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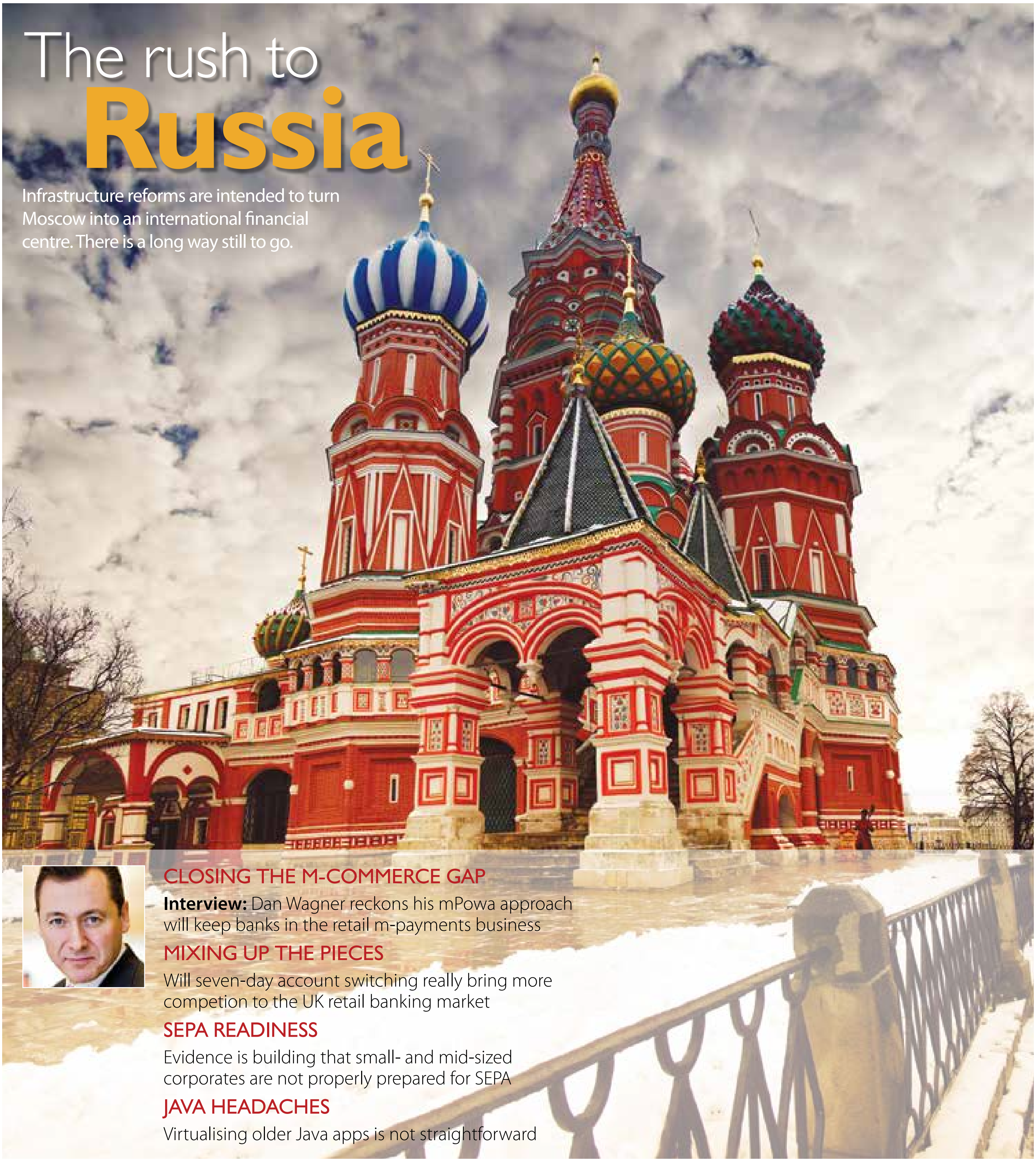

The rush to Russia

Infrastructure reforms are intended to turn Moscow into an international financial centre. There is a long way still to go.

CLOSING THE M-COMMERCE GAP

Interview: Dan Wagner reckons his mPowa approach will keep banks in the retail m-payments business

MIXING UP THE PIECES

Will seven-day account switching really bring more competion to the UK retail banking market

SEPA READINESS

Evidence is building that small- and mid-sized corporates are not properly prepared for SEPA

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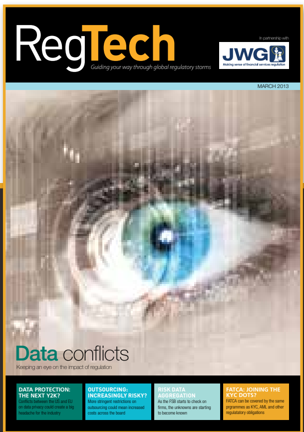


OUTSIDE BACK COVER – REGTECH

The latest edition of the collaboration between Banking Technology/JWG examining the technology impact of regulatory compliance looks at the clasu between US and EU data regulations, the challenges of risk data aggregation, new stringent outsourcing rules – and the good news about FATCA reqirements.

Put out fewer flags

There are many ugly words bandied around in this industry – disintermediation, fungibility, for starters – so I'm loath to add another, but here goes: deglobalisation.

For years, a nautical wagon-train of container ships has been plying the oceans between the manufacturing centres of Asia and the consumer centres of the West. Such is the imbalance of trade that some of these slab-sided monsters make the return journey with empty holds.

You can book a relatively cheap ocean cruise on them, but you might prefer to spend your leisure time on a weekend break. New York or Dubai are popular, in contrast to your parent's generation, which will think of Paris for the weekend. That's a day-trip now that the London tube's been extended to Gare du Nord.

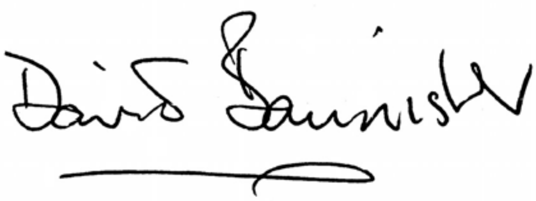
A whole generation has grown up watching the world shrink: round-the-world travel has become the norm for gap-year students rather than just Hollywood stars and business tycoons.

That was globalisation. Post financial crash and in the face of growing ecological awareness, welcome to deglobalisation, a period when nation states start reasserting their individuality.

The euro crisis certainly fuelled this in Europe, as the tensions between North (rich) and South (not-so-rich) Europe threatened to undo all the work towards union and harmonisation that has been going on since 1945. The differences between the French, German and UK approaches to their financial services industries are starting to have a similar effect, as the UK government tries to prevent its European partners imposing regulations that will affect its schizophrenic relationship with the UK banking sector.

The US, meanwhile, seems to be heading towards its own nervous breakdown, and may well have fallen (or jumped, if you prefer) over a fiscal cliff by the time you read this.

National pride is a fine thing, but nationalism can lead to some very horrible places. Let's not go there.



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News in FOCUS

NY techies more bullish about jobs

Technologists in financial services are the least loyal to their employers, even though they also have the worst perception of the economy and of their employment prospects.

A survey of financial services workers in London, New York and Singapore by recruitment consultants Selby Jennings found that those working in technology are "the least likely to remain in their role regardless of the current economic issues".

The New Yorkers are the most optimistic in the financial technology world, with 23% saying that they think their prospects for promotion are getting better, while 35% said that employment prospects are improving against 17% saying they are worsening.

In London, the balance is gloomier: 5% think things are getting worse on the job front, against 2% who say it is getting better. In Singapore, the techies – and almost everyone else – are very gloomy about the employment situation.

"New York is one of the most buoyant markets for technology, with many organisations looking to drive competitive advantage by making key hires across all levels of seniority," said Clare Cooper, head of technology at Selby Jennings. (*above*)

The New York techies are the most negative about their bonuses, though, with 24% saying that they expect less this year. Only those working in fund management were more pessimistic, with 27% saying things are getting worse. New Yorkers are also more concerned about their bonuses than their salaries.

Across all three locations, the most optimistic group are those working in risk management and analytics, while those in sales and trading are the most negative. *BT*

Tradition leads the charge for FX systems transparency

A flurry of announcements from banks and systems suppliers heralds changes in the FX market, reports *Elliott Holley*

A new FX platform built by inter-dealer broker Tradition and backed by 11 major global banks aims to remove the competitive advantage of low-latency trading in FX.

Due to launch "within weeks, not months", ParFX is an electronic spot trading market that will offer trading in all the currency pairs supported by the CLS settlement system. The core idea is to provide open access to all users on a fair and equal basis – regardless of latency.

To make that happen, the platform uses randomisation technology – users submit their orders to a 'green room', which randomises the input of the trade to the matching engine for a very short period of time – milliseconds – and then hits the matching engine. The result is that there is no longer any advantage to low-latency strategies such as co-location, operating through multiple connections. In theory, even a market participant trading from Australia against another trading from London should have the same opportunity in terms of reaching the matching engine.

"Banks are spending a fortune out there to fine-tune their systems to ensure that they can compete effectively with HFT," said Dan Marcus, global head of strategy and business development at Tradition. "Our platform removes all that. It's an environment where everybody trades on a level playing field. It is designed for people who need to trade, rather than people who want to spoof or game the market."

Pricing structures for ParFX are also designed to be different to other FX ECNs. Marcus says that the platform will charge connections at slightly above cost just to cover the firm's expenses, but will not make it a profit centre, nor will it offer any special fees to favoured participants. The same principle will be applied to market data.

"ECNs make a fortune from market data, and they provide different quality packages, so you can get faster or slower data depending on how much you wish to spend," said Marcus. "We are going to provide quality market data to all participants at cost. The idea is everyone's got the same market data, so you can't use it to get a competitive advantage."

Thomson Reuters and EBS aim to provide the most accurate picture of live prices

Historically, the two main FX platforms for origination have been ICAP's EBS and Thomson Reuters. The main alternative platform is FXall – itself now owned by Thomson Reuters. However, concerns over liquidity and transparency have prompted some entrants to the market in recent years. In August 2011, SURFACExchange opened a central order book trading venue for FX. Headed by Evgeni Mitkov, the venue aims to provide an alternative for buy-side customers to the custodian banks. Last month EBS and Thomson Reuters agreed to combine the sources for their FX pricing, in a co-operative bid to increase transparency.

The stated intention of the EBS/Thomson Reuters collaboration is to provide the most accurate picture of live-traded prices possible. Although prices have been posted every 30 minutes since March 2011, the rates were based solely on the main liquidity pool for each currency without taking into account the entire market. The new blended FX fixing will be available on the EBS Market before the end of this year. It is already available on Thomson Reuters Eikon.

"This collaboration between Thomson Reuters and EBS is a great example of the industry working together to improve the overall trading experience for the benefit of all market participants," said Phil Weisberg, global head of foreign exchange, Thomson Reuters. "By blending Thomson Reuters and EBS sources for our 30-minute FX fixings we are ensuring that maximum liquidity has been calculated within each currency fixing and therefore providing maximum transparency for the marketplace."

However, ParFX is also seeking to market its transparency.

Other platforms generally do not require market participants trading through a prime broker to reveal their identity; ParFX requires users to provide full names.

"The idea is crime prevention rather than punishment," said Marcus. "On most other platforms, you can sit behind the prime broker's disguise and trade in a way that counterparties won't be happy with, without the counterparty identifying who they are dealing with. But on our model, if you are Morgan Stanley dealing with JP Morgan, and you have Pimco going through JP Morgan, Morgan Stanley will see that they dealt with Pimco. If you have legitimate intentions, you shouldn't have an issue giving up your identity to the counterparty." ***BT***

Nordea backs Holvi plans for online European banking revolution

A new start-up bank from Finland plans to open across Europe, using an online-only service that it says will redefine what it means to have a bank account.

Holvi plans to provide debit cards as well as online banking services; it will also combine elements of personal financial management with social media tools. On Holvi, users create a profile. They are able to create different profiles for different purposes, such as running a business or organising a wedding, and can use Holvi to set targets and manage their budget. Users can also create a shared account and start group discussions.

The idea is to create a more community-led approach. Users will also be able to buy and sell services directly from each other, such as learning to speak a new language or sports training, through a kind of iTunes-style store.

Holvi is backed by Nordic banking group Nordea, which will provide the transaction banking infrastructure the company needs to complete its planned pan-European rollout by the end of the year. The company has said it will not attempt to build the entire banking infrastructure itself. Instead, it is keen to partner with other firms so that it can focus on building the customer interface. Nordea is also providing Holvi with the APIs that it needs to connect the front-end that the customer sees, with Nordea's underlying core banking systems.

"We've re-thought every aspect of what an account is," said co-founder Kristoffer Lawson. "Traditionally banks offer everything in house – investments, cards, everything. But that model doesn't recognise the changes the internet has brought. Much more nimble companies like Wonga and Nutmeg are eating away at the core bank business. Our plan is to be part of that wave, and to partner with the transaction banks to provide a far superior user experience to the siloed systems of the past."

Other online banks have existed for a long time. Smile, the UK's first full internet bank, has existed since 1999, while all major conventional banks offer online banking. But Holvi currently has just nine employees, and is proud that its founding members do not come from a traditional banking background. Instead, their origins are in technology.

"Innovation often comes from people who have a different background," said Lawson. "Apple went into mobile phones. They had no experience. The iPhone looked nothing like another phone. Nokia laughed at it. But it improved the user experience, and Nokia is not laughing anymore. Coming from a different background frees a company to think about things in a different way, without being tied to the old model." ***BT***

VocaLink study finds people prefer banks for mobile payments

Banks may have a poor reputation with the public, but the majority of people in the UK would be more likely to adopt mobile payment services if they are provided by a bank.

New research from VocaLink into UK consumer appetite for alternative ways to pay on mobile devices shows that 81% of those interested in new digital payment methods say they are more likely to adopt such services if they are provided by their bank.

VocaLink developed and will run the mobile proxy service that underpins the Payment Council's planned mobile payments service, currently scheduled for introduction next year. It will be similar to the Pingit service offered by Barclays.

The research, undertaken by Accord for VocaLink, includes both qualitative and quantitative analysis across 5,000 UK consumers, merchants and businesses. Among the quantitative findings are:

- 33% of smartphone owners in the UK have used them to shop online
- 42% of smartphone owners have used them for online banking
- 43% of tablet owners in the UK have used them to shop online
- 33% of tablet owners have used them for online banking

On the qualitative side, convenience and ease of use were cited as important factors in encouraging consumers to adopt these new ways to pay. However security remains as important for new digital methods as well as existing payments methods.

"Banks are trusted to provide safe and secure transactions, regardless of channel and the delivery of alternative payments is a clear opportunity for banks to maintain and build greater customer engagement. Traditional institutions have a key role to play and should be at the forefront of payments innovation by delivering services based on consumer demand," said Paul Stoddart, managing director for strategy and business development at VocaLink. ***BT***

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News in BRIEF

FircoSoft has signed a partnership with Indian IT services specialist iSolve to resell its watch list filtering products in order to help financial institutions better comply with tightening regulations within India. iSolve already sells compliance solutions to financial institutions in India, making the addition of FircoSoft's filtering solutions to iSolve's portfolio a logical step. It will be mainly targeting and serving large banks in India, the partners say. iSolve will resell Firco Continuity to filter transactions and avoid processing illegal payments, Firco Trust to filter entities and/or customers' information to prevent doing business with risky parties, and the Firco List Service to enhance list management and filtering performance. Implementation and support services will be also offered by iSolve.

While card payments continue to grow – up by 10% in 2011 – the use of cash is still growing "at a more than healthy pace", says the latest edition of the European Payment Cards Yearbook.

According to the yearbook, the use of cards to withdraw cash at automated teller machines was also up – with 17.3% more ATMs issuing 2% more cash during the year.

In 2011 there were 41.99 billion card payments across the 33 countries, showing a growth rate of 9.1% and amounting to an average 69.7 payments per capita per year – the national figures ranged from 3.8 payments per capita per year in Bulgaria to the "exceptional" high of 327.8 in Iceland.

Market data and technology company **Activ Financial** has expanded its risk gateway tool to cover all Canadian exchanges, in response to new rules that require market participants in Canada to have pre-trade risk controls in place across all asset classes from this month. The Activ Financial tool, TradeDeck, allows brokers to control pre-trade risk on all orders that enter the market, with real-time intra-day adjustment, order monitoring and a kill switch. The technology covers market data feeds, order routing and credit risk. It also has the ability to set credit controls for intraday margin calculations.

Market participants using NYSE Technologies' market data feed SuperFeed and SFTI network will soon be able to get social media sentiment statistics, following a deal between NYSE and specialist company Social Market Analytics. The SMA engine evaluates data in real time to attempt to generate directional and volatility indications on individual stocks, exchange-traded funds, sectors and indices by measuring the level and quality of social media interactions. SMA's engine uses seven statistical indicators to track sentiment, in addition to volume, change and dispersion of social media commentary.

The National Bank of Abu Dhabi has adopted a monitoring service from Canadian technology company Inetco Systems, to keep track of its ATMs and ensure they are working properly. NBAD currently has 120 branches and 490 ATMs across the UAE, The NBAD ATM and IT teams receive instant notification when transactions slow down, time out or fail and can use the information to find problems such as communications failures or infrastructure bottlenecks.

High frequency trading specialist Rapid Addition has partnered with IBM to provide an ultra-low latency service for financial firms that are very sensitive to speed. Rapid Addition's Cheetah FIX engine will be integrated with IBM's WebSphere MQ Low Latency technology to ensure the highest possible speeds through FIX messages.

"We are always looking to build on our portfolio of technology partners and IBM is one of the biggest names," said Kevin Houstoun, chairman of Rapid Addition. "Our work with them will continue on into future projects to improve performance of the joint offering and on other innovative services in the pipeline."

Using Rapid Addition's Binary FIX message format as the IBM WMQ LLM message payload allowed specific optimisation of the Cheetah FIX engine interface for transmitting and receiving messages over the IBM LLM message bus, it also minimises latency.

Commerzbank has adopted a visual transaction signing tool from UK security firm Cronto for its online banking customers, designed to protect against Trojan malware.

The CrontoSign technology has been deplyed under the photoTAN brand, replacing the iTAN security solution where a unique number is used to authorise each banking transaction. With photoTAN, users will be able to verify payments with a mobile app or a standalone device using a unique authorisation code (TAN) to sign the transaction. Cronto and Commerzbank have been collaborating since 2008.

Danish bank **Jyske Bank** has gone live with **SmartStream**'s TLM Corporate Actions processing software, which includes different modules such as reference data manager, event manager, communications, election management, entitlement calculation and posting to keep control of the bank's data, milestone dates and key tasks associated with all events.

Experian has improved its Hunter anti-fraud software, allowing users to group several customer applications into a single case, allowing the investigation of all related applications to check whether they are linked to earlier instances of fraud. The aim is to prioritise potentially dishonest claims based on the risk and outcome of previous related applications. Those that pose a significantly higher threat are highlighted by Hunter. Where users identify a possible fraudulent application, they can now capture more detailed information including the type of fraud and the potential loss if the request were to be accepted.

