

## **ANNEX – HSBC Summary Response to The European Commission Consultation on A New Digital Finance Strategy for Europe / Fintech Action Plan**

HSBC welcomes the opportunity to provide a submission to the European Commission's consultation on, 'A New Digital Finance Strategy for Europe/ FinTech Action Plan' ('the Consultation'). The HSBC Group is one of the world's largest banking and financial services organisations. Headquartered in London, HSBC operates through an international network of around 3000 offices in 65 countries and territories in Europe, Asia, the Middle East and Africa, North America and Latin America. We serve more than 39 million customers worldwide through three global businesses: Wealth and Personal Banking, Commercial Banking and Global Banking and Markets.

The Consultation is an important and positive step towards deepening the European Single Market for digital financial services. The Commission's 2018 FinTech Action Plan and a series of horizontal policies have helped to encourage the digitisation of the industry. To ensure the continued competitiveness of Europe, the Digital Finance Strategy must build upon and accelerate this digital transformation by enabling the scaling up of innovative technologies within robust regulatory foundations.

HSBC is supportive of the Commission's three priority areas as set out in the Consultation (and the four overall) and believes that the right developments in these areas will help to further support innovation within a balanced, accommodative regulatory framework. It will be important for the new FinTech Action Plan to outline a clear, consistent and compelling strategy for the digital transformation of financial services, and how it fits within the horizontal EU Digital Strategy. There are multiple initiatives currently underway, including the Data Strategy, the AI White Paper, an EU framework for Cryptoassets and proposals for Cloud and broader Digital Operational Resilience. **We recommend the Commission develop a clear roadmap and set of targeted actions, showing how these and other relevant initiatives will interact with and complement each other. This will provide firms with greater clarity and reduce the potential for duplication and overlap.**

### **Fundamental principles**

The global nature of technology, the breadth of application and the speed of developments presents challenges for both the industry and policy makers when examining appropriate regulatory frameworks. These and other factors have led to regulatory fragmentation, both between the EU and other countries and also within the EU itself.

As the Commission prepares its new FinTech Action Plan, we outline a set of fundamental principles that should always be applied in order to promote innovation while ensuring adequate protections:

- **Balancing regulation with innovation** – existing legislation provides a robust regulatory framework for the development of technology in financial services. Policies should combine a clear assessment of risks with the opportunities offered by different technologies. We encourage the Commission and supervisory authorities to continue to work with the industry to help foster further collaboration between incumbents, new entrants, policy makers and regulators.
- **Ensure principles-based regulation** – regulatory frameworks should be forward-looking, technology neutral and holistic, include a realistic assessment of gaps in current regulation, and ensure that the same activities entailing the same risks are regulated in the same manner. They should not only address prudential concerns but also areas such as conduct, privacy and data protection, consumer protection, cyber security, market integrity and financial stability. This will continue to encourage innovation and competition while preventing a two-tier approach to regulation, ensuring a more flexible and proportionate regulatory regime.

- **Harmonise regulation globally** – financial technology solutions will require globally harmonised regulation and interoperable standards to reach scale, requiring cross-border regulatory collaboration. This will help to reinforce a consistent regulatory approach, balancing innovation and competition with security and stability. The Commission should work with industry, regulatory authorities and national governments to develop clear, consistent regulatory frameworks at both an EU and global levels.
- **Harmonised implementation of EU regulations** – harmonised regulation across the EU is essential to ensure better solutions for customers and greater efficiency and resilience for firms. As reviews of regulations such as the Network and Information Security Directive (NISD), the General Data Protection Directive (GDPR) and the Payment Services Directive II (PSDII) continue, it will be important to identify where harmonisation across the region can be improved.
- **Establish end-user trust** – end-users, particularly consumers, will ultimately determine the success of any particular technology. Industry and policy makers should collaborate on increasing trust through awareness and education, but also through mechanisms that secure this trust, including authentication, accreditation and assessments of resilience and security. This will be particularly important for open API schemes such as PSD2 and also cross-industry data mobility.

