

Creation of the SEPA and its impacts on companies in Finland

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Bachelor's Thesis
DP in International Business
2010



Degree programme

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<p>The title of your thesis Creation the SEPA and its impacts on companies in Finland</p>	<p>Number of pages and appendices 61+5</p>
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<p>The long integration process of European monetary policy has taken long step during the last decade. First the euro was introduced in 1999 and now the European payment system is being standardized. SEPA means Single Euro Payments Area. Its purpose is to standardize and to create more efficient payment systems in the euro area. SEPA consist of all EU euro zone countries, EU non-euro zone countries and EEA zone countries. The first steps of implementation of SEPA were conducted in beginning of 2007, when the IBAN account number was taken into use in the euro area.</p> <p>The objective of this thesis was to study the shift from national payment transactions to a European payment practice SEPA. Hence cash management is an important part of business, and especially it is crucial to ensure the sufficient volume of money available for the business. Managing short-term financing, controlling the cash flows and choosing and maintaining good bank relations are all important aspects of cash management. Therefore, aim was to gain thorough understanding of how these changes in payment methods affect medium and large sized companies' operating in Finland and especially to their cash and liquidity management.</p> <p>The study of this thesis was conducted through a qualitative research. Theory was based on literature published on the subject. Background information of SEPA was collected mainly from various sources of the Internet and colleagues from Sampo Bank. This is because there was a lack of relevant literature at the time this thesis was done. Moreover, researcher's own findings and working experience in banking industry was used to gather source material.</p> <p>The findings indicated that the knowledge of SEPA among medium and large companies was relatively good, and mainly proper preparatory actions have been taken. As there is still transition time left, companies were not in haste to make changes to their payment systems. In this thesis, it appears that moving towards SEPA is a very challenging project but also beneficial to all stakeholders.</p>	
<p>Key words SEPA, cash management, liquidity management</p>	

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Terminology

BIC

Bank Identifier Code. Also referred to as SWIFT code. The BIC of the beneficiary's bank is required for cross-border credit transfers in the EU and EEA.

B2C

Bank to Customer - from the bank to the customer.

C2B

Customer to Bank - from the customer to the bank.

EBA

Euro Banking Association - service centre providing settlement and cover transfer services regarding interbank payments; an ACH (automated clearinghouse), which banks use in SEPA payments.

ECB

European Central Bank

EEC

An international organization of European countries formed after World War II to reduce trade barriers and increase cooperation among its members.

EMI

European Monetary Institute was the forerunner of ECB

EMS

European Monetary System

EMU

European Monetary Union is an agreement by participating European Union member countries that includes protocols for the pooling of currency reserves and the introduction of a common currency.

EMV

Europay MasterCard Visa - standard for new chip-based debit cards in international common use.

EPC

European Payments Council - a European decision-making body common to European banks in European-wide payment matters. A body developing the SEPA standards and rules.

ERM

Exchange Rate Mechanism

ESBC

The European System of Central Banks is a composition of ECB and the national central banks of all 27 EU Member States.

EU payment

An EU payment is euro-denominated. A cross-border account transfer between and within the member states of the European Union, Iceland, Norway and Liechtenstein. EU payments are transferred at the price of domestic account transfers. The SEPA account transfer will replace the EU payment.

FTP

File Transfer Protocol

IBAN

International Bank Account Number. The beneficiary's IBAN is required for cross-border credit transfers in the EU and EEA.

ISO

International Organization for Standardization. See <http://www.iso.org/>.

PSD

Payment Service Directive prepared by European Commission to harmonize legislation on payment services, which shall be incorporated into the national legislation of all EU Member States.

PE-ACH

Pan-European Automated Clearing House - a clearing system for payment transfers between European banks.

PKI

Public Key Infrastructure

PATU

Banks' customer connection information security. PATU is used for identifying the customer and the bank and ensuring the invariability of material transmitted between companies and organizations and the banks. It cannot be used for encrypting data. PATU is poorly adapted to securing XML data.

SEA

Single European Act was the first major revision of the 1957 Treaty of Rome

SEPA

Single Euro Payments Area

SEPA Credit Transfer

SEPA account transfer, which meets the pan-European rules and standards within the Single Euro Payments Area.

SEPA Direct Debit

SEPA direct debit meets the pan-European rules and standards within SEPA.

SME

Micro, small and medium-sized enterprises

SWIFT

SWIFT, Society for Worldwide Interbank Financial Telecommunication. A bank-owned transmitter of payment messages and supplier of interface software for cross-border interbank payments.

Web Services

A software product based on open standards that support compatible interactive data transmission between computers. The encrypted connection (HTTPS) means that no separate encryption is required.

UNIFI (ISO 20022) XML standard

A standard agreed to be used in uniform European credit transfer and direct debit transactions and the European standardization of customer connections.

1 Introduction

1.1 General introduction

This report is a research-oriented bachelor's thesis in Haaga-Helia University of Applied Sciences. The subject concerns the creation of Single Euro Payments Area (SEPA) and its impacts on medium and large companies in Finland and especially companies that have operations across Europe, and hence have international payment transactions.

Along with the creation of European Union and integration of monetary policy, financial environment has changed tremendously in Europe. Substantial changes such as introduction of euro and now implementation of SEPA in motion create challenges and opportunities for companies' financial management.

Cash management is a vital function in a company, and significant savings can be achieved with proper management of it. Efficient cash management relieves working capital and thus improves company's profitability. Now it is crucial for companies to take advantage of possible opportunities from the forthcoming changes in order to prepare themselves to maintain operational and competitive in changing environment.

The subject is current, because the implementation process of SEPA has began already in beginning of year 2008 and utmost importance because the transition period will endure only till the end of end of year 2010.

1.2 Objectives of the Thesis

The level of knowledge in many companies concerning SEPA is adequate and possible benefits from SEPA to companies are not necessarily clear. Relieving though is that several companies have started to prepare to the forthcoming changes. In addition, companies and the banking industry in Finland are struggling to keep up with the tight deadlines of the transition process. In addition, companies and the banking industry in Finland are struggling to keep up with the tight deadlines of the transition process.

The main objective of the thesis is to learn what SEPA is, how it will affect medium and large sized companies in Finland, and how companies can manage and control these changes.

In order to understand this huge transition process that affects the whole Europe, it is important to provide historical background for it. What events have led to this situation, and why banks, governments and various institutions are contributing to the SEPA integration. Therefore, the development of European monetary integration and the reasons for it are thoroughly examined and explained.

1.3 Research problem

The thesis aims to answer following research questions related to the topic: "Creation of SEPA and its impacts on medium and large companies in Finland".

- What changes SEPA creates to payment transactions and how will these changes affect companies' cash management?
- How companies can prepare themselves for SEPA?
- How companies can benefit from SEPA?

1.4 Significance

It can be said that the SEPA project is bigger change in European financial markets than the introduction of Euro, or maybe even the largest and most important since beginning of 20th century. It affects all European countries, institutions, companies and natural persons.

Though, there have been much discussion about SEPA and its importance in the media, companies' interest towards it and preparations for it have been relatively low.

Although there are multiple surveys done by various facets concerning the subject, the process of SEPA is developing continuously and updated information is needed. Therefore, the findings of this research will be significantly important and useful for outlining the whole process that companies have to do in order to cope with forthcoming changes.

1.5 Structure and limiting

Common understanding is that companies have not prepared well enough for SEPA. Instead of concentrating on a single company and its operations, wider perspective is taken to study the subject. The research was conducted to find out the knowledge of medium and large companies concerning SEPA and what is their readiness for SEPA at the moment. There have been conducted multiple researches abroad, thus the object of this research was to clarify the situation in Finland. In addition to company interviews, comprehensive perspective is guaran-

ted by taken into account EPC's, banks and software houses' point of view. Furthermore, this study concentrates on how communication between banks and companies will change, how foreign payments will change and how SEPA affects on payment standards. Though, SEPA will also change Direct Debit procedures, this subject is left for less attention. Also new payment cards and E-invoicing is left out from this particular survey, in order to turn focus into payment processes and companies liquidity management.

Companies were selected carefully according to certain criteria in order to gain comprehensive picture of the transition state in Finland. Moreover, this was guaranteed by choosing companies to the survey from different business fields, such as healthcare, cloth wholesale, retail, and cosmetics. Furthermore, this survey concentrates on medium and large companies, because impact of SEPA is more extensive and the implementation processes are more complex and require more resources from large companies than from small companies. Hence the information that would be received from small companies, would not present how large and important transition process SEPA is for companies.

2 Financial management

In a well-organized business, each section should arrange its activities to maximize its contribution towards the attainment of corporate goals. The finance function is very sharply focused, its activities being specific to the financial aspects of management decisions. The finance functions can be structured as illustrated in Figure 1.1.

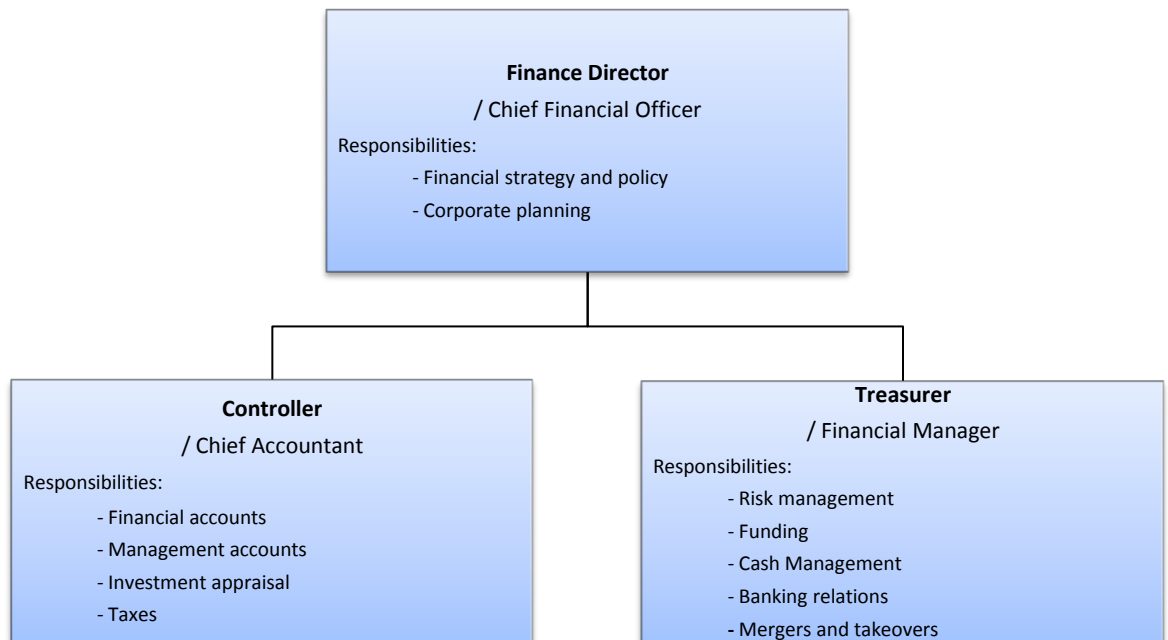


Figure 1.1 The financial function in large company (Pike & Neal 2009, 6)

It is the task of the accounting and finance functions that are shown in the figure above to plan, raise and use funds in an efficient manner to achieve corporate financial objectives, and the two main activities are:

1. Providing the link between the business and the wider financial environment.
2. Investment and financial analysis and decision-making.

The finance function provides link between the firm and the financial markets in which funds are raised and the company's shares and other financial instruments are traded. The financial manager, whether a corporate treasurer in a multinational company or the sole trader of a small business acts as the vital link between financial markets and the firm. Corporate finance is therefore as much about understanding financial markets as it is about good financial management within the business. (Pike & Neale 2009, 5-6)

For any company, there are likely to be many different corporate goals, some of which may end up in conflict. For instance, finance and marketing departments may end up in a conflict for having different opinion on certain issues. Often in finance point of view, the aim of the company is to maximize shareholder value. According to Pike & Neale (2009, 10), the financial manager can pursue the corporate objectives in the following ways:

1. *Strategic investment and financing decisions.* The financial manager must raise the finance to fund growth and assist in the appraisal of key capital projects.
2. *Dealing with capital markets.* The financial manager, as the intermediary between the markets and the company, must develop good links with the company's bankers and other major financiers, and be aware of the appropriate sources of finance for corporate requirements.
3. *Managing exposure to risk.* The finance manager should ensure that exposure to adverse movements in interest and exchange rates are adequately managed. Various techniques for hedging are available.
4. *Forecasting, coordination and control.* Virtually all important business decisions have financial implications. The financial manager should assist in and, where appropriate, coordinate and control activities that have significant impact on cash flow.

2.1 Short-term financing

Financial planning in general creates a board net of problems as a whole, therefore, financial managers who are responsible of it use most of their time trying to solve short-term financing problems. These problems can be for instance granting credit, specifying the optimal level of the payment date of invoices and bank account balances, and determining the needs for short-term investments and borrowings. Short-term financing includes all the decisions which affect company's activities in short-term, usually less than one year time period. (Niskanen & Niskanen 2007, 365)

Short-term financing can be divided into six fundamental sectors as shown in figure 2.1. Short-term financing decisions mostly concern inventory management, accounts receivables, accounts payables, cash, short-term investments and loans. (Niskanen & Niskanen 2007, 366)

Cash budgeting has an essential role in short-term financing, in order to predict the future cash flows as precisely as possible. This way the successful planning of short-term investments and loans is secured. (Niskanen & Niskanen 2007, 366)

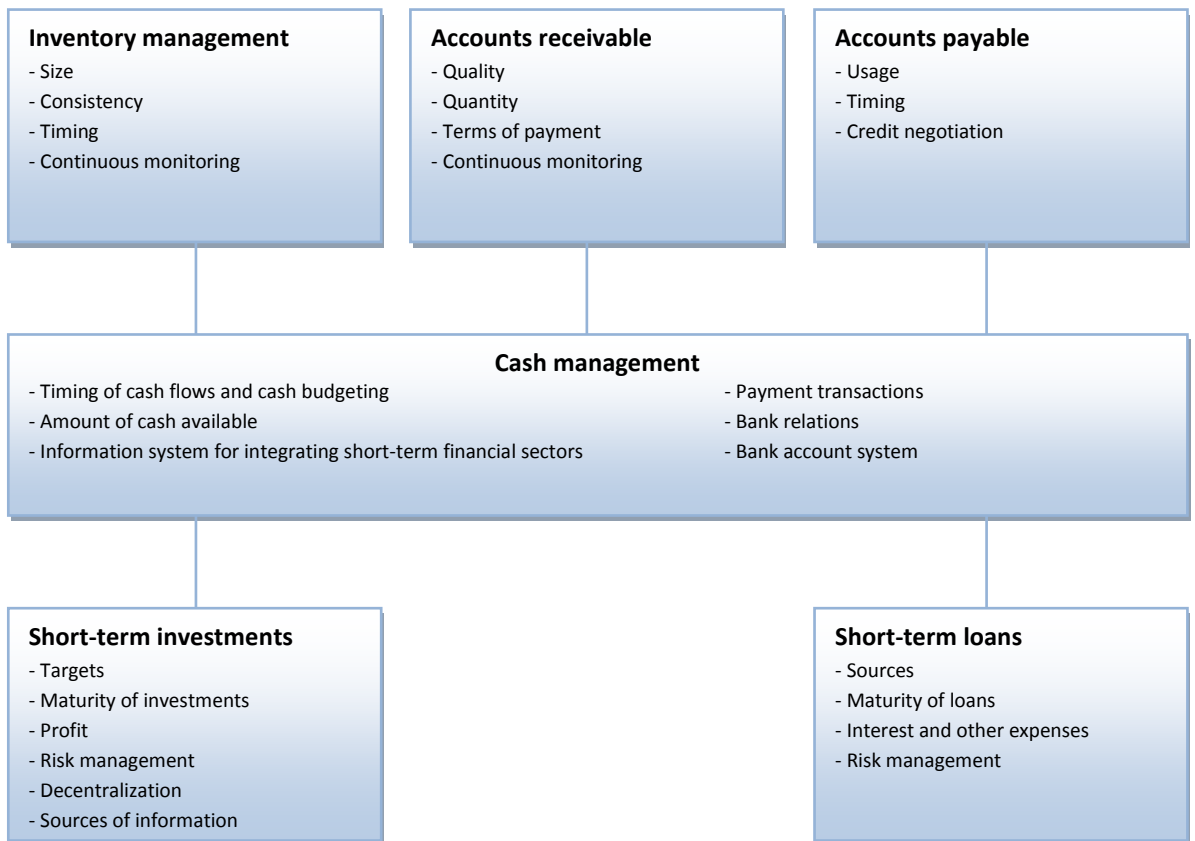


Figure 2.1 The six fundamental sectors of short-term financing (Niskanen & Niskanen 2007, 366)

3 Cash management

Cash brings security and risk considerations and its handling costs are relatively high. Though cash gives the recipient same-day value since it can be used immediately to make payments, the use of cash is in general decline. (Cooper 2004, 266)

Though use of cash is generally in decline, central to the whole of finance is the generation and management of cash. Pike and Neale (2009) see the cash as “lifeblood” of the business, flowing to all essential parts of the corporate body (Figure 3.1). If the flow of cash is not managed properly and there occurs disturbances which are not addressed in time, it can prove fatal to the company.

