Open finance: ambition and policy approach

1. Open finance use cases and current stage of development

1.1 Open finance objectives and use cases

The Chair explained that Open Finance refers to the sharing with third-party providers and subject to the approval and control of the customer, of personal and non-personal customer data held by financial sector intermediaries and other data holders for the purpose of providing a wide range of financial and information services. This concerns both individual customer data and company data. It is an extension to a broader range of data (credit, savings, investment, insurance, pensions) of the Open Banking concept which focuses on payments and the sharing of bank account data.

A regulator suggested that the starting point for open finance is data, so for it to work financial services firms need to be enabled to better use data. Some have started to leverage the experience of tech companies, which have developed significant know how in this area. There are a number of use cases for open banking, from helping people to manage their finances through to helping customers who have credit-worthiness issues to prove that they are able to access credit. If people accept to share more of their financial information, this will enable more useful and innovative financial products and services, extending potentially beyond financial services. Insurance companies for example have a great deal of non-financial information that is important for providing the right level of insurance cover. Getting access to more of that kind of data will allow providers to better hone products and services for individual customers and firms and to better manage risks.

An industry representative emphasized that open finance creates many opportunities in terms of new services, risk prevention and improved underwriting in the insurance industry, beyond the sharing of insurance data with some third parties. With open finance the insurance sector could collaborate with banks in novel ways. When a bank agrees a mortgage, it collects a great deal of data from customers. Insurers could reuse that data to make an offer for real estate insurance for example. Open finance can also facilitate the switching of insurance, which involves knowing the claims history of a customer coming from another insurance firm. Open Finance can moreover be used for steering increasingly complex supply chains and anticipating problems, using the internet of things (IoT) and satellite data. There are many examples of data sharing already. The speaker's firm has for example developed a digital commercial platform for its business customers, which aims to enrich the data for customers so that they have better risk control.

A second industry representative observed that open banking has created an expectation for frictionless user experiences, which is not yet a reality in the insurance sector but could be supported by open finance. Flight delay insurance products historically required the filling up of long forms and the provision of extensive evidence of the costs incurred by customers for example. Open finance allows new products to be developed such as a time-guaranteed flight delay insurance product, whereby if a flight is delayed by 30 minutes, the service is automatically triggered and payment automatically enters the customer's account within an hour of them reaching their destination. This is the type of frictionless experience that customers are expecting in a digital world. Open finance also enables options that were not possible in the past by linking different parts of an ecosystem in a more efficient way supported by computation. This is the case of rapid damage assessment, which uses real-time aerial photographs to handle natural catastrophe events combined with proprietary models powered by AI. This helps risk managers to send the right response very quickly. Another example concerns risk and data services. The speaker's firm, a major insurer, has partnered with a leading data analytics organisation to develop a supply chain resilience solution for corporates' supply chain risk managers. With this tool risk managers can identify the main vulnerabilities of the supply chain network and monitor risks such as climate-associated risks.

1.2 Stage of development

An industry representative stated that open finance already exists in the market and has preceded regulation. Open finance has started in two ways: banks as a platform (BAAP) and banks as a service (BAAS). With BAAP, customers of the bank such as SMEs can benefit from an enriched banking offer, with the integration of financial and extra financial innovative services from external partners, such as access to legal advice, insurance or bookkeeping services. With BAAS, the bank provides its core banking services (e.g. payments, fight against fraud) to third parties such as distributors in an embedded way. Open finance therefore works both ways with financial institutions integrating some non-financial services, and vice versa and is about creating interactions between finance and providers from other sectors, which is supported by European data regulation, such as the Data Act.

A regulator agreed that open finance is already a reality in the market, because the fintech world did not wait for regulation to implement new services. The Payment Services Directive 2 (PSD2) regulation written over 10 years ago focused on payments and account information services for individuals to obtain a consolidated view of their personal finance, but it was already outdated when it started to be implemented. B2B business models sharing data beyond the scope of PSD2 such as accounting information e.g. to support accounting activities or evaluate credit-worthiness were already starting to emerge. In addition, while PSD2 focuses on payment accounts, fintechs are already accessing savings account and insurance data by web scraping.

2. Expected benefits and challenges of open finance

2.1 Expected benefits

A public representative emphasised that open finance facilitates access to more financial information in a concise manner, which could help with the provision of credit scores and risk assessments for individual and corporate customers. For an individual, there is the opportunity for improved credit assessments and access to financial products that are more tailored and to innovative personal financial management and investment solutions. For businesses, open finance can support accounting processes, as well as facilitate access to funding. Cashflow management could also be conducted in a more effective and efficient manner. One of the most important benefits and use cases of open finance is that it will likely facilitate the access of smaller companies such as start-ups and SMEs to effective financial solutions and funding. This is an opportunity to level the playing field with larger firms, provided the latter players do not capture all the advantages of these innovations. The public representative noted that open finance can also enhance competition in the financial sector by allowing the emergence of novel services and new players such as fintechs. Open finance can therefore also contribute to the digital transformation in the financial sector.

