COUNTRY SPOTLIGHT

Canada treads carefully on Open Banking

In the global race to roll out Open Banking, Canada has been a slow starter. Is it sluggishness or sensible caution?

Canada has a stable financial sector that has earned the confidence of its people. Its strong financial regulatory framework has shielded the country, to a certain extent, from many of the shocks and repercussions of the 2008 global financial crisis.

Canadians are careful borrowers, and mortgage arrears in Canada remain very low. Only 0.23% of bank mortgages were in arrears as of August 2019, according to the Canadian Bankers Association (CBA). This compares with 0.92% in the UK for Q3 2019.

This reputation for caution may explain why Canada has seemed slow to adopt Open Banking, which has been embraced by other markets including Europe, the US, Asia and Australia.

"We are behind other jurisdictions such as Great Britain and Australia and there are indications that other countries will soon follow suit," says Richard Remillard, a Director of the National Crowdfunding & FinTech Association of Canada.

"These days, observers point to countries as diverse as Kenya and Singapore when looking to FinTech leadership," he adds. "And, then there's China and the US, each with a host of flagship firms and FinTech, often bundled together in novel ways."

Early adoption

Several factors are conspiring to slow early adoption of Open Banking in Canada, Remillard suggests.

"First, public opinion research commissioned by the federal government seems to indicate a lack of enthusiasm on the part of retail banking customers. There have been several high-profile cases recently wherein retail customers' personal data has been accessed by hackers and this has contributed to this unease around the sharing of banking information.

"Second, the major banks appear to have adopted a 'make haste...slowly' approach to Open Banking, which is reflective of a conservative, risk mitigation business culture and, likely, internal disagreements over whether or not individual financial institutions would benefit or lose.

"Third, no single champion of Open Banking has emerged to drive the debate and put it on the government agenda. Simply put, proponents have not been able to crisply define what problem Open Banking is designed to solve."

Could Canada's apparent hesitation be a warning to other nations to pause and consider the full impact of Open Banking?

Remillard believes that, unlike other innovations, there is probably no 'first mover' advantage to the country that adopts Open Banking before others. This is likely due to the timing mismatch between when benefits and costs are likely to emerge.

"Benefits will be slow, incremental and measured in years, if not decades," Remillard says. "In contrast, costs – security, system stability – are likely to manifest themselves in short order. Other countries will need to do their own cost/benefit calculations, in part determined by the state of competition in their own domestic markets. From a global perspective, the best outcome might be for there to be a lot of spaghetti thrown at the wall – and then see what sticks. In other words, countries might collectively benefit from different approaches to Open Banking being taken, and then assessing what works best."

Fast followers

At the margins, Remillard believes failure to move on Open Banking will negatively impact the growth and development of the FinTech sector in Canada. But there may be other ways of stimulating competition among financial institutions, quite apart from Open Banking, and that could deliver the same benefits to consumers and small and medium-sized enterprises (SMEs).

"These could include opening up the banking system to more foreign competition, easing the rules for new bank formation, and removing the disincentives that are barriers to retail and SME customers switching banks."

Canadian banks have long been 'fast followers' – rather than first movers – with respect to financial sector innovation. It is quite possible that the same approach is now playing out regarding Open Banking, Remillard says.

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Richard Remillard,
National Crowdfunding & FinTech Association of Canada

"Also in play are two new factors. Canada has emerged as a leading hub for artificial intelligence and the main financial institutions are closely involved in the development of this tool, which should provide them with a competitive advantage going forward. On the other hand, all eyes are on the American and Chinese Big Techs, such as Google, Amazon, Apple, Facebook, Alibaba, Tencent, and the looming threats they pose to established financial institutions, not only in Canada but globally."

Widely trusted

In May 2019, Accenture published a report on the Canadian market entitled Open Banking in Canada: Opportunity Knocks.

Authored by Andrew McFarlane, Managing Director, Canadian Payments Practice Lead and Global Open Banking Lead, and Robert Vokes, Senior Managing Director, Financial Services for Accenture in Canada, the report found that three-quarters of Canadians were not interested in Open Banking at this early stage.

Nine out of 10 were also concerned about the privacy of their financial data, and most do not trust large tech companies with that information.

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At the same time, most Canadians do trust their banks. A significant 70% of Canadians in Accenture's survey said they would trust only their banks with their financial data, even if a third party could provide added benefits.

"Canada's banks are widely trusted, in part thanks to their prudent approach to risk that saw them weather the 2008-09 global financial crisis," writes McFarlane in the report. "They should use this trust element to leverage Open Banking's opportunities."

He adds: "We know the Canadian banks are very interested in Open Banking and they are taking pre-emptive steps in advance of the regulatory framework to ensure that it would be adopted in an effective and secure way – that benefits clients and upholds the long history of client trust they've built."

Data concerns

Although nine out of 10 Canadians say concerns over the privacy of their financial data make them wary of Open Banking, 71% say better security measures would help to address those issues.

Accenture's survey also shows younger Canadians are more interested in Open Banking, with one in three respondents indicating they would allow third-party providers to access their financial data if it meant they received a better deal or other benefits. A similar proportion are prepared to let non-financial firms manage or access that information.

"To succeed, banks must work with FinTech providers and others to develop Open Banking ecosystems that will see them become central hubs in their customers' lives," Accenture's report suggests. "If banks don't, others will – and banks will run the risk of losing that critical customer stickiness and loyalty."

At its heart, Accenture says, Open Banking is about data. It is a process in which customers authorise their banks to share their financial data with registered third-party providers, and also – for multi-banked customers – among banks. Ecosystems can be built on this data through application programming interfaces (APIs) – the software that connects banks with third-party providers – and bring together financial and non-financial services on new platforms.

