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Digital Disruption in Financial Markets – Note by BEUC

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More documents related to this discussion can be found at

<http://www.oecd.org/daf/competition/digital-disruption-in-financial-markets.htm>

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1. Introduction

1. Financial services, while being a regulated sector, are amongst the worst performing markets in Europe in terms of consumer satisfaction¹. One of the reasons is lack of competition and consumer choice amongst providers of financial services², other important reasons being product complexity, lack of trustworthy financial advice³, and consumers' behavioural biases. In the EU, the Payment Services Directive 2 aims at opening payment markets to competition and thereby providing consumers with more choices⁴. Although the principle of open banking is to be welcomed, its success depends on whether its implementation will effectively lead to more competition. In this note, BEUC provides the consumer viewpoint on open banking in what concerns its impact on competition and on consumers⁵.

2. Open banking in the European Union

2. The revised Directive on Payment Services (hereafter PSD2) is the baseline legislation for open banking as it enables Payment Initiation Services (hereafter PIS) and Account Information Services (hereafter AIS) to access consumers' online banking data to be able to provide their own services requested by the consumer, which would compete with the services provided by the consumer's bank.

3. A practical example of a PIS is when a consumer pays by credit transfer when shopping on a merchant's website, provided that the merchant offers such means of

¹ "Results of a Commission study on consumer detriment in the EU showed that among six sectors assessed, the average level of post-redress financial detriment per problem was second-highest for the 'loans, credit and credit cards' market. The detriment in this market ranged between EUR 83.0 and EUR 154.9. Aggregating results over the last 12 months in the different EU-28 countries, the total post-redress financial detriment for 'loans, credit and credit cards' ranges between EUR 1.3 billion and EUR 8.8 billion. This shows the magnitude of consumer concerns for this particular financial sector". Consumer Market Scoreboard 2018, https://ec.europa.eu/info/sites/info/files/eujus15a-1816-i02_-_the_consumer_markets_scoreboard_2018_-_accessibility_final.pdf

² A study for the European Commission concluded that "The relatively limited choice of payment methods in spite of technological progress suggests market entry barriers for new payment service providers"., TSN, Study on the effects of information disclosure on consumer choice of payment instruments, <http://ec.europa.eu/competition/sectors/financial_services/mif_final_report_en.pdf>

³ See BEUC campaign on "The price of bad advice", <<https://www.thepriceofbadadvice.eu/>>

⁴ Directive (EU) 2015/2366, <<https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32015L2366>>

⁵ For additional information see: BEUC, "Consumer-friendly open banking. Access to consumer financial data by third parties", <https://www.beuc.eu/publications/beuc-x-2018-082_consumer-friendly_open_banking.pdf>

payment. The best known PIS are iDEAL (in the Netherlands)⁶ or Sofort (in Germany).⁷ The former is an interbank system, the latter an independent system. The essential feature of a PIS is to use the credit transfer payment instrument, which is much cheaper for the merchant than a card payment.

4. An AIS aggregates information from the consumer bank's account(s) for performing the service requested by the consumer. It can be advice on money management, credit scoring, access to targeted credit offers, insurance comparison, etc.

5. Before PSD2 and even today when consumers agree to give access to their account, PIS and AIS are using the home banking channel (which consumers use when connecting to their online banking). This means, PIS and AIS would have access to the same information that is available to the consumer when he or she is using home banking (also referred as "screen scraping"). As many banks refused to give this access to third parties, the activity of PIS and AIS was rather limited before the adoption and entering into force of PSD2. Thus, the great innovation of PSD2 is to require banks to grant that access to a PIS or an AIS in order to open-up competition for consumers. As a result, PIS and AIS are now regulated under PSD2 which sets provisions related to their obligations and, to some extent, liabilities in case of incidents.

6. According to PSD2, AIS and PIS must have a licence delivered by the national competent authority to be able to have access to the consumer payment data. This licence given by one country is a European passport. In term of competition, it is worth noting that platforms like Google, Amazon and Apple, which are present across Europe, are rapidly entering the payment market and must obtain a licence for such activities

7. PSD2 mandates the creation of a new channel for communication between the consumer's bank and the AIS and PIS. The legislation⁸ refers to a "dedicated interface". In the banking world this channel is called API (Application Programming Interface). As the United Kingdom is ahead in implementing its own Open Banking project⁹, the term 'open banking' is also used¹⁰. This expression corresponds to a new reality, where the bank becomes open to third party providers (FinTechs, but also other banks and traditional service providers). The idea of open banking is not limited to Europe, it is also being explored in several other countries outside Europe.¹¹

⁶ <https://www.ideal.nl/en/>

⁷ <https://www.klarna.com/sofort/>

⁸ RTS – Regulatory Technical Standard, level 2 implementing measure setting the details of the PSD2 provisions.

