

Funding Circle's Submission to the Canadian Open Banking Consultation

The Advisory Committee to the Open Banking Review
Financial Institutions Division
The Financial Sector Policy Branch
Department of Finance Canada,
90 Elgin Street
Ottawa, ON K1A 0G5, Canada

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To: The Advisory Committee to the Open Banking Review

Introduction and recommended next steps:

We are delighted to respond to your Open Banking (OB) consultation request.

We see great potential for OB to improve the way Canadian SMEs access finance and manage their cash flow whilst responsibly protecting both investor returns and consumer privacy. Based on our learnings from the UK and Europe, we believe OB will achieve the most positive impact for Canadian SMEs if roll-out is managed centrally by an empowered government-mandated entity who is able to balance industry demands, customer needs and data protection concerns. Given our view that Canada should move forward with implementing an open banking system, we would recommend that the federal government takes the following steps:

1. Create a central implementation entity and ensure it has power to enforce standards on banks.
2. Form an industry working group across stakeholder groups (including banks and non-bank financial institutions) and independent members.
3. Review the UK standards, with a view to assessing aspects that have worked well, and those that could be improved, and take the opportunity to improve on the points outlined below:
 - i) Ensure critical information is included in OB
 - ii) Create clear guidelines for how customers give consent to share OB data
 - iii) Ensure customer consent to share OB data on an ongoing basis is valid for more than 90 days

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About Funding Circle:

Funding Circle is a leading global small business loans platform. We allow investors to lend directly to small businesses looking for finance. We operate in four markets (UK, US, Germany and the Netherlands) and have originated £6.3 billion of loans. Every business must first pass a rigorous credit assessment process before investors can lend to them. We typically support businesses on the smaller end of the SME spectrum¹ who have a proven track record² and are looking for finance to expand and grow or to finance working capital³. In 2017 alone, businesses we supported used their funds to create and sustain more than 75,000 jobs globally, and contributed £4 billion to the global economy⁴.

We are not currently active in Canada, but we plan to enter later in 2019. We view this letter as the beginning of a deep and cooperative relationship to help shape the regulatory landscape for marketplace lending in Canada and ensure appropriate regulation of our novel business model, as we have done in the markets in which we already operate. We would appreciate if our submission was not disclosed in any form without our express consent until March 8th, when we plan to announce our intent to enter into the Canadian market.

Funding Circle has been closely involved in the UK OB process. As winners of the NESTA “Open Up Challenge” in the UK, we have access to a sandbox environment with UK OB data. We are not using the OB APIs in our core business today for a number of reasons outlined below, but we believe OB will be integral to delivering great customer experiences and wide access to finance to our SME customers in the future.

The benefits of Open Banking for Canadian SMEs:

1. Expand credit criteria to serve more SMEs: We will be able to expand our credit criteria responsibly by reviewing longer time-series of bank data from customers through OB than what is feasible to collect directly from customers (for example, through PDFs). This will entail more accurate pricing of risk which better protects our investors and supports a stable financial system, whilst expanding our credit criteria to include more SMEs (for example, to seasonal businesses, younger businesses or businesses with thin credit files).

2. Enable better customer journeys for SME loan applicants: We will be able to remove the need for SME customers to submit documents (in particular bank statements) ahead of credit approval. This will speed up the loan application process and facilitate competition as it becomes easier to compare loan providers. Taken together, we strongly believe that the expansion of risk criteria and the better customer journey enabled by OB will open up a significant portion of the underserved markets, whilst improving the stability of the financial system.

¹ UK SMEs taking out finance with us have on average 6 employees and £800,000 turnover pa.

² UK SMEs taking out finance with us have on average been trading for 9 years.

³ UK data point: >85% of Funding Circle loans are for growth, expansion or working capital.

⁴ Source: Oxford Economics “The Economic Impact of Lending Through Funding Circle” (June 2018)

3. Help SME business owners better manage their finances: SME business owners often express a need for support with cash flow forecasting, particularly those with lower financial literacy. We are currently developing a tool for SME business owners based on OB data to help them forecast their cash flow and manage their business better. It is our work in this space - in particular our proposed solution to the problems faced by small businesses - that led to us winning the “Open Up Challenge”.

