DIGITAL FINANCE: KEY PRIORITIES

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The trend towards the increasing digitalisation of the insurance sector

Over the past years, an increasingly important role has been assigned to digitalisation as a way to enhance the design, development and distribution of innovative insurance products and services through new digital platforms, ecosystems and other digital distribution channels. The digitalisation of the European insurance sector is currently varied and, in most cases, still at an incipient stage. There is a wide range of practices in the market and the level of digitalisation can substantially differ from one insurance undertaking to another and can evolve quickly.

However, it is clear that leveraging on the increasing availability of data and new technologies such as Artificial Intelligence, Open Finance, Blockchain or Internet of Things, digitalisation offers a wide range of new opportunities for insurance undertakings, insurance distributors, consumers, and supervisors. Digitalisation and innovation also bring new challenges—frictions between market practices and regulation that was not designed with these in mind, alongside new risks for consumers and the market.

A Europe fit for the digital age has been one of the key priorities of the current Commission. The aim has been to empower people with a new generation of technologies and to make this Europe's "Digital Decade" by strengthening digital sovereignty and EU standards, rather than following those of others. The focus is on on data, technology, and infrastructure.

The insurance sector has been heavily impacted by this strategic priority over the past years. In 2020 the Commission adopted a digital finance package, including a Digital Finance Strategy, setting out how Europe can support the digital transformation of finance, while regulating its risks.

The strategy set out four main priorities: removing fragmentation in the Digital Single Market, adapting the EU regulatory framework to facilitate digital innovation, promoting a data-driven finance, and addressing the challenges and risks associated with the digital transformation. The latter includes enhancing the digital operational resilience of the financial system.

The strategy was accompanied by proposals on DORA, MICA, and DLT Pilot Regime. Furthermore, proposals were published on the Data Act, Digital Markets Act, Common Data Spaces, Digital Services Act and Data Governance Act, European Single Access Point (ESAP), AI Act and Financial Data Access (FIDA).

The pace of innovation has created an urgent need for such a regulatory framework. The very recent uptake of generative AI is an example. The same speed has also made it challenging to complete policy cycles and to take the time necessary for implementation.

Today, more and more financial services policy making happens through cross-sectoral proposals. This is the case for the AI Act, the Data Act, the Digital Markets Act, the Digital Services Act and others. This trend is expected to continue. Going forward, it is important to thoroughly consider the impact of cross-sectoral legislation on insurance and to engage with the insurance and supervisory communities early on in the process. This way, sector specialties can be considered and the whole regulatory framework can fit together well.

In addition, it is important to consider diversity and inclusiveness when making policy, by listening to Member States for practical examples on digitalization, including the smaller ones. Regulation needs to remain fit for purpose, proportionate, and forward-looking, and at the same time, allow for benefits to materialize. This is important for the European insurance sector in order to remain globally competitive without hindering our common values.

Forward-looking regulation can help the European insurance sector remain globally competitive.

The trend towards an increased digitalisation of the insurance sector is expected to progressively continue in the years to come. In this process, EIOPA will continue to support the supervisory community and the industry to mitigate the risks and seize the opportunities of the digital transformation, including by further promoting a data-driven culture. This is indeed one of EIOPA's key priorities, as recently published in our Digital Strategy.

In implementing the strategy, EIOPA will consider the best interest of consumers first, adopting a technology neutral approach. EIOPA also aims to be flexible to keep pace with innovation, without compromising its mission. EIOPA's role will range from monitoring developments, facilitating and promoting innovation, contributing to digitalisation of National Supervisory Authorities and implementing its own digital transformation.

MARIA TSANI

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Financial regulation and supervision in an evolving digital environment

In recent years digitalization has changed the face of the financial sector, from the way we bank on a daily basis to the emergence of crypto assets and many other use cases. The digital transformation has undoubtedly brought considerable opportunities in terms of enhancing the customer experience, enhanced resilience and security. Thanks to technologies such as cloud services, financial institutions can improve their security and ability to meet compliance requirements, including on resilience, data protection and confidentiality, while also allowing them to innovate faster. At the same time, the regulatory community is grappling with new challenges arising from emerging market dynamics and the entrance of new players. Such a sea change requires authorities and supervisors to significantly rethink their approaches and even the way they operate.

As regulators turn increased scrutiny on cyber resilience, there is understandable focus on the use of cloud by financial entities. This has materialized in the EU with the Digital Operational Resilience Act (DORA), in the UK with the Critical Third Party (CTP) regime, and in other regions as well with a number of emerging initiatives. Novel challenges require novel solutions. In this context, we must apply digital-era thinking and supervisory approaches in an evolving digital system to deliver a satisfactory and effective response.

