



Don't get left behind: why FIs and large corporates should migrate to ISO 20022 standards

WHITE PAPER

NOVEMBER 2020



Payment systems and schemes around the world are migrating to ISO 20022 message standards as part of modernisation initiatives that typically involve the introduction or upgrade of real-time clearing and settlement infrastructures.

While it's easy to be distracted by speed as the main benefit, greater value can be derived from the standard's robust data and messaging capabilities. The improved structure of ISO 20022 message standards enables the transfer of rich remittance information, which helps financial institutions and their customers to improve operational efficiencies, monitor fraud and risk, and provide other business insights.

The extensible message set also includes a range of non-payment messages such as 'request to pay' and 'credit confirmation' that enable financial institutions to develop new customer propositions. In turn, this generates new revenue opportunities for banks and drives differentiation within a marketplace that is becoming increasingly crowded with alternative financial service providers.

Once widely adopted, the standard allows for interoperability between related industries, and between domestic and international payments systems, helping to achieve greater resource efficiencies and levelling the playing field for competition and innovation.

Hung up on the past

Financial institutions exchange significant amounts of information, both among themselves and with their customers as part of their everyday operations and transactions. Over time, a plethora of different messaging standards have evolved to support different systems.

Maintaining a multitude of standards across different systems is costly, complex, and makes it's difficult to achieve straight-through processing between corporates and their banks. Meanwhile, many of these legacy standards are limited by the amount and quality information contained within the message, which impedes organisations' ability to innovate and ultimately optimise the end user experience.

But these standards have largely persisted because of the significant time and resource investment required to migrate. Given many of the benefits associated with ISO 20022 message standards depend on interoperability between ecosystem players, the commercial rewards tend to accrue over the long-term, and financial institutions can be reluctant to make the first move.

Acknowledging there's a considerable effort involved in migrating to new standards, most operators are allowing for a phased transition from legacy formats and ISO 8583 using a translator. Doing so eases the pressures on financial institutions and large corporates in the short term, but delays them from taking full advantage of the newer standard's potential. With

faster movers already bringing ISO 2022-enabled solutions to the market, organisations that remain wedded to old standards risk being left behind.

Benefits of ISO 2022

When asked about the implementation of real-time payment systems, 100 percent of financial institutions we interviewed agreed that “Modernisation of systems to accommodate modern message standards is crucial to ensuring that the most value can be derived from real-time payments in terms of the ability to leverage the enhanced data to build new propositions.”¹

1. Mastercard-commissioned research among global financial institutions, 2018

The financial benefits of ISO 2022 derive from three key features of message standards:

Interoperable

Implementation of the standard leads to interoperability between players, both within domestic payment systems and internationally.

1. Many large corporates already use the standard, helping them to reduce the number of payment formats they work with. From a bank’s perspective this can help it **reduce the maintenance** costs of working with its corporate customers.

By reducing or else eliminating the need to translate between different standards, the **likelihood of errors is lower**. This **reduces the cost and time** associated with retrieving and collating information that is truncated during conversions and having to be transmitted by other means, such as email.

Common standards enable linkages between different payments systems, thus reducing technical challenges when processing both **domestic** and **cross-border transactions**.

ISO 2022 messages are also available across domains, including payments, securities, trade services and foreign exchange. Since 2010, the development of cards related ISO 2022 messages has boomed. Today, a portfolio of about 60 messages is available, which provide an ISO 2022 alternative to the ISO 8583 standard.

2. By acting as an interoperability hub, ISO 2022 allows payment service providers to **harmonise previously non-interoperable formats**, both across back-office systems and across geographies. This presents an opportunity to **consolidate and rationalise payment systems** (and associated back office systems, such as cash management) as well as external communications platforms.

