By Anna Burgess Yang

Is it time to explore Banking-as-a-Service?

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Your bank probably uses at least one — if not many — SaaS products. Software-as-a-Service providers have exploded over the past several years and come in every variety imaginable, from e-signature platforms to many core accounting providers. The vendor assumes the responsibility of hosting the product in these subscription-based, web-based models.

When SaaS providers first emerged, bankers were wary of placing customer data "in the cloud." It seemed to invite the risk of customer data being compromised. But over the years, we've learned and accepted that SaaS providers are security experts with audits, credentials and partnerships with the best-of-the-best hosting platforms (AWS, Google, Microsoft) to back them up.

Fintechs have become great partners for community banks, offering sleek, easy-to-use products that can compete with the customer experience provided by megabanks. Fintechs can help extend a bank's reach beyond its existing target market, integrating with existing bank infrastructure, such as the core provider.

Yet an even more all-encompassing approach is to provide banking services when and where the customer needs them. Think about flexible financing at the point of sale or offering a business line of credit when an inventory order is placed. This is where Banking-as-a-Service comes into play.

How BaaS is different

Financial market commentator Chris Skinner defines BaaS as the provision of complete banking processes, such as loans, payments or deposit accounts, as a service using an existing licensed bank's secure and regulated infrastructure with modern API-driven platforms.

That's quite a dense definition but think of it this way: Your bank may be using APIs for a singular process, achieving a specific task at a specific point in time. With BaaS, you are using APIs but allowing other providers to connect to your entire range of financial products at any time. This is often referred to as embedded finance: Customers don't need to leave an app to get a new financial product or service they need.

The end result is the reverse of the traditional bank-fintech relationship: Your bank is essentially the "vendor," the provider of banking services, through BaaS access.

What BaaS means for growth

This indirect route blows the possibilities for customer acquisition wide open. Any non-bank company that needs to provide financial services in its digital customer experience would pick and choose capabilities offered through BaaS and embed them into its platform. These partnerships help the companies grow since they can provide a seamless customer experience and help banks grow both sides of their balance sheet. According to venture capital firm Andreesen Horowitz, banks that have implemented BaaS have two- to three-times above-market ROE.

This "outsourced" method of customer acquisition and customer experience addresses several of the pain points that banks are facing in the coming decade — extending beyond a geographical footprint and managing the demands of younger generations that are increasingly considering neobanks for their traditional banking services.

BaaS puts your bank in the driver's seat. You have something that fintechs, retail or other companies need as a licensed and regulated financial institution. They provide the product and the distribution, and you provide the service.

Developing a BaaS strategy

As you have probably assumed, BaaS is a massive undertaking. Not only do you need the technology in place to become a BaaS provider, but also the operational infrastructure to handle a potentially huge influx of additional loan and deposit customers. Technology providers can help community banks turn their legacy technology stack into a flexible environment. You'll also need to consider the compliance implications since the fintech or non-bank company will rely on your expertise — and you'll be the one facing the regulators.

You'll also want to think about the partnerships your bank would consider. Not all companies that want to use your BaaS technology will be a good fit. At a high level, you'll want to define the types of relationships that make the most sense and your parameters for assessing a potential partner. Beyond that, you'll want to think about the policies and procedures that would govern an agreement, covering everything from reporting to customer service.

BaaS is a hot topic right now, and rightly so. If it's on your bank's radar and knowing it will be a significant initiative, it's time to start creating a roadmap to offer BaaS. ◆