Sectoral Assessments
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Block submission: Consumer Data Right Open Finance Sectoral Assessment of non-bank lending

Introduction

Block Inc. (Block) welcomes the opportunity to provide a submission to Treasury's Open Finance Sectoral Assessment of non-bank lending.

The Consumer Data Right (CDR) is an important piece of national digital infrastructure that aims to improve Australian consumers' ability to compare and switch between products and services, encourage competition and drive innovation.

In this submission we outline who we are and our recommendations for how non-bank lenders can be proportionally and appropriately incorporated into the CDR framework to achieve its policy objectives.

Setting the appropriate regulatory conditions for Open Finance at this early stage will be key to its long-term success. To maximise the long-term potential and useability of the CDR framework, we believe regulation must:

- Centre on the needs and interests of consumers by empowering them to access better products and services across a range of industries;
- Acknowledge the diversity of the non-bank lending sector and the nature of BNPL products and address these differences through proportionate and targeted regulation; and
- Provide incentives for innovation and experimentation in consumer and business finance by appropriately balancing strong consumer outcomes with the technological complexity and financial costs of complying with the CDR regime.

About Block

Block (NYSE: SQ; ASX: SQ2) is a global technology company with a focus on financial services. Made up of Square, Cash App, TIDAL, TBD, and now Afterpay, our mission is to build tools to help more people access the economy.

Afterpay

In January 2022, Block completed its acquisition of Afterpay - a leading international player in the Buy Now Pay Later (BNPL) sector, with 1,300 staff across Australia, New Zealand, Asia, the United States, Canada, the United Kingdom, and Europe.

Afterpay has revolutionised the way that consumers pay for goods and services by turning the traditional model of high-cost consumer credit on its head.

Afterpay is a no cost service to the customer if instalment payments are made on time. Responsible spending rules and consumer protections are built into the service – these rules help ensure customers never revolve in debt, with no exceptions. In circumstances where the customer does not pay their instalment payments on time, their service is immediately suspended, and late payment fees can be applied. Late payment fees are fixed, capped and do not accumulate or compound over time.

Merchants benefit significantly by being part of the Afterpay ecosystem, as it delivers them value, reduced risk, and deeper engagement with customers. Merchants invest in providing the Afterpay service to their customers because Afterpay provides a powerful marketing platform for reaching consumers, as well as reducing their operational costs. As a result, the cost of Afterpay is not borne by the consumer which in turn drives positive merchant outcomes.

Square

Square helps merchants more easily run and grow their businesses with its integrated ecosystem of commerce solutions.

Square offers purpose-built software to run complex restaurants and retail operations, versatile e-commerce tools, embedded financial services and banking products, an appointment booking platform, staff management and payroll capabilities, and much more – all of which work together to save merchants time and effort.

Today, we are a partner to merchants of all sizes – large, enterprise-scale businesses with complex commerce operations, merchants just starting out, as well as merchants who started out with Square and have grown larger over time. Square supports merchants from Australia to Ireland, Canada to Japan and across all 50 United States. These millions of merchants from across the globe trust Square to power their business and help them thrive in the economy.

In 2021, Square launched Square Loans in Australia. Available to current and eligible Square merchants, Square determines a business's eligibility for a small business loan and provides a customised offer based on the card sales it processes with Square. The business then chooses its loan size (within the offered range) and once approved, repays the loan automatically as a percentage of daily card sales through Square.

Overview of recommendations

To achieve the strongest consumer, business and regulatory outcomes, the expansion of the CDR into Open Finance must be underpinned by proportionate and fit-for-purpose regulation. To that end, Block recommends that Treasury:

- **Adopt a phased approach to designating entities within the broad non-bank lending sector, rather than designating the whole non-bank sector at the same time.** Entities to be prioritised first for designation should be those that provide standardised lending products and products where data does not already largely exist in the current Open Banking/CDR framework. The designation of other entities within the non-bank lending sector should be deferred until the evidence-base and industry maturity supports further expansion.

- **Prioritise the designation of standardised consumer lending products (and not business lending products) that parallel existing designations in Open Banking**. This targeted approach will facilitate the useability and uptake of the CDR regime in line with its goal of helping consumers switch, and support the evidence base for further product expansion.
- **If and when required, adopt a phased approach to the designation of BNPL and business lending datasets when these entities are designated.** Product data should be prioritised first, followed by consumer data and finally transaction data, in order to reduce regulatory burden and avoid the overlap of datasets between banks, non-bank lenders and BNPL providers.
- **Introduce de minimis principles for designated participants and products.** This will ensure that smaller entities are not unnecessarily burdened with compliance and regulatory costs, and at the product level, promote experimentation at all levels of the finance sector.

