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FUTURE OF PAYMENTS

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Contributors

Jon Axworthy
A journalist, specialising in health, tech, science and the future, with work published in *T3*, *Wareable* and *The Ambient*.

Charles Orton-Jones
A PPA Business Journalist of the Year and former editor of EuroBusiness, specialising in fintech and high-growth startups.

Tim Cooper
An award-winning freelance journalist with work appearing in *The Spectator*, *The Guardian* and *The Telegraph*.

Sally Whittle
A freelance business and technology writer with work published in national newspapers and B2B magazines.

Raconteur

Special projects editor
Ian Deering

Contributing editor
Neil Cole

Commercial content editor
Laura Bithell

Commercial content executive
Jessica Lynn

Commercial production manager
Emily Walford

Production executive
Sabrina Severino

Design and illustration
Kellie Jerrard
Colm McDermott
Samuele Motta

Design director
Tim Whitlock

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B2B PAYMENTS

Now you see it... Can invisible payments work for B2B firms?

The ultimate in frictionless transaction tech has proved its worth to retail businesses, but most companies are still struggling to envisage its suitability beyond the B2C sphere

Jon Axworthy

When you order a taxi via Uber or food through Deliveroo, the act of paying for those services may not even register with you until the next time you check your bank balance. These are known as invisible payments, meaning that the transactions are instant, with no need for the consumer to use a card or enter any account details.

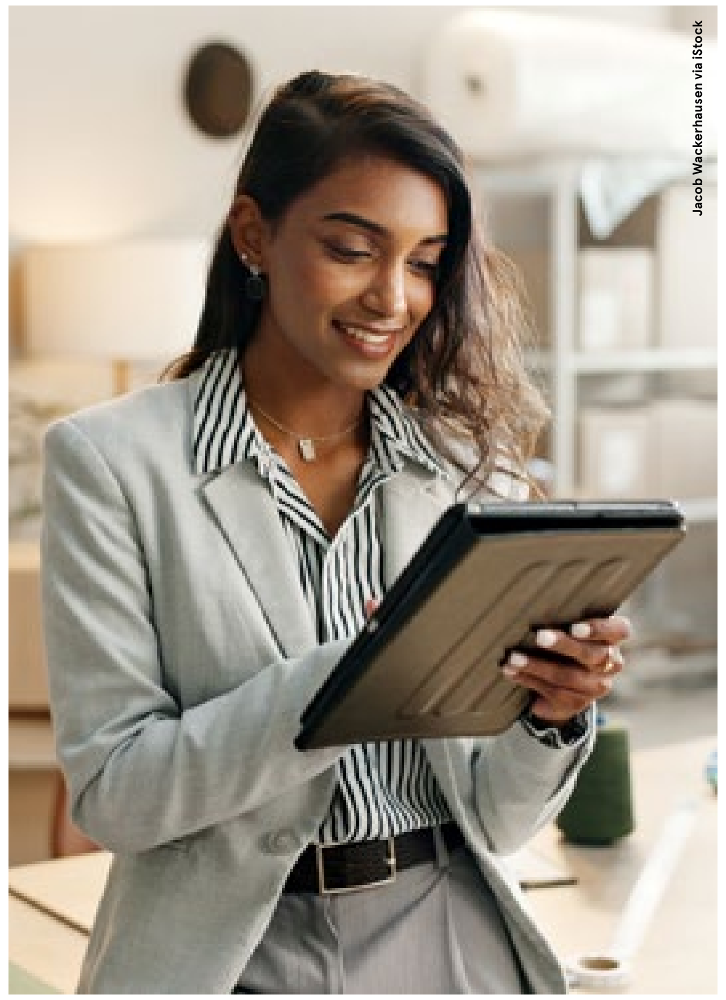
While their frictionless nature is convenient for the consumer, it also benefits the business by serving as a catalyst for repeat custom and better cash flow. This can be especially attractive for smaller businesses, which often struggle to maintain liquidity.

But problems with cash flow are not exclusive to the B2C sector, of course. For B2B firms, more frictionless transactions could certainly help the 58% of small and mid-sized businesses found by recent Barclays research to be awaiting funds tied up in unpaid invoices.

Invisible payments could even reduce the amount of human error that affects commercial transactions in larger companies. A survey of US corporations by data management firm PRGX, for instance, suggests that they lose up to 3% of their budgets each year to simple mistakes such as the duplication of payments. Even if a small portion of those B2B transactions could be made invisibly, the business benefits would be significant.

But there has been a pronounced lag in the digitalisation of B2B transactions, which are more complex than consumer-facing transactions. After all, such payments aren't simply for a ride home after a night out. They represent the services of large supply chains involving several operators.

"The B2B market is an intriguing proposition for invisible payments," says Nick Maynard, vice-president of fintech market research at Juniper Research. "There is a definite efficiency challenge, as transactions typically involve high levels of manual processing. Plus, B2B payments tend to be far larger than consumer ones, making the risk of unexpected charges much greater. There are also potential compliance risks, meaning that businesses tend to operate strict approval thresholds."



Jacob Wackerhausen via iStock

There is also an overreliance in the B2B sector on legacy tech, particularly verification systems that identify the payee and establish that the right sum has reached the right account, he adds. This involves a significant amount of data generation, which typically ends up in a complex matrix of spreadsheets.

Moreover, there's "a level of complacency and a lack of relevant technology to power invisible payments in a B2B context", Maynard says. "Businesses sometimes lack the ability to accept anything other than a bank transfer or a card payment, making automation a much bigger challenge. As such, invisible B2B payments look a long way off."

All but 12% of B2B transactions in Europe are completed using bank transfers, according to research published by consultancy firm Kaiser Associates. This statistic is a good indication of the work that must be done if businesses of any size in this sector are to change their established payment practices.

But the technology that drives invisible payments is developing quickly, while efforts to make B2B transactions more like B2C ones are gaining momentum. Furthermore, the rise of open banking and a pioneering payment instruction called variable recurring payments (VRPs) could be significant for B2B vendors. That's the view of Andrew Boyajian, vice-president of product for payments and the customer experience at Tink, an open banking platform.

"Open banking, and particularly VRPs, will help to drive greater usage of invisible payments in B2B," he predicts. "It's a construct that allows for long-lasting consent to be given by the payer against a set of criteria."

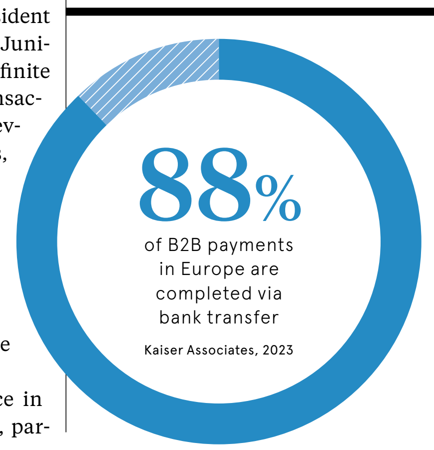
Boyajian continues: "The layering of parameters – for example, the number of payments per period and maximum transaction values – helps to satisfy business control criteria. Think of an approvals process needed to authorise a business payment: by applying that 'approval' to the parameters, payments can occur invisibly as needed within the approved circumstances."

