



# Open Banking – a game changer for financial capability?

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Most UK adults have a bank current account or basic bank account.

The income coming into that account, the things it is spent on and whether the account holder maintains a positive balance or frequently dips into the red creates a rich set of data.

Banks have long used that data, for example, to help them assess the creditworthiness of customers and cross-sell other products.

Open Banking starts with the premise that customer's data belongs to them and could be used by them for their own financial advantage if they choose to share their data with other organisations.

## NOTES

There are 65 million active PCA accounts (CMA, 2014).

# Consumer engagement



If there are impediments to customers being able to: access information about – and **compare – alternative offers**; assess which offers are best for them; and act on this knowledge by **switching** products or providers, competition will be weak... CMA, 2015a

For liberalised retail energy markets to work effectively customers need to be adequately engaged. It is through customers **shopping around** and making choices between the offerings of rival suppliers that the benefits of competition emerge. We have, therefore, considered a range of remedies to address barriers to **customer engagement**. CMA 2015b

... sufficiently and targeted information at the right time so that they can **easily and quickly compare** their savings accounts with alternative ones and know how to switch if they want to do so...  
• Making the **switching process** as easy as possible FCA, 2014a

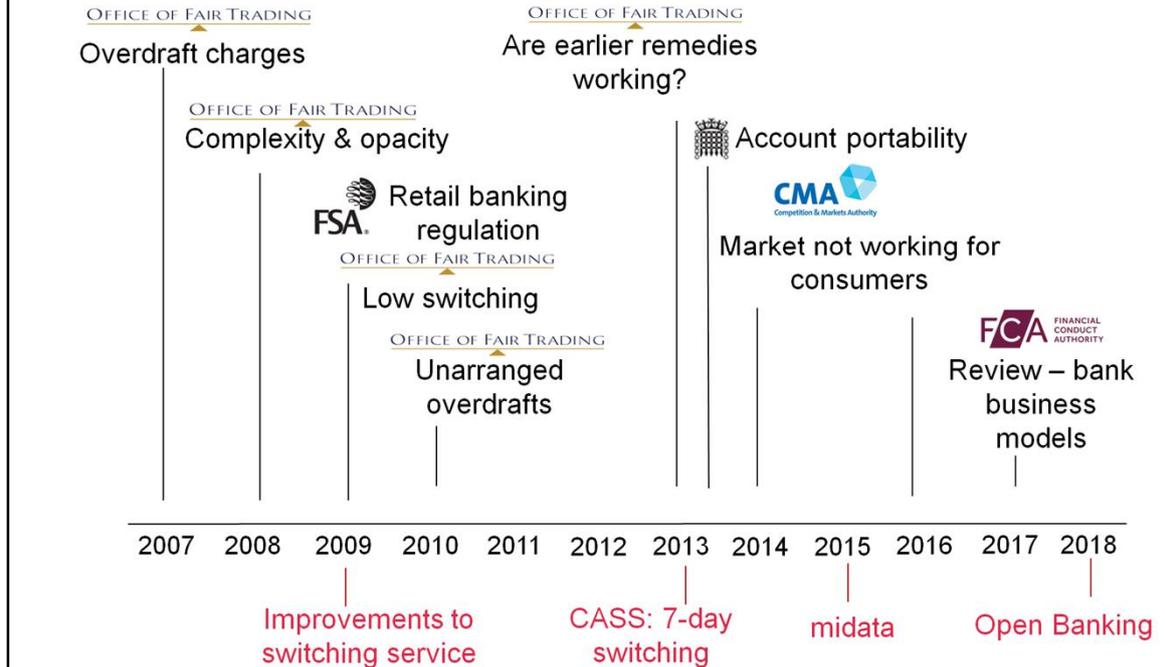
... particular, the study seek to identify ways of **improving consumer engagement to prompt shopping around** FCA, 2014b

I first became interested in Open Banking as a result of a thread of research I have been pursuing for the last couple of years.

