

12 December 2016

Ms Roslyn Bell
Data Availability and Use Inquiry
Productivity Commission
Canberra ACT 2601

Via online: www.pc.gov.au/inquiries/current/data-access

Dear Ms Bell

Productivity Commission Draft Report into Data Availability and Use

COBA is pleased to provide this submission in response to the Productivity Commission's (PC) draft report on data availability and use.

COBA welcomes measures proposed in the PC draft report that are intended to empower consumers and spark competition and innovation in banking.

COBA suggests the PC's final report on data availability and use should:

1. recommend a deadline for major banks to implement open APIs and if this deadline is not met, support mandatory participation in open APIs
2. recommend a materiality threshold for mandatory participation in open APIs
3. address security standards and establish an appropriate regulatory framework for open APIs
4. give greater specificity around the comprehensive credit reporting (CCR) participation threshold
5. introduce a materiality threshold for mandatory participation in CCR if the 40% target is not achieved
6. support resolution of the payment arrangement issue.

1. Deadline for major banks to implement open APIs

COBA supports the PC's recommended 'comprehensive right' for consumers to access data held digitally about themselves. Empowering consumers to better compare banking products and services will lead to better consumer and market outcomes.

In addition to the consumer benefit of making it easier to compare products, the PC draft report notes that capacity to share data with third parties enables consumers to benefit from personal budgeting tools and to enhance their creditworthiness.

The PC draft report also notes that the broader potential benefits flowing from opening up access to customer data include increased competition, greater innovation and enhanced consumer choice.

COBA suggests that the PC should explicitly nominate the best method of data sharing to maximise the benefits of the new 'comprehensive right' to consumers to control their data.

The PC draft report notes that:

"the provision of data in an API format most closely achieves the objective of allowing consumers to derive value from their data, and most closely satisfies the criteria for improving the availability and usefulness of consumer data."

The PC's draft report stops short of recommending mandatory participation in open APIs because of the costs of building the necessary technical infrastructure, ongoing compliance costs for financial service providers and security risks for customer data.

COBA acknowledges these concerns, but we also see significant risks if open APIs are not implemented in our market.

Australia's banking market is oligopolistic and there is a lack of robust competition. This has been acknowledged by:

- ACCC Chairman Rod Sims: *"there seems a lack of very robust competition in banking"* and *"we are not seeing as much robust competition as we would like."*¹
- ASIC Chairman Greg Medcraft: *"we are in a market which is, frankly, an oligopoly...Competition has declined since the global financial crisis. We have a more concentrated banking sector."*²
- The House Economics Committee: *"Australia's banking system is such an oligopoly. Australia's four major banks have significant pricing power, higher than average returns on equity and large market shares."*³

In an oligopolistic banking market, there is a high probability that the major players will, in seeking to protect their dominant position, not voluntarily adopt open APIs.

The PC draft report notes this risk, stating:

*"On balance, it is likely that access to data provides some degree of competitive advantage for incumbents, at least in the short term. To the extent that governments can encourage data availability, there could be scope for increased competition in markets for financial services."*⁴

This is not just a theoretical argument. We have seen similar behaviour from some large incumbents in the rate of take up of CCR. As the PC draft report notes:

*"A high level of participation might only be achieved by mandating participation in circumstances where large incumbent banks face significant disincentives to participate."*⁵

The risk is that relying on the dominant major players to participate voluntarily in a pro-competitive initiative, without Government intervention, may delay the benefits indefinitely.

The House Committee on Economics has recommended mandating APIs because it will promote competition, and address the structural problems in banking of high barriers to entry, opaque pricing and consumer inertia. The Committee noted:

"markets work best when customers are informed. At present banks, not consumers, hold the data. This gives banks a significant degree of power".

¹ Hansard, House of Representatives Standing Committee on Economics, ACCC annual report 2015 14/10/2016 page 2.

² Hansard, House of Representatives Standing Committee on Economics, ASIC annual report 2015, 14/10/2016 page 5.