B2B companies remain largely wary of adopting new payment tech, owing to the complexities they associate with ditching traditional methods. But, as they contend with the growing threat of fraud, the promise of more secure transactions could yet persuade them to change.

"The fact that the business payment process is very manual means that it's still easy for bad actors to compromise it and steal funds," notes Shai Gabay, co-founder and CEO of Trustmi, a business payment security platform. He points out that fraudsters can divert money using phone calls and emails – "unsecured communication channels that are still used to facilitate transactions".

Invisible payment systems that enable companies to safely connect authorised payment providers directly to their accounts will eliminate those weak spots and make transactions more secure.

But it may prove to be demographic, rather than economic, pressure that drives B2B firms to overcome their reluctance to modernise. Over the past decade, millennials have become accustomed to the convenience of frictionless payments in their consumer lives. As more and more members of this generation enter leadership roles and take responsibility for their firms' key purchasing decisions, they may come to expect similar payment experiences in their corporate lives too.



Commercial feature

How to navigate shifting EU legislation in the cross-border payments landscape

In the gap between PSD2 and PSD3, evolving payment legislation leaves electronic money institutions in uncertain territory. Yet, strategic navigation of regulatory guidance may unlock safeguarding opportunities

With businesses increasingly looking for lower cost payment services, the number of electronic money institutions (EMIs) and authorised payment institutions (APIs) across Europe has surged. There are now close to 600 EMIs in Europe and the UK, according to Celent research – a number that has accelerated since 2015.

Evolving payment regulations in Europe are, however, creating uncertainty for some payment institutions, particularly in the wake of Brexit.

"One of the key challenges that EMIs and APIs are facing is the opacity of legislation," says Robert Turner-Kerr, senior relationship manager at iFast Global Bank. "Sometimes the legislation is guidance and sometimes it's an EU directive and must be passed into national law. This means there is often significant variation across the single market."

This uncertainty makes it challenging for European payment firms to operate across borders if domestic regulations appear to restrict where they can safeguard customer funds. Post-Brexit, for example, existing PSD2 (Payment Services Directive) regulation technically meant the UK became a 'third country'. Yet, the UK was the first country to sign PSD2 into national law. So, can EEA/EU Payment institutions continue to safeguard funds in the UK? Do local regulators have a precise view on this?

As a result, it can be problematic for regulated firms that have customers doing business in the UK requiring access to GBP accounts or local clearing schemes.

"This effectively means two things: the client base the payment institution can attract may be more limited, and the currencies and payment rails (especially GBP), on offer, are reduced or limited in scope," says Turner-Kerr.

"Where local safeguarding guidance hasn't been updated with specific reference to the UK, EU EMIs and APIs may be uncertain what the position is regarding safeguarding in the UK until PSD3 regulation is introduced," says Turner-Kerr.

"What we've seen recently is some EU payment institutions notifying their local regulator that they intend to safeguard in the UK," he says. "We've seen this in at least two EU markets where there has been no objection

and anecdotal evidence that the UK is considered a competitive and equivalent environment to safeguard funds in, with a wider choice of providers.

This information gap means European EMIs and APIs are potentially missing an opportunity to safeguard customer funds in the UK, simply because they are not aware local guidance may allow them to. They may also be reluctant to challenge their own internal reading of guidance from central banks, which can be outdated.

That matters if these firms have customers with UK currency needs. It means they may have to safeguard GBP in Euro, creating exchange rate risk, reducing competitiveness and increasing costs.

"Not all European banks are willing to provide competitive credit interest on safeguarded funds," says Turner-Kerr, another potential downside. Therefore, there is a potential missed opportunity if they can safeguard in the UK.

"iFast Global Bank can provide these solutions to EEA-based non-bank financial institutions offering credit interest in seven currencies. iFast will also provide indirect access to faster payments and CHAPS, says Mark Garrity, general manager at iFast Global Bank. We will enable firms to take control of their payments with the bank using dedicated IBANs," he says.

"All of which is underpinned by iFast's three corporate pillars of innovation, integrity and transparency coupled with our newest bank pillar, customer centricity."

Being part of a large fintech group – Singapore-listed iFast Corporation (XSES: AIY) – also means the bank can develop new products and services quickly and effectively.

European firms, therefore, may have an opportunity to benefit from enhanced solutions whilst also safeguarding funds in the UK, an option they might not have thought possible post-Brexit.

"Regulated EU firms that simply assume they can't safeguard in the UK may be incorrect," says Turner-Kerr. "Therefore, if you have a business requirement for GBP and want to enhance your credit interest across seven currencies with iFast Global Bank, then it's worth doing some research. Explain to stakeholders why it is important for your business competitiveness and an advantage to your customers.

Discuss with your peers the opportunities that may exist. PSD3 will, undoubtedly, change where and how EU firms operate, by which point iFast Global Bank will have established our European Banking Subsidiary, providing continuity for our clients in any eventuality."

For more information please visit ifastgb.com/en/business

iFAST Global Bank

Commercial feature

WITH GROWING PRESSURE ON FINANCIAL STABILITY, CFOS NEED TO RETHINK HOW THEY DEFINE EXPENSES

28%

of UK businesses have strong visibility of their financial health across the business

98%

of business leaders agree that the CFO role is undergoing a transformation

Pleo, 2024

The CFO renaissance: what the rebirth of the role means for businesses

The role of the chief financial officer (CFO) is rapidly evolving beyond traditional financial management to encompass strategic business partnering and expertise across various domains. Embracing automation is key if CFOs are to master their new-found responsibilities

It's hard to imagine a more challenging period for UK businesses than the last five years. They've had to contend with the aftermath of Brexit, Covid-19 and the associated lockdowns, as well as soaring inflation and rising borrowing costs following the war in Ukraine. In truth, however, every era has had its challenges. The 2000s saw the global financial crisis, and back in the 1990s businesses had to navigate a severe recession and 15% interest rates.

Today though, executives have one big advantage over their predecessors: significant advances in technology. Ones that are not only changing our productivity at work but are also unlocking a level of digital transformation that brings much greater visibility and control to business leaders. They certainly need that visibility too, as Sean Moylan, head of financial reporting at Pleo, explains: "An incredibly small number of UK businesses – just 28%, according to a 2024 Pleo survey – believe they have strong visibility of their financial health across the business."

