FinTech Australia

SUBMISSION PAPER:

Senate Issues Paper Response

December 2019

This Submission Paper was prepared by FinTech Australia working with and on behalf of its Members; over 300 fintech Startups, VCs, Accelerators and Incubators across Australia.

FinTech Australia

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About this Submission

This document was created by FinTech Australia in consultation with its members, which consists of over 300 company representatives. In particular, the submission has been compiled with the support of our Co-leads:

- Rebecca Schot-Guppy, FinTech Australia
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Submission Process

In developing this submission, our members held a series of member roundtables/teleconferences as well as circulating working drafts of the submission to each member to ensure everyone had the opportunity to provide input on the issues relating to the Senate Enquiry into FinTech and RegTech.

We also particularly acknowledge the support and contribution of our policy partners to the topics explored in this submission.

Questions on Notice

1. What would the mandate for competition look like in practice?

Looking abroad to the UK, one of the Financial Conduct Authority's ("**FCA**") operational objectives is to promote effective competition in consumers' interests, as long as it does not conflict with the FCA's duty to protect consumers and enhance market integrity.[1] The Monetary Authority of Singapore ("**MAS**") has a similar mandate, where the MAS must undertake supervision of the market in a way that does not unnecessarily impair the competitiveness of financial services market participants. This mandate also requires that MAS take into account the business and operational concerns of these businesses so as to not hinder them, provided that these businesses exercise good risk management and governance, and are supported by long-term and sustainable strategies.[2]

In the Australian context, there is a challenge around designating the regulator that would be held responsible for such a competition mandate. This stems from the fact that Australia has a different regulatory system with respect to financial service in comparison to both the UK and Singapore. In the Australian context, responsibility for financial market integrity is split between the Australian Prudential Regulation Authority (**"APRA"**) and Australian Securities & Investment Commission (**"ASIC"**). While broader competition issues are handled by the Australian Consumer and Competition Authority (**"ACCC"**). At first blush, the issue of financial services competition would tend to fall to the ACCC. However, for the ACCC to intervene there must be an alleged breach of the *Competition and Consumer Act 2010* (**"CCA"**). However, what we propose is a more proactive approach as has been adopted by both the FCA and MAS. Under this approach, the designated regulator would look to accelerate competition in the financial services industry by reviewing and then implementing (subject to their legislative power) changes that could 'substantially enhance competition in the financial services industry'.

In our view, this would likely need to be administered by a regulator that has the ability to implement these changes by way of, for example, administrative exemption. In this regard, we are of the view the best placed regulator would be ASIC. It is worth noting, the 'proactive competition' approach we propose should be distinguished from the amendments made under the *Treasury Laws Amendment (Enhancing ASIC's Capabilities) Bill* in 2018 that require ASIC to take into account the impact their decisions have on competition. This again, is not pro-competitive but simply ensures decisions made by ASIC are competition neutral.

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[1] Financial Conduct Authority, 'FCA Mission: Our Approach to Competition' (December 2017) 5 <https://www.fca.org.uk/publication/corporate/our-approach-competition.pdf>

[2] Monetary Authority of Singapore, 'Objectives and Principles of Financial Supervision in Singapore' (2004) 18 <https://www.mas.gov.sg/~/media/MAS/News%20and%20Publications/Monographs%20and%20Information%20Papers/Objectives%20and%20Principles%20of%20Financial%20Supervision%20in%20Singapore.pdf>.

Alternatively, we'd proposed a new authority be created that is charged with enhancing competition in the financial services industry. We acknowledge that this would require further amendments to the current regulatory framework. Having said this, it may provide a more robust means to ensure continued enhancement of the industry's structure from a competition perspective.

2. What should a CDR education campaign look like?

The CDR education campaign should be composed of various modules that address different parts of relevant markets.

