



We have a vision of how electronic payment systems will look in the future with the knowledge, scale and resources to deliver it.

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Bringing merchant acquirers into the 21st century

An industry article from ACI

Merchant acquiring - an often overlooked part of the payments market - has now become a key element of a growing and vitally important payments industry. Card transaction volumes and types are growing rapidly. If merchant acquirers don't keep up the pace and invest in new technologies, they could lose out.

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As the dust settles from the financial crisis, one thing is clear: high-risk banking activities are out, while payments as a source of income for financial institutions are back on the agenda. As the bedrock of banking, payments have proven their worth in recent years.

According to the Capgemini World Payments Report 2010, the payments business has withstood the financial crisis well. The latest data shows that the global use of non-cash payments continued to grow in 2008, despite the financial crisis. The overall growth in volumes accelerated to nine percent in 2008 from seven percent in 2007. Globally, cards remain the preferred non-cash payment instrument, accounting for more than 40 percent of payments in most markets and above 58 percent globally¹.

With card payments being such an important part of what has become a vital banking operation – and with new technologies such as contactless payments being deployed at the point-of-sale – it is key that every element of the cards system remains as resilient, operationally efficient and as effective as it can be. More than ever, merchant acquirers are a critical part of the payments industry, providing an essential service to retailers. Without high-quality services provided by the acquirers, the smooth processing of payments from the vast array of card issuers on the market could begin to show cracks.

But despite this risk, many merchant management systems currently in use across the globe were designed and constructed in the 1980s and 1990s. For decades these systems have been working effectively, but their age is starting to show. They are becoming increasingly costly to maintain, difficult to update with compliance mandates, hard to scale as electronic payments grow, and often do not support new card products and channels such as contactless and mobile payments.

In fact, operational staff often find themselves fighting to stand still. Neither budget nor resources are available to do much more than maintain the status quo. Overall,

the pressure of maintaining and supporting legacy systems consumes resources and risks seriously reducing a merchant acquirer's ability to remain profitable.

To compound this technological challenge, merchant acquirers are required to compete in an increasingly competitive market – and one where merchants are increasingly powerful. They need to offer competitive terms to merchants in order to attract them, and provide good service to retain them. Acquirers therefore have to maximize their customer service while continuing to optimize their revenue and keep costs under control if they are to survive in the 21st century.

This perfect storm of legacy technology combined with new challenges means it is high time that merchant acquirers invest in new systems that will allow them to survive and thrive in this increasingly buoyant market.

The tipping point

The case for technology investment is clear, but it is the bottom line that dictates business decisions. In the case of merchant acquirers, it is the opportunity for growth, merchant attrition rates and ultimately their cost per transaction that will spur them into action. When their operations are no longer able to support strong growth and their costs get so high that their margins come under increasing pressure, then it is time to put a plan in place. This will not only allow them to lower costs, and provide a better service to existing customers, but will also give them the opportunity to create new revenue streams through new products and services, or through expansion into new markets.

But before taking the plunge, there are some things to keep in mind. From the outset any new system should be based on core principles of openness, flexibility and efficiency. It is important to choose a solution with a core technology that is common to others being used within the business. This will ease integration, set-up and management in the short and long term. It is also

¹ World Payments Report 2010, Capgemini, October 2010

worth considering whether a solution has a strong, flexible, modern, message-based design. A highly modular approach means that a system can be upgraded, modified and supported in discrete areas without impacting other parts of a system.

Costs can be significantly lowered through the use of modern technologies to streamline operations. Just one example is the real-time boarding of new merchants remotely, through leveraging new technologies. This typifies the benefits an acquirer should be looking for since it ensures customer satisfaction, facilitates growth and provides for improved efficiencies in customer service. Other ways of lowering costs through technology are through scalability. It pays for the acquirer's return on their investment to ensure that their platform can support future growth through linear scalability. It means they can grow their merchant base without further significant investment.

Other issues to consider include ensuring that a system can acquire payments from multiple international card schemes, provide global processing through support for multiple currencies, and support central and cross border acquiring. With globalization continuing its march forward, being able to deal with a range of countries and their domestic regulatory requirements is a must.