I was spurred to start this research by the procession over many years of regulatory reports all claiming that a key reason for lack of competition was lack of consumer engagement. If only consumers would shop around (and if appropriate switch) their energy provider, their bank account, their savings accounts, their pension annuities – all would be well.

Proposed remedies have typically included more and better information for customers, making switching simpler and increasing consumer awareness of switching facilities. Yet, when remedies have been reviewed, they seem to have had a disappointing impact on consumer engagement.

# Personal current accounts



The banking industry provides an example.

In 2014, the British Bankers Association grumbled that The British Bankers Association commented in 2014 that *'Competition in UK banking ...has ...been the subject of more than 30 reports in just the last 15 years.'* This timeline shows just some of those reports over the last 10 years and the main remedies aimed at encouraging consumers to switch their personal current accounts (PCAs).

Remedies involved:

- “ In 2009: improvements to the switching service such as
  - better communication between banks to reduce payment failures . especially of direct debits . during switching
  - better systems to directly transfer account data between banks, and
  - extending the promise in the Banking Code of refund of any erroneous fees incurred during switching beyond just signatories to the code.

Switching at this time typically took 18-30 days.

- “ So next milestone in 2013 was an improved switching service, the Current Account Switching Service (CASS) - including a commitment to 7-day switching. By 2014, the Competition and Markets Authority was reporting high customer awareness of CASS (99%) but the annual switching remaining stubbornly low at just 3% of customers.

Idl come back to midata and Open Banking in a minute.

# Multi-tasking

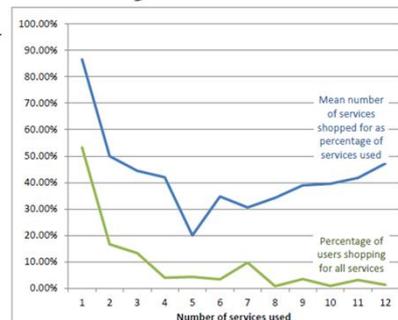
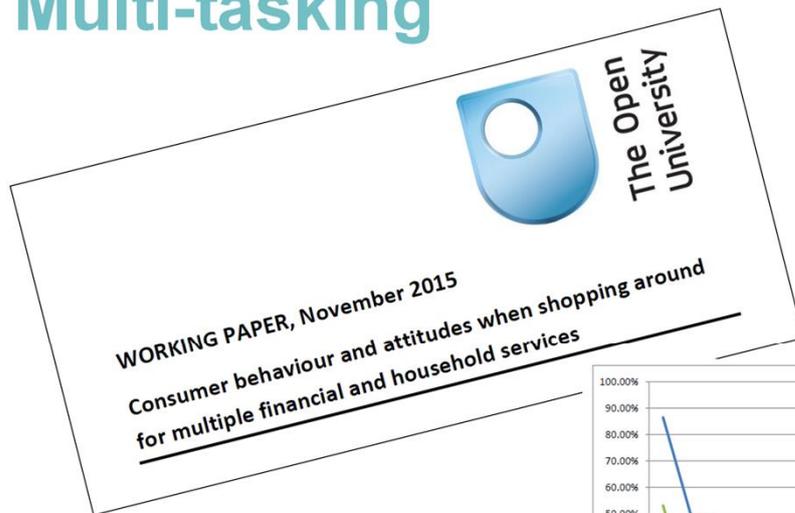