Infosys has formally announced its BigDataEdge platform, designed to allow banks to bring together Big Data analytics onto one platform. By integrating different elements, Infosys reckons that user organisations can reduce the time taken to extract information by "up to 40% and generate insights up to eight times faster". ***BT***

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Clear thinking

The UK Government is committed to reforming the payment system. Don't hold your breath, says *Heather McKenzie*

In a speech last month the UK Chancellor, George Osborne, said his government would "bring forward detailed proposals to open up the payment systems", ensuring new players can access such systems in a "fair and transparent way".

At present, he said, new players have to go to one of the existing big banks to use the payment system. Moreover there are apparently no incentives for the big banks to deliver "new and better services for users – like saving the cheque or creating new services like mobile payments". Clearly the cheque isn't a new service, so Mr Osborne must envisage there is a "better" way of delivering cheques.

The speech made no reference at all to the Faster Payments system in the UK, which was developed by UK banks and reduced payment times from three working days to a few hours. But Mr Osborne wanted to look tough on banks, so Faster Payments took a back seat. As did details of the government plans.

Debating payments system reform in the UK is nothing new – in 2001, another inquiry into the banking system, which resulted in the Cruickshank Report, suggested a separate payments regulator and a new governance structure for payments. It was rejected and subsequent alternatives have foundered on the rocks of vested interests.

The latest round of debate is of course tied into the global financial crisis and the issue of 'too big to fail'. It is also related to the furore that surrounded the Payments Council's attempts to phase-out cheques in the UK. This was an issue pounced on by the tabloid press in the UK – many stories about little old ladies appalled at the thought of no longer being able to use cheques, etc.

So, the payments system must be reformed (or the Government has perhaps deemed that it must be seen to be doing something). A solution could be the development of a single platform for payments that would act as a utility for the industry. This view is gathering support and was mooted by Andrew Haldane, executive director for financial stability at the Bank of England, at a meeting of the UK Parliamentary Commission on Banking Standards Committee in November last year. "Now is the right time to think about alternative models," said Haldane. "Whatever governance body comes into play has to have an overt public interest objective that leans against the inevitable tendency of banks to structurally under-invest in payments technology."

Around the same time Mr Osborne was making his speech Eurogiro was celebrating its 20th anniversary. Created in the early 1990s by a group of European postal organisations to modernise their common, cross-border payments businesses and "prepare themselves for stronger competition", Eurogiro's members include postal companies, post banks, small and large banks and other payments services providers and mobile operators.

All of the profit generated by Eurogiro is invested back into the company, to improve the electronic payments network it runs. The network is highly automated and based on an architecture that enables bulk payments. Based in Copenhagen, the company has just 14 employees (yes, 14!). Eurogiro now processes more than 30 million cross-border payments each year in 50 countries.

Obviously Eurogiro is a different type of beast from a utility for UK payments, but it shows what can be done collectively.

Governments around the world are increasingly identifying payments as an important part of their economies. In Australia, for example, central bank The Reserve Bank of Australia, last year called for local debit card issuers to agree on reforms to support multi-network cards. This is considered an important step in order to ensure the local EFT/POS debit system can compete with Visa and MasterCard.

A study published in Canada last month found that the growth in the use of electronic payments products such as credit and debit cards added $9.7 billion – USD – to the country's GDP during the past four years. Conducted by Moody's Analytics, the study of 56 countries stated: "card usage makes the economy more efficient, yielding a meaningful boost to economic growth". Globally, electronic payments contributed $983 billion to the GDP of the 56 countries examined between 2008 and 2012. Over the same period, GDP in those countries grew by an average of 1.8%.

The study was conducted on behalf of Visa, which could explain the rosy portrayal of card payments. However, there is little doubt that the trend in payments is electronic and not, as the UK Chancellor seems to believe, towards the paper cheque.

VocaLink commissioned research into digital payments in the UK, published last month, which says consumers are more likely to adopt mobile payments methods if they are provided by a bank (*see page 5*).

VocaLink's Paul Stoddart, managing director, strategy and business development, reckons there is an opportunity to "revolutionise the UK payments industry" by using portable devices. However, many people can get left behind in a revolution (particularly cheque-using old dears). As recent history suggests, any reform to the UK payments industry is likely to be played out in very slow motion. **BT**

OTC derivatives reforms must be global to work

International efforts to reform the derivatives markets will not work unless they are consistent – and the DTCC sees itself at the centre of this, reports *Elliott Holley*

US post-trade services utility the DTCC is positioning itself as the provider of a global network of trade repositories – but OTC derivatives reform will only work if consistent measures are taken everywhere, says Stewart Macbeth, president and chief executive at the DTCC (*right*).

"A global approach is needed to make the G20 reforms work," said Macbeth. "Regulatory overheads would be huge without a coordinated effort. We believe the best way to do this is with a centralised system that can bring economies of scale."

At the Pittsburgh summit in 2009, world leaders agreed to reduce systemic risk in global financial markets by mandating the central clearing and reporting of the vast bulk of OTC derivatives trades. This was done partly as a reaction to the massive default of Lehman Brothers in 2008, in which a lack of clarity over complex OTC derivative positions led to a freeze on bank lending.

The DTCC is positioning itself as the champion of the new reporting obligation. As far back as 2003, the organisation had established a subsidiary, Deriv/SERV, that provided confirmation matching for OTC credit derivatives. That service was expanded to create a Trade Information Warehouse in 2006, which later became the inspiration for today's trade repositories, according to Macbeth.

"We've gone from a situation where data wasn't available, and what was available wasn't shared, to a situation where regulators can see market risk exposures to a good level of detail," he said. "True, our coverage of FX and commodities is limited today due to different regulatory timelines for their rollout. But that will change."

In the US, reporting began for rates and credit on December 31 2012. Reporting rules for FX, equities and commodities took effect on 10 January under the Dodd-Frank act, but market participants are not required to comply until 28 February. Reporting across all asset classes is due to begin on 12 April 2013.

In Europe, under the European Commission's EMIR legislation reporting requirements begin from 1 January 2014 for commodities, equities and FX, with reporting for credit and rates due by 1 July. The DTCC has said it will look to register as a trade repository with the European Securities and Markets Authority.

In Asia, Japan will require reporting by 1 April this year for rates, credit, equities and FX. Singapore is working on detailed rules and will hold a consultation in March; Hong Kong has developed a trade repository which is testing in Q3, although the legislation is not yet in place; and Australia is currently consulting on the final rules.

"By the end of this year, the major global economies will have substantially completed their regulatory process for the implementation of reforms to OTC derivatives," said Macbeth. "Using the DTCC's Deriv/SERV you can access the public data (which includes aggregated, anonymous position data) on those derivatives from any computer. That is the improved transparency we have all been talking about."

As in Hong Kong, some jurisdictions are either considering or are already building their own trade repositories. These initiatives are generally intended to help meet the G20 obligation on reporting of OTC derivatives; however, the DTCC has warned that there is a risk of too many repositories, potentially fragmenting the data and making it harder rather than easier for market participants and regulators to gain a complete picture of derivatives trading activity.

In response, the organisation has developed a strategy of forming partnerships with local repositories wherever possible, based on reciprocal sharing of data. The idea is that the DTCC will provide the local repository with a global perspective, while the local repositories can feed their data into the DTCC's network to help build a single picture for the world.

"Bringing all the data together consistently is the key thing," added Macbeth. "We believe there are hard economics behind our case. Scale reduces costs and fragmentation, and providing greater global transparency on OTC derivatives is in everyone's interests." ***BT***

Banks to go the same way as pubs? OFT boss moots branch sharing

Increasing political pressure to increase competition among the UK's high street banks could mean forcing them to share infrastructure p or even branches. *David Bannister* reports

UK retail banks could be forced to share branch premises with rivals under plans to increase competition in the market, according to the chief executive of the UK's Office of Fair Trading, Clive Maxwell.

Giving evidence to the Parliamentary Commission on Banking Standards Committee, Maxwell said that a range of options could be considered as ways of increasing competition if the OFT were to refer the issue to the Competition Commission, which has statutory powers to reform industry sectors.

He outlined several models that could be used, the "most obvious" of which would be a "horizontal chopping up of the banks" that would "take out certain bits and put them under different ownership".

The intention would be to overcome the cost barriers to entry for new entrants – so-called "challenger banks".

Asked if this would lead to a market structure where some banks would opt to become providers of back-office services to others offering "front-office", customer-facing services, Maxwell said: "You could envisage that, but whether it's the right thing to do is not clear."

While this could reduce the cost of entry to the market by minimising IT investments for some, others would be left with sunk costs that would have to be written off, he said.

Another option, said Maxwell, could involve some sort of shared access to branch facilities. "Access to a branch is something that most people want," said Maxwell. "It is possible to envisage sharing of that."

He suggested a possible parallel in the way that a perceived monopoly in the UK brewing and pub industry was reformed by the Monopolies and Mergers Commission a decade ago. At that time, six brewers were responsible for 75% of beer production and owned more than half of all pubs, which had to sell their owners' beer – known as "tied houses".

This, it was decided, constituted a complex monopoly that acted in favour of those breweries that owned tied houses. The solution was to limit the number of pubs breweries could own to 2,000 each, which created a new market into which stepped new entrants – known as "pubcos" – the effects of which remain controversial.

Industry analysts were unanimous that the suggestion that retail banks might share branch premises with competitors is unlikely to gain traction, but agreed that there are opportunities for banks themselves to change the structure of the industry.

"I've been following the Commission hearings and some of the ideas are insane," said independent analyst Ralph Silva. "My views are simple: retail banking as we know it is dead, let it die."

Silva agreed that there is still a demand among consumers for branch-based services, but argues that this is largely for advisory services, which are no longer on offer.

"Retail banks have a strong history of advisory centres, and as such they were incredibly valuable: people would walk into a branch and talk to a human being about how they should invest or manage their money. Today, however, banks have all but pulled out of advice and this is what's killed them," he said. "People no longer have a reason to talk to a banker, they are pushed to technology channels and as a result product decisions are based on price points. On this level, the high street banks are perceived to be the same as grocers, car companies and electronic giants."

Daniel Mayo, practice leader for financial services technology at industry analyst Ovum, said: "It is quite old school thinking in terms of regarding the branch as the hub of customer relationship for new entrants these days. If they really want to facilitate new entrants they would be better to make it easier to set up from a regulatory and capital perspective."

This was echoed by Peter Farley, an independent banking industry consultant, and former European head of IDC Financial Insights. "The real barriers are on the capital requirements," he said. "There are plenty of things that the banks could share in terms of infrastructure, but the presence that branches give isn't going to be one of them."

Farley agrees with the proposition that IT costs constitute a barrier to entry, but he says that this is also a major problem for the incumbents as they face plummeting profit margins.

Plenty of precedents exist outside the UK, and in other areas of banking, he points out. Deutsche Bank, for instance, makes a virtue of the white labelling model in the transactional banking services it markets to smaller banks; banking co-operatives like Rabobank in the Netherlands have grown up with this approach as part of their business model; and it has been deployed successfully by the likes of Cincinnati-based Fifth Third Bank in the US, which provides IT and infrastructural services to other banks in its region through a division that has now been spun-out as Vantiv, running on a single platform.

He is less optimistic about such an approach catching on in the UK in the near future, however: "The big banks just don't talk about this in any real sense," he said. ***BT***

Malware on the move

With a 400% jump in the number of malware programs for mobile devices, it is only a matter of time before they become the latest line of attack, reports *David Bannister*

A 400% increase in malware for mobile devices masks a security scene where many of the threats are much as they have been for several years – but where the volume of attacks means that firms should think in terms of when their defences will be penetrated, rather than if they will be.

They should also be more proactive in looking for breaches that may already have occurred: according to the latest Trustwave Global Security Report the average time from initial breach to detection was 210 days, more than 35 days longer than in 2011. Most victim organisations (64%) took over 90 days to detect the intrusion, while 5% took three or more years to identify the criminal activity.

"It is very difficult to detect a breach, and most victim organisations are not very good at self-detection," said John Yeo, director of Trustwave's SpiderLabs in the EMEA region.

For the same reason, the fact that the 400% increase in malware smartphone applications is largely directed at the phone owner doesn't mean that it hasn't already happened. "It is a bit of a paradox," said Yeo. "It is mostly targeted at the individual, for instance by setting up SMS reverse billing so that the user racks up a huge bill. We haven't yet seen mobile malware penetrating the enterprise, but that is not to say it hasn't happened, and we expect that we will see it sooner or later. Bring-your-own-device polices are becoming an issue, adding more potential entry points, so undoubtedly mobile will be an attack vector in the future."

The vast majority of the mobile malware detected in 2012 was directed at Android-based devices, but Yeo cautioned users of Apple's iOS devices not to be complacent. Most mobile app developers do not think in terms of security, and many of the Top 20 apps in Apple's AppStore contain control weaknesses that could be exploited by malicious code.

Mobile developers are not alone in failing to have basic security considerations in mind: "There is a tendency for security managers to focus on the front door," and not look at other points of entry, said Yeo. Web-based applications, for instance, greatly increase the number of points of weakness.

End users are notoriously poor – the most common end-user password is still "Password1" – but the user credentials compromised in most of Trustwave's investigations were administrator credentials, usually as a result of leaving default settings in place and failing to update to the latest versions of operating systems and applications.

The proliferation of networked systems means that attackers are increasingly adopting the tactic of using a compromised device as a "beachhead" from which they can mount reconnaissance attacks on connected systems – starting with the assumption that the connected system is on the same release version of the operating system and using the same defaults often pays off.

Where the money is

Not surprisingly, the primary data type targeted by attackers in 2012, as in 2011, was cardholder data that can be fed into the well-established underground market for stolen payment card data; it is bought and sold quickly for use in fraudulent transactions.

Because of their reliance on card payments, the retail (45%), food & beverage (24%) and hospitality (9%) sectors are the main victims of cybercriminals. This is not helped by a perception that they are not targets and they do not have a strong security focus, unlike banks and financial services firms who are naturally more security conscious.

In the financial services sector, there was a small increase in attacks, with attackers "continuing to look at central aggregation points like payment processors and merchant banks as viable targets". The Payment Card Industry Data Security Standard has made comprehensive security controls more commonplace in larger organisations, so they are more difficult to compromise. "This by no means indicates that attackers have given up on these high-dollar targets, simply that they are better defended, presenting a bigger challenge to would-be intruders," says the report.

Law enforcement agencies continue to struggle with the fact that cross-border prosecutions are difficult. Specific countries continue to appear on the list of sources of attack. In 2012 Romania topped the list, with 33.4% of attacks originating there, ahead of the 29% that originated in the US.

SpiderLabs is a "white hat" or "ethical hacking" group set up by Trustwave, which has a background in payments systems.

As well as services such as penetration testing to identify that can be exploited by hackers, it also has an incident response and forensics team that has investigated the largest and most high profile breaches in history.

"All of the data in the report comes from our real-world experience of actual attacks and breaches – this is not data from a survey of security manager's perceptions, it is what is actually happening out there," said Yeo. ***BT***

The changing face of payments

The Payments Council's latest report, *The Way We Pay*, shows rapid changes in use of payment methods over the past decade – but cash is still in the mix.

Despite the big shift away from notes and coins, Payments Council statistics show that, though decreasing in its use, cash is still very important in people's daily lives, and it "continues to hold its grip on frequent, low-value payments". It made up three out of five of one-off payments in 2011, of which 44% were between £1 and £5. The average value of a one-off cash transaction was £11.

There is some evidence that people are now using debit cards to pay for small transactions: Less than two thirds of payments in shops are made in cash (56%), compared to 75% in 2001.

Debit cards are currently making gains in sectors previously dominated by cash and are likely to take a greater share as contactless cards reach mass adoption. More than one in four (28%) of spontaneous transactions are made on a debit card (a rise of 59% over the last five years), with the average transaction size at £42 and falling.

Nearly three in five debit card purchases (56%) are between £10 and £50. 91% of all one-off cash transactions were under £25, so the contactless payment limit of £20 will allow many cash payments to potentially migrate onto cards. Debit card use is widespread across all ages and socio-economic groups.

Cheques account for just 1% of spontaneous transactions, but have an average value of £375, as they are more likely to be used for high value payments such as financial transfers. There is now a quite narrow demographic profile for cheque usage which reflects its diminishing status as a mass payment method. According to the Payments Council cheques tend to be favoured by "older people who are used to paying that way", the self-employed and families with children who have to pay for childcare and children's activities.

Among regular payments for household and other commitments like car insurance, mobile phones and donations to charity, direct debits and standing orders comprise three quarters of the total (76%) of which direct debits alone account for 66%. In 2001, cheques and cash accounted for 37% and direct debits only 50%.

Figures on overseas spending by UK citizens reveal some interesting changes in the changing patterns of use between cash, credit and debit cards

In total, spending abroad roughly doubled between 2000 and 2011 to £21.6 billion. As other countries increasingly accepted cards their use abroad exploded, almost tripling to 415 transactions between 2000 and 2011.

Even more dramatic was the expansion in the use of ATMs. Getting cash out of ATMs abroad increased by 130% between 2000 and 2008, when it peaked at £7.9 billion. This fell in each subsequent year to a total of £6.5 billion in 2011, in contrast to plastic card spending, which despite a fall in 2009 registered growth in 2010 and 2011. This is likely to have been driven by ever more widespread card acceptance abroad at hotels, restaurants and cafes, leaving travellers much less dependent on carrying foreign cash.

In 2001, debit card use abroad totalled £1.6 billion which was approximately 18% of credit card spending abroad. The growth in debit card ownership in the UK, coupled with wider acceptance of UK cards in foreign locations has driven some of the switch from credit card to debit card , with spending in 2011 amounting to £9.3 billion which was approximately 75% of credit card spending.

> *"The 2010s are likely to be the decade of the mobile phone. Just as we can't imagine how we ever did without the internet, many people will soon wonder how we used to be so dependent on cash and cheque*
>
> **Adrian Kamellard,** the Payments Council

"As in the UK, the traditional ways we pay abroad are falling by the wayside," says the report. "In the next 10 years it will be interesting to see whether other countries adopt contactless technology and develop the same mobile payment technologies as the UK."

"We scarcely notice the steady changes in the way we pay, yet someone in their thirties today will see more change in their lifetime than in the entire history of money. Even recent innovations such as payment via a mobile phone, which ten years ago some felt to be science fiction, will soon be commonplace," said Adrian Kamellard, chief executive of the Payments Council. "The 2000s were the decade of the debit card. The 2010s are likely to be the decade of the mobile phone. Just as we can't imagine how we ever did without the internet, many people will soon wonder how we used to be so dependent on cash and cheque. Twenty years from now even cards may seem archaic. It's easy to imagine a future where we merely pat our pockets for our keys and phone. The wallet could become a historical curiosity." ***BT***

New players on the world stage

Exchanges in emerging markets stole the show at a recent event in London, but the incumbent European exchanges still enjoy unfair advantages, delegates said. *Elliott Holley* reports

Emerging markets including Brazil, India and Turkey took the spotlight at the World Exchange Congress event in London last month, as senior executives highlighted rising technological investment, growing competition and successful index performance.

