

# Instant payment attractiveness for EU citizens

## 1. Instant payments are promising though unevenly developed

A policymaker stated that instant payments are currently available in around 60 countries worldwide. The European Commission's conclusion is that instant payments can deliver benefits for all types of payment users. In the European Union the average uptake of euro instant payments is quite moderate, at around 14%. That 14% is driven by the strong performance of a small number of member states. The uptake in the remaining member states has been quite weak, and in some of them it is still around 1%. That is why the Commission has concluded that the situation would require some legislative action.

### 1.1 A versatile, reassuring and swift payment is good for individuals and merchants

A Central Bank official noted that when they are talking about instant payments, they are referring to the payment standards as defined by the European Payment Council: the Single Euro Payments Area (SEPA) Instant Credit Transfer (SCT Inst), because it is the best and the most used instant payment in the European Union. There are no limits to the possibilities to use instant payments. The most obvious use case is at point of sale. E-commerce would be a great use case to have instant payments, and then peer to peer. Notaries or intermediaries will not be needed. For P2P transactions there is a large value added in instant payments, because at that moment there is no intermediary.

An industry representative stated that instant payment is everything for EPI, because it focuses and bases all its transactions on instant payment, even though it does not just use the European rulebook. EPI also has its own rulebook. Merchants want something very complete and do not want specific niche use cases. They are interested in a solution which can address all needs, and be addressed in a better way with instant payments than with cards. There are clear advantages for the merchants, as receiving the money directly in e-commerce is of substantial value for them.

Instant payments can work everywhere. EPI tries to manage all requested payment use cases, fragmented, deferred, split payments, and all advanced use cases that are necessary to make it a complete payment means and not just an instant transfer. EPI sees instant payments as the choice of the consumer if they do not want to do card transactions. It is very interesting that instant payment provides total control to the consumer, because at all times they perfectly know their financial situation. It would be a pity if Europe misses out on its positioning in the international frame, where there are so many real-time instant, immediate, faster payment solutions emerging.

### 1.2 Some use cases also address B2B transactions

A Central Bank official noted that it is not only citizens who can use instant payments. There is also a use case for corporates. If a company has urgent transactions to do such as a treasury transaction then instant payments will be a great tool to do that, because the funds can be wired to another account very easily or very quickly. The possibilities of instant payments are almost limitless; although the scheme foresees a cap of €100,000 there is no obligation to do so. In Belgium the financial industry opted to not have the cap.

An industry representative observed that on the corporate and SME side it is a bit different, as there the B2B case is probably less obvious given the offer already provided and the specific needs. Companies do not run an infrastructure for free, so they need to be certain that someone is paying at the end. If companies want to have that working then they need to be sure that costs are borne, be it investment in IT, anti fraud, or the cost of fraud, which is still higher on instant payment, and also on anti money laundering, which is one of the points that is still under discussion in the proposed legislative framework. Still this framework is welcome.

### 1.3 Instant payments also offer opportunities to improve cross border payments

A Central Bank official noted that it makes little sense to talk about use cases for instant payments because they can be used in any circumstance, but there are some areas where their growth potential is the greatest. One of these is the payments at the point of interaction, and another is cross-border payments. There are very interesting experiments going on, because fast payment systems are particularly suitable for interconnecting different currency areas. There are important initiatives, both from the private sector and the public sector. The private sector has the IXB pilot by EBA CLEARING, TCH and Swift, which is very well advanced. In the public sector there is an important project by the Bank for International Settlements (BIS) called Nexus, which interlinks many different platforms.

### 1.4 Many initiatives are underway to improve and accelerate cross border payments

An industry representative stated that Swift welcomes the Commission instant payment proposal and supports its overall 2020 Retail Payments Strategy for three reasons. As a European company with a global scale Swift aims to connect the world, making it possible for individuals, SMEs, and businesses to trade, invest or send or receive payments all over the world, and to do that in an instant and frictionless way. Swift is embedded into the European payments and financial ecosystem and ensures connectivity to all major market and payments infrastructures, including the instant payment systems of the Eurosystem TIPS and that of EBA

CLEARING RT1. Swift's core mission is to achieve instant and frictionless cross-border payments at the cross-border level and to contribute to this economy growth, because it has been well-documented that there is a clear link between rapid payments and economy growth. It has a network of 11,500 financial institutions, which in turn connect four billion accounts in the world.