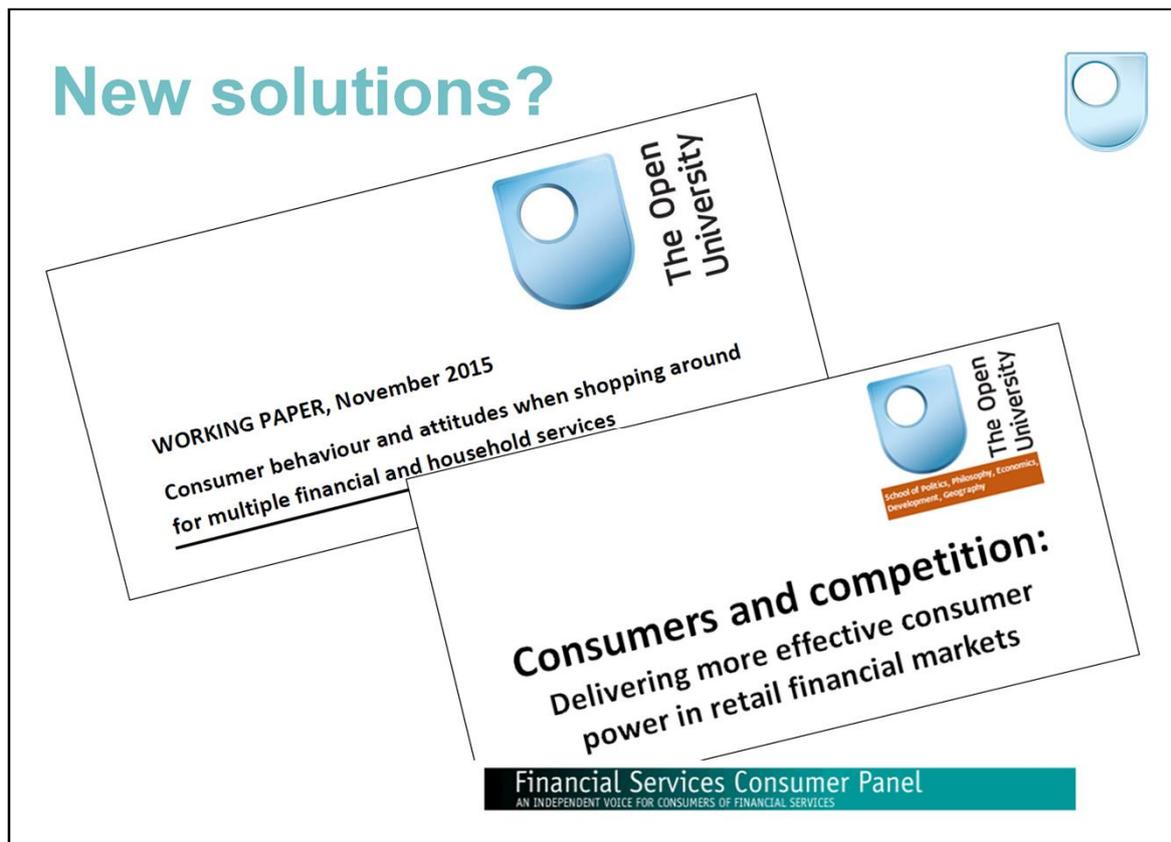
Figure 3: Mean number of services shopped for as a percentage of services used and percentage shopping for all services  
Base: All respondents

It seemed to me that the exhortation to shop around made by each new review of a retail household or financial services market might sound reasonable taken in isolation, but in reality households could be mighty busy if they followed this exhortation in every market.

So, in 2015, I carried out some research into consumers behaviour when faced with shopping around for multiple household and financial services. Using a survey-based approach, I asked 1,000 consumers about 12 commonly used services, such as energy, banking and savings accounts, household and car insurance, and so on.

I found that the average household shops around for fewer than half of the services they use. Comparing consumers who do not shop with those that do, the non-shoppers tend to overestimate the difficulty of the task, are more likely to think that providers are all the same (especially for energy) and that the potential savings are too small to make shopping around worthwhile (particularly in the case of energy, insurance and credit cards).