A phased approach to designating non-bank lenders

Consultation question: If non-bank lending is designated, which entities should be designated as data holders?

At a high level, Block supports the designation of the non-bank lending sector into the CDR framework. It has the potential to enrich the scope of datasets available to consumers and accredited third parties, and support the useability of the ecosystem.

The non-bank lending sector is a broad church. It encompasses both traditional and emerging companies that offer a wide spectrum of standardised, emerging and innovative products to consumers and businesses. In addition to more established non-bank lending institutions, financial technology companies - or fintechs - have become part of the market landscape.

The question of how to define the extremely broad range of non-bank lenders for the purpose of designation is an important one and sets the table for Open Finance moving forward. As Treasury outlines, the definition of ‘credit facility’ in the *Australian Securities and Investments Commission Act 2001*) or the definition of a registrable corporation in section 7 of the *Financial Sector (Collection of Data) Act 2001,* could provide a useful starting point for considering what subset of non-bank lenders that should be brought into the scope of the CDR.

On their own, however, these definitions are limited because of their breadth. They cast an extremely wide net while failing to engage with the diversity of non-bank lenders and the actual consumer useability of the CDR ecosystem.

Block supports Treasury taking a phased approach to designating entities within the broad non-bank lending sector, rather than designating the whole non-bank sector at the same time (even if there may be different implementation dates). In other words, specific entity types within the non-bank lending sector should be designated (with potentially phased implementation dates for these entities if appropriate), while the designation of other entities within the non-bank lending sector should be deferred until the evidence-base supports further designation.

A phased approach should prioritise entities based on the following criteria:

- Entities that provide *standardised* consumer lending products that are more suited to being designated under the CDR framework. Lending products such as credit cards, mortgages and personal loans are well established and generally quite standardised.
- Products where the data does not already largely exist within Open Banking due to the way such products work. In particular, transactions that are associated with interest-bearing products such as credit cards, mortgages and personal loan accounts are not necessarily reflected in other bank accounts.Although mortgage and personal loan *repayments* may be visible in another bank account, mortgage and personal loan interest charges are only visible within the credit card, mortgage or personal loan account itself.

In contrast, BNPL products are not standardised, and BNPL transaction data is largely visible in bank accounts that are already subject to the CDR. This is because BNPL products are not interest-bearing and BNPL transactions are fully reflected in consumers' linked debit card or credit card accounts (which are part of Open Banking). When a consumer completes a purchase with Afterpay, it is Afterpay that appears as the merchant of record on the consumer's debit card or credit card statement. Consumers who consent to this information being shared under Open Banking already have the opportunity to benefit from accredited third parties using this data to provide insight into their spending and budgeting patterns.

As Treasury highlights, the regulatory framework for Open Finance should avoid duplication of datasets in the system. The right balance must be struck between designating a broad scope of data to support product comparisons and the cost of making these datasets available across the broad spectrum of non-bank lenders participating in the market.

The diversity of the BNPL sector

There are significant differences between the BNPL sector and the traditional non-bank financial sector. This is because the non-bank financial sector provides the same types of products - like credit cards, personal loans and consumer leases - as the banking sector. These products are highly standardised, mature and equivalent to the existing datasets designated in the Open Banking regulations. Despite strong competition in the BNPL sector, there are also significant differences between BNPL products, business models, and the consumers and businesses they serve.

Regulation must be attuned to these differences, which will ultimately influence the long-term success of Open Finance in terms of its implementation, business participation, and consumer engagement.

The Australian BNPL sector has grown significantly in recent years with an increasingly diverse range of providers offering materially different services under the banner of BNPL. While growth has been rapid, the sector is still in its nascent stages of development. From a retail perspective, BNPL payments in Australia account for only 5% of total retail spend, according to analysis by Accenture. Analysis by Accenture also found the sector represents less than 1% of total payments in Australia and consists of a wide variety of products and competitors. The Australian Securities and Investments Commission has recognised the diversity of the BNPL industry, finding that the market for these arrangements is diverse, evolving, and growing rapidly.[1]

Key differences within the BNPL industry centre around borrowing limits, fee structures and repayment requirements. When considering repayment schedules, Afterpay's service differs

[1] https://download.asic.gov.au/media/5852803/rep672-published-16-november-2020-2.pdf.

from other providers, offering four fortnightly repayments with the opportunity to repay the full amount owing early. Other providers have no fixed repayment term but require a minimum monthly repayment. Some BNPL providers offer a number of repayment options over 2–36 months, while others offer continuing credit contracts with repayments over 2–60 months.