Firstly, ads and explanatory materials should be available to consumers that explain what the CDR is, and the benefits that it can bring. These explanatory materials should come in the form of electronic and paper materials, and should be made available by the participating banks and fintechs, as well as government bodies. As highly technologically literate individuals, high school and university students would also be ideal candidates for targeted marketing. These campaigns could concentrate on leveraging their existing technological knowledge and familiarity, with an aim to improve financial literacy and fiscal behaviour.

Secondly, increased adoption of the CDR can be driven through an increase in professional development, particularly in key industries such as legal and professional services. Should individuals in these industries better understand the CDR and the benefits it can bring to themselves and their clients, the higher adoption rates will be. Professional development should also be provided to those in more consumer facing roles, such as customer service professionals at participating banks and fintechs.

To promote adoption through an increase in consumer trust, a consumer's interaction with a bank's CDR related interfaces, such as web pages that facilitate the movement of data or provision of consent, should be consistent with any other experience with that bank. Members have noted that in the UK these experiences can differ significantly, which can negatively impact consumer trust. Adoption of the CDR by everyday consumers necessitates accessibility and ease of use. Making the web pages that facilitate the consent process straightforward and easy for the consumer to navigate through is essential, as well as ensuring that any legal language is in plain english, and clearly sets out that customer's rights.

3. How should the government invest in fintech? what should the structure be?

There are several ways by which the government could invest in fintech.

Dollar-for-dollar matching during the financial downturn

During the current period of economic downturn, it is important that the government consider measures to support the fintech ecosystem. To alleviate some of the financial burden imposed on fintechs, the government could provide dollar-for-dollar matching of existing investor commitments for bridge finance up to a pre-determined dollar limit. This can also be coupled with a non-recourse loan with a 2 year timeframe that is fully repayable at a lower interest rate. This loan could also be tied to a requirement that there is no, or minimal, loss of employees during the period of the loan to encourage businesses to retain employees. Such an initiative is particularly attractive, as the relevant fintech would have already received validation from existing investors, streamlining the government's due diligence processes.

Improving cash flow and access to capital and lending for neo banks.

Improvement in cash flow for neo banks could be facilitated through the provision of zero or low rate subordinated loans from government entities that qualify as Tier 1 capital.

Additionally, it would be beneficial if the government made available to banks, particularly smaller banks, measures that were previously provided during the global financial crisis, such as:

- increasing the Financial Claim Scheme guarantee from $250K per customer to $1m per customer; and
- guaranteeing the wholesale funding lines of the smaller banks.

Access by neo banks to capital could also be facilitated by championing initiatives such as more generous tax incentives for investments in early stage fintechs (including neobanks) for amounts up to a certain amount (for example, $20m). Unfortunately, current legislation prohibits venture capital limited partnerships ("**VCLP**") and early stage venture capital limited partnerships ("**ESVCLP**") from investing in Authorised Deposit-taking Institutions ("**ADIs**"). There is, however, a potential tax advantage for an investor using a VCLP/ESVCLP, which may encourage these investors to specifically look at neo banks if ADI investment restrictions are lifted.

As you'll see from our submission to the Senate Select Committee on Financial Technology and Regulatory Technology,[3] extending the funding accessibility of ESVCLP funds would not only

[3] FinTech Australia, Submission No 19 to Senate Select Committee, *Inquiry into Financial Technology and Regulatory Technology* (December 2019) 93.

benefit neo banks, but also for fintechs in the areas of property development, land ownership, finance, insurance or making investments directed at deriving passive income.[4]

Direct capital injections into neo banks by the government would also be highly beneficial. This would require a consideration of things such as the quantum of the investment and the investment period. We note that such an injection was made by the Australian Office of Financial Management in residential mortgage backed securities during the global financial crisis to support lenders during a period of market failure.

Finally, neo banks could also benefit from a relaxation of supervisory capital floors and required buffers. For example, the ECB has indicated that it will allow banks to go through their capital conservation buffers ("**CCBs**") and liquidity coverage ratio buffers ("**LCRs**") as a precedent. A similar initiative in Australia will help increase lending and reduce the burden of regulatory capital during difficult financial periods. In addition to this, neo banks would benefit from a reduction in capital requirements for newly licenced ADIs.