#### **Key messages and recommendations**

We have been active contributors to and are supportive of industry responses to the consultation. HSBC's response is intended to complement these submissions. While we have provided answers to questions in the strategy, for ease of reference we provide below key messages and recommendations under each of the three Commission priority areas:

#### **1. Ensuring a technology-neutral and innovation friendly EU financial services regulatory framework (questions 4-14)**

- **Technology neutral regulatory framework (questions 1; 4-6)**  
The European Commission and other European authorities have put considerable efforts towards ensuring a technology-neutral approach to regulation. On the whole, we believe that this has been successful. As identified by the Expert Group on Regulatory Obstacles to Financial Innovation (ROFIEG) report, there are still areas that would benefit from review in this regard, particularly the prudential perimeter and access to, processing and sharing of data. There are also areas that would benefit from greater clarity and guidance, particularly around the use of AI, Cloud and Data. **We recommend the Commission conducts a thorough review of relevant regulation, now and on a regular basis, to accelerate the safe deployment of innovative technologies in financial services.**
- **Consumer impact (question 2)**  
Coupled with arguably the most mature consumer and data protection frameworks in the world, an accommodative regulatory regime has enabled the growth of technology driven services, products and business models that have improved access, choice and personalisation. Achieving high levels of consumer trust will be key to further success. **This will require even greater commitment from the Commission and the ESAs to activities-based regulation, particularly as non-bank firms increase their market shares.**
- **Prudential regulation and the new financial ecosystem (questions 8-12)**  
The consultation outlines a number of risks associated with non-financial players increasingly offering financial products and services – including large technology platforms – whilst subject

to lighter-touch regulation and supervision than firms with full banking licenses. These are also identified in the ROFIEG report. Payments is where the greatest developments have occurred, but non-financial services firms are also offering a number of other (mainly retail) banking products and services. Along with bank disintermediation, the growth of new market entrants brings with it a myriad of other potential risks, including operational, credit, consumer and investor protection, liquidity and systemic concerns. **We recommend that the Commission and the ESAs undertake a full analysis of how the proper application of technology-neutral, activities-based financial and non-financial regulation should be adapted to provide appropriate risk mitigation while still encouraging innovation and fair competition.**

- **Enhancing cooperation between authorities (questions 13-14)**

The growth in the use of new technologies and of non-financial players within financial services raises a number of key challenges for authorities. These include inadequate supervisory powers, inconsistent application of regulation across the EU and insufficient cooperation between financial, data protection and competition bodies. **In addition to regular regulatory reviews, we recommend the Commission and the ESAs establish a formal cooperation framework/network to increase regulatory harmonisation, collaboration and information sharing.**

## **2. Removing fragmentation in the single market for digital financial services (Questions 15-25)**

- **Digital Financial Identities (questions 16-19)**

For Digital Identity to achieve its full potential, regulation needs to be harmonised. In the EU, implementation of KYC rules under AML legislation must be harmonised across the bloc, aligned with global standards. We believe that the use of technology, providing appropriate access to customer data digitally, will provide the opportunity to improve the lives of citizens, improve the ability of the Financial Services Industry to manage financial crime risk and will reduce friction in the access of citizens to banking products in the EU. Customers must remain at the centre of what we do on digital identity, and maintaining their trust as data subjects will be essential to success. **To deliver these benefits most efficiently, we recommend the Commission enables financial institutions to access directly customer data attributes via APIs and to accept liability directly for decisions, rather than relying on intermediaries.**

- **Supporting innovation (questions 20-23)**

Innovation hubs are a useful mechanism for exchanging knowledge between innovators and regulators, helping firms to better understand regulatory obligations and offering supervisors greater insight into technology and market dynamics. They are different to regulatory sandboxes, which enable closer cooperation and testing on the development of a technology business model and a useful alternative to lighter touch regulation or the introduction of 'special licenses'. **HSBC would support greater cooperation between national sandboxes and hubs, with the aim of creating a set of best practices and standards for regulators across the Single Market. This could take the form of a regulatory sandbox framework or 'hub' operated jointly by the European Commission and the European Supervisory Authorities (ESAs) in partnership with the European Forum of Innovation Facilitators.**

