Chapter X

E-Commerce in the Financial Services Industry

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INTRODUCTION

The financial services industry consists of retail financial services such as retail banking, consumer lending and mortgage banking, insurance (life, health, property) and financial markets. Each of these sectors has seen tremendous growth in the services and products delivered over public internetworks such as the Internet. The recent signing into law (November 1999) of the Gramm-Leach-Bliley Act in the U.S. has enabled firms such as retail banks to provide an unprecedented array of financial services. As competition within the industry increases, firms of all sizes are looking to achieve competitive advantage through Electronic Commerce (EC). According to a recent study by the Securities Industry Association and the TowerGroup, securities firms in North America spent $3.9 billion on Internet-related information technology (21% of their total IT spending) in 1998, and this is expected to double by 2002 (SIA, 1999).

Implementing such services is not a trivial task, however. Concerns over security, privacy, legal compliance and other sources of risk must be addressed. While specific enabling technologies have been developed to address some of these issues, innovations in technology and policy will still be required. For example, some interesting issues arise from the application of Internet technologies, such as cookies and Web advertising, to financial services such as online banking and bill payment, and investment advertising.

In this chapter, we will present an overview of some of the current services and products provided by the financial services industry through EC. We will then discuss some important issues specific to the application of EC in financial services. Finally, we will present business strategy issues facing companies in the industry.
PRODUCTS AND SERVICES IN THE FINANCIAL SERVICES INDUSTRY

Virtually every aspect of financial services has been affected by the growth of the Internet, World Wide Web and EC. In this section, the main sectors of the industry will be outlined, along with an overview of how firms within these sectors make use of EC to interact with customers.

Retail Banking

Account Maintenance

Most major retail banks now offer a set of services via the Internet. As personal computers became more commonplace in the home in the late 1980s and early 1990s, many banks developed proprietary “PC banking” systems with custom software running on personal computers that would connect over private networks to the bank’s central information systems. Such an architecture required each bank to maintain a private, secure network. Software distribution was also an issue as bug fixes and new features had to be distributed via floppy disk or CD-ROM to customers who were then responsible for upgrading.

Today, the Internet and Web-based applications have displaced these PC-based systems. With enabling technologies such as Web browsers and encryption implemented in protocols such as Secure Sockets Layer (SSL) over the Web, online banking applications have migrated to Web-based applications. The burden of establishing a connection to the Internet and for installing a standard Web browser is placed on the customer while the bank can more easily maintain and update the applications that reside on their servers.

The basic set of consumer-oriented personal banking services are directed at basic checking and savings account maintenance. Such services include checking account balance, check clearance, account transaction history, stop-payment on checks, check re-ordering and so on. Many banks also offer basic search tools to locate checks or other transactions by date or amount. This set of services is generally also provided via Automated Teller Machines (ATMs) and via touch-tone telephone in addition to proprietary PC banking and Web-based banking applications.

Another interface to this set of services comes from the integration of online banking and personal or small-business accounting software packages (often called Personal Financial Management (PFM) software) such as Quicken®, Microsoft Money® and QuickBooks®. In this case, the personal accounting software includes a module that provides access to personal banking transactions via the Internet. Transactions initiated via the PFM software are also recorded locally in that software’s internal database for future reference. In this fashion, the PFM software can act like an aggregator of one’s financial information by accessing the relevant data from one or more banks.
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