According to Moylan, this could mean that budgets are being overrun, which is serious for any business but particularly for venture-capital-backed startups. The problem, he notes, lies in the fact that finance departments have traditionally been viewed as a back-office function, with little input into the business's key strategic planning. They're often thought of as raking over old paper receipts and expense claims looking to make cuts, when the truth is today's finance teams are dynamic, technologically proficient and future focussed.

The increasing availability of real-time, accurate data – powered by digital transformation programmes – means that the role of the CFO and of the wider finance department is changing significantly. In fact, 98% of business leaders surveyed in Pleo research agreed the role was undergoing a transformation.

What's driving this opinion is the addition of key priorities that include non-financial reporting, such as Environmental, Social and Governance (ESG), and compliance in a rapidly evolving regulatory environment. Modern CFOs are also expected to be proficient with emerging technologies such as AI, machine learning and blockchain, which all help to automate routine financial tasks, enhance accuracy and enable more sophisticated financial modelling. It's a full plate but Pleo's ambition is to ensure that CFOs have the means to execute their new responsibilities effectively and are finally able step out of the back office to occupy a key role in strategic decision making.

> "Modern CFOs need to master a rapidly evolving skill set, ever-expanding remit and be able to apply forward-looking, strategic value across their organisations

Today, Pleo is Europe's leading spend-management solution, enabling 33,000 companies across Europe to run their finances efficiently and in doing so, promote business success without compromising on control, transparency or financial safety. With its forward-thinking solutions, Moylan says Pleo can play an important role in "enabling CFOs to add value in other areas. Plus, with access to more accurate and timely information, they're able to make better, often real-time decisions."

Integrating solutions like Pleo across an organisation can have compounding benefits, believes Moylan, including helping to connect critical areas and "ensure the accounting system talks to the payroll system, the expense management system and the tax authority – all of which is critical to effective decision making".

Smart spending is not only crucial to business outcomes but collaboration too. Blanket cuts can be devastating to businesses and throw off the equilibrium in-house, meaning the only thing you're balancing is the budget. It's far more important to understand the priorities, resource requirements and opportunities of each area of the business, so that your CFO can allocate finances effectively and redistribute them as needed. This means outgoings are signed off with one eye on ROI and support long and short-term strategic objectives.

The need for collaboration doesn't stop there though. Finance leaders need to find ways to ensure that all the data and insights they are collecting are effectively communicated to all levels of the business. Across the organisation, they need to show their workings because trust and control, particularly in the workplace, come from communication – whether it's the C-suite or the junior team.

This is true of those at the very top of the business too. CFOs are key communicators with investors, analysts and the board of directors, and they need to be able to effectively convey the financial health and strategic direction of the company. This is how trust and confidence is not just built but maintained – something that is impossible to do without clean, insightful data.

Modern CFOs need to master a rapidly evolving skill set, ever-expanding remit and be able to apply forward-looking, strategic value across their organisations. Essentially, they are the renaissance employees of the modern workplace: proficient in a range of fields and capable of changing the status quo.

But, as Moylan observes, picking the right partners to enable success is key, believing that "the intelligent use of technology is essential to support the decentralisation of finance and allow the modern CFO to act as an efficient and strategic leader." Done in this way, the CFO renaissance won't just result in the rebirth of the role – but how businesses operate as a whole.

AUTHENTICATION

5 things you need to know about behavioural biometrics

Behavioural biometric authentication is becoming ever more popular as a defence against fraud, but experts warn that its use comes with key caveats

Sally Whittle

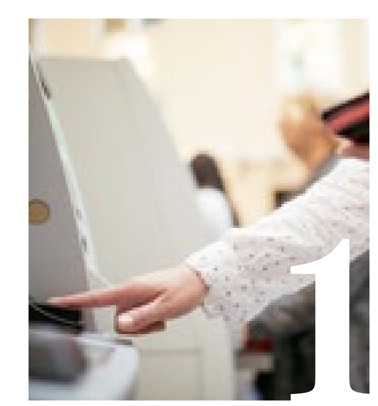
If you've ever made a point-of-sale payment with a digital wallet, it was probably authenticated using a fingerprint or facial scan, but more sophisticated technology could also have been working behind the scenes. Systems known as behavioural biometrics may have been tracking factors ranging from your average stride length as you walked around the shop to the way you held and interacted with your smartphone.

The AI algorithms underpinning behavioural biometrics can analyse such data to detect out-of-character activities that suggest a criminal could be trying to use your identity to commit a fraud.

Barclays, for instance, uses biometric indicators in its mobile banking app to track each user's typing speed on their device and even the pressure of their screen touches.

Global investment in this tech is booming as financial institutions develop next-generation ID systems in a concerted bid to counter payment fraud. One leading player in this field, BioCatch, has attracted £16m of finance from Barclays, Citi, HSBC and National Australia Bank, for instance, on top of earlier funding from American Express. Annual spending on behavioural biometrics worldwide is set to exceed £7bn by 2030, according to a forecast by Grandview Research.

Early adopters say that behavioural biometric features are ubiquitous, convenient and harder than other forms of ID to repudiate. But there are some key questions about this tech that any enterprise should consider before deciding whether to join them on the biometric bandwagon.



Will consumers buy into behavioural biometrics?

"There is always a risk that people will find it creepy or invasive if an organisation is recording their voice, eye movements or typing," says Andrew Doukanaris, an expert in payment tech and CEO of Flotta Consulting. "The industry isn't doing a great job of addressing that concern at the moment, because we're talking about biometrics as a fraud-prevention tool. But most consumers don't care about fraud unless it happens to them."

He believes that selling people the idea of behavioural biometrics means highlighting its most obvious benefit from a customer-experience perspective: frictionless service.

"Brands such as Revolut use behavioural biometrics successfully with their gen-Z customers, because they're focused on making things easy," Doukanaris explains. "Rather than talking about fraud reduction, tell them how easy it is to open an account – on your phone, in your bedroom. Gen-Z consumers are very willing to trade biometric data for that kind of convenience."

What privacy concerns must be considered?

So-called function creep is another privacy issue that may arise from the use of behavioural biometrics. This occurs when information is used for a different purpose than the one for which it was originally gathered.