Financial institutions and big corporates can use Swift to send billions every day in a quick and secure way. 50% of those wholesale payments are processed in less than five minutes, two-thirds in less than an hour, and 99% in one day. Swift has recently launched an initiative called Swift Go. Retail and SMEs can also benefit from highly competitive, quick, transparent, international payment from their bank accounts. Swift now has 600 banks on that solution. Another initiative is linked to what the Commission is trying to achieve with the International Bank Account Number (IBAN) and name check, which Swift calls "Payment Pre-validation". At the international level it is very important to try to minimise the friction in the process and pre-validate essential account data before the payment is sent. Swift also has sanctions screening services at the international level, which is very important because it can immediately inform the user that there is something suspicious.

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## 2. Getting instant payments' full value requires achieving critical mass and accessing the benefits of network effects

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A Central Bank official added that, although those situations exist and not every use case has the same value added, they are still a big supporter of pushing forward instant payment, because in the payments market the one word that count is volume. Volumes need to be created to generate the network effects to make payments effective in the time that it takes to process them, but that are also cost effective. All use cases need to be catered for to create network effects, as well as introducing and advocating instant payments in use cases where the added value is not that large at first.

**The different payment means should be focused on certain needs to leverage their specificities and avoid costly duplication also sources of complexity.**

A Central Bank official stated that, while instant payments in Europe can take advantage of the Eurosystem's TARGET Instant Payment Settlement (TIPS), the real question is not whether instant payments have use cases, but whether non instant payments have use case. In a long-term perspective, Europe may find itself in a payment ecosystem in which ordinary credit transfers will no longer be available. This will depend on whether or not the option to settle in one day has economic value. If it does Europe will continue to have ordinary wire transfers in the future. The one-day delay could be used, for example, as a cooling-off period in purchases, a payment reconciliation period, or to provide a payment guarantee. If such use cases continue

to be of value to payers and payees Europe will continue to have a mixed system in which there will be both instant and non-instant payments.

An industry representative agreed with most of what has been said so far. There is probably a different use case for the needs of individuals and of corporates. It is clear on the individual that there has been progress on instant payment. At a point in time cash payment and credit card payment can be replaced, as we noticed with contactless. Possible usages of instant payments are vast and it is clearly something that is there to stay. The question is for which proportion of the payment that will be done. La Banque Postale was the first large French bank to offer free instant payment at the beginning of 2022, making it simple for clients, because it is the default option. If clients want, they can easily switch to the non instant payment transfer. It is working but the challenge is that the infrastructure needs to run with two ways of functioning.

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## 3. Instant payments: Key success factors and actual threats

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A policymaker observed that there is great potential while there are a lot of challenges that Europe needs to master, both legal, technical, and commercial.

### 3.1 A demanding multipronged change management programme in a complex and fast evolving regulatory environment

An industry representative commented that she sees many challenges, as there are a number of legislations to implement on various issues. One of the challenges is to move on environmental, social and governance (ESG), transition and on a number of topics at the same time. When it comes to clients, habits are difficult to change. They have evolved a lot in the past three years due to external factors such as the pandemic and a higher ceiling for contactless payment, and because payment habits may not be exactly the same in every country. Payment providers need to reassure customers, especially elderly customers or customers that are less comfortable with technology or suffer from illiteracy. Some customers are completely ready for new technologies, and they think companies are moving too slowly, but other customers are not ready. The challenge is to onboard everybody and not to have two-party systems.

Companies need to see that as the mass market, which would address all needs. That is on the client side. It is moving, but there are parts of the population that have not started to move that will be more complicated to integrate and to reassure on those topics. La Banque Postale have done a lot of pedagogy on a collective basis. Big banks have been the other actors in the system, as well as public authorities.

