Open Finance: Past, Present and Future

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Introduction

Open Finance is often hailed "the future of banking", given how it will revolutionize the way both banks and users utilize financial data. So what does Open Finance entail and how can it help both the financial institutions as well as the customers themselves?

In this white paper we will dive deeper– exploring its definition, recent historical context, the current regulatory framework, as well as looking ahead towards the future, with the implementation of FIDA. We will also look at how Open Banking makes banking more convenient for customers, while providing additional opportunities for Financial Service Providers. Despite its clear benefits, given the ease in which financial information can be exchanged, Open Finance brings forth its own security and technology considerations, which banks must proactively find solutions for. This is where SBS comes in; providing various compliance offerings for banks, helps them to manage the new demands brought on by Open Finance, while ensuring the evolving regulatory and standard requirements are met.

01 Open Finance – a definition

> Open finance refers to **the sharing of personal as well as non-personal customer data held by financial sector intermediaries alongside other data holders, with third-party providers.**

This is done with the purpose of providing a wide range of financial and information services. (1) **Open Finance essentially expands the scope of Open Banking, by transitioning payment and bank account data into a broader range of consumer data (credit, investment, insurance, pensions)**. It therefore has the potential to offer a more tailored, informed, and innovative service to help consumers and businesses better manage their finances. It also may help to foster innovation, competition and cost efficiency within the wider financial sector.

According to Eurofi, the European think tank, the main objectives of Open Finance are the following:

- To offer those individual consumers and businesses, who consent, to share their financial data in an effort to offer an improved range of financial products and services, which leverage the potential of data-enabled innovation in finance.
- To increase competition in the provision of financial services, in order to benefit customers and of the overall financial system (1) From a regulatory perspective, Open Finance may also support oversight and supervisory capabilities through the direct provision of prudential, product or consumer information, potentially on a real-time basis.

Open Finance will undoubtedly affect various sectors. Banks, but also lenders, electronic money and payment institutions, insurance and mortgage companies are expected to benefit from increased data sharing, provided they also manage possible risks and challenges.

(1) EUROFI REGULATORY UPDATE . (2023, April). Open finance: opportunities, challenges and policy implications.

02 The current regulatory framework

> In June 2023, the EC published the legislative proposal for **a framework for financial data access (FIDA), which was designed with the objective of fostering the safe implementation of more innovative financial products and services.**

FIDA is positioned to work alongside PSD3 and PSR open payments. These legal frameworks regulate the access to activities surrounding providing payments and electronic money services. They also provide supervisory powers and tools for the supervision of payment institutions. Account Servicing Payment Service Providers (ASPSP) own the data, which includes traditional banks, payment institutions, e-money institutions, and fintech companies. In this case, data users are the Third Payment Services Providers (TPSPs). FIDA also works alongside the Digital Markets Act, which defines how the data generated by platforms may be used with prior consent by users. It is dedicated to platforms that provide core platform services, such as: Amazon, Apple, Meta Platforms and MS.

FIDA is solely dedicated to Open Finance, including managing data from mortgages, loans, savings, investments, financial instruments, crypto-assets, real estate, pension rights, non life insurance products (health insurance not included) and any other data providing information about credit worthiness. This data is held by credit institutions, payment institutions, investment funds and managers, crypto asset service providers, PEPP, insurers and reinsurers, and so forth. The data will be used by Financial Information Services Providers (FISP) and the aforementioned data holders.

FIDA is structured around several key aspects. First, data access: The data holder needs to make data accessible upon the electronic approval of a customer in real time, continuously and free of charge for the payment service users (PSUs). For third-party providers (TPPs), it provides a legal environment where market participants can create monetization model. Next, responsible data use: data transfer requires explicit permission by the customer, and should be easily controllable via digital means (i.e. using a permission dashboard). The data holder is responsible for making this accessible, providing real time updates and cooperating with other institutions for access.

This leads to the financial data sharing scheme: Within 18 months of the implementation of the regulation, all stakeholders (data holders, data users and associations) must adhere to the financial data sharing scheme (governing body of a specific type of data). If required, they may become a member of several financial data sharing schemes. Furthermore, we must take into account the eligibility for data access and organizations. Financial Information Services Providers must submit an application for access to customer data, to the governing central authority (CA). This application needs to include the type of data requested, as well as a business plan for the next 3 years, illustrating the ability to manage the data appropriately.

03 Looking ahead - implementation of FIDA

As it stands, it is predicted for potential adoption to take place sometime in late 2024 or early 2025. This depends on the pace of negotiations and political agreement. Regarding enforcing entry, once adopted, FIDA will have a 24-month implementation period. This means it wouldn't be fully operational before late 2026 or early 2027. In terms of specific features, some FIDA features might have additional delays. For example, rules concerning financial data sharing schemes become applicable 18 months after the regulation comes into force.