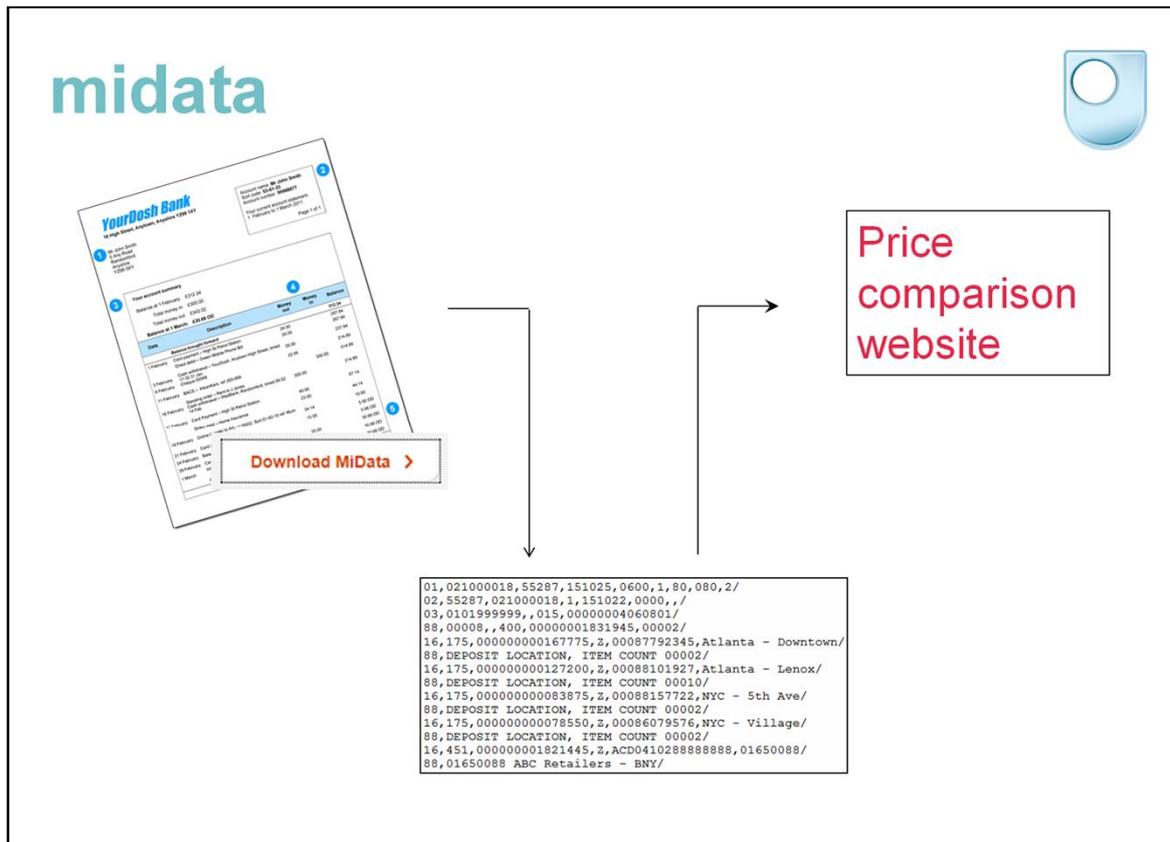
Combining my finding that consumers reckoned shopping around for any one service took on average about 2 hours with an Ofgem finding that energy consumers would need to make savings of at least £240 a year before being enticed to switch provider, one might deduce that consumers put a very high value on their leisure time of around £120 an hour which could make failing to shop around a rational decision.



A second strand of my research was a commission late last year from the Financial Services Consumer Panel to look at how consumer power in retail financial markets could be enhanced.

The research, which was published this week, was a mix of literature review and a consumer survey. My key findings were that financial firms, in the main, aim to maximise their profits and to do this have strong incentives to use strategies, such as opaque and complex pricing, complicated product features and competing for new customers while charging loyal customers extra. Consumers are ill-equipped to deal with the resulting opaque and confusing markets. Individuals have numerous behavioural traits that incline them towards making decisions based on short-cuts and rules of thumb, such as focusing on headline price or sticking to brands they know. These behaviours are a gift for firms, making it easier to pursue their profit-maximising strategies and harder for new firms . who might compete those profits away - to get a foothold in the market.

