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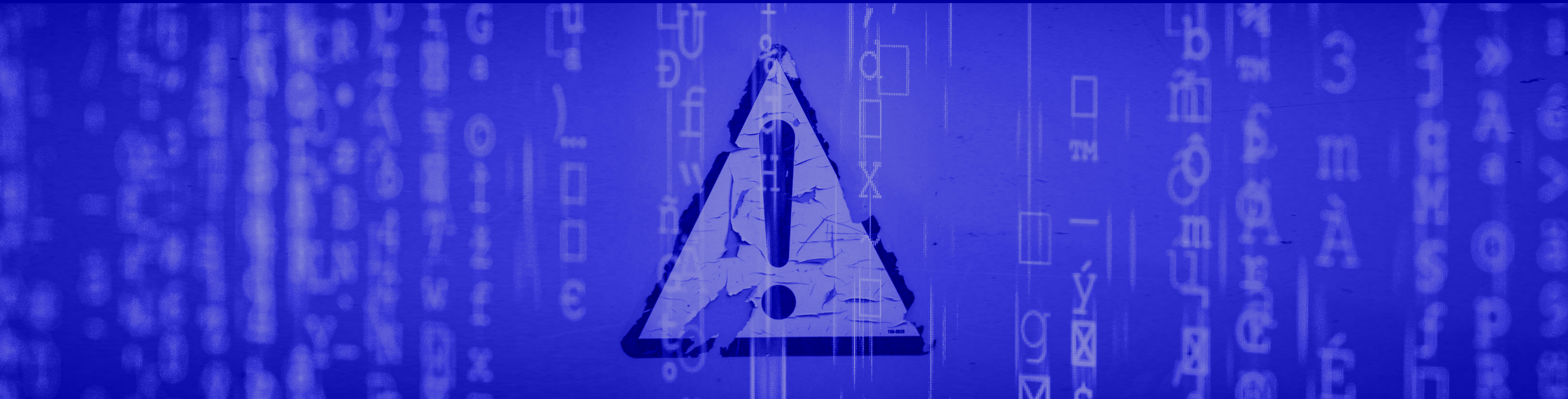
ISO 20022: How banks can avoid becoming a cautionary tale



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01 | Introduction

Transitioning to the ISO 20022 financial messaging standard has been high on the agenda for financial institutions for several years, but as deadlines loom, the true advantage of early adoption means institutions are facing new pressure to migrate, and to do so quickly.

By late 2022, institutions across the globe will have begun their migration to the new ISO 20022 financial messaging standard for high-value payments. SWIFT's timeline delays have somewhat hindered the process for many institutions, but the project is resolutely on track for completion by 2025.

The benefits of transitioning to the data-rich standard are well documented, but executing the migration itself is relatively new territory for financial institutions and the counterparties that transact with them.

Naturally, with any new project comes uncertainty and a degree of the unknown. Yet, organisations can and should approach their ISO 20022 projects with an honest view of the strengths and weaknesses of their existing infrastructure so that avoidable mistakes remain just that.

Understanding the type, location, and systems governing existing data in need of transformation is not always apparent to teams overseeing the ISO 20022 migration within financial institutions. Not all banks boast IT departments with the expertise and understanding of what is required by the ISO 20022 transition.

ISO 20022 cannot be viewed as a plug-and-play product. Given the sheer volume of archaic technology, infrastructure, and data within every institution, there needs to be a clear connection between the data cleansing and the transformation processes to ensure old flows are joined seamlessly with new flows.

While IT teams within financial institutions will always play a fundamental part in technology transformation, given the complexity and resources required to complete an effective ISO 20022 migration, there may be more effective methods for achieving a smooth execution than relying solely on internal efforts.
While outsourcing ISO migration efforts can be costly, the cost to recover from incorrect ISO implementation or a failed ISO audit can be crippling.

Partnering with third party technology providers to assist with the transition means that IT departments within banks aren't left to navigate the complex project on their own.

Transitioning to ISO 20022 should not be met with trepidation, it should be met with full commitment and a sense of pragmatism around precisely developing the best timeline and structure to execute the migration successfully.

A clean handover of quality data for integrated payments is of increasing value to banks' corporate customers, and ISO 20022, implemented correctly and consistently, can help to deliver this.

