A solid SEPA foundation

While others talk about it, BankAustria Creditanstalt has pushed on with a major payments system overhaul. The expanded Unicredit Group looks set to benefit from this, not least in terms of readiness for SEPA. What has been achieved in terms of a consolidated, cross-border payments infrastructure?




There has probably been more words spoken about payments, at least in Europe, than about any other subject in banking over the last couple of years. But for all the talk, the majority of banks are still at an early stage in their readiness for SEPA and for other payment-related challenges and opportunities. As such, those that have got on and done things – the likes of Deutsche Postbank and Société Générale – stand out. BankAustria Creditanstalt, now in the guise of Unicredit, can certainly be added to this number. It set about centralising much of its payment infrastructure a couple of years ago and, as a result, looks well prepared for the coming changes. As well as readiness from the perspective of its own requirements, the bank also has in mind to offer outsourcing for other banks.

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The work has been centred on a shared services model. Discussions about this type of approach began a few years ago in Creditanstalt's head office. Over a fair while, there was a study to consider which areas of the bank might be appropriate for this, with a decision coming out in favour of cross-border payments. It was decided that this should be centred on Prague, based on 'market decisions about the existing environment', says managing director, Business Transaction Services, Johannes Majer. The Czech Republic had traditionally been used by the bank as the pilot site for payment products and had the highest volumes of cross-border payments. 'So it had the knowledge base and the infrastructure was well developed.'

That infrastructure had been overhauled in the previous few years, with the selection of a new payments platform in early 2004. Changes in the market meant that the existing in-house systems would have needed significant redevelopment, says Majer. The relatively standard nature of cross-border payments meant, this time around, it was felt that a package was appropriate.

The initial selection had taken in around 20 suppliers, of which around half responded to an RFI. There was then a 'significant' RFP with a lot of input from the banking side, says Majer. In the end, the bank wanted a sizeable partner with reliable references, says Majer. In other words, it swayed away from some of the newer players, touting promising but largely untried solutions.

It came out in favour of Fundtech's Global PayPlus (GPP), with this implemented in both the Czech Republic and Hungary. One key criterion had been to find a solution that could provide multi-entity support because, says Majer, while the selection was done ahead of the establishment of the service centre and while there were separate implementations in Prague and Budapest, the hub model was already in mind and the bank was not intending to implement the new payment system in each country. At this stage, Citigroup's long-running roll-out of GPP was starting to gain momentum. Fundtech marketing head, Joe Mazzetti, admits that Fundtech had 'learnt the hard way' in terms of multi-entity support, not just from a technical perspective but also from an operational one. As Majer points out, not only does the system need to be able to cope with multiple start and close of business days but also country-specific differences such as national holidays and local regulatory reporting requirements.

Since the establishment of a separate company to run the shared service centre in 2005, seven countries and one external entity have been brought onto the Prague-based system. Those countries are the Czech Republic, Slovakia, Slovenia, Romania, Croatia, Bosnia and Serbia. The three Baltic country operations are scheduled to cut over by the end of June, to be followed by Hungary which, at present, is still using its own version of GPP. Prior to this, payment processing was totally decentralised, says Majer.

Not surprisingly, a major part of the roll-out has been interfacing. The nature of the payment business means that most are on-line, including those to banking systems, Swift, Step 2, booking systems and balance checking systems. The only batch interfaces are really for exchange rates and static data. In terms of performance, this is always a topic, says Majer, but is generally to do with hardware not software. The bank has worked closely with Fundtech on how to scale and plan the next upgrades. The system has worked fine until now and the bank is running GPP on Windows servers. Majer feels that this platform will be fine for the volumes from the next batch of countries being added but that at some stage it might need to move to the Unix and Oracle version of GPP. Mazzetti points out that the two versions of GPP use the same code base.

The scale of the project has increased because of the mergers that have occurred in that time, with the country operations often seeing a marked increase in size with the incorporation of the BankAustria Creditanstalt, HVB and Unicredit operations. In fact, the one strictly non-Group entity using the shared service centre is a result of this activity. The merger meant that Unicredit would become the largest bank in Croatia but, with the national authorities resisting the creation of a single dominant player, it ruled that one of the operations had to be sold. This business was acquired by SocGen but the payments processing continued to be supported by the Prague centre. Recently, says Majer, SocGen has decided to retain this arrangement going forward. Work is under way to interface to SocGen's Swift connection in Paris but this is the only change. The decision comes despite SocGen's own significant strides of late to centralise its own cross-border payments infrastructure (IBS, April 2003).

Beyond this, Unicredit has not yet sought business from other banks. If a potential customer were to approach the bank now then it wouldn't say 'no', he says, and would seek to squeeze it into its current projects. There have been a few discussions, 'but we have not been concentrating yet to really find some business'. With the current workload, the incorporation of additional countries will run through to the middle of next year. And, in parallel, there is preparation for SEPA, Target 2 and enhanced high-value payment services, with all of these having been worked on since the outset with Fundtech.

There has been 'very intense, close co-operation', says Majer. At the outset, there were a lot of workshops with the supplier and there has been a lot of joint development work to add functionality to GPP. That functionality has been rolled into the GPP core, says Mazzetti. The bank is now much more self-sufficient. 'They have really learnt GPP,' says Mazzetti, and largely do definition work by themselves. Adding countries has become faster and smoother over time, adds Majer.