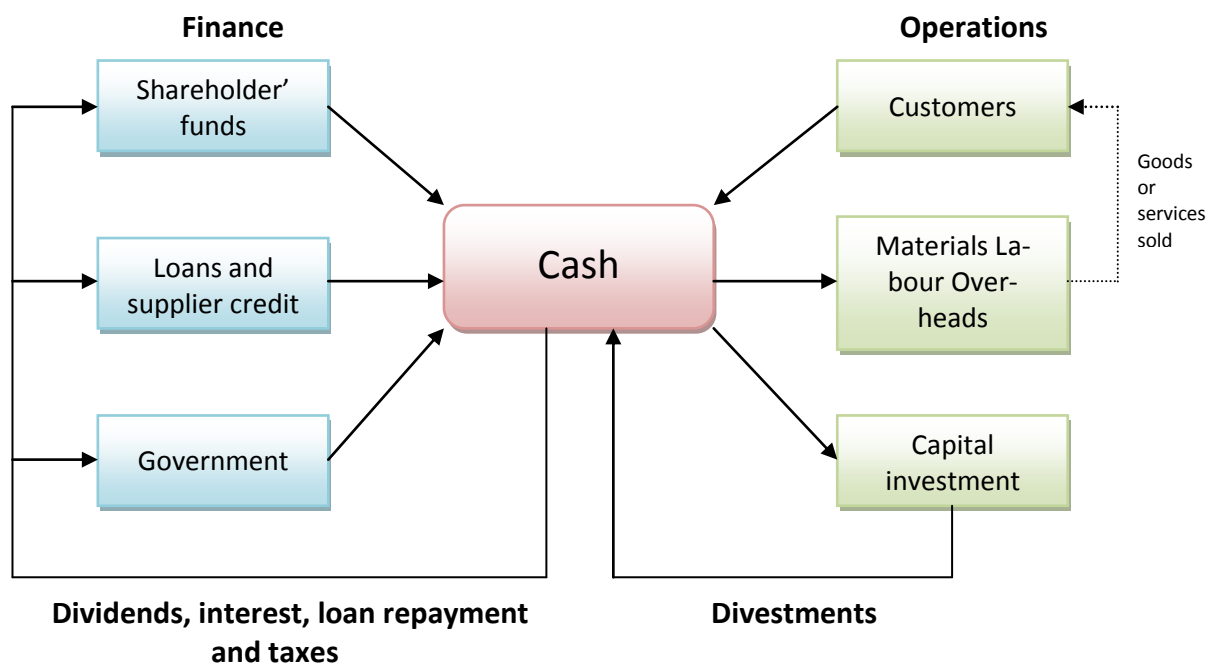


Figure 3.1 Example of cash flow structure in large company (Pike & Neale 2009, 7)

Cash management in simplistic terms, is most commonly described as the way that a business administers and invests its cash in other words, liquidity. However, cash management brings together many various functions associated with short-term financial flow management: liquidity management, banking management, management of treasury surpluses and deficits and financial risk management; it is a broader concept than the mere management of payments and collections (Iturralde, Maseda & San José 2008, 194).

Robert Cooper (2004, 320) condenses the objectives of cash management to following activities:

- Minimize the time involved in converting receipts into usable funds
- Concentrate those funds into a central account where they can be most effectively managed
- Control and minimize the cost of payments
- Reduce or eliminate borrowings

It is worth remembering that the treasury cash manager only manages cash at one narrow point of the company's business cycle. That is from the time that receipts become usable funds until the time those funds are used again to make payments. However, an organization is concerned with the effective management of cash at every point of business cycle. For instance, efficient working capital management will in practice be linked to a company's production, sales and marketing and administrative controls. These are established to ensure an efficient control over company's business processes and to minimize the use of working capital.

According to Pike and Neale (2009, 363) and Leppiniemi (2009, 173) there are a number of reasons why companies hold cash balances:

- *Transaction motive.* Day-to-day cash inflows and outflows do not match perfectly; cash serves as a buffer to ensure that transactions occur at the appropriate time. Cash balances are particularly important where the patterns of cash inflows and outflows differ greatly, e.g. where business is highly seasonal.
- *Precautionary motive.* Cash flows are often difficult to predict. Cash balances are required to cater for unanticipated cash disbursements.
- *Speculative motive.* Cash flows allow the business to be highly flexible and to exploit wealth creating opportunities more easily. Large are common among acquisitive companies where a cash alternative to takeover bid is required.
- *Compensation balances motive.* Banks provide range of financial services, many of which are 'free' as long the company keeps a positive bank balance.

Good knowledge of financial markets reduces the need of cash balance, and consequently especially importances of precautionary and speculative motives are decreased (Leppiniemi 2009, 174).

3.1 Cash flow

Cash is the lifeblood of every business. For a business to stay healthy, it is cash, not accounting that matters. This may sound like a contradiction, but many profitable, fast-growing companies have gone out of business because of desynchronized inflow and outflow of cash. This causes a deficit or a surplus to cash but managing your working capital efficiently can ease these liquidity problems. (Hickman, Hunter & Byrd 1996, 104; Niskanen & Niskanen 2007, 367-368)

Often the cash inflow and outflow will not schedule optimally; therefore, a need for short-time investments or loans will occur. Though at one time a company may have to find uses for excess cash; and at other, it may have to raise cash to pay bills. Such activity does not necessarily indicate poor management; it simply reflects the uneven timing of cash flows in companies. Iturralde et al. (2008) stated that to prevent breaks or gaps in the trading cycle due to lack of cash, administrators must calculate the cash amount best suited to their level of activity, plan the right timing of the relevant payments and collections and draw up a policy of investment in assets with high liquidity that can be converted to cash at a low transaction cost to serve as support for the treasury funds maintained by the company (Kamath, Khaksari & Hylton, 1985). Hence, it is important to establish right level of disposable assets to be used as short-term investments. Moreover, wrong amount of cash or disposable assets may interrupt the normal flow of the company's business operations and company may also be unable to take advantage of unexpected investment opportunities. Maintaining the right amount of cash surplus helps companies to manage normal transactions caused by business activities and also cover unexpected need of cash.

Surplus cash is not always reinvested immediately in the business. The cash-or near cash-balance in some companies can be far greater than required for normal trading purposes. The financial press publishes the main types of short-term financial investment opportunities available to companies, showing the relationship between maturity and interest rate. Pike & Neale 2009, 364)

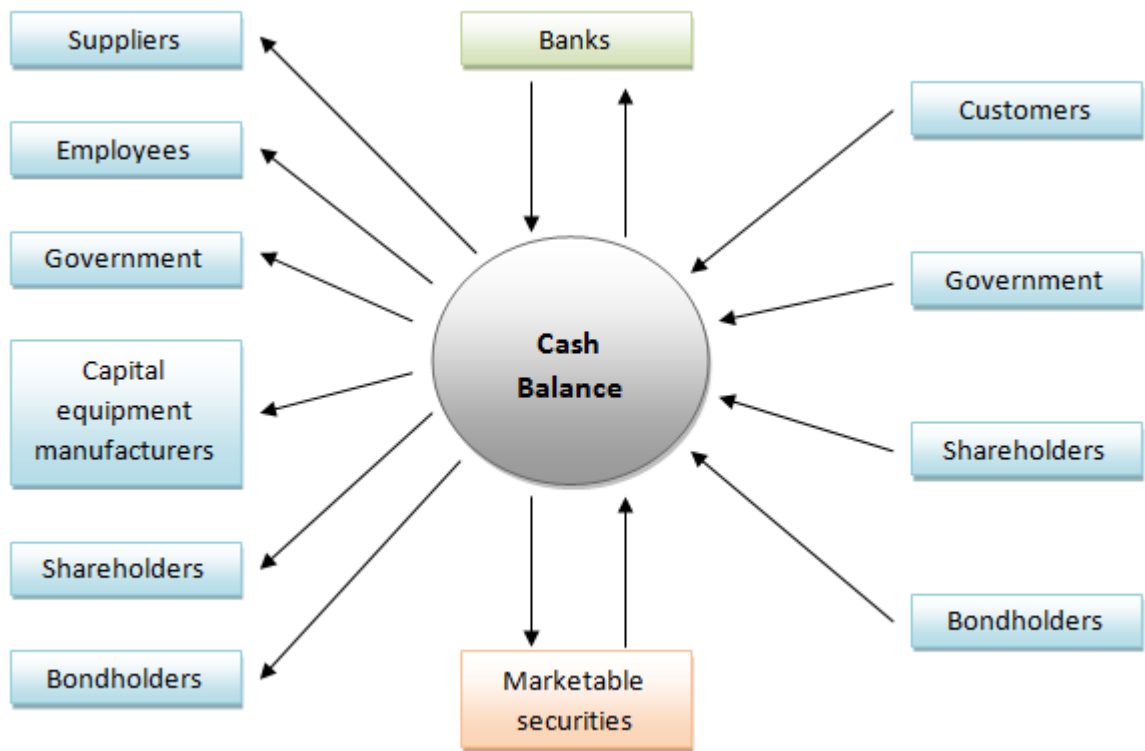


Figure 3.2 Cash flow activities for main stakeholders (Pike & Neale 2006, 364)

According to Pike and Neale (2009, 364), the figure above demonstrates the pivotal role played by cash in a typical business. The cash balance is the result of the interaction of various activities with stakeholders.

- Operating activities – cash from customers fewer payments to employees and suppliers.
- Servicing finance – dividends and interest on loans
- Taxation – Corporation Tax VAT.
- Investing activities – purchase and sale of fixed assets.
- Financing activities – new finance from shareholders and bondholders, and loan repayments.

The cash balance is restored to its appropriate level by short-term bank borrowing or repayment and the sale or purchase of marketable securities. The financial manager should therefore project the firm's ability to finance its operations and to manage corporate cash flows. (Pike & Neale 2006, 364)

3.2 Working capital

Net working capital or simply working capital refers to current assets less current liabilities. Current assets include cash, marketable securities, debtors and stock, whereas current liabilities are obligations that are expected to be repaid within one year (Pike & Neale 2009, 334). Working capital management refers to the financing, investment and control of net current assets within policy guidelines.

The treasury manager should ensure that the firm operates sound working capital policies. These policies cover such areas as level of cash and stock held, and the credit terms granted to customers and agreed with suppliers. Successful implementation of these policies influences the company's expected future returns and associated risk, which, in turn, influence shareholder value. Pike and Neale (2009, 388) states that failure to adopt sound working capital policies may jeopardize long-term growth and even corporate survival. For example:

1. Failure to invest working capital to expand production and sales may result in lost orders and profits.
2. Failure to maintain current assets that can quickly be turned into cash can affect corporate liquidity, damage the firm's credit rating and increase borrowing costs.
3. Poor control over working capital is a major reason for overtrading problems.

Shapiro (2010, 667) argues that the essential difference between domestic and international working capital management include the impact of currency fluctuations, potential exchange controls, and multiple tax jurisdictions on these decisions, in addition to the wider range of short-term financing and investment options available.

3.3 Payment transactions

An essential criterion in cash management is efficiency of cash inflows and outflows in order to reduce barren or low profit assets and also the non-profitable payment days. To intensify the decisions of payment transactions, the sender and the receiver of the invoice must go into details of various payment transaction methods and technology, and maintain good bank relations to gain all possible benefits available. Moreover, it is essential to develop information systems for company's cash management so that information of incoming payments and the time when the funds will be in use is known as soon as possible. Bank account decisions are important to payment transactions; therefore, company's funds should be deposited in an ac-

count that gives the best possible interest and meets the requirements of company's risk levels. (Leppiniemi 2009, 179)

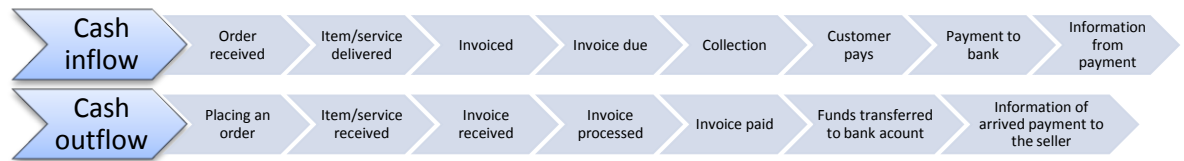


Figure 3.3 Process of cash inflow and cash outflow (Leppiniemi 2009, 167-169)

As shown above in figure 3.3, managing the cash inflow and outflow in a corporation is multifaceted operation, involving various departments, processes and employees; for instance credit management, pricing, invoicing, accounts receivable, deduction and collections. Essential in management of sales revenues is to accelerate cash inflow to avoid possible or react to delays in cash inflows and cash deficit. Leppiniemi (2009, 167-168) states that efficiency of the processes can be developed that time used between receiving the order and getting the payment is shortened. First of all, the internal processes can be developed: delivering of an order, synchronizing invoicing and delivery and reminder of debt collection. Moreover, the payment transactions and bank relations can be improved so that the payment will come to the receiver's account as shortly as possible when the customer has paid the invoice. Important for the management of inflow of cash is to receive information of the payment instantly after it has actualized.

In figure 3.3, when thinking of cash inflow, the most important step for a company is the 'Customer pays'. This is when the forecast of company receivables realize, and money is credited to account. This affects greatly to company's cash forecasting and planning of cash outflow, and especially when the invoice is actually paid and the account is debited.

Ideally, during the business cycle, company will have more money flowing in than out to build up proper cash balance. Rarely though income and expenditure cash flows occur together, with inflows often lagging behind. Therefore, aim is to speed up the inflows of cash and slow down the outflows of cash, which can also be achieved by developing the internal routines. Development areas can be for example in quantity of purchase, improvement of inventory, work and planning methods (Leppiniemi 2009, 169).

Payment transactions are closely related to a company's cash management. It is basically question of how to increase profit feasibility and how to cut costs. Successful payment transaction decisions can benefit the company's business operations more than mere cash management. Connections of payment transactions which banks offer can be combined with comprehensive information and reporting services. (Leppiniemi 2009, 180)

From cash management point of view, in payment transactions, focus is put into float time costs which derive from lingering payments. Float time days are unprofitable days for company, when the payment is being processed and is under its way (Kauppila 2009; Leppiniemi 2009, 180).

Furthermore, direct costs deriving from payment transactions are important issue in company's cash management. First of all, costs can arise from creation and maintenance of payments systems, submitting and paying the invoices; and from the value date practice applied by banks. (Leppiniemi 2009, 181)

3.4 Bank relations

In banking activities, the importance of information and communication technology and related services provided is increasing. Importance of banks in companies' cash management is often remarkable explains Leppiniemi (2009, 136; 178-179). With good bank relations can be created flexibility for both; cash deficit and cash surplus. Banks' transactions systems and connections in domestic and foreign payments are important part of company's successful cash management. Moreover, company has to integrate its own systems to fully exploit the banks' transaction systems.

Though company may be satisfied with bank's cash management services, they may not realize that they are being poorly served by their bank. Alan Shapiro (2010, 682-683) argues that poor cash management services mean lost of interest revenues, overpriced services, and inappropriate or redundant services. Shapiro summarizes common problems of bank relations to four issues:

1. *Too many relations.* Using too many banks can be expensive. It also invariably generates idle balances, higher compensating balances, more check clearing float, and diminished control over every aspect of banking relations.
2. *High banking costs.* Treasury management must carefully track not only direct costs of banking services – including rates, spreads, and commissions – but also the indirect

costs rising from check float, value dating, that is when value is given for funds – and compensating balances. This is not crucial only in developing countries, but also in European countries such as Italy, where banks enjoy value dating periods of as long as 20 25 days.

3. *Inadequate reporting.* Bank often do not provide immediate information on collections and bank account balances. This delay can cause excessive amounts of idle cash and prolonged float. To avoid such problems, firms should instruct their banks to provide daily balance information and to distinguish clearly between ledger and collected balances.
4. *Excessive clearing days.* In many countries, bank float can rob firms of funds availability. In such nations as Spain and Italy, checks drawn on banks located in remote areas can take weeks to clear to headquarters accounts in the capital city.

4 The development of European monetary cooperation

4.1 The origins for cooperation

The 20th century has been terribly unprofitable for Europe and its nations. In the beginning of the century Europe was the wealthiest, most sophisticated and developed continent in the world. One might say the centre of the world and yet the leading nations were drifted to a long range of wars. The First World War destroyed orderliness which had endured hundred years and as Sir Edward Grey, the British Foreign Minister at the time, said “The lamps are going out all over Europe; we shall not see them lit again in our lifetime” describes well the consequences of the WWI. The World Wars have had incredible impact on evolution of European countries. During the 20th century Europe has gone through vast changes regardless of watching for instance from political, legal or economical point of view.