This creates a marked asymmetry of power between firms and consumers that is unlikely to be addressed simply by extra information and new switching services. I came to the conclusion that a more efficient way to drive competition and achieve better consumer outcomes would be to delegate shopping around to computer algorithms and even automate switching for consumers who want it. Firms may be able to bamboozle behaviourally biased consumers, but computers can cut through complexity.



Of course , to some extent computers are already being deployed in this way. Price comparison websites have revolutionised shopping around for consumers who have internet access and are looking for products where features can be readily compared. But they are less effective where complicated price structures and consumer usage affect the deals . as in the case of household energy and personal current accounts.

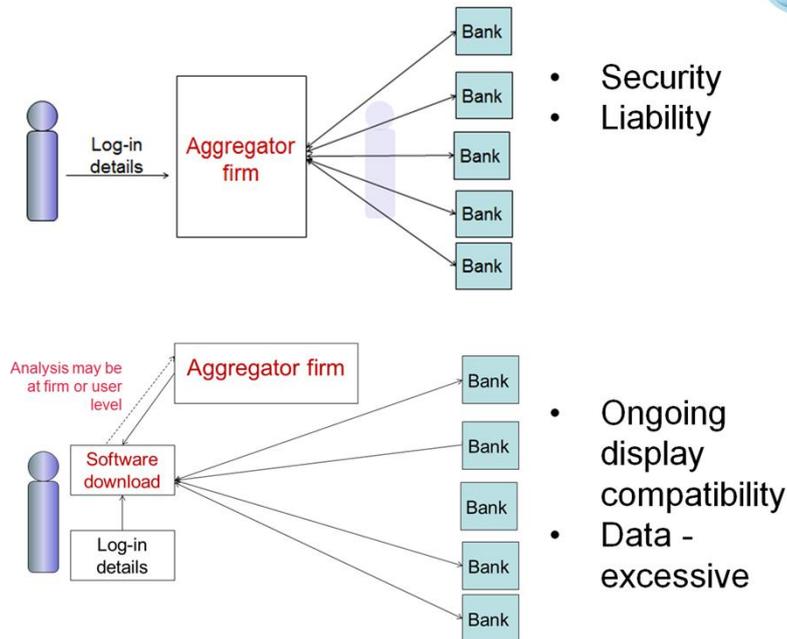
I said I would come back to midata. This is a government initiative, introduced in 2015, that enables price comparison websites to give personalised comparisons for products like energy and bank accounts.

It does this by letting consumers download their usage data from participating energy providers and banks as a CSV file and then upload it to a price comparison website.

Potential drawbacks of midata:

- one-off snapshot of data
- clunky process
- the consumer downloads the CSV file eg to their PC and this typically is the least secure link in any digital chain.

# Screen-scraping



- Security
- Liability

- Ongoing display compatibility
- Data - excessive

Another form of data sharing that has been around for a while is screen-scraping. This is used by account aggregators - intermediaries whose service lets consumers see the balances of multiple accounts all in one place . for example, current account, savings accounts, credit cards and other financial products. (For convenience, the diagram says Bank but these could be other types of financial provider.)

In addition to collating and delivering information to consumers., aggregation services typically also include analysis tools . for example, to help with day-to-day money management or portfolio analysis.

Screen-scraping started in US around 1999. Initially it involved passing log-in details to the aggregator. However, this raised concerns about security and whether the customer would be liable if something went wrong, given that passing on log-in details is typically a breach of a bank's Terms & Conditions.

So there was a move towards services using software downloaded to the user's computer so that log-in details remain on the user's device.