⁹ Ref.: <https://www.openbanking.org.uk/>

¹⁰ It must be noted that Open Banking project of the UK is the result of a decision of the Competition and Markets Authority (CMA). The CMA has imposed to the 9 main banks to create this API as a remedy to low level of consumer mobility. The reasoning was, as competition is not working due to consumer inertia, competition will be generated by giving to various service providers the possibility to access to consumer data.

¹¹ See a map on page 15 of this study by Innopay and Deutsche bank, <http://www.cib.db.com/insights-and-initiatives/white-papers/unlocking-opportunities-in-the-api-economy.htm>

3. Open banking can be good for competition but must deliver to consumers

8. While open banking can significantly reduce barriers to entry and stimulate the market of payment services, authorities must ensure that its implementation does not contain features that can jeopardise the objective of creating a competitive market and / or eventually lead to consumer harm:

3.1. Competition and Application Programming Interface

9. First, it is important to highlight that the banking sector is strongly concerned about the competitive pressure that third party providers (both PIS and AIS) is introducing on their business models. A report of the European Banking Authority on the impact of FinTechs on incumbent bank business models confirms this:

Figure 1. How do you see FinTech firms affecting the current business model (business lines) of your bank?



Source: EBA report on the impact of FinTechs on incumbent banks business models, July 2018.

10. This could lead to banks making the entrance of third-party providers more difficult through technical barriers, for example by developing different communication interfaces. This could force third-party providers to adapt their systems to each bank communication channel or API. Therefore, this is why BEUC advocates for a standardised European API that all banks should be required to use. BEUC's argument is that competition will never thrive if the 4000 EU banks establish their own specific API. The PSD2 required the EBA (the European Banking Authority) to define the general principles of this new channel. After very long discussions a new implementing regulation was published on 13 March 2018 to come into effect on 14 September 2019.¹²

¹² Commission Delegated Regulation EU 2018/389, <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32018R0389&from=EN>

<https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32018R0389&from=EN>

11. Defining the technical modalities for the implementation of this open banking was crucial. As a first step, a working group on PIS only was set up under the auspices of the ERPB in December 2016.¹³ This group, where the banks and the PIS and AIS were in broad disagreement, eventually came to the conclusion that it is by comparing the different national open banking projects that a solution could be found. This led to the creation of a new working group (API EG - API Evaluation Group) under the auspices of the European Commission.¹⁴

12. BEUC participated in this working group aiming to develop a standardised European API (Application Programming Interface). The mandate of the group was: "... to evaluate standard APIs in order to help ensure that they are compliant with the requirements of the revised Payment Services Directive (PSD2) and meet the needs of all market participants". As a result, the group should: "make recommendations aimed at API specifications convergence on a European level and to help establish harmonized market practices." For BEUC, the important point is "the need of all market participants".

13. The EC working group API EG published in December 2018 its recommendations¹⁵ for the convergence of the existing APIs. The work now continues under the chairmanship of the European Banking Authority (EBA).

3.2. Competition and access to consumer data

14. Secondly, in what concerns the impact of open banking on consumers, we must always bear in mind that the open banking implies accessing data from consumers, with all the risks associated to it (fraud, data breaches, cyber-attacks, etc). While these concerns seem to be outside the remit of competition considerations, it is important to highlight that the take-up of third-party providers (PIS and AIS) depends on consumers having trust in such services. And trust can be achieved only if all necessary measures are adopted to reduce those risks and guarantee that consumers will be protected if things go wrong.

15. As a very practical consideration, the access by PIS to the consumer data should not be done through the consumer's home banking. There are two reasons for this. First, the consumer's confidential data for identification (security credentials) is passed to the PIS hence increasing the risks of data breaches. Secondly, because of screen scraping, the PIS could read all the information available on the consumer's home banking (current account transactions, savings account, running credit contracts, insurance contracts, etc.). Thus, this is another important reason of why a consumer-oriented standardised European API is a pre-condition for the success of open banking in Europe.