In the EU, DORA represents an opportunity for the EU to raise the bar in terms of security and resiliency. In order for the framework to be effective, it should prioritize what is important in terms of security and resiliency, and use this to proportionately protect financial organizations. It is also important that, given the fast pace of technological innovation, the framework remains flexible enough in order to handle dynamic complexities and the evolving technology environment.

Technologies like cloud, artificial intelligence and machine learning are central to how financial firms will drive innovation and global competitiveness in the future. The EU's regulatory framework will need to be suitably flexible in order to accommodate the fast changing technology landscape, and ensure firms can continue to access world class technology platforms.

From the perspective of a technology provider, we have different experiences to those of firms traditionally under the remit of financial supervisors. For example, AWS provides services to firms not only in the financial space, but in many others as well as to governments. In this sense, a tailored approach to regulation and supervision that considers these different realities would be not only more efficient, but also lead to better outcomes in managing risks. Furthermore, given the global nature of cloud operations, any approach must entail global regulatory and supervisory coordination, as recognized internationally by the Financial Stability Board (FSB).

Operational resilience and security have been rightly identified by the regulatory community as key policy concerns of the digital age. Well implemented, cloud can deliver significant resiliency gains for firms and the overall financial system. Equally, the ability of our customers to leverage our cybersecurity capabilities means a significantly higher level of encryption than legacy technology, leading to watertight security.

It is imperative we collectively get digital operational resilience right.

Digitalization has not only impacted regulatory and supervisory priorities, but has also introduced new tools to better address them. Key to supervision in the digital age is the effective use of data, and we see supervisors are increasingly enhancing their data infrastructure and leveraging advanced analytical techniques harnessing the power of the cloud. As a key enabler of supervisory technology (SupTech), cloud services allow regulators to access and deploy cutting-edge tools, such as AI, to oversee the financial system in a more efficient and secure way.

As the financial sector becomes increasingly digitalized, it is imperative we collectively get digital operational resilience right.

At AWS, we want to be an active and collaborative partner in discussions in how to achieve the robust baseline of cyber resilience we need. This is an objective we certainly share with the regulatory community.

JOE HENEGHAN
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Europe's Digital Single Market needs a revolution

Europe stands out as a market with forward-looking regulation that promotes innovation and competition. Regulatory initiatives, such as Open Banking and Open Finance, play a pivotal role in the growth of the digital finance sector. Setting regulatory frameworks for newly emerging areas, such as crypto, and embracing new technologies such as AI also impact the attractiveness of the EU as a market with clearly defined rules, regulatory clarity, and a focus on promoting new developments.

If we look at some of the most widely used metrics to assess the level of digitalization (market capitalization/revenues of FinTechs, use of digital payments versus cash, and the number of FinTechs founded), Europe is holding the top positions and is expected to maintain this status.

At the same time, there are also lessons to be learned from how digitalization is happening in competitive markets. Taking China as an example, the Asia-Pacific regional leader, we see its strong position in the digital space attributed to BigTech giants (Tencent and Alibaba) driving the FinTech revolution. They control e-commerce and social platforms while venturing into the financial services space. Using big data from users' interactions with platforms helped them scale and adopt tailored solutions for customers. This demonstrates the benefits of Open Data economies, which can boost European GDP in 2030 from about 1 to 1.5 percent[1].

The second market, relevant for the EU, is the US, generally defined as the most developed innovation ecosystem involving venture capital firms, entrepreneurs, and access to funding. The US has successfully fostered an ecosystem that encourages financial support for innovative ventures, enabling them to flourish and contribute significantly to economic development. Europe has made major progress since 2016 when venture capital investment amounted to €6.5 billion compared to €39.4 billion in the US[2]. Nevertheless, by taking the example of the US, the EU can further promote its Capital Markets Union and access to finance for digital companies.

Closing the gaps and bringing Europe to the forefront of digitalization should be one of the priorities for the next political cycle and a key component here is the EU's truly Single Digital Market, allowing seamless access for companies to almost 500 million European citizens. It can bring Europe to the next level of the digital revolution and advance its competitive edge against other big markets, such as China and the US.

As a pan-European champion with over 20 million users in Europe, we have good insights into the barriers to the Single Digital Market, namely: (1) IBAN discrimination; (2) different implementation of rules across Europe; and (3) the lack of pan-European solutions. While some of the above issues might be solved via new rules and policies, such as new harmonised frameworks, the heavy lifting is on enforcement and single procedures and practices.