The technical infrastructure has to be profitable in the long run. Supervisors are also looking at that, so companies need to be sure that what they run as a whole is profitable. Resilient infrastructures are needed. If someone needs to make an instant payment in 10

seconds they first need an alternative when it does not work. Companies will make everything so that it works on a permanent basis, but there is still operational risk. Those risks need to happen as little as possible, meaning that there is the need for stronger investment on the surveillance of the system. Companies need to be sure that it is also safe from a cybersecurity perspective, because everyone is interconnected if there is an attack or a threat.

One additional topic that is more on the fraud side is anti money laundering, which is to reassure the bank and the management of the banks, because banks have high responsibility when it comes to anti money laundering. It is important to ensure that the rules are clear and that they are implementable, otherwise it puts banks in an extremely complex position to implement the directive. The faster it goes the less time a bank has to check that there is anything wrong, and that they have looked at things like the list and the transaction screening.

### **3.2 Significant fraud, inadequate pricing, and fragmented EU payment are limiting instant payment cost effectiveness, adoption and credibility**

A policymaker agreed that there are lots of benefits in having a very quick transfer, but also challenges to address as e.g., money laundering suspicion where time is of the essence.

A Central Bank official stated that two factors hold back the development of instant payments. The first is the fragmentation of the market on the supply side and the second is the slow pace of change in people's habits. In both cases intervention by public authorities and public-private cooperation could be very helpful. Regarding market fragmentation, it is important to keep in mind that different automated clearing houses that Europe already has cannot ensure a full, pan European reachability of payment system providers. This is the issue with fragmentation, and this is why the European authorities have asked players to open an account on the Eurosystem instant payment platform TIPS, without any obligation to use it, in order to allow each payment system provider to be reachable.

The slow pace of change in customer's habits has already been mentioned. There are two factors that make people reluctant to use instant payments: cost and frauds. As costs are concerned, the greater competition that Europe will be able to achieve through the interconnection to the full reachability of payment system providers will play a role in putting downward pressure on costs. Another important development for costs are two recent proposals by the European Commission that the price of instant payments should not exceed the price of non-instant payments, and that the provision of non-instant payments should be accompanied by the provision of instant payments.

The incidence of fraud in instant payments is much higher than for non instant payments for normal credit risk transfers, which is a significant problem. The recent Italian experience with public private cooperation is very reassuring, because in Italy a very large share of the frauds in instant payments have been blocked or the

funds have been recovered, thanks to a protocol that was defined by the Italian banking association, together with Banca d'Italia. This is a very successful example of industry initiative. Another example of useful initiative is in the field of awareness raising campaigns. Banca d'Italia, as well as industry associations and players in the Italian banking and insurance sectors are carrying out important awareness raising campaigns for a safer use of digital channels and tools.

A policymaker agreed that Europe sees a lot of fraud happening, and the timing is a challenge. What to do if the money is transferred requires a lot of innovative steps.

### **3.3 Further harmonisation and steep efforts to achieve payment systems and CBDC interconnectivity and interoperability at the global level should help a swifter implementation**

An industry representative noted that Swift has been discussing the instant payment regulation with many European banks. Consensus is that a large proportion of SEPA credit transfers will become instant payments, especially for the retail flows. There are challenges that remain in terms of the timing of implementation, investment in the different pillars, and non-European standards for value-added services like the confirmation of payee i.e., the IBAN and name check. The check is a technical challenge, but it will be very important because the industry wants to avoid the creation of a patchwork of confirmation of payees all over Europe that will use different systems and standards. Even though there are some convergence in global infrastructures there are many differences that remain in terms of systems, jurisdiction and standards, which make it very difficult to interconnect them and to ensure truly instant payments across borders.

Interconnectivity and interoperability is an issue that the G20 leaders have made a priority to improve cross-border payments. There are different targets. One of them, which was raised in February 2022 as a priority, is interoperability between payment systems and instant payment systems. Europe is a key player in the global payment space, as it has world-class market payment infrastructures and is at the forefront of innovation; it should ensure that its payments infrastructure will be future proof, meaning that they can be interlinkable and interoperable with the other instant payment systems so that the value can flow more easily. That point needs to be tackled from the beginning.

