

Slide 1 of 28 2006 e-Financial WorldExpo
Sustainable Models for B2B* eFinancial Service Delivery (Part 1: Looking under the Hood)



Nahum Goldmann www.ARRAYdev.com © ARRAY Development, 2006

Slide 2 of 28 2006 e-Financial WorldExpo
Presentation Covers

- **Compliance-driven transactional FI**
 - Profitable, responsive, innovative and accountable*
 - B2B value-added payment and treasury services
- **Main conclusions:**
 - New *business models are required* to sustain transactional delivery of eFinancial services
 - B2B transactional outsourcing is an *intermediary* business
 - *Smart* transactions transform *technical requirements*
 - To ensure successful service delivery, *in addition to their processing costs, all regulated entities (FIs) have to quantify the costs of online compliance policies**
- Here are the questions... Not all the answers...

Nahum Goldmann www.ARRAYdev.com © ARRAY Development, 2006

Slide 3 of 28 2006 e-Financial WorldExpo
Looking at Things Differently

- Paradigm shift -- forces a radically different way of doing business
- Asking wrong questions -- one gets wrong answers
- Turning old paradigm on the head -- by looking under the hood -- what'd really happened?
- Ensuring win-win outcomes -- between all the stakeholders

Nahum Goldmann www.ARRAYdev.com © ARRAY Development, 2006

Slide 4 of 28 2006 e-Financial WorldExpo
New Reality: Globalization Contradictions

- **Disparity between**
 - Global eBusiness infrastructure (*One size fits all*; Low cost outsourced global "grid"; *homogenic ubiquitous basic offering for all clients*; *Carr*: IT *shift* from competitive edge to commodity)
 - Commodity service model: Globally dominating market segment "gorillas" (1Amazon!; 1eBay+1PayPal+1Skype!; 1Google!)
 - Limited life of personalized solutions and ongoing technology renewal (4-12 months moral obsolescence; *Technology has a shelf life of a banana" -- McNealy's Law)
 - Managed by multinationals (impersonal; mainly selling existing solutions [bad fit?])
- **and**
 - Need for personalization + competitive differentiation (i.e., heterogeneous offering by definition very expensive, bleeding edge, unreliable)

Nahum Goldmann www.ARRAYdev.com © ARRAY Development, 2006

Slide 5 of 28 2006 e-Financial WorldExpo
Adding eFinancial Value in B2B Transactional Procurement

- **B2B Transactional Procurement**
 - Usually defines transactional delivery of services
 - Especially if outsourcing is involved
- **1980-90s paradigm:** Procurement value-added by
 - Negotiating cost discounts due to *bulk purchasing*
 - Locking organization in *5-10 years inflexible contracts*
- **Transactional commodities* purchasing paradigm**
 - Intermediaries typically *subtract value* in bulk long-term commodity procurement (i.e. Canadian Government is a far too *small player**; Negotiation overhead; i.e., long distance, travel, etc.)
 - It is *agile purchasing with integrated eFinancial enablers* that wins today (i.e., Shopping for the best-lot deal *online*; Switching to new technologies such as VoIP; Reverse auctions, TWIST standards, etc., etc.)

Nahum Goldmann www.ARRAYdev.com © ARRAY Development, 2006

Slide 6 of 28 2006 e-Financial WorldExpo
Transactional Procurement Projects: Contradictions

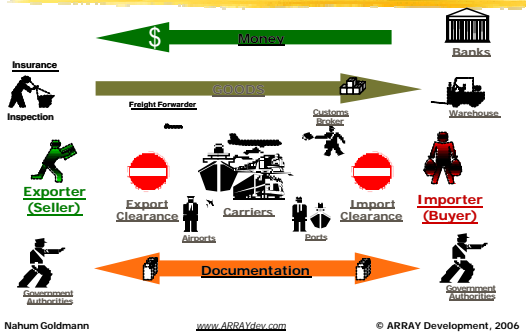
- **Persistent disparity between**
 - FIs (i.e., *eFinancial departments*): New opportunities require financial engineering innovation (bleeding-edge change!!!)
 - Clients (i.e., *purchasing departments*): Seek ubiquitous services (mature, lowest cost) from *well established Vendors*
 - Vendors (increasingly a limited number of multinational service "market gorillas"): Seek Clients (consolidated, long term, predictable margins) to *secure monopoly offerings*
 - **and**
 - Enduring failures of large procurement projects (various FIs, government and large industry — examples abound; Vendors typically deliver *What Client asked for* not *What Client will require**)
- Advanced project management, accountability, and process improvement frameworks do not address the core problem!*

Nahum Goldmann www.ARRAYdev.com © ARRAY Development, 2006

Slide 13 of 28

2006 e-Financial WorldExpo

Example 2: International Trade (ViaSafe)



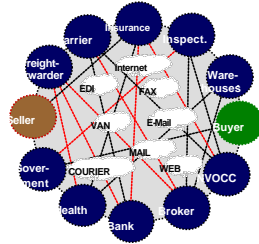
Nahum Goldmann www.ARRAYdev.com © ARRAY Development, 2006

Slide 14 of 28

2006 e-Financial WorldExpo

Example 2: International Trade (ViaSafe)