³ House of Representatives Economics Committee – Review of the four major bank banks (first report), page 22.

⁴ 2016, PC draft report on data availability and use, page 545.

⁵ 2016, PC draft report on data availability and use, page 548.

The Financial System Inquiry (FSI) noted similar arguments in 2014 in relation to CCR. The FSI recommended support for industry efforts to expand credit data sharing and *"if over time, participation is inadequate, Government should consider legislating mandatory participation."*⁶

There is arguably more urgency now to implement open APIs in banking than when the FSI considered making CCR mandatory in 2014. The urgency exists because some third party applications are using 'screen scraping' to access consumer data. This practice will continue unless open APIs are widely available.

'Screen scraping' raises fraud and security concerns and creates uncertainty about a consumer's protection under the e-Payments Code.⁷ If a customer discloses their banking username and password to provide access to their data to a third party application, there is doubt about that consumer's protection from liability for unauthorised transactions.

The Treasurer, Scott Morrison, acknowledged this issue recently, when he said:

"In Australia, guidelines have not kept pace with practices by innovators, particularly those that rely on big data. There are a number of FinTech companies already using aggregated financial data to power their innovations ...

*There is ambiguity around legitimacy and the standards by which they currently access customer financial data, especially where a user's banking credentials are required. There is a need to reform the code and implement a strict standard to protect Australian customers while allowing them the benefit of technology innovations."*⁸

We suggest the PC should adopt the approach taken by the FSI in relation to CCR, and recommend a deadline for the major banks to implement open APIs, and if the deadline is not met, participation should become mandatory for participants of sufficient scale in the banking market.

The House Economics Committee recommended that APIs should be mandated for all banking institutions in respect to personal and small business data by July 2018. This timetable may be too ambitious and the Committee's recommendation does not sufficiently take into account cost and proportionality.

The major banks have the critical mass to ensure the consumer and market benefits of implementing open APIs are delivered and the House Economics Committee noted that:

"In their appearance before the committee, each of the major bank's CEOs supported government action to facilitate greater data sharing in the banking sector."

Recommendation 1

The Productivity Commission should recommend a deadline for major banks to implement open APIs and if this deadline is not met, support mandatory participation in open APIs.

⁶ 2014 Financial System Inquiry *Final Report* page 190.

⁷ ASIC acknowledged these problems and risks in its submission to the Productivity Commission's Issues Paper (page 15).

⁸ Address to the Fintech Australia Summit, Melbourne, 4 November 2017, accessed at <http://sjm.ministers.treasury.gov.au/speech/021-2016/>

2. Materiality threshold for mandating open APIs

As noted by the PC draft report, the UK's Competition and Markets Authority (CMA) mandated open APIs for the largest banks in the UK by the first quarter of 2018,⁹ noting:

"..the older and larger banks, which still account for the large majority of the retail banking market, do not have to work hard enough to win and retain customers and it is difficult for new and smaller players to attract customers."¹⁰

The CMA also noted:

"Open APIs can transform the financial services sector...Requiring the banks to adopt and maintain a common open standard will accelerate this pace of change."¹¹

The PC draft report noted the cost of implementing open APIs as a significant reason for not recommending mandating open APIs:

"There is the cost – to the bank or other financial enterprises that provide the data – of building the technical infrastructure required to facilitate the transfer of data to the third party."¹²

The PC further noted that *"that the costs of building APIs could be relatively large, and would have a relatively larger impact on smaller financial firms"* and these costs *"would be relatively more burdensome for smaller providers."*

The PC draft report also noted that the UK estimated the cost of open APIs at £1 million, with smaller ongoing annual operating costs.¹³ We have applied the UK cost estimate of implementing open APIs to our sector, and have found it could cost A\$144 million, or nearly a third of our sector's annual profit in 2015-16.