Provide cheaper access to debt for SME lenders

Given SME lenders are in a better position than any traditional bank to assess unsecured risk intraday (and at scale), some form of support would be beneficial to the economy at large.[5] Nonetheless, to ensure SME lenders continue as they have over the past seven years, balance sheet support, either through equity or warehouse funding, is essential to allow them to continue to serve the market as they currently do.

Government-as-a-customer and a Government Banked Investment Fund

While we consider the above to be of the utmost importance to the longevity and health of the fintech ecosystem, it is important that to maintain this ecosystem the fintechs and startups need to be supported beyond investment. Many fintechs in the market would benefit from having the government as a customer. This would allow for the government to integrate efficiencies into the it's systems and would have the added bonus of ensuring that these fintechs would be able to provide future jobs, with the job growth potential increasing over time. For example, the

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[4] FinTech Australia, Submission No 19 to Senate Select Committee, *Inquiry into Financial Technology and Regulatory Technology* (December 2019) 93.
[5] The Australian Business Securitisation Fund may be an appropriate vehicle for this.

integration of e-invoicing has the potential to save $30 billion over 10 years in Australia and New Zealand.[6] Here, the return on investment potential is clear.

As developers of new concepts and products, fintechs and startups also often encounter marketing difficulties as users generally do not accept their new concepts or products. The government could assist with this problem through education campaigns (similar to the CDR campaign) that could, for example, demonstrate to the public what fintech is or what fintech products are, and the benefit they can bring to an individual or a business. This is already being done in other jurisdictions such as New Zealand and Singapore, with these governments producing online and television content to help promote and support the ecosystem.

Finally, the government could consider implementing a Government Backed Investment Fund that could assist in helping fintechs develop and grow, thereby producing more jobs. Queensland has had recent success with the Business Development Fund,[7] which provides funding of between $125,000 and $2.5m to eligible Queensland businesses. While the fund has a focus on innovative businesses that require seed, early stage or follow-on investment, it only funds businesses that already enjoy venture capitalist investment. As a result, the fund allows the venture capitalist market to be the leading investors and determine the potential markers for a high growth business.

The implementation of a similar fund, but one that focuses specifically on fintechs at a federal level, would provide much needed funding support and greater confidence in the fintech ecosystem on a national scale. Providing a fund that is specific to fintechs allows that fund to more effectively operate within the fintech ecosystem than a generalist fund, allowing for better support of market participants.

4. How do we get superannuation funds to invest without breaching the sole purpose test?

Other means of investment

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[6] Jacinda Ardern, 'Joint Statement by Prime Ministers the Rt Hon Jacinda Ardern and the Hon Scott Morrison MP Auckland, 22 February 2019' *Beehive.govt.nz* (Web Page, 22 February 2019) <https://www.beehive.govt.nz/release/joint-statement-prime-ministers-rt-hon-jacinda-ardern-and-hon-scott-morrison-mp-auckland-22>.

[7] 'Business Development Fund', *Advance Queensland* (Web Page, 13 August 2019) <https://advance.qld.gov.au/entrepreneurs-and-startups-industry-investors-small-business/business-development-fund>.

Aside from any concerns surrounding a breach of the sole purpose test, our Members are also concerned about the relatively low (but growing) proportion of superannuation funds that invest in fintechs and startups. This low rate of investments seems to be a product of the superannuation funds' individual investment processes and risk appetites, with some superannuation funds expressing that the same level of effort and due diligence is required to invest $100,000 as it is to invest $100m. This results in a lack of incentive for superannuation funds to invest in early stage companies that are raising smaller amounts of capital. To rectify this, superannuation fund investment processes and frameworks need to be modified to better accommodate smaller companies. Promoting investment in fintechs by superannuation funds would also provide benefit to their members, as it would allow a diversification of that fund's portfolio and risk profile. One potential solution is implementing a voluntary agreement where superannuation funds commit to investing a certain proportion of their funds in Australian fintech companies.[8]