Screen scraping potentially gives the account aggregator access to more data from the underlying accounts than is needed to deliver its particular services, which might then be used for, say, cross-selling other products. There can also be problems, if the way data or security arrangements in the underlying accounts are changed, leading to glitches in the aggregated display and analysis. (Fujii et al, 2002)

# Open Banking



Date	Description	Debit	Credit	Balance
14/01/2018	Direct Debit - Water	15.00		100.00
14/01/2018	Direct Debit - Gas	20.00		80.00
14/01/2018	Salary - ABC Corp		500.00	580.00
14/01/2018	ATM Withdrawal - 123 St	50.00		530.00
14/01/2018	Interest - 0.5%		2.50	532.50

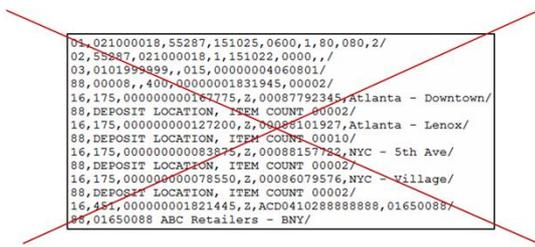


Price comparison website, account aggregator, etc



Payment initiation

- No sharing log-in info
- Can specify only selected data
- Dynamic



So if data sharing already happens, what's so special about Open Banking?

Open Banking is a bit like the midata model, but it is a process that enables data sharing to happen in a formalised and dynamic way that aims to be easy to use and secure.

There is no sharing of log-in details or clunky downloading and uploading CSV files. Instead your bank can exchange information with third parties directly without any human intervention, using APIs.

APIs (Application Programming Interfaces) are a set of functions and procedures that enable different programs or apps to communicate and exchange data with each other. Can think of it as a pipeline along which data flows.

Open Banking is seen by the competition regulators as a way of financially unleashing the consumer power needed to drive competition in the retail banking sector. So much so, that the CMA's remedies from its latest review require banks to implement Open Banking by 13 January 2018 . so where an account can be accessed digitally, the bank must release a customer's data to a third party if the customer says so.

But more than simply enhancing competition through more efficient, data-driven product comparisons, like screen-scraping Open Banking enables third party firms to add innovative services, like money management tools, onto your bank account. And banks are unlikely to sit back and see their traditional dominance leach away . for example, some banks are already developing their own aggregation services. (And CitiBank has been a player in this field since 2000.)

# Open Banking



The fact that Open Banking is due to launch on 13 January 2018 is not a randomly chosen date. It is the date by which the UK must implement a new European Directive, the Second Payment Services Directive (PSD2).

PSD2 builds on the first payment services Directive which came into force in 2009. It means that banks, card companies, remittance services and similar organisations offering payment services have to be authorised by the Financial Conduct Authority and abide by its rules.

PSD2 brings account aggregators and similar providers into the regulatory net and, amongst other measures, improves consumer protection. For example, it:

- “ Reduces the amount that a consumer has to pay if an unauthorised payment is made from their account (from E150 to E50), and
- “ Bans surcharges for using, say, a credit card.
- “ Requires payment service providers to have a dispute resolution procedure.

PSD2 will also require secure authentication . eg biometrics (and this week we've seen announcement that TSB has introduced iris recognition)

# PSD2 jargon



Account aggregator;  
personalised price  
comparison  
websites

**AISP**



Payment initiation

**PISP**

**AS PSP**

**Payment service provider (PSP)** Bank, building society, Post Office, credit union, e-money issuer etc and NEW PISP and AISP.

**Account servicing payment service provider (AS PSP)** The provider where a person has an underlying account.

**Account information service provider (AISP)** An online service that consolidates information from one or more payment accounts held with one or more payment service providers.