Global pharmaceuticals company Merck optimised its business performance by deploying ISO 2022 to reduce the 400 bank interfaces it maintained across various countries into one. Today, the company creates just one file output, which includes the payment, payment information and instruction, value and country, which it submits to the relevant bank for processing.²

2. ‘The five numbers that can make payments more efficient’, Finextra, 2017

3. 'Costs and benefits of migration to ISO 20022 in SEPA', Europe Economics report, 2016

Consolidation and rationalisation of systems helps to **streamline internal processes** and **improves time- and cost-efficiencies**. According to a study by Europe Economics of SEPA's ISO 20022 implementation, while overall it noted a mixed bag in terms of time and cost efficiencies among parties – 19 percent and 23 percent of payment service providers and users said they had significant reductions in transaction processing time and costs respectively.³

3. A common standard used widely around the world makes it easier for software providers to the industry. This gives financial institutions and corporates a **wider choice of off the shelf products** that can be easily and cheaply integrated, thus avoiding costly legacy builds.

4. Interoperability **promotes competition**. The presence of common rules and standards with ISO 20022 levels the playing field between existing providers and supports market entry by new service providers.

Structured

The structure of ISO 20022 messages improves the quality and accuracy of data exchanged between financial institutions.

1. ISO 20022's structure allows for easy consumption of data by business IT systems. As a result, it **increases rates of automation** and **straight-through-processing**.

In 2004, the securities industry migrated from the legacy ISO 7775 standard to ISO 15022 (a standard very similar to ISO 20022 and with technically and functionally superior messaging to ISO 7775), resulting in significant benefits to the community. By mandating the inclusion of important processing information, it increased straight-through processing rates for clearing and settlement from 60 percent to more than 95 percent, which translates into billions of dollars of savings on operating costs.⁴

4. ISO 20022 for dummies, 2010

Similarly, with ISO 20022, improved straight-through processing rates can help to shorten cash conversion cycles, thus **improving transparency of cash flows** and **cash management**. This can translate to **improved liquidity management** and **reduced liquidity risk**.

It also allows for more effective integration of payments information into analytics systems and applications, **resulting in time and cost efficiencies** and providing insights to inform **better business decision-making**.

Additionally, ISO 20022 is capable of carrying more information with reduced risk of information getting lost. More information also means it is easier to identify mistakes.

2. ISO 20022 is human-readable. This means **tracing and solving errors or inconsistencies is simpler**. This transparency also facilitates audit and compliance processes.

Given that global regulators may soon prevent banks from processing international payments if all party information cannot be validated, the structured format of ISO 20022 could help **to ensure compliance** with scheme specifications such as Pay.UK's Confirmation of Payee.⁵

5. 'Introduction to ISO 20022 for U.S. Financial Institutions', NACHA

By providing for transfer of information on originators and beneficiaries in a more structured format it can improve **detection and prevention of financial crime**, such as push-payment fraud and other payments fraud.

3. Use of an extended character set for alphabets and special characters provides **strategic flexibility for future changes**. This vastly reduces costs associated with change management.

Extensible

Extensible message sets provide for transfer of richer information within the payment message.

1. The ability to include remittance information **facilitates reconciliation and other back-office processes**. The ISO 20022 standard may therefore support the transition from paper-based processing, which still makes up over 50 percent of business-to-business transactions. Widespread adoption of the standard could also expedite paper-based cheque elimination in favour of lower-cost electronic payments.

2. Additional functionality of ISO 20022 presents **commercial opportunities** across pre-payment and post-payment activities, such as 'know your customer' solutions or analytics and reporting.

3. Richer messages deliver **richer insights** into customers' payments activities, enabling the development of financial products better suited to user needs. Use cases enabled by ISO 20022 include:

Use cases enabled by ISO 20022

Bill presentment and payment

The 'request to pay' (or 'request for payment') message, which is included in the catalogue of ISO 20022 standard messages, allows a business or other entity to issue a payment request to a customer with remittance information included. The customer simply and securely responds this request, and systems initiate the credit transfer. This reduces the processing costs and risk of error compared to manual capture and processing of invoices, streamlines reconciliation processes, and reduces delays in accounts payable to improve cash flow management.

Digital billing solutions using the ISO 20022 standard request to pay message allows billers to reach Direct Debit rejecting customers and give them greater flexibility and control of their outgoings.

Learn more about Mastercard Bill Pay Exchange, our bill presentment and payment solution, at vocalink.com/billpayments

Insurance claim disbursements

ISO 20022 message standards allow insurance companies to disburse claim payments with automatic reconciliation and an improved, secure user experience. It overcomes the complexities of obtaining and tracking claims related information and reconciling payment information, which reduces delays in settlement and reduces the risk of error handling.