Potential adoption

Implementation period

Fully operational

LATE **2024** EARLY **2025** LATE **2026** EARLY **2027**

04 End user experience: how does Open banking make banking more convenient for customers?

Open Finance broadens the open banking approach to almost all financial services, including banking and savings accounts, investments, insurance and pension products.

This wider sharing of financial data and interconnection of accounts may bring value to retail and business customers, in combination with data analytics and Artificial Intelligence (AI).

Examples of use cases of open finance include dashboards aggregating personal and business financial accounts, Wealth management or investment management advice tools, product and supplier comparison tools, creditworthiness and mortgage assessment, insurance, as well as ESG and managing our carbon footprint.

Dashboards aggregating personal and business financial accounts refer to bank accounts, savings, investment, and various other pension schemes and products. Over 90% of consumers surveyed said they would use dashboards that consolidate the view of pensions, savings, and investments in one place according to a TISA/ EY survey (2). Dashboards allow users to gain a holistic view of their finances, therefore getting a better understanding to optimize their overall financial position (cash flow, savings, investments, future projects and pension needs). For instance, Citi is currently offering its My Citi dashboard to its UK customers.

Another customer benefit falls under wealth management, or investment management advice tools designed to support the financial decisions of retail investors, aggregating data on various investments in one place. Automatising tools such as automatic saving, where excess funds are automatically transferred to a savings account, and covering a possible overdraft, saves the customer both time and money. For business customers, Open Finance also fosters the automation of key business processes, including accounting, billing, and invoicing, improving the user experience and simplifying transactions.

The product and supplier comparison tools within Open Finance allows customers to compare products, fostering innovation and cost-optimisation for the customer. The transferability of customer-profile data and information on current savings and investments has also dramatically increased, facilitating on-boarding and supporting financial advice, and in turn facilitating the switch of products and providers.

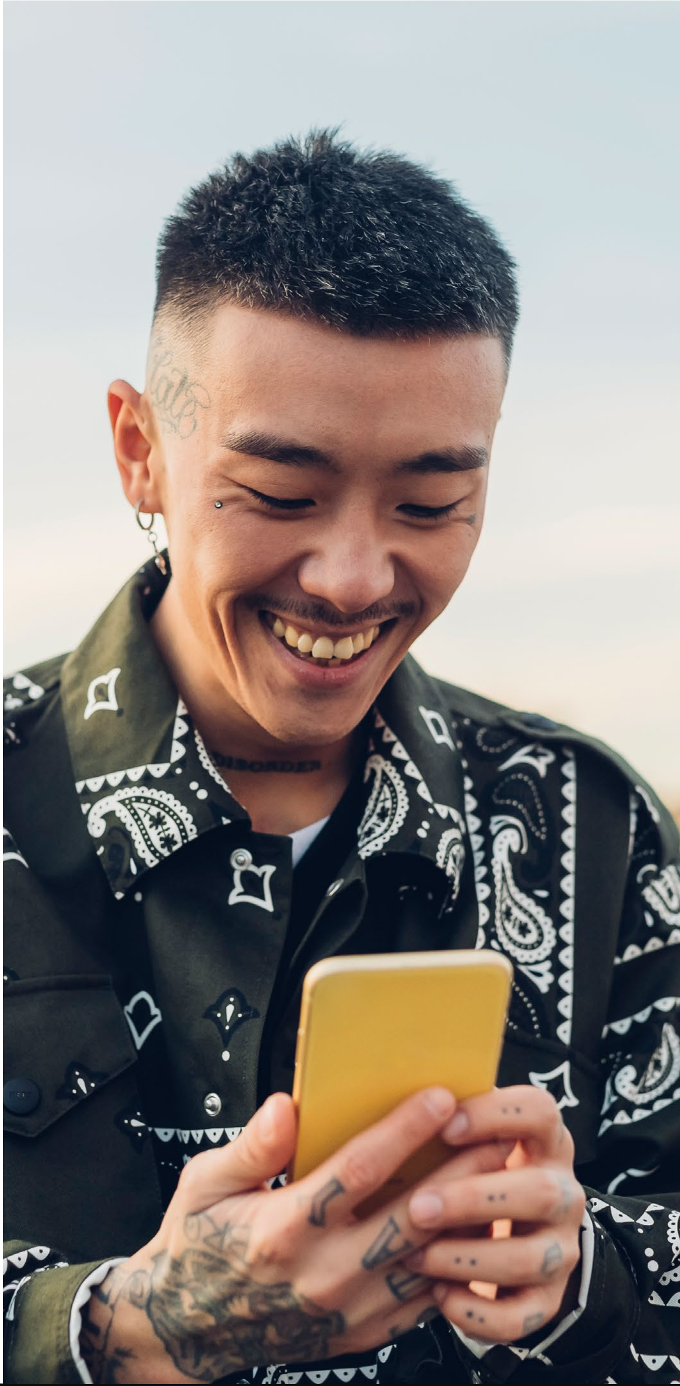
In regards to creditworthiness and mortgage assessments using a wide range of financial data, Open Banking enables lenders to analyze financial data for up to two years from various financial intermediaries and providers. It can also provide a more holistic view of the financial picture for SMEs and individuals, based on their financial assets, cash flows and payment and account history. As such, Open Finance streamlines the credit and mortgage application processes, making it possible for services such as credit embedded sales processes and credit-as-a-service.

