



# The future of payments

Changes in regulations and technology have created a new landscape in payments, but as our panel reports, there may be more challenges to come.



## Attendees, left to right:

**Tero Pollanen** (TP) 41st Parameter, ex-counter intelligence and electronic warfare expert  
**Simon Barrows** (SB) Lloyds Banking Group  
**Parth Desai** (PD) president of Ace Software Solutions  
**Guy Pantall** (GP) JP Morgan  
**Jeremy Cheetham** (JcM) Global Email Company  
**Douglas Soon** (DS) Standard Chartered Bank  
**David Hannam** (DH) Fujitsu

**Paul Smee** (Chairman) (PS) chief executive of the Payments Council  
**John Chaplin** (JC) First Data  
**Ruth Wandhöfer** (RW) head of payments strategy & market policy, Treasury and Trade Services, Citi  
**Peter Cremona** (PC) business development director for Dovetail  
**Dave Birch** (DB) director of Consult Hyperion, chairman of The Digital Money Forum, Visa Europe Research fellow in innovation in payments at the Centre for the Study of Financial Innovation

**PS** Good evening. At the moment we have a series of framework changes – regulatory through the Payment Services Directive, strategic through the national payments plan, quasi regulatory/market through the Single Euro Payments Area. How do we respond to the challenge?

**DB** I'm generally quite negative because I don't understand what the goal is. At the moment all the targets seem to be random; some MEP finds out that he can't use his Finnish debit card on his Greek holiday and all of a sudden everyone is up for a £10 bn investment.

**JC** I think there was a plan, but it wasn't very well formed and it wasn't particularly well quantified. There was a plan and I think it's been lost.

**PS** Maybe what we should take from

these frameworks is that payments matters. If you don't have a European sweet industry it doesn't really matter – apart from Yorkie Bars, which obviously have to be protected – but the point with payments is that it touches everybody.

**PC** I might add that a lot of the authorities outside Europe are very interested in what PSD and SEPA will do. So I think, that the rest of the world are looking to the EU to see if we are going to do it right. I think the main problem with new initiatives and trying to push new unified standards result in changes that banks have to make in their systems. So the challenge for the banks is how quickly they can apply the changes that are being forced on them; and continue to do business because ultimately that's what it's about – offering better services.

**PD** The initiatives are good, but built from a point of view of creating a commercial level playing field. Now we're seeing that banks are part of the infrastructure for the economy or for the country.

**RW** SEPA is there to harmonise and make things easier. So if everything were to happen at the same time: you have one currency zone, (let's say everyone had the euro); if we have around one or two permanent clearing providers; we have one standard to operate on; well, then we can compete in that area. That was the idea, but because of all the legislative interference we could only launch one scheme which almost existed before. I think if SEPA could have been developed by banks – in the absence of any regulatory barriers – the project would be a success.

## ROUNDTABLE: PAYMENTS



**PD** Faster payments are a good example. There was a clear cut direction and a good deadline and it got done. The technology now exists!

**GP** Are we not saying that we feel that if the industry were to do this on its own it would be a business driven approach? I think the issue is we're all still trying to understand it whilst it's rolling.

**SB** It's a huge cost for banks to introduce all these regulatory changes and it isn't something we can do very quickly because there's usually a long lead time during which the regulations are interpreted and the banks decide how to respond. There is a significant risk we just spend all our time trying to interpret and implement all these various potentially conflicting regulations, and what is the end product? If you ask the customer he or she wouldn't really understand what is going on or what the benefits are.

**PC** Ruth's point is a good one in terms of the ultimate aim is to have a harmonised way of making payments anywhere in Europe, both domestically and across borders; you know what you're going to pay and you know how to do it, and the standardisation also enables banks to actually start offering standard services.

**PD** Banks don't always want to offer standard services? The standards have to be there for communication, but then you offer valued added services, and differentiate yourself from others. That would be the only way to succeed.

**JC** The biggest opponents of standardisation are the entrenched providers. In some markets where competition is not strong, I would argue it's been a very profitable franchise and there's not been that much interest in expanding it.

**DB** But that can't be the right explanation of the dynamic because the average merchant service charge paid by

retailers has gone up because all of the low cost domestic debit schemes have been abandoned.

**JC** That's a different issue. The issue is why did somebody decide to do it, because the market clearly wasn't doing it on its own. Look at faster payments – would the market players have come up with faster payments all on their own?

**JCm** They would still like to keep your money for four days!

**JC** Look at how the card market is in the US. The counterintuitive reaction to Wal-Mart was to increase the charge to retailers, not to decrease it. So the thing doesn't work. However, I would argue that the regulators have stepped in and then did a bad job. They weren't wrong to step in, they diagnosed the problem correctly, but then they only listen to some of the players. The banks don't run the card business alone – much of the processing is outsourced to outside providers and retailers have a major role as well. If they can't support a service, then a bank can't do it either.

