**ECSDA RESPONSE TO THE**

**EUROPEAN COMMISSION CONSULTATION ON DIGITAL FINANCE STRATEGY**

*Please note that the consultation is in the form of a survey. Below are the questions, the related Commission’s considerations and the responses to the questions which ECSDA found relevant for it to respond to.*

*ECSDA responses are provided in a light blue format.*

**General Questions**

**Question 1.**

What are the main obstacles to fully reap the opportunities of innovative technologies in the European financial sector (please mention no more than 4)?

Please also take into account the analysis of the expert group on Regulatory Obstacles to Financial Innovation in that respect.

**ECSDA Response**

Increased control from authorities and increased prescriptive requirements imposed by laws and regulations upon the financial institutions (in order for authorities to obtain indirect control over the technology providers) are hindering the smooth development and use of new technologies within the financial industry.

New technologies create new challenges and risks, which need to be mitigated. The European financial sector would benefit from measures that are principle-based rather than being too prescriptive.

**Fragmentation among Member States:** A lack of harmonization as well as ‘gold-plating’ regarding the regulatory framework especially regarding the use of new technologies (e.g. DLT/Blockchain) makes cross-border activities very difficult today. One solution would be targeted legislative changes in existing EU regulations to allow for a harmonized use of new technologies, based on common standards.

**Legal uncertainty:** As some of the financial markets’ regulations are not covering the technical aspects in detail, it is sometimes unclear whether it is possible to make use of a new technology (e.g. outsourcing rules use against the background of cloud technology). Therefore, we are in favour of target changes of existing regulation, as market participants and competent authorities are already familiar to these rules. Until then, guidance is helpful, as long there is no legislative framework in place as it could reflect recent developments within existing rules and regulations. This would help market participants, as it shortens time to markets for services and products.

**Problems /risks of the current cloud market**: Asymmetry of power of negotiation between customer and CSPs, i.e. high efforts and time are required to agree on regulatory compliant contracts with CSPs in the financial sector. Therefore, we actively support the EU´s work designing Voluntary Standard Contract Clauses to facilitate future negotiations. Also, it is very difficult to procure and adopt new and innovative cloud solutions, as it takes a long time to ensure that these new services are regulatory compliant. Often, new solutions are not meeting regulatory expectations right from the start.

The outsourcing activity, in which cloud-based services are often included, is already subject to extensive regulatory requirements for financial institutions. Even though the recently issued EBA guidelines have brought some clarity, definitions or qualifications, the area remains very unclear.

The fact that financial institutions are sometimes not in a position to impose such requirements on cloud service providers, also limits the usage of the cloud technology within the industry.

# Ensuring a technology-neutral and innovation friendly EU financial services regulatory framework

**Question 4.**

Do you consider the existing EU financial services regulatory framework to be technology neutral and innovation friendly?

**Yes**  
No  
Don’t know / no opinion / not relevant

**Question 4.1**

If not, please provide specific examples of provisions and requirements that are not technologically neutral or hinder innovation:

**ECSDA Response**

The EU financial services regulatory framework does not impose or prohibit the use of a certain technology. In that sense, it is technology-neutral. However, certain regulatory concepts may benefit

from clarification in the context of a new technology (e.g. how to apply the MiFID conduct of business rules in respect of robo-advice, how to apply requirements applicable to a designated and licensed entity in a distributed environment (DLT)?). Moreover, the use of a new technology may require an additional layer of regulation. For example, the use of AI (and their ‘black box algorithms’) seems to require legal intervention to enable the allocation of liability and the enforcement of certain (ethical) standards and to clarify certain GDPR provisions (such as the requirement to explain how and why personal data are processed by the algorithm – which is not always straight-forward in practice in respect of certain algorithms).

From our point of view, a technology-neutral approach as an overarching principle is very important, as regulation should be independent of the used technology. However, not all of these challenges can be tackled by ensuring the principle of tech-neutrality, but have to be addressed technology-specific, as every technology mentioned presents its own challenges:

1. Cloud: outsourcing of material functions, proper risk management, clarity of the liabilities on both sides and currently missing standard contract clauses to facilitate the burdensome negotiations of compliant contracts with CSPs, especially for small / mid-sized institutions as well as a missing appropriate overarching oversight paradigm for CSPs, given the increasing importance of their services for companies in different sectors, etc.