"In 2012, foreign investors opened 4,000 new accounts with us," said Sergio Gullo, chief EU representative at Brazilian exchange BM&F Bovespa. "The previous year, we saw 7,000 new foreign participants. Some 40% of equities trading and 26% of derivatives trading in Brazil now comes from foreign investors. In the last 12 months, many of these are coming from Europe."

Brazil has long been favoured by the electronic trading community. Since 2010, every major global bank has launched electronic trading tools in the country, including direct market access and algorithms. Global technology and connectivity companies such as SunGard and Fidessa have been falling over themselves to establish a presence in Brazil, while the BM&F Bovespa exchange has installed co-location technology to reduce latency, formed an alliance with US derivatives giant CME Group, and is currently rolling out Puma, its new high-tech trading platform. Brazil's exchange is also collaborating with its BRICS partners, especially the Chinese exchanges in Shanghai and Shenzhen, to encourage more Chinese to invest in Brazil and to develop cross-listed products.

The success of the country has also generated interest from new participants, including Americas Trading Group, which is planning to open Brasil ATS, an alternative trading venue in the country later this year, and BATS Global Markets. But according to Gullo, there is still more work to be done.

"If you look at size of Brazilian economy and the number of listed companies, you can see there's big room for improvement," he said. "We've been working with banks to travel round the world, visiting important markets such as England, Spain, Poland, Korea and the US and drawing on their experience to help us attract companies to list on exchange."

Meanwhile in India, the launch of new contender MCX-SX in Mumbai in equities and equity derivatives this week drew attention from Hirander Misra, board advisor at India's Ahmedabad Stock Exchange, who pointed out that recent moves by the Securities Board of India were creating new opportunities. At the end of January, SEBI mandated the debt market to move on-exchange; earlier, it also decreed that small regional exchanges across India must either provide a minimum level of liquidity or lose their licence – a move that should help concentrate liquidity on the main venues.

The other main bourses in India are the National Stock Exchange and the Bombay Stock Exchange, which largely focus on equities and derivatives respectively. SEBI has made other reforms in the last 18 months, including permitting smart order routing, which should help to draw in investors. However, there are still some anomalies in post-trade practices, according to Misra.

"In India, you can't cross margin between trades on different venues even if they are using the same CCP," he said. "That's strange because it means you can't use collateral efficiently, and ultimately the clearing members are paying for that. It's down to a siloed exchange model, and that could be improved."

Turkey also drew praise from delegates. Robert Barnes, chief executive at UBS MTF, told *Banking Technology* that the Istanbul Stock Exchange's national 100 index was one of the top performing exchange indexes in the world last year. Turkey's attainment of advanced emerging market status on the FTSE index in 2011 also placed Istanbul

ahead of Moscow in the race to become an international financial centre, Barnes added.

Turkey has become increasingly welcoming to international investors in recent years.

Lured by the domestic market capitalisation of €215 billion reported on the Istanbul Stock Exchange, and by an IPO pipeline that saw €422 billion in new capital enter the market last year, western capital markets companies have been quick to pick up on the opportunities presented by Turkish modernisation and economic growth.

Solid macroeconomic performance has helped – Turkey is currently the seventh-largest economy in Europe – while reforms to the country's Capital Markets Law in July 2012 saw Turkey adopt the same legal definitions of financial instruments and other terms as used by the European Union in its MiFID directive.

Further refinements, such as a rule change in late 2010 that effectively unlocked the door to algorithmic trading in the country, have prompted large banks including Citi to release advanced trading products including algorithmic and direct market access offerings in the country.

Barnes is currently chair of the Turkey Advisory Group, an initiative that aims to build closer business links between the UK and Turkey. As part of its efforts in this direction, the group plans to send a delegation to Ankara on 18 March including the Lord Mayor of London.

Not a level playing field

While emerging markets players are rising in the rankings, senior market participants expressed outrage that incumbent exchanges continue to charge high fees for market data, while MTFs still lack the means to compete on auctions and are not represented on international indices.

"Exchange and MTF competition doesn't really exist," Olof Neiglick, chief executive at Nordic MTF Burgundy told delegates at the congress in London. "Institutional investors want to use the opening auction. But as long as auctions can only take place on exchange, the customer has to take the incumbent prices. That annoys a lot of people more and more. The market isn't working and it really isn't good enough."

Regulation that maintains the stock exchange as the only entity allowed to hold a closing auction has long been a bone of contention between exchanges and MTFs. As early as 2011, Alasdair Haynes, former chief executive at Chi-X Europe, spoke out forcefully for the right of MTFs to hold auctions of their own. Yet as equity market flows have deteriorated, the issue has become even more charged. Barnes pointed out that the value traded in the closing auction has grown to around 20% of daily volume in Europe, reaching as high as 50% on some days.

The European Commission's MiFID legislation promised in theory to open up securities markets to competition and improve transparency.

But nearly six years after the original directive, there are still some serious gaps. The questions of who should provide market data, how it should be distributed and how much users should expect to pay have also been fiercely debated.

Some observers content that MiFID has essentially failed, because exchanges typically charge significant fees for market data while no single tool exists to provide an affordable consolidated tape of post-trade data to offset the fragmentation of liquidity caused by competition.

"The London Stock Exchange has seen a 43% rise in market data revenue since MiFID," said Jerry Avenell, co-head of sales at BATS Chi-X Europe. "The exchanges aren't going to give up that revenue stream unless the regulators force them to do something about it. We need the regulators to step up and get involved."

Other market participants concurred. "Market data is a €1 billion revenue stream pan-Europe," said Neiglick. "It's not going to move itself. In the Nordic countries, exchanges lobbied hard not to allow market data on users screens, but we made Nordic light, a 'poor-man's consolidated tape' for retail investors. Not everyone can afford a $3,000 a month Bloomberg terminal."

BATS Chi-X Europe began charging for market data at the end of 2012. ***BT***

Finovate Europe lets in Old Guard

Not for the first time, a sense of *déjà vu* pervaded Finovate Europe last month, reports *David Bannister*

For an event that is based around the idea of introducing newcomers and new concepts to the financial technology world, this year's Finovate Europe was heavy on familiar faces and some increasingly familiar concepts.

Personal financial management tools remain popular, social media and networking are still to the fore, and mobile is an absolute must – either in the form of mobile point-of-sale devices or person-to-person money transfer services.

While one set of presenters espoused the "Banks are Dead" line, on the other side several banks were actually taking part – Credit Agricole even made the list of winners – while the vendor line-up featured names that you could expect to see at a mainstream event.

Temenos, for instance, was on early on the first day with its LiveDesigner user interface tool. Looking around the exhibition floor, other familiar names could be seen among the logos – Akamai, BBVA, Fiserv, NICE, TSYS and Sage among them.

Still in the minority, certainly, but probably balanced by the number of others whose concepts are too similar to their peers, or to the better funded. Using QR codes on invoices to pay bills? Nice idea – as used in Barclays Pingit for corporates, of course, so good luck …

Temenos got a largely positive reaction from the audience for LiveDesigner, a dynamic user interface designer that allows customers to edit and review web pages while an application is actually running.

LiveDesigner is part of the EdgeConnect user experience platform that underpins its approach to channel management. EdgeConnect was launched to enable customers to develop once and deploy many times across different channels and devices. LiveDesigner takes this to the next level with changes to the UI made just once, and automatically propagated across all channels.

Alex Kwiatkowski, research manager, IDC Financial Insights, comments: "When creating a dynamic user experience you have to have consistency across channel, experience, and brand, and that is the part which is missing at the moment – all the good work that has been invested in a silo mentality has reached a point whereby institutions are saying 'we must embrace these technologies holistically'. At present, the infrastructure of financial institutions still feels disjointed and not seamless which is creating a headache for a lot of people."

As it happens, channel management for existing banks was the basis of one of the Best of Show entries, the Lithuania-based Etronika, which was showing its Banktron e-channels management platform, due for launch in the second quarter of this year.

The buzz around the event remains, though the audience has also started moving towards the mainstream, with many familiar faces from the banking systems world walking around the Old Billingsgate venue.

Finovate continues to offer a forum for the new, but it is increasingly becoming mainstream both in terms of its content and its audience. A telling remark came during the London event when a well-known payments systems consultant tweeted: "Another PFM – how very 2011 …" The same person had tweeted about the plethora of PFM offerings during the 2011 event.

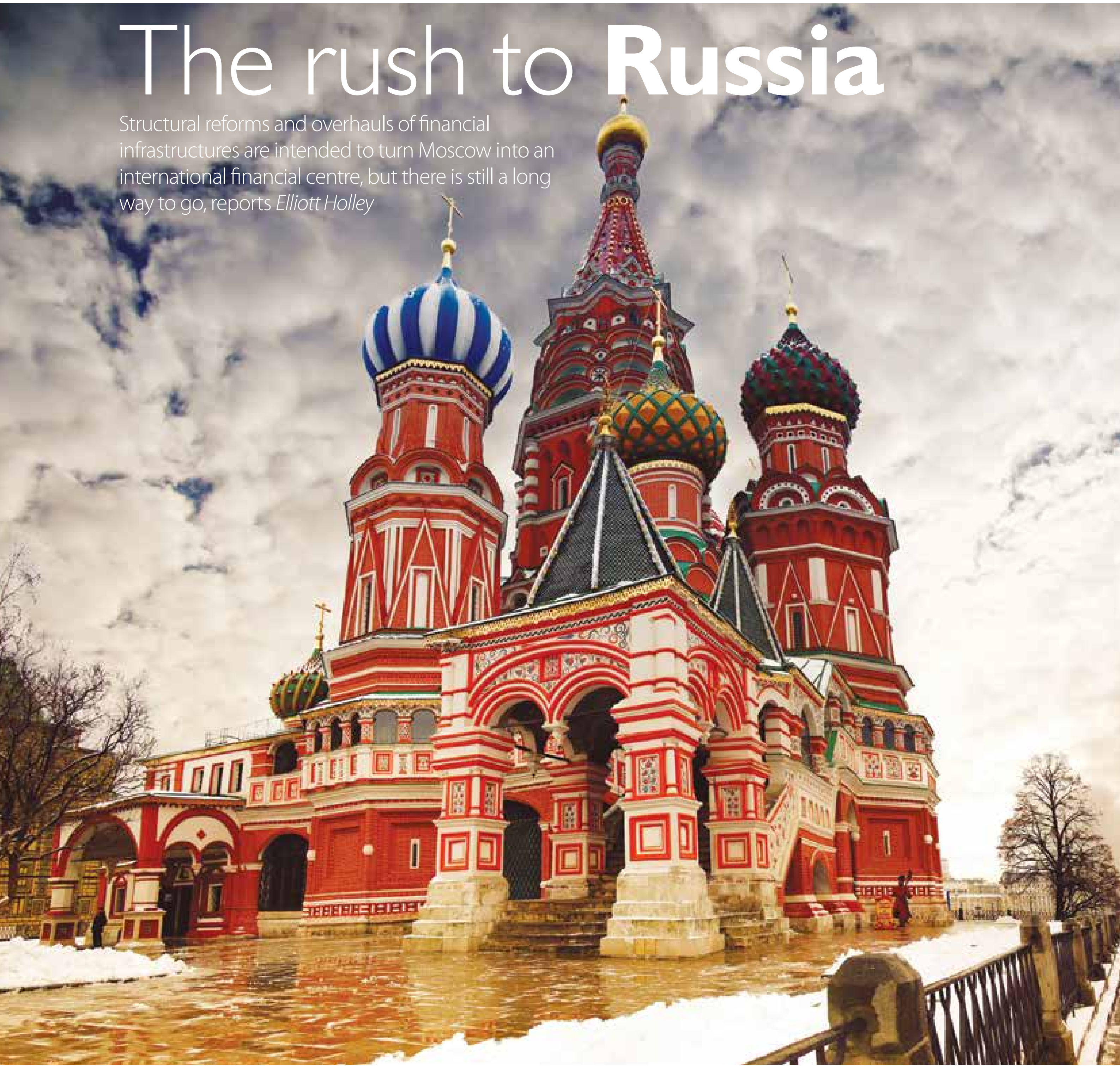
With the emergence of newer innovation initiatives such as the Accenture-backed FinTech Innovation Labs in London and New York, and the Innotribe Foundation from Swift, Finovate will have to look to its laurels. ***BT***

Finovate Europe 2013: listing of show winners

- **Credit Agricole:** the CA Store gives customers access to unique apps including social media and games. External developers are encouraged to contribute through financial incentives.
- **Etronika:** the Banktron e-channel management platform manages personalisation of online banking across channels and devices.
- mBank and Efigence: last year the internet-only mBank became Poland's third largest retail bank. It is now adding Facebook & social networking platform
- **Meniga:** a white-label personal financial management platform designed for European banks that can be integrated with online banking systems.
- **Moven:** the worldwide launch of the mobile bank formerly known as Movenbank. Brett King, author of Bank 2.0 and driving force behind Moven, used the event to launch the mobile-optimised bank, which is in beta release.
- **Pockets United:** a group purchasing mobile service that lets people split costs among themselves using a mobile app.
- **SumUp:** a mobile point-of-sale system
- **Virtual Piggy:** a payment system that allows parents to set up a monthly allowance for their children, who can then make payment savings and other money management decisions. It recently teamed with WorldPay to provide a global capability.

The rush to **Russia**

Structural reforms and overhauls of financial infrastructures are intended to turn Moscow into an international financial centre, but there is still a long way to go, reports *Elliott Holley*



A determined push by the Russian government to open up the country's capital markets and make Moscow an international financial centre is gradually gaining ground. But the Moscow Exchange faces a fierce fight as it attempts to claw back Russian listings business from the London Stock Exchange's hugely successful international order book.

Russia is the world's seventh biggest economy, according to statistics provided by Russian broker Otkritie. The country's obvious attraction is its energy market, including oil and gas, which have contributed to massive Russian companies such as Rosneft and Gazprom. With a population of 142 million, Russia is a major European market that spans the bridge between the European and Asian timezones.

In November, one major obstacle to foreign investment was removed when

Russia established a central securities depository, NSD. Under US Securities and Exchange Commission rule 17F7, US investors have to place assets with a depository. Without a CSD, settlement arrangements for Russia were widely viewed by outsiders as complicated, expensive and inefficient. A CSD provides transparency over securities ownership and can help reduce risk in the event of a bad trade.

Equally important for the future is the planned switch of the entire Russian market to T+2 settlement later this year. At present, Russia operates a T+0 settlement cycle, which means that trades settle immediately at the point of the transaction. This system is a major obstacle to many foreign investors, because the seller must be able to pay at the moment of the transaction. Most of Europe uses T+3 settlement, with the exception of Germany, which operates on a T+2 basis. But the Moscow Exchange is due to move 20 of the most liquid stocks from its MICEX order book to T+2 settlement in March, with the remainder due to follow by the end of July.

"Our task is to make the Russian stock market competitive in the full sense of the word, make it attractive for Russian and foreign market players"

Vladimir Putin, president of Russia

"Everyone is looking at Moscow," said Emmanuel Carjat, chief executive at TMX Atrium, the market data and connectivity business of Canada's TMX exchange group. "The spectrum of interested parties ranges all the way from long-only investment managers to high-frequency traders."

TMX Atrium launched a new low-latency link from Frankfurt to Moscow in January, clearly aimed at capitalising interest on western investors in accessing the Russian market.

Tug of war

However, there are also problems. At the Moscow Exchange, there has only been one IPO in Russia in the two years between January 2011 and January 2013, according to figures provided by PricewaterhouseCoopers. Over the same period, there were 14 Russian IPOs in total – of which eight were on the LSE. Most of the 46 Russian companies listed at the LSE use global depository receipts, but there is a select group of eight that have opted for a premium listing. Dual-listings both in Russia and in London are also very popular. The IOB also lists 10 companies from Kazakhstan, six from Ukraine, two from Georgia and one from Turkmenistan; the top most traded stock on the LSE is now Russian energy giant Gazprom. Russia's political leaders have been quick to comment on the need to reform the country's domestic market to attract more listings business.

"This is a sign that Russian companies are forced to go abroad to look for money to finance their development," admitted Vladimir Putin, president of Russia during a speech on financial markets on 25 January. "This is sad. We have taken a number of measures to improve the financial infrastructure of late. Our task is to make the Russian stock market competitive in the full sense of the word, make it attractive for Russian and foreign market players. It has to meet business' demands and also be up to our new and more ambitious economic development goals."

On 15 February, Moscow Exchange launched its own IPO on the Moscow market as the spearhead of that effort to encourage Russian companies to list on their own market. The IPO raised approximately $500 million and brought the company a valuation of $4.2 billion. But domestic liquidity is limited, with only 1.5 million out of a total population of 142 million participating in the stock market, according to Otkritie figures. Russia's relatively small pension market has been contrasted with other former Soviet-bloc countries such as Poland, which enacted a compulsory contribution pension system in the 1990s that ostensibly covers all of its 38.5 million inhabitants, creating a far larger domestic fund market. By comparison, pensions account for just 4% of Russian GDP.

Furthermore, the IPO only represented the sale of a minority stake in the Moscow Exchange – around 10%, according to Berenberg Bank. Since some of the major buyers were Chinese and Russian sovereign funds, the transaction could be seen as one branch of government buying another, according to Pras Jeyanandhan, analyst at Barenberg. Meanwhile, Berenberg's research indicates that the exchange is earning around 80% of its profits from high-margin interest income – leaving Moscow Exchange "looking more like a bank" than an exchange.

"Moscow collects deposits from clients to clear and settle," said Jeyanandhan. "These balances have been increasing. The exchange provides treasury services, then puts those resources in the market and earns interest. Recently, they've added more risk to the equation by buying corporate funds. All that revenue goes straight to the exchange's bottom line – no other exchange earns so much from this source. But as T+ settlement is coming, we would expect that revenue stream to decrease in future."

To help draw in foreign investors and drive up liquidity, the Moscow Exchange has upgraded its matching engine and capacity. According to Russian broker BCS, it is providing much more granular information and much better co-location, hosting and networking facilities than it used to. The company currently has 120,000 retail clients on its books, but its figures also show that the Russian equity market is still registering average trading volumes below $1 billion per day – well below the $8 billion recorded for derivatives contracts and $14 billion for FX transactions.

The lack of an institutional market in Russian equities has been highlighted by BCS as one of the main challenges for the Moscow Exchange, whose domestic clients primarily consist of retail investors. The need for pension reforms in Russia to increase domestic flows has also been identified by Moscow's rival the London Stock Exchange as a key necessary step if Russia is to expand Moscow's appeal as an investment centre.