Fee structures vary considerably for both consumers and merchants. In Afterpay's case, we have intentionally designed a merchant sponsored model that offers our customers a free service. Although Afterpay charges late fees, these are capped both in dollar terms ($68) and as a percentage (25%) of the transaction amount - with the cap being the lower of the dollar amount or percentage. Unlike interest-bearing traditional credit products, Afterpay's late fees are reflected in the linked debit or credit card accounts of customers. Other BNPL providers limit fees to up to $200 in the first year and $125 in subsequent years (regardless of the amount of credit). Missed payment fees across most providers range from $4.99 to $15.

While other BNPL providers would also argue that they rely on customers paying them back on time, their business models are different in important ways. Other providers do not require customers to repay a BNPL purchase in a defined period. Customers may extend repayment periods indefinitely so long as minimum repayments are met and/or a fixed monthly fee is paid. Other BNPL providers provide interest-free loans to cover very significant purchases - from $2,000 all the way up to $30,000. These business models - while still classified as BNPL - are based on substantially different arrangements.

The types of consumers that BNPL providers serve also differ greatly. Afterpay offers amounts of up to $3,000. With an average purchase order of around $150, our customers skew toward younger Australian demographics who are looking for alternatives to traditional credit products. By comparison, other BNPL providers offer amounts up to $17,500 and $30,000 to access products and services as diverse as solar panels, home improvement upgrades and dental treatments.

The implications of this diversity are significant for policymakers and regulators. As new business models and products are created through innovation, regulation needs to be attuned to their specificity regardless of whether they fall under a single banner, like 'BNPL'. Setting data definitions within standards for a diverse and evolving category like 'BNPL' risks forcing some providers to either change their product offering to accommodate the required data items or else to not provide the data in a meaningful way. Neither would be sensible outcomes.

A phased approach to designating datasets

Consultation question: Feedback is sought on the potential costs or regulatory burden implications across the spectrum of potential data holders and scope of product types and datasets that could be captured.

Afterpay supports a phased approach to designating non-bank lending products and datasets. We recommend that Treasury prioritise the designation of consumer products that parallel existing designated products and datasets in Open Banking, to help facilitate the useability and uptake of the CDR regime, and support the evidence base for further product expansion.

Given the relative nascency of the BNPL sector, the lack of standardisation of BNPL products which are still early in their product development cycle, and the extent of BNPL data already captured by Open Banking, we recommend that BNPL datasets be designated after these mass market consumer products have successfully been integrated and there is strong consumer uptake of data sharing under the CDR.

The designation of non-bank business lending products should also follow the designation of consumer lending products. Currently, the CDR lacks the user base and value proposition for businesses to gain significant value from these products being designated.

When considering the scope of obligations on BNPL providers and non-bank business lenders, it is vital to consider the actual levels of participation in the CDR from consumers, businesses and accredited third parties, and what benefits can practically be derived from this data. Flexibility, proportionality and tailored solutions will be key ingredients to achieving the right balance.

Based on existing precedents in banking and energy, the phased commencement of obligations will provide fintechs, like Afterpay and Square, as well as start-ups and smaller non-bank lenders, with requisite time to upscale resources, develop and implement technical build programs, and assess delivery risks.

De minimis principles

Consultation question: Which entities, defined either by size or product offering, would be less suitable for CDR data holder obligations from a cost or technological sophistication point of view, and why?

To encourage innovation and avoid unnecessary regulatory and financial strain on the emerging Australian fintech sector, Afterpay supports the implementation of de minimis principles. These principles should be applied to both designated Open Finance participants and products to incentivise experimentation at all levels of the finance sector.

As the rollout of Australia's Open Banking framework highlighted, the CDR must be applied progressively and with a strong focus on the actual technological and financial capabilities of much smaller businesses. Across a single sector of largely heterogeneous businesses, proportionality is key. This will be particularly important for Open Finance, whose various markets and participants span an even larger range of commercial contexts when compared to the banking sector.