2. Big data / AI: quality, and source and ownership of data, data protection and data sovereignty as well as ethical questions (e.g. reconciliation of decisions, biases)

3. DLT/blockchain: liability and accountability in public permissionless chains, and smart contracts, material outsourcing considerations data protection and new IT-risks. With regard to the existing framework, we find the third example in the realm of DLT/Blockchain very important, where the principle of tech-neutrality should be upheld.

We think that regulators should treat the technology, as any other IT system, based on the principle ‘same business, same risk, same rules’ regarding its use and connected risks. Further, regulators should focus especially on the ‘records’ maintained in this environment, as they could be digital representations of different forms of assets, used in the financial industry. From our point of view, these digital or crypto-assets should be treated in a ‘substance-over-form’ approach. This means that if for example, they fulfill the criteria of a financial instrument in accordance with the current regulatory framework, they should be treated as such. The current regulatory framework is widely in accordance with tech-neutrality and, therefore, applicable. If digital or crypto-assets represent a currently existing financial instruments (e.g. shares, commodities etc.), then they should adhere to the existing regulatory framework (MiFID II/EMIR/CSDR etc.), again following the ‘same business, same risk, same rules’ approach.

However, MiFID II must clarify as to which digital assets fall under the scope of financial instruments (as stipulated in Annex I of MiFID II Section C), to reflect these new assets. To this end and in order to ensure tech-neutrality further a number of other, existing regulatory requirements to financial instruments should be also applicable (e.g. MiFID II, EMD, MAR, SSR, Prospectus, CSDR, SFD, FCD, EMIR, UCITS, AIFMD).

**Question 6.**

In your opinion, is the use for financial services of the new technologies listed below limited due to obstacles stemming from the EU financial services regulatory framework or other EU level regulatory requirements that also apply to financial services providers?

Please rate each proposal from 1 to 5:

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
|  | 1 (irrelevant) | 2  (rather not relevant) | 3 (neutral) | 4  (rather relevant) | 5  (fully relevant) | N. A. |
| Distributed Ledger Technology (except crypto- assets) |  | **X** |  |  |  |  |
| Cloud computing |  |  |  | **X** |  |  |
| Artificial Intelligence/Machine learning |  |  | **X** |  |  |  |
| Internet Of Things (IoT) |  |  |  |  |  |  |
| Biometrics |  |  |  |  |  |  |
| Quantum computing |  |  |  |  |  |  |
| Other |  |  |  |  |  |  |

**Question 6.1**

Please explain your answer to question 6, specify the specific provisions and legislation you are referring to and indicate your views on how it should be addressed:

**ECSDA Response**

The existing EU financial services regulatory framework does not preclude the use of DLT in general, but it does not fit well with public permissionless DLT networks, because it always designates a central entity as being subject to a licensing requirement and responsible for meeting legal requirements. In the financial sector, there are good reasons to take such an approach. More specifically, the policy objectives of financial services regulation (investor protection, market integrity and financial stability) require a certain degree of central governance and operation of the relevant technology.

The existing EU financial services regulatory framework does not preclude the use of AI, but it could be deemed as insufficient to cover all risks related to AI (e.g. liability, data protection, etc.).

See also comment on cloud computing in Q1.

**Question 7.**

Building on your experience, what are the best ways (regulatory and non-regulatory measures) for the EU to support the uptake of nascent technologies and business models relying on them while also mitigating the risks they may pose?

Please rate each proposal from 1 to 5:

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
|  | 1 | 2 | 3 | 4 | 5 | N.A. |
| Setting up dedicated observatories to monitor technological and market trends (e.g. EU Blockchain Observatory & Forum; Platform Observatory) |  |  | **X** |  |  |  |
| Funding experimentation on certain applications of new technologies in finance (e.g blockchain use cases) |  |  | **X** |  |  |  |
| Promoting supervisory innovation hubs and sandboxes |  |  | **X** |  |  |  |
| Supporting industry codes of conduct on certain applications of new technologies in finance |  |  |  | **X** |  |  |
| Enhancing legal clarity through guidance at EU level for specific technologies and/or use cases |  |  |  |  | **X** |  |
| Creating bespoke EU regimes adapted to nascent markets, possibly on a temporary basis |  |  | **X** |  |  |  |
| Other |  |  |  |  |  |  |

**II. Removing fragmentation in the single market for digital financial services**

**Make it easier for firms to carry out technology pilots and scale up across the Single Market**

**Question 21.**

In your opinion, how could the relevant EU authorities enhance coordination among different schemes in the EU?