Despite the wars and dictators striving to power, Europe continued to develop and economically integrate different nations. The idea of an economic and monetary union in Europe started well before the Treaties established the European Communities after the Second World War. For Example, already in the League of Nations in 1929, Gustav Stresemann proposed the creation of a European Union and a European currency against the background of an increased economic division due to a number of new nation states in Europe after the Treaty of Versailles (European Commission a.). The origins of EU derive from the World Wars. After 1945, there was a strong will to ensure that wars derived from nationalist conflicts would never again occur. Moreover, the ending of the war soon revealed that the wartime allies were, in fact divided with the two major powers, the USSR and the USA, were confronting each other in a bid for world supremacy. This led to series of schemes that culminated in the establishment of the European Economic Community (EEC) under the Treaty of Rome on 25 March 1957. This was the first step towards integrated Europe and which eventually became the EU (Appendix 1).

Since the establishment of the EEC in 1958, the movement towards more integrated European financial market has been marked by several events, of which the most important were the introduction of the euro in 1999 and its launch in 2002. When the Economic and Monetary Union (EMU) was created, the world's monetary and currency system begun a new era. The position of the dominant currency, the United States dollar, was challenged by the new common European currency, the euro. When the euro came to being, monetary policy became the responsibility of the independent European Central Bank (ECB), which was created

for that purpose, and the national central banks of the Member States having adopted the euro (European Commission b.). Since the adaptation of euro, integration has been relatively fast and new Member States have joined the Union. SEPA will renew the transaction system in whole Europe and continue the development towards more unified economical area in Europe, the process that was started at the creation of EEC.

4.2 Economic and Monetary Union (EMU)

Because of the Second World War, most currencies of the industrialized countries were tied closely to the US-Dollar under the so-called “gold standard” under the Bretton Woods system. The supremacy of the US-Dollar and forced devaluations of several European currencies led European politicians seek to correct this imbalance. The solution was to increase economic integration between European countries. Strong fluctuations of the European currencies against the US-Dollar implied even stronger exchange fluctuations between the European currencies. In 1979 the European Monetary System (EMS) was established to link European currencies and to prevent the high fluctuation among their respective values. It created an Exchange Rate Mechanism (ERM), under which the exchange rates of each member state’s currency was to be restricted to narrow fluctuations (+/-2.25%) on either side of a preference value. (EU4Journalists 2009.)

During the 1980’s the market of each Member state grew closer to its neighbors. Despite the stability brought by ERM, international trade was hindered by exchange-rate risk and high cost of transactions. Therefore, tension towards the integrated European monetary market increased. In June 1988 the EC confirmed the objective of the progressive realization of Economic and Monetary Union (EMU), which was laid down the Single European Act (SEA). It authorized a committee to study and propose concrete stages leading to this union. The chair of this committee was given to Jacques Delors, the President of the European Commission and the members of the committee were governors of the various national central banks. In 1989, Delors introduced a three stage implementation plan to create EMU. (European Central Bank 2009.)

The Plan was nonetheless ambitious in that it called for the irreversible stage-by-stage creation of a European economic and monetary union endowed with fundamental political significance. The Plan emphasizes the need to consult economic and social sectors before defining the guidelines of Community economic policy. Moreover, it pointed out that EMU presupposed a satisfactory level of economic growth, a high degree of employment, the abolition of

regional and social disparities, mobility of production factors, and the elimination of fiscal frontiers among the six Member States and the liberalization of world trade. (European Central Bank 2009.)

<p style="text-align: center;">Stage One 1.7.1990</p>	<p style="text-align: center;">Stage Two 1.1.1994</p>	<p style="text-align: center;">Stage Three 1.1.1999</p>
<ul style="list-style-type: none"> • Complete freedom for capital transactions • Increased co-operation between central banks • Free use of ECU (European Currency Unit, forerunner of the €) 	<ul style="list-style-type: none"> • Establishment of the European Monetary Institute (EMI) • Ban on the granting of central bank credit to the public sector • Strengthening of economic convergence • Process leading to the independence of the national central banks • Preparatory work for Stage Three 	<ul style="list-style-type: none"> • Irrevocable fixing of conversion rates • Introduction of euro • Conduct of the single monetary policy by the European System of Central Banks • Entry into effect of the intra-EU exchange rate mechanism (ERM II) • Entry into force of the Stability and Growth Pact

Figure 4.1 The three stages of Economic and Monetary Union (European Central Bank 2009.)

Stage One

In June 1989, on the basis of Delors report, the Stage One was to begin in 1 July 1990. The Stage One declared that all restrictions between Member States on the movement of capital were to be abolished. The Treaty of Maastricht in 1992 established the completion of the EMU as a formal objective and set a number of economic convergence criteria related to inflation rate, public finances, interest rates and exchange rate stability. Moreover, the Treaty of Maastricht identified 1999 as the year of the introduction of the single currency and the convergence criteria for Member States economy to adopt the single currency. (European Central Bank 2009.)

Stage Two

The establishment of a temporary EU body, the European Monetary Institute (EMI) on 1 January 1994 started the Stage Two of EMU. EMI's task was to strengthen monetary cooperation between the Member States and their national banks and to make the preparations required for the establishment of the European System of Central Banks (ESCB), hence it was basically the forerunner of the European Central Bank and in 1 June 1998 EMI was replaced by the ECB. (European Central Bank 2009.)

In December 1996 the EMI presented its report to the European Council, that formed the principles and fundamental elements of the new exchange rate mechanism (ERM II), which was adopted in June 1997. In addition, In order to complement and to specify the Treaty provisions on EMU, the European Council adopted the Stability and Growth Pact in June 1997. The Stability and Growth Pact is intended to ensure that Member States maintain budget discipline in order to avoid excessive deficits, and therefore contributes to monetary stability. (European Central Bank 2009.)

Stage Three

On 1 January 1999 EMU commenced the Stage Three. A single monetary policy was introduced under the responsibility of the ECB with the irrevocable fixing of interest rates of the currencies of the 11 Member States initially participating the Monetary Union. The European Monetary System EMS and its Exchange Rate Mechanism (ERM) were replaced with the commencement of Stage Three of the Exchange Rate Mechanism, ERM II. The ERM II made it possible to those European Union countries outside the euro area, to link their currency to the euro (Bank of Finland). Furthermore, the euro became a real currency and a three-year transition period begun before the launch of the actual euro notes and coins (European Central Bank 2009.).

For each state to adopt the new currency on 1 January 2002, they had to meet the “Convergence Criteria“ set out by the Maastricht Treaty. The criteria include four requirements (EU4Journalists 2009).

- Currencies has to stay within the bands set by the ERM for at least two years
- Long-term interest rates could not be more than two percentage points higher than those of the three, best-performing member states
- Inflation had to be below a reference value (within 3 years prices may not be higher than 1,5% of best performer)
- Government debt had to be below 60% of GDP (or moving towards this objective) and budget deficits below 3%

5 The Single Euro Payments Area

5.1 Overview of SEPA

The euro and EMU were catalysts that accelerated the integration of financial markets (Boot 2003, 37-38), and establishment of the Single Euro Payments Area is another crucial step towards to the completion of the European internal market. The Single Euro Payments Area (SEPA) will allow customers to make non-cash euro payments – e.g. by credit card, debit card, bank transfer or direct debit – to any beneficiary located anywhere in the euro area using a single bank account and single set of payment instruments. Thereby, all payments done in euro will become “domestic” payments and there will be no differentiation between national and cross-border payments within the euro area.

The aim of SEPA is to advance the European integration with a competitive and innovative euro area retail market that can bring with higher service levels, more efficient products and cheaper alternatives for making payments. The overall goals were defined by EU governments in the Lisbon Agenda, which envisages the EU internal market as the most competitive knowledge-based economy globally. According to the Lisbon Agenda, the integration of euro payments markets is a major pre-requisite for the realization of this vision. SEPA is therefore, a necessary step towards strengthening the European economy as a whole. (European Central Bank 2006, 7)

On a practical level, SEPA means that you will be able to make fast and secure transactions between bank accounts anywhere in the euro area; while you are shopping abroad you will be able to use your bank debit card to make payments in euro, just like at home country. In addition, SEPA will help to improve all payments, whether the payments are domestic or cross-border payments within two euro area countries. All consumers will benefit from new rules which will ensure transparent pricing and prompt transfers. Below in figure 5.1 is illustrated the roadmap of SEPA and the orderliness of the process towards the completion of SEPA.

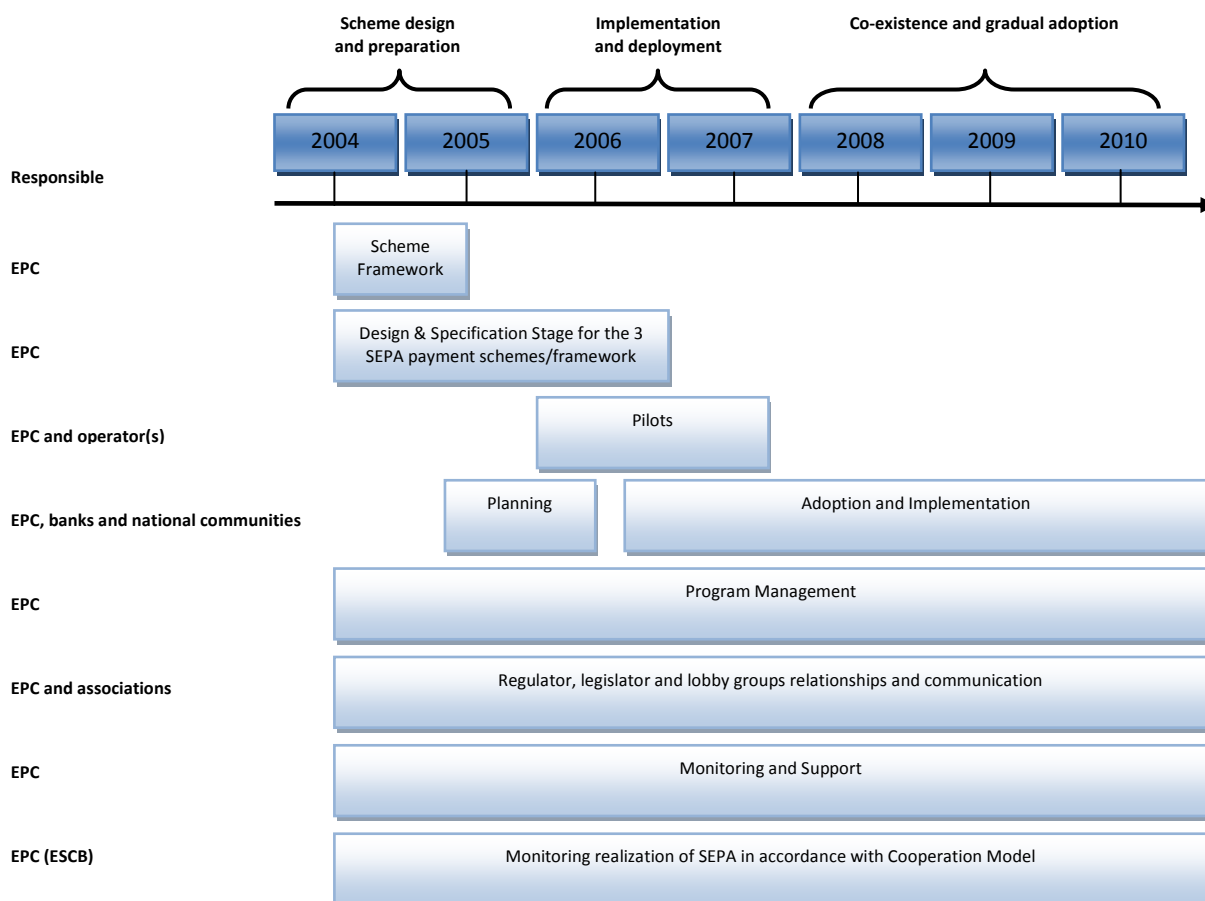


Figure 5.1 The timeline of SEPA (European Payments Council 2004a, 12.)

5.2 Scope of SEPA

According to ECB's Blue Book database, currently the euro area is processing circa 50 billion electronic transactions and between two to four times of this volume in cash yearly. This mass of payments is generated by 321.5 million citizens, 16-18 million large and small corporate, some 8000 banks, 5.75 million points of sale and 293003 ATM.

Geographically SEPA is not limited only to euro area. It consists of all EU euro zone countries (16), EU non-euro zone countries (11) and EEA (European Economic Area) zone (5) countries (Table 5.1).

Table 5.1 List of SEPA countries. (European Payments Council 2009g, 1.)

Euro 16	EU 27	EEA
<ul style="list-style-type: none"> •Austria •Belgium •Cyprus •Finland •France •Germany •Greece •Ireland •Italy 	<ul style="list-style-type: none"> •Bulgaria •Czech Republic •Denmark •Estonia •Latvia •Lithuania •Hungary •Poland •Romania 	<ul style="list-style-type: none"> •Iceland •Monaco •Liechtenstein •Switzerland

5.3 Establishment of the European Payment Council

The political and economical goal of creating a single European market has been clearly established. In 1999, when the founding of EMU was complete and the euro was introduced, politically this was expected to eliminate most of the barriers hindering the freedom of movement of trade and goods within the EU. The vision of SEPA foresees Europe in the future as a market of 500 million Single Euro Payment Area citizens and consumers making and receiving over 100 billion non-cash payments transactions each year (European Payments Council 2002b, 2.)

In 2002, main European banks and their associations took part in a workshop considering self regulatory and harmonisation of payments markets. The conclusions were consolidated into the White Paper. The White Paper articulated the principals and commitment to industry action. It stated the need for convergence between domestic and cross-border payments in euro and common vision of SEPA. The White Paper made recommendations in relation to customer & business requirements, Straight Through Processing (STP), infrastructure, cards and cash and it identified the payment instrument needed to support SEPA. Moreover, it presented governance structure which became the European Payment Council. (European Payments Council 2004b, 3)

Afterwards the new self regulatory body, the EPC was established in June 2002. It is the body which defines common positions for core payment services within a competitive market place, provides strategic guidance for standardization, formulates best practices and supports and

monitors implementation of decisions taken. This is done in such a way that banks can maintain self-regulation and meet regulators' and stakeholders' expectations as efficiently as possible. (European Payments Council c.)

The SEPA vision is supported by Europe's banks working together towards the integration of euro payments markets through the European Payment Council (EPC). The EPC consist of 74 members comprising banks and banking communities and, also the European Banking Association (EBA) is co-ordinating the process. More than 300 professional from various payment sectors from 32 countries are engaged in the work programme of the EPC. (European Payments Council 2009d, 14)

5.4 EPC governance structure

Gerard B.J. Hartsink is Chair of EPC and is a Senior Executive Vice President at ABN AMRO Bank and Claude Brun is EPC Vice-Chair and is Managing Director at the Banque de l'Economie du Commerce et de la Monetique/ Credit Mutuel –CIC Group. (european Payments Council 2009c.)

Figure 5.2 illustrates the governance structure of the EPC. The highest decision making body of the EPC is the Plenary. The seven working groups prepare the guidelines and rulebooks of EPC and send them either to Co-ordination Committee that overhauls and forwards those for Plenary. Certain issues working groups may prepare and send straight to the Plenary to be approved and put into force. (Tolvanen, 2009)

SSG (Standards Support Group) handles the standardization issues in SEPA implementation. Petri Aalto is the chairman of the SSG and he also represents Pohjola Bank in EPC Plenary and Coordination Committee.

Every working group has their own sub groups and their own legal support to handle issues concerning the working group's own area. The LSG (Legal Support Group) gives consultation to all groups, and secures that legal issues on working group level are prepared properly. (Tolvanen, 2009)

The Scheme Management Committee (SMC) is responsible for performing the administration and compliance processes of SEPA scheme management as regards the SEPA Credit Transfer

Scheme, which was launched on 28 January 2008, and the SEPA Direct Debit Scheme, which is in principle scheduled for launch in November 2009. (European Payments Council c.)

NGC (Nominating and Governance Committee) is the executive organ for selecting members to various positions in EPC.

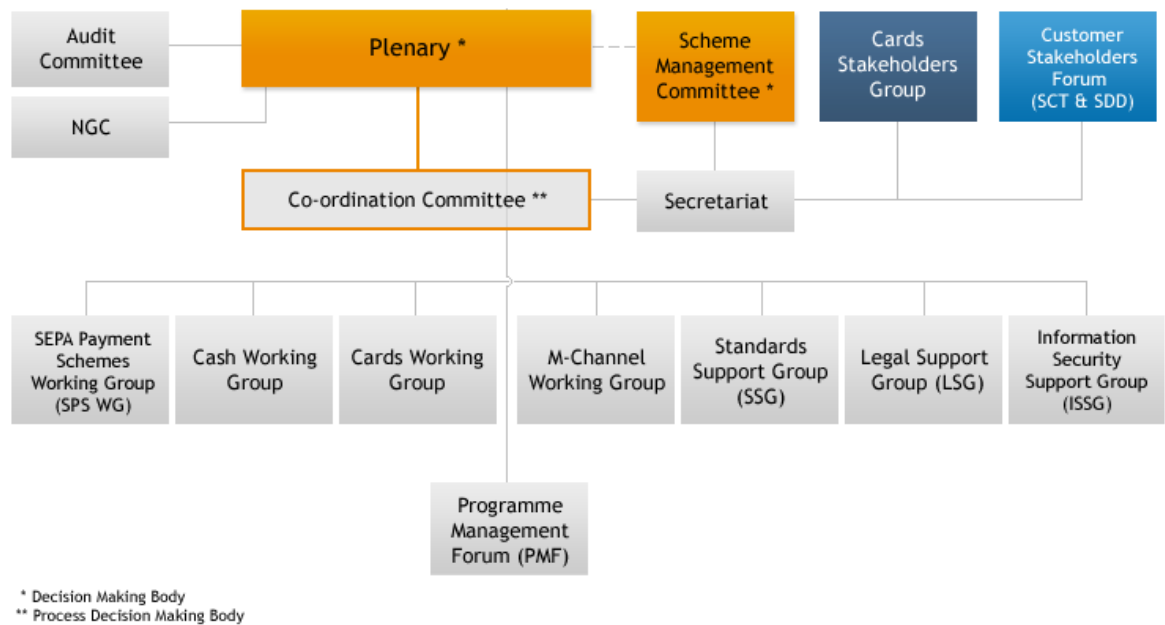


Figure 5.2 EPC Governance Structure. (European Payments Council c.)