When considering insurance, the sharing of personal data such as the actual living situations inferred from the analysis of bank accounts, can check whether a policy is up to date. It also helps with the handling of insurance claims made by third parties. Lastly, it can provide more customized policies due to this sharing of data or in-vehicle data, which can also be included in the sales process (LexisNexis in the US). [1]

(2) Finlay , S. (2022a). Pensions Dashboards Programme Willingness to pay research. IPSOS.

05 Open finance opportunities for financial services providers

> Both newcomers and incumbent firms benefit from **an easier and expanded access to customer datasets within the Open Finance framework.**



Open finance will introduce new forms of competition for traditional banks and insurers, while bringing new opportunities to better serve existing customers, as well as attracting new ones. Traditional players through the use of Open Finance solutions improve their offering, and develop cross-selling opportunities, by integrating services from third parties seamlessly through APIs. In addition, the consolidation of customers' financial data in one place, gives banks and insurers a more holistic view of the financial situation of a client, allowing them to offer new services, while improving the advice they currently provide to their customers.

Open Finance will also create opportunities for new services providers. New entrants such as Fintechs, will be able to offer new services based on the data sharing and aggregation possibilities, in the areas of investment and financial advice, pension preparation, mortgage and credit and insurance. Just as Open Banking has increased business efficiency by introducing more effective payment methods, Open Finance can take it a step further by creating even more opportunities for various businesses. For all players, the increased efficiency surrounding a number of processes, such as credit application, on-boarding, AML verification, claims management, and so forth, are made possible by the streamlining of data collection. Decision-making in bank lending processes or more effective wealth management services or insurance processes is also facilitated by expanded access to customers' financial history.

06 Security considerations for banks and customers

Overall, Open Finance requires more security measures from financial providers in an effort to improve the customer experience. This is made possible through four main aspects.

- The first element surrounds account opening. Instant Account Verification (IAV) technologies are designed to verify accounts in less than 5 seconds, using direct OAuth connections, eliminating the reliance on microdeposits.
- Next is the account login, which utilizes Multi-Factor Authentication (MFA) and biometric options.
- Following this is account aggregation; Open Finance eliminates the need for consumers to share their credentials, in order to connect financial accounts into a single view, moving away from the need of screen scraping.
- Finally, daily financial management is improved, as tapping into customer data allows financial institutions to identify patterns and anomalies, thus proactively making actions against fraud. (3)

Despite its clear benefits, Open Finance is not without its challenges, for both customers and financial services providers. Customers must pay attention to several key aspects. First of all, Open Finance leads to increased vulnerability of customers to financial crime, fraud and scams, as well as operational ICT risks such as API security risk and cyber risk. Next to this, the disintermediation in the provision of financial services, may allow for the development of advisory tools, possibly leading to misleading recommendations or oversimplified recommendations, replacing the traditional financial intermediaries. In fact, the use of sophisticated data analysis and AI may lead to biases concerning certain customer profiles, errors due to out of date or incomplete data or unfair price optimisation practices, possibly leading to discrimination, exclusion and over-charging.

In order to best combat these issues, banks should pay attention to several key aspects, the first of which being trust. The sharing of customer data with new service providers, such as FinTech's, creates a potential concern in terms of customer trust. Banks will need to prove compliance to adequate security standards (such as ISO 27001 and ISO27701), as well as communicate about this directly to customers, in order to build and maintain trust. Furthermore, there are a unique set of operational risks. Those relating to API use, interoperability issues between different types of systems and applications including legacy systems, an increasing complexity and dependency in the interconnectedness with third-parties, greater exposure to cybersecurity risks, and a possible shortage of skills for operating such environments.