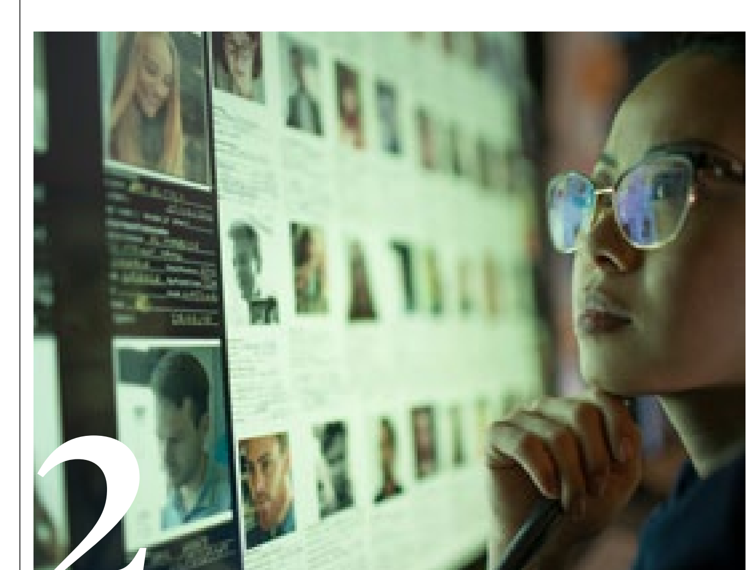
Amnesty International, for instance, has voiced concerns about the collection of biometric data through passport control, suggesting that this material could be used in ways that contravene the rights of asylum-seekers.

In a payment scenario, any data captured could easily be analysed by AI to provide insights that are useful to payment providers but beyond the consent given by consumers, according to Doukanaris.

"You could be happy for a bank to use your expression to authenticate you, but would you be happy for it to analyse your expression to understand your mood when making different types of transactions?" he asks.

Yiannis Zourmpanos is a financial consultant and the founder of Yiazou Capital Research, a platform designed to improve investors' due diligence processes. He believes that payment companies can win over the sceptics by "fostering trust through transparency. It's essential to not only collect consent but also engage in open dialogue with customers about the what, why and how of collection."

Consumers need reassurances that their biometric data won't be used beyond consented purposes, Zourmpanos stresses. Giving them such peace of mind involves "structuring data governance policies limiting data usage that will be strictly adhered to, reinforcing customers' control over their data".

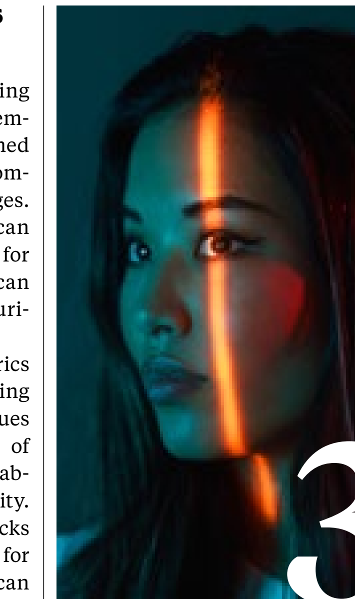


What security controls are in place?

Most biometric systems work using one of two methods: by storing templates that users can be matched against, or by storing original biometric information such as images. Opting for the latter approach can make your database a target for criminals seeking data they can extract, which calls for extra security controls and audits.

"Good behavioural biometrics should offer the possibility of storing personal, identifiable data," argues Eward Driehuis, vice-president of fraud engineering with Threat Fabric, a specialist in payment security. "There are many technical tricks you can use to achieve this – for instance, 'hashing', where you can describe a unique aspect of someone's behaviour without linking it to that person."

He continues: "A good implementation doesn't need to store retina scans or other identifiers. Instead, it should create a mathematical model of what normal behaviour looks like and calculate how differently a person is behaving from that model during any given transaction."



Can biometric systems be biased?

Organisations should consider that a biometric system can build in bias in several ways. There could be physical, medical or cultural factors that limit some people's ability to enrol in biometric programmes. Moreover, margins of error can be influenced by the demographic characteristics of the sample data used to train the system.

The machine learning on which most behavioural biometric systems are based is packed with assumptions. And, as Driehus notes, assumptions are the starting point of bias.

"A good way to reduce bias with AI is to create a unique model per user," he says. "We need to ensure that the model asks whether this is how an individual normally behaves rather than asking how that person differs from other people."

An organisation must also monitor the outputs of its models and examine the results for inherent bias that might affect how it interacts with users in different demographic groups. Ensuring that the system treats everyone fairly, regardless of their age, gender and ethnicity, is vital in maintaining public trust in the technology.

How vulnerable is the technology to a data breach?

Unlike passwords or ID tokens, biometric characteristics cannot be reissued or cancelled. If a person's physiological biometric were compromised, it would be extremely hard, if not impossible, to change that feature. Data breaches of biometric data can and do happen. In 2015, for instance, hackers stole the fingerprint images of 5.6 million US government employees.

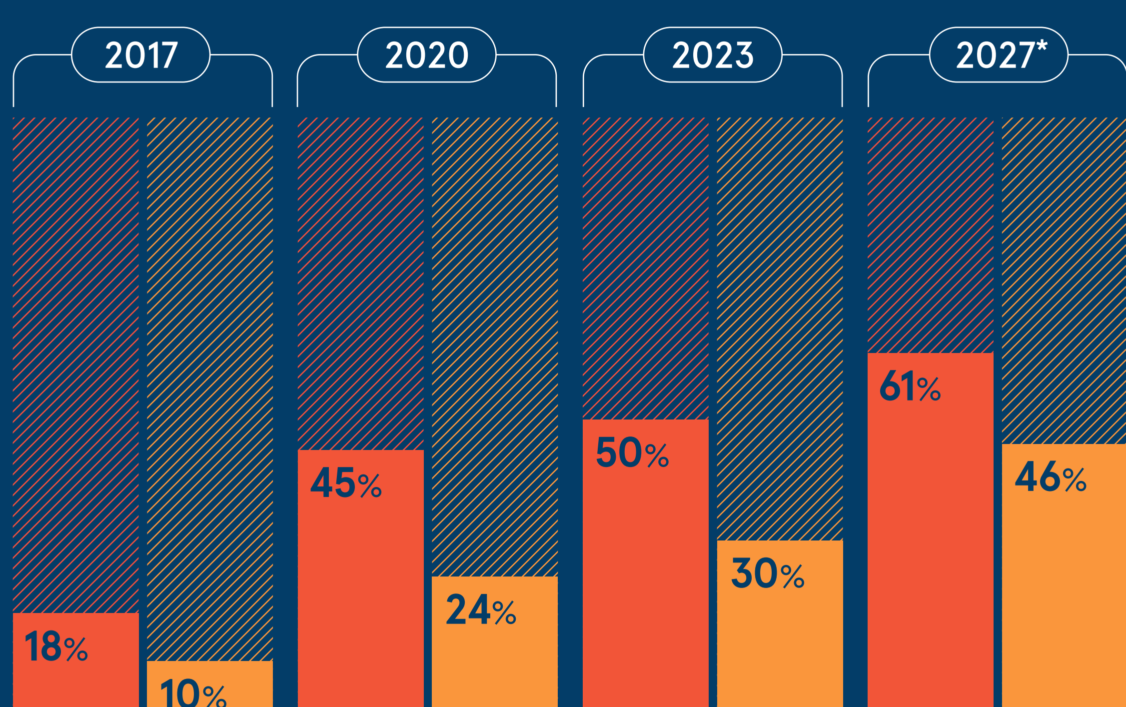
But behavioural biometrics are less susceptible than fingerprints to fraud, because they are mathematical models rather than static images that can be reproduced, Doukanaris explains. Authentication models created by BioCatch, for instance, rely on up to 2,000 behavioural signals, using machine learning to analyse user behaviour in real time. This makes it incredibly hard for a fraudster to recreate someone's ID from stolen data, compared with PINs, passwords and even iris scans.