Please rate each proposal from 1 to 5:

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
|  | 1  (irrelevant) | 2  (rather not relevant) | 3  (neutral) | 4  (rather relevant) | 5  (fully relevant) | N.A. |
| Promote convergence among national authorities in setting up innovation hubs and sandboxes, through additional best practices or guidelines |  |  |  | **X** |  |  |
| Facilitate the possibility for firms to test new products and activities for marketing in several Member States (“cross border testing”) |  |  |  | **X** |  |  |
| Raise awareness among industry stakeholders |  |  |  | **X** |  |  |
| Ensure closer coordination with authorities beyond the financial sector (e.g. data and consumer protection authorities) |  |  |  | **X** |  |  |
| Promote the establishment of innovation hubs or sandboxes with a specific focus (e.g. a specific technology like Blockchain or a specific purpose like sustainable finance) |  |  | **X** |  |  |  |
| Other |  |  |  |  |  |  |

**Question 22.**

In the EU, regulated financial services providers can scale up across the Single Market thanks to adequate licenses and passporting rights.

Do you see the need to extend the existing EU licenses passporting rights to further areas (e.g. lending) in order to support the uptake of digital finance in the EU?

**ECSDA Response**

Yes, all regulated financial service providers should be able to benefit from an EU passport. Hence, from our point of view, the existing EU licenses passporting rights should be extended to the area of the crypto custodian business, as they also should be regulated. However, this would require EU wide harmonized rules.

**III. Promote a well-regulated data-driven financial sector**

**Consent-based access to personal data and data sharing in the financial sector**

**Question 29.**

In your opinion, under what conditions would consumers favor sharing their data relevant to financial services with other financial services providers in order to get better offers for financial products and services?

**ECSDA Response**

Consumer’s concern is about the flow of its own personal data. Often the data subject is not entirely aware of all the financial institutions processing its personal data. It is advisable to a clear view on this, in line with the transparency principle. Only if well and constantly informed, the data subject may express a valid and broader consent to the sharing of its personal data.

**Question 30.**

In your opinion, what could be the main benefits of implementing an open finance policy in the EU?

Please rate each proposal from 1 to 5:

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
|  | 1  (irrelevant) | 2  (rather not relevant) | 3  (neutral) | 4  (rather relevant) | 5  (fully relevant) | N.A. |
| More innovative and convenient services for consumers/investors, e.g. aggregators, comparison, switching tools |  |  | **X** |  |  |  |
| Cheaper traditional services for consumers/investors |  |  | **X** |  |  |  |
| Efficiencies for the industry by making processes more automated (e.g. suitability test for investment services) |  |  |  | **X** |  |  |
| Business opportunities for new entrants in the financial industry |  |  |  | **X** |  |  |
| New opportunities for incumbent financial services firms, including through partnerships with innovative start-ups |  |  |  |  |  |  |
| Easier access to bigger sets of data, hence facilitating development of data dependent services |  |  |  | **X** |  |  |
| Enhanced access to European capital markets for retail investors |  |  |  |  |  |  |
| Enhanced access to credit for small businesses |  |  |  |  |  |  |
| Other |  |  |  |  |  |  |

**Question 31.**

In your opinion, what could be the main risks of implementing an open finance policy in the EU?

Please rate each proposal from 1 to 5:

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
|  | 1  (irrelevant) | 2  (rather not relevant) | 3  (neutral) | 4  (rather relevant) | 5  (fully relevant) | N.A. |
| Privacy issues / security of personal data |  |  |  | **X** |  |  |
| Financial exclusion |  |  |  |  |  |  |
| Poor consumer outcomes (e.g. unfair pricing strategies) |  |  |  |  |  |  |
| Misuse of consumers’ financial data |  |  |  |  |  |  |
| Business confidentiality issues |  |  |  | **X** |  |  |
| Increased cyber risks |  |  | **X** |  |  |  |
| Lack of level playing field in terms of access to data across financial sector activities |  |  |  |  |  |  |
| Other |  |  |  |  |  |  |

If you see other risks of implementing an open finance policy in the EU, please specify and explain:

**ECSDA Response**

One additional concern is touching upon the trust of consumers and clients regarding the safety of their data:

As it stands, if an open finance policy would be implemented, currently most of the collected/used data would be processed by non-EU CSP´s, which do not necessarily respect EU laws. Therefore, if an open finance policy would be implemented, guidance on this issue would be welcomed in order to create certainty among market participants.

**Question 32.**

In your opinion, what safeguards would be necessary to mitigate these risks?