"You need a strong domestic market to attract international investors," said Jon Edwards, deputy head of primary markets – emerging markets at the LSE. Edwards is personally responsible for developing the London Stock Exchange's business in Russia and the CIS, a group of countries closely associated to Russia that includes Belarus, Kazakhstan and 7 other post-Soviet states. "It has been estimated that pension reforms could inject as much as $34 billion of funds into the Russian equity market. That reform is much-needed."

Russia's payment systems under scrutiny

With the outgoing head of Russia's central bank saying that $49 billion – around 2.5% of GDP – was illegally paid out of the country last year by an organised crime group, the suspicion with which the whole of the country's banking system is viewed by outsiders might seem to have some justification.

Like so much else in the country, the payments system is undergoing considerable modernisation, with new legislation – the National Payment System Law – covering the infrastructure brought in 2011 and introduced in stages, ending in September last year.

NPS "is intended to ensure the legal regulation of modern payment and settlement services, which have emerged as a result of the nation's technological and informational development," according to the Kremlin.

It establishes legal and organisational foundations for a national payment system, regulates the procedures for rendering payment services, and determines the requirements to the organisation and operation of payment systems, as well as procedures for supervising and monitoring the national payment system.

Under the law, all payment service operators have to be licenced by the central bank (it also monitors all payments, which is where the $49 billion figure came from).

The law will cover the creation of a national payment system and the issuing of a single identity and payment card to all Russian citizens that enable them to receive social security and pension payments, as well as to pay taxes and purchase products in ordinary shops.

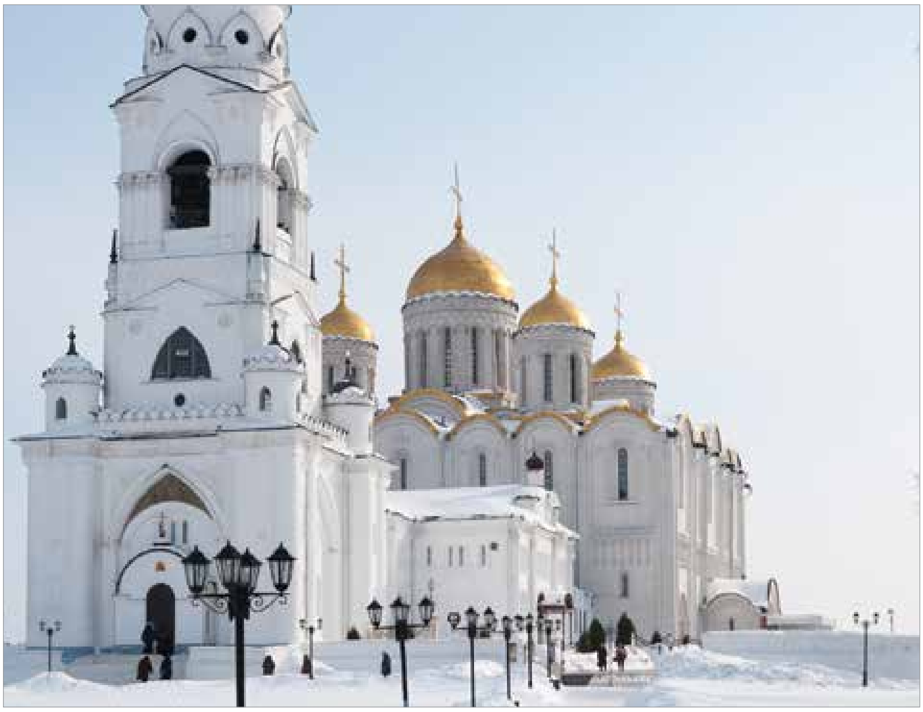
The NPS principally addresses new forms of payment that existing legislation didn't cover, particularly electronic forms and – after amendment – mobile payments.

One of the central aspects of the new law was the introduction of multilateral netting, and changes to the rules relating to bankruptcy to protect the system against failure of a participant.

More problematic for international players, the NPS also brought in restrictions on cross-border payments – "The Federal Law defines the procedures and features for conducting electronic monetary transfers, including a payment system operator's right to involve operating centres located outside of Russia for granting operational services to payment system participants," says the Kremlin.

Originally it was intended to force international operators like Visa and MasterCard to become local players, with in-country processing centres, but this was later amended.

Payment card penetration in Russia is actually relatively low, at only 5%. According to the Central Bank of Russia, retail payments account for only 10% of card transactions, the remaining 90% being cash. Traditionally a totally cash-based society, Russia's transition to cashless payments is very slow, especially outside of large cities.



Taking stock

Other perennial issues that concern long-term investors in Russia include the rules around corporate governance, treatment of minority investors and the strength of law. In the US, many mutual funds hold stock via trusts, which are not recognised under Russian law. Some market observers note that while the Russian market's planned move to T+ settlement later this year should appeal to the tier one banks, that will not solve the core comfort issues for the buy-side.

"It's not always the changes that get the headlines that count," said Tim Bevan, director of prime services sales at BCS. "Recent changes in corporate actions law are also especially relevant. But let's not kid ourselves – corruption is still rife at every level of economic activity in Russia. This is not a one-year or 18 month project. We are talking about fundamental, in-the-DNA changes. It will take at least five years."

According to Edwards, part of the problem is that institutional investors from abroad need a mandate to invest in Russia, which many funds do not currently have. To trade in Russia, a company needs to be a Russian entity. All the major global banks have Moscow-registered entities that enable them to meet that requirement, but smaller brokers may not. That leaves them no alternative but to buy depository receipts in London. "The listing rules in Russia need to be more aligned with international best practice, and there needs to be more English language disclosure to attract foreign investors," he said.

"This is not a one-year or 18 month project. We are talking about fundamental, in-the-DNA changes. It will take at least five years."

Tim Bevan, BCS

Not everything is black for the Moscow Exchange, however. Bevan notes that much of the flow on the Moscow Exchange and the LSE's IOB is actually arbitrage between the two – so the competition over business need not necessarily be seen as a "nihilistic one-horse race". Furthermore, although the Moscow Exchange's habit of setting aggressive deadlines and then missing them has damaged its credibility in some circles, the admission of Russian OFZ government bonds in February 2013 and equities next year into the Euroclear system should make a positive difference for investors. The OFZ bond market is worth $100 billion, according to figures provided by Baring Asset Management. Other observers were more bombastic in their predictions.

"The 7 February milestone marks a new era in the ability of Russia to fund its growth and development through the international capital markets," said Frederic Hannequart, chairman of Euroclear Bank. "Industry experts are predicting new foreign capital inflows to Russia in the region of $20 billion. Euroclear Bank is proud to become part of the new Russian financial centre by making OFZs eligible for Euroclear Bank services."

Investor rights

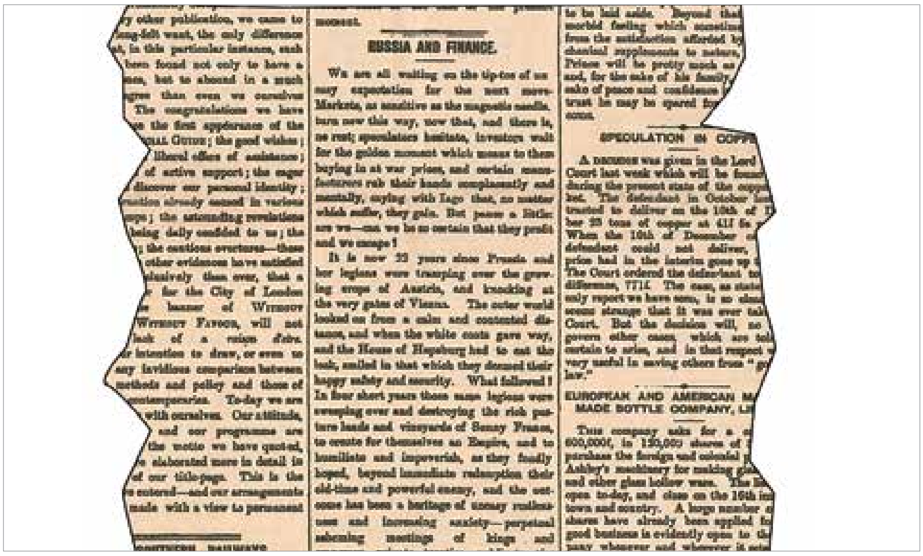
But besides the details and practicalities of investing in equities and other asset classes, there is another issue. Corruption and allegations of government complicity in human rights abuses inevitably tarnish the image of Russia as a viable location for an international financial centre. Undoubtedly, there are sections of the government that are trying hard to improve Russia's image.

"The international financial centre [Moscow] will be used to attract and allocate Russian and foreign investment capital," said Dmitry Medvedev, prime minister of Russia in a speech in February. "We'll have to create an effective and stable regulatory environment, which will encourage the creation and development of modern financial products and services for all investors, and which will ensure high standards of corporate governance and, of course, the protection of investor property rights and interests."

At the same time, however, those efforts are undermined by cases such as lawyer Sergei Magnitsky, who was arrested after he alleged that Russian officials were implicated in a tax fraud scheme. Magnitsky was held for one year on fabricated charges before being beaten to death, according to Russia's Presidential Council for the Development of Civil society and Human Rights.

"The cases of former Yukos chief Mikhail Khodorkovskyand his colleagues Platon Lebedev, Vasily Aleksanyan, Svetlana Bakhmina and others awakened the world to Russian justice under Putin," said Bruce Misamore, former chief financial officer of Yukos in a letter published in the *Moscow Times* earlier this month. "Magnitsky and the corruption exhibited by the Russian administration in everything associated with that case are indicative of complete lack of a rule of law."

Yukos had its assets frozen by the Russian government in 2003 following a tax reassessment which claimed that the company owed $27 billion. In 2006, the company was declared bankrupt. The company's assets were subsequently bought up at low prices by government-owned companies; former owner Khordokvsky was arrested and imprisoned. The Parliamentary Assembly of the Council of Europe condemned these actions as manufactured for political reasons and a violation of human rights. It is also alleged that Svetlana Bakhmina was effectively the victim of a political vendetta against Yukos and its employees. Bakhmina served three years in harsh prison conditions where she was denied contact with her young children; colleague Vasily Aleksanyan was also imprisoned until forcibly released following a decision by the European Court of Human Rights, which found Russia in violation of four articles of the European Convention on Human Rights. Aleksanyan died later the same year, at the age of 39. Khordokovsky is still in prison. ***BT***



moment.

RUSSIA AND FINANCE.

We are all waiting on the tip-toe of uneasy expectation for the next move. Markets, as sensitive as the magnetic needle, turn now this way, now that, and there is no rest; speculators hesitate, investors wait for the golden moment which means to them buying in at war prices, and certain manufacturers rub their hands complacently and mentally, saying with Iago that, no matter which suffer, they gain. But pause a little: are we—can we be so certain that they profit and we escape?

It is now 22 years since Prussia and her legions were tramping over the growing crops of Austria, and knocking at the very gates of Vienna. The outer world looked on from a calm and contented distance, and when the white coats gave way, and the House of Hapsburg had to eat the leek, smiled in that which they deemed their happy safety and security. What followed? In four short years those same legions were sweeping over and destroying the rich pasture lands and vineyards of Sunny France, to create for themselves an Empire, and to humiliate and impoverish, as they fondly hoped, beyond immediate redemption their old-time and powerful enemy, and the outcome has been a heritage of uneasy restlessness and increasing anxiety—perpetual scheming meetings of kings and

The markets have been watching Russia for a long time – as the first ever issue of the Financial Times reported in 1888

Banking at a crossroads

While foreign-owned banks face challenges entering the Russian markets, the local players are engaged on aggressive expansion strategies, both internally and in neighbouring Central & Eastern European countries, where they are starting to take share from Westerners.

Western European banking groups lost some market share in Russia in 2011, according to study from Raiffeisen Research, which it says can be largely attributed to the strong performance of locally owned players and/or larger state-owned banks such as Sberbank and VTB. It is also the case that banks like Sberbank and VTB have a strong deposit funding base in the retail and/or corporate segment, a position that helps them to outpace the overall market average in times of scarcer funding.

In the specific case of Russia, some mid-sized locally-owned banks like Alfa Bank and Nomos Bank have also expanded much more strongly than most of their Western European peers, says Raiffeisen

The foreign-owned players among Russia's Top50 banks were expanding rapidly until 2008, when their market share peaked at 10.7% and has declined since then, says the report, but adds that this ought to be treated with a degree of caution. "The largest portion of the pre-crisis growth posted by foreign-owned banks took place via acquisitions and most of the acquired banks were rapidly growing loan books prior to the change of control; as a consequence, the figure was inflated somewhat," it says.

Raiffeisen is one of the three large foreign-owned banks in Russia, along with Société Génerale and UniCredit, all of which are "firmly maintaining their position within the Top 10".

In its 2012 report, *A Chessboard Strategy for Russia's Banking Market*, AT Kearney says that the market can be described in two words: "consolidation and adrenalin".

According to AT Kearney, the Russian banking industry will have grown 16% between 2009 and 2015, and while this is a slowdown compared to the 27% CAGR reported from 2005 to 2010, there is more room for growth.

"Over the past six years, consolidation has resulted in some 300 banks being taken over by large state-owned or international institutions," the report's authors note. "But there's also a kind of frenetic, thrill-seeker side to the Russian banking market, most apparent in very little transparency, lots of governmental involvement, fluid regulatory environment and capital flight. In short, this is not a market for the timid – it is dynamic and changing rapidly. Banks seeking success in Russia need not only a well-thought out game plan, but also the flexibility to adapt to unforeseen events."

That said, it goes on to foresee two potential futures: "continuing domination by state-owned banks with minor banks playing a minor role; or dominance by many large state-owned and private banks, with niche and smaller banks making up a second level".

Which of these futures plays out will largely depend on the approach of the Russian Government, it concludes.

Still a need for Kremlin-watching, then.

Mixing up the pieces

The introduction of a seven-day account switching service in the autumn is meant to increase competition among UK High Street banks. Will it succeed, asks *David Bannister*

Back in the 1980s, the late Douglas Adams, author of The Hitchhiker's Guide to The Galaxy, collaborated on a computer game, the object of which was to get a bank to acknowledge a change of address.

The frustrations of dealing with bureaucracies since then have worsened, and in an increasingly digital world, are only likely to continue in that direction.

So the UK government is probably to be applauded for trying to simplify one aspect of modern life: changing your bank. As of September this year, UK retail banks will be required to offer a seven-day account switching service.

Currently, according to the Payments Council, which is in the driving seat for the initiative, the "best time" for successfully switching between banks is 18 days.

Essentially, from September a consumer who wants to move bank for some reason or another, will select a new bank, which will give them details of the new account that they can give to their existing bank. Seven days later, all of their accounts, standing orders, direct debits, and suchlike, are up and running at the new bank without any interruption.

There are some obvious pitfalls: what happens to incoming payments to the old bank account? For how long do they have to forward such things – in other words, how much data on a former customer should they be keeping? What are the data protection implications?

To take a concrete example, if a person receives a regular annual payment – a pension, company dividend or royalty cheque for sales of their computer games, for instance – at what point does the former bank stop having responsibility for passing on the money? The recipient may even have forgotten about the payment.

There are less obvious pitfalls, one of which is that anti-bank groups could organise flash mob-style groups, creating (potentially) disruptive spikes of activity and generally being a nuisance. (And while it might be some fun to mess around with a big bank, what if they all decide to move to a small building society, for instance? Innocent bystanders could suffer …)

More importantly will the change actually do what it was intended to do? Simplifying the lives of consumers by removing bureaucracy is only a side benefit: the *point* is to increase competition among the UK's High Street banks.

The signs are not that good. Some banks are clearly going to make a play to encourage customers away from rival banks – some are already, with Nationwide advertising its mutual status, and the newcomers Metro and Virgin Money promoting their services. Once the service comes online we can expect to see more of this sort of competition.

Whether it will make any real difference is a moot point, suggests a recent study, Simon-Kucher & Partners, a strategy, pricing and marketing consultancy, asked current account holders which brands they would consider moving their current account to. They found that while more than one third (37%) would consider switching to a 'challenger' brand as a result of seven-day switching, the vast majority – 73% – would consider moving to one of the established Top 5 banking brands.

In other words, although the study found customers showing strong interest in the challenger brands and mutuals, the big banking brands will maintain their dominance

Among the challenger bank brands Virgin Money is most popular, despite having just over 70 UK branches since acquiring Northern Rock's estate. Supermarket brands also proved popular. The top four brands that would attract current account customers are:

- Virgin Money
- Tesco Bank
- M&S Money
- Sainsbury's Bank

According to the study, The Co-operative Bank, Nationwide and HSBC are set to become net beneficiaries once the Seven-Day Switching service goes live and switching rates increase. It is these brands that have the greatest relative appeal compared with their current market shares. Previous research from Simon-Kucher estimated that nearly half of UK current account holders are likely to consider moving bank, and realised switching rates likely to grow to 6-12% (*see panel*).

Ben Snowman, director and study author said: "The dominance of the Big 5 is set to be challenged by more competition on the high street and the greater ease and speed of switching. Whether their dominance is simply dented or substantially reduced, remains to be seen."

The seven-day switching service should perhaps be seen in the context of wider changes that are being made post-crisis, and in the wake of taxpayer bail-outs of banks. UK Chancellor George Osborne has talked of a wider opening of the UK payment infrastructure, though without any detail, and the Payments Council is possibly to be replaced by another body – perhaps with statutory powers, but certainly less bank-friendly in the eyes of politicians and the popular press.

"We agree with the Chancellor that 'payments systems sit at the heart of the banking system'", said Adrian Kamellard, chief executive of the Payments Council. "I am determined that the Payments Council will continue to deliver positive change for the benefit of customers. We recognise the critical need for continuing innovation and vibrant competition, including easy access to payment systems for new entrants. This is why we are focusing on developing a payments strategy that meets the needs of customers, the economy as a whole and satisfies any new regulatory requirements. Examples of what a good strategy can deliver include our new account switching service and mobile payments service."

Kamellard said that the new service "will make switching accounts simpler, faster, hassle-free and will be backed by a cast-iron customer guarantee". The Payments Council will also be running a national TV advertising campaign to make sure everyone is aware of the change. "We are confident this will increase competition in the market for new and existing current account providers and increase customers' confidence in the switching process."

The hypothetical changes foreseen by Osborne and others are not without dangers, say observers. "Banks payments are an essential service, like electricity or telecommunications. We take them for granted but the impact is immediate when things go wrong," said Stephen Ley, partner in banking and payments risk services at Deloitte. "Innovation in the highly-connected banking and payments world takes time because of the scale and expense of any change and the extreme penalties for getting it wrong. Despite these obstacles, the market is changing fast. 2014 will see the launch of m-payments across the UK which, combined with the UK's leading Faster Payment service, will enable payment to be sent via a mobile number in near real time 24-hours a day 365 days a year. The new payments regulator will need to carefully balance the desire for more competition and innovation with consumers' needs for resilience, reliability and security." ***BT***

Loyalty at a price

Almost half – 49% – of UK current account holders are likely to consider switching their account as a result of the seven day switching regulation coming into force in September.