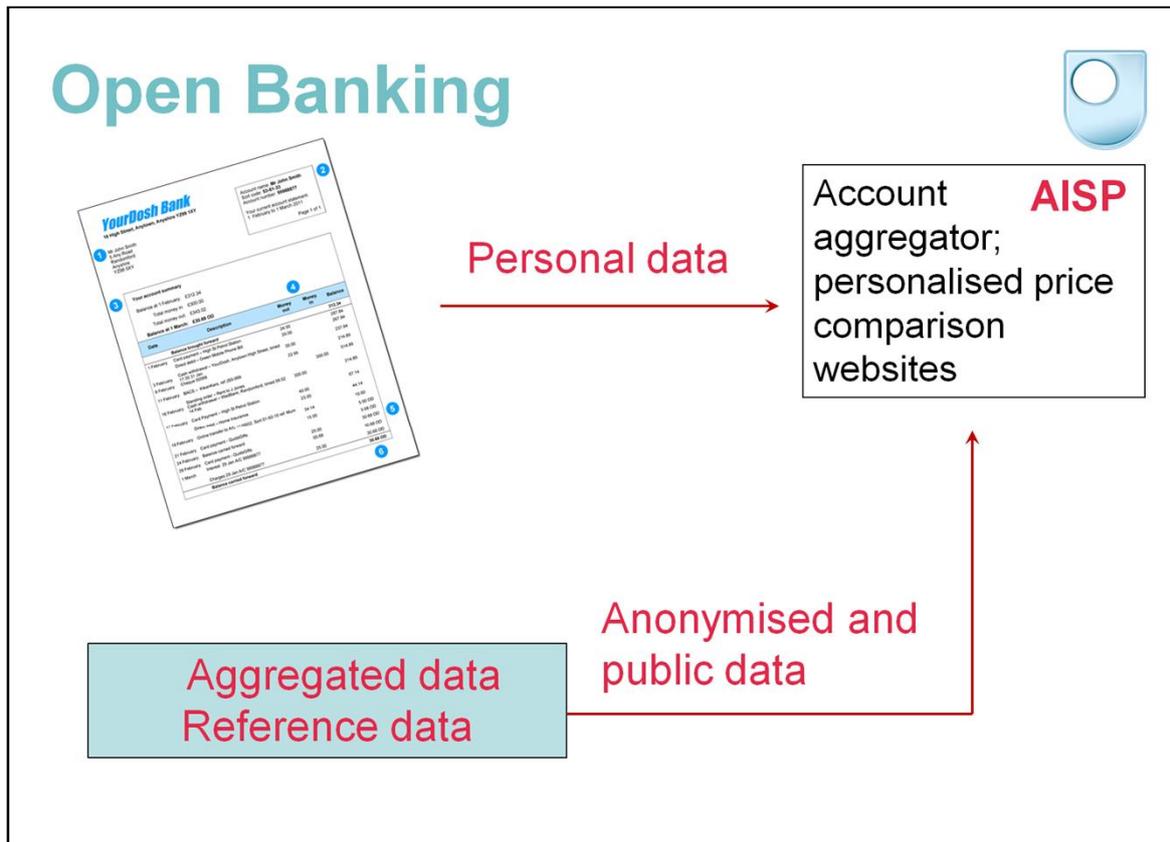
**Payment initiation service provider** A service that initiates a payment direct from a person's account when that person instructs them to do so.

It may be helpful at this point to get to grips with some of the jargon in the Directive.

PSD2 in fact creates two new types of payment service provider:

- “ AISP
- “ PISP

And AS PSP is the name given to the underlying bank or other account where the data or payments come from.



The CMA's Open Banking remedy does not just deal with personalised data

CMA requirements:

Requiring banks to publish trustworthy and objective information on quality of service on their websites and in branches, so that customers can see how their own bank shapes up. Whether a personal customer or small business is willing to recommend their bank to friends, family and colleagues will be a core measure but we will also be requiring banks to publish and make available through Open Banking a range of other quality measures. (GOV.UK news release, 9/8/16)

Aggregated anonymised data can be used for research - eg to analyse who is most likely to develop debt problems . and so inform new interventions to help consumers avoid debt problems.

Reference data may include the quality measures, for example, customer reviews, level of complaints, and so on, as well as features such as overdraft charges. Useful for comparison websites. May also include branch and ATM locations . useful for apps that work with your geographical location.