**JCm** The banks have outsourced to providers. If you want good design, you have to involve the people.

**PC** Could it be the banks were not prepared to pick up the costs perhaps? Could that be the reason they were the main body that were consulted?

**JC** I think the decision structures of the industry no longer reflect the actual operating model. A lot of the business has been outsourced and this has a real impact on who needs to be involved in decisions

**PD** Looking directly at the current situation, people know that banking is part of the infrastructure and they should just make SEPA as part of the bail out plan for the banks.

**PS** A deep philosophically held view of mine is that if you're confronted by a regulator, try and understand where

they're coming from and then grab the agenda. I think if you look at faster payments the Regulator wanted a same day service – BACS but a bit quicker! If we'd given them that, nobody would have been interested. Faster payments actually took us forward a bit to real time retail payments, but that was the banks that drove that – it wasn't the Regulator who said you've got to do real time.

**DB** So is the summary that actually the net welfare of the EU is not improved one iota by SEPA or PSD and everything else, but it could have been had circumstances been different?

**RW** But it's still work in progress. I think if we look in 10 years time it could be a very different situation. Almost everyone will be a euro country and you will have more innovation and value added.

**GP** But what would be the tipping point to get from where we are now to there?

**RW** I would say the ECB or EC.

**GP** So you think it's going to be regulated?

**RW** I think that would be the only solution.

**PD** So you think the European Commission will set a date?

**RW** Somehow they will do something, and we are pushing them to do so.

**PD** The banks?

**RW** Well, I'm pushing them!

#### Of security and child benefit

It's really important that you look at multiple channels and not trying to find one solution for one of your payment channels, but also looking hard as well to your future channels. I would think chip and PIN for example, has fixed one problem, but enabled other problems.

**PS** Do you feel that there is a solution



out there, or is it always going to be multiple solutions to different problems?

**TP** There is one solution: not using the internet. But if you want to do online transactions, you compromise from that point and then you are talking about usability. Do you want your users to donate blood to the screen before you are able to do a £10 transaction? Of course you don't! Then we have to go looking into what would be more feasible. I don't personally believe that biometrics should be used as identification for online transactions because online was never meant to be used that way, no one put in the requirement when it was built. Before Web 2.0, we just need to find some kind of solution to mediate those risks, but also keeping in mind the customer experience.

**DS** I'm a biometric fan. Malaysian passports have a biometric chip. Driving licences, ATM cards; credit cards too and security has been pretty good.

**DB** I think Malaysia could well illustrate what's going to happen in the UK: everybody in Malaysia has an ID card with biometric, but virtually nobody has a reader, so as a consequence there's a colossal industry in bogus ID cards because nobody can tell whether the card is real or not.

**DS** There are readers on the borders.

**DB** True there's a few readers at the borders, but Malaysia is interesting from another point, which I don't think really has been picked up in the UK yet, there are already two large petrol chains where you can buy petrol using your ID card. If I was Tesco, the day that ID cards come out in the UK, I would say to people come down to Tesco, bring a blank cheque for us to scan and from then on you can just pay with your ID card.

**JC** Yes, but David, I know somebody who actually tried to sell that to a major supermarket. The fact was, when they looked at it, they said wait a minute, we're within a sniff of getting our debit card

transactions for nothing anyway so we're not willing to pay you for a service at all because we think we're actually winning the game with the Regulator – we're about to get the whole payments network for nothing. Maybe they will come back to that when they think they've hit the bottom in terms of getting the best deal they can from the regulators, but I don't think they think they're at the bottom yet.

**DH** The key word is that they've got a strategy.

**TP** One question around that: if you're looking at biometrics, it's a really good idea now while we have a card and are going physically somewhere to authenticate the physical card, but how can you put biometric information online? And how do you transfer biometric information across international borders? And what happens if your biometric information is lost? You can't go and change your fingerprint. You can't go and change your DNA.

**DB** There's a fascinating case study in the newspapers a couple of weeks ago about South Korea where the illegal immigrant brokers have been supplying people with bogus passports which come with a set of tapes to put on your fingers.

**GP** Biometrics may be a staging post, but is it true that all identity technology can be subverted?

**TP** I think that within 10 years we're going to have fewer branches and more internet activity, so we can't just design an authentication strategy or secure an authentication strategy for something we have today, because we know we are trying to migrate to another thing.