Realised switching rates are likely to grow from a current level of between 2.5% and 5% to between 6% and 12% as a result of perceived benefits, according to a study by Simon-Kucher & Partners, a consulting firm specialising in pricing and marketing

The study questioned over 1,000 current account holders, finding that the number of participants likely to consider switching their current account increased from 19% to 49% due to the benefits arising from seven day switching. The main reasons why they are more likely to switch include:

- Speed and simplicity (83%)
- Assurance of accurate migration of direct debits and receipt of salary payments (83%)
- Ease of trying another bank (73%)

The good news for banks is that the survey suggests they can stem switching rates by incentivising current account holders to stay. Current account holders will respond to the right incentives.

Online banking is the main feature that attracts current account holders when looking for a new bank when deciding to switch, followed by the ability to transfer all regular payments. Introductory bonuses for switching are also a highly popular feature. This is currently being promoted by banks; First Direct now offers £100 to new current account customers.

The main incentives cited by the survey respondents were:

- One-off gift up to £100
- A better interest rate on savings account
- A better interest rate on current account balance

These incentives would serve to retain 86% of those who would consider switching their current account.

"Banks need to develop propositions to retain current account holders as there will be an increase in switching rates," said Jens Baumgarten, banking partner of Simon Kucher. "There are opportunities for banks to understand the price of loyalty in order to retain these customers and protect their market shares."

SEPA Uncertainty

Big banks and their large corporate clients are in the final stages of preparation for the SEPA end date of February next year, but what about the smaller clients in the non-euro countries? *David Bannister* reports

At the top end of the banking and corporate pile, SEPA-readiness is almost a given, and for some has been for a while. Further down among the medium-sized corporates, however, things are less clear.

To try to gain some clarity on the situation, payment systems consultant Peter Miller recently carried out a survey, asking some basic questions, (with the collaboration of Neil Burton, director of product strategy at Earthport.)

The main conclusion was stark: corporates are being provided with little basis upon which to judge whether SEPA provides them with an opportunity to improve their cash management or whether it simply represents another compliance matter.

Miller says that this is important for a number of reasons: it determines the method and the urgency with which they address the issue and initiate the necessary projects and budgets. "Education of the private sector on the effects of imposing new law, apparently aimed at banks, is required, whether this is offered by trade bodies, the UK Payments Council or by government itself," he said.

The survey was intended to be "a quick and informal study of opinion surrounding the implementation of SEPA for UK customers … it is a narrow national view, intended to discover the extent to which the UK industry as a whole is aware of the issues".

The study was conducted over a two week period in Jan 2013, during which 40 experienced practitioners, bankers, suppliers, consultants and industry commentators were asked to respond, by email, to a survey.

The questions were not aimed at singling out technical fact, but were aimed at bringing out the high –level issues. If the quantity of responses received was mildly disappointing, their quality and depth were not.

The questions were set against the certainty that the end date regulation for SEPA is now set.

- Countries in the Eurozone will have to cut over all existing direct credits and direct debits in euro to new instruments which comply with the end-date regulation and the Payment Services Directive – February 2014. This means that all "heritage" instruments will be replaced by the SEPA Direct Credit and the SEPA Direct Debit managed by the European Payments Council, as there is today no alternative which complies with the PSD and the SEPA end-date regulation.
- Other non-euro EU countries making payments in euro will have longer to comply with the same requirement – by the end of October 2016.

Ad hoc discussion suggested that there is uncertainty as to the commercial, rather than functional, impact of SEPA on UK firms; and that the scale of the impact might be considerable. In the face of this we asked five questions, which are questions for the UK payment industry, but which might equally be posed in other euro-out countries.

The responses elicited comments beyond straight answers (*see panel*), providing a useful snapshot.

The most significant practical obstacle to be overcome is for corporates with multiple transactions/high volumes. Typically, these will be sent from the corporate in files. The design of SEPA (its "four corners") assume that it is the sender's responsibility to ensure the quality of data within the files, that they will be sent in XML format (ISO 20022) and that banks are prevented from converting instructions from non-XML to XML (this is part of the SEPA regulations). The banks' responsibility is to clear and settle – not to reformat. Thus, corporates with volumes to send/receive have to have a capability to operate accurate and complete transmission of data using a technical method

which they are unlikely to have today and which requires a significant effort to implement.

The use of a standard XML approach also enables the corporate to change their banking supplier easily – from a technical perspective. This enables the advantage to choose the country / bank with the best conditions (charges) and enables the corporate to change account from one bank to another to gain cheaper pricing / lower cost on transactions.

There was no mention of the difficulty of nominating beneficiary accounts as IBANs.

The most important effects of late or non-compliance are:

- Slower euro payment flows, higher charges and increased repair fees. In a friction-free payment infrastructure (which is what SEPA is designed to enable), payment service providers in Europe will penalise wrongly completed, and incomplete and non-compliant instructions.
- And if SEPA is implemented across Europe by European banks and their corporate customers by end 2014, then UK banks and their customers are exposed to competition with more efficient, and cheaper payment services, which are more easily connected into the corporates' payables and receivables systems – until they themselves are compliant, which may be a period which lasts up to two and a half years.
- Thus, UK trade with the Eurozone – held to be the UK's most important trading partner(s) – is disadvantaged against its European competition. The unanswered question is by how much?

The UK payment community has not moved much from its long-held scepticism of the SEPA initiative. a common view, expressed by most respondents is illustrated by one quote: "UK banks and corporates have been lagging behind SEPA developments anyway, even before the 2016 deadline for the UK was announced, because they thought SEPA would never come and were in denial-mode."

The introduction of SEPA disadvantages those smaller banks that compete for the business of corporates which trade in Europe. SEPA compliance will be managed by the large UK banks and the international banks operating in the UK and European markets.

Interpretation of legislation (the PSD was the cited example) tends to end up with each bank interpreting the rules – and differently. The UK Payments Council was most frequently named as the body which could both focus the issues and publicise them.

The importance of education was highlighted by most respondents, as the following responses indicate:

> *"It does matter because businesses are not informed sufficiently to make decisions on the commercial impact, negative or positive. What we witness is bland statistically led reports on bank adherence to scheme, reachability etc. As one chief executive said three or four years ago, 'Please, no more roundtable debates on SEPA – let's workshop a business case.' This should really matter to Treasury but they delude themselves and are poorly informed of the situation. Even Vince Cable doesn't ... talk about it."*

> *"Today companies look at all ways of centralising/managing their payments and collections and if SEPA contributes to this it matters. As far I as I see it the only assessment of the opportunities is with businesses and they are at varying degrees of knowledge, awareness or interest in SEPA."*

> *"The real issue is ensuring UK companies have the best means of managing their business and if this is aided by SEPA they need to be informed. They continue to be under-whelmed by their banks in this regard. This is well documented feedback. As one financial director said, 'If the banks are unclear on what SEPA means to them they are not in a position to guide my company.'"*

Miller says that the responses "were driven from two entirely opposite points of view".

- From those who regard SEPA as an "over there" issue, relating to a project which about which they are sceptical anyway. They regard SEPA as a c ompliance matter, to be addressed by a date sufficiently far in the future to be unthreatening, with little or no medium or long-term relevance to UK clearing, which is heading in its own directions. We drive on the left hand side, they drive on the right.
- From those that regard SEPA as a means of making the European payments infrastructure more efficient, cheaper and more open to the implementation of e-commerce applications. These people regard SEPA as a competitive advantage matter from which both corporates and their banks can benefit. These recognise that UK corporates could be disadvantaged against their European competition and that UK-based banks' hold on their customers' euro business is fundamentally threatened. For these, this is a competitive advantage issue, in which the end-date for the UK of 2016 is irrelevant. In their view, compliance is required at all possible speed, particularly as European banks will turn their attention to competitive markets once their own customer bases have been converted to the SEPA techniques.

Miller – who readily admits that he has always been a sceptic – says it worth remembering what SEPA is about "and why our view of it will change as it becomes a reality".

The SEPA programme is expensive – it will have cost an estimated €9 billion to implement. This sum is applied to electronic payments in euro (direct credits and debits) adding up to over 38 billion transactions a year in 2010 within Eurozone and accession countries and growing at an annual rate of 4%. "This means a capital cost per transaction of about 5 eurocents written off over a five year period, causing reduced processing, clearing and settlement costs, and offering greater usability across the entire Single Market," says Miller. "Less attractive business cases have been approved."

While it is a huge programme, with all of the inherent risks that apply to grand plans, Miller says that from the UK perspective "it looks quite different now it is happening" and will look more attractive once it has happened. "Initial cynicism will have to be replaced by the recognition that it exists and that the UK banking community and its corporate customers will have to comply for their euro business – the laws applying and the infrastructure are in place within the UK alongside the sterling infrastructure," he says.

From a 35,000 foot vantage point, he says, you might conclude that it was in the national interest to:

- Encourage corporates not simply to comply by a distant end-date, but to seize the opportunity to comply in their own commercial interests within their EU trading plans and as soon as possible. Perhaps by pointing out that postponing the end-date is to the benefit of the UK by postponing the date on which mandatory penalties come into force; however were it to be interpreted to mean delay or lack of urgency, the advantage of the space created by the regulators will be swamped by the commercial disadvantage of mass late adoption.
- Regard this European programme as a viable experiment to judge the viability of the theories surrounding SEPA and its techniques. Any view as to whether ISO 20022/XML represented a future path for Sterling clearing could then be made on an informed basis and with the knowledge that the UK banking community was already practicing it successfully.

"The message for regulators is that there is considerable uncertainty in the UK payments community, in contrast to euro-based countries such as Ireland which has an active education programme," says Miller. "The message to banks is that they are responsible for educating all their customers. And they will form the group which is likely to suffer from any backlash that may result from late adoption." ***BT***

Banking Technology would like to thank Peter Miller for his input to this article. He can be contacted on peterjwmiller@btinternet.com

Q&A

Are some UK corporates in danger of putting themselves at a significant commercial disadvantage if they postpone adoption of SEPA for euro transactions until 2016?

The majority answered with a clear yes, with some qualifying their answer with the suggestion that while it would be advantageous for UK corporates with European payments to use SEPA early, this might not be their biggest problem and that the cost/effort of enabling SEPA might be a constraint. 2 answered no.

Which segments of the corporate market are most disadvantaged – large corporates, mid-sized or SMEs?

The majority answer was

1. No-one is disadvantaged yet.
2. All those engaged in cross-border business would be the most affected (although this was assumed by the question.)
3. Small SMEs will mostly be managing single credit transfers which aren't impacted by SEPA (which for corporates applies only to bulk transfers). Their online banking products and or FX payments will continue to manage their requirements adequately. They are unlikely to have a significant problem.
4. Opinion was split between large and medium corporates with a majority assuming that the mid-sized corporates with less banking clout had the greater problem in sending SCTs and that large multinationals which may see the benefit of using SDDs have a significant issue.

Is it presumed that this is almost entirely about direct credits rather than direct debits, for which the changes required are significantly more complex, but for which the cross-border volumes today are not significant?

Almost all replied yes. But most respondents added the rider that since the direct debit business was growing, primarily because it offered corporates the ability to collect funds more efficiently and cheaply, it would become more important.

A typical reply was: "There is ample evidence that the costs and risks of collection inhibit businesses, especially small businesses, from engaging in export. SEPA DDs are intended to reduce this barrier, for firms which bill in euro to clients in the eurozone. While perhaps relatively few UK firms do that today, the availability of such a service might be seen as an enabler by some."

Is the UK economy as a whole in danger of putting itself at a significant commercial disadvantage if it regards the end date of 2016 as the only critical date?

The majority answer (60/40) was yes and included multi-national companies with European headquarters in the UK.

Is someone responsible for informing the markets, corporates or consumers, about SEPA. Who is this? And are they doing what is necessary?

Here the answers were both most complete and varied.

Most respondents acknowledged that it was the banks' responsibility to inform their customers about the change. (Miller himself trades as an SME with international payments flows, and says he has yet to receive any SEPA education or advice from his bank. Other SMEs have a similar experience.)

Those customers that are aware of SEPA are not aware of the 2016 date or believe their bank will sort it out for them. A distinct lack of leadership and education was cited. A typical answer was:

"No. I think there is a distinct lack of leadership here. By closing the euro schemes, it feels as if the industry thinks it has cunningly side-stepped the issue. I would have thought that a forum of bodies, including the Payments Council, Treasury and corporates should be doing a risk assessment at the very least. By not doing anything, in effect they've chosen 2016 by default."

But most respondents also suggested, as criticisms, that:

1. There was no information campaign to corporates and specifically that:
2. The Payments Council was too worried about its own future and burdened enough with sterling issues and clearings;
3. The Government was regarding this as a "minority interest."

Java in the cloud

Java is the most ubiquitous programming language out there, but it doesn't work well in the cloud. *David Bannister* reports on one approach to overcoming the problem

When Accenture announced the winners of its FinTech Innovation Lab London at the beginning of the year, most of the entries were what have become familiar at innovation-oriented events – totally new ways to integrate social media into retail online banking services, for instance.

Only one firm of the seven isn't working on a bank-to-customer product or service .

Dublin-based Waratek describes itself as "a Java virtualisation company", with a product called Cloud VM for Java. At this stage there are proof of concept installations at "a couple" of different banks.

And it reckons it has a solution for one of the problems facing Java applications – how to continue using the myriad Java applications that are scattered throughout firms, in the modern computing environment of virtualised servers and cloud architectures.

Firms are in a difficult situation with this: with so many applications, rewriting the code is not an option, but neither is continuing to throw expensive hardware at the problem in order to get more capacity.

Going back to basics, Java is a 17 year old language, originally developed by Sun Microsystems, and now owned by Oracle. It is pretty much the most ubiquitous programming language in use. "There is no other language in which so many enterprise applications are written – somewhere above 50% of enterprise apps are actually written in Java, " says Howard Tolman, director of Waratek's UK operation.

Being 17 years old isn't really the problem: the issue is that in those days, compute power was relatively inexpensive. "It was one server for one app," says Tolman. "In these days of virtualisation and cloud you are talking about running lots of different Java apps on multiple servers. Java will take memory from other applications, and if they are written by different programmers they may have unpredictable issues."

The end result is that people tend to put java apps in containers, isolating them, but this is a far from ideal solution.

"In reality, there are still some gaping holes in the server virtualisation story, and one of them is Java-shaped," wrote John Abbot in a 451 Research report last year. "You still can't run multiple Java apps on top of a single Java virtual machine, and that leads to some gross inefficiencies."

The isolation capability exists in environments like VMWare and Azul, but each Java app is still running in isolation, which leads to the second half of the problem: the lack of dynamic configurability.

It is a reasonable solution, but if you are running, for example one application in one virtual container, it is not the most efficient. When you set the parameters of the JVM, you have to allow for all of that, and you can't' then optimise the server. "You have to set it up at the extreme level, not the optimum level, so that it doesn't degrade," says Tolman.

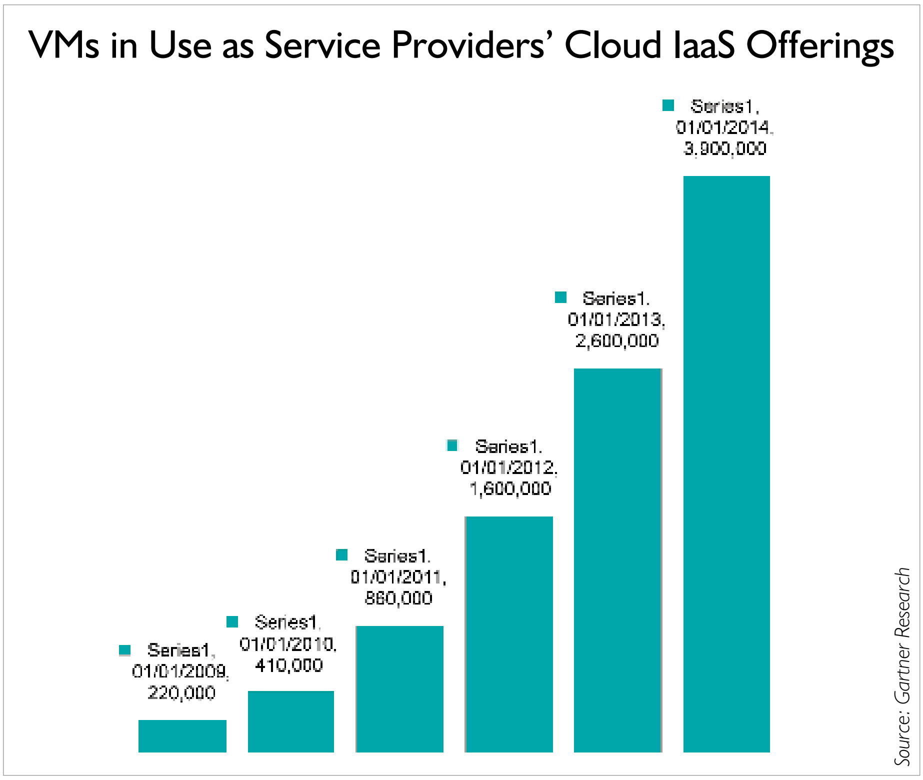
An application or routine that uses variable resources over time – perhaps only a fraction of the system for most of the time, but half the available resources at particular times – will have to be set up with the resources that it uses at the maximum period.

What the Waratek approach does is to allow multiple Java Virtual Containers to work within a single JVM. That means instead of having one JVM with one application on it, you can have, say, 16 applications in individual Java Virtual Containers, all isolated from each other and completely discreet on a single JVM", says Tolman.

"This brings a further degree of integrity to the applications and on top of that you only need one version of Java to drive the whole set of applications. If, example, those applications had Apache Tomcat, or WebSphere or WebLogic supporting them as an application server, you could have just one instance of it. What this does is massively increase the application density. Whereas before you had to set memory capacity with a view to the maximum, you can now plan, knowing that not all of the 16 applications are going to be at maximum at the same time."

This also leads to a considerable reduction in maintenance cost, claims Tolman. "Within a traditional JVM you can't do that on the fly, so if you have to change the parameters of an application you have shut the whole production system down, which is why you are sending teams of people in at the weekend, because that's the only way to do it," he says.

A lot of this comes down to a concept called multitenant elasticity. The first part is easy - multiple different applications hosted on the same server, or sharing the same resources, and is a common characteristic of cloud environments. While multitenant has become a feature of mainstream cloud and enterprise computing solutions, existing Java application servers don't deliver multitenant support to cloud-based applications, for the reasons outlined above.



The elasticity part comes from being able to use dynamic configuration, with applications being able to demand resources as and when they are needed.