However, to cater to the data-rich, purely digital, API-driven world of the (near) future, the ISO 20022 project must be carried out well.

We are already seeing the negative impact of firms which approach ISO 20022 migration as a 'box-ticking' exercise, rather than a project which can equip institutions to deliver a more competitive offering. Conversely, those choosing to commit to a comprehensive transition are better placed to reap the long-term benefits of a redefined infrastructure that prioritises innovation through the leveraging of data, and can then pass on those benefits to their clients.

This impact study will set out four key areas that institutions must address when approaching their ISO 20022 migration to avoid unnecessary complications and instead build an infrastructure that caters to a data-led, customer-centric future.

02 | Understanding the gravity of the ISO 20022 migration: a legacy technology problem

Every financial institution is unique, and therefore the approach to managing the ISO 20022 migration will depend on the complexity and breadth of the organisation's specific needs. Some financial institutions have decided to embark on the ISO 20022 migration independently, others see value in partnering with third party providers to assist in the transition process. There are a diverse number of tailored solutions that firms can deploy in order to make the migration as smooth as possible.

It's essential to recognise that ISO 20022 is not just another payment type. Banks' current systems - typically burdened by legacy technology stacks - are unlikely to be able to provide or accept the additional information required by the new messaging format.

Potential data truncation issues remain a challenge for the financial services industry, and the UK, for example, is staggering the transition through a 'like-for-like' phase (limited ISO 20022 messages) from June 2022, until its enhanced phase (full ISO 20022 messages) from February 2023. Additionally, there are significant differences between implementation guidelines which must be addressed for each payment scheme, such as CBPR+ or HVPS+.

The risk of data truncation underscores the essential element in the navigation of ISO 20022 transition: outlining the type of mapping and translation changes that future current flows will require. It is vital for banks to map those of their systems which predate ISO 20022 to the new standard through the use of a translation solution. This will need to include rules tied to AML, fraud, and compliance checks.

Throughout this process, firms must keep a keen eye on the impact the transition may bear on operations, ensuring that they are able to process or translate ISO 20022 messages in their existing back-office systems. Relying heavily on translation solutions will be vital for many organisations, however, by 2025, firms with back-office systems that are unable to handle ISO 20022 will require permanent translation solutions.

This positions the ISO 20022 transition as the perfect springboard to upgrade legacy payments applications. While short term translation solutions may suffice to bridge the transition phases, the cost of these over time may prove inhibitive and importantly, are unlikely to offer the opportunities that a modern, more permanent product could provide.

03 | Understanding the market to shape a thorough, long-lasting solution for the future

In their approach to crafting a seamless technology portfolio, banks must consider how their ISO 20022 strategy will fit into this overall vision. As the financial services market is evolving, resilient digital infrastructure is no longer considered a luxury, but instead a foundational component in how they will continue to do business. As a result, implementing or bolstering a robust technological strategy has never been higher on the agenda.

The payments ecosystem is already on its way to becoming friction-less and real-time. Cross-border, domestic real-time gross settlement (RTGS), and instant payments rails are all experiencing dramatic evolution with a digital future at their heart. ISO 20022 is the key to this new payments ecosystem, however, by nature, it demands a level of digital interoperability that all financial institutions do not yet hold.

Most traditional rails that carry financial messages will need to change in order to transport the new ISO 20022 XML structure, and new features for extracting wrapped messages will demand the adaptation of gateways. New rails will also emerge via APIs, which will likely necessitate infrastructure upgrades for financial institutions.

While a significant project, ISO 20022 is just one of multiple digital transformation projects being juggled by financial organisations. Regulatory deadlines also mean that firms are under pressure to allocate financial resource to these upgrades within tight timeframes, and it can be difficult to secure the budget for the best and most robust technology solutions.

Rather than viewing the ISO 20022 project as another project for which budget needs to be stretched, firms would do well to shift their thinking toward the benefits and opportunities that effective transition can bear for the long term.

Positioning the benefits presented by investing in a strong ISO 20022 migration as a business case allows banks to better understand the new opportunities the transition will provide. Such benefits may include:

- Reduction of costs through the elimination of legacy systems and applications;
- Increased automation and improved straight-through processing, resulting in reduced friction;
- Growth of available opportunities through the building out of new APIs based on ISO 20022;
- Development of new customer-centric products and services with greater speed, transparency and granular in tracking; and,
- Increased fraud detection and efficiency of security processes.