The data standard also enables enhanced interoperability with insurance brokers and claimants by creating a more traceable, secure process, helping all parties realise operational efficiencies.

Learn more about Mastercard Send™, our solution to enable near real time payments to cards, bank accounts and digital wallets at mastercard.com/send

A future-proof data standard

One of the problems with many legacy formats is that they do not evolve to meet changing requirements. This results in restrictions and/or poor implementations of new requirements. Part of the ISO 20022 message standard methodology is that the standards are continuously reviewed and updated.

The current edition of the ISO 20022 standard, published in May 2013, establishes a consistent format conveyed (syntax) and consistent meaning (semantics) for financial messages. This amounts to a single common 'language' for financial communications between parties, including financial institutions, their clients, suppliers and market infrastructures whatever the business domain, the communication network and the counterparty.

In the payment schemes that have made best use of ISO 20022, there is also a regular update process which includes the use of ISO 20022 standards. For example, the SEPA rulebooks, which users have to adopt, are updated every year. This baked-in change process ensures the standard continues to remain relevant and fit for purpose.

It's extensibility also helps future proof the standard as there is effectively limitless potential to the business processes (for example, new payment types, conditional terms, additional information) that can be defined and incorporated in the message.

Migrating to ISO 20022 standards

The benefits of ISO 20022 can range far, but they tend to accrue over the long term. The significant initial investment required in cost and resource, creates a potential stumbling block for implementation, making it difficult, but not impossible, to build a business case.

Legacy back-office processes can delay the implementation of new and improved standards because of the complexity and costs required to update them. But migrating causes less disruption to financial institutions' back office processes than is commonly thought. In many cases of migration from a legacy format, much of the 'plumbing' will already exist – the principal effort will be in adapting to the new message formats and connectivity requirements. Many off-the-shelf products offered by enterprise resource planning, payment platform and gateway software providers already support the standard across the services they offer, thus reducing the total cost of ownership (TCO).

While migration to ISO 20022 involves temporary disruption including IT, training, operational and architecture change, as well as investment, several

notable financial institutions that have migrated report to Mastercard that it was worth the effort.

While planned disruption is expected as staff are trained and IT systems and technology are upgraded and migrated, those who have completed the process have achieved cost savings, efficient time to market and simplification in supported message formats.

ISO 20022 is future-proofed then because it can easily be adapted and reshaped to meet the needs of yet unknown requirements. While it has been possible to do a 'work around' by translating from legacy messaging standards in order to meet modern requirements, only a full migration to ISO 20022 message standards will enable full exploitation of their value over the long-term.

Conclusion

In an increasingly competitive landscape, where both businesses and consumers are demanding new solutions from their financial Institutions, ISO 20022 message standards are greasing the wheels of innovation and competition.

There's no doubt that ISO 20022 delivers operational efficiencies while promoting and supporting the development of value-add products and services for banks, businesses and consumers alike. Additionally, financial institutions that fully exploit the functionality of ISO 20022 can save time, resources, mitigate risk and support compliance while exploiting new revenue streams in the context of a future-proofed standard.

As the shift to ISO 20022 message standards pick up pace globally, those financial institutions that stay wedded to older standards risk being left behind. Not only can ISO 20022 help banks innovate and develop new revenue streams, but it also represents a fantastic opportunity to improve efficiency and customer service.

What next?

Mastercard Advisors has the expertise, experience and assets to support industry participants during the transition to ISO 20022 message standards, including in critical phases such as the development of playbooks (technical, business and operational), and the value articulation of the use cases enabled by ISO 20022. For financial institutions that have already migrated to the standard, our experts can help you maximise its potential.

"Mastercard's experts are very well versed in the ISO 20022 standard; I would argue some of the premiere people in the industry as far as understanding goes. Being able to access those resources and speak to them, as we've designed our standard and our way forward has been immensely helpful."
— Irfan Ahmed, senior vice president for product development at The Clearing House

Contact services.mastercard.com to learn more about unlocking the value of data with ISO 20022.



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