5.5 Payment Service Directive (PSD)

The Directive on Payment Services (PSD) provides the legal foundation for the creation of an EU-wide single market for payments. The PSD aims at establishing a modern and comprehensive set of rules applicable to all payment services in the European Union. The target is to make cross-border payments as easy, efficient and secure as national payments within member state. In addition, PSD seeks to improve competition by opening payment markets to new entrants, hence fostering greater efficiency and cost-reduction. The PSD also provides the necessary legal platform for the Single Euro Payments Area. (European Commission, 2007c.)

Currently each Member State has its own rules on payments, and the annual cost of making payments through these fragmented systems is as much as 2-3% of GDP. Payment service providers are effectively blocked from competing and offering their services throughout the EU. Removal of these barriers could save the EU economy €28 billion per year overall. The Directive will bring major benefits to all the users of payment services. It will ensure that all

euro or domestic electronic payments (as well as certain other payments involving euro currency exchange) are completed in a maximum of one day after the payment order is given. It provides the legal foundation for the launch of cross-border direct debit schemes. It should also lead to lower prices and greater choice for users by fostering competition in the market and allowing non-banking institutions to enter the payment markets. (European Commission, 2007.)

5.6 Changes in payment systems

During decades, the payment systems have developed tremendously and nowadays there exist various money transactions systems that Nicholas Anderson (2000, 149) divides as follows:

- Notes and coins
- Check payments
- Money orders made by payment machine, computer or mobile phone.
- Payments made through banks' invoicing system
- Bank and credit cards
- Chip card
- E-money in internet

All these options are in use as well as in domestic markets as in foreign markets. Though there exist multiple payment methods, as stated in Cruickshank's report in March 2000, the Great Britain's payment systems are expensive and not competitive. Report argues that:

- Few banks dominate the payment systems market
- Retail stores' bank and credit card costs are high
- Cash withdrawals are charged even six percentage over the actual costs derived from the withdrawal
- Payment systems are inflexible and adapt slowly to requirements of e-shopping
- Many customers are unaware of terms of payment services
- Barriers for changing from bank to another are too high

Though Finnish payment system has developed tremendously during the decades (Appendix 2) and is more efficient than the system for instance in Great Britain crucial developments are being made within the progress of SEPA. In figure 5.3 below is shown the changes that SEPA brings to the payment systems. The color coding illustrates well the diversity and complexity of payment systems in Europe, and how it will improve in consequence of SEPA.

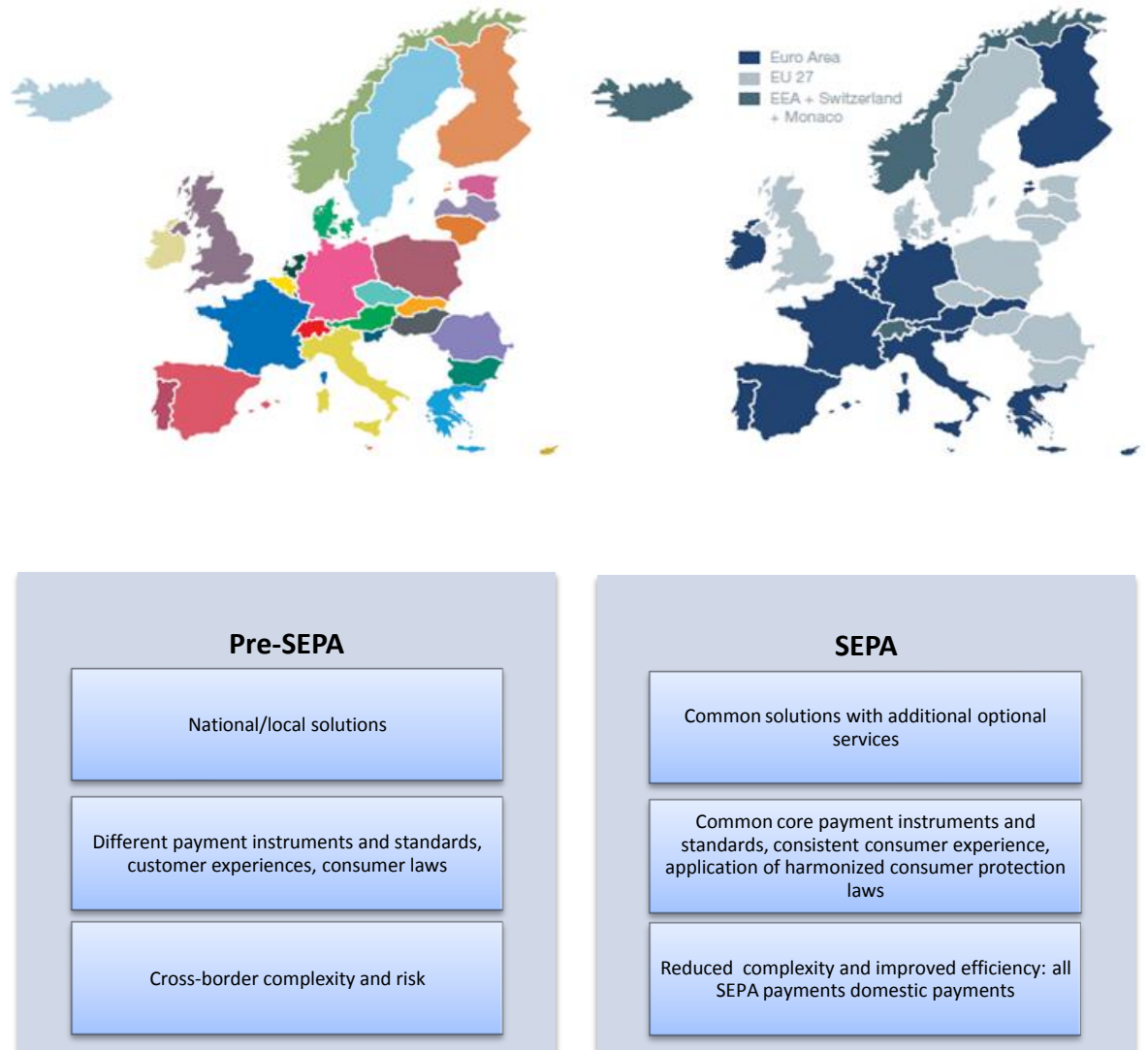


Figure 5.3 Changes in payment system in Europe (EPC Roadmap 2004-2010)

From the point of view of European banks, one or several centralized Pan-European Automated Clearing Houses (PE-ACH) will be needed to enable smooth payment transmission between all banks operating within the area. All banks that operate in Finland will join such a PE-ACH clearing house, the Euro Banking Association's (EBA) system to ensure their payment transmission.

5.6.1 SEPA Direct Debit

The legal frameworks and different national direct debit procedures that exist, the EPC decided in very early stage to harmonise these national procedures and develop a completely new scheme, the SEPA Direct Debit Scheme (SDD). The SDD creates for the first time a payment instrument that can be used for both national and cross-border euro direct debits

throughout the SEPA area, and therefore it replaces the existing domestic direct debit schemes. From Finnish perspective, the currently used direct debit will change a lot, whereas it will contain many similar elements which are recognisable for instance from the German collection procedure. (Deutsche Bundesbank 2007.)

The SEPA Core Direct Debit Scheme applies to transactions in euro. The debtor and creditor must each hold an account with a credit institution located within SEPA. The credit institutions executing the direct debit transaction must be scheme participants; that is, both must have formally adhered to the SEPA Direct Debit Scheme. The Scheme may be used for single (one-off) or recurrent direct debit collections; the amounts are not limited. (European Payments Council 2009e.)

The SEPA Direct Debit Scheme Rulebook establishes the basis for the processing SDD for the private sector. It defines the internationally applicable processes, terms and formalities (e.g. mandate administration, one-time and recurring debits) and among other things stipulates that: (Six Interbank Clearing 2009.)

- Debtors must be granted the right to object.
- The pre-notification of an upcoming debiting of the debtor by the creditor is required.
- Clearly defined chargeback processes such as returns, revocations, reversals, refunds and rejects exist.
- The transactions are processed using standard formats (ISO 20022) and data content (IBAN and BIC).

5.6.2 The SEPA Business to Business Direct Debit

The SEPA Business to Business Direct Debit Scheme (B2B) will serve as the basis for the development of specific direct debit products and services that allow business customers in the role of debtors to make payments by direct debit as part of their business transactions.

The most important differences between the SEPA Core Direct Debit Scheme and the SEPA Business to Business Direct Debit Scheme are: (European Payments Council 2009e.)

- In the B2B Scheme the debtor is not entitled to obtain a refund of an authorized transaction.
- The B2B Scheme requires debtors to ensure that the collection is authorized by checking the collection against mandate information; debtor banks and debtors are required to agree on the verification to be performed for each direct debit.

- A debtor bank cannot offer the B2B Scheme to a debtor who is a ‘consumer’ under the law of the country where that debtor bank is providing the payments services.
- Responding to the specific needs of the business community the B2B Scheme offers a significantly shorter timeline for presenting direct debits and reduces the return period.

5.6.3 SEPA Credit Transfers

The SEPA Credit Transfer Scheme enables payment services to offer a core and basic credit transfer service throughout SEPA area, whether for single or bulk payments made in euros. The scheme’s standards facilitate payment initiation, processing and reconciliation based on straight-through-processing (STP) and the scope is the payments in euro within SEPA countries. The BIC and the IBAN will be used to identify the customer’s bank and customer itself. Finnish banks will change over to using XML-standards in communication between banks and customers and in interbank transactions. New customer standards will be introduced according to each bank’s own timetable. These new standards require modifications in customers systems which adoption banks will agree separately with their customers. Appendix 3 illustrates the Finland’s transition timetable from current domestic payment standards to SEPA Credit Transfer. The green boxes are common deadlines for all the banks, whereas the orange boxes may vary depending on the bank. (Kauppila 2009.)

5.6.4 Changes in standards

All SEPA countries have had national payment and data security standards, but with SEPA these will be unified. Finnish national payment standards that are sent to banks via FTP (File Transfer Protocol) connection are LMP, TS and LUM2 and the PATU security standard have been used in Finland since beginning of 1990s. These national standards will be replaced by Web Services channel and PKI (Public Key Infrastructure) that is internationally approved security standard. According to EPC’s Rulebook, new SEPA payments must be done according to ISO 20022 XML-standard. As illustrated below, the national payment standards (LMP, TS & LUM2) will be replaced by ISO 20022 XML. Moreover, use of FTP channel and PATU security will end and new Web Service channel and PKI security solution are introduced. (Nyholm 2009.)

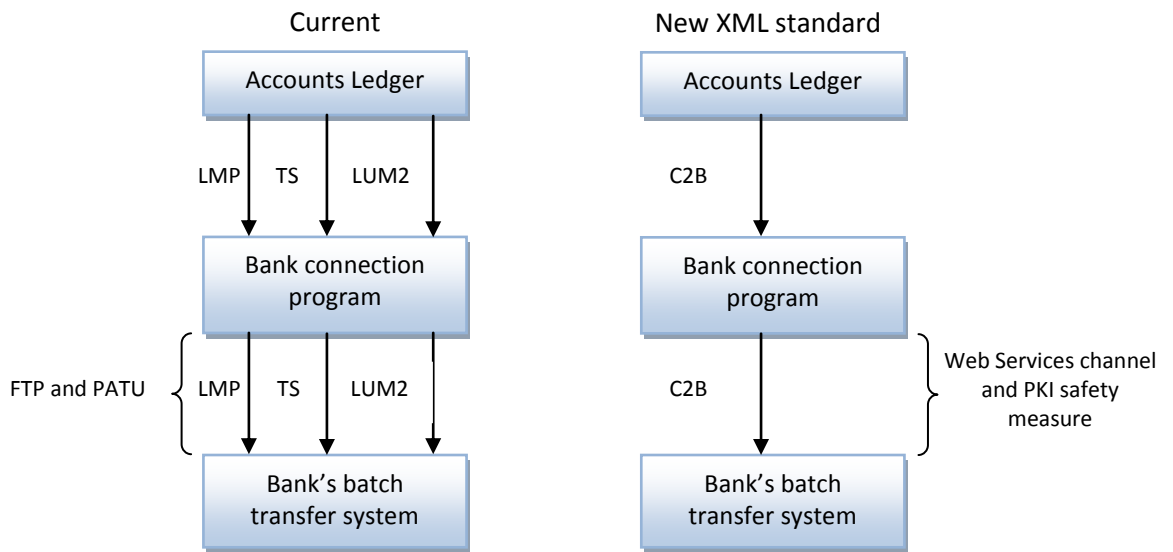


Figure 5.4 Payment data transfer services; current and C2B method (Nyholm 2009.)

If company do not want to update their bank connection systems so they can send payment files to bank in C2B format, company can buy a conversion service from a software house (figure 5.5)

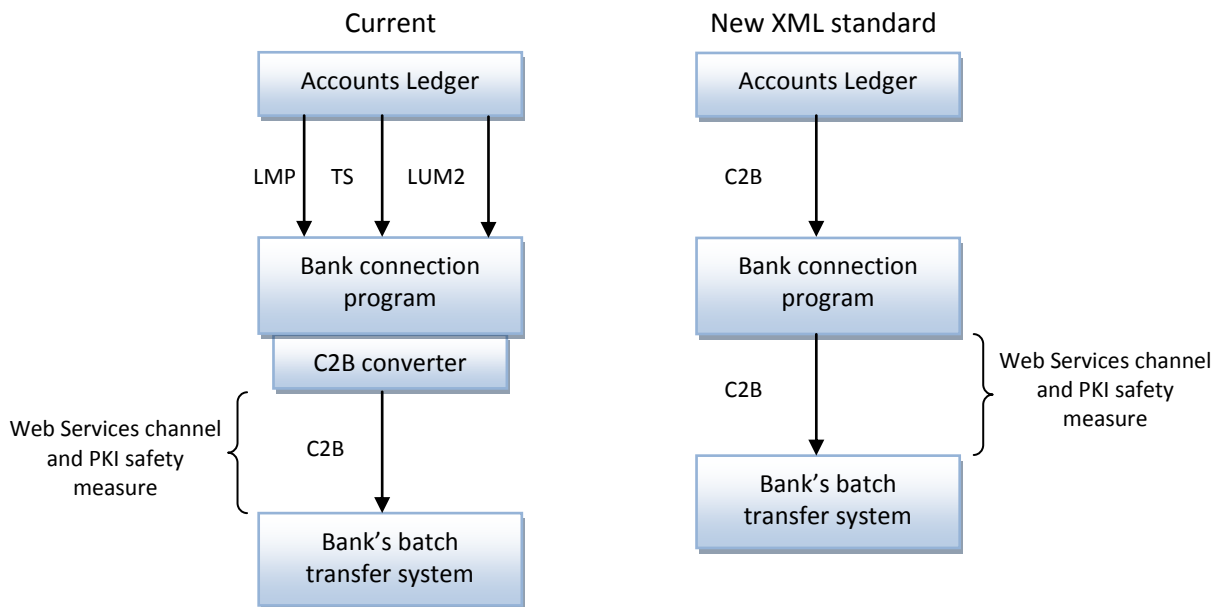


Figure 5.5 SEPA conversion service from a software house and C2B (Nyholm 2009.)

SEPA converter changes domestic, foreign and periodic delivery payment files to a C2B format; hence the files are transferred to bank in similar format as it would, if company has had updated its bank connection program to send SEPA C2B files. (Nyholm 2009.)

5.7 Web Services channel

Web Services is a broad term that represents all technologies used to transmit data across a network by using standard internet protocols, usually Hyper Text Transfer Protocol (HTTP). An eXtensible Markup Language (XML) format is used to represent the data, which is why Web Services are known as XML Web Services. Bank customers have used nationally standardised or bank specific connectivity and security solutions to send computer generated financial data to their banks. Web Services is new solution to communicate and send data information between banks and corporate customers. This new solutions is based on an international standards (ISO20022) to enable implementation with modern software development tools and to encourage ERP (Enterprise Resource Planning) and financial software vendors to implement adapters and communication tools for clients. The Web Service channel security and authentication is based on PKI, which function like banking codes but are intended for a connection between computers. (Nyholm 2009.)