An industry representative added that data sharing with appropriate security measures could generate a great deal of benefits for the customers of insurance companies by e.g. streamlining the access to services through pre-populated information, simplifying underwriting processes, or improving risk prevention with data monitoring and analytics.

A regulator observed that many benefits have already been seen from the implementation of open banking in the UK. Today, over 7 million consumers and 750,000 SMEs are using open banking products and services to manage their money and to make payments. The tax authority, HMRC, is also a major proponent and user of open banking.

2.2 Potential challenges and risks

A regulator remarked that there is a trust challenge with open finance that needs to be resolved. There is a need to prove to consumers and SMEs that there are strong benefits in terms of sharing their data. For customers to consent on a regular basis, they need to understand that it is safe to do so. Therefore, we need to address the potential risks of data sharing and ensure that players who control, use and manipulate the data can be trusted.

The Chair agreed that trust is key in this area. Customers need to know what is happening with their data and be able to control it, which links to the issue of consumer consent. The younger generation however seems to care less about what happens to their data.

A regulator observed that PSD2 had been implemented to build trust. A number of actors were already operating in the payment space before PSD2 and the legislation was put in place to regulate these actors and to ensure that accounts were accessed in a more secure way. This helped to build trust between consumers and the financial counterparties involved such as banks and new service providers. Replicating this approach and building trust in a broader environment is the core issue to be tackled for making open finance a success.

3. Main issues to consider in the EU open finance framework and lessons learned from PSD2

3.1 Main objectives and issues to consider in the open finance framework

The Chair stated that the Commission is working on a legislative proposal on open finance. The aim is to empower consumers and also to foster innovation in the provision of financial services, building on the experiences of open banking and PSD2. To encourage open finance further there is probably a need for additional rules. A key question is what can be learned from the PSD2 experience, which was quite challenging to implement. PSD2 is being revised in parallel to adapt it to today's challenges. There are questions about what regulation is needed to foster open finance, what further incentives policymakers and regulators can build into the regulatory framework to encourage future developments and how this interacts with existing EU horizontal data frameworks, in a context where the use of data may go far beyond the financial sector.

An industry representative suggested that there are some prerequisites that need to be considered to make open finance useful and beneficial for customers and to contribute to innovation in the financial ecosystem. The first concerns the type of data being shared. Insurers have a great deal of intellectual property in their data, for example concerning the way tariffs are fixed and tariff structures which they can probably not share. Secondly, there is a need for a very clear legal, and also probably contractual, framework defining the conditions under which data can be shared and the use that will be made of it. Thirdly, a case-by-case or step-by-step approach should be adopted in the policy approach, because the number of use cases is vast and their specificities need to be taken into account. Additionally, it has to be ensured that the required technical infrastructures are available in Europe to implement open finance, because much of the technology needed to support such concepts is currently provided by big tech companies, which are typically outside of Europe. The conditions need to be in place to ensure that European organisations are not prevented from leveraging the data that they manage and produce in the first place.

A second industry representative noted that the implementation of a new technology always has to start with the question of what business problems it aims to solve and then which underlying technologies are best suited e.g. APIs[1], blockchain… Otherwise there is a great deal of unnecessary hype. Secondly incumbent players no longer need to build a specific digital strategy, they need to think first about how their business strategy should be adapted to a new digital world and how new technologies and data can be used to support this new business strategy. Companies should focus on the business problems that need to be solved and the related use cases and then evaluate how technology can help them to achieve this.

A regulator emphasised that the role of regulators is not to create new markets, it is to avoid market failures and remove obstacles to the emergence of new services. For example, incumbents not sharing their data or creating the appropriate incentives in terms of standardisation, liability and level playing field for the market to develop effectively. Open finance regulation should therefore be an enabling framework. It was easier to start with open banking because there was available current account data, deposit data and suchlike in standard formats. For pensions, investments or insurance, which are due to be covered by open finance, there is a great deal of inconsistency across firms in the way data is held and in some cases, it is not available in a digital format. These are key issues that will need addressing. It is also very important to anticipate the data sets that will need to be used in an open finance and data sharing economy and to ensure that there is full access to that data and information, because much of it sits in places beyond Europe.

A public representative noted that all of the regulatory tools needed to support the development of open finance and create a level playing field in this area are present in Europe, with the AI Act, the Data Act, the digital finance package, PSD2 and its revisions. Now there is a need to look at the use cases that will emerge in the market and the players concerned and what additional rules may be needed.

3.2 Potential areas of focus for the open finance framework

3.2.1 Standardisation

An industry representative stated that insurance activities are not particularly standardised, either within markets or across markets. There is some work to be done to standardise data and to be able to feed APIs so that data are transportable and transposable. Insurance companies due to their legacy systems still have much work and investment to do to get their technology up to a standard that can be applicable everywhere and the same is true for banks. The Chair agreed that standardisation is a key issue for open finance. The framework should work across all financial sectors and also consider the international dimension outside the EU.

An industry representative highlighted the importance of effective integration. For cross-sectoral data sharing, the architecture needs to be modernised and API-based, leveraging existing API standards. This will be challenging for incumbent companies due to their legacy systems. A regulator agreed that API standardisation is essential. This is one of the main lessons from open banking.