Swift will play a role in the interoperability of payment systems. It has done that with the correspondent banking systems and connecting non-instant payment systems, but it will also have a role in the instant payment space in whatever the money or the value can take as a form. Central bank digital currency (CBDC) will be discussed at a later date, but there are 100 central banks looking at CBDCs. Based on the Digital Monetary Institute at least 25% of them will issue a CBDC in the next two to three years, but they will use different technologies and standards. Interoperability is needed. Swift made a very large-scale experiment with 18 commercial and central banks to ensure that they can exchange CBDCs between themselves, but also with fiat money, with real-time gross settlements (RTGS) and traditional systems.

A policymaker stated that an important project that is being worked on at the European Union level, together with the European Central Bank, is the digital euro. Many questions have been received, such as the impact of the digital euro on instant payments, whether a digital euro is needed if there are instant payments.

### **3.4 Given the still missing level of instant payment acceptance and fragmentation, possible digital euro mandatory acceptance is a concern**

An industry representative highlighted that EPI would try to ensure as large a usage of the payment solution as possible. There is the possibility to integrate the digital euro into the EPI solution to make it available for all use cases. There can be synergies. For EPI it depends on what the final design is, which is why it is participating in the compatibility working group. EPI is trying to make instant payments big, and then the digital euro comes up. EPI has to be mindful about the potential confusion in the market, because it hears it in conversations with the merchants. Merchants want to understand where the priorities are and how that will be implemented. One particularly big question mark is mandatory acceptance. EPI hears that the digital euro should be accepted as the current fiat euro, so then it is everywhere and it is mandatory acceptance. The same is not true for instant payments. That will create a difference and a competitive advantage for the digital euro only, therefore pushing back the acceptance of instant payment.

What is missing is the acceptance of instant payment by the merchants, because Europe either has no solutions or fragmented solutions. That is why EPI is trying to address this and overcome this, to have one solution which will have one unified functioning which allows merchants who have just one integration and not one per market. The challenge is to understand how Europe functions with the digital euro. Europe is still struggling to become independent in payments. A public private partnership is needed to make it work, to allow competition in the market and fluidity, and to ensure it is understandable for the consumer and for the merchant side.

### **3.5 To avoid financial players slowing down investments on instant payment, the digital euro should be focused on replacing cash for specific use cases**

A Central Bank official expressed their hope that the digital euro will come. The digital euro is partially a reaction to the declining use of cash. The use of central bank money in transactions is declining. One of the reasons to introduce the digital euro is to keep providing central bank money to the public so that citizens can use central bank money. Since it is digital it will be another means of payment. It will be another possibility to pay in stores, peer to peer or e-commerce. In that sense it will become a competitor for the existing payment methods already in place, but it can provide a boost for instant payments.

A digital euro will almost certainly be instant, so Europe will probably introduce the digital euro through a staggered approach. Not all use cases will be available

within the first release. Europe will probably start with peer-to-peer transactions and also e-commerce possibilities for instant euro. A CBDC would take slightly longer than two to three years to introduce the first release, but at that time the hope is that instant payments will have already penetrated through the market, and at that time that will be the standard. If that is not the case then it can offer a boost to instant payments, because if central banks are providing a solution that will be instant the commercial players will have to follow and 'beef up' their offerings to the public. In that case it can be beneficial for the penetration rate of instant payments in the market.

There can also be negative effects for the existing private sector. The uncertainty on the impact linked to the introduction of the digital euro on the payment market may slow down investments today by private parties to invest heavily in introduction of instant payment possibilities. A digital euro will not be introduced as an instrument that wants to crowd out all the commercial payment possibilities. When looking at European studies, before the pandemic almost 80% of transactions in the Eurozone at point of sale were paid in central bank money with cash. After the pandemic that percentage is now at about 50%. The National Bank of Belgium has experienced a 30% decline in market share from its payment method, which is something that the private parties have captured for themselves.

The payment market is big enough to have a central bank offering in those possibilities, and private parties can build on what central banks are going to offer. Central banks will offer a basic product, and then it is for the private and commercial parties to build on top of that with innovative solutions like conditional payments. The two can go hand in hand. When looking at the final balance the digital euro can provide a boost for the penetration of instant payments.