The right approach

The challenge for Canada in terms of implementing Open Banking is finding a balance between a top-down regulatory approach, a light-regulation route, and a collaborative model, Accenture believes. Lessons can be learned from other countries.

The UK introduced Competition and Market Authority (CMA) regulations to encourage higher levels of account switching and regulated the design of APIs to ensure standardisation.

"On the one hand, this made it easier for third-party providers to connect to banks; on the other, it stifled innovative approaches," Accenture says.

"This can be contrasted with the market-driven approach in Singapore, where the banking sector drove the changes, bringing new products, services and marketplaces to Singaporean customers. The industry has worked closely with the regulator to ensure the market's needs are met."

Accenture believes Canada would benefit from a New Zealand-style collaborative approach to implementing Open Banking.

"New Zealand's approach was more collaborative: it set up a proof-of-concept pilot that involved banks, the regulator, FinTech firms and software providers such as those involved in payroll and accounting," Accenture explains in its report. "The result was agreed standards for APIs that allow interconnectedness, and innovation, and a proof-of-concept that could iron out any issues prior to going live on a broader scale."

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Public consultation

In January 2019, the Canadian government launched an Open Banking consultation to measure the public's appetite for sharing financial data with third-party providers.

A spokesperson for the Department of Finance Canada explains: "To assess the merits of Open Banking, the government appointed an Advisory Committee on Open Banking to undertake a thorough examination of how Canada's financial sector might offer innovative products and services, while keeping the highest regard for privacy, security and financial stability.

"To support the Committee's work, a public consultation paper was released in January 2019, and roundtable consultations were held to learn more about how Canadians feel about Open Banking. During the consultation period, the government received over 100 stakeholder submissions."

The consultation seeks to learn more about Canadians' views on Open Banking, specifically: would Open Banking provide meaningful benefits to and improve outcomes for Canadians? If so, in what ways? For Canadians to feel confident in an Open Banking system, how should risks related to consumer protection, privacy, cyber security and financial stability be managed? And: if you are of

"There are specific characteristics of Open Banking which increase the risk of financial crime."

Canadian Bankers Association

the view that Canada should move forward with implementing an Open Banking system, what role and steps are appropriate for the federal government to take in the implementation of Open Banking?

Consumer confidence

The Advisory Committee on Open Banking completed the first phase of the review in 2019 and, at the time of writing, the Department of Finance Canada was considering its findings.

"Canadians deserve a financial sector that is globally competitive and promotes consumer choice, while also delivering financial stability and economic growth," the Department of Finance Canada spokesperson says.

"They must also have confidence that it operates with the highest regard for privacy and security. Protecting the privacy and security of Canadians' financial data is an objective that is shared by both the government and the private sector and one that is crucial for maintaining continued trust in Canada's financial system."

The CBA represents more than 60 domestic and foreign banks, including Canada's big five banks, smaller domestic banks, and Canadian subsidiaries of foreign banks.

In its submission to the government's Open Banking consultation, it agrees that Open Banking offers benefits to consumers, including small businesses, financial institutions such as banks, and other third-party financial service providers. But that key risks must be addressed in four key areas: consumer protection, privacy and confidentiality, financial crime, and financial stability.

For example, customer information should be shared only with informed customer consent obtained in a transparent manner that enables the customer to understand how their financial transaction data will be used and secured. As a priority, financial institutions must invest substantially in technology, infrastructure, and training to protect the personal and confidential information entrusted to them by their customers.

Addressing the risks

On financial crime, the CBA says: "There are specific characteristics of Open Banking which increase the risk of financial crime, including data proliferation, increased connectivity and the use of log-in credentials by third-party providers to access data on behalf of customers. It is crucial to understand these risks, and how they can be managed by Open Banking participants."

Consideration must also be given to risks to the safety, soundness, and stability of the overall financial system in Canada, with third-party provider access to financial data in an Open Banking system.

"Canadians trust our financial system due to its stability, as evidenced by the banking industry's performance during the 2008-2009 financial crisis," the CBA says in its submission. "As the federal government explores the merits of Open Banking, it is important to ensure that Canadian's trust in their financial system is not put at risk."

A spokesperson for the CBA adds: "The Canadian Bankers Association strongly supports innovation and competition in Canada's financial services sector, and we support the federal government's ongoing efforts to explore the benefits and risks of Open Banking within the Canadian context.

"Policymakers in Canada are taking the appropriate time to make the necessary and important analysis of key areas of potential risk before introducing an Open Banking regime. Canada is moving forward prudently to assess the full scope of Open Banking to ensure it meets the goals it is intended to achieve.

"We will continue to work with the federal government in its ongoing, multiphase process and we believe in continuous dialogue between the banking sector and key stakeholders to arrive at an outcome that optimises the possibilities of Open Banking by recognising Canada's unique characteristics, while also protecting the interests of customers in a digital environment." CB

CANADA – KEY BANKING FACTS

- Number of banks in Canada: **88**
- People employed by banks in 2017: **275,825**
- Contribution to Canada's GDP by banks: **approximately 3.3%**
- Percentage of women senior managers with the six largest banks (2017): **37.6%**
- Number of financing relationships with SMEs across Canada: **1 million+**
- Bank mortgage arrears (at August 2019): **0.23%** (compared with 0.92% in the UK for Q3 2019)
- Spend by Canada's six largest banks on technology in the last decade: **CAD$84.5bn**
- Percentage of Canadians who do most of their banking digitally, using online and mobile banking: **76%.**

Source: Canadian Bankers Association