Capitalising on such opportunities is imperative in an increasingly competitive market, where demanding clients expect access to the most innovative products and services – which soon will only be attainable for institutions that have invested sufficiently in their technology portfolio. Those which invest early and wisely will also be better positioned to meet this demand and increase market share through first mover advantage.

04 | Building a clear picture on the true cost and alignment necessary to complete ISO 20022 transition

The transition to ISO 20022 impacts a bank's entire value chain and the overhaul required to modernise is no small endeavour. Though financial organisations may instinctively treat the ISO 20022 migration as a typical IT project, the benefits of outsourcing the management of this project can often outweigh the strain of in-house delivery.

The shift to ISO 20022 is just one of a portfolio of projects any given bank is working on, and the need to ensure the migration is achieving the attention it requires means a dedicated staff may be called for. This is expensive, difficult to chorale and takes time.

Deutsche Bank's Ultimate Guide to ISO 20022 Migration explains that for a mid-sized bank, the ISO 20022 migration project can result in a high four-digit outlay in terms of 'project working days,' and for larger banks, this outlay is likely to be even higher.

Third party providers equipped with the relevant technology and expertise offer a pragmatic option for institutions embarking on their ISO 20022 transition. Though completion of these migration efforts are unavoidable, the attention and level of disruption they cause to ongoing business matters can managed.

Outsourcing ISO 20022 migration ensures not only that the project is handled by professionals who are dedicated to streamlining this specific process, but protects IT staff who likely have little if any bandwidth to give the project the attention it requires.

On top of this, risks associated with ineffective migration to ISO 20022 are not small, and improper implementation has the potential to cause long-lasting impacts which can damage client relationships and reputational image for the institution.

05 | Human resource: allocating talent wisely

The Deutsche Bank report notes that the following areas of an organisation will be typically impacted during the migration process: top management; transaction banking (payments and securities); treasury; IT (process management, IT infrastructure, etc); sales/relationship management; vendor management; operations; service; risk management and legal. The ISO 20022 migration evidently bears impact on many, if not all, departments within a financial institution.

The report states that "significant and complex internal changes are on the horizon for banks. It is crucial, therefore that senior management are aware of the magnitude of the project in terms of resources and budget." It elaborates that the IT migration itself will have an impact that goes far beyond core payments processing, affecting peripheral systems such as anti-financial-crime applications, liquidity management, billing, accounting report, nostro reconciliation and archive systems.

"It is therefore not just a cash management product challenge; everyone from top management to operations to human resources will need to be involved."

Given the scale and breadth of the impact that any ISO 20022 migration project will bear across an institution it is clear that the undertaking is immense, and banks would be well-advised to consider engaging third-party expertise to assist in the project.

Certain technical questions which firms should be able to answer at the outset of their migration process may include the following:

1. Who will write the Message Implementation Guides?
2. How will production support be set up for translation failures of messages?
3. Who will provide Training and Knowledge transfer across teams within the institution? (operations, support, sales and implementation)
4. Who will provide Sales Enablement so that the value of ISO 20022 is passed on to the bank's customers?

06 | Conclusion

Crowded regulatory timelines, busy internal roadmaps, clunky legacy systems and growing pressure to reach compliance as deadlines loom, mean that any digital transformation project is a true challenge for financial institutions.

However, given the centrality of ISO 20022 and the pivotal role it is set to play in the future of the payments ecosystem, firms do not have the luxury of time, nor the luxury of erring in their approach to migration plans.

Without sufficient (and early) attention given to the ISO 20022 project, banks run the risk of failing to finalise their transition and finding themselves in breach of compliance regulation. Further, an inability to operate using the landscape's new standard for payment rails would render banks unable to fulfil basic duties – let alone leverage the bountiful opportunities for innovation in the sector.

Helpfully, the emergence of technology solutions offered by third-party providers provides institutions with a resilient route to navigating ISO 20022 migration. The ability to lean on the expertise of dedicated providers ensures that financial institutions can avoid becoming a cautionary tale during their transition.

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