

PORTABLE IBANS

HOW TO EXTRACT EVEN MORE BENEFITS FROM SEPA?

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Background

The Single European Payment Area (SEPA) has been designed to improve cross-border credit transfer services and notably their efficiency and cost to the customer. The aim is to enable consumers and small and medium-sized enterprises to make credit transfers rapidly, reliably and cheaply from one part of the euro area to another – in fact to remove the current differentiation between domestic and cross border payments.

However as has been highlighted by the paper "Realising SEPA Benefits", a white paper published by the TWIST Innovations Centre in May this year, there are concerns raised by corporates as to whether SEPA, as currently structured, provides the required benefits – in particular that corporates should be able to implement SEPA as well as change payment services providers with minimum cost to themselves or their counterparties.

The Payment Services Directive that is under review by the EU Council and EU Parliament will define a legal framework for the provision of payment services in Europe. This Directive complements the EU Directive 2560/2001 which was issued by the EU Commission in 2001.

The EU Directive 2560/2001 requires corporates to print their International Bank Account Number ("IBAN") and Bank Identification Code ("BIC") on their invoices. Where the European Payment Council initially embraced BIC and IBAN for the implementation of SEPA, this risks introducing anti-competitive, structural rigidities into the European Union's financial markets.

The anti-competitive, structural rigidity of EU Directive 2560/2001

The requirement that corporates are to print their IBAN and BIC on their invoices means that:

1. Corporates will subsequently find it very difficult, in practice, to change their accounts. This means that they are effectively locked into their existing banking relationships; preventing the cost benefits and payment service selection that a free market would allow.
2. Small banks that are not members of SWIFT¹ are faced with the dilemma of either:
 - a. quoting their own non-SWIFT BIC to their corporate clients, but then they take the risk that paying banks will not know how to route the payment to them²; or
 - b. quoting the BIC of their correspondent bank who is a SWIFT member, in which case they become effectively locked into that correspondent banking relationship.

Furthermore, should any bank change its BIC (either because it changes its SWIFT status or through a merger) this will result in a major disruption for all its corporate clients who then have to change their invoicing details.

Therefore in order to rescue the spirit of SEPA it is necessary to address and resolve the issues of Fixed, Non-Portable IBANs as well as the current requirement for corporates to quote the BIC of their bank. However, it is critical that any proposals must not disturb SEPA's implementation. It is the scope of this paper to provide input to the discussion about SEPA implementation in a manner to achieve these objectives.

¹ These number over 6,000 in the European Union.

² This is what the strict letter of the Directive requires them to do.

Fixed Non-Portable IBANs versus Portable IBANs?

Very simply:

1. a Fixed Non-Portable IBAN always identifies a fixed account at a fixed bank – the account number and the bank cannot be changed.
2. a Portable IBAN does not identify a fixed account at a fixed bank. These details (bank account number and/or bank) can be changed in close to real-time by the owner of the Portable IBAN. (When a payment is made to that IBAN, it is automatically redirected by the ACH or other processing infrastructures to the new account.)

Therefore a Fixed, Non-Portable IBAN locks a client into their banking relationship. A Portable IBAN allows the owner of the IBAN to change their banking relationships at any time.

Another crucial difference between the two types of IBAN is that a Fixed Non-Portable IBAN has a fixed link to a BIC whereas a Portable IBAN does not. Therefore, in order for Portable IBANs to conform to 2560/2001 then it would be necessary to release corporates from their obligation to also quote the BIC. At this point, it would be necessary for customers to simply quote the IBAN³.

N.B. This does not mean that BICs would no longer play a role in payment messaging, simply that the customer no longer needs to quote them.

What are the benefits of Portable IBANs?