In designing its package of measures, the CMA considered cost and proportionality, which is why it has taken the approach of only making open APIs mandatory for the largest banks. This avoids imposing unacceptable costs on smaller banking institutions while still delivering a more competitive market.¹⁴

COBA supports the PC recommending a similar approach in Australia.

There is a strong, built-in incentive for smaller banking institutions to participate in open APIs because, as challengers to the dominant players, they are motivated to maximise their competitive potential and their visibility and to offer consumers the full range of new products and services.

Recommendation 2

The Productivity Commission should limit mandatory participation in open APIs to the largest players in the market, to avoid imposing unacceptable costs on smaller banking institutions while still delivering consumer and market benefits.

⁹ These banks were RBSG, LBG, Barclays, HSBC, Nationwide, Santander, Danske, Bol and AIBG. 2016 CMA, Retail banking market investigation Final Report page 441.

¹⁰ CMA *Making Banks Work Harder for you* page 1.

¹¹ CMA *Making Banks Work Harder for you* page 6.

¹² 2016, PC draft report on data availability and use, page 556.

¹³ 2016, PC draft report on data availability and use, page 556.

¹⁴ 2016 CMA, Retail banking market investigation Final Report pages 434 – 438.

3. Security standards and regulatory framework for open APIs.

Our sector supports data sharing via open APIs, provided:

- consumers give their informed consent
- consumers remain in control of their data
- an appropriate governance/regulatory framework is in place
- security and trust concerns are satisfactorily addressed.

Trust is an essential prerequisite for consumers to embrace data sharing. A key component to establish this trust is to ensure that consumers are able to give fully-informed consent before they allow access to their data by a third party.

Informed consent means that a consumer understands who they are sharing their data with, for what purpose, and for how long the authorisation will last. Consumers must also have the ability to revoke access for a third party at any time.

The UK Treasury commissioned the Open Banking Working Group (OBWG) to produce an open banking standard and framework based on APIs. The Working Group consisted of industry experts from banking, open data, and consumer and business communities.

Australia could look to replicate this model in developing an appropriate co-regulatory approach to open APIs.

We suggest that a voluntary co-regulatory regime could include legislative reform so that all entities wishing to access ADI account data under an open API regime must meet minimum probity and competence requirements, and comply with a business-to-business code of practice.

Interested industry stakeholders could then develop a code for data sharing using open APIs. Participants in this process might include banking and finance sector industry bodies, ADIs, fintech groups and fintechs.

A recent precedent for this is the co-regulatory model developed by industry for comprehensive credit reporting in Australia.

The UK and EU have taken measures to address the security concerns raised by open APIs. The UK's Open Banking Standard (which underpins the CMA's reforms) and the draft Regulatory Technical Standards for PSD2 (EU) provide potential frameworks to resolve these security issues. Both standards incorporate strong security processes, including authentication.

APIs can also allow for granular permissions that can limit access to data and specify time limits for data access that are controlled by the customer.¹⁵

Some international banks have already resolved these security concerns and are allowing their customers to share their data with third parties using APIs. For example, BBVA, a Spanish Bank, makes a number of APIs available to third parties, subject to terms and conditions, to develop new products and services for BBVA customers.¹⁶

Recommendation 3

The Productivity Commission should recommend that government facilitate development of an appropriate regulatory framework for open APIs that addresses security concerns and allows customers to control access to their own data.

¹⁵Open Banking Working Group, *The Open Banking Standard*, section 7c.8 and European Banking Authority, *draft Regulatory Technical Standards under PSD2*, Article 1.

¹⁶<https://www.bbvaapimarket.com/>

4. Greater specificity around CCR threshold

COBA requests that the PC provide greater specificity about '40% of accounts' in draft recommendation 4.1 in its final report. As a member of the Australian Retail Credit Association (ARCA), COBA supports ARCA's submission and requests the PC to specify that:

- the 40% target is for participants to report data in public mode
- the appropriate denominator is 'financial services credit accounts where CCR data is being reported to bureaux in public mode' – meaning all active credit accounts provided by ASIC-licensed credit providers'.