Learnings from the UK implementation:

The UK implementation of OB has benefitted from a strong and transparent implementation unit led by an independent Chair, but has also suffered from a number of significant issues which we would hope the Canadian implementation would be able to avoid.

1. Create a single, well-empowered implementation unit: The UK opted for an implementation model where a single entity, the Open Banking Implementation Entity (OBIE), was set up to deliver OB. OBIE was created by the Competition and Market Authorities (CMA), which is a public enforcement agency responsible for ensuring that competition and markets work well for consumers, where needed through the use both criminal and civil powers. The advantage of this model is that a central unit can create consensus between the various interests (particularly those of the banks versus those of the non-bank community) and ensure timely progress, whilst responsibly protecting consumers and their privacy. The OBIE has ensured that implementation in the UK has moved at pace without compromising cyber security. For example, instead of rolling out in a “big bang” release, the implementation unit chose a controlled gradual roll-out where industry players could beta test the software in small batches before fully rolling out. This centralized and managed approach to implementation has allowed the UK to become a global leader in Open Banking, and the common standards that have been created are already allowing third parties to create new and innovative financial products for UK consumers and SMEs.

Whilst the implementation model in the UK has been positive, we - and other non-incumbent financial institutions like us - have also encountered a number of challenges.

2. Ensure critical information is included in OB: Some critical information is not currently included in the data made available through OB in the UK. Most importantly, the OB data set does not include account names, and instead identifies customers on the basis of their bank account numbers and sort codes. This is due to guidance set out by the European Banking Authority under the Second Payment Services Directive (PSD2) which is the European-level legislation underpinning UK OB. We are not able to rely on this information alone to confirm that a person applying is directly linked to the business account for which we are receiving OB data. This unduly increases fraud risk and is the main reason we are not using OB data in our credit process today. We are currently exploring other data sources to help improve this process but it would be a much better solution for OB data to include account name information.

3. Create clear guidelines for how customers give consent to share OB data: In the UK, the lack of clear guidelines on the customer journeys for giving consent to share OB data has meant that the take-up rate amongst customers has been lower than expected. The implementation approach taken in the UK requires customers to log in to their online banking portal to give consent for OB data sharing. This supports strong cyber security because it avoids sharing log-in credentials with a third party. However, since there are no guidelines for the design of this consent-giving experience, banks have, in some cases, added additional steps or created experiences that look unlike their native banking environment; this discourages customers from giving consent for data sharing. This weakens the case for products relying on OB and hampers investment in alternatives. Guidelines have now been created and will be in effect within 6 months. Canada will be able to ensure a strong uptake of OB if guidelines are formulated to underpin smooth customer journeys in advance of implementation.

4. Ensure customer consent to share OB data on an ongoing basis is valid for more than 90 days: The precise legislative formulation of how data must be shared could reduce the value of OB data in the UK. Under PSD2, OB only allows for up to 90 days of ongoing data access after which a customer will have to again consent for data to be shared, but 90 days is not enough time for most services to create lasting customer relationships and therefore provide genuine competition to incumbents. When we have spoken to our borrowers about OB, they have typically told us that they would expect data sharing consent for third parties to last for 180 - 360 days or to be on a continuous basis, whilst having the control to revoke consent at any time.

I hope this is useful as you consider how to progress with Open Banking in Canada. To reiterate, we believe OB has fantastic potential to revolutionize how SMEs access finance and manage their cash flow, whilst supporting a stable financial system.

Naturally, we are keen to engage further with the Advisory Committee, the Ministry of Finance and other stakeholders on this topic, as well as other regulatory topics that impact on innovation generally and our marketplace-lending model in particular.

Please do not hesitate to reach out if you have any questions, or we can be of further assistance.

Best wishes,

Tom Eilon – Country Manager - Canada, Funding Circle