Despite this, we note that there are currently a number of superannuation funds that have invested in fintechs and startups, and this activity seems to be increasing.[9]

Investment through venture capitalist funds

The most prevalent model for superannuation funds to invest in startups appears to be through venture capitalists. For example, Hostplus has put money into early stage companies such as Culture Amp and Canva through venture capitalist firms including Blackbird Ventures,[10] Square Peg, Artesian, Cathona, the CSIRO Innovation Fund, Main Sequence Ventures and the Carnegie Innovation Fund.[11] First State Super also started investing through Blackbird Ventures.

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[8] Such a solution was recommended in the Australian Computer Society in their supplementary submission to the Senate Select Committee on Financial Technology and Regulatory Technology, see: Australian Computer Society, Submission No 3 to Senate Select Committee, *Inquiry into Financial Technology and Regulatory Technology* (20 January 2020) 4.

[9] Matthew Burgess, 'Venture Capital Is the New Buzz Word for Australia Pension Funds', *Bloomberg* (Article, 19 September 2019) <https://www.bloomberg.com/news/articles/2019-09-18/venture-capital-is-the-new-buzz-word-for-australia-pension-funds>.

[10] Matthew Burgess, 'Venture Capital Is the New Buzz Word for Australia Pension Funds', *Bloomberg* (Article, 19 September 2019) <https://www.bloomberg.com/news/articles/2019-09-18/venture-capital-is-the-new-buzz-word-for-australia-pension-funds>.

[11] Dinushi Dias, 'Seed-stage venture capital fund Artesian gets $85 million boost from superannuation giant Hostplus', *Smart Company* (Article, 27 February 2017) <https://www.smartcompany.com.au/startupsmart/news/seed-stage-venture-capital-fund-artesian-gets-85-million-boost-from-superannuation-giant-hostplus/>.

[12] Some superannuation funds, however, such as AustralianSuper favors co-investments in later stage rounds to minimize risk. For example, AustralianSuper, along with Sunsuper, Statewide Super and invested in Airtree's latest round in 2019.[13]

It should be noted that a considerable amount of venture capitalists generally focus on later stage companies. While this may be a more feasible vehicle for super funds, this investment mechanism is still not opening up investment opportunities to seed stage and other early stage companies. Currently, the Victorian Labor Government, First State Super and VicSuper are working together on the $250m Victorian Business Growth Fund, which aims to help fund businesses with a high growth potential.[14] On the point of funding, we also note that the Reserve Bank of Australia and the Family Enterprise Ombudsman have stated that the economy is being held back by a lack of access to funding.[15]

Direct investment

As noted above, direct investment by superannuation funds is less common. However, we note that there have been a few examples in the market. These instances include Hostplus and AustralianSuper investing in Athena's Series B and Series C rounds, respectively.[16] One of the earliest examples of direct investments was from Equip Super, who invested in robo advisor Clover in 2015.[17]

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[12] 'Innovation investments', *First State Super* (Web Page, 1 September 2018) <https://firststatesuper.com.au/investment-and-performance/investments/investment-types/innovation-investments>.
[13] Mike Butcher, 'Sydney's AirTree Ventures closes $275M fund as Aussie unicorns gather pace', *Tech Crunch* (22 October 2019) <https://techcrunch.com/2019/10/21/sydneys-airtree-ventures-closes-275m-fund-as-aussie-unicorns-gather-pace/>.
[14] '$250 million Victorian Business Growth Fund established', *Business Victoria* (Web Page, 7 June 2019) <https://www.business.vic.gov.au/news/2019/june/$250-million-victorian-business-growth-fund-established>.
[15] '$250 million Victorian Business Growth Fund established', *Business Victoria* (Web Page, 7 June 2019) <https://www.business.vic.gov.au/news/2019/june/$250-million-victorian-business-growth-fund-established>.
[16] 'Home loan disruptor Athena breaks Australian investment record', *Athena* (Blog Post, 22 October 2019) <https://blog.athena.com.au/news/home-loan-disruptor-athena-breaks-australian-investment-record/>.
[17] Sally Rose, 'Equip Super takes stake in robo-advice start-up Clover' *Sydney Morning Herald* (Article, 28 September 2015) <https://www.smh.com.au/business/banking-and-finance/equip-super-takes-stake-in-roboadvice-startup-clover-20150928-gjw7jo.html>.