For almost 10 years now, there has been no market where one European IBAN has been accepted across all countries with no obstacles. It is a question for the next European Commission's term whether additional means to enforcement are needed, such as a single European IBAN number or allowing payment service providers to receive an IBAN without the need to open a branch.

Our hope is that Europe takes the opportunity to deliver a truly Single European Digital Market.

Having operations across Europe as well as launching branches of our bank in four countries, we see how every country is unique in its approaches and market practices. The price we are paying is the absence of the Single Digital Market.

Lastly, simple tools like data sharing schemes or more sophisticated tools such as a pan-European payments solution could bring immense benefits to the effectiveness of the financial system and allow citizens to benefit from a secure and uninterrupted experiences as consumers move around Europe.

Our hope is that Europe takes the opportunity to deliver a truly Single European Digital Market, enabling seamless interoperability, and driving the continent's digital finance ecosystem to new heights.

1. *https://www.mckinsey.com/industries/financial-services/our-insights/financial-data-unbound-the-value-of-open-data-for-individuals-and-institutions*
2. *VentureEU: Pan-European Venture Capital Funds-of-Funds Programme: https://ec.europa.eu/commission/presscorner/detail/en/MEMO_18_2764*

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Towards a stronger EU leadership in digital finance

The digital transformation of the financial sector has accelerated during the pandemic and continues to be fostered by emerging technologies and changes in customers' expectations. Digital finance is key, as it contributes to the overall transformation of the economy, which is paramount to find new opportunities for growth and development.

With the rise of fintech startups and tech giants, the financial sector faces increased competition through new models of collaboration and innovation, which are based on an open architecture available to external parties. For instance, Bank as a Platform (BAAP) allows customers to benefit from an enriched banking offer, and Bank as a Service (BAAS) provides core banking services via third parties.

The core challenge for digital regulation is to organize and accelerate this natural evolution of the market without undermining the EU's overall competitiveness, the safety of customers, and the stability of the financial sector. And this all depends on how it is designed and implemented.

The EU digital transition being a key priority for the current Commission, an impressive number of new regulations has already been implemented, while many are still under negotiation. The scope of these regulations covers, among others, crypto assets, digital resilience in financial institutions, digital identity, digital platforms, artificial intelligence, blockchains, payments and most recently Open Finance.

Even if we naturally support the priorities of the European Commission's Digital Finance strategy, one of the key questions is whether these numerous regulations will really support the market transformation and not have the unintended consequence to hinder competition.

For instance, we appreciate that the proposal for a Regulation on a framework for Financial Data Access (FIDA) is built around some key principles: a contractual approach between stakeholders for sharing responsibilities and costs, the development of tools to give customers meaningful and effective control over their financial data, and the eligibility rules to make sure that all data intermediaries are subject to authorization and supervision. These principles are important to ensure the level playing field and to secure data sharing while building trust in the ecosystem.

However, we have some concerns regarding both the level of ambition of some provisions and the vagueness of others. FIDA could also have consequences in the competitiveness landscape as it does not provide for any cross-sectoral reciprocity provision and does not prevent "gatekeepers" from accessing data. It could also have an impact on the voluntary ecosystems spontaneously developed by the market.

The cumulative impact for retail banks of various regulatory packages, including FIDA, PSD3 / PSR, the Retail Investment Strategy, and the Digital Euro proposals is also a major concern for us. These regulatory changes could trigger major challenges for retail banks' business model, whose core pillars are both mutualization (universal banks serve all kind of clients) and granularity (universal banks serve all geographical areas).

The Commission must now focus on consolidating the existing digital regulation.

After a period of intense regulatory activity, the next European Commission should, therefore, focus on consolidating existing regulations and ensuring that they are properly enforced rather than introducing new regulations that may weaken both the competitiveness and profitability of EU financial institutions.

It will be, for example, specifically important to finalize the Level 2 regulation on DORA, MICA, and the soon-to-be-voted IA act to avoid regulatory uncertainty and to allow for a harmonized implementation. The proper implementation of the EU digital identity wallet will also be key, as it will be essential in many digital finance customer journeys. And finally, Europe must not get its Open Finance framework wrong either: the framework is not implementable as it is and should be deeply reviewed.

Boosting European competitiveness should be the top priority for the incoming European mandate. In that perspective, we strongly support Ursula Von der Leyen 's decision to ask Mario Draghi to prepare a report on the future of European competitiveness, with proposals to revitalise the European Union's economy in the face of competition from China and the United States.