5.8 ISO20022 XML Standard

As know, the objective of ECB, EPC, EC and European banks is to create an integrated payments area to Europe. In order to achieve this goal the standardization of payments is crucial. In accordance with the EPC implementation guidelines, new UNIFI (ISO20022) XML standards, published by the ISO will be introduced for interbank SEPA credit transfer and SEPA direct debit transaction transmission. The ISO20022 Standard determines a framework for methodology for the development of financial message standards. ISO20022 messages are based on XML (eXtensible Mark-up Language) standard. (International Organization for Standardization 2010.)

International XML message standards will be adopted for the connections between the customer and the bank with regard to credit transfer and direct debit services. ISO20022 Standard provides a common platform for financial industry for the development of messages in a standardized XML format (Appendix 4). The first focus of ISO20022 is on cross-border financial communication between financial institutions and their clients. European banks as well as Pan-European payment transactions clearing and settlement solutions have pledged to implement ISO20022 standard. (International Organization for Standardization, 2010)

6 Research Methodology

Interest towards the topic woke during cash management training in Sampo Bank in spring 2009. The topic is related to my daily work and additionally the topic is current, because the implementation process of SEPA has began already in beginning of year 2008 and utmost importance because the transition period will endure only till the end of end of year 2010.

6.1 Research method

The research method used for the study was qualitative. The study is supported with literature, articles and other publications related to the topic. Besides, interviews were made to deepen the understanding of the issues; as well as the researcher's own observations became a remarkable source of information in this process.

Deadline for the transition to SEPA is closing and soon over 30 European countries will standardize their laws on transactions, banking services and cross-border payments. As stated by many companies, this will be larger change than the implementation of euro. However, still many live in an assumption that SEPA concerns only banks and software houses, and common understanding has been that so far companies have prepared poorly for SEPA. Truth is that, it concerns everyone, especially companies. Hence the purpose of this research was to clarify the actual state of companies' readiness for SEPA in Finland.

During the years 2009 and 2010 an extensive research project was conducted to get a real sense of the state of transition state of SEPA in Finland and how companies in Finland have been prepared for it. The survey ran throughout the winter and spring 2010, surveying experts related to the subject from various interest groups, from banking sector, software houses, European Payment Council and companies.

It was decided to conduct the research to companies by e-mail questionnaire to reach sufficient amount of respondents. Moreover, in the selection of respondents, it was essential to make sure their readiness to answer the questionnaire. Therefore, the questionnaires were sent to key personnel to finance and IT departments who are responsible of the financial issues or have deeper knowledge of technical side of the implementation process of SEPA in the company. Face to face interviews were carried out only to banking personnel to gain profound understanding of the general situation in Finland, and also to get in-depth and accurate information concerning technical issues of SEPA.

Companies were selected carefully by certain criteria to gain comprehensive perspective of the transition state in Finland. Companies chosen for the survey were medium and large companies according to classification made in 2004 by Ministry of Trade and Industry (current name Ministry of Employment and the Economy). According to the classification macro companies are at most 2 million euro turnover companies and small companies less than 10 million euro turnover. Medium sized companies have a maximum turnover of 50 million euros whereas large companies have over 50 million turnovers. Focus groups of the research were the medium and large companies, hence in the research the macro and small companies were left out from the survey.

Furthermore, companies were selected to the survey from different business fields, such as healthcare, cloth wholesale, retail and cosmetics. All the companies in the survey have operations across the Europe and therefore, all are affected immensely by SEPA.

All of this was supplemented by a significant amount of primary research reviewing the European monetary development and Finland's plan to sift from national payment transactions to a European payment practice SEPA.

6.2 Company selection

Basware Ltd is an international software company developing solutions designed to automate the financial processes of organizations. Basware Ltd's software solutions automate purchase and travelling expenses, account handling and processing of purchase management. Basware was founded in 1985 and during the years it has spread its operations to more than 30 countries and has over 1 000 000 end users of their products. Basware Ltd has 8 subsidiaries in Europe and the US, and employs over 700 persons. In year 2009 Basware Ltd had a turnover of circa € 93 million. (Basware 2010.)

Diesel S.p.A. is an Italian design company that is best known for clothing aimed at young adult market, especially jeans but the brand can be found everything from underwear to fragrances. The company was established in 1978 by Renzo Rosso. Diesel has circa 2 200 employees in 18 subsidiaries across Europe, Asia and the Americas, and its products are sold worldwide in over 5 000 retail outlets. Revenue in year 2009 was about € 950 million. (Yahoo 2010.)

Eltel Networks Ltd provides electricity, telecommunications, railway, public safety, aviation, and enterprise networks. It is one of the leading providers of network services in Northern Europe with turnover of € 983 million in 2008 and employees of about 9 000. The headquarters is located in Espoo, Finland, but in addition to Finland it also operates currently in Sweden, Norway, Denmark, Germany, Poland, and in the Baltic countries. Eltel Networks Ltd also design, manage, and construct networks through their large projects business across the globe. (Eltel Networks 2010.)

Lidl, founded in 1930's is a German based discount supermarket chain that operates in about 8 000 stores worldwide. Lidl is owned by Dieter Schwarz and ownership is governed by a foundation. In Germany, foundations are not required to publish financial information; hence Lidl does not inform much of their sales and profitability numbers. However, turnover in year 2009 was circa € 635 million. First retail stores were opened in Finland in 2002 and nowadays there exist over 120 stores across Finland with employees about 2 500. (Pyykönen 2009.)

Lumene Ltd engages in the development, manufacture, marketing and sale of beauty care and hygiene products. Its products include skin care and colour cosmetics, and cleaning and hygiene products. Lumene Ltd was founded in 1948 and is headquartered in Espoo, Finland. Lumene Ltd's turnover in 2009 was € 78 million, and most of it circa 90% comes from its main market areas Finland and other Scandinavian countries, US and Russia. Lumene Ltd has operations worldwide and currently employs 510 persons. (Lumene 2010.)

Medixine Ltd specializes in multimodal communications software for healthcare and wellness. Its solutions include population based health forecasting and reminder systems, expert based scheduling and feedback systems and patient based disease management and e-care systems. At the moment Medixine Ltd. solutions are used in 16 countries and company's turnover in 2008 was circa 2 million. (Medixine 2010.)

Opus Capita is one of the leading providers of automated financial management solutions in the Baltic Sea region. Their core competence lies in centralized liquidity management systems and the supporting finance and electronic invoice processing solutions. Their customers include more than half of Finland's top 200 businesses and thousands of other companies in the Nordic countries. Opus Capita was established in 1984 and has now offices in Finland and Sweden. Its turnover was approximately € 13.8 million in year 2009 with number of staff reaching 100. (Opus Capita 2010.)

Sampo Bank is a part of Danske Bank Group, which is one of the largest financial enterprises in the Nordic region. Sampo Bank has more than 1.1 million personal customers and more than 100 000 corporate and institutional customers in Finland. (Sampo Bank 2010.)

6.3 Research questionnaire

1. How aware are you of SEPA details? – Its details and term?
 - Well aware
 - Good
 - Moderately
 - A little uncertain
 - Not at all
2. From where have companies heard of SEPA?
 - Banks
 - Federation of Finnish Financial Services
 - Software houses
 - Other
3. When will the SEPA vision of “all Eurozone payment transactions to be processed as though they were domestic” be realized?
 - 2010
 - 2011
 - 2012
 - 2013
 - 2014
 - After 2015
4. What are the largest changes caused by SEPA for companies operating in Finland?
 - Extensive technical data format changes
 - Software updates
 - Telecommunication changes
 - Changes in Direct Debit
 - Other, what?
5. What do you believe are the most positive aspects of SEPA and PSD?
 - Better and more competitive banking services
 - Easier cross-border movement of goods and services
 - Increased automation of financial processes

- Increased trade
 - Simpler business processes
 - Increases transparency
 - Other, what?
6. Why do you believe that SEPA Credit Transfers (SCTs) have been so slow to take off?
- Unsure of benefits
 - Lack of availability
 - Companies do not want SCTs
 - Banks are waiting for full SEPA and PSD
 - Companies are waiting for full SEPA and SPD
 - Lack of motivation because there is no end date
7. What are the most important benefits to companies deriving from SEPA?
- Savings in foreign payments service fees
 - Reduction of value dates
 - Improvement of cash flow forecasting
 - Standardization in group level
 - Security improvements
 - Standardization of payment formats
 - Number of foreign banks accounts can be reduced
 - No significant changes
 - Other, what?
8. What are the possible threats and disadvantages of SEPA?
- Slow implementation process
 - High implementation costs
 - Lack of resources in software houses
 - Possible ascending card payment fees
 - Possible ascending bank fees
 - Lack of information from banks
 - Pile up of software updates to the end of the year
 - Companies too slow to react to the changes
 - Without specific deadline process may be hindered
 - Slow implementation process of less developed banking systems elsewhere in Europe
 - Problems between different interest groups
 - Other, what?

9. How well have companies in Finland prepared for SEPA?
 - Very well
 - Quite well
 - Little bit
 - Not at all
10. Has your company prepared an implementation plan for SEPA?
 - Plan made and in progress
 - Plan made, but no actions taken
 - Procedures has not been started
11. Will the banking program be updated for SEPA or will conversion service be bought from software house?
 - Programs will be updated
 - Conversion service will be bought
12. How big are the implementation costs for you company deriving from SEPA?
 - Not sure
 - 0€ - 1 000€
 - 1 001€ - 5 000€
 - 5 001€ - 10 000€
13. Do significant cost savings derive from SEPA to companies?
 - Yes
 - No
 - Not sure
 - Other, what?

Certain questions were formed little bit differently for software houses and banks. The questions below corresponds the previous questions as follows: question 1 below corresponds with question 11 above, and question 2 below corresponds with question 12 above. Additionally questions 3 and 4 were only asked from banks and software houses.

1. How many of the companies will update their finance programs to function with SEPA requirements and how many will by conversion service from software house?
2. How big are the SEPA implementation costs for companies?
3. How much does it cost for companies to buy a conversion service from software house?
4. Does the price of the conversion service rise towards the end of the year?

6.4 Reliability and validity

Reliability in quantitative research is “the similarity of results provided by independent but comparable measures of the same object, trait, or construct” (Churchill 2001, 373). For a research to be reliable it needs to be done systematically with controlled treatment. Research must also be traceable and explicate the rules of data collection and analysis. Saunders, Lewis and Thornhill (2003, 101) quote Robson (2002) and declare that there are four main threats to reliability: subject or participant error, subject or participant bias, observer error and observer bias, and all of these threats are relevant to this research.

Subject or participant bias means respondents might say what they think should be said, for instance to give better impression of the company’s condition or interviewee’s own professionalism. Observer error has been eliminated to the minimum by introducing the structure of the interview and by explaining the questions to the interviewees. Answers to the questions have been marked properly and in similar way in every interview, and there was only one person interpreting the answers, hence this eliminates the risk of observer bias (interpreting the answers in different ways).

Validity is defined as the extent to which differences in scores on measuring instrument reflect true differences among the characteristics it seeks to measure (Churchill 2001, 369). In other words, attention should be paid to the findings being about what they appear to be about. Saunders et al. (2003, 102) quote Robson (2002) and list the main threats to validity:

- History
- Testing
- Instrumentation
- Mortality
- Maturation
- Ambiguity about causal direction

History might affect to the respondents answers for instance if they just experienced something negative concerning the issue and were irritated by that when answering the questions and this could influence their answers. Testing

All things considered, reliability and validity issues have been taken into account in the research. Secondary data sources have been selected carefully and recent literature have been chosen. Alternative theoretical approaches have been looked at and the suitable and accurate literature has been chosen and the choices of the main theories have been argued.

Reliability of the research in this study is relatively good. For the interviewees the subject of the research topic is familiar and everyone has professional expertise concerning the subject. In the research is discussed interviewees' work related issues, systems and methods. Moreover, the characteristics and proficiency of the interviewees are not discussed and therefore they do not have reason to prettify their answers. Interviews are also conducted between interviewer and interviewee, so outsiders have not heard the discussion. One crucial issue that might affect the quality of the answers is corporate secrets. Interviewees might not be able to answer to all questions as well and accurately as they could because certain facts concerning the question are not public information yet and cannot be revealed. (Hirsjärvi 2004, 216-218)

7 Results of empirical research

The result of this survey has conclusively proved what had anecdotally been suspected. Generally SEPA is no more unfamiliar issue for companies, but there are still some companies who are not entirely aware of SEPA and its impacts of their business processes. In addition, Europe's payment program is on track, depending naturally from which way you look at it. There are multiple points of views dependent whether you are a policy maker, bank, corporate, infrastructure provider, payment institution or implementer.

7.1 Companies' awareness of SEPA

According to prevalent perception, companies have not prepared properly for SEPA yet. Reassuring is though, that SEPA is not entirely unfamiliar concept to companies. In the study, all of the respondents have heard about SEPA. As the figure 7.1 below indicates, 60% of the respondents know very well what SEPA is. Inkeri Tolvanen (2009) argues that smaller companies do not necessarily acknowledge the extent of the implications of SEPA, which came out in the research. Concerning was that from few companies where the questionnaire was sent, reply was that "I am not familiar with the subject and therefore will not answer to it, good luck with the research", or "Our company is relatively small and we operate only in Finland, so this does not concern us that much". Hence, though the figure gives the picture of good awareness of SEPA, it is not entirely true. This indicates that larger companies are more familiar of SEPA.

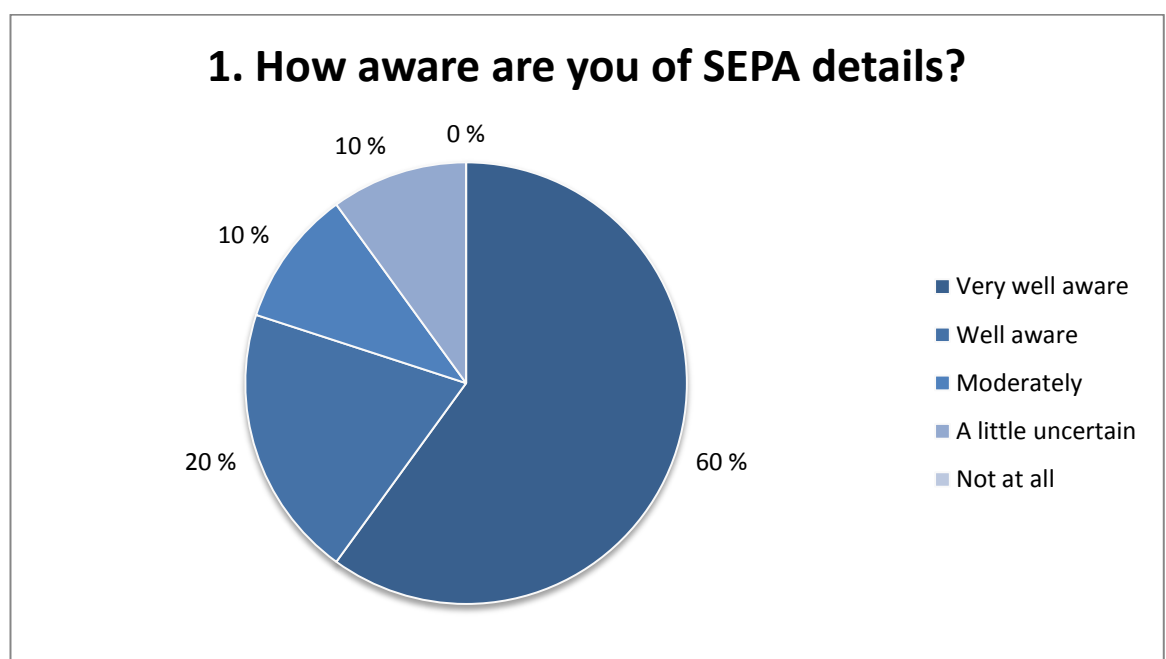


Figure 7.1 Awareness of SEPA

Figure 7.2 shows the various sources of information for companies. Almost half of the companies (46%) have obtained information from the banks, and second source of information has been software houses (23%). Moreover, Federation of Finnish Financial Services' SEPA Foorumi has been valuable source of information. Companies perceive it as a source of general information that gives perspective of the current situation in Finland. Banks and software houses on the other hand have been used more for gathering information of exact implementation procedures and issues concerning their own specific needs and interests. Furthermore, companies have enquired information also from various seminars and from media (15%).