One positive for superannuation funds to consider when determining whether direct investment is suitable is that the superannuation fund may not need to pay management fees.

Screen scraping

Many of our members are concerned about the future of practices such as screen scraping, which many rely on in order to provide their products and services. Fintechs that rely on screen scraping often use it as a means to meet banking and lending requirements. For example, rather than requesting bank statements and an expense estimate, screen scraping can be used to precisely analyse a customer's data to determine whether a lender can satisfy their responsible lending obligations. Banning screen scraping would prevent many fintechs from effectively assessing whether these responsible lending obligations can be met. One member noted that the alternative would be to adopt the best practices in ASIC's Regulatory Guide 209, which acknowledges screen scraping as a method of data collection and aggregation.[18]

In its current form, the CDR would not be able to assist in meeting responsible lending obligations for several reasons. An affordability assessment requirements data all of that customer's financial institutions, some of which may not be covered by the CDR until the rollout of its later phases. Information is also generally gathered regarding that customer's existing relationships with alternate lenders, however, alternate lenders are currently excluded under the CDR regime.

While we acknowledge that the Open Banking Review ("**Review**") recommended that the sharing of data should be facilitated by application programming interfaces ("**APIs**") and not by the use of screen scraping,[19] the Review did not make any express recommendations in relation to screen scraping. Instead, the Review stated that the CDR should aim to eventually replace screen scraping as a more efficient means of data transfer,[20] but should not be mandated as the sole method by which banking data is transferred, and that other competing methods should be allowed to provide a test on the CDR's design quality.[21] Scott Farrell, who led the Review, noted

[18] ASIC, Regulatory Guide 209: Credit licensing: Responsible lending conduct, RG 209.125.
[19] Scott Farrell, 'Open Banking: customers, choice, convenience, confidence' *Treasury* (Report, December 2017) 74.
[20] Scott Farrell, 'Open Banking: customers, choice, convenience, confidence' *Treasury* (Report, December 2017) x.
[21] Scott Farrell, 'Open Banking: customers, choice, convenience, confidence' *Treasury* (Report, December 2017) 10.

these points in his submission to the Senate Select Committee on Financial Technology and Regulatory Technology.[22]

Until CDR and CDR Data is readily and widely available across the economy ie. cheap, accessible, all required data and all the major data holders are live, banning the use of screen scraping would cause significant disruption in the business models and operations across the fintech market. Such a ban would require these fintechs to change business processes, update core systems, reduce efficiency or may even result in business closures. Considering the current economic climate, we would consider banning screen scraping to be a particularly dangerous proposition for the fintech ecosystem.

About FinTech Australia

FinTech Australia is the peak industry body for the Australian fintech Industry, representing over 300 fintech Startups, Hubs, Accelerators and Venture Capital Funds across the nation.

Our vision is to make Australia one of the world's leading markets for fintech innovation and investment. This submission has been compiled by FinTech Australia and its members in an effort to drive cultural, policy and regulatory change toward realising this vision.

FinTech Australia would like to recognise the support of our Policy Partners, who provide guidance and advice to the association and its members in the development of our submissions:

- Baker McKenzie
- Cornwalls
- DLA Piper
- Hall & Wilcox
- King & Wood Mallesons
- K&L Gates
- The Fold Legal

[22] Scott Farrell, Submission No 140 to Senate Select Committee, *Inquiry into Financial Technology and Regulatory Technology* (17 February 2020).