**PC** So what you're saying is keep payments and online banking away from your ID card.

**PS** Do you have an alternative then to ID cards?

**TP** I still think that for the security it's

multi-layered. You need to have something in the entrance, but you don't want to make it difficult for your customers to transact payments. If you go five years back, IP verification was something you could do, but unfortunately proxies and organised crime syndicates have started to use more sophisticated technologies. I represent a company that is focused on device recognition, regardless of IP; regardless of who's the user behind the computer. I believe this is something that will have 5-7 years of shelf life, and during that time I hope my organisation will be able to find the next good thing to do.

**DH** If I go back to the 90s when we were trying to decide in the banks whether we were going to go chip and PIN. I mean the debates about usability are exactly the same debates that we're having now about biometrics. It becomes a question of economics as to how bad is it going to be if you don't, and you don't always have the business case exactly nailed to be able to find that out, but it means you need to unwrap the next layer. There does come a point where you won't bother going to the next level because it's that extra percentage that you are not happy to accept is the cost of doing business.

**JC** But it is the iniquity of this thing isn't it? If you're putting something in one market it won't make any difference if you can still use it in the US. Take the Finnish for example, they haven't got much fraud on their debit cards because you can't use it outside Finland. And when you say you go from a local parochial system to a global one, you increase the fraud and the cost.

**DH** Which goes back to the original question about maintaining the integrity.

**SB** If you go into a branch you can commit one fraud. There's a physical limit as to how many times you can go into that branch before you get caught. With online there's no stopping you.

**DB** When EMV started out something went wrong because you all sat round in the committee and said here's the most



amazing technology – the smart card and the chip and the manufacturers have spent gazillions making these chips really secure and blah, blah, blah, so we'll put the payment information in there and then, purely for amusement purposes, we'll put a trivially copyable magnetic stripe on it and we'll make sure we can emboss it so that it can be ripped off – it's like there was a dynamic in the creation of it which was undermining it from the very beginning.

**DH** Yes, but interoperability and the ability to use it outside of the UK were the reasons why all those things stayed.

**JC** I mean, don't blame the UK – start with the French! You know, we're dismissive about it now and say the French card was proprietary technology, but then it was very good in controlling fraud in France, it was after the cards needed to be used outside France that fraud grew. We're just repeating what happened in France.

**DH** It goes back to the whole question of inter-operability and the market area that you're trying to cover and what's the problem you're trying to solve at that particular moment in time.

**PS** I was talking to somebody at a very top end private bank when we were talking about switching off the fallback to the magnetic stripe, and they said, well frankly, the sort of people we're dealing with will get so angry if one day they couldn't use their card in a machine because something was wrong with the chip; and as far as we're concerned it's a business decision!

**DH** And that will always come back to a business decision that will need to be made; either individually or collectively, by organisations based on what they can afford. If you look at today's market place timing is going to be very interesting within the next two years as to what people are going to do.

**DB** If you look at today's market place

then all of the money spent on security since the dawn of banking was completely wasted, because you could never have lost as much money through fraud as the banks lost through their 'normal' operations.

#### **Of customers vs banks**

**PS** Can we look at the relationship between the provider of payments and the people who actually use them? We've referred to the fact that bank branches are shutting, but where else can you see the changes happening?

**DB** Well, the average person in the street hates banks and given any reasonable alternative they would take it; that's the straightforward cultural issue at the moment. If Tesco issued free bank cards to people and said, "put your money in here instead of the bank", we're stuffed.

**PD** Something makes me think that the new generation are going towards mobile very quickly and will use online banking as opposed to cheques.

**SB** People using eBay use PayPal because it's there. It says PayPal, therefore it's to do with payments. It at least gives the impression of being secure and whether it's associated with a bank it almost doesn't matter.

**DB** We associate payments with banks, but the next generation might not. They regard the confluence of banking and payments as essentially a historical accident which isn't relevant anymore.

**DH** They're a credit card generation. And for most of them it is a question: I need to do something; how/what's the easiest way of doing it?

**PS** Perhaps, but Marks & Spencer which, in the mid-90s had a world brand to die for, went into life insurance. You'd have thought they'd have swept the market, but it somehow failed to do as well as that. There was some way in which the brand did not translate into finance.

**SB** Typically brands have an association with something and when they say 'now we do this completely different thing as well', then there's probably less acceptance of that from customers than for a green field. People used PayPal, there was a viral spread and suddenly people realised if they bought or sold on eBay then PayPal was the default and suddenly we banks realised there was a boat there to do with online payments that we didn't even realise that we'd missed!

**DB** Do you think a big part of that is just basically culture and age? It's not people rationally thinking this is the best thing for payments.

**SB** No, not at all. Would PayPal have been as successful as it has been if it hadn't had that natural follow on from eBay? Clearly it wouldn't. It starts with one thing then spreads its tentacles and ambitions, and then suddenly from being one of those niche things that the banks may be aware of but not overly worried about it becomes a serious competitor.