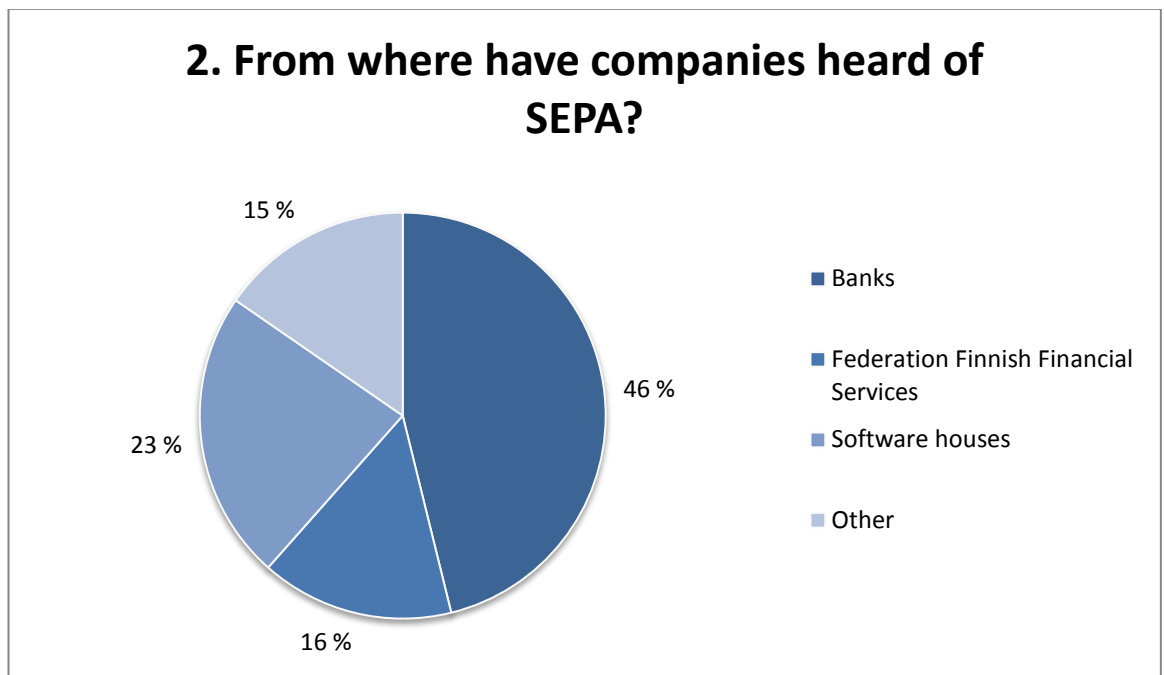


Figure 7.2 SEPA information sources

Harmonization of European payments market will take years to be fully completed. Process of SEPA is still unclear to companies, which can be seen from figure 7.3 responses. Answers vary from year 2010 to after year 2015. 20% of the survey's respondents think that the SEPA vision will be fully realised soon as 2011, but most (30%) believe sometime after 2015. The truth probably lies somewhere in between, but without an end-date companies will certainly have difficulties to start large implementation projects. In Treasury and Cash Management 2010 conference Erkki Poutiainen, Senior Vice President, Head of Payment Infrastructure of Nordea bank questions the need of end date and states that it could also pose a threat. Would development of payment systems and methods end to a possible end date? This is an issue that EC is discussing at the moment and according to Poutiainen, EC will be making decisions concerning the matter during the year 2010.

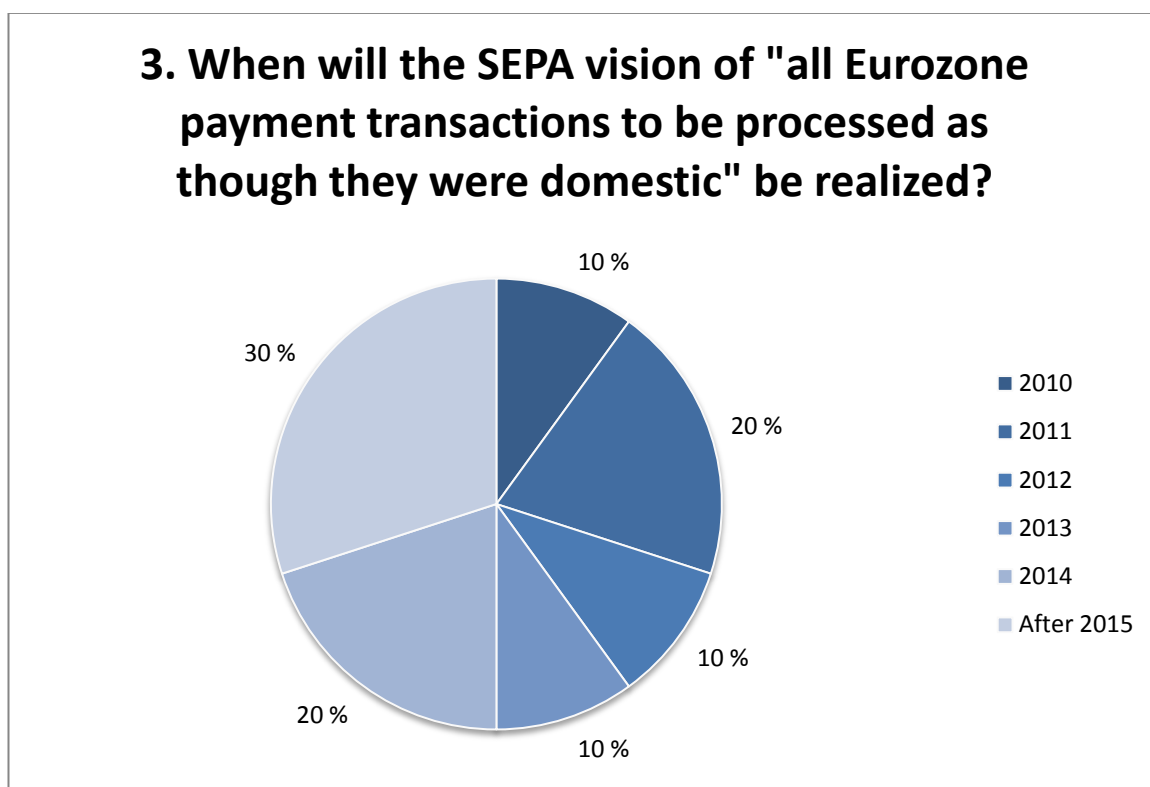


Figure 7.3 Realization of SEPA vision

7.2 Expectations of SEPA

As the results below in picture 7.4 shows, companies are experiencing the technical data format changes to be the biggest change in SEPA. Though it might sound small matter, the change of all current payment standards (LMP, TS & LUM2) to XML format is tremendous process to companies, which requires lot of recourses and time for testing. Moreover, software updates are considered to be relatively heavy burden to companies, especially large companies that have to integrate multiple finance software and ERP systems in group level and in many countries to SEPA competent.

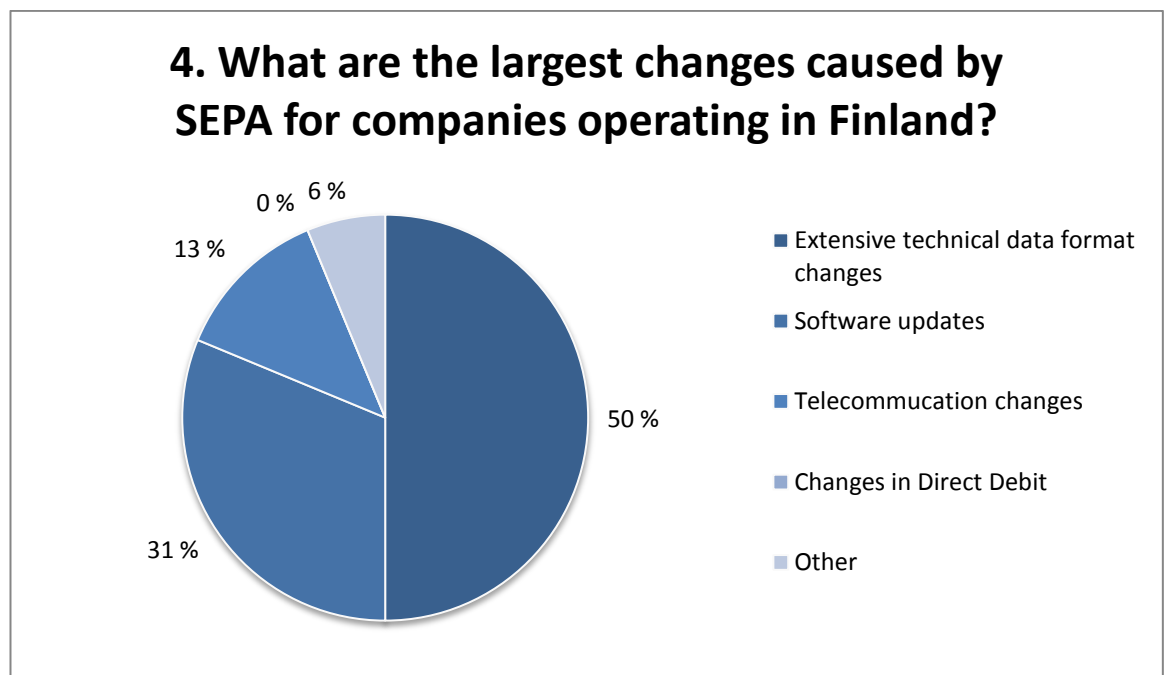


Figure 7.4 Expectations of changes due to SEPA

When asked what the key benefits of SEPA and PSD would be, 39% of the respondents are expecting SEPA and PSD to create more automated payment environment and 23% state it would simplify business processes. Furthermore, companies consider these changes to create more competition in banking services and hence to offer better banking services (15%). One respondent argued that one of the most beneficial results will be freedom to organize payment processing within a group of companies operating in SEPA area, hence all payments are domestic. Moreover utilization of unified reference payments to automate reconciliation processes was seen as a fundamental benefit.

5. What do you believe are the most positive aspects of SEPA and PSD?

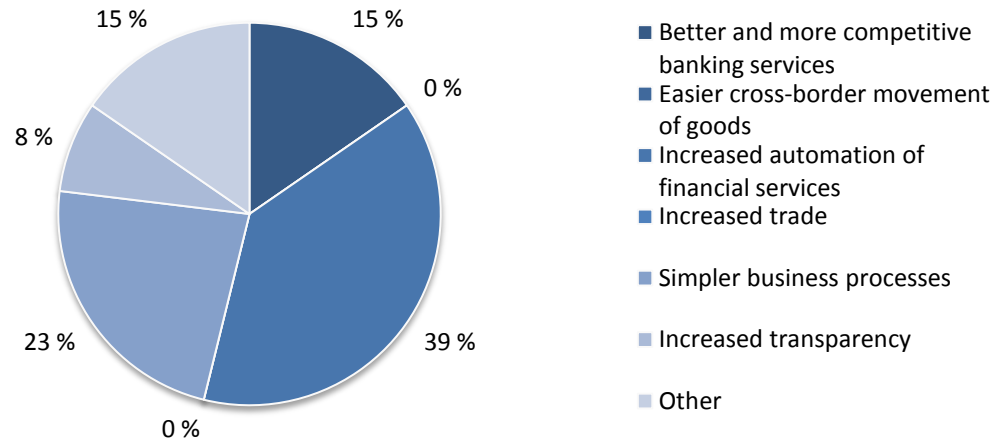


Figure 7.5 Benefits of SEPA and PSD

When asked why SEPA SCTs are taking so long to take-off, the clear answer (29%) is that companies are not aware of its benefits and if they are clear banks are not offering SCTs (29%). A further 18% felt that it was because there is no end date; companies tend not to have motivation to implement the SCTs. As companies are unaware of the possible benefits and there is no end date for SCTs, companies tend to easily pass over it and concentrate on other more urgent matters concerning SEPA.

6. Why do you believe that SEPA Credit Transfer (SCTs) have been so slow to take off?

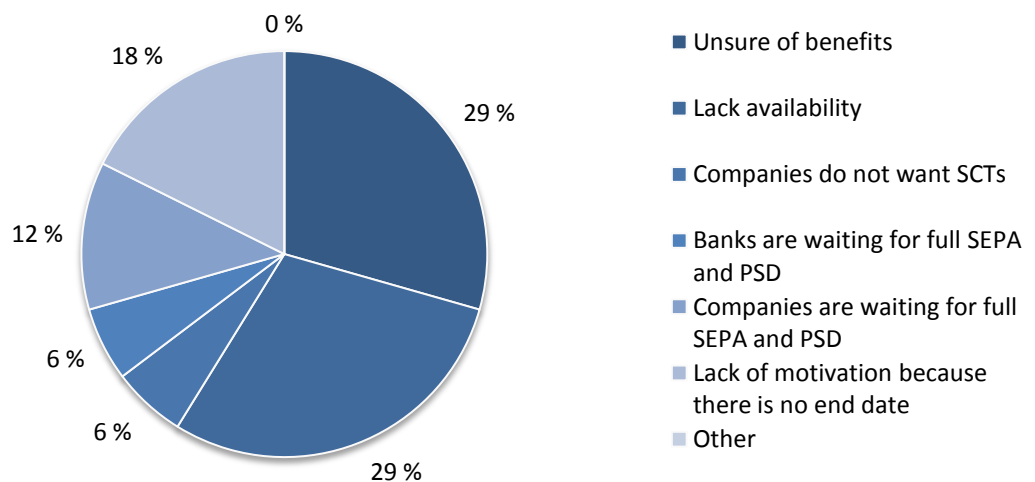


Figure 7.6 Hindering issues in SCT's implementation

At the moment companies are not well aware what changes SEPA will actually bring. Mostly companies expect SEPA to improve foreign payment procedures. Savings in foreign payment service fees (19%) with value day reductions (19%) are seen the most important benefits that SEPA will provide. Companies brought up, that SEPA will hopefully increase transparency in banking fees and hence bring cost savings to companies. Furthermore, standardization of payment formats is seen as an important reform (19%). Also international companies felt major benefit to be rationalization of bank relationships' by reduction of foreign accounts and thus concentrating and strengthening co-operation with banks (13%). Especially in companies that have operations in various countries across the Europe and have different currency accounts in many countries. This is thought to make the management of cash surpluses easier and companies can concentrate cash to one country and certain accounts to receive better interest for it. Thus SEPA is especially felt to improve cash management in group level.

However, small amount of the respondents were not sure what benefits SEPA brings on a practical level if any. Companies that do not have operations abroad feel that SEPA does not offer them anything.

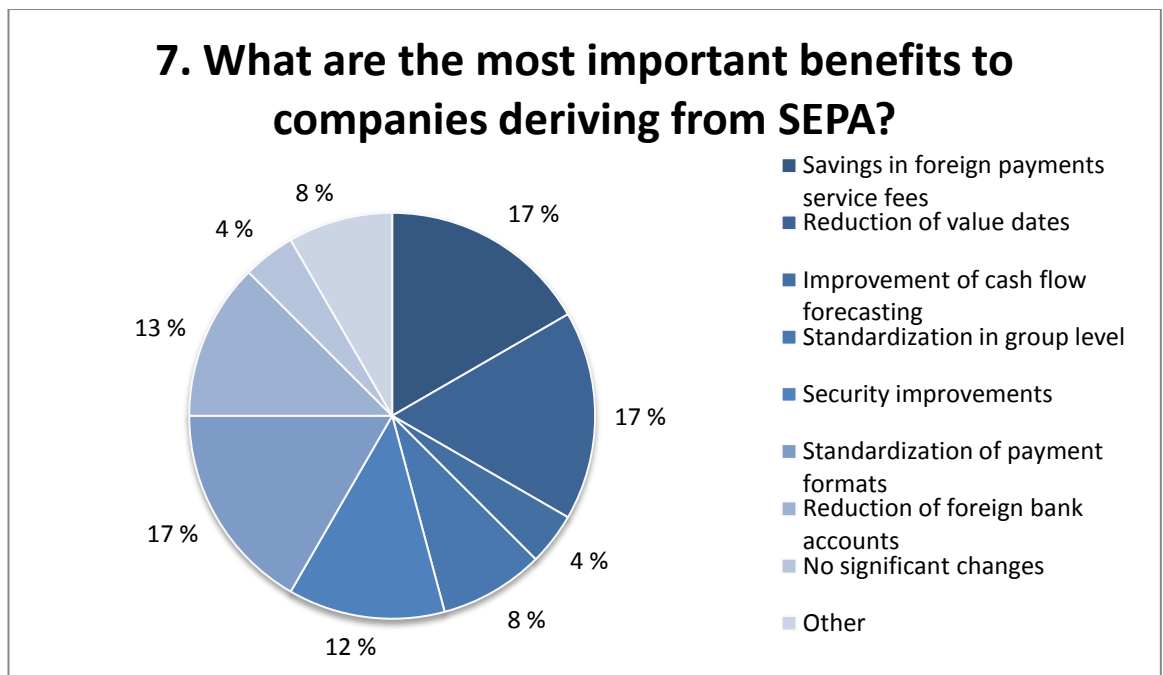


Figure 7.7 Benefits of SEPA

Though companies expect great benefits from SEPA they also downsides caused by SEPA. Figure 7.8 illustrates these presumptions. Implementation to SEPA is seen very expensive (20%) and slow process (14%) for companies. Moreover, lack of resources in software houses (10%) is seen as a threat especially if companies put off the implementation processes to the

end of the year, which will cause a peak to software updates and overload software houses. As seen in Appendix 3, timetable for certain changes vary depending on banks. This lack of specific deadline (10%) for certain changes may be one reason for companies' slow implementation. According to Basware, this is also because companies do not want to invest to a matter which does not turn into immediate benefit. Companies also see the possible ascending banking fees as a threat (10%), which may derive from poor briefing from banks (10%).

