

Resolution on Fintech

Introduction

In the past decade, the world has seen the growth of the fintech industry which has offered the possibility of new and more user-friendly ways to deliver financial service products to consumers. Fintech is defined as technologically enabled financial innovation that can result in new business models, applications, processes or products with an associated material effect on financial markets and institutions and the provision of financial services.¹ While TACD welcomes potential positive innovations into a current financial services market currently limited by its opacity, lack of competition and failure to offer appropriate products and services to many consumers, it is imperative that firms (both new entrants and established institutions), products and data analytic uses and systems are properly regulated and that consumer protection and privacy standards are firmly established.

TACD RECOMMENDATIONS

Promoting Competitive Markets by Empowering Consumers through the Regulation of the Use and Control of Data

TACD recognizes that the use of data can have a profound impact on consumer outcomes in the area of retail finance by enabling the development of innovative and improved financial products and services, increasing competition in financial markets, and empowering consumers to take greater control of their financial lives.

Nonetheless, the current expanded use of data has created new, ongoing, and increasingly challenging threats to privacy and a consumer's ability to control how personal and non-personal data about their online and offline behavior are collected and used. There continues to be a growing number of new data sources used in the identification and/or the verification of individuals, as well as the classification of consumers and in the making of predictions about them. Sophisticated data-processing capabilities allow for more precise micro-targeting, the creation of comprehensive profiles, and the ability to act instantly on the insights gained from consumer behaviours. Moreover, new mobile-payment technologies offer third parties, banks, and fintech firms the increased ability to collect information about the payments-transaction process and to share it with different participants, such as merchants and payment providers. The emergence of "open banking" will further facilitate the third parties' access to consumers' financial data.

It is essential that EU and US regulators develop, apply and enforce strong data protection rules in this new fintech-enabled market environment. Further, because we have seen algorithms created by the development of fintech products in other nations impact EU/US consumers, it is essential that worldwide customers of EU/ US designed products are equally protected.

¹ <http://www.fsb.org/what-we-do/policy-development/additional-policy-areas/monitoring-of-fintech/>

Consumer privacy rules and regulations must require the fair and transparent use of data and provide consumer control over their own data. This consumer control must include an absolute right to access, clear consumer consent before collection and use, and the right to not only receive notice and explanation when a data-based decision is made, but also the right to contest that decision. While the EU's General Data Protection Regulation (GDPR) currently provides much of these protections to European consumers, the US needs to recognize and adopt substantially similar rules.

Regulatory bodies must carefully restrict the collection, use, protection and control of all personal consumer data collected or used by financial service firms. This should specifically include:

- Explicit recognition of consumers' ownership of personal data generated by the consumer, whether that is data generated by transactions, internet use, shopping, telematics or wearable devices. Closely related to consumer ownership of personal data is the right to take one's data from vendor or service provider to another.
- Careful evaluation of the types of data being analyzed to determine whether they have any real predictive value or are merely based on junk science and/or whether their use is against the interest of consumers and/or society as a whole. For instance, the use of some data - predictive or not - may lead to discriminatory results against consumers based on their age, gender, race, ethnicity, income, physical or mental disability or medical condition, educational status, behavioral patterns or geographic location. Discrimination against protected classes must be defined not just as action that is intentional, but also data use that has a discriminatory effect or disparate impact. The recognition of disparate impact as unfair discrimination is now particularly important because of the far greater potential for service providers to utilize data that are proxies for prohibited classification.
- Appropriate licensing and oversight of data brokers and their activities. Consumer protection demands that data used for marketing, pricing, and, in the case of insurance claims settlement, be complete and unbiased. In addition, enhanced antitrust oversight of data vendors, data brokers and firms offering data-based algorithms is needed to ensure that the firms collecting outcome data from financial service providers (loan defaults, insurance claims, suspected fraud) and combining this data with new types of personal consumer information to create new predictive algorithms are not creating a mechanism for collective pricing or claims settlement decisions.
- Limitations on the nature of the consumer data that can be collected and processed. One of the guiding principles of the GDPR is that consumer data must be collected and processed fairly. Just because data may have some predictive value does not mean that firms should collect and process it, particularly if access to this data violates a consumer's fundamental right to privacy.
- Providing explicit control over personal data to the consumer themselves. Consumers should always have the ability to determine which personal data a firm can collect from them and what they can use the data for. Before firms can use this data, they must first explain how the data will be used or treated and obtain the consumers' explicit consent. Because firms implicitly and explicitly direct consumers to obtain "consent," consumers must be informed about the potential use and impact of that data usage, prior to giving their consent. The information must be presented in a short and easily understandable way. Consumers must also be provided the opportunity to limit the data firms can use to that which is specifically relevant to the fintech services they are requesting. Finally, use of their data – including its

use in evaluating third parties - must be revocable by consumers at any time and for any reason. This is stated in GDPR and the same rights should be given to consumers in US or users from outside the EU or US whom are using fintech products provided by EU or US based firms.

- In instances when consumers grant access to their data to fintech entities, limiting the firms' access the data necessary to provide the services the consumers have selected and allowing the data to be maintained only for as long as necessary for the provision of those services.
- Requirements that all data be accessed, stored, used, and distributed securely, to ensure the accuracy of the data, and to enable consumers to dispute issues of inappropriate access and data accuracy.