**DB** I use PayPal all the time and if I'm on any website, if I see the PayPal button I will always hit it, because if I see PayPal that means I know all I've got to do is type in one password.

**GP** It's always a challenge for a bank to keep up, and that's down to the business case.

**DB** Banks are so hopelessly inefficient in most things that the business case will never stack up.

**GP** It can, depending upon the bank and the proposition.

**DH** If you think about business cases and one-year pay backs, it becomes a very interesting case.

**JC** How long is the payback for faster payments, just out of curiosity?

**PS** Well, bear in mind that it was a



mandatory requirement, but the cost of the overall central system was just over twenty million. I think one of the things within payments is that better electronic systems do enable you to get rid of some of your costly paper processing too.

**PC** And in trying to replace cheques as we've all been trying to do, faster payments hopefully play a big part.

**PS** As will mobiles, online and some of the other new developments.

**TP** I do have to say that one of our customers is actually happy with faster payments, and that's the fraud community, especially if we're going to start issuing faster payments across multiple borders.

**PC** I was reading somewhere, that one out of eight people that do online banking through the internet forget to log out, and only one in four check that it is a secure site or not. So of those four, they check if it is a secure site, and then forget to log out!

**DB** That's because we don't care! So for example, if I'm logging on to World of Warcraft I'd be really careful to make sure it's the real World of Warcraft site because if somebody gets my password and steals my magic sword that's it, you can't ring up Blizzard Entertainment and ask for my magic sword back. I couldn't care less about logging in to Barclays, because if I log in to Barclays and discover that Ukrainian fraudsters have wired all my money away, I don't care, Barclays are going to give it to me back.

**SB** So if you've got that assurance that if something does go wrong, you can go back to Lloyds, Barclays, whoever it happens to be, and you'll be recompensed, then you will have a much lower concern.

**TP** Is that the right approach from a security point of view? If you teach your customers they don't have to care, they don't care. They don't really care if they have an anti-virus, they don't care to buy

the latest upgrades, and in that kind of way, are we creating a culture that is irresponsible? Using PayPal as an example, it's a success story and because PayPal isn't in the media talking about their fraud losses, banks are seen to be less secure and PayPal's strategy on returning funds is different than banks because they will investigate every case and make a judgment on the case.

**RW** But the Regulator will take away even more responsibility from the consumer, even saying that almost grossly negligent behaviour would still be covered under the consumer protection rules of the PSD, allowing for consumers to be reimbursed for the full amount. Only if you, as a bank, prove that fraud is involved on that customer's side, your organisation will be able to refuse reimbursement.

**TP** There's a problem with online gaming where, because I was a little drunk this Friday evening, I lost €5,000. Will I just call my bank on Monday and say it wasn't me?

#### **Time is money - literally**

**PS** Will relationships change with the new forms of doing payments? People are used to paying for an SMS message. Are you going to be able to charge for payments made via mobile phone because people will just assume when you send a text message or something over the phone, you pay for it?

**PD** I think they will, depending on the transfer of value. For example, in Nigeria they are transferring mobile minutes as part of payment from one person to another. So it's a monumental change. For a new generation they're going to start using the most convenient way, so the banks or the telecom companies will have to justify their charges.

**DB** We're the consultants for Vodafone and M-Pesa, which is by a country mile the most successful new payment product I've ever worked on. In some other countries

where minutes are transferred, one of the key reasons is because they're more stable than the local currencies. You know a minute is a minute, whereas the Zimbabwean Dollar isn't. So that's not some sort of crazy, wacky, technology solution - that makes complete sense.

**SB** Absolutely, the thing is whether in the future people will leap straight to mobile? It's a case of working out what the model is; what that technology is, but also more importantly, what the business model is in terms of all those players in that space - the banks, the network operators, the phone manufacturers. We need to deliver something that's usable and meaningful and, going back to the conversation with eBay and PayPal, there has to be some sort of context in which you can use those mobile payments. Like online banking and use of cards today, you'll look back and think well, how did we ever get by without it.

**GP** Mobiles are all about channel and relevance and the consumer end. When you put a bank in the picture, they start thinking about the risks - it's more of a traditional view of what a payment is. I'm not well-versed in mobile payments, but from what I've seen, it seems that it is a low value, slightly over-simplistic product which has specific relevance to a niche. The companies that produce those mobile payments now won't be able to accept the risk management associated with the kind of payments that the banks make and do it in the same way. So as it grows it will collide with the more traditional skills of the banking industry, and that's when the banks can decide to enter the business.

**RW** The PSD offers the possibility to any business, e.g. a large telecom provider, to obtain a licence as a payment institution under the PSD with very small capital requirements. Such entities are allowed to provide payment services, but not to take deposits.

**PS** I don't think there's anything to stop us continuing the discussion over drinks...