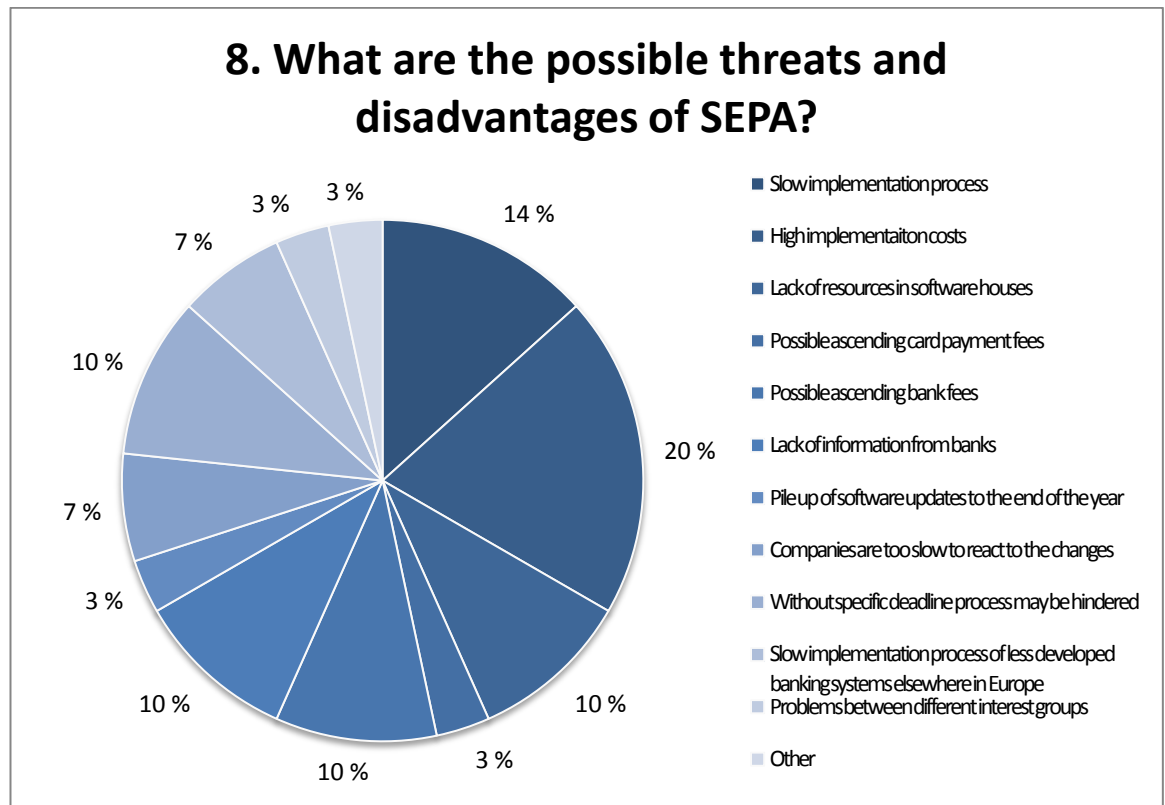


Figure 7.8 Threats and disadvantages of SEPA

7.3 Companies' preparation for SEPA

The figure 7.9 gives the picture that companies have prepared relatively well for the forthcoming changes. However, this research concentrated on medium and large companies and therefore, the results look different from larger and wider researches that include all companies regardless of the size. On the other hand, this result strengthens the common presumption that the larger the company is, the better is the preparation for SEPA at the moment. Large companies have mainly started preparations earlier and more carefully than smaller companies, states Tapani Oksala (2010) from software house Opus Capita, and partly because their systems are considerably larger and more rigid and therefore are long projects. The most worrying are medium sized companies at the moment says Oksala (2010). Their systems can be very sturdy and old, and there may be lack of knowledge, hence medium sized companies

may face problems and surprises more than others. Quite similar is software house Basware's view. They say that large companies have woken up to the situation and medium sized companies are beginning to realize the situation.



Figure 7.9 Companies' readiness for SEPA

The readiness of companies has indeed improved, which can be seen from figure 7.10. Many of the companies have implementation plans for SEPA and during spring 2010 majority of the respondents have started the implementation stage (83%). over quarter of the respondents stated that the plan has been made in group level and person in charge has been appointed to carry out the process. One company stated that they had to put on hold their implementation process due to lack of availability of Web Services Channel and XML File Transfer from banks. Tuula Pasanen from Sampo Bank argues that after companies' have finished their balancing of accounts, they have activated and started their processes.

10. Has your company prepared an implementation plan for SEPA and started the process?

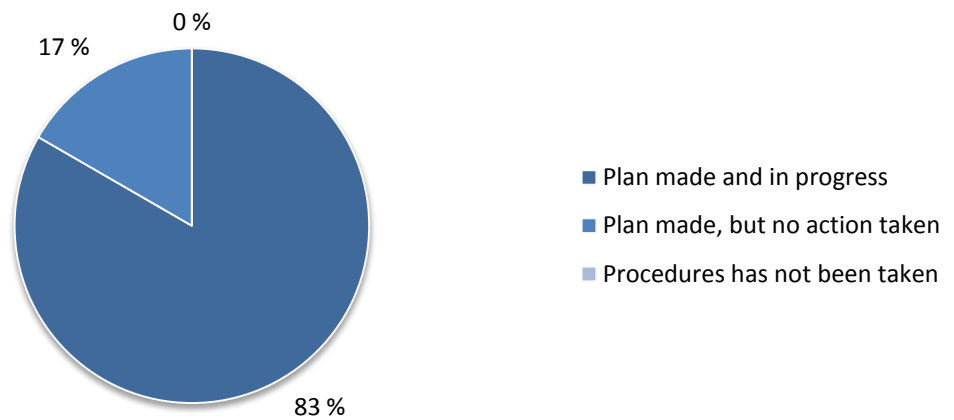


Figure 7.10 Stage of the SEPA implementation process

Surprisingly many companies (57%) according to the research will update their banking programs for SEPA. Some of the companies will first buy a conversion service from software house to guarantee systems functionality trough transition period and later update all systems for SEPA. Both Basware and Opus Capita however, estimates that majority of the companies will buy conversion service and roughly third of Opus Capita’s customers have already bought conversion service, says Oksala (2010).

11. Will the banking program be updated for SEPA or will converison service be bought from software house?

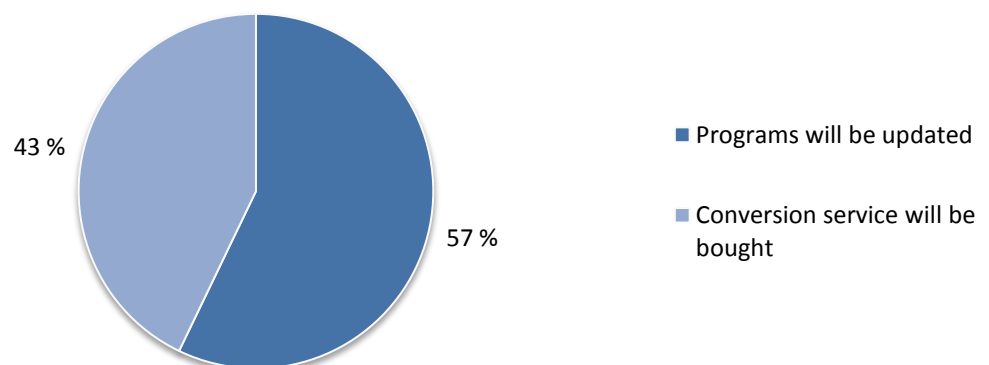


Figure 7.11 Software update plans

The preliminary estimates of SEPA implementation costs shown in figure 7.12 are relatively realistic according to Basware. Results show that one third of the companies estimate costs to be in scale of 1 000€ - 5 000€, and same amount has calculated the costs to be between 5 001 – 10 000€. Tapani Oksala states that it is difficult though estimate costs deriving from SEPA as it depend much what and how many systems company is using. Furthermore, costs may rise towards the end of the year. This way software houses try to get companies implementation processes started as soon as possible and at the same time to avoid possible peak in the end of the year.

Estimates of less than 1 000€ indicates strongly that the company does not have enough information concerning needs of SEPA implementation. But then again this might occur from a situation where company will change provider of the banking program, when costs deriving from SEPA is difficult to separate from other costs due to change of program provider.

Reason for not being able to determine the costs can be due to many reasons. Firstly, changes in cash management procedures are implemented on a group level, from where companies get instructions and other information needed.

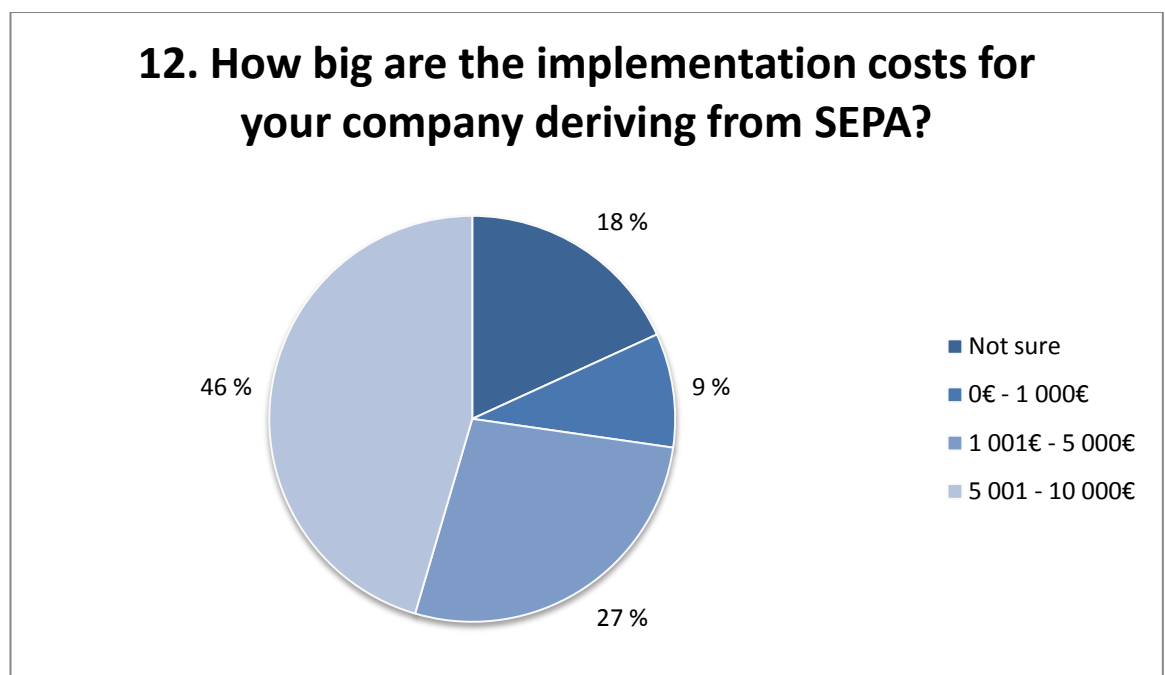


Figure 7.12 SEPA implementation costs

About one third of companies are not sure if SEPA creates significant cost savings (36%). All the respondents said that no accurate calculations have been made yet. One reason for this may be that the exact implementation costs are not certain at the moment. However, 27% of the respondents believe that cost savings will arise whereas 37% believe otherwise. Some of the survey's respondents said that in the beginning they do not see any significant costs savings, but possibly in the long run savings may appear.

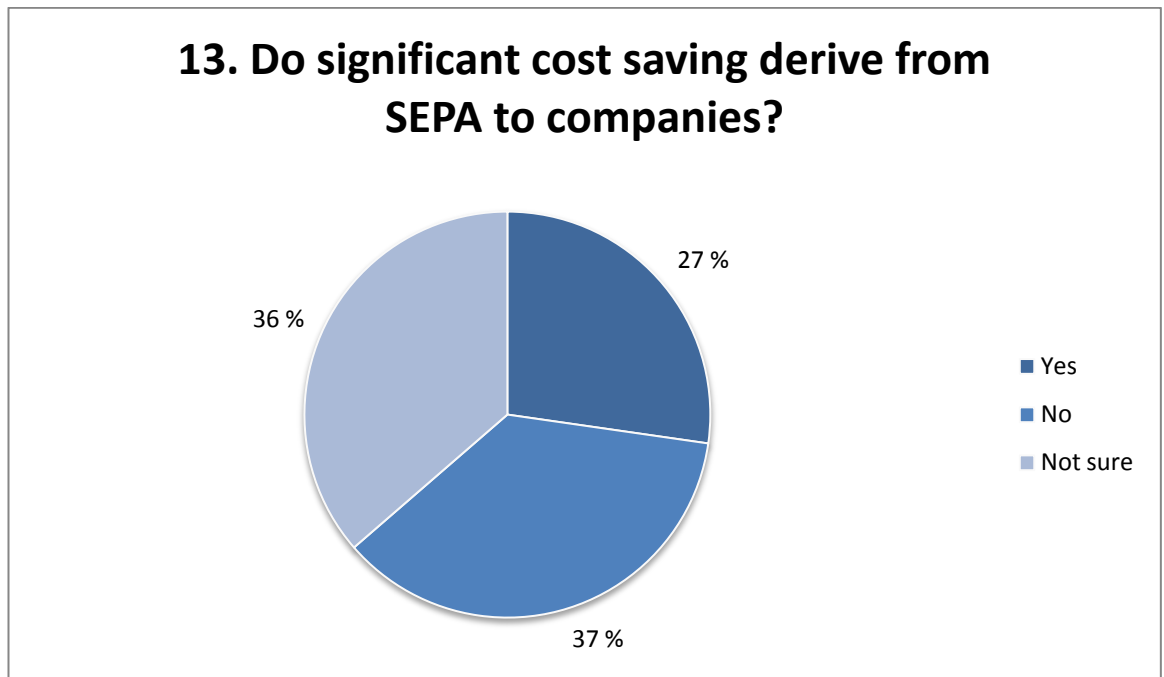


Figure 7.13 Cost savings to companies from SEPA

8 Conclusions and recommendations

Impact of SEPA from market perspective is still unclear and what benefits and opportunities it may offer or possible disadvantages and threats for all stakeholders. In figure 8.1 are illustrated four possible outcomes depending on how various stakeholders act during the SEPA transition.

This market scenario figure is used to predict and clarify possible impacts of SEPA to payments market. It concentrates to two essential parties and drivers of SEPA integration. The supply side of the stakeholders, mainly banks, is on the horizontal axis. This reflects the strategies and actions of the banks towards SEPA, which is categorized into reactive and pro-active. The vertical axis illustrates the demand side (companies, consumers, etc.) strategies to SEPA. It is divided into opposition to SEPA and require of SEPA products.

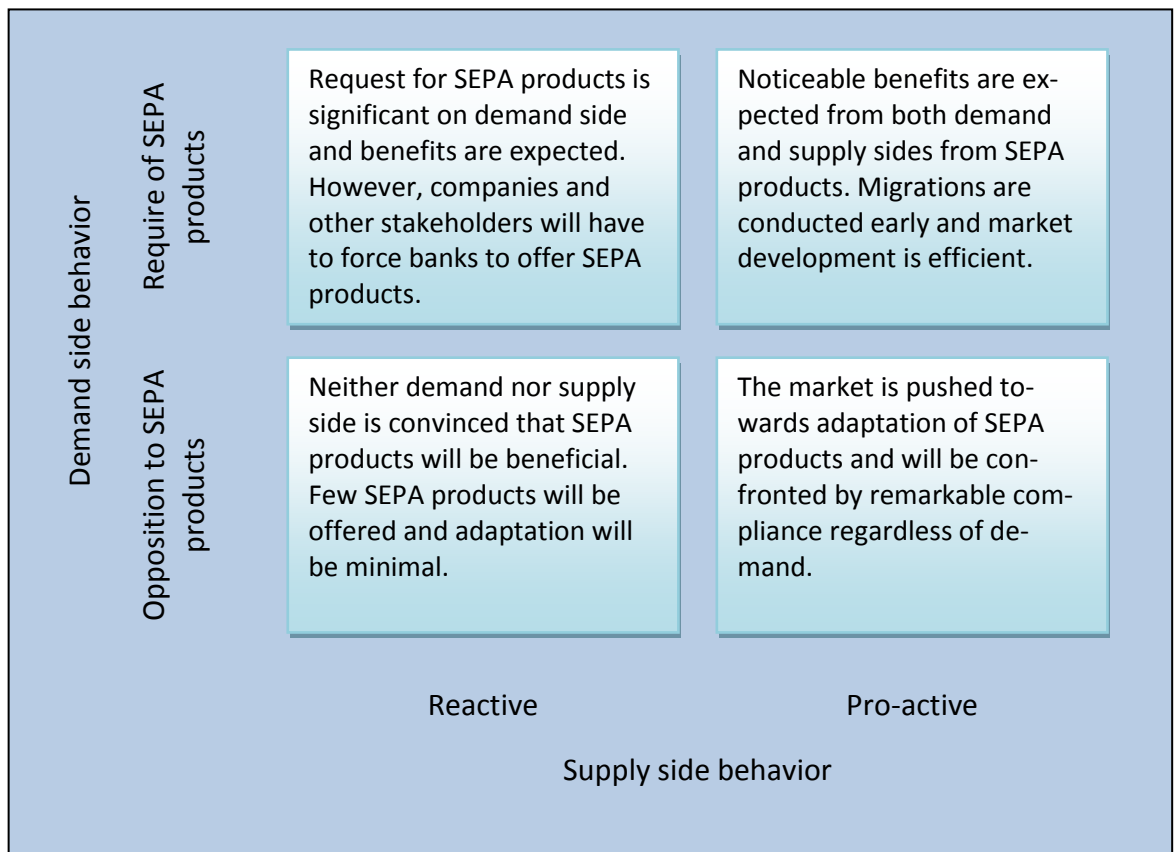


Figure 8.1. Possible market developments due to SEPA

Each one of the four market scenarios represents a possible outcome of SEPA. Which one will it be, is yet to be seen. The SEPA has taken outstanding amount of time and resources to get where it is now and to reach its final destination. The costs may be high to rationalize the unified European payments market, but the possible long-term benefits may justify the needed

changes. As of spring 2010, the success or failure of SEPA is still in balance and moving towards the goal of integrated European market, which basically have been visualized already in 1929 in the League of Nations. The benefits ascending from SEPA to all parties depends much of what market scenario will come true. If banks are reluctant to develop new products and cannot provide relevant information to demand side, companies may experience SEPA as a burden which only creates costs and therefore will not actively promote it. If some companies do see the possible benefits of SEPA regardless of banks reluctant behaviour towards changes, it will be difficult to take advantage of these opportunities. In this scenario, the large powerful companies with good banking relations may be able to force the banks to develop and provide new tailor made SEPA products to enhance their cash and liquidity management, whereas the smaller companies have to settle with less developed procedures and products.