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Johannes Majer, MD,
Business Transaction Services,
Unicredit

While the existing project rolls on, there are additional considerations to enlarge the scope within Unicredit for Austria, Germany and Italy. One decision that is unlikely to be reversed in the near term is HVB's strategy of moving its payment processing facility to Deutsche Postbank (IBS, December 2006/January 2007). Due to different labour regulations relating to offshoring, which goes hand in hand with staff reductions, different countries require different considerations. For HVB, it was felt to be easier to come up with a separate 'in-country' payment processing strategy than try to move to Prague.

In terms of the benefits of the project, one aspect is cost but this was not the priority. Indeed, if cost were the main incentive, then Majer doubts that a service centre would be the most appropriate solution. If you outsource from Austria or Germany to the Czech Republic, for instance, then the labour costs might be a third but the difference for other countries is much less. Reduced costs, in terms of cheaper processing, are important but so too are faster time to market for new products and improved customer service.

The bank now has standard payment products, with these available, providing there are no regulatory issues, in all countries. Investment is made only once whereas before no one considered neighbouring requirements, says Majer, so there was a lot of duplication of effort. Payment specialists are all in one location and this is important, he points out, as GPP is quite a complex system requiring a fair amount of training. New products are made available to all countries at the same time and, particularly for some of the smaller countries, this has brought a significant improvement in services. In Bosnia, for instance, he feels Unicredit now has by far the most modern banking system in the country. While Unicredit's operations have been formed by the coming together of three banks to create the largest presence in the country, volumes are still relatively small and the Bosnian operation could never have afforded such a platform on its own. 'It is like giving them a Ferrari to drive but without the investment or maintenance.' Indeed, the country operation only pays for 'fuel' – in other words, it pays fees based on transaction volumes. The only other cost is project fees where there is a development that is specific to that country.

This approach means that generic requirements for SEPA will not be incurred by each country. SEPA was not a major driver at the start of the project because it was only starting to emerge. 'For us, it is really the proof that the decision three years ago was the right one.' Unicredit is a major European bank so it needs to be SEPA-ready across all areas. Separate investment in each country for SEPA would have been 'a big lump sum'. Similarly, for Target 2, the Slovenian operation will gain this for free, with this country being one of the first to join alongside Austria and Germany in November.

The bank has recently done a study to look at its STP rates. There is constant work to improve these and, in some countries, there has been a 15 per cent improvement in the last year but there are a number of factors, many of which are not to do with the processing system. Criteria include client training and the functionality of electronic banking systems, with the need for correct data, including BIC and IBAN. The service centre charges different rates for STP and non-STP processing to the country operations. In the Czech Republic, it has also now introduced a facility to allow the country operation to introduce non-STP charges for end-customers, with this likely to be introduced for other countries as well.

The operating mode is flexible. For the Czech and Slovak operations, the service centre handles exceptions, with staff liaising with relationship managers to resolve queries. When Hungary comes onto the system, the expectation is that repairs that require a bank decision will be done by the

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particularly those handling less than ideal debt, the delicate interaction of loss mitigation, and with that the retention of the customer relationship, may replace the hammer of collections.

Finally, at least two vendors market ASP services that can work with different servicing systems, while helping a servicer avoid the cost and complexity of setting up a standalone solution. For example, MSTD Inc., based in Baltimore and acquired by LandAmerica Financial Group in 2006, offers BackInTheBlack, a complete default management offering via the web, with all the standard functionality. Computer Sciences Corporation's EarlyResolution, which the company acquired from Freddie Mac in 2004, is a similar web-based default management 'front-end' for a servicing system.

Olrich feels that, once the current subprime disaster dissipates, subprime mortgage servicers will be stronger. 'We are talking now to companies that are buying a lot of the subprime loans [being sold by troubled servicers]. They know that technology is a big part of the answer.' Many of the companies that are buying subprime portfolios from bankrupt servicers such as New Century Financial Corporation of Irvine, California, are Wall Street investment banks. 'Wall Street has gotten into subprime mortgage servicing very heavily, creating their own servicing departments. The ones I have seen are sophisticated and well-run.' And, notes Olrich, investing in default management technology. Luckily, today, subprime servicers can evaluate and purchase 'prime' technology. Whereas default management systems barely existed only ten years ago, they are now available in many shapes and with strong functionality.

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country staff instead, partly because of the language issue. The decision which route to take is partly up to the country operation but in terms of whether or not to use the service centre per se, this is a central decision. The real target, says Majer, is to centralise as much as possible.

What about an extension of the service centre model for other areas of the bank? In fact, such a facility for card processing for central and eastern Europe was introduced, also in Prague, at the same time as the payments centre. The bank has had shared IT resources for a long time. And the Czech centre also handles the processing of all paper-based payments for Austria. These are scanned in Austria and then entered and repaired in Prague.

The topic of extending the model is of major importance within Unicredit, says Majer. The treasury, securities and retail back office systems of Unicredit's two banks in the Czech Republic have been brought into the Prague centre and will run from here (the two banks are set to merge at the end of the year). 'This might be the basis for the future for additional shared services,' says Majer.

Whatever happens, the efforts of the last few years look to have given the Group a sound platform for payments, putting it considerably ahead of many of its peers. With that model shown to work in this arena, it looks as though it might be applied to others as the strategy for the expanded Group takes shape.