This provides greater certainty for the credit reporting industry about the benchmark and makes it easier to assess whether it can be achieved.

Recommendation 4

The Productivity Commission to refine draft recommendation 4.1 to define '40% of accounts' as 'financial services credit accounts where CCR data is being reported to bureaux in public mode'.

5. Introduce a materiality threshold for CCR if the 40% target is not achieved

COBA supports CCR, but does not support mandatory CCR for all credit providers. There is marginal economic benefit from forcing the very smallest credit providers to make significant systems investments to enable them to participate in CCR. This could have unintended anti-competitive impacts.

As noted in the PC draft report, the market is likely to evolve once a 'tipping point' of participation in CCR has been reached (whether it is mandated or reached voluntarily):

"Credit providers that do not participate are at risk of adverse selection with respect to potential new borrowers, a risk that becomes more acute as the level of industry participation increases."¹⁷

"As participation and the level of system-wide data grow, net benefits increase for all CCR participants, providing an incentive for participation."¹⁸

These market impacts, seen in overseas jurisdictions, are likely to occur in Australia. This means that once the 40% threshold has been reached, more lenders will see the benefits of CCR and will participate voluntarily.

For smaller credit providers, the cost of participating may out-weigh the benefits.

COBA's larger members will voluntarily participate in CCR. COBA's largest member, CUA, with an asset base of \$12.9 billion, is one of the earliest adopters of CCR. More COBA members will choose to participate voluntarily once the tipping point is reached.

For these reasons, COBA requests that the PC amend draft recommendation 4.1, to say that if the 40% threshold is not reached, CCR should be mandated for financial service credit providers with assets of more than \$200 billion.

We suggest this threshold because lenders with assets of more than \$200 billion currently hold 77.3% of the mortgage market and 72.6% of the total lending market in Australia, which represents the vast majority of customer accounts about which positive data might be reported.¹⁹

¹⁷ 2016, PC draft report on data availability and use, page 548.

¹⁸ 2016, PC draft report on data availability and use, page 549.

¹⁹ Source: APRA, RBA. Figures correct as at March 2016.

Recommendation 5

The Productivity Commission to refine draft recommendation 4.1 to say that if the 40% target is not achieved by 30 June 2017, the Government should circulate draft legislation to impose mandatory reporting on credit providers with assets of more than \$200 billion by 31 December 2017.

6. Support resolution of CCR 'payment arrangement' issue

COBA would like to see the PC urge government to resolve the issue of how CCR repayment history information (RHI) is reported for consumers in a payment arrangement or indulgence.

The PC draft report notes that: "*Greater clarity on how the hardship provisions should interact with CCR could help pave the way for broader industry participation in the scheme.*"²⁰

One of the major barriers to the commencement of CCR appears to be the position the Financial Ombudsman Service (FOS) has taken in relation to *non-hardship* payment arrangements.

COBA understands that ARCA has sought guidance from the OAIC about its interpretation of how RHI should correctly be reporting during an indulgence or payment arrangement that is not a hardship situation.

Resolving this issue is important, because lenders who are reporting RHI to credit bureaux need certainty and consistency that the same situation is being reported in the same way. This issue is critical and COBA understands that without satisfactory resolution of this issue industry transition to CCR will stall.

Recommendation 6

The Productivity Commission to urge the Office of the Australian Information Commissioner to resolve the way hardship information is reported in repayment history information.

About COBA

COBA is the industry association for Australia's customer owned banking institutions, i.e. mutual banks, credit unions and building societies. Collectively, the sector we represent has \$103 billion in total assets and provides the full range of retail banking products to more than 4 million customers.

The customer owned model is the proven alternative to the listed model in the Australian banking market, delivering competition, choice, and consistently market leading levels of customer satisfaction.

Yours sincerely



LUKE LAWLER
Head of Public Affairs

²⁰ 2016, PC draft report on data availability and use, page 143.