# Open Banking: benefits



Holistic information...Money Management...Alerts...Cheaper services...Personalised product comparison.

So Open Banking delivers the infrastructure that enables a wide range of new digital services to help consumers exploit their own banking data. The possibilities include:

- More convenient, easier to use aggregation services so consumers have a more holistic view of their money and can manage it better. Instead of just viewing all their accounts in one place, aggregators may also become payment initiation services enabling consumers to move money from one account to another within the aggregation service.
- Analysis services that can categorise spending and feedback how much is being spent on different areas and deliver personalised budgeting advice or maybe predict the signs of financial stress before it becomes a problem and so steer consumers back onto a safe course. And credit rating . alternative to CRAs; mortgage affordability checks.
- Monitoring services which, for example, track a person's bank balance and top it up automatically either from savings or cheap loans that cost less than an overdraft
- Personalised price comparison websites that recommend the cheapest bank account based on the consumer's actual usage of that account or better savings accounts or suggest whether spending on, say, car or home insurance looks high.
- There are already services that not only shop around for the best mortgage, say, when the product is first taken out but then continuously monitor the market and alert the consumer when they could save by switching to a better deal. It would be a short step to automating the switch to better deals on a regular basis.
- And we've already seen that third parties will be able to set up payment initiation services giving consumers a new, often cheaper way to pay for things direct from their bank accounts without the need for plastic cards.

# Potential risks



- Conflicts of interest
- Data sharing
- Privacy and control
- Sharp practice
- Market complexity and trust
- Data security
- Digital exclusion
- Financial exclusion

Source: Reynolds (2017)

Conflicts of interest . business model - free servicesq commission payments.

Data sharing . how might be used (eg combining data sets and using to cross-sell products); lengthy terms and conditions

Privacy and control . business model - onward sale of data. PSD2 regulation . will all types of third party be covered?

Sharp practice . eg debt collection. Access for loan affordability checks might be bundled with ability to initiate debt collection if repayments missed. Inability to juggle priority and non-priority debts if lenders have payment initiation permissions. Affordability checks might be used to assess ability to upscale the product you are buying . eg a new car.

Market complexity and trust . shifts shopping aroundqproblem from the bank accounts, savings accounts, annuities and so on to how to shop for the best account aggregator. How to choose between them? What happens when algorithms get things wrong?

Data security - Passing data from aggregators to other third parties . eg mortgage lender . is this covered by PSD2? Hacking? Scams . aggregators will need to be authorised. But scammers may . as now . pass themselves off as legitimate firms. We've been told that banks will not check that a third party is authorised before accepting the customer's instruction to allow payment initiation.

Digital exclusion . low-income households, people in rural areas and urban not-spots, older people.

Financial exclusion - will firms cherry pick?

# Implications for fincap?



...it breaks the whole advice, guidance  
and education paradigm...  
[Industry expert]

Source: Reynolds (2017)

I think maybe we need to get to a  
situation where we help people really  
understand what data is first, what sort  
of data they own and are generating  
and then control is of course about data  
utility... I think people are a long way  
from being able to control their data...  
[Consumer expert]

Source: Reynolds (2017)

Consumers are generally not making informed  
decisions around data security considerations.  
Instead they are responding to how big or well-  
known the service provider is, and employing this  
as a proxy.

Source: Ipsos-Mori (2015)

Open Banking . and similar initiatives, such as the Pensions Dashboard (which will let consumers see all their pensions in a single place) . both uses and facilitates digital innovation.

It may be only a matter of time before many of the skills that we currently think are essential parts of financial capability, such as money management and shopping around are routinely replaced by labour-saving and cognitive-saving apps.

But consumers may have new needs to be more aware of the value of their data, how to exploit it to their advantage and how to protect it.

Is it time to rethink our concepts of financial capability and lead an evolution in the knowledge and skills we try to foster in consumers?

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