- Mandatory, bureaucratic paperwork.
- Per shipment:
 - 27 – 30 different parties
 - 40 documents
 - 200 data elements (30% of which are repeated at least 30 times)
 - Re-keying of 60 – 70% of all data at least once



Nahum Goldmann www.ARRAYdev.com © ARRAY Development, 2006

Slide 15 of 28

2006 e-Financial WorldExpo

Relevant Accountability/Compliance Regulatory Requirements (Barbados example)

Regulatory Requirement	Regulatory Source
The Financial Action Task Force (FATF) Money Laundering and Financing of Terrorism (Prevention and Control) Act Cap. 129	GB, OECD and international Barbados Anti-money Laundering Authority
"Know your customer" Guidelines under Act Cap. 129	Barbados Anti-money Laundering Authority, Central Bank of Barbados, The Office of the Supervisor of Insurance, Securities Exchange Commission, the General Post Office, Ministry of Industry and International Business
The Caribbean Financial Action Task Force (CFATF)	Caribbean regional
International Accounting Standard 36	OECD and international
International Financial Reporting Standards (IFRS), Financial Reporting for Commercial and Industrial Entities (CI)	International Accounting Standards Committee
Basel I or II	Basle Committee on Banking Supervision (BCBS)
Financial Sector Assessment Programme	The International Monetary Fund (IMF)
Standards on exchange of information on anti-money laundering	International Association of Insurance Supervisors

Nahum Goldmann www.ARRAYdev.com © ARRAY Development, 2006

Slide 16 of 28

2006 e-Financial WorldExpo

Relevant Accountability/Compliance Regulatory Requirements (Barbados example, con't)

Regulatory Requirement	Regulatory Source
Standards on exchange of information on anti-money laundering	International Organization of Securities Commissioners
USA Patriot Act	US
Financial Modernization Act (Graham-Leach-Bliley)	US
Sarbanes-Oxley Act	US
SEC rule 17a-4	US
Treasury Department's Office of Foreign Assets Control	US
The "travel rule" 31 CFR 103.33(g) of the Bank Secrecy Act	US Treasury Department
US Public Health Security and Bio-terrorism Preparedness and Response Act	US
California Security Breach Notice Law	US, California
EU Privacy laws	European Union
The Financial Services Action Plan (FSAP)	European Union
Single Euro Payments Area (SEPA)	European Union and international
Prudential Sourcebook (PS)	United Kingdom

Nahum Goldmann www.ARRAYdev.com © ARRAY Development, 2006

Slide 17 of 28

2006 e-Financial WorldExpo

Transactional Conflicts

- A typical online transaction
 - Many participants — *Who is accountable?* (Hierarchical accountability: Often in different organizations; Sometimes in several countries with different legislative requirements)
 - Today's Clients (corporate and individual) demand quantitative transactional accountability from their FIs who they see as B2B intermediaries*
- Between Client's policies and industry's offerings
 - I.e., cost of \$1M insurance vs. \$750k industry standard
 - Global changes to implement small local differences
 - Sometimes the most flexible wins...
 - but sometimes the Vendor takes unreasonable risks..
 - Commodity processes have transparent margins -- nowhere to hide inefficiencies and additional costs*

Nahum Goldmann www.ARRAYdev.com © ARRAY Development, 2006

Slide 18 of 28

2006 e-Financial WorldExpo

Compliance-Controlled Transactions

Typical industrial transaction
"Lean" data format = Basic Data

Example:
• Simple online purchase

Basic Data:

- Vendor
- Customer
- Goods/services
- Quantity
- Value
- Date

Average management costs: 3% (Australia/New Zealand IT sourcing study - CIO Australia 2005)

Typical compliance-controlled transaction
"Fat/Expandable" data format = Basic Data + Policy Smarts
I.e., entitlements, constraints and what if policy attributes

Examples:
• Government procurement/travel
• Anti-Money Laundering (AML)
• SafeBox

Basic Data:

- Vendor
- Customer
- Goods/services
- Quantity
- Value
- Date

Average management costs: 7.1% (premium for "accountability and transparency")

Insurance 1:

- Accidental death/dismemb. - \$1M
- Note: Voided in a war zone
- Note: Voided if piloting a light plane
- Note: Voided if postmortem found

Insurance 2:

- Emergency Cash Transfer - \$5K
- Note: Increase to \$10k with EX-4 authorization
- Note: Increase to \$20k with EX-6 authorization

Insurance 3:

- Last document and ticket replacement - \$5K
- Note: ...

Slide 19 of 28

2006 e-Financial WorldExpo

Policy Smarts *Must* Follow Transactions

- Governments regulations require comprehensive policy-driven *accountability/transparency trails*
 - Including *entitlements, constraints* and *what if* policy attributes is essential for accountability trail systems
 - Accountability necessitates *policy-compliant smarts* — “fat” expandable data-handling formats
- Current industrial standards and systems are *conceptually unsuitable* for extensive transactional compliance-handling formats
- *but* Financial Industry is [*slowly!*] moving to accountability trails [i.e., SarbOx, Basel, AML, anti-terrorist, ...]