To Corporates:

- Portable IBANs would increase competition in payment services, enabling customers to change banks without changing account numbers. In other network industries, e.g. mobile telecom, portable addresses have tightened competition considerably.
- The easing of company mergers or restructuring. If your receivables accounts have Portable IBANs, then it is easy to redirect funds to the new post-merger accounts. Most importantly trading partners need make no changes to their systems.
- Since multiple Portable IBANs can also point to a single account, you can use Portable IBANs to set up a sub-accounting structure for easier tracking of funds from different business lines or regions without having separate accounts.
- A reasonably sophisticated directory behind the Portable IBAN will effectively eliminate the need for third parties to maintain a directory of Corporate Standard Settlement Instructions⁴ ("SSIs").
- There would be no need to quote a BIC in addition to the IBAN. The routing bank\ACH will have all the necessary routing information.

To banks:

Although the concept of portable accounts to many banks is anathema, there are in fact a number of benefits that they can derive from requiring IBAN only information and then to automatically generate the correct routing and identifying BICs from a IBAN-BIC cross-reference table.

- **BIC changes.** BICs change essentially as a result of: mergers, name changes and SWIFT status changes. A Portable IBAN-only solution has less maintenance need compared to one where customers have to be informed about BIC changes that have to be implemented in all their systems, invoicing forms etc.
- **Key in costs.** Given 12 billion credit transfers and 10 billion direct debits (per Blue Book 2002) in the euro area there are approximately 15 billion BICs to be keyed in every year.⁵

³ It is understood that the European Payments Council is already considering whether this requirement from the customer for BIC plus IBAN should be simplified to IBAN only.

⁴ SSIs - Some corporates request that certain payments are made to specific accounts. With enough flexibility built into the electronic tools provided to the owner of the IBAN, this could allow the owner to also specify different accounts for different currencies and for different amounts.

This would translate into about 10,000 man years⁶. This calculation shows that there is a clear advantage in creating an automated IBAN-BIC cross-reference table instead of keying in redundant data.

- **Conflicting data and data input errors.** The IBAN has a good international check digit system. The BIC has no check digit and there is no mathematical check that a given IBAN belongs to a specific BIC. Furthermore, BICs are 11 character alphabetic codes, in which key-in errors can be frequent. Automatic BIC cross-referencing would reduce/eliminate these errors.

Implementation issues

All customers in Europe have been assigned Fixed, Non-Portable IBANs. It is also the case that each country has implemented the IBAN standard to accommodate national legacy routing systems.

Portability will have a deep impact in the European payments structure. To make fundamental changes, such as the implementation of SEPA, takes a long time e.g. about 10 years for SEPA. Therefore, any changes proposed must be as easy and as cheap to implement as possible.

SEPA is designed to be one common payment area and therefore it is desirable to have a single standard for Portable IBANs within the EU. However, in practice if the concept of Portable IBANs is to be accepted, it must accept the realities and limitations imposed by the current infrastructure. To impose a single EU Portable IBAN would require a fundamental change to existing payment and clearing systems – and therefore cannot be envisaged in the near future.

Implementing a system whereby current Fixed, Non-Portable IBANs could become Portable IBANs is the only way forward that can be envisaged to allow for a relatively quick and cheap solution. Furthermore, this provides the flexibility for each Country\ACH to effect implementation according to national timetables and changeover conventions.

At a later stage, should the European Commission deem it desirable, a EU-wide new IBAN standard could be created, so allowing for a 2-stage process for the implementation of Portable IBANs.⁷ However, as discussed below, the issues surrounding such a EU-wide single standard will take some debate to resolve.

Two Stage Implementation?

First Stage – Allowing for existing Fixed, Non-Portable IBANs to become Portable

These IBANs would have no outward difference in appearance to fixed, non-portable IBANs and therefore payments to these accounts would be forwarded to the correspondent in the country indicated by the IBAN and from there to the appropriate national ACH or other acceptable payment processing infrastructures.

In order to work therefore, the national ACH would have to be the point where the details of current routing for given IBANs must be registered. This would mean that customers would be tied to a given ACH serving a given number of banks. Therefore, all transactions have to pass via that ACH and the ACH would secure its market monopoly.