## **3. Promote a well-regulated data-driven financial sector (q26-47)**

- **Publicly available data (questions 27-28)**

HSBC is supportive of measures intended to facilitate greater and easier access to financial and supervisory data that firms are already mandated to make available publically. To avoid unnecessary additional obligations, it will be important that any activity takes into account existing regulatory requirements. Common, interoperable and clearly defined standards, including APIs, will be essential. **As the Commission will be aware, other jurisdictions are also exploring this area, so it will be important for international standards to be used where they exist.**

- **Personal data sharing (questions 29-35)**

HSBC supports the concept of Open Finance, though it is important to recognise that PSD2 is still new and requires a period of sustained focus on resilience. Common and secure standards are a key enabler, particularly Open APIs, and the management and funding model supporting it therefore needs early consideration. **We recommend a consumer and market-led approach, rather than regulation, to facilitate the broadest consumer and economic benefits, whilst delivering them in a commercially viable manner.**

Further development of the regulatory framework will be required, both to mitigate potential customer detriment and to act as an enabler. The development of Open Finance will also require effective institutional arrangements that command industry-wide support. **We recommend the Commission and the European Supervisory Authorities conduct an initial gap analysis, alongside encouraging industry-led innovation.**

It is essential for competition and consumer choice that Open Finance is part of a broader regulatory initiative to facilitate end-user centric, cross-industry, personal data sharing and mobility, as part of the Commission's Data Strategy. As we have seen in other markets and most recently with the current COVID-19 crisis, relevant customer data goes far beyond the Financial Services industry. End-users should be able to control and through informed consent grant access to any data they themselves generate (raw and observed) across all industries, with harmonised mechanisms, a standards and safeguards. For the full benefit to be realised, data also needs to be able to flow across borders, both within the EU and with third countries. **We recommend that the Commission uses the forthcoming Data Act to enhance Article 20 GDPR on data portability, as well as the work undertaken for PSD2 in relation to mechanisms and standards and to reinforce the importance of the free movement of data across borders.**

- **Artificial Intelligence (questions 36-40)**

AI is still at a nascent stage of development and the technology is almost continuously evolving. Overall, we believe that the EU policy and regulatory landscape remains largely supportive of AI development and deployment, although there are still challenges around interpretation of certain regulations. HSBC is committed to ensuring data is protected securely and used appropriately in line with legislation, but additional regulation may limit development and application. HSBC has developed principles for the ethical use of Big Data and AI to govern AI development in the bank globally. **We recommend DG FISMA and the European Supervisory Authorities work with the financial services industry to develop sector-specific ethical principles and guidelines to help to provide greater clarity and certainty.**

In the context of the Commission's AI White Paper, it will be important for DG FISMA to continue to communicate the specifics of the financial services industry. Highly regulated industries such as financial services have mature risk management and governance processes. Many of these are directly applicable to the use of AI and specifically tailored for the lifecycle of an application. **We recommend DG FISMA lead a gap analysis of the current regulatory**

**framework for financial services firms in relation to AI, including relevant horizontal legislation. Any gaps identified could be better addressed via targeted action, such as sector guidance, supervisory adjustments or focused legislative amendments.**

Many of the proposed ex-ante measures for 'high risk' AI in the Commission's AI White Paper are already required by financial supervisors and are part of the building, development, testing, deployment and auditing of applications within financial services firms. Labelling the sector high-risk could create duplication and possible conflicts with existing regulatory requirements. **We recommend the industry should not be designated 'high-risk', as defined in the AI White Paper, in order to encourage competition in and development of AI applications in EU financial services.**

- **RegTech (questions 41-45)**

RegTech has the potential to reduce risk and increase efficiency, transforming the way that banks manage risk and compliance requirements and improving the quality of regulatory supervision. Although the use of technology to address regulatory challenges has existed for some time, recent years have witnessed an increased focus. To make significant progress, supervisors will need to accept that a greater degree of pooling data across industry is required, as data aggregation underpins effective use of transformative technology. Central to this will be standardisation of data definitions, inputs and formats linked to a Common Input Layer. **We recommend the Commission and ESAs collaborate with the industry via an EU RegTech regulatory sandbox, building upon and linking to initiatives in third countries.**