Nahum Goldmann www.ARRAYdev.com © ARRAY Development, 2006

Slide 20 of 28

2006 e-Financial WorldExpo

Compliance-driven Service Transformation

- Effective service transformation means:
 - *Radically* overhauling financial (eFinance and legacy) business processes
 - Seeking opportunities for outsourcing
 - New B2B Partnerships for eFinancial institutions
- Exploiting opportunities for outsourcing:
 - Compliance policies should be optimized for transactional delivery (will they be enforced in India?)
 - Ensuring business profitability in transactional outsourcing [for all 3 partners — FIs, Vendors and Clients]
 - In long-term transactional bids *eFinancial intermediary has to monitor survival* of “Vendor-gorillas” on behalf of its business clients

Nahum Goldmann www.ARRAYdev.com © ARRAY Development, 2006

Slide 21 of 28

2006 e-Financial WorldExpo

Quantitative Financial Optimization

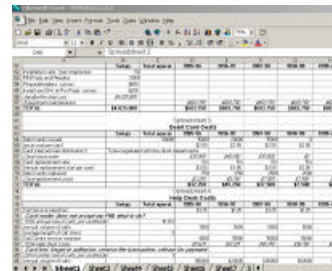
- Key objectives of service delivery optimization
 - For FIs and Clients: Ensure *benefits harvesting*
 - + for FIs and participating Vendors: Long term *profitability*
 - > by modeling microeconomics of transactional business lines and support processes
- Tool
 - Multidimensional *transactional spreadsheet*
 - > *populate* by projected and benchmarked costs
 - > *optimize* by FIs, *Clients and Vendors business criteria*
- Outputs
 - Quantitative and Qualitative business architecture
 - > Cost/performance inputs/constrains for technical architecture

Nahum Goldmann www.ARRAYdev.com © ARRAY Development, 2006

Slide 22 of 28

2006 e-Financial WorldExpo

Defining Business Architecture — To Ensure Sustainability



By optimizing transactional spreadsheets

Nahum Goldmann www.ARRAYdev.com © ARRAY Development, 2006

Slide 23 of 28

2006 e-Financial WorldExpo

Optimizing Business Architecture

Outsourcing leads to transparency by

- Ensuring *performance levels*
- Addressing evolving *user expectations*
- *Benchmarking* competitive performance/cost
- Recovering *initial investment* and Client's *costs*
- Ensuring FIs and vendor's (long-term-5-9 years) *profitability*
- Critical role of *Exception Management (94% rule!)*
- *Risk management* (service failure, overspent, security, insurance coverage)
- Taking into account *commodification* of routine offerings/need collapse of personalized offerings
- *Service guaranties* for routine online services

Nahum Goldmann www.ARRAYdev.com © ARRAY Development, 2006

Slide 24 of 28

2006 e-Financial WorldExpo

Sustainable Models for B2B* eFinancial Service Delivery (Part 1: Looking under the hood)



Nahum Goldmann www.ARRAYdev.com © ARRAY Development, 2006

Slide 25 of 28

2006 e-Financial WorldExpo

Our Model's Application: Key Conclusions

- Micro-economics of this business must be fully understood ASAP —> to be in an *informed negotiating position*
- *Upfront financing is essential for all transactional delivery models* (i.e., *VC financing model*)
- *The FI and the Client cannot fully transfer their business risk to the Vendor*
- *Services that can handle transactional policies don't have to be exclusive*

Nahum Goldmann

www.ARRAYdev.com

© ARRAY Development, 2006

Slide 26 of 28

2006 e-Financial WorldExpo

Our Model's Application: Key Conclusions (con't)

- *Structural lack of profitability is a major risk factor for FIs, Vendors and the Client*
- *Leveraging its outsourced services might greatly benefit the FI and the Client*
- FI's (and Client's) principal challenge: *Delegate, but don't abdicate!* (D.McGaw)
- FI's need for *ongoing marketing/sales/maintenance cycles to Clients* (*competitive positioning*) and Vendors — *costly but essential!*
- *The critical role of the FI's Business Prime as the Compliance-Driven Marketing Intermediary (it is NOT about technology)*

Nahum Goldmann

www.ARRAYdev.com

© ARRAY Development, 2006

Slide 27 of 28

2006 e-Financial WorldExpo

RFPs: Top Concerns to Address

- *Articulation of transactional compliance policies* (Multiple jurisdiction requirements + Smart Transactions)
- *Agile flexible contract* is a must
- *Technology architecture should be based on profitable business architecture*
 - *Agile development* through prototyping
 - Ensuring *affordability of exception management*
 - Does profitability of service providers depend on *retaining manual service business model?*
 - IT Vendor's "cost-plus" mentality is no longer affordable
 - Who at FI will *market services to Vendors and Clients?*
- *Re-engineering* of old business practices

Nahum Goldmann

www.ARRAYdev.com

© ARRAY Development, 2006

Slide 28 of 28

2006 e-Financial WorldExpo

Sustainable Models for B2B* eFinancial Service Delivery (Part 1: Looking under the Hood)



Nahum Goldmann

www.ARRAYdev.com

© ARRAY Development, 2006