DIGITAL WALLETS

Digital wallets such as PayPal, Venmo and AliPay are quickly becoming the preferred payment method for gloabl consumers, both for ecommerce and point-of-sale (POS) transactions. By 2027, it is projected that digital wallets will account for three in five ecommerce purchases and one out of every two POS transactions. But while market observers highlight the accessibility and enhanced security of digital wallets, adoption rates differ significantly around the world

THE RISE OF DIGITAL WALLETS

Share of total transaction value completed with digital wallets globally, by year and transaction type

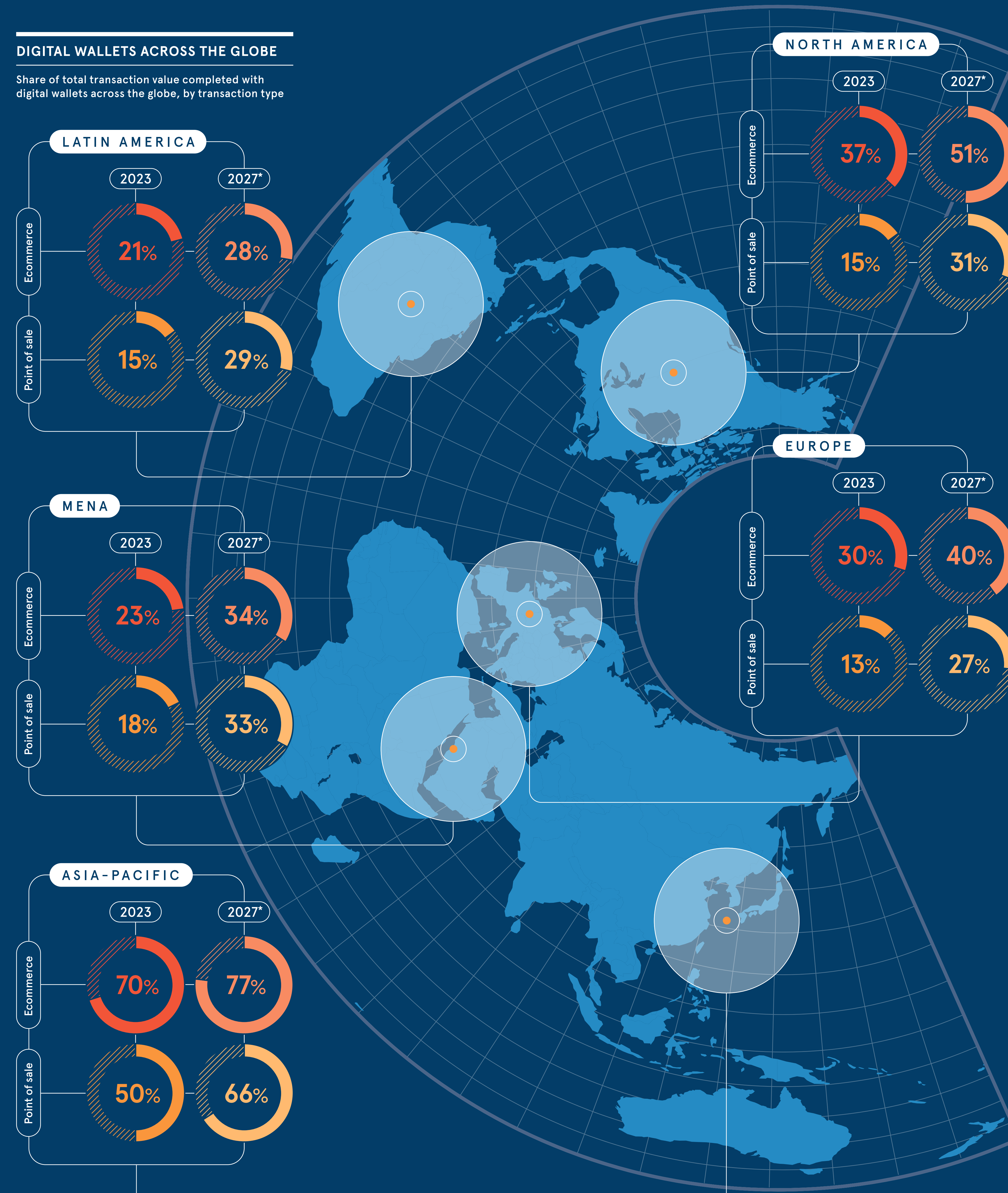


*forecast

Worldpay, 2024

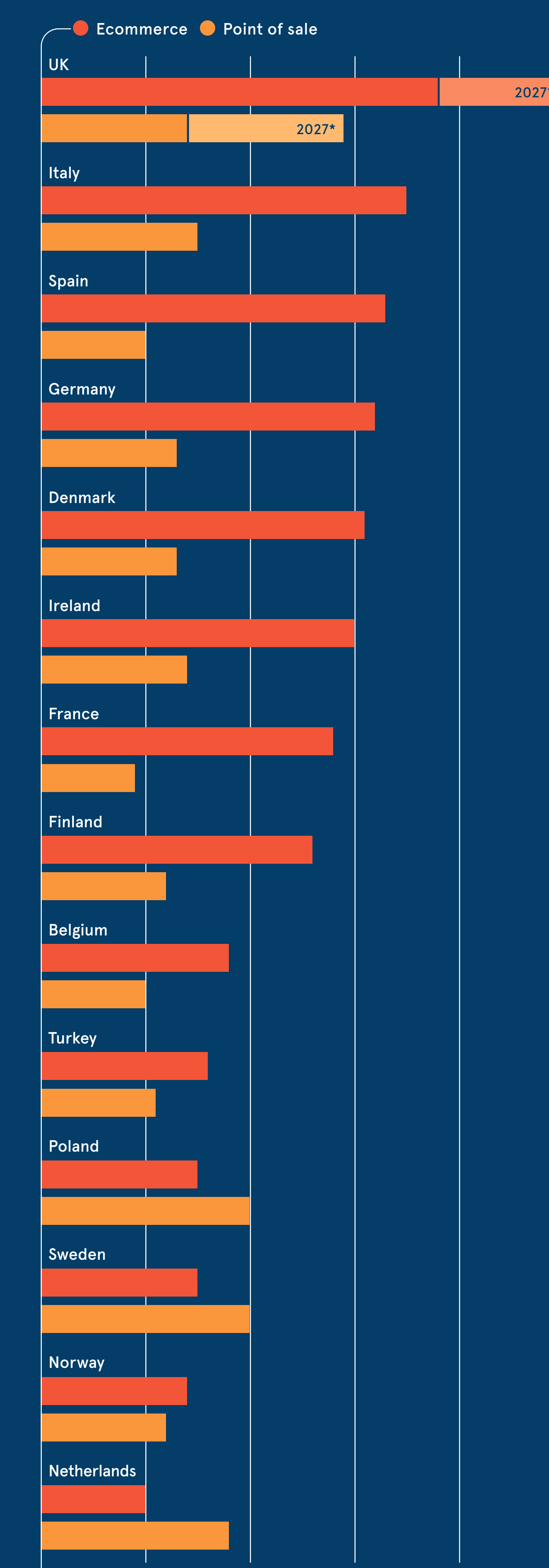
DIGITAL WALLETS ACROSS THE GLOBE

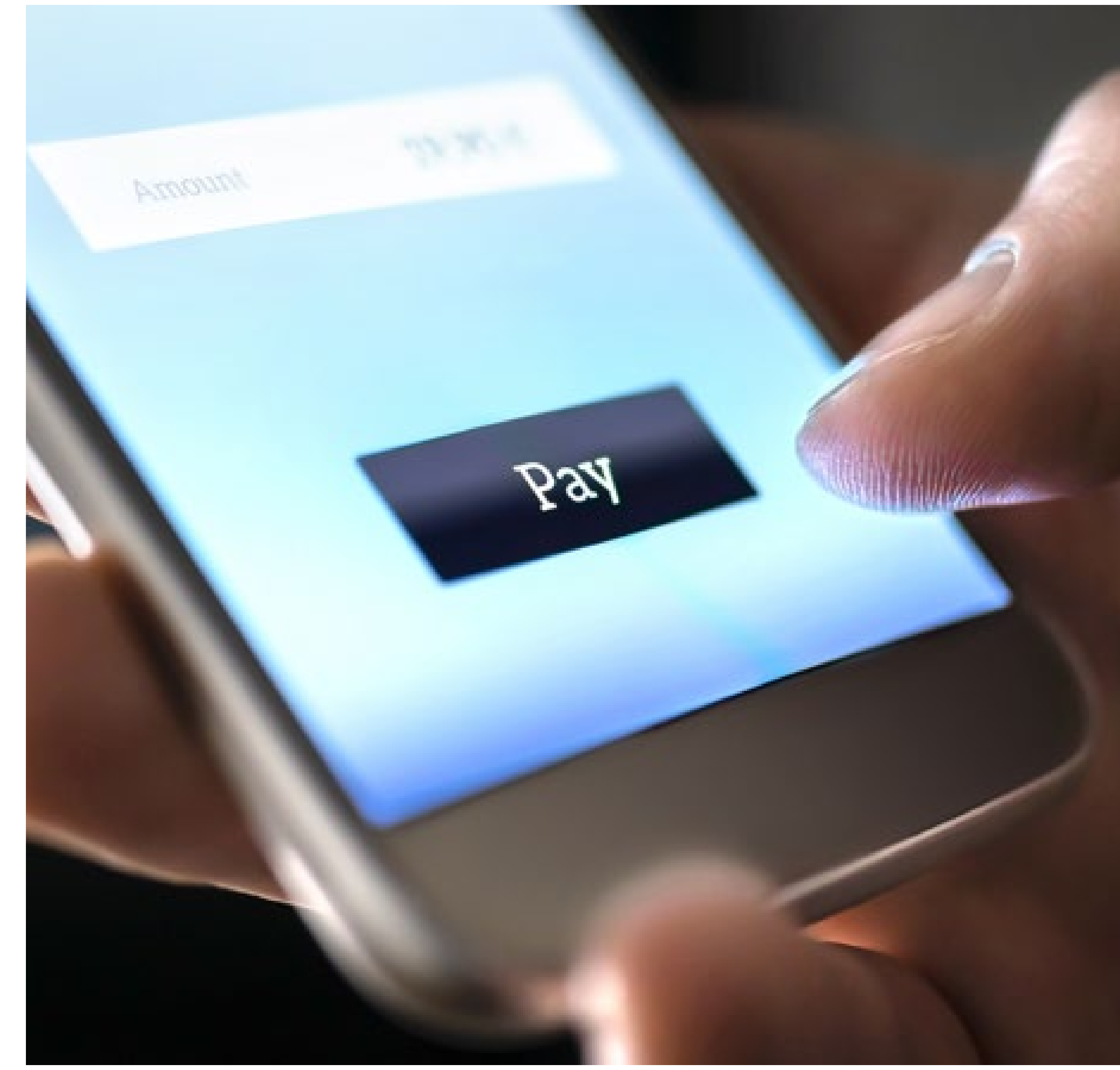
Share of total transaction value completed with digital wallets across the globe, by transaction type



THE UK LEADS EUROPEAN NATIONS IN DIGITAL WALLET USAGE WITH THEIR USE EXPECTED TO GROW RAPIDLY

Share of total transaction value completed with digital wallets in Europe in 2023, by country and transaction type





Tero Vesalainen via iStock

FINANCIAL INCLUSION

From fintech to 'in' tech – solving financial exclusion

As the cost-of-living crisis drags on, what more can the sector do to tackle problems such as the digital divide and bring the nation's most marginalised consumers into the fold?

Tim Cooper

The payments industry has developed some innovative solutions to help the poorest and most vulnerable members of society in recent years, including those worst affected by the ongoing cost-of-living crisis. But despite this, the sector could still do much more to boost financial inclusion, according to experts in the field, who point to several problems that remain largely unaddressed.

Between September 2022 and January 2023, almost a quarter (23%) of adults in Great Britain experienced financial vulnerability, according to the Office for National Statistics. Throughout that period and beyond, factors such as energy price inflation have exacerbated the poverty premium, whereby poorer people must pay more for essential services including electricity and gas because they can't access online deals and take advantage of cheaper payment options such as direct debits.

Fair by Design, a charity dedicated to ending the poverty premium, has urged the industry to come up with more inclusive and flexible payment methods to solve this problem, but more cooperation is needed from service providers taking payments.

Adele Atkinson is professor of practice in financial literacy and wellbeing at the University of Birmingham. She says that payment providers could partner with internet and data providers to promote discounts for people on benefits, which would improve their access to cheaper deals and payment options.

