

# Regulating open banking

The transition to open banking is part of a larger movement in the digitization of banking. Beyond the introduction of new technology, an influential driver that is having a significant impact is regulation – of the technology used, policies and processes, and the market itself.

When talking about open banking, we are generally referring to the banking practice that provides third-party financial service providers with open access to consumer banking, transaction, and other financial data using application programming interfaces (APIs). API interconnectivity provides opportunities for efficiency gains in back-end operations for banks and non-banking financial institutions, however, with that comes the need for tighter regulation not only from the

banks' perspective but also in the way third-party providers (TPPs) interact with them. As a result, the expectation is that regulation will drive API design to facilitate the interplay of various actors and bank functions in order to support innovation and cohesiveness within the financial services ecosystem.

In recent times, open banking has become synonymous with general technology-enhanced customer services provision, or

Banking-as-a-Service (BaaS), and hence regulators active within this area will find themselves focusing on customer-centric services, not simply the back-end and operational aspects.

## Saudi Arabia's phenomenal advance in open banking

A little over two years ago, there was little open banking in Saudi Arabia. Today, the Kingdom is well-placed to take advantage of a fintech-driven open banking ecosystem. A target has been set to establish 525 Saudi-native fintech registrations by 2030, and the fintech market is predicted to grow at a CAGR of 15 percent over the next five years.<sup>10</sup>

Claims that Saudi Arabia is late to the game are unfounded, considering that only 30 percent of financial institutions were using APIs as of early 2021, and especially because this was partly due to incumbents facing challenges with older tech infrastructure.<sup>11</sup> Saudi Arabia will have no such problems. Large-scale investments in infrastructure and systems, including a cloud-grade computing backbone, coupled with substantial investment by the industry, is helping to build an advanced open banking ecosystem.



There is also something to be said for the sensibility of an initially cautious approach. Lessons can be learned from the global rush to adopt open banking. For example, digital challenger banks in Australia struggled to gain a foothold in developed market segments against mainstream banking, with three digital neo-banks ceasing operation (or independent operation).<sup>12</sup>

The benefits of open banking are well understood by the industry. Banks can build richer applications and enhanced financial products that complement their existing traditional services to help them increase cost efficiencies, reduce manual and operational burdens, create more customer-focused payment experiences, unlock new revenue streams, and exploit opportunities for promotion and cross-sell of products. Developers have more scope in creating new services and tools for banking consumers to manage their finances. And customers can reap the benefits of account aggregation, greater variety and speed in product applications, and more streamlined wealth management options.

## Regulatory challenges facing the open banking model

It is the role of regulators to establish rules and regulations on compliance, set targets and ensure that risks are mitigated throughout the industry. In addition to operational compliance factors, other more general challenges impact open banking:

**Unified strategy:** SAMA is promoting a unified data strategy that leverages existing capabilities and identifies new opportunities for enhanced services. The regulator's goal is to achieve a stable and resilient open banking



## Saudi Arabia has an opportunity to lead not only in open banking innovation, but also in the regulation of the new banking model.

system based on best practice and with full protection against risk for customers and the industry.

**Open API architecture:** Open banking is dependent on the seamless access to data and the delivery of functionality served by an open API architecture. Regulators will need to ensure that TPPs seeking competitive advantage keep to the spirit of the open API architecture model, by ensuring that interoperability remains unrestricted and free from protectionist business practices.

**Establishment of standards in API design:** Regulation has a direct influence on initiatives in standards across API design, including endpoints, parameters and definitions as well as API design patterns such as design by role, positive assertion of truth, pre-arming, and authorization as a resource.

As open banking matures and API platforms are adopted by all participants, the influence of regulation on API design will diminish as the banking sector fully integrates into the API economy. With regulatory commitments met, APIs will eventually focus on meeting market demand, with API designs that are aligned more to tailored offerings that consumers want, as opposed to reflecting on a legislative mandate.

**Data and cyber compliance:** Data protection and handling regulations and cybercrime guidelines will require continual review and refreshing to protect customer privacy and security against a backdrop of a dynamic risk environment.

**Customer focus:** When new technology is first adopted, the customer experience can initially take a back seat. With open banking, the regulator will play an essential role in ensuring that consumers' rights are protected, that services offered are fit-for-purpose, and that new models seamlessly integrate with the existing regulatory framework. Through upholding standards in service provision and by putting the consumer at the center of regulation, customers will benefit from greater choice, convenience, and control, and the industry will be emboldened by regulation that protects and maintains trust.

## Going forward

The development of open banking will enable Saudi Arabia to expand its financial services ecosystem, a vital part of its plans to become a global financial powerhouse. To achieve this, it is critical to build the regulatory infrastructure in order to pave the way for the next phase of Saudi-led innovation in open banking.



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