16. As regards AIS, they could have potential benefits for consumers, but there are also controversial aspects. An AIS can analyse the consumer's banking data and based on that analysis provide money advice or offer credit or insurance products to the consumer. The consumer interest can be that AIS might increase competition for consumer credit and

¹³ Euro Retail Payments Board, of which BEUC is a member, <https://www.ecb.europa.eu/paym/retpaym/euro/html/index.en.html>

¹⁴ Terms of Reference API Evaluation Group, https://www.europeanpaymentscouncil.eu/sites/default/files/kb/file/2018-03/API%20EG%20002-18%20v1.2%20Terms%20of%20Reference%20API%20Evaluation%20Group_0.pdf

¹⁵ Recommended functionalities of the API Evaluation Group, <https://www.europeanpaymentscouncil.eu/document-library/guidance-documents/api-evaluation-group-recommended-functionalities-psd2rts>

deposits/savings, through allowing providers access to consumer bank account data. For example, in the case of credit, access to bank account data will allow alternative providers to assess the consumer's creditworthiness. But the AIS is also accessing sensitive information, contained in consumers' bank accounts, such as information on health conditions, political affiliations, and personal relationships (they can derive this sensitive information by analysing payment transactions on the consumer's account)

17. An important point is that any bank can act as a PIS or an AIS. If a retailer decides to work with a bank as a PIS, he will be paid by credit transfer, a solution which is much cheaper than classic card payments. If a bank decides to act as an AIS, it will allow the consumer to access all his accounts by using only the mobile app of this bank. The drawback is that this bank will have access to the consumer's data in other banks.

4. The role of personal data in open banking

18. Access to personal data enables firms to produce detailed profiles of consumers that can be used for different purposes, from the tailoring of offers to price discrimination¹⁶. Accessing consumer' bank data by third-party providers is one of the main novelties introduced by PSD2. It creates new opportunities to develop services for consumers, something that can be positive from a competition perspective , but it also raises many critical questions and concerns related to:

- Consumer control: How to ensure that consumers remain in control of their account data?
- Consent: how consent should be given to ensure that the third-party payment providers (hereafter TPPs) have the consumer permission to access the necessary information through the API to provide the payment solutions?
- Data minimisation and purpose limitation: How to make sure TPPs do not get access to more data than they need to provide the service requested by consumers and that they do not use for other purposes? What can be considered compatible purposes in these scenarios?
- Profiling.
- Processing of sensitive data.

19. In our contribution to the European Data Protection Board on the interplay between the GDPR and PSD2 we assessed these different points¹⁷, however in what concerns the impact of access to data under PSD2 for competition it is worth highlighting the following elements:

20. First, authorities need to remain vigilant about the agreements between banks and third-party service providers for the use of APIs. This is because, aside data protection concerns, third-party providers should not be able to gain access to data that would go beyond what is necessary for the provision of the service to avoid gaining an anti-

¹⁶ See BEUC note on personalised pricing in the digital era, [https://one.oecd.org/document/DAF/COMP/WD\(2018\)129/en/pdf](https://one.oecd.org/document/DAF/COMP/WD(2018)129/en/pdf)

¹⁷ See BEUC's recommendations to the EDPB on the interplay between the GDPR and PSD 2, https://www.beuc.eu/publications/beuc-x-2019-021_beuc_recommendations_to_edpb-interplay_gdpr-psd2.pdf

competitive advantage over rivals if they are able to provide personalised services to consumers based on users profiles.

21. Secondly, a liberal interpretation of data sharing under PSD2 could undermine consumer trust in the whole open banking ecosystem. Consumers need to know that the service they are using is safe and no data is being compromised or accessed by other parties without their consent. It is worth reiterating that third parties should not access consumers' personal security credentials.

22. Finally, we should not underestimate that third-party providers might be already in possession of consumers' data through other channels (e.g. services they are offering in other markets like social media, entertainment services like video and music streaming, app stores, etc.). Big Tech (i.e. Amazon, Google, Facebook) are also very interested in providing financial services and to become active in the open banking market. For example, Google already has an AIS service. Thus, the non-financial data these companies hold in combination of the financial data they can get through open banking, can provide them with an even more granular profile of consumers and therefore enable them to develop personalised services or engage in discriminatory practices and manipulation. Something that other providers who do not have access to these other sources of data would find much more difficult to do.

5. Scope of open banking – inclusion of “other accounts”

23. PSD2 covers only payment accounts (current accounts) and not "other accounts" such as savings accounts. Consequently, the scope of the work of the API would be limited to payment accounts. Nevertheless, it is possible for the API Expert Group to extend the scope of its work to other accounts. This is what AISs are also requesting. The position of AISs is quite clear: if they cannot use the API for “other accounts” they will use the consumer home banking channel, the old screen-scraping. In such a situation the only applicable legal text is the GDPR, and not PSD2. As a consequence, work should be undertaken by regulators to ensure that consumers are adequately protected against data breaches, misuse of data, privacy and security risks associated with sharing of consumers' financial data. BEUC is in favour of the extension of open banking to data which are not covered by PSD2 such as savings accounts. However, this extension must be done in full transparency and in conformity with the principles we have outlined for the implementation of PSD2.

24. To conclude: Open banking is a concept that is promoted as beneficial for consumers and competition. Whether it will deliver according to the expectations, can be assessed in the medium to long term and depending on how convenient and secure will be for consumers the adoption of these new payment solutions.