Atkinson also argues that the sector contributes to some people's financial hardship by making it too easy for them to make payments, some of which might be for inessential impulse buys that will put them further into debt. It must therefore add "friction" – slowing transactions by, say, adding extra processes before the checkout – for those who want a few extra seconds to consider their purchasing decision.

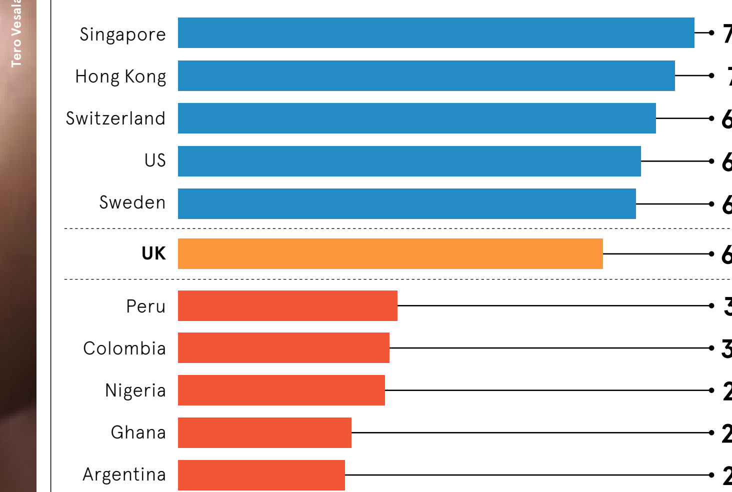
"Repeated studies show people regretting contactless payments," she says. "These transactions are also easily forgettable, which means that people risk spending more than they intended. Consumers actually want to slow the purchasing process, which is the opposite of what retailers are trying to achieve."

Neil Harris is chair of the Payments Association's advisory board and financial inclusion committee.

> "Consumers actually want to slow the purchasing process, which is the opposite of what retailers are trying to achieve

FINANCIAL INCLUSION ACROSS THE GLOBE

Index scores for financial inclusion for top- and bottom-five jurisdictions, compared with the UK



Principal Financial Group, 2023

He agrees that more friction can be a good thing, but adds that it must be "proportional to the size and frequency of the spending". The solution, he says, will lie in the fintech sector's smarter use of data to ensure that the amount of friction imposed is appropriate for each customer and transaction type.

The advance of open banking, which requires banks to share customers' data with each other and third-party service providers, has boosted financial inclusion in recent years. Open banking technology has used the improved flow of information to make financial products more widely accessible by enabling alternative payment options for unbanked individuals, for instance, and helping a wider range of people to qualify for products.

Open banking has also contributed to a proliferation of payment service providers. There are 1,400 such entities in the UK, according to the Payments Association.

"This makes the market more competitive for all customers," Harris says. "It also allows great diversity for meeting specific needs – from Sibstar, a payments service designed to help people with dementia, to Incuto, which has modernised credit union payments."

Payment service providers that are emerging to tackle financial exclusion have attracted significant investment. Fair by Design's funding arm has invested in 14 startups addressing the cost-of-living burden, for instance. These include SteadyPay, which uses earnings data to help hourly workers manage their money; Wagestream, a credit card that helps front-line workers to access earned pay; Hi, which helps employers provide workers with flexible access to their pay; and Credit Kudos, which uses banking data to improve the accuracy of credit checks.

Traditional providers have been playing their part too. HSBC has worked with charities to help people affected by homelessness to access banking services, for instance.

Karen Elliott, chair and professor of practice in finance and fintech at the University of Birmingham, believes that such initiatives are a sign that the sector is heading in the right direction. Nonetheless, open banking covers only about 15% of the payments market – and the industry has a problem with helping people who don't use smartphones. It rarely talks about this openly, she says, but "off-the-record discussions have revealed that it doesn't provide a high return on investment".

The way to solve such problems is to form a nationwide inclusion strategy under which payment providers partner with the government and not-for-profit enterprises on initiatives, argues Martin Coppack, a director at Fair By Design.

"A joined-up strategy would make a meaningful change for millions of people who are excluded from financial services," he says.

Harris agrees, noting that the Payments Association hopes to catalyse such a development by working with Westminster, industry regulators and the third sector. The association is also calling on the government to prioritise funding for inclusion services and set regulatory frameworks to support more data-sharing. In particular, it admits that there remains a dearth of financial products and services tailored to people receiving benefits. Startups and established firms want to tackle this shortfall, but the lack of a system akin to open banking for benefit payments is a barrier.

The high cost of borrowing and tough economic conditions are hindering the sector from addressing financial exclusion as effectively as it otherwise might. Moreover, Elliott notes that the problem is rooted in long-standing and seemingly intractable social ills such as race and gender bias, the poverty trap and educational inequality.

"There is also a fallacy that people in challenging circumstances cannot manage money," she says. "Research clearly shows that this is not the case. Instead, bias in technology combines with other factors to preclude them."

Elliott admits that advances in fintech may enable the sector to address this problem by, for instance, capturing more data to adjust credit models and open access to more payment options.

However, she adds that fintech companies "have to make a profit first and explore more nuanced purpose later".


Urbazon via iStock

INSTANT PAYMENTS

Quick-quick, slow: why banks are struggling with instant payments

Europe-wide rules on settling transactions within 10 seconds are due to come into force next year, but a significant number of institutions don't seem to be ready for them

Charles Orton-Jones

We live in an instant world. Send a WhatsApp message and it arrives immediately. Ping an email and bang – it's there. But what about payments?

The UK's Faster Payments Service offers impressive speed. A transfer of funds from Monzo to Revolut typically takes less than a second. But other transactions can take several hours. It can even take days in some parts of the EU, where older banks are still wedded to batch payments, processed in bulk, usually at night.

This is all set to change with the imposition of the Single Euro Payments Area (Sepa) rules on instant payments. From 9 January 2025, payment service providers must be able to receive "instant" payments That means no more than 10 seconds, with a further 10 seconds to notify participants. And from 9 October 2025, providers must be able to send instant payments. It's a huge shake-up.

The Sepa spans 36 European nations, including Norway, Iceland and the UK, so it's considerably larger than the EU. It's an integration initiative that commands the support of the whole European banking and payment industry, the European Commission and the euro currency's Eurosystem. When its new rules take effect, Europeans should be able to make payments without delay, all around the continent.

But are the banks ready? A poll of 200 payment professionals in France, Germany, Italy, Spain and the UK by RedCompass Labs in January found that 32.5% weren't confident that their firms would be ready to receive instant payments by the start of next year. Only 7.5% were "very confident" of meeting the deadline. UK-based respondents were the least optimistic that their companies would be ready, with 20% saying that they were "very unconfident".

Payment providers have had years to prepare. Surely they should be equipped to meet this basic threshold in time? What's going wrong?

