



Australian Government



Australian
**Small Business and
Family Enterprise**
Ombudsman

26 September 2017

Mr Scott Farrell
Open Banking Review Secretariat
The Treasury
Langton Crescent
PARKES ACT 2600

By email: OBR@treasury.gov.au

Dear Mr Farrell

RE: REVIEW INTO OPEN BANKING IN AUSTRALIA

Thank you for the opportunity to provide comments on the Review into Open Banking in Australia. The role of the Australian Small Business and Family Enterprise Ombudsman (ASBFE0) is to advocate for small business and family enterprise. We support the development of open banking in Australia. Opening banking will improve the experience small businesses and family enterprises have with the financial system through increased competition, transparency, and customer mobility. An open banking regime will encourage new participants in the financial system. More competition between established banks and newer entrants will result in lower costs for consumers, and a better customer experience. More directly, allowing small businesses greater access to their own banking data will allow them to get a better idea of their financial situation independent of their existing bank, to better inform their decisions.

We have two concerns which an open banking regime should address. These are the extant barriers to accessing finance for small businesses, and imbalances in the relationship between established banks and business borrowers.

The current financial system underserves small business and family enterprise

The current financial system is an oligopoly dominated by the four major banks.¹ This is in part a result of high barriers to entry and prudential regulation, which in turn contributes to a higher cost of capital for small business lending. The dominant requirement affecting small business lending is an entrenched preference for real property as a security, rather than other types of security such as business cash flow. This contributes to a higher cost of capital on lending to small businesses, resulting in a portion of small business demand for finance not being met.

There are alternative sources of finance emerging in the Australian financial system, including crowdfunding and non-bank authorised deposit-taking institutions (ADIs), though the playing field is still far from level. An open banking regime will assist in levelling this

¹ House of Representatives Standing Committee's First Report into the Review of the four major banks, pg 21, http://www.aph.gov.au/Parliamentary_Business/Committees/House/Economics/Four_Major_Banks_Review/Report

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playing field by increasing the ability of customers to transfer their banking affairs between participants due to increased portability of their own data.

Opening banking regimes are increasingly being implemented overseas. This is allowing new small business entrants to the financial system to grow. Following the Payment Systems Directive 2 (PSD2) passage through the European Parliament, Europe has already seen more interest in small business financial services, particularly by smaller financial companies and startups. Consequently, there has been a rise in Fintech valuations in these markets.

The Fintech sector in the UK is focusing on the use of open application programming interfaces (APIs) to create tools specifically targeting small- and medium-sized businesses, encouraging new market entrants to employ technology to better service small businesses. Fintech companies are making use of APIs to position to become Account Information Service Providers, Payment Initiation Service Providers, credit reporters, and raisers of capital to take market share from banks. These companies are using machine learning and other digital tools to quickly and efficiently extend credit to small businesses, gaining a competitive advantage over established banks, as well as partnering with established banks to enhance small business lending. This is also developing in Australia but would be accelerated with the introduction of an opening banking regime.

As shown in the European experience, open banking should result in small businesses finding it easier to open accounts, switch accounts, control their own data and have greater access to reliable alternative sources of finance. In parallel, this should drive banks to be more transparent about the cost lending and associated services.

Improvement is needed in small business lending practices in Australia

Through our research we have identified lending practices as a major concern for small businesses. Our inquiry into small business loans released its Final Report in December 2016 with recommendations to address gaps in the existing regulatory environment and shortfalls in the practices of industry participants. In the context of financial lending to small businesses, we consistently found an asymmetry of power in the relationship between banks and small business borrowers. This manifests through prohibitively complex contracts, inadequate timeframes, misleading signals between bank sales staff and credit risk staff, and an overall lack of transparency in dealings with third parties. Despite numerous inquiries and reviews relating to the banking sector since the global financial crisis - there has been little change to this dynamic. Since August 2016, the Government and the industry have started to address some of these issues though we believe more action is still needed. We welcome the proposed open banking system as a way to increase competition in the sector and improve the small business lending experience.

We hope these comments assist you and we would be pleased to further discuss these matters with you. Please feel free to contact either myself or Mr James Strachan, by telephone 02 6263 1537 or email james.strachan@asbfeo.gov.au.

Yours sincerely,

A handwritten signature in black ink that reads "Kate Carnell". The signature is written in a cursive, flowing style.

Kate Carnell AO
Australian Small Business and Family Enterprise Ombudsman