In a competitive market flexible pricing options are essential. The ability to offer merchants incentives such as volume-based rebates, revenue sharing or dynamic currency conversion (where they can enjoy the benefits of exchange rate gains along with the acquirer) are all ways of gaining market share. The spread of different standard pricing offerings such as interchange-plus, tiered and blended-rate pricing are increasingly in demand by larger retailers due to the industry trend towards the unbundling of merchant fees. In order to be able to support these demands, acquirers must ensure that they are qualifying transactions for the best possible interchange rate. In addition, providing the larger retailers with the MIS information necessary for them to submit transactions that qualify for the cheapest possible fee programs is a real value-added service.

An overhaul for Moneris

Moneris Solutions, the world's eighth largest processor of debit and credit card transactions, has transformed its merchant management service and saved more than \$10 million in just two years with the implementation of new technology. The company has also reduced merchant fraud by 25 percent year-over-year by overhauling its systems.

In 2005, the Canada-based company decided to move away from its existing in-house developed processing system and bring in a leading solution that would enable it to respond to the constantly changing requirements for its approximately 350,000 merchants, and provide scalability and stability for the future. The project integrated with the existing systems it had for authorization processing, and now processes more than three billion transactions a year.

Moneris Solutions also implemented a risk management system to detect and manage merchant fraud. The powerful rules-based engine automates what were manual processes, allowing analysts to spend more time working on fraud cases and reducing potential threats that will further limit the company's exposure to financial risk.

Jim Baumgartner, President and CEO of Moneris Solutions said, "We have revolutionized the way we work with our customers, through improving all aspects of customer service from the way we handle calls to the data that we are able to provide them. This has directly improved our customer satisfaction levels."

Meanwhile, to further boost customer service levels to merchants, a successful acquiring system should allow the creation of customized merchant contracts and management – a one-size-fits-all approach is no longer acceptable. It is also important to add flexible fee structures, frequency and transaction segmentation options for settlement, and the ability to provide settlement advice and merchant statement channel delivery options. Ideally acquirers should be able to quickly and easily offer new targeted packages of terms and conditions, perhaps based on volume and market sector, but where necessary target specific merchants with promotional, introductory or periodic offerings.



“Big bang” or phased approach

Once the tipping point has been reached and all the considerations have been taken into account, the next step is to decide on how to migrate to a new system. In the first instance, it is vital that the acquirer teams up with a trusted partner with a strong track record in migrations. It sounds obvious, but it can't be over emphasized - any migration must go smoothly with no downtime, merchant impact or lost payments.

There are basically two ways to go about this process: a phased approach or a big bang approach. The former allows an acquirer to move a set number of merchants (or type of processing) over a period of time to allow for new features to be introduced to the new system as it is implemented. This has the advantage of allowing an acquirer to bring a basic system up and define each subsequent phase to meet specific business requirements in a controlled manner. An example might be for an international acquirer to convert merchants across to their new platform by country (or possibly to migrate authorizations processing by card scheme network e.g., Visa, MC, AMEX®, JCB, CUP, etc.)

The big bang approach - where conversion takes place as one event (typically over a weekend) - can also work just as well. The key to success in this case is to ensure that acceptance tests and dress rehearsals have been run

several times during a testing phase, and there is a clear, step-by-step process with a confirmation checklist for turning one platform off and turning on a new one. It is also vital that the system can be rolled back if there are any problems throughout the process - with a detailed plan developed to guide the process.

Whatever the approach - and both can be effective - having a technology partner that can illustrate that their work is tried and tested is vital. A partner with expertise in working with acquirers' business and IT organizations to develop the conversion strategy is key. The use of standard tools and a proven capability enables the process to be consistent, reliable and repeatable - and mitigates the risk significantly.

Taking on such a process can be daunting, but it is key that merchant acquirers take a look at their profitability and cost per transaction - and make some important decisions about how to redesign or accelerate their technology strategies. This will allow them to effectively handle the next generation of electronic payments, while facilitating growth through new products and services, and through geographic expansion. By doing so, they will also be able to remain competitive, reduce their merchant attrition rates and increase efficiency, while meeting increasing compliance and regulatory requirements. And ultimately, it will cement the profitable future of the forward-looking merchant acquirers in the 21st century.



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