Competition risks are another area of concern. Open Finance may lead to asymmetrical access to, alongside the greater sharing of data between financial institutions and third-party providers. It may also lead to an unfair sharing of costs for setting up and running APIs and Open Finance services, with barriers possibly hindering the access of newcomers to APIs and OF applications, due to insufficient proportionality in the calibration of rules or proprietary standards. Furthermore, investment is required for setting up Open Finance systems and platforms. In addition to an impact and feasibility assessment, banks need to verify whether costs should be shared along the Open Finance Value chain[1].

(3) From Money to Data to Trust: How Open Finance Improves Security.

07 Use cases (SBS customers)

Sopra Steria offers various compliance offerings for banks, helping them manage the new demands brought on by Open Finance,

including the constant regulatory changes and standards updates, alongside valid security concerns, managing user consent, traffic, and so forth. For such purposes banks often utilize third parties, such as Sopra Steria, as a large team is required to continuously manage the various Open Finance processes taking place simultaneously. Sopra Steria supports the Berlin Group standards in the EU, by offering a full compliance platform focusing on processing account information, alongside providing payment and card information services linked to the bank's core banking system, in order to extract the proper information.

Sopra Steria is able to work with different banking budgets, thus offering a tailored solution no matter the size, which fosters the interconnectivity of 3500+ banks, and opens up the door to additional collaborations and growing FinTech partnerships at scale. This provided platform does everything the standards require, so that the flow of Open Banking remains as smooth as possible, allowing banks to remain fully compliant without worry. The platform is also continuously updated, and is always evolving to meet new regulations and strengthening security alongside improving the end user experience.

It's important to mention that the SSG solution already has the authorisation dashboard available in its software suite; at the moment, banks often choose to manage the necessary authorisations with internal tools themselves, which do not cater to FIDA. This will change in the future.

If banks don't have to deal with APIs or are not yet at such a high level of maturity requiring them to expose their data to the outside world, Sopra Steria offers another solution, "The Fallback Solution". This historic method involves screen scraping technology, which exposes the raw data the old fashion way, as it was done prior. This method, though available as an interim solution, will likely disappear in the near future.

08 Look forward: future opportunities in Open Finance

> Open Finance will no doubt benefit both new and incumbent financial institutions, **by providing easier and expanded access to customer datasets within the Open Finance framework.**

Open Finance essentially expands the scope of Open Banking, by transitioning payment and bank account data into a broader range of consumer data (credit, investment, insurance, pensions).

Next to creating opportunities for new services providers, especially within the FinTech sector, Open Finance will open up the doors to new services, based on data sharing and aggregation possibilities, in the areas of investment and financial advice, pension preparation, mortgage and credit and insurance. Open Banking thus has the potential to offer a more tailored, informed and innovative service to help consumers and businesses better manage their finances. It also may help to foster innovation, competition and cost efficiency within the wider financial sector.

Despite its clear benefits, Open Finance is not without its challenges, for both customers and financial services providers. Banks will have to do their utmost to meet security standards and keep their customers safe from the increased risk of financial crime, which Open Finance may potentially create through easier information sharing.

As we look towards the future, we realize that Open Finance is a worldwide phenomenon, that in many places initially began with "Open Banking" and is now establishing more use cases and a long-term goal, to achieve full Open Finance. Advanced ecosystems can be seen across different geographies, from Australia to Brazil, including some countries in Africa, the Middle east and Asia. If we take the example of the USA, we see them pushing section 1033 of the "Dodd-Frank Wall Street Reform and Consumer Protection Act" supported by the CFPB (Consumer Financial Protection Bureau). To put it in perspective, the Dodd-Frank Act is actually one of the most important regulatory reforms in the U.S. since the Great Depression. Essentially, this legislation does the following: it restricts banks from using their own funds to trade (the "Volcker Rule"), it increases the monitoring required of systemic risks, strengthens regulations concerning financial products as well as introduces initiatives surrounding consumer protection. (4)

As of right now regulatory bodies have largely not issued sanctions regarding Open Finance, but this will likely change in the future as part of PSD3, which will require banks to evolve.

(4) Council on Foreign Relations. (2023, May 8). What is the dodd-frank act?. Council on Foreign Relations.

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Sopra Banking Software

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Nicolas serves as the Lead Product Manager for Open Banking, bringing extensive expertise in open banking, regulatory compliance, and the broader banking sector. Since 2016, he has been at the forefront of technological projects, driving innovation and product delivery.

With over a decade of experience in the financial industry, Nicolas has worked across retail and private banking sectors, with a solid foundation in financial planning and product management. His career spans multiple continents and countries, where he has honed his skills in banking, insurance, and software industries. Nicolas is recognized for his strong expertise in product delivery and his ability to spearhead innovative solutions, making significant contributions to the advancement of financial services.