The market would have to accept this level of national monopoly as the price to pay for portability⁸. The question to be answered is whether this national monopoly is better than a monopoly at bank level. If this monopoly is acceptable, then the portability of accounts could be introduced with just one European ACH agreeing to implement the system.

⁵ If BICs were to be supplied each time for all paper-based credit transfers and all one-shot direct debits and approximately every fifth time for electronic credit transfers and direct debits (based on the possibility of storing the information).

⁶ If the work time for keying the BIC information is assumed to be 3.6 seconds (a moderate assumption considering the code complexity and checking need) – or 15 million work hours.

⁷ This example would be similar to the url system, where national schemes already existed for a long (e.g. .co.uk, .fr, .de .it, etc.) but are now complemented with a European-wide scheme (“.eu”).

⁸ This approach would appear to be no different than that for the EU Telecom industry. EU legislation created portability of numbers within the EU territories – but only within national boundaries.

Second Stage – A single Portable EU IBAN Standard

In SEPA it would be more consistent if the portability were EU-wide, i.e. customers could change bank freely within the euro/EU area without changing bank account numbers (IBAN). However, prior to its introduction a European-wide solution would need to have in place its own setup, which would include national sending and receiving capabilities and administration services in all the countries.

Then the following issues would have to be resolved:

- Who would be authorised to issue the new IBANs?
- How to avoid issuing duplicates by different issuing entities?
- Who would maintain the portable indirect reference table?

The portable indirect reference table needs to have one or more maintaining/administrating institutions that would, on the basis of customer requests, update the pointer of a given portable number to the new current direct account.

- What would be the new structure of the EU IBAN?

A suggested structure could be something along the lines of:

Country Code	Check Digit	Account Number
EU	2n	10n

The EU IBAN in this case would therefore contain a total of 14 characters – shorter than the current shortest IBAN in use (16 characters – moving to 16 characters would allow an increase in the account number length to 12).

In this format there is no need to identify the issuer, provided that the directory of Portable EU IBANs and their routing details are equally available to all ACHs.

In this example there are 10 characters available for the account number – the shorter this is the easier it is to remember and the less likely key-in errors will occur. However:

1. are 10 characters enough?
 2. should alpha characters be allowed – or simply digits?
- What Legislation would be required and by when?

As noted above, even for Stage 1, at a very minimum the requirement to quote BICS with IBANs would have to be relaxed.

Authorities will only act if they can be convinced that this is a very necessary issue and will bring political good will from the society. Therefore, how can the "lobby groups", such as TWIST, convince the appropriate authorities that this is a necessary issue?

What structural issues need to be addressed for Portable IBANs to be adopted within SEPA?

The electronic systems for giving control over the issuance and maintenance of Portable IBANs and the portable indirect reference tables behind them would have to be put into place. These tables would then have to be integrated within the relevant payment systems in order to provide the current routing information.

In order to generate critical mass, a marketing campaign informing industry of the benefits of Portable IBANs would have to be undertaken – and financed.

Cost issues

Even though portability will bring cost benefits and new efficiencies to the industry, any introduction of portable accounts will involve some extra set-up and maintenance costs – new technical

infrastructure, marketing, training etc. The question who is to pay for this? Probably those who would expect to gain most – the corporates and those ACHs which offer Portable IBAN facilities.

European banks have stated that introducing portability would be costly. However, maintenance and usage of portability features in a real-time network environment with modern tools are relatively low in costs, as has also been shown in other industries. Indeed, examples of portable account numbers for which cost has not been an issue can be found in Scandinavia, The Netherlands and USA (the UPIC of NYCH).

Therefore, perhaps this position by the European banks can be interpreted simply as reluctance to pay for a system which would only increase competitive pressures within the banking industry. However, It must be recognised that banks will be reluctant to promote Portable IBANs if they just increase competition and costs without generating any income. On the other hand if ACHs sponsor Portable IBANs, and the major corporates demand the service, perhaps the banks will find themselves with a fait-accomplis.