With multitenant elasticity, you can manage individual containers dynamically. "You can increase or decrease memory, for instance, without having to shut things down, you can allow for bursting, and all sorts of things," says Tolman.

With this approach, IT managers can now square the circle – preserving investment in existing code, increasing application density on existing hardware, and removing the need to shut down the production systems for maintenance are all good things in themselves.

And because the applications are running natively, it is possible to migrate relatively easily. "You can shift an application from its existing environment into a Java Virtual Container and it will boot up and run without any changes," says Tolman. "There will, of course, be configuration issues, but the cost savings justify that interim work."

"The actual cost savings are very dramatic," he says. "The management problems of running these systems are difficult enough on their own, so you save in management overhead, but if you look at it in terms of where you can save, you are exploiting massively underutilised server capacity. The more you can drive up server utilisation the more you can see in direct operating cost saving for IT."

Moreover, it means that IT services can be more quickly provisioned, which is another benefit arising from the same capability.

"Banks have huge Java estates, generally speaking, that they can't really get rid of – we are talking about a reduction by a massive percentage. If you look at the money that is being spent on hardware, third party software licences, electricity and carbon footprints – costs are increasing across the board," says Tolman.

"At the end of the day this is what it comes down to – no-one is going to use a bank because it uses particular JVM, but they are going to use a bank that charges them less because they have lower IT costs." ***BT***

Wagner aims at m-commerce gap

With his latest venture, mPowa, *Dan Wagner* reckons he can help banks keep abreast of the revolution in mobile commerce. He outlines his strategy to *David Bannister*

Dan Wagner is pretty sure that he has an idea how the use of mobile devices will play out in the commercial world and how the relationships between banks, merchant acquirers, merchants and customers will change.

He's been pretty sure about things before, so it might be worth paying attention. Back in 1984, Wagner set up MAID – Marketing Analysis and Information Database – one of the first online database services.

A decade later, the company was listed on the London Stock Exchange and had offices in New York, Paris and Los Angeles. It also had deals to supply data to Microsoft for MSN, and with CompuServe, IBM and British Telecom.

In 1997 it acquired Knight-Ridder Information in a $420 million deal that created the world's largest online retailer, merging the US company's Dialog database with MAID. In 2000 it was sold to Thomson for $330 million.

Getting information online these days is, of course easy. If you want to know more about Wagner's colourful career, a reasonable place to start would be to type the phrase "serial entrepreneur" into Google. A 2007 article in the *Daily Telegraph* uses the phrase twice in the first three paragraphs.

For the past few years, Wagner has been involved in the world of e-commerce through Venda, a company that he set up in 1998, originally as a subsidiary of MAID, and which provides e-commerce solutions for TK Maxx, Tesco and others.

Amid a scattering of other ventures, his main interest these days is Powa, another e-commerce platform, and mPowa, a subsidiary that is developing and manufacturing a mobile payments solution for the point-of-sale.

There are, of course, other mobile PoS devices, notably Square and iZettle. The US Square device, introduced by Twitter co-founder Jack Dorsey, was an inspiration to Wagner, he says, but it is flawed by the fact that it uses the magnetic stripe on the card rather than the EMV chip and pin standard. "When I saw the Square device, suddenly it crystallised how to move the online world into the physical world," says Wagner. "It isn't appropriate anywhere else in the world."

The iZettle device, is even worse, says Wagner, as it involves the retailer physically handing over their smartphone for the customer to key in details. In the real world – particularly the world of the small retailer – he thinks this is unrealistic. "Who, on a

Curriculum Vitae: **Dan Wagner**

1981: Works in advertising at WCRS
1984: Founds MAID as an online information service in London
1986: Moves company to New York
1994: MAID listed on London Stock Exchange
1995: MAID floats on Nasdaq
1997: Knight-Ridder Information acquired and merged with MAID as Dialog
2000: Dialog sold to Thomson; Wagner retains some IP in new vehicle, Bright Station, which is subsequently taken private to act as the parent for Venda and Locayta, m-commerce ventures delivered on a SaaS basis
2012: MPowa formed to target mobile commerce

market stall, is going to hand a $500 smartphone to someone buying a pair of cut-price jeans?" he asks.

The mPowa pitch is to close a gap between banks and infrastructure players, the payment processors and the retailers. Square and iZettle are about card-enabling those retailers that currently can't afford to take cards, or work in environments where existing terminal aren't practical. "This is not intended for the new-to-card vendors," he says. Instead he sees a market for the mPowa device among the existing infrastructure players, replacing current PoS systems with far cheaper mobile devices. "Banks and others are going to have to build systems, or they could buy from us," he said.

Essentially, it is a white labelling play for a small – cheap – EMV card reader that has a Bluetooth link back to a mobile device, which acts as a portable PoS terminal. Consumers are comfortable with their cards, and the card schemes are well-entrenched. In fact, Visa and MasterCard have both said that they see a blended future for cards and mobile devices acting as a card replacement.

Behind his thinking is a belief that things are changing in the world of commerce, and traditional retailing is under threat – the UK has seen the disappearance of several high profile retailers in the past few months, with Jessops, HMV and Comet all exiting the scene.

But Wagner is optimistic that there is a future for retailers and that mobile commerce is the a key part of that future. "When we set up mPowa, the feeling was that mobile commerce is about to change again, particularly moving from the desktop to the mobile device," he says.

The big difference between the modern physical retailing environment and online shopping, is that in the latter case, anti-intuitive as it may seem, the consumer has a more personal relationship with the vendor and vice versa. Amazon's recommendation system, flawed as it undoubtedly is, is still a more personal interaction than wandering around a large department store.

"The fact is that retailers with a physical presence don't know who their customers are, whereas online they know exactly who you and can therefore serve you properly. Retail is a dumb environment," says Wagner.

The people that are most threatened by this whole revolution are the people who provide the acquiring services – people like HSBC or Barclays

Even so, he continues: "retailers are not going away, but they have to change, and who is best placed to effect change in a physical retail environment? I'd say it is the e-commerce provider, because they are running all the other channels."

In the future, retailers will be assisted by technology, blending the technologies of e-commerce and data analytics in the retail environment (just as has been talked about in retail banking for some time).

One step at a time, however. The next stage for mPowa is to manufacture the card-reading widget, which is so cheap compared to existing devices that Wagner expects many of them to be simply given to retailers by the payments or point of sale vendor. "It is a fifth of the weight, a third of the size and a eighth of the cost of anything else that is out there, so it is dramatically cheaper and more portable," he says.

There are several things that make the mPowa approach different, he says. "The first is the ubiquity of acceptance – it will take cards from anywhere in the world, either mag stripe or chip and pin. The second thing is that we are not interested in the new-to-cards market like Square and iZettle. Those Tier 5 retailers are not well served by the banks, because there isn't any real volume – they prefer cash, pretty much."

A third difference is that mPowa has set up its infrastructure to be white-labelled by banks and partners. "The people that are most threatened by this whole revolution are the people who provide the acquiring services – people like HSBC or Barclays, but not Square," says Wagner. "They are serving the merchants that have bank accounts with them, but they do not understand what it takes to provide mobile apps and provide APIs to connect all the mobile devices."

It is into this space that Wagner is pushing mPowa. "What we are doing for them is providing an infrastructure to extend their reach. I said that banks are going to have to build that capability or lose out, and decided that we would build it for them and provide it to them. We are competing with the people that make the till systems and the card readers – VeriFone and Ingenico."

In a market with lots of new, unknown and, ostensibly, exciting players, Wagner seems to be positioning mPowa as the known – he emphasises the infrastructure behind it all, and the lack of disruption that his solution involves, rather than the disruptive nature of the technology., which is much-beloved of its exponents.

It's certainly a different approach – and worth watching. ***BT***

POWER TO THE PEOPLE

Chris Dunne,
Payment Services Director

"The introduction of Universal Credit, administered by the Department of Work and Pensions (DWP), is the most fundamental change ever to the welfare system."

The UK is a relatively highly banked economy; according to Payments Council data 91% of the adult populations hold a current account and 96% have a bank account of some form, including savings accounts. So it is not surprising that over recent years the UK Government has made increasing use of electronic channels to deliver benefit payments to citizens. Almost 98% of benefit payments are now paid via Bacs or Faster Payments, and with the advent of Universal Credit this year that proportion will increase further.

The introduction of Universal Credit, administered by the Department of Work and Pensions (DWP), is the most fundamental change ever to the welfare system. It replaces six existing benefits, including housing benefit and income support, with a single monthly payment similar to a salary payment. This payment will flex according to a claimant's individual circumstances; broadly speaking as their income from employment increases the need for benefit payments will decrease and so their Universal Credit payment will change accordingly. This is largely possible because the vast majority of salary payments also flow through the Bacs service; the new HMRC Real Time Information service matches the salary payment to the employer's regular tax submissions and so can provide the DWP with an accurate, timely view of a claimant's income.

Universal Credit must be paid into a bank account or to a prepaid card account; it will also be almost entirely administered online; according to the DWP, 78% of claimants are regularly online so it is a natural channel for most users.

One of the biggest changes will be that housing benefit will be paid directly to claimants rather than to their landlord; this is currently being piloted in six local authorities across the country. This leaves the responsibility for budgeting with the claimant, and so there is a clear need for more, and better, budgeting tools to be available to manage this shift to larger monthly payments that require active management by the claimant.

One well-established and well-recognised way of meeting some of the budgeting challenge is to encourage claimants to set up Direct Debits with their landlord to ensure that as the universal credit payment is received, the rent gets paid to the landlord. However, there are a number of people for whom Direct Debit isn't appealing; they feel that they need to remain more in control of their finances, dictating when a payment should be made and for how much. This demand can be met by alternative payment solutions that allow someone to make account-to-account transfers quickly, easily and safely. Research by VocaLink and Accord showed that 81% of people interested in new digital payment methods say they are more likely to adopt such services if they are provided by their bank. A key element of such services is the ability to be presented with a bill and be able to make that payment instantly at a time of their choosing. Such services, provided by banks or alternative payments providers, will provide everyone with secure and flexible control of their finances.

VOCALINK
safer payments, smarter partner

APPOINTMENTS

Sear quits Travelex for Weve mobile wallet marketing venture

Weve, the advertising and commerce joint venture between mobile network operators **Vodafone, O2** and **EE**, has hired payments industry veteran **David Sear** as its permanent chief executive.

Sear replaces Nancy Cruickshank, who led the venture – formerly known as Project Oscar –through regulatory clearance by the European Commission as chief executive since September 2012. She will remain on board part-time until the end of March 2013 to ensure a smooth transition.

Sear has spent six years at Travelex, the world's largest non-bank payments provider, as divisional managing director of its Global Business Payments and prior to that as divisional managing director of outsourcing. Before joining Travelex, Sear spent three years as commercial and scheme managing director at VocaLink, the UK payment processing operator.

Weve currently offers location-based video and SMS messaging and is developing a mobile wallet and voucher service for loyalty schemes that will offer businesses in the UK "a single point of contact and a single point of technical integration". With the addition of Vodafone customers it has an opted-in database of 15 million customers.

BI-SAM, a developer of data management, performance, attribution, risk, GIPS and reporting solutions for asset managers, has appointed Sean Murray as head of account management and sales engineering for the Americas.

Based in Boston, Murray joins BI-SAM from Eagle Investment Systems where he was the head of sales engineering. Previously, he held customer facing roles in sales engineering and professional services at companies such as DST International and Misys.

Murray will lead the integrated account management and sales engineering function, focusing on strategically growing the new customer base in the Americas and supporting existing customers.

Nadeem Chowdhry, formerly sales director of financial services for **QlikTech**, the makers of the QlikView business intelligence system, has joined data visualisation specialist Panopticon as senior vice president in the UK

Chowdhry has 20 years of experience in selling enterprise software to global organisations. Since 2005, he has helped develop the market for QlikView products in the UK banking and insurance sectors, working with clients including HSBC, Deutsche Bank, JP Morgan, Morgan Stanley, Bank of America Merrill Lynch, and RBS.

Consulting and IT specialist firm **Rule Financial** has hired **Emily Cates** as a principal consultant. Based in the London office, Cates joins Rule Financial with over 18 years of experience across securities financing, prime brokerage, equities, fixed income and structured trades.

Cates joins from Knight Capital Europe, where she worked for 18 months as head of London operations. Prior to her role at Knight Capital Europe, Cates spent eight years at Dresdner Kleinwort, most recently holding the position of global head of client and cross-products services. She also spent four years at Credit Suisse, where she held the post of vice president strategic change management and prime banking.

Capco has expanded its UK partner team with a series of internal promotions. **Simon Brownlee, James Curzon, Steven Hargreaves** and **Kim Sgarlata** join a team of 12 partners in Capco's UK practice.

Brownlee has more than 13 years' experience across tier one investment banks specialising in front office IT strategy, target operating models, post-merger integration and finance transformation programmes. He works in Capco's capital markets along with Hargreaves who has 14 years' experience in the space, with more than 5 years leading global strategic change management teams in equity derivatives, collateral management and securities. Sgarlata is also part of the capital markets practice and has been delivering large scale derivatives change programmes for more than 11 years. She specialises in target business and operating models, post-merger integration and the establishment of counterparty portfolio management functions. Curzon has more than 15 years' expertise in delivering business/IT transformation across the retail banking, insurance and cards/payments industry and operates within Capco's banking team.

DST Global Solutions is expanding its team in the Asia Pacific region with the appointment of **John Hogan** as Regional Anova Solution Manager, Australia and New Zealand and **Daniel Kennedy**, in the same role for Asia. Anova is a post-trade data management, analytics and reporting system.

Hogan is based in Melbourne and Kennedy in Singapore. Both report to Julian Webb, global head of data management and analytics. Hogan brings more than 17 years of financial services and technology experience to DST Global Solutions. Most recently he was responsible for a major investment management system upgrade at AMP Capital. Previously, he managed business analyst teams at Macquarie Funds

Group, Citistreet Australia and Queensland Investment Corporation and brings technology software experience from Princeton Financial Systems.

Kennedy has more than 20 years of financial services and technology experience, 10 of which have been in Asia. Most recently at Dion he was involved in product strategy, acquisitions and on-boarding and creating new product divisions for wealth management, financial analytics, governance, risk and compliance and messaging workflow.

US financial and technology consultancy **Morgan Frankin** has announced a number of senior hires in its UK operation, including that of **Hans Christian Iversen**, a former strategy director for Walt Disney in Europe, who has been appointed managing director. His arrival comes as Washington-based MorganFranklin, increases its headcount in London.

Recent additions also include the appointment of director **Jon Kidd**, former head of global IT applications management at **Barclays**. Kidd has been a strategic director with Capita, as well as the global operations director of Mastek, a Mumbai-based software company. Kidd was headhunted by the government of Abu Dhabi to set up Musanada, its shared service company. While at Barclays, he led a comprehensive programme of service transformation, cost reduction, and global rollouts.

Enyx, a provider of FPGA accelerated market data feeds, is expanding commercial coverage into Asia during 2013. Connectivity to the Tokyo Stock Exchange' Arrowhead is already available with Korean options and futures, Hong Kong equities and derivatives and Australian Securities Exchange equities and options due for delivery later this year

To support the growth in requirements for its products and services, Enyx is establishing a local presence in the region. **Nicolas Karonis** has been recruited as managing director for the APAC region. Initially based in Sydney, he will be responsible for the growth of the business and the establishment of the Asian operations team to cover client support and project management during trading hours in the Asian time zone. Nicolas brings close to 20 years' experience in the electronic trading industry working in Paris, Tokyo and Sydney. As chief technology officer with GL Trade in Asia, he supervised the growth of exchange connectivity to over 20 electronic markets in the region.

Kevin Cullen, communications and marketing director of **Information Mosaic** in New York, has been appointed to the Securities Industry and Financial Markets Association Industry Leadership Committee of its corporate actions section in the operations & technology society, which is focused on education and the sharing of best practices in the corporate actions, proxy, and settlement sectors of the financial services industry.

Cullen also serves on the board of the International Securities Association for Institutional Trade Communication, the industry trade group focused on standards in transaction processing and related communications, and is the co-executive sponsor of ISITC's corporate actions working group, as well as its marketing committee.

The **Alternative Investment Management Association,** which serves hedge funds, has chosen two deputy chairmen from its existing directors and an investor appointee to the AIMA Council.

The new deputy chairmen are **Andrew Bastow**, head of government and regulatory affairs and general counsel, Winton Capital Management; and **Chris Pearce**, Asia chief operating officer, Marshall Wave Asia. The new investor appointee is **Robert De Rito**, head of financial risk management at APG Asset Management US.

Bastow has been Winton's general counsel since 2005 and is responsible for spearheading the firm's interaction with regulatory bodies and lawmakers in Europe, the US and the Far East. He was elected to the AIMA Council in September 2010.

De Rito has global risk management responsibility for APG's hedge fund and fixed income investments as well as responsibility for real estate and other alternative investments for the Americas. *BT*

EVENTS

MARCH 20-22 2013
EPCA Payment Summit, Brussels

The 2.5 day programme consists of dedicated pre-conference workshops followed by a plenary and specialised tracks.The EPCA Summit 2013 will cooperate closely with European Banking Associations, such as NVB, the Dutch Bankers Association, in setting the agenda.

http://transactives.dcportal42.nl/

APRIL 9-11 2013
International Payments Summit, London

The 21st anniversary of this industry fixture sees it moving venue to the Hilton London Tower Bridge. The draft agenda shows an emphasis on new opportunities in technology, developing markets and – of course – mobile.

www.icbi-events.com

APRIL 16-18 2013
TradeTech Europe, London

Since its launch in 2001, TradeTech, has become one of Europe's leading financial trading technology conferences, and a prime source of strategies, information and networking.

Top of the agenda for 2013 are the effect of market fragmentation of the buy-side; the lack of a consolidated tape; finding liquidity; flash trading; and technology – what new technologies are going to most affect the order flow and the markets? How can you best prepare for the next big technological change in the markets?

www.wbresearch.com

APRIL 21-24 2013
NACHA Payments 2013, San Diego

The main event will have 130 session in eight programme tracks covering ACHs, card solutions, corporate payments, global issues, healthcare opportunities, mobile banking and payments, risk & compliance and "The Payments Biz" – a track focussing on trends, challenges and strategies.

https://payments.nacha.org

APRIL 24-25 2013
Meftec 2013, Doha

The long-running Middle East Financial Technology Exhibition and Conference continues to be "a bespoke learning, networking and business experience that blends an industry-leading conference with a tightly focused exhibition and high-class social functions". This year it is moving venue to Qatar, after previous events in Bahrain, Abu Dhabi and Dubai.

www.meftec.com

Heightened banking cyber threats require clear focus

Seth Berman, executive managing director and UK head of Stroz Friedberg

As the US Federal Reserve joins a growing list of financial institutions targeted by cyber criminals, reports of an organised campaign to recruit hackers for a large-scale malware attack, dubbed Project Blitzkrieg, has further highlighted the challenge facing the banking sector.