**ECSDA Response**

Clear guidance for companies based on existing rules would be beneficial. Further, there is a clear need for EU rules covering cloud outsourcing, which on the one hand promote the uptake of the technology to make the financial industry more competitive and on the other hand incorporates existing standards, which are already used by the industry.

It would be also important to be transparent about the allowed purposes for the use of the data and set up specific limitations. Moreover, every data subject should be constantly able to get information about the data flow relevant to own data.

**Question 34.**

What specific data (personal and non-personal) would you find most relevant when developing open finance services based on customer consent?

To what extent would you also consider relevant data generated by other services or products (energy, retail, transport, social media, e-commerce, etc.) to the extent they are relevant to financial services and customers consent to their use?

Please explain your reasoning and provide the example per sector:

**ECSDA Response**

The personal data included in the financial transactions are already governed by specific regulations identifying scope, principles and obligations. It is important to reduce the publicly available data to the minimum necessary elements in order to avoid any misuse and any potential damage to the related data subject. Attention should be also put on the data flow and on the data traceability.

The consent given for a specific sector should remain applicable only to that specific sector. Otherwise, there might be an increased risk to lose traceability of the data itself and to nullify the initial value of the consent.

The use of non-personal data is already now wider than the one for the personal data.

Furthermore, it has yet to be defined what ‘personal data’ exactly means. For example, would a business email address of a company A used to request a service from another company B be considered personal? If so, would company B be allowed to use this information only with the consent of company A? If so, this would require two different databases, according to the GDPR. This could be circumvented with an onboarding process, including an opt-in solution for clients.

In the context of B2B, we think that energy data would be interesting. But if businesses are grounded within two sectors (e.g. energy and finance), they have to comply with different requirements from different regulators, which could increase complexity with regard to data sharing.

**Question 35.**

Which elements should be considered to implement an open finance policy?

Please rate each proposal from 1 to 5:

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
|  | 1  (irrelevant) | 2  (rather not relevant) | 3  (neutral) | 4  (rather relevant) | 5  (fully relevant) | N.A. |
| Standardisation of data, data formats |  |  |  |  |  |  |
| Clarity on the entities covered, including potential thresholds |  |  |  |  |  |  |
| Clarity on the way data can be technically accessed including whether data is shared in real- time (e.g. standardised APIs) |  |  |  | **X** |  |  |
| Clarity on how to ensure full compliance with GDPR and e- Privacy Directive requirements and need to ensure that data subjects remain in full control of their personal data |  |  |  |  | **X** |  |
| Clarity on the terms and conditions under which data can be shared between financial services providers (e. g. fees) |  |  |  |  | **X** |  |
| Interoperability across sectors |  |  |  | **X** |  |  |
| Clarity on the way data shared will be used |  |  |  |  | **X** |  |
| Introduction of mandatory data sharing beyond PSD2 in the framework of EU regulatory regime |  |  |  |  |  |  |
| If mandatory data sharing is considered, making data available free of cost for the recipient |  | **X** |  |  |  |  |
| Other |  |  |  |  |  |  |

**Support the uptake of Artificial intelligence in finance**

**Question 39.**

In your opinion, what are the main challenges or risks that the increased use of AI- based models is likely to raise for the financial industry, for customers/investors, for businesses and for the supervisory authorities?

Please rate each proposal from 1 to 5:

1. **Financial industry**

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
|  | 1  (irrelevant) | 2  (rather not relevant) | 3  (neutral) | 4  (rather relevant) | 5  (fully relevant) | N.A. |
| 1.1. Lack of legal clarity on certain horizontal EU rules |  |  |  |  |  |  |
| 1.2. Lack of legal clarity on certain sector-specific EU rules |  |  |  |  |  |  |
| 1.3. Lack of skills to develop such models |  |  |  |  |  |  |
| 1.4. Lack of understanding from and oversight by the supervisory authorities |  |  |  |  |  |  |
| 1.5. Concentration risks |  |  |  |  |  |  |
| 1.6. Other |  |  |  |  |  |  |

Please specify what other main challenge(s) or risk(s) the increased use of AI- based models is likely to raise for the financial industry:

**ECSDA Response**

There is a need for an efficient certification process, to enhance innovation.

We support a certification of high-risk AI applications. Further, for non-high-risk AI applications it should be allowed for companies to receive a voluntary certification. We prefer an official harmonized labelling system for both applications with clear requirements and an official certification process performed by a formally authorized actor. This service could be offered by a public authority directly or by a private institution with a public permission on behalf of public authorities.