The experience with CDR in the banking sector shows that there is a long tail of small institutions (including start-ups) that will struggle to implement the very costly data sharing, consumer interface and compliance infrastructure required for CDR data holder compliance.

The phased approach taken by Open Banking required a progressive approach to the inclusion of different products and types of data that banks were required to be made available. Even for the big four banks, this proved difficult. In part, the delayed rollout of Open Banking and its gradual adoption foregrounds the significant financial upfront and ongoing costs involved with complying with the CDR as a data holder. The technical aspects of participating in the regime require considerable investments in new technology and people expertise. In addition to the financial costs, there are ongoing compliance and administrative requirements that many smaller organisations and start-ups may not be able to meet. The ACCC has already granted 60 CDR exemptions to ADIs reflecting the technical challenges and costs of complying with the regime.

The application of de minimis principles in the energy sector is an important lesson that should be adopted in Open Finance. Only a subset of designated energy retail data holders are required to share data through the application of a de minimis threshold. Consultations in this sector found that the cost of the CDR obligations on smaller retailers would outweigh the benefits to consumers. As the consultation makes clear, below the threshold, entities are not subject to mandatory data sharing obligations (unless they are subject to reciprocal arrangements as an ADR), but can choose to share data voluntarily.

For Open Finance, a de minimis threshold should be set for both the size of a designated participant (using measures such as total revenue and balance sheet, for example) and the size of a designated product (using measures like total customers and total product revenue).

Applying this threshold to designated entities will allow smaller businesses and start-ups to reach financial maturity before having to invest considerable resources into CDR compliance. Like the banking and energy sectors, this approach will ensure that the majority of consumer datasets can be made available in the open data ecosystem through the participation of the largest companies, enabling innovation inside the framework (through the work of accredited third parties) and outside (by reducing barriers on smaller firms).

Likewise, applying de minimis thresholds to products will encourage companies - both large and small - to experiment and innovate in established product categories and build customer momentum, without the pressures of regulatory compliance where there is little consumer benefit. Incorporating such thresholds has the potential to mirror the success of ASIC's enhanced regulatory sandbox, which allows businesses to test certain innovative financial services or credit activities without first obtaining an Australian financial services licence or Australian credit licence.

Block also supports the ACCC's sandbox for compliance with the CDR obligations. As the ACCC states, the sandbox "aims to help current and prospective CDR participants build and test their solutions faster, and improve accuracy and quality." We believe that a pathway should exist from the graduation from de minimis thresholds to the ACCC sandbox. This could facilitate the upscaling of compliance solutions for both companies and emerging products.

Opportunities to enhance financial inclusion

Consultation question: How could sharing non-bank lending data encourage innovation or new use cases for CDR data? Are there cross-sectoral use cases that non-bank lending data can support, in particular with Open Finance/Banking?

Pooling financial information from multiple sources gives consumers - and accredited third parties - an enhanced understanding of individual financial circumstances in more detail – helping provide tailored solutions to empower consumers to take control of managing their money, such as by supporting better budgeting and financial literacy. It can also provide credit providers and BNPL providers with a more holistic picture of a customer. Compared to the current credit reporting regime, the CDR can ensure that consumers are not unfairly excluded from safer forms of unsecured credit.

The credit reporting system in Australia presents a number of access barriers for a range of vulnerable people in society. One of the key hurdles is credit checks. Credit checks are a lagging customer indicator, are unhelpful for assessing creditworthiness of younger adults with no credit bureau history, and often provide an incomplete picture of a customer. In addition, the constant checking of user's credit files can lead to more consumer harm than good.

By contrast, Open Banking and Open Finance data has the potential to be much richer than credit bureau information. In other countries, where similar CDR regimes are being established, Open Banking is providing opportunities for firms to access up-to-date financial information, without having to perform credit checks. Real-time insights enable firms to gain a broader understanding of their customer's individual circumstances, and protect vulnerable customers.

Block is also exploring how Open Banking can revolutionise the way people pay around the world. For example, in the United States API integrations between banks, fintechs and other third-party providers will enable ACH payments to be processed seamlessly. In the UK, the advanced Open Banking framework will provide access to real-time data on a customer's financial commitments, enhancing our lending decision model and protecting consumers from the negative consequences of traditional credit checking and reporting.

Conclusion

Thank you for the opportunity to make this submission. We look forward to engaging with Treasury further on this important piece of national infrastructure.

Please do not hesitate to contact us if you require further input or clarification.

Yours faithfully

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