Adversaries are becoming more sophisticated, as signs suggest state-sponsored attacks could also be on the increase. The chairman of the US House Intelligence Committee, Mike Rogers, last month went as far as suggesting he was "99.% confident Iran initiated recent cyber-attacks on PNC and other major banks and that it clearly has the capability and desire to trigger more destructive assaults".

Such risks have caused financial services institutions and, in particular, banks to seek greater preparedness. However, as with any security system, there is no fool-proof way to prevent a cyber-attack. There is consequently, a growing need to focus on how such threats can be tackled more effectively.

Addressing these concerns requires equal measures of prevention and preparation for a response – to use a real world analogy, banks need to take steps to prevent a fire, as well as to deal with one.

A key step is one that sounds simple, but is all too rarely done: conduct an audit of the IT and physical security system. A security assessment, like a financial audit, should be carried out by an outside team without a stake in the existing IT infrastructure.

The team will be looking at the organisation's threat profile and vulnerabilities. In addition to ensuring that IT security practices are up to industry standard, a thorough security assessment will also identify where sensitive data is stored and whether this can be segmented or further removed from the rest of the IT system.

For example, a recent breach occurred through a heating control system that was accessible from the internet. Because no one at the organisation was particularly concerned that hackers might adjust the office temperature remotely, the system was poorly defended. However, since the heating system and primary user data were hosted on the same server, a hacker was able to use the entry through the control system to install software that ultimately provided access to all data, including key corporate secrets, on the server.

A good security assessment will go beyond the infrastructure security, to review the weakest link in any security system: the users. Are passwords up to date, or can they be easily guessed or broken? Do users know not to click on attachments to suspicious emails? Are they tested to see if they in fact do not click on such attachments? Do users know who to call if they accidentally do click on such an attachment?

However, as with physical security, the best preparation cannot prevent all attacks and preparing a response strategy is essential. Banks should determine what the chain of command will be for the incident response team. A specific executive should be nominated to lead the internal response team and the organisation must designate in advance its external lawyers and IT consultants.

After a breach is discovered, one immediate goal will be to determine whether to notify law enforcement. This is not a simple decision.

A hacking or data breach may require a different response compared to other types of crime. In particular, incidents triggered by outsiders are likely to present a much steeper challenge to law enforcement, as the perpetrators could be thousands of miles away and using proxy servers to hide both their location and identity, greatly limiting law enforcement's effectiveness. Moreover, law enforcement will have trouble determining the scope of the incident – what was actually taken - without detailed knowledge of the corporate IT infrastructure. Most banks prefer to avoid giving law enforcement the necessary level of unfettered access.

In my experience, most companies faced with this situation conduct a private investigation before notifying law enforcement, with three factors often driving this decision:

- Sophisticated hackers rarely advertise their presence. As initial evidence may be confusing or hard to interpret, it is not always immediately clear whether any laws have been broken or not.
- Hackers do not leave detailed lists of what they stole. Only painstaking reconstruction of a hacker's activities through sophisticated computer forensics can determine the scope of the offence. This requires nearly unlimited access to secret corporate data and restricted networks, which most banks do not want to grant unless legally required.
- It is much easier to control the public relations and communications strategy if the extent of the problem is known before going public. By handing the investigation over to the authorities, a bank would lose control over the timing and content of any public notification. This could prove a public relations disaster.

Banks are likely to remain prime targets for cyber criminals for years to come. Tackling this challenge will require a clear understanding of the underlying risk, a strategy to mitigate such threats, alongside a rapid response at the first signs of a breach.

Will Dodd-Frank trade reporting prepare you for EMIR?

by Mark Steadman, co-leader of the Regulatory Reporting practice at Sapient Global Markets

On February 28, most of the approximately 70 registered swap dealers will stumble across the finishing line for the remaining asset classes (equities, commodities, and FX) of the Commodity Futures Trading Commission implementation of Dodd-Frank trade reporting regulations.

Some may be forgiven for breathing a sigh of relief, thinking the worst is over. While undoubtedly a major milestone, it is worth noting that this is one of the first of the G20 reporting commitments to go live, with many more to follow. There is enough difference between it and the EU equivalent, EMIR (regulated and implemented by the European Securities and Markets Authority), to stand up and take notice.

Though not an exhaustive list, the following are some of the key differences between EMIR and Dodd-Frank requirements that are likely to represent additional implementation challenges for organisations that have already implemented Dodd-Frank under the CFTC:

Product Scope

One of the fundamental differences between Dodd-Frank and EMIR is the product scope. Dodd-Frank regulates OTC Derivatives, whereas EMIR – taking its product scope from MiFID – covers both OTC and listed derivatives. There are several points to consider:

- While recognising the role that CCPs and/or exchanges might take in reporting, the range and sheer number of fields to be reported (though familiar to those in the OTC world) are not typically communicated as part of a futures transaction lifecycle.
- The inclusion of futures could significantly increase the implementation effort, depending on how many trading systems an organisation uses.
- The number of stakeholders will increase across functional areas, which will contribute additional complexity to governance and the reporting control framework.

Reportable Data

Each regulator requires a minimum set of data fields to be reported and while there is significant overlap, the fields outlined in the final technical standards for EMIR create additional challenges above and beyond those required by the CFTC. Some notable additions include:

- Extensive counterparty information (required if you report on behalf of your counterparty)
- Trading activity information
- Additional collateral data

Collateral data requirements within EMIR are far more extensive than within the CFTC regime, which only requires an indication of collateralisation. EMIR requires organisations to indicate the amount (including ongoing MTM), type and basis (portfolio or otherwise).

Reporting Obligations

Under the CFTC, there is a concept of "reporting counterparty"—making only one party of the trade responsible for reporting, based on a hierarchy of market participants. The emphasis on reporting is placed on the major market participants (swap dealers). By comparison, ESMA has adopted a slightly different model. Although the reporting obligation can be delegated within EMIR, the legal obligation for accurate reporting remains with both parties, and thus, under EMIR, smaller organisations carry the same reporting burden.

There is also a subtle, yet important difference between the focus of EMIR and the focus of the CFTC in implementing Dodd-Frank. While both are very focused on the gathering of data to monitor systemic risk, the CFTC seeks reporting that is achieved as quickly as possible so that price data may be distributed onto a price ticker. That is, the CFTC is very focused on price and volume transparency to the market, believing this will fuel healthy competition and increase market participants. In theory, the more market participants, the less concentration of risk. But with T+1 reporting, EMIR is less focused on this. Instead, and by keeping in line with MiFID 1 reporting, EMIR seems to be looking more closely at market abuse. This focus is specifically called out in the ESMA technical standards, and requires a reporting log that records:

- Modifications of data already reported
- The identification of the person or persons that requested the modification
- The reason or reasons for such modification
- A clear description of the changes.

Considering the amount of attention and effort placed on global harmonisation, you might think it only fair that the industry assumes the European standards will tie closely with their US counterpart. Though there are similarities, important differences between the two sets of regulations are likely to represent additional common challenges for the implementation of EMIR – even for those institutions that have already implemented for Dodd-Frank.

If you assume that implementing reporting under EMIR will just be an incremental build on your Dodd-Frank reporting solution, then you will need to reconsider. It would be wise to begin planning and budgeting for a similarly lengthy and costly implementation of reporting as under Dodd-Frank.

Ready for retail revival

Tim FitzGerald, finance & banking sales manager, Casewise

Today, maximising profit is harder than ever for banks. The large retail banks have been forced to sell off branches and their investment arms are under increasing scrutiny. The need to change – be it adapting to newly-imposed regulatory frameworks, to differentiating yourself from the competition and growing organically while also encouraging customers to switch to you requires agility never before experienced in the financial sector. Organisations that can change quickest will win.

All this requires financial institutions to examine how they might better interact with their customers, see how best they can improve service to their customers whilst making it more cost effective to process once a piece of business has been initiated – be that a trade, a payment, selling a product or indeed introducing new products.

For the financial services sector, successful use of software and IT systems should mean more than just being able to maintain a good working relationship with your customers; it's about continual improvement, offering more to your existing customers while attracting new ones and growing.

The banking sector relies heavily on IT – electronic trading and settlement is a mainstay of the industry. However it is this myriad of siloed systems and their complexity that makes it hard for management to visualise an end-to-end business process.

We have to ask what the bank is, and what does it aspire to be? How do you make the journey from 'as is' to 'to be' without mapping it, planning it and making best use of your resources? How do you do Basel III? How do you cope with RRP? How do you introduce that new mortgage product? How do you separate investment from retail?

We only have to look at recent calamities in the financial sector. The Libor scandal, mis-selling PPI, rogue traders, liquidity inadequacies, bank bail-outs and system outages leaving customers unable to access their accounts or pay bills. All of these are down to a lack of proper process or adequate process rigour.

Everyone is responsible for process rigour, but the bank's board and senior directors are accountable.

Financial institutions operate in a highly regulated industry and it is everyone's responsibility to follow the right process. But is that process properly documented? Is it published, accessible and digestible by those who need to follow it? Is it auditable? Is it relevant and up to date? Is it aligned with the need to change or operate differently? I suggest that often the answer to most or all of those questions is "no". Then how can any financial institution effectively mitigate against operational and reputational risk unless this is put right?

You have only to recall the day the London Stock Exchange's rules changed – 27 October 1986. It was dubbed Big Bang because of the aggregation of measures designed to precipitate a complete alteration in the structure of the market. Traders no longer walked the floor of the exchanges but conducted business electronically from their desks. The introduction of ATMs, BACS, CHAPS, Faster Payments, SEPA, credit card authorisation and Chip & PIN, contactless technology, as well as the information for traders to understand the market, such as services provided by Bloomberg and Reuters and now 'Bank 2.0' – the advent of mobile banking services – all these require a heavy reliance on technology. Without this technology enablement we would never have seen the services provided today.

However, for banks to be truly competitive there has to be not just better system integration but better visualisation of the business processes. Better visualisation of how the business process of selling a mortgage interfaces with a current account, better visualisation how a trade is influenced, how it is settled and better visualisation of how the transfer of funds occurs. Who owns that process, when was it last reviewed? What different geographies and locations does that process encompass? Who is involved in that process? Where are the bottlenecks, where are the risks? What else runs on those systems hosting this process? What happens if a location is closed, individuals leave the bank, get promoted, roles made redundant that operate within your process but are outside your remit?

There are three key elements the banking sector should take from the recession:

- The ability to adapt to change will separate the winners and the losers;
- Better process visualisation is the only way to remain competitive;
- Better process rigour is the only way to survive.

Transformation and adaption are the watchwords of today's financial sector. However, one should not look at this downturn of the economy as being where the bloodletting will occur. Unless an organisation can effect agility and be adaptable when the upturn comes; if an organisation isn't capable of seizing the new opportunities a resurgent economy brings; if it cannot cope with new invasive regulation while simultaneously growing its business; if it cannot attract new customers and launch new products quicker than competitors – that is when it will die.

Organisations need the tools in place to see the 'bank on a page', to be able to stand at the chart table in the captain's cabin, to be able to plot the course and know immediately the hazards along the way. Because if you can't, here be dragons.

Eurograbber: the £30m mobile banking heist

*by Terry Greer-King, UK managing director of Check Point**

In the history of bank robberies, the £30 million stolen by the Eurograbber attack in 2012 ranks as one of the all-time biggest, globally. And when you consider that this sum was stolen from more than 30,000 accounts across 30 banks in four European countries, using malware that affected both PCs and bank customers' mobile phones, it must also rank as one of the most sophisticated thefts ever discovered.

But the most worrying aspect of Eurograbber was that it worked within banks' existing two-factor authentication security, so that – from the banks' viewpoint – the fraudulent transactions appeared perfectly legitimate. This helped Eurograbber to remain active and undetected for months. So how was it able to do this?

The key to Eurograbber's success was that the hackers behind the attack had an in-depth understanding of how both consumer and business online banking systems work. The attack specifically targeted the two-factor authentication method using one-time passcodes sent by SMS to mobile devices, and relied on intercepting those text messages so that legitimate passcodes could be exploited.

Attacking on two fronts

What the attackers did was to develop a two-stage attack. The first involved infecting the customer's PC, and phishing their details. This was done by transparently infecting the customer, using either a phishing e-mail with a malicious link, or by surfing to a malicious link on the web. This downloaded a customised version of the well-known Zeus Trojan onto their PC.

Then, when the bank customer accessed their bank account, the Trojan woke up and launched a fake version of the bank's web page, containing instructions for 'upgrading' the user's online banking system. As well as asking the user to re-key account numbers and other bank details, it requested their mobile phone details. The page then instructed the user that in order to complete the upgrade, instructions would be sent to their mobile by text.

This was the second stage of the attack. When the user received the text, which appeared to be from their bank, they were directed to complete the 'banking upgrade' by clicking on a link. However, doing this caused the Zeus in the mobile – ZITMO – Trojan to be downloaded. If the user had a BlackBerry, Android or Symbian phone it was infected.

This completed the circle of infection for the user's PC and mobile device. From then on, every time they accessed their bank account online, the attack initiated a transaction to transfer money out of their account. This worked by the Trojan on the PC recognising that the user was accessing their account, and sending a request to the bank to transfer an amount of money to the attacker's 'mule' account.

When the bank received that request, generated the transaction authentication number and sent it via SMS to the customer's mobile device. This was intercepted by the Trojan on the mobile. The Trojan then, extracted the TAN and sent it back to the bank to complete the illicit transaction.

The fraudulent transactions were completely invisible to customers, as they didn't see the bank's SMS messages on their mobile phone. And to the bank, they looked like legitimate transactions. The attackers even configured the Zeus trojans to restrict the amount transferred in each transaction to a percentage of the account's balance, helping them to remain undetected.

So what security lessons can be drawn from the Eurograbber attack? It was certainly successful in exploiting out-of-band authentication methods, in which a one-time passcode is created and sent to a mobile device, which are quite commonly used.

While banks that use other authentication methods were not vulnerable to this specific attack, it highlights the fact that exploits can be developed to target specific authentication systems – and that attackers have the patience and resources to do so.

However, it also highlights the critical role that online banking users themselves play in security. Eurograbber targeted customers, not the banks themselves. So the best protection against possible future attacks like Eurograbber is to ensure online banking customers have up-to-date protection on the network that gives access to their bank, and on the PC they use.

It's worth reiterating to users that banks should never send an unsolicited email, and so any they get will be phishing mails. Users should be encouraged to use up-to-date antivirus software and a firewall on their home PCs. Cost is not an issue here: there are free solutions from ZoneAlarm and others that deliver protection matching leading paid-for products. These solutions will detect variants of the Zeus Trojan before the user's PC becomes infected. Another key preventative measure is for users to regularly install software updates on their PCs.

There is no 'silver bullet' solution that protects against cyber-attacks like Eurograbber. It's a matter of ongoing vigilance, and ensuring that the security protections used by banks and their customers are as comprehensive, and as up-to-date as possible.

Check Point, together with Versafe, discovered the fraud

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Osborne drags UK financial system kicking and screaming into 12th Century

George Osborne, the UK Chancellor of the Exchequer, may be a here-today-gone-tomorrow politician, but the essential working of his office goes on as it always has.

Last month just a day after Osborne vowed to drag the UK payments systems into the 21st century by, er, improving cheque clearing times, a ceremony dating back to the 12th century was getting underway in the City of London.

The Trial of the Pyx involves making sure that coins produced at the Royal Mint are "within the statutory limits for metallic composition, weight and size". This is done by dragging about 50,000 coins, one from every batch of every denomination put aside during the preceding year, from the Royal Mint to the Assay office of the Worshipful Company of Goldsmiths in the City of London.

Once there, the Queen's Remembrancer summons the jury, made up of members of the Goldsmith's Company, and they start counting and testing. The day job of the Queen's Remembrancer, you'll be aware, is being the most senior judge in the Courts of Justice, so this is a proper court of law.

The whole business, as is fitting, takes about two months, after which there is the Delivery of the Verdict. This is also presided over by the Queen's Remembrancer and attended by the Master of the Mint.

Guess who the Master of the Mint is? That's right: the Chancellor of the Exchequer, a post currently held by that thorough-going bank moderniser, George Osborne. ***BT***

New York technologists most upbeat about job prospects – but not bonuses

Technologists in financial services are the least loyal to their employers, even though they also have the worst perception of the economy and of their employment prospects.

A survey of financial services workers in London, New York and Singapore by recruitment consultants Selby Jennings found that those working in technology are "the least likely to remain in their role regardless of the current economic issues".

The New Yorkers are the most optimistic in the financial technology world, with 23% saying that they think their prospects for promotion are getting better, while 35% said that employment prospects are improving against 17% saying they are worsening.

In London, the balance is gloomier: 5% think things are getting worse on the job front, against 2% who say it is getting better. In Singapore, the techies – and almost everyone else – are very gloomy about the employment situation.

"New York is one of the most buoyant markets for technology, with many organisations looking to drive competitive advantage by making key hires across all levels of seniority," said Clare Cooper, head of technology at Selby Jennings.

The New York techies are the most negative about their bonuses, though, with 24% saying that they expected less. Only those working in fund management were more pessimistic, with 27% saying things are getting worse. New Yorkers are also more concerned about their bonuses than their salaries.

Across all three locations, the most optimistic group are those working in risk management and analytics, while those in sales and trading are the most negative. ***BT***

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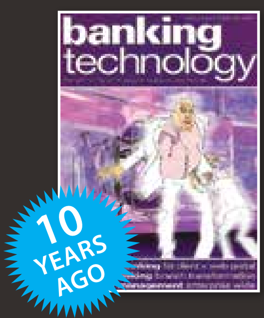

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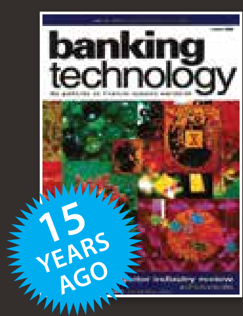

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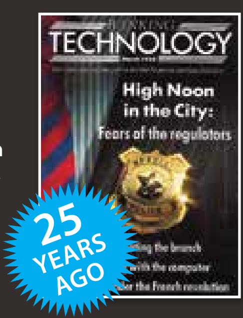

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RISK DATA AGGREGATION
As the FSB starts to check on firms, the unknowns are starting to become known

FATCA: JOINING THE KYC DOTS?
FATCA can be covered by the same prgrammes as KYC, AML and other regulatatory obligations


Finding a route between regulators

It has been clear for some time now that some of the regulations coming into force around the globe contain contradictions and inconsistencies. A large part of JWG's work has been in identifying these, working out their impact on systems and processes and what issues are thrown up.

In general, these are issues of detail and definition (or, rather too often, a lack of definition) and it can be the case that where two requirements are in conflict, satisfying the most onerous of them will satisfy the other by default.

That's not going to be the case with the conflict between the US Foreign Intelligence Surveillance Act and the European data privacy and data protection proposals.