Portable Accounts – Concept Proven

In Scandinavia and The Netherlands, portable account number schemes have been provided at a local (national) level. In these cases, the clearing centre keeps track of which bank account the clearing centre number should point to at a given time.

What is needed to make Portable IBANs available to the market?

There are basically two ways of creating portability for IBANs:

1. Market Solution: - One or more national ACHs, supported by a few major corporates, agree that they put into effect a portability scheme.
2. Legislation: - The EU Commission decides that it is important to promote competition and therefore regulates for portability (e.g. as for mobile phones)."

Of the two scenarios, the fastest that could be expected to be implemented is the Market Solution. However, even here, the issue of the formal requirement for BIC plus IBAN needs to be dealt with; at least at the level of the European Payments Council, if not the EU Commission itself. Discussions need to be had with these two bodies to understand what issues if any could impact on a Market Solution.

Conclusions

SEPA is certainly having a major impact on the European payments scene and will go a long way to improve payment flows across European borders. However, there is a danger that these benefits will not go as far as they could and indeed could introduce new, unintended rigidities.

The adoption of Portable IBANs could provide the final key to realising the whole spirit behind SEPA – the creation of an efficient, low-cost, flexible payments service within Europe. Furthermore, although this paper has been written largely with the corporates in mind, it is the opinion of the author that it should also be extended to individuals.

It is very important to understand that there is no difference in structure whatsoever between one type of IBAN and the other. No new IBANs need be issued. Any Fixed, Non-Portable IBAN could be registered with the appropriate ACH as being Portable. The owner of the IBAN is then given the electronic tools to redirect payments away from the original account – everything else stays the same. This factor means that the 2 stage approach suggested here:

1. would not disturb SEPA's implementation.
2. would not require a fundamental change to existing systems – and therefore can be envisaged for the (very) near future.

All these issues and ideas are very much part of on-going debate. Through its Identifiers Working Group, TWIST is bringing together Corporates, Financial Services Providers and Solutions Providers to help this debate to come to full fruition. If you wish to join the TWIST Identifiers Working Group to ensure that your views get heard and to contribute to seeking agreement on requirements and solutions in this domain, then you should get in touch with pguldentops@twiststandards.org.

Notes to Editors:

About CB.Net

CB.Net is a data provider dedicated to the delivery of reference data solutions to the global banking community. Established in June 2000 by a group of ex-bankers and IT professionals. London-based CB.Net recognises the importance of reliable reference data in being a major contributor to cost savings and greater efficiency in international payments and compliance requirements. The strategic focus of CB.Net is to develop products and solutions for the international payments industry which are innovative, operationally useful, and easy to implement.

CB.Net's flagship product, BankSearchPlus™, is the definitive international payments directory, delivering critical operational data in one source – both as a web based query tool and as a data feed – directly into back office systems.

CB.Net has an impressive portfolio of clients in over 40 countries, including leading bank groups

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About TWIST Process Innovations Ltd (www.twiststandards.org)

The Transaction Workflow Innovation Standards Team (TWIST), led by an executive team drawn from across the industry, is a not-for-profit industry group of corporate treasurers, fund managers, banks, system suppliers, electronic trading platforms, market infrastructures and professional services firms. The primary aim of the TWIST organization is to connect the financial supply chain to the physical supply chain to release the enormous value locked up in disjointed paper-based processes. To achieve this, TWIST rationalizes financial industry standards by creating user-driven, non-proprietary and internally consistent XML-based standards for the financial supply chain. TWIST covers wholesale financial market transaction processing, order management, e-invoicing and payment processing, bank account opening and closing, billing of bank services, credit management, supply chain financing plus identity management and security. TWIST also participates in the management of the ISO 20022 standards for financial markets aiming to make this the umbrella for its comprehensive suite of standards.

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