Several deep-rooted infrastructure problems are causing mayhem, says Nick Botha, global payment lead at AutoRek, a provider of software and data services to the sector. "Banks work on operational flows designed around settlement cut-off times, which are incompatible with the instantaneous nature of Sepa instant payments," he explains. "Processes such as risk management, reconciliation, reporting, regulatory compliance and data management are all tailored to fit a model based on market closures at set times each day. In a 24/7 settlement regime, these processes become inadequate."

Upgrading to instant payments is not a simple case of installing a new software module, then. A bank may need to upgrade or even replace its entire tech stack.

Botha points out that, when payments become instant, "fraud is more difficult to detect and non-real-time reconciliations become completely unfit for purpose. Moreover, liquidity and settlement operations including reporting can no longer be organised as an end-of-day process; regulatory and central counterparty risk becomes much more pronounced; and data management processes turn into operational bottlenecks."

In short, Sepa is a spotlight illuminating the banking sector's technological shortcomings.

At the core level, several banks may still be running legacy software that can't easily be improved. (In banking parlance, the core is akin to the operating system.) The industry is still riddled with cores that were designed in the 20th century.

Some banks have migrated. Lloyds, for instance, upgraded from a legacy core to a cloud-native platform made by Thought Machine. This cutting-edge infrastructure has made instant payments simple for the bank. But several other institutions remain hamstrung by obsolete cores.

"Banks tend to be reluctant to update their core systems, as it's costly and time-consuming," says Michael Greenwood, research analyst at Juniper Research. "Updates can mean downtime, preventing a bank from offering its services while the migration takes place. This could be avoided by using a staggered migration strategy, but that would increase the overall time taken."

Migrating to a new core will take 18 months at best, but three years is more likely. Big banks run spaghetti systems – tangled networks of cores and applications that are almost impossible to port to a new platform. One UK high-street bank runs on more than 50 cores, with about 7,000 applications, for instance. For such institutions, migration may be the toughest task in banking.

> Innovation and compliance come at a significant cost and, unfortunately, banks don't move at pace

"Banks that haven't begun transitioning to a new core will struggle to complete the process and integrate instant payments in time," Greenwood says. "This means that adopting solutions that can integrate instant payments into legacy systems is their only real option for making the deadline. But doing this will push the issue of legacy infrastructure further down the road."

Given that the details of both parties must be verified and anti-fraud analytics completed in a fraction of a second, each instant payment is a logistical miracle.

Willem Wellinghoff, chief compliance officer at online payment provider Ecommpay, believes that many organisations still lack the firepower to deliver anti-money-laundering (AML) checks and fraud detection at the speed required by instant payments.

"There is already a significant focus on managing AML risks in banks, while automation and the use of AI is a priority in many institutions," he says. "But this work is still evolving rapidly, with early-stage adoption, so there's still a reliance on rule-modelling overlaying human intervention. Operating instant transfers will therefore put significant pressure on compliance functions to manage a fine balance while ensuring the outcomes of the Sepa scheme. We've seen a significant amount of authorised push-payment fraud [where bank customers are duped into transferring funds to scammers] – and instant payments might increase this."

Busy shopping periods will put banks' AML systems and processes to the test. While they may perform adequately in normal times, Black Friday, say, could prove problematic. As transactions spike, they may hit full capacity, slowing down transactions. One bottleneck, such as a third-party provider lacking bandwidth, could affect a whole payment ecosystem.

International variations only add to the complexity of the harmonisation challenge. The goal of Sepa is to coordinate payment systems across Europe, but regulatory concepts vary from country to country. France, Italy, Spain, the Netherlands and the Nordics all run their own payee verification schemes, for example. A single protocol is being developed, but it's not yet uniform.

Progress is being made. For instance, 80% of financial institutions in Europe have a Sepa instant credit transfer facility in at least one segment of their business. Nonetheless, achieving universal compliance by the start of next year is a tall order.

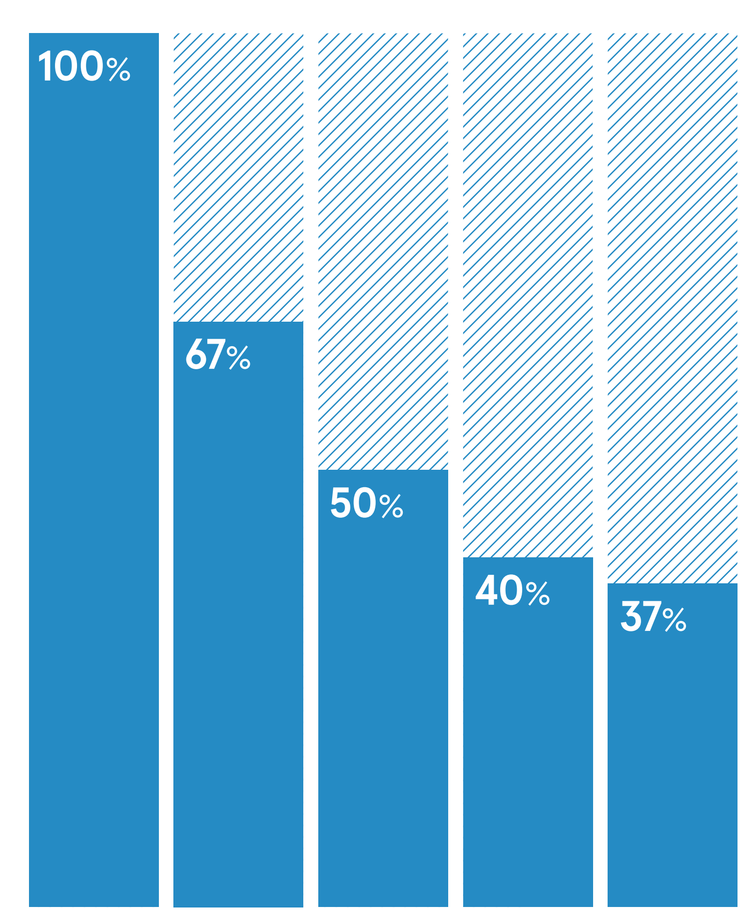
Some industry insiders, including Wellinghoff, believe that the Sepa deadline should be pushed back.

"Innovation and compliance come at a significant cost and, unfortunately, banks don't move at pace," he says. "It would therefore be a good proposal to extend the deadline by another 12 months."

But this looks unlikely. Rules are rules – and Europe's financial institutions have had plenty of time to prepare for them. Consumers want instant payments. Companies do too. Any bank that can't meet the Sepa deadline, for whatever reason, is sending a clear warning to the market: avoid us and deal with someone more competent.

HOW REALISTIC IS THE SEPA DEADLINE?

Share of senior payments professionals who believe the Sepa implementation deadline is realistic, by select European country



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