In a nutshell, the US wants to be able to see all the data there is about everything, and the European Union thinks that there is a human right to privacy – including the "right to be forgotten", which sounds like a nice idea.

Sidestepping, for the moment, the fact that the rather ugly rationale behind FISA is to give the US government the right to snoop for political purposes, the practical implications are enormous. In order to comply with EU law, data has to be protected, so anything that touches the US would be non-compliant, presumably.

Cloud and virtualisation issues around data protection and security have long been issues for the financial services industry, but they are about to get a whole lot worse. What about a US bank operating in the EU, storing customer data on its private cloud? Will it have to split the data, somehow? FISA covers non-US citizens and the EU legislation covers non-EU companies.

All of this will require a close look at data structures and data-handling procedures. The potentially good news is that so will most of the other regulations, and there is potential for that fabled thing, a holistic approach to the problem.

The requirements of FATCA, AML and KYC regulation are close enough for this to be a no-brainer, though more than 70% of firms don't seem to have noticed, preferring to treat FATCA classification as a stand-alone issue.

Perhaps they've spotted a way to get round the FISA/EU conflict by doing that, but we're not convinced.

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JWG Making sense of financial services regulation

Data protection: the next Y2K?

Conflicting demands of European data privacy and US intelligence gathering legislation are coming together to make the issue a serious problem for banking technologists

Transatlantic friction over data protection isn't exactly a new problem – the industry has been faced with pending regulations from the US and EU for over a decade.

Until recently it has been possible to ignore these developments, or at least wish that they did not apply to the banking industry or their data providers. However, new proposals from the EU may well bring the long-simmering pot to boil over and it's time to take these issues seriously.

With EU fines of up to 2% of global financial turnover for breaches, professionals should examine the changes, costs and upgrades to their operating models and supplier contracts today.

The heat began to rise again in December of last year when the Obama administration gave everyone a quiet Christmas present, in the renewal of the Foreign Intelligence Surveillance Act. FISA gives US authorities, including the National Security Agency, FBI and CIA, the ability to delve deep into the data mines of cloud and data providers containing the files of non-US citizens without any public warrant for, broadly defined, 'political purposes.' This means that, if you live outside the US but use US based companies, your data can be freely inspected by US-authorities. If the data centre provider is incorporated in the USA, your data can be turned over to the US authorities, even if the server is physically based elsewhere. The plot thickened when it was publicised by Microsoft that loopholes in the current EU data protection rule offer no protection.

In mid-February, Brussels let it be known that its data privacy gloves were off, and that it was going to take a bold new direction. Viviane Reding, the EU Commissioner for Justice, reiterated that "data protection is a fundamental right in Europe" and asserted that "exempting non-EU companies from our data protection regulation is not on the table." Recent European legislative developments certainly support this statement, explicitly stating loopholes will be closed. In other words, a big step up for data protection is in the works.

The Directive, 'To ensure a high common level of network and information security', and the Cybersecurity Strategy of the European Union released in February, aim to complement and supplement the pre-existing Data Protection Regulation. Taken together, this data privacy 'suite' has not only a purpose in Europe, but also globally to "promote the fundamental rights and EU core values abroad".

The Directive outlines onerous requirements for "market operators", defined "non-exhaustively" as banking/credit institutions, financial market infrastructures, e-commerce platforms, cloud computing services and application stores. They must report breaches to the national authorities, at the same time providing documented security policies on how their networks and information systems are secure. If firms get this wrong, as with the data protection regulation, they may be fined up to 2% of their global turnover for breaches and potentially have their transgressions made public.

As if this wasn't enough, firms still have the looming Data Protection Regulation to implement. Due to commence from 2014, but more likely to take hold in 2015, it defines data protection as a "human right" and includes the "right to be forgotten". These aren't small asks, requiring firms to inform clients, or 'data subjects' of the legal reasons for their data processing, and to appoint a data protection officer to oversee the process.

The bottom line is that this is very different from previous data protection BAU and firms need to re-examine how the business controls not only email, social media and personal computing, but also payroll, sales and marketing, AML and, yes, even regulatory reporting.

What is likely to change? Firstly, data management controls, monitoring and record keeping strategies will need to be revisited.

On top of this, firms are going to have to assess the impact of notifying these data subjects of what exactly is being done with their data, and the burdens on their systems – not only to report this, but also to maintain it. Most importantly, firms will have to ensure the integrity and security of data transfer to foreign jurisdictions, including maintaining appropriate data for required periods, and instituting rectification and blocking procedures.

Europe's regime is by no means settled yet, but it will quickly become a reality. Though politics, lobbying and transatlantic friction will undoubtedly still shift this landscape, firms need to figure out what the implications of EU data protection regulation might mean for their suppliers, contractors and customers, especially when their data is maintained by a US supplier, crosses a US border or is held by a US subsidiary in the EU.

If you haven't started looking at this one yet, it's time to put your antennae up and start scoping the size of what could be as big as another Y2K. Stay tuned …

TOP TWITTER ALERTS

- Transatlantic data privacy showdown looming? EU Justice Com: exempting non-EU companies from data reg "off the table"
- Privacy Law Identifier? CFTC no-action relief for LEI reporting notes conflict between transparency and data protection
- Banks step up possibility of united front to sift through bank data to catch hackers – data privacy implications?

KNOWN UNKNOWNS

- How will the EU's new stringent data protection rules apply to non-EU institutions?
- Will transatlantic political rifts over data protection accelerate the adoption of EU data protection rules?
- When will fines begin to be levied for data protection breaches in the EU?

THEMES

- Data protection regulation now looks certain to affect the banking industry, including some financial market infrastructures
- US and EU friction over data protection regulation could mean radical changes to operating models and supplier contracts
- The EU's new 2% turnover penalty will reshape the global data protection agenda.

Outsourcing: increasingly risky business?

More stringent restrictions on outsourcing arrangements affecting all suppliers could lead to increased costs across the board for financial services firms

Since the 1980s, outsourcing has been a way to leverage global wage imbalances to lower the cost/income ratios of the banking industry. The rules of the game changed in 2007, with MiFID controlling how outsourcing should be done. However, few outsourcing relationships have come under scrutiny – until now.

In 2008, the financial crisis hit, and outsourcing once again came into regulators' sights as an obvious source of operational risk. The bottom line is that more stringent restrictions require a deeper level of engagement that could lead to increased prices.

This is not just a problem with your Indian or Russian technology houses. This affects all suppliers – including the large firms that provide custody services, depositary functions, payments and the like. The FSA has recently brought the increasing importance of this issue to the fore, writing a 'Dear CEO' letter to multiple asset managers to assess if they have contingency plans allowing them to continue business during the failure of an outsourced function.

What does this mean? Since MiFID there have been notable differences: firstly, what might have historically been OK to outsource may no longer be permitted to go to a supplier. Secondly, if that supplier resides outside the EU, greater controls may be required. Finally, and perhaps most importantly, the firm must hold suppliers to account for new requirements like data protection, business continuity planning, data centre locations, record keeping and reporting.

Will MiFID II/MiFIR radically change the game? Probably not. The outsourcing requirements under MiFID look to remain unchanged. That means a MiFID-authorised firm may continue to outsource non-investment functions, provided it takes the same 'reasonable steps' to avoid undue operational risk and ensures its ability to monitor compliance is not inhibited. Given the continuity of these requirements, it seems unlikely that we will see any sudden change in enforcement practices.

However, the incoming technical standards could well give firms more to worry about when they are released next year. For the present, the existing standards place a number of heavy requirements on firms.

For a start, they forbid the outsourcing of management functions, or any function where its outsourcing would affect regulatory compliance or client relationships. They also require that the third party service provider be able to deliver a "professional" service and make full disclosure of their regulatory compliance as well as permitting supervisory oversight, such as on-site visits, to be carried out. The Level 2 requirements also affect the contractual document itself, specifying that it must include SLAs and be terminable with minimal disruption to the service.

The big changes in 2013 are being driven by the European Parliament's passage of EMIR, which extends many of the MiFID requirements to CCPs, and global adoption of Recovery and Resolution Plans. Both initiatives raise the level of scrutiny and responsibility for outsourced CCP functions. In a nutshell, outsourced functions must be run to the same standard as those run in-house.

Now is the time for firms to run an analysis of organisation-wide service provision. In doing this, financial institutions should take account of the EU's definition of outsourcing: "an arrangement of any form between an authorised entity and a service provider by which that service provider performs a process, a service or an activity which would otherwise be undertaken by the investment firm itself". With this in mind, firms should take a broad approach as to what counts as outsourcing, ignoring how relationships are currently classed and asking how they appear objectively.

For service providers engaged by both investment firms and CCPs, the picture gets more complicated. Faced with differing requirements, the issue becomes how to bridge the gaps between MiFID and EMIR in order to make compliance cost-effective. To resolve this, many firms will seek to find common standards. In most cases this will mean taking the greater requirements of MiFID and applying them to both critical and non-critical functions.

Regulatory eyes will continue to be increasingly vigilant of firms' outsourcing arrangements. UBS's £30 million fine last year confirms this, with the Swiss regulator, FINMA's, report saying that the bank's India-outsourced systems to track deferred settlement trades contributed to failings that resulted in a £1.4 billion loss.

Want to avoid being a target? Better contact your procurement department soon …

TOP TWITTER ALERTS

- Dear CEOs: FSA asks asset managers to find out if their back-office outsource providers have operational contingency plans
- Customer data reviews req? AMLD expands PEP def, harmonises calculation, new disclosure reqs for beneficial ownership
- Now asset mgmt RRPs? FSA consults asset mgrs to review outsourcing arrangements as part of #RRPs push for AM industry

KNOWN UNKNOWNS

- How will EMIR and the forthcoming MiFID II technical standards change the model for provision of outsourcing for front and back-office services?
- Will the industry see forthcoming legislation include specific penalties for poorly managed outsourcing arrangements?
- How will firms reconcile the risks controlled by trading regulation with the critical functions described in living wills?

THEMES

- The definition and scope of what is defined as 'outsourcing' has changed
- Improper outsourcing can result in a loss of authorisation requirements or potential fines
- Firms need to begin engaging with their suppliers about what changes to EU outsourcing regulation might mean for their contracts.

Risk data aggregation: the great unknowns revealed?

The Basel Commitee is planning to start checking on firms' risk data aggregation plans from early 2013 but awareness surrounding the issues remains low

In 2009, the G20 committed, in their action plan, to strengthening risk management controls and policy principles. This was followed up with a 2010 report by the Senior Supervisors Group (SSG), highlighting poor IT infrastructure practices which were having a negative impact on risk data. During the Olympics, the BCBS sprang into action with a consultation paper entitled *Principles for Effective Risk Data Aggregation and Risk Reporting*. This paper received only nine responses but it was adopted with minimal changes and the final principles issued in January.

The BCBS expects firms to implement these measures in full by the beginning of 2016 "at the latest". However, if that comes as a shock, they are also planning to begin checking up on firms from "early 2013" (i.e., pretty much as you are reading this) to make sure that implementation goes according to schedule.

JWG research has identified four big capabilities that require significant upgrades.

Firstly, governance: both the board and senior management will be required to explicitly consider risk data issues and set the firm-wide agenda. In this regard, firms will have to think about how they introduce leadership of material data issues without overburdening themselves. Not only will a data officer need to be hired, they will need to be given the support required to do the job.

Secondly, new policies and procedures will have to be implemented, such as formalised SLAs, internal and external reconciliations and alignment across the firm of how data is provided during a crisis – including business continuity.

Thirdly, improvements will have to be made to existing data architecture. The requirements call for new functionality, more automation and better cohesion across departments and risk data types. For instance, firms should be moving towards a "single authoritative source for risk data" within their organisation – for each type of risk – which is flexible enough to meet *ad hoc* requests from both colleagues and supervisors. In a surprisingly granular principle, regulators have called for a common dictionary with consistent data definitions and a taxonomy that includes the metadata from across the group.

Finally, the new principles tackle one of the biggest industry elephants: the way in which end user controls are put in place for spreadsheets.

With no explicit technical specifications, or further regulatory documents, due in this space, firms will have to interpret the 'so what' and create internal guidance. At this juncture, it is unclear how much appetite there is for external guidance – but there is a distinct opportunity for the firms to define 'what good looks like'.

Some of the problems posed by these principles could well help the industry come to a consensus on *de minimis* practice soon. For instance, the problem of singular counterparty identifiers, which is slowly being brought to a conclusion, could be expedited by a statement from the risk community that they require it.

What should be in the budget this year to get the programme moving? A lot. In 2011, McKinsey and the International Institute of Finance estimated that a mid-sized firm would spend between €35 and €45 million on IT and operations in order to comply with new risk data requirements. Then add the caveat that outlay would increase should the Basel Committee for Banking Supervision consultation result in stricter demands for firms – which it did. The report also said that, on average, investments of approximately $390 million would be required by each firm to continue its journey toward the target state over the next five years. This represents roughly a 46% increase in the average firm's current spending on risk IT and operations. Clearly, efficiency savings will have to be made.

Most worryingly, the BCBS Principles seem to have come in largely under the radar. There is a distinct lack of noise surrounding the issue, and awareness among professionals is relatively low.

To be Rumsfeldian, we have unknown unknowns in our midst. What are the workstreams that should be running now? Which milestones are on your critical path? What targets will you set for 2013 and who will set them?

With hundreds of regulatory change projects active in any one firm this year, it's time to see what you are already doing to improve your risk management programme.

The reality is that the BCBS Principles are part of a much larger regulatory movement towards enhanced supervision of all stages of risk monitoring and management – and eventually all functions within a bank. These principles are a good way to get moving and rationalise the totality of the impact of regulatory reform.

TOP TWITTER ALERTS

- Smarter way to look at risk data req: OFR calls for "agent-based" risk modelling to chart amplifying feedback effects
- Questions remain; time for industry guidance? BCBS issues final risk data aggregation principles & JWG's CP response!
- ESMA issues final #AIFM remuneration guidelines; incl remuneration committee "unfettered" access to risk mgmt data:

KNOWN UNKNOWNS

- What does compliant risk data aggregation look like?
- What is on the critical path to success? How are current regulatory reform efforts helping or hindering progress?
- What will firms need to solve internally, and what will need industry collaboration?

THEMES

- The principles require 4 robust capabilities to be defined in 2013
- There are real synergies in getting the programme right across the group
- Work needs to start now, the regulators may be knocking soon …

FATCA: joining the KYC dots?

FATCA compliance might not need a separate programme – it ought to be covered by the same approach as AML, RDR and KYC regulations, among others.

The recent high profile decision by the board of Wegelin, Switzerland's oldest bank, to close after helping US citizens evade taxes of $1.2 billion in offshore holdings, has ensured that Foreign Account Tax Compliance Act is on the 2013 compliance agenda for all. But how big a deal is it?

It's no secret that complying will be confusing, difficult and costly. However, if we look at the FATCA requirements in the larger context of EMIR, AMLD IV, the FTT, MiFID and the Retail Distribution Review, we see that similar requirements can be delivered by one thematic programme.

While the implications are not exactly the same, in general they require dynamic, flexible client data systems that can produce reference information to the granularity required by regulators.

Even though FATCA is the first regulation of its type requiring KYC upgrades of this scale, it certainly won't be the last. EMIR offers strong examples of how these demands are not unique to FATCA. For instance, the classification demands for non-financial counterparties under EMIR require systems that can differentiate between financial (FCs) and non-financial counterparties (NFCs).

We were therefore surprised to see a recent Fenergo survey showing that 71% of firms are building new FATCA classification solutions and engaging in extensive data mining to identify US clients.

Customer data quality and maintenance is central to complying with FATCA. Identification of whether or not a customer can be considered 'US' means customer data systems will have to trawl through the entirety of their customer accounts for US 'indicia'. Passports, place of birth, addresses and even residence information will have to be checked, while any incriminating 'US' data must be assessed, verified, and reported. New linkages between customer data systems will be required to adequately ensure the entirety of your customer data is fit for purpose. Firms will need to be able to prove that their data, showing an account for John Smith, who is a US citizen by birth and citizenship, but not a resident for tax purposes and, thus FATCA exempt, is accurate.

If a piecemeal, regulation-by-regulation approach is taken to managing client data, firms will be forced to self-certify each requirement, leading to an increase in costs, suboptimal solutions and annoyance for the customer. In the instance of FATCA, this means physically contacting each client to find out if they are a US or non-US citizen, updating and 're-papering' these records, causing customer dissatisfaction and creating data that is costly to refresh.

With the final US regulations having been released in December, and HMRC publishing its draft regulations and guidance in January, the industry now has line of sight as to what exactly needs to be accomplished. But, there is still very little detail on the report formats, the registration requirements and the transmission protocols – and that remains a pressing concern. However, key provisions that would have required wholesale customer self-certification have been softened to allow firms to 'pre-classify' identified accounts. But, despite the additional detail the problems remain the same: FATCA requires a big step up for the management of client data.

Having set the reporting deadline at the end of this year, the IRS is pursuing bilateral intergovernmental agreements (IGAs) with 50+ countries, exempting firms in those countries from reporting client information directly. Differing bilateral standards have led to divergences across borders and, with over 37 possible FATCA account classifications now in existence, tracking data in this way is a new and tall order for any firm's KYC framework. This is especially true when operating across multiple jurisdictions, and with requirements for both high and low levels of detail. Client systems must be able to judge whether their counterparty participates in a FATCA IGA, is 'non-financial' or is US based. Not being able to make an accurate classification may mean being forced to apply the FATCA 30% withholding tax.

The real difficulty here is in linking your databases to identify and maintain this information, something never before required to this level in other regulations. While providing 'single customer views' across regulation is nothing new, adding fields for tax tracking purposes is. Not only must this data be linked across a domestic institution, but also across borders and group levels. For instance, firms that fall under the same national IGA are no longer 'foreign' to each other and consequently do not have to report to the US. This means that if firms are trying to get a single FATCA view of a customer across a group, systems must be aligned.

There are plenty of unknowns to be discovered, and we won't have all the answers this year. Regardless, joining the dots now will pay big dividends to your future KYC agenda. Who knows, it might even be good for business.

TOP TWITTER ALERTS

- Many gaps left! HMRC releases new #FATCA implementation doc: registration format, data submission protocol missing
- Customer data reviews req? AMLD expands PEP def, harmonises calculation, new disclosure reqs for beneficial ownership
- EMIR back on schedule! Issues to be ironed out by further "guidance". But will this help simplify implementation?

KNOWN UNKNOWNS

- Can regulations with similar KYC demands, such as FATCA, EMIR, the FTT and AMLD IV, be addressed by the same compliance programme?
- How will firms link their databases to maintain granular regulatory client data demands?
- How much time will be given to firms to implement the final provisions of FATCA in advance of the 2013 reporting deadline?

THEMES

- Customer data management requires a renewed focus under FATCA
- Firms should look to coordinate FATCA implementation with other regulatory regimes' impact on KYC
- Despite FATCA deadlines looming, many questions over fundamentals, such as reporting formats and registration requirements, remain