**Risk Assessment:** In general, any AI application must have clear and well-designed rules & objectives to minimize the associated risks. *High-risk AI applications*: A combination of ex-ante assessments, based on an external conformity procedure, as well as ex-post market surveillance, would be useful. *Non-high-risk AI applications*: A combination of ex-ante assessments, based on a self-assessment, as well as ex-post market surveillance, would be useful. In cases where ex-ante assessments are difficult, more ex-post assessments are needed. Either way, it is crucial that the necessary capacities are in place to assess the AI, to ensure the efficiency to support the launch of AI products.

**2. Consumers/investors**

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
|  | 1  (irrelevant) | 2  (rather not relevant) | 3  (neutral) | 4  (rather relevant) | 5  (fully relevant) | N.A. |
| 2.1. Lack of awareness on the use of an algorithm |  |  |  |  |  |  |
| 2.2. Lack of transparency on how the outcome has been produced |  |  |  |  |  |  |
| 2.3. Lack of understanding on how the outcome has been produced |  |  |  |  |  |  |
| 2.4. Difficult to challenge a specific outcome |  |  |  |  |  |  |
| 2.5. Biases and/or exploitative profiling |  |  |  |  |  |  |
| 2.6. Financial exclusion |  |  |  |  |  |  |
| 2.7. Algorithm-based behavioural manipulation (e.g. collusion and other coordinated firm behaviour) |  |  |  |  |  |  |
| 2.8. Loss of privacy |  |  |  |  |  |  |
| 2.9. Other |  |  |  |  |  |  |

**3. Supervisory authorities**

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
|  | 1  (irrelevant) | 2  (rather not relevant) | 3  (neutral) | 4  (rather relevant) | 5  (fully relevant) | N.A. |
| 3.1. Lack of expertise in understanding more complex AI-based models used by the supervised entities |  |  |  |  |  |  |
| 3.2. Lack of clarity in explainability requirements, which may lead to reject these models |  |  |  |  |  |  |
| 3.3. Lack of adequate coordination with other authorities (e.g. data protection |  |  |  |  |  |  |
| 3.4. Biases |  |  |  |  |  |  |
| 3.5. Other |  |  |  |  |  |  |

Please specify what other main challenge(s) or risk(s) the increased use of AI-based models is likely to raise for the supervisory authorities:

**ECSDA Response**

In order to achieve a successful use of, we are in favour to build upon already existing rules and regulations in general. Not only would this create certainty amongst market participants but would it also be more efficient for supervisory authorities. In general, it might be useful to ask whether a completely new and, therefore, unregulated task is performed by an AI application, in contrast to an already known and, therefore, regulated task. In the latter case, adjustments to the existing framework might be sufficient. For example, if a company can prove that it fulfilled all requirements, it should not be held liable because of negligence. Notwithstanding a human or an AI application caused the accident.

Within the context of the approval of new AI applications, it is important to differentiate between AI applications operating in ‘open systems’ (e.g. road traffic) or ‘closed systems’ (e.g. playing chess) from a regulatory perspective. In ‘open systems’, the AI will never be able to cover all eventualities, as the training data is always limited. Here humans must make the final decision. This is also true for high-risk AI applications in ‘closed systems’. Additionally, as an ex-ante risk assessment is not fully possible for every AI application, a distinction between ‘self-learning’ and ‘release-based’ might be useful. In the case of ‘self-learning’ AI applications, again, a focus on ex-post control mechanisms seems beneficial. Therefore, regular reviews and potential re-training ‘check-points’ might be established in the process, this is especially necessary for ‘self-learning’ AI applications (see the controversy around the chatterbots in 2016).

**Question 40.**

In your opinion, what are the best ways to address these new issues?

Please rate each proposal from 1 to 5

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
|  | 1  (irrelevant) | 2  (rather not relevant) | 3  (neutral) | 4  (rather relevant) | 5  (fully relevant) | N.A. |
| New EU rules on AI at horizontal level |  |  | **X** |  |  |  |
| New EU rules on AI for the financial sector |  | **X** |  |  |  |  |
| Guidance at EU level for the financial sector |  |  |  | **X** |  |  |
| Experimentation on specific AI applications under the control of competent authorities |  |  |  | **X** |  |  |
| Certification of AI systems |  |  |  | **X** |  |  |
| Auditing of AI systems |  |  | **X** |  |  |  |
| Registration with and access to AI systems for relevant supervisory authorities |  |  |  | **X** |  |  |
| Other |  |  |  |  |  |  |