One scenario is that banks will take pro-active actions to promote SEPA, but they are unable to inform companies well enough of the possibilities and benefits of SEPA. This may lead to a situation where banks are pushing the market to adapt to the changes, which requires lot of resources from banks. Though benefits may derive from new SEPA products, increased costs force banks to ascend service fees in order to maintain competitive and hence hinder the integration process of SEPA. However, an ideal outcome would be that banks are pro-active and market is requiring SEPA products which will create on time and highly integrated market with various new SEPA products.

When thinking of what changes SEPA creates to payment transactions and how will these changes affect companies' cash management? The main benefits of SEPA for corporate derive from the ability of making and receiving payments within the euro zone as easily as within their own country. However, an important benefit of SEPA for many companies in Finland will be the potential impact on their liquidity management; the methods of using cash balances in multiple countries and currencies for efficient short-term investment in order to maximize earnings or decreasing the internal funding costs.

Commonly companies in Finland that have operations abroad have had accounts in each country where they operate, often resulting in multiple banks. This is why companies are faced with various operating practices, and different terms and conditions, which reduces the ability of companies to manage their liquidity efficiently. SEPA will remove this lack of standardization and offers the possibility for companies to consolidate their transaction processing with one bank and to use one central account.

SEPA is a further evolutionary step affecting how companies manage their liquidity, cash balances and payments in the future. Although there has already been a considerable level of concentration of liquidity management; SEPA will potentially simplify euro liquidity management further and will take its place alongside other regulatory initiatives and changes that are driving the trend for companies to extend the range and scope of existing practices to encompass multiple currencies and countries outside of Europe.

Companies can benefit from SEPA in various ways. For instance, SEPA has accelerated current trends in cash management. These current trends in cash management and corporate treasury strategy more generally, are being shaped by the two drivers of technological advances and the objective to fully utilize significant investments made in standardized ERP solutions, such as SAP and Oracle, as well as other treasury systems. In terms of regulatory changes, SEPA has been the key issue. In order to meet the challenges faced by changing standards, as well as leverage the maximum benefit from technological developments, a strategy of standardizing, centralizing and automating treasury functions continues to underlie best practice in corporate cash management. While treasury centers in different companies will take different strategies in their respective roles depending, for instance, on their industry or whether the business as a whole has a cost-led or profit-led approach to treasury management. Two associated needs will emphasize the work of almost all: achieving reduction of costs without sacrificing service delivery or functionality and efficiently managing working capital and various risks.

For companies that do not operate centralized service centers, SEPA could prove a relief to liquidity management. However, the nature of companies must be taken into account when weighing the potential benefits of adopting a single account to process transactions across the SEPA region. Companies with decentralized and complex multiple legal entity structures, the logic of moving to a single account structure are weaker. Where a company has a situation where local subsidiaries are responsible for local payments, the challenge of moving to a single account is even greater. SEPA provides an impetus for centralization but it may not justify the necessary ERP technology spend and change in working practices required by this level of centralization.

SEPA should get companies ask themselves why they currently have local accounts and what purpose those are serving and review them in light of these issues to survey if these accounts are needed in any way in the SEPA environment. Banks have a role to play in helping the companies to understand these issues and to make sure companies will be engaging with them

sooner rather than later. Though there have been relatively much discussion that small companies do not benefit from SEPA and it is only seen as a burden, regardless of a company's size, operating environment or structure, SEPA offers a good reason to map their account operating model for opportunities to enhance efficiency and competitiveness.

The Single Euro Payments Area is now a reality. SEPA Credit Transfers (SCT) and their mandated operations are now in production, and with the new amendments the market is seeing a glimpse of life in the post-SEPA era. For many, confidence is high and the ability to deliver against a mandated change is now proven. Looking forward, all focus is now on the SEPA Direct Debit (SDD), long seen as the more complex of the instruments, and therefore a bigger challenge. Hence, many companies have utilized E-invoicing which corresponds more the current national direct debit in use.

As the research shows, companies in Finland have prepared well to SEPA migration. Knowledge in companies is appropriate, and actions have been taken in order to implement SEPA products and procedures. However, those companies that have not taken actions yet, now is the time for companies to contact their banks, software houses and ERP providers to finish the SEPA projects as soon as possible, despite what market scenario will become true. This way companies can make sure they will utilize all benefits concerning cross border payments, enhanced liquidity and cash management as well as standardized group level ERP system solutions. Moreover, companies should continue to adopt the SEPA products, because these products already available will not be the last ones. Banks will definitely develop new products; hence the implementation will be much easier for companies if they can adopt new products and procedures step by step. In addition to new payment standards, new account statements will replace the current account statements (Appendix 5.) and payment feedback standards. For instance, the Federation of Finnish Financial Services has already published standards for the new account statement. Overall, this seems to be only the beginning of SEPA and constantly developing corporate cash and liquidity management.

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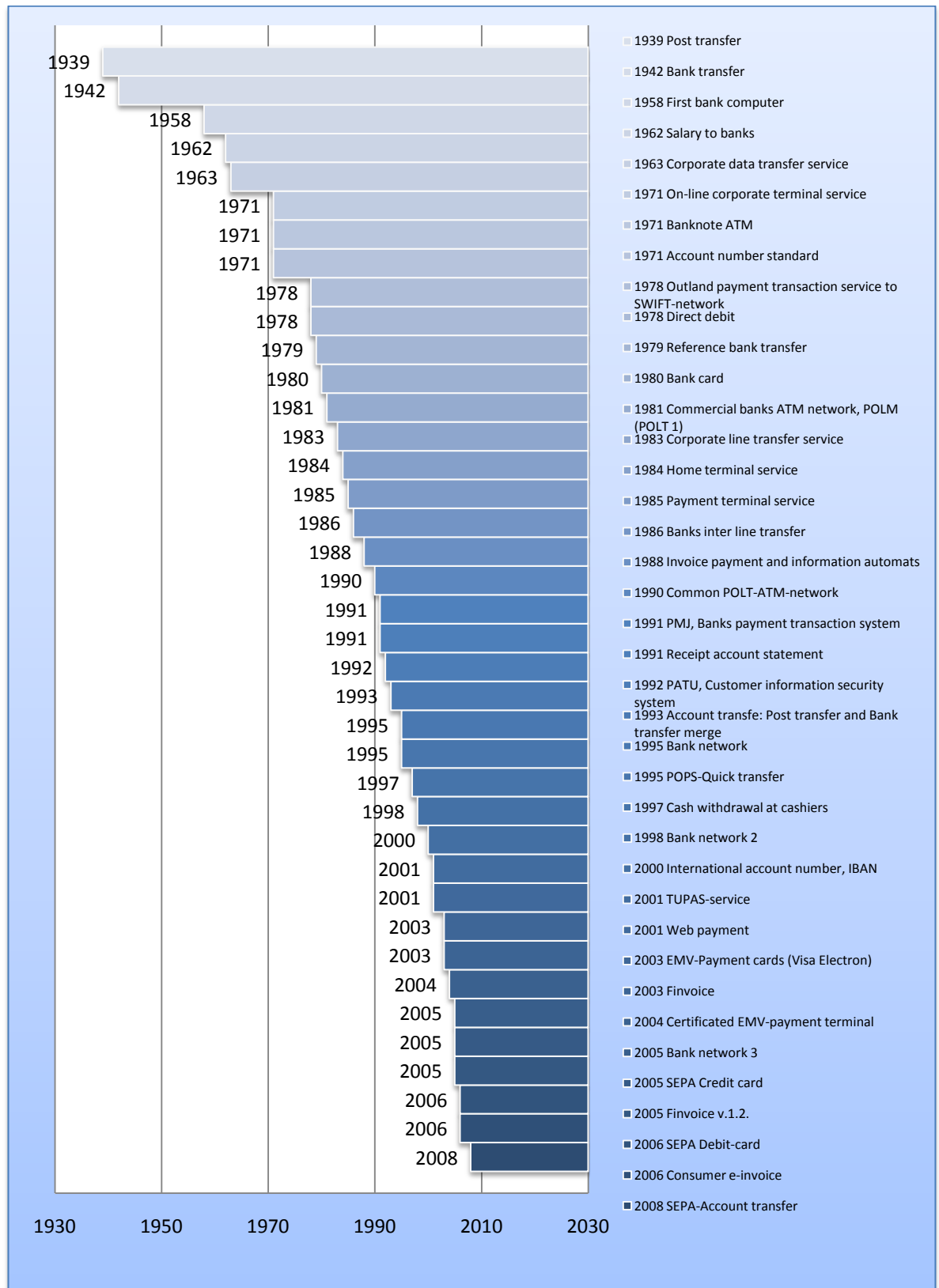
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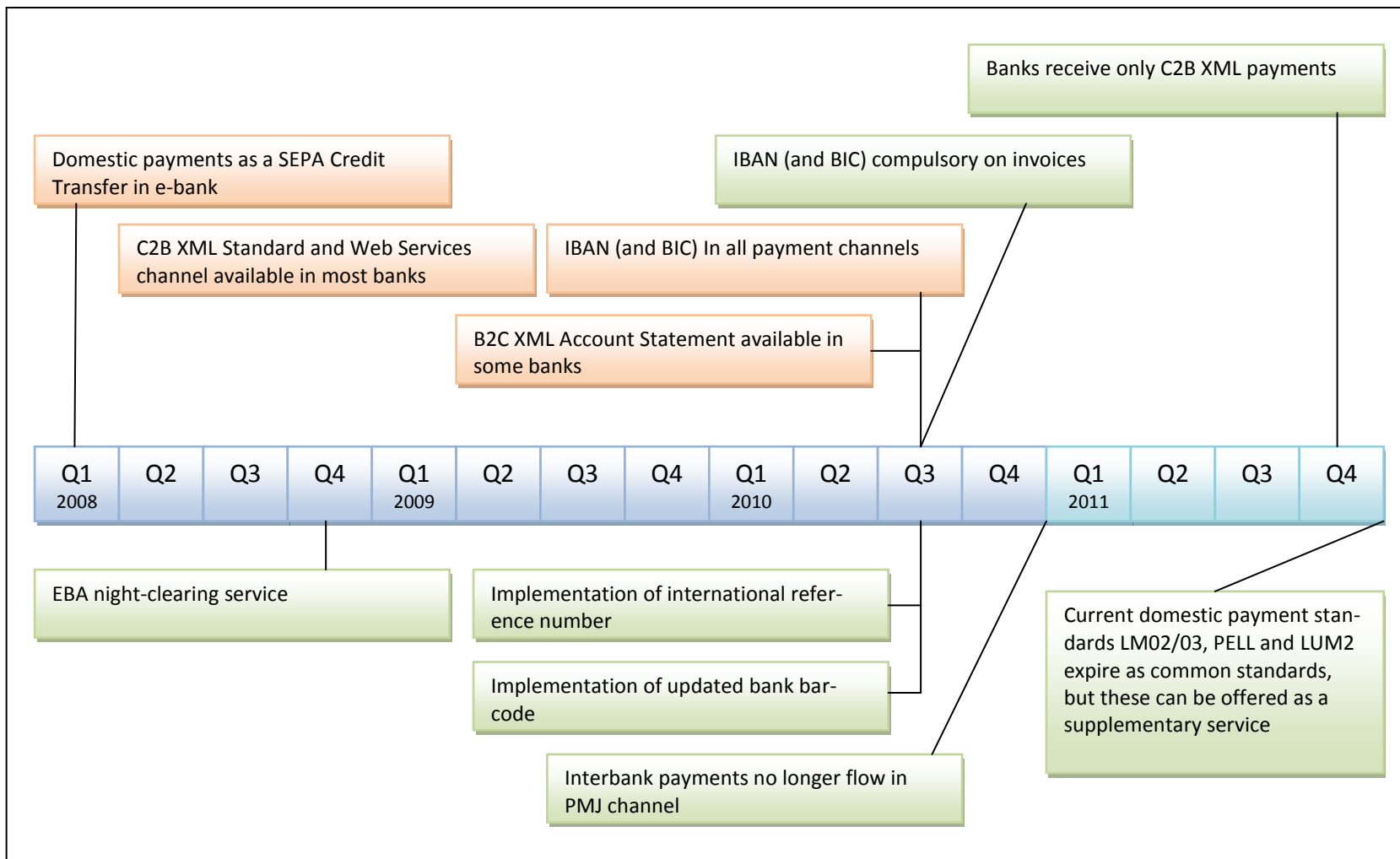
Appendix 1. Timeline of European integration (ILSP & MIRC)



Appendix 2. Development of bank technology in Finland (Handbook of Financial Activities)



Appendix 3. Finland's transition timetable of SEPA Credit Transfer (Sampo Bank)



Appendix 4. Example of XML file. (Nyholm 2009.)

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Appendix 5. Example of account statement (Pasanen 1992.)

POSTIPANKKI POSTBANKEN
 ASIAKASPALVELU KLO 8.30-16.30 PUH. (90) 164 4900

TILIÖTE 43/92 ①

Sivu 1

Kausi ②
 19.10.-24.10.1992

Päivämäärä ③
 24.10.1992

SHRTOTILI
 2199 812

Limiitti

ASIAKAS
 C/O OSOITE
 JAKELUOSOITE

POSTIN:O JA OSOITETOIMIPAIKKA
 SIJAINTIMAA

ARKISTOINTITUNNUS SAAJAN TILINUMERO	MAKSU/ ARVO PVM.	SAAJA/MAKSAJA VIESTI	TAP. N:O	TILIÖINTI	MÄÄRÄ
⑤ KIRJAUSPÄIVÄ 19.10.92 921019 800300012312 K	1910 1910	POHJOLA VAKUUTUSYHTIÖ 710 SIIRTO KASSALLA VAK.NO 123 PALAUTUS	⑩ /J 1	SALDO 19.10.92	35.000,00 + 3.100,00 +
⑥ ⑦ ⑧		PANOT YHTEENSÄ 1 KPL OTOT YHTEENSÄ 0 KPL	0 0	SALDO 19.10.92	38.100,00 + 3.100,00 + 0,00 -
KIRJAUSPÄIVÄ 20.10.92 921020 801000008823 A 5 027	2010 2010	SUOMEN LVI-TUKKU OY 702 MAKSUPALVELU LASKUNNE 1.10.92 ⑭ ASTAKASNO 7234590	/J 2	SALDO 20.10.92	315,00 - 37.785,00 + 0,00 + 315,00 -
KIRJAUSPÄIVÄ 22.10.92 921022 800530A06777 K	2210 2310	H. HUHTAMO 710 PANO VIITE 9221711149008922	/K 3	I	1.015,00 +
921022 800720001123 K	2210 2310	SALLINEN MERLEVI ⑬ 710 PANO VIITE 9221711149008922	/K 4		850,00 +
KIRJAUSPÄIVÄ 23.10.92 921023 800450A08881 K	2310 2310	⑫ 722 SHEKKI NO 123	5	SALDO 22.10.92	39.650,00 + 1.865,00 + 0,00 -
		PANOT YHTEENSÄ 2 KPL OTOT YHTEENSÄ 0 KPL	0 0	SALDO 23.10.92	11.000,00 - 20.650,00 + 0,00 + 11.000,00 -
TILIÖITTEEN YHTEENVETOIEDOT:		⑮ PANOT YHTEENSÄ 3 KPL OTOT YHTEENSÄ 2 KPL OTTOJEN KORJAUKSET 0 KPL PANOJEN KORJAUKSET 0 KPL		SALDO 23.10.92	20.650,00 + 4.965,00 + 11.315,00 - 0,00 + 0,00 -