gugerell:

I refer to a McKinsey study, which tried to make the case for SEPA two years ago and they also made this cross-border comparison with the United States. But it is difficult to say what exactly could be the reason. Maybe interest payments for loans are cheaper in the United States and payments services are charged directly. I don't know about the reasons. This is just the fact. Profitability is higher, which is directly allocated to payments services.

Mr. Ken Howes, Director, Edgar, Dunn & Company:

Could I ask about proposals regarding possible regulation of payments schemes and card schemes? Could you perhaps comment on that?

Ms. Tumpel-Gugerell:

I am not aware that there is a regulation envisaged.

Mr. Howes:

I think that is something that has been announced today about potential proposals and inviting comments by August on that?

Ms. Tumpel-Gugerell:

Do you mean our proposal on oversight standards for cards payments? This was a proposal by the ECB, the euro system, and this is just describing how we think card schemes should be overseen. That is not foreseen as a regulation.

Mr. Howes: It is not proposals for a regulation?

Ms. Tumpel-Gugerell:

No, it is a proposal how oversight work should take place.

Mr. Ross Anderson, Professor, Cambridge University:

There is a very wide variation in Europe in standards of consumer protection, for example, when there is dispute resolution procedure involved. I see that the draft Payments Services Directive more or less entitles the bank to specify its own dispute resolution procedure and its terms and conditions.

This seems a bit of a copout. Doesn't there thereby arise a risk that there will be a competitive race to the bottom in terms of consumer rights in Europe?

Ms. Tumpel-Gugerell:

The harmonized consumer protection framework would be the best solution, but this was not possible and it is too complex to go into legal harmonization. We see it also in other fields. For instance, in the field of large-value payments, we have chosen to keep national rights but harmonize the contract as much as possible. We have achieved that, so this is a way of dealing as well as possible with the existing different legal systems and traditions. I do not think banks would win business if they are more relaxed on consumer protection also. There are other elements in winning a customer above the consumer protection issue.

Mr. Anderson:

So consumer protection, then, is really still unfinished business and we will perhaps see a consumer protection directive coming out in a few years' time?

Ms. Tumpel-Gugerell:

It would be a nightmare for the banks maybe. I think it is a big step forward what we have in the PSD. It is basically a framework defining what happens if there is cross-border business taking place. This is sufficient for the time being. And a complete legal harmonization I do not expect for the next decade or so.

Mr. Hoenig: One more question.

Mr. Jamie McAndrews, Vice President, Federal Reserve Bank of New York:

One of the striking differences between the United States and Europe is the less use of credit cards in Europe, especially the northern European countries. Do you have an opinion about why that is, whether it is a cultural difference or, as some have suggested, perhaps greater data privacy laws in Europe?

Ms. Tumpel-Gugerell:

It partly has to do with, in some countries, high fees for the use of credit cards. This may be one of the reasons that merchants are

reluctant to accept, and the lower the volume of transactions, the higher the fees have to be. So this is a kind of hen-and-egg problem.

In certain sectors, cash is also used for tax evasion purposes. Tax authorities are always fighting against this. And it is also very much about habits. It is an issue for different generations. Of course, banks would like very much that customers would use the cards more. But it is difficult to educate them.

Mr. Hoenig:

Thank you very much, Gertrude.