3.2.2 Operational resilience and cybersecurity

An industry representative stated that the framework needs to consider cybersecurity and operational resilience. That is probably the most important aspect for ensuring customer confidence and market integrity and will be quite challenging, although the necessary technologies are available. A public representative noted that data privacy and cyber security issues will evolve as the technology and the market for open finance develop. This will be an on-going process with a constant need for revision or extra protection.

3.2.3 Level playing field

An industry representative emphasised the importance of neutrality in the open finance framework. There has to be a true level playing field between the different players operating in the open finance ecosystem and all players should be on equal footing with respect to the portability of data.

A second industry representative agreed about the need for fair competition for example between banks providing non-banking products and non-banks providing financial services. The question is whether the regulation should be changed in a faster and more effective way to make sure that it captures all of the players, or if new players should be placed into the existing regulation. The first option seems preferable, the regulation should be changed because players are evolving. The industry speaker also stressed that there is a question about which data to open to third parties, because some of it is proprietary data. A bank's credit opinion is indeed based on their own know how and experience, and there might not be comfort opening it up to a third party.

3.2.4 Economic incentives

A regulator referred to the importance of economic incentives. We should ensure there are sustainable business models with products and services flowing through APIs that can be supported by commercial agreements. This would allow providers to make money on them. That puts skin in the game for the incumbent institutions. Being an incumbent means there is legacy to share and engage on.

3.2.5 Customer control and consent

A public representative remarked that transparency and customer control are essential particularly when

1. API : application programming interfaces

data is being used across service providers, which is the basis of open finance business models. Customers should know how their data is collected, used and shared, and that information should always remain available to them. The regulation needs to provide the conditions to ensure customer trust and guarantee protection in an open finance environment with adequate transparency and customer control.

An industry representative added that customer consent is essential to build trust. The General Data Protection Regulation (GDPR) should be relied on to explain how to manage the consent of customers for data that relates to them personally.

3.2.6 Liability and responsibility issues

A regulator noted that liability is a further issue to address as it becomes more complex to figure out with open finance and open data sharing across sectors. The issue is what happens when something goes wrong in an open finance environment. Ways for dealing with this have to be found, with consideration of skin in the game. If an entity is handling data, for example as a third party service providers (TPP), it has a responsibility towards the SME or the customer concerned. However, it may not be the same responsibility as for a bank, depending on what the entity does with the data.

An industry representative agreed that there are questions of responsibility to tackle, when opening data to other providers. For example if a bank's credit opinion is used by a third party for making a credit decision the question is who is responsible in case there is a default or a mistake. In addition, in that case the bank does not have skin in the game, which might create risks in the financial system, similar to those witnessed during the 2008 financial crisis when rating agencies were providing inadequate opinions on risks with no skin in the game and risky loans were sold to other players or divided into small tranches and re-aggregated. In banking operations there has to be a link between the opinion making and the risks taken.

3.3 Lessons from the implementation of PSD2

A public representative suggested that the open banking framework should not just be replicated for open finance. There is a need to look at the lessons learned from open banking to be able to properly move forward with open finance. An industry representative observed that although PSD2 provided greater security in the system, it did not generate a great deal of financial innovation. The reason for this is that PSD2 did not create a valid economic model. If access to information is free, the available information will be limited and innovation will be restricted. There has to be caution, when broadening the scope of data sharing with open finance, to provide the different players in the ecosystem with the opportunity to find an economic interest in moving ahead with the implementation of open finance.

The Chair observed that despite the issues mentioned with regard to PSD2, a great deal of financial innovation has happened over the last 10 years, since the implementation of the legislation and it continues to evolve quickly.

A regulator noted that PSD2 was implemented in the first place because there was no agreement between market participants about data sharing. Banks were refusing access to accounts for third parties and were putting a great deal of pressure on consumers to not share their credentials. At that time, there were no market standards to exchange data, and banks were very critical of web scraping, considering it as anti-competitive, which is why regulators had to step in to allow access to data in a secure way and establish standards about how to exchange data. The issue however is that standards had to be established from scratch for the new environment of PSD2, which was very time consuming, notably concerning APIs. The situation now is somewhat different. There are at least two API standards in Europe that can be built on, although there are still implementation issues with standards that remain optional in some aspects. There is also a more uniform level of service across banks and national markets, with all banks having developed APIs. The main elements needed for open finance are captured in PSD2, which is in the process of being fine-tuned. The question is how to use the open banking framework and infrastructure to go to open finance.

The regulator considered that the main issue for developing open finance is for market participants to find valid business models. Market participants are best placed to deliver and implement the standards needed to support open finance and to find the appropriate business models. Regulation can provide a framework for an appropriate development of open finance but cannot create the market and the less regulation there is the better it will be for all market participants. Progress is being made in terms of standardisation. The European Payments Council has developed a scheme for premium APIs that allows the exchange of data outside of payments data. That should facilitate the development of profitable business models. On the market participant side, there is also a need to work towards more consistent implementation, because differences have been observed across banks in the implementation of the same open banking standards.