Prohibiting Fintech Unfair and Deceptive Practices

As with any new innovation, new opportunities will arise for bad actors to engage in unfair and deceptive practices against consumers. Three potential areas of concern include (1) "traditional" products and services offered by fintech that are not properly regulated because they are offered by fintech firms; (2) new products and business models that have not previously been considered under existing regulation; and (3) new aggressive data-driven marketing of fintech and other financial service products.

- *Fintech firms offering traditional financial service products:* While fintech offers the promise of greater competition for traditional financial service firms, marketplace pressures cannot and will not ensure safe financial products. For fintech services and products that mirror traditional financial service products – i.e. bank accounts, secured and unsecured loans and credit evaluations - all levels of existing standards, rules and regulations must be complied with regardless of the entity that offers them. Public regulators must treat all financial services firms the same – be they fintech or non-fintech – and vigorously regulate, supervise, and enforce all applicable rules regardless of the firms' status. Consumers must also have the right to enforce these rules for themselves either individually or collectively.
- *New products and business models enabled by fintech:* For non-traditional products and services developed by fintech firms, new rules, regulations and standards must be developed to provide all necessary consumer protections. For instance, consumer organisations have identified several problems with fintech-enabled "crowdfunding" platforms. Recent analysis of platforms that offer investment opportunities to consumers, has found that many platforms do not properly assess the risk of investment projects; deliberately underestimate risks, while highlighting positive elements; lack transparency on the default rates of projects financed; and net return rates much lower than advertised. In this space – which currently is not specifically regulated - rules and standards should make certain that consumers receive clearly visible risk notices and disclosures about organizational requirements, as well as the right of cancellation. Further liability standards must be established for platforms that fail to comply with these rules and/or fail to conduct due diligence of potential investments and investment amount caps.
- *The use of fintech in marketing.* The growth of fintech has led to the extensive use of the latest data-driven targeted marketing and advertising tools. This includes the use of data-driven targeting platforms that make decisions in 200 milliseconds about whether and how to target an individual consumer. The combination of powerful ways to gather and use data (such as lead generation), along with alluring and personalized interactive applications are used to identify and target consumers in real time. These practices often foster consumer behaviours that are not in the best interest of the individual, and raise

concerns about the use of data profiling. Making matters worse, unregulated online advertising practices are likely to cause the most harm to the financially most vulnerable consumers, such as consumers that are overindebted or at risk of over-indebtedness because of small economic margins. Existing standards must be applied to new fintech generated marketing schemes and new rules and regulations must be developed and applied where necessary.

Promoting financial inclusion while preventing discrimination

Fintech, if properly regulated, has the potential to create new and important financial service opportunities - including traditional savings and checking accounts and fairly priced loans and credit - for low-income and minority consumers and communities. First, the rapid spread of low-cost electronic payment systems and related banking services provides a clear potential benefit to consumers who have long been priced-out and excluded from traditional banking services. Second, both the use non-traditional payment data, as well the ability to quickly evaluate a consumer's monthly cash flow (regardless of the lack of information in the person's credit report), may provide new opportunities for low-income consumers seeking fairly priced and necessary credit. Of course, it's essential we recognize that credit can never be a substitute for having sufficient income to maintain a decent standard of living. Consumers who live on a cash basis must have access to all the same services available to consumers using credit.

While these new fintech technologies and alternative credit risk assessment models can be a boon for the underbanked, it also presents very real dangers. First, if not carefully monitored and regulated, financial service firms can and will use data to further individualize the cost of credit, creating an even bigger wealth and credit gap between classes of consumers. Alternatively, firms, if unregulated can and will use and create data models that judge individuals against group profiles based on past data. Unfortunately, too often, this group data inevitably incorporates elements of past inequality and discrimination. Second, as discussed above, increasing access to credit is not always a positive (see the 2008 financial crisis). A vast increase in consumer debt – spurred by the fintech market – can and will do damage to the whole financial sector.

Government regulators must be cognizant of these very real risks and take action to not allow the potential of fintech to increase existing wealth gaps or create a discriminatory impact. Some of the ways these potentially negative consequences can be prevented include:

- Providing greater control to consumers of their own data, including allowing them to decide what information and with whom and when their data can be shared.
- Placing limits on the type and amount of the data that fintech and/or traditional financial services firms can collect and evaluate, and making certain that the data used are predictive of what is being determined about the consumer.
- Maintaining ongoing and constant evaluation of specific sets of data to determine whether their use has a discriminatory impact on vulnerable consumers. This evaluation must also include the impact of data sets on consumer behaviour. While positive credit behaviour may be one result, because of the breadth of data contemplated and used by fintech firms, potentially socially damaging behaviour may also be increased, i.e. encouraging consumers to change their behaviour in social networks (even to defriend people who are considered poor credit risks because association with them could negatively impact consumers' perceived credit-worthiness). Also to individualize insurance premiums by the use of

personal data does not only increase the risk of discrimination it is also a deviation from the fundamental idea of insurance as a way to collectively spread risk. This development must be stopped by clear regulations as to not leave unprofitable consumers outside the safety net provided by insurance.

- Requiring fintech and/or traditional financial services firms to develop products and data analytic systems that create greater privacy protections than the existing financial system.

Finally, governments must ensure that consumers always have choices in how they access and use financial services. While fintech, and technology in general, may provide consumer benefits, consumers should not be forced to use a particular technology or to waive their privacy rights in order to obtain these benefits, nor should they be discriminated against for using cash rather than electronic payments.