

Fostering digital distribution and fintech innovation



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Single market still looking for Fintech push

To what extent and in which areas does EU Fintech action plan help (or not) to address both the challenges and specificities of the EU?

EU Fintech action plan was a sensible set of actions to help Europe consolidate fintech initiatives into the single market. It included many important elements – assessment on how blockchain would fit into regulation, how to organise sandboxes, a proposal to regulate crowdfunding etc. And specifically how to handle it in the complex single market universe.

However, the plan is only helpful if it also delivers decisions and actions. And on that the jury is still out as notable parts of the plan are still ‘work in progress’.

Is digital disruption helping to speeding up integration of EU markets for financial services despite existing differences in habits, languages and legal frameworks?

Yes and no. There are areas that would have not been witnessing present level of cross-border activity without these advances in technology. Like some portions of retail payment market and also certain business lines of crowdfunding.

However, more broadly the promise remains yet to be delivered. One reason is that in some elements the technology has never been the prime constraint on integration. While home bias is surely somewhat influenced by limitations on information exchange (that digital technology helps to overcome somewhat), the root cause for that seems to be deeper inside the way how business life is arranged inside Europe. Particularly in SME world. For example, the way the business transactions are arranged and recorded on country level tend to support more fragmented market. Taking advantage of technological advances could help overcome these to some extent. But for the serious change stronger socio-political will is probably needed.

Do digital initiatives taking place have a sufficient cross border dimension?

With some exception the answer is rather ‘not enough’. There are good examples in the area of main payment infrastructures that have led to reasonable cross border integration with good quality, including in retail payments. And it might be, that main initiatives on data handling and protection beyond strictly financial field are containing sufficient cross border dimension already.



>>> However, in many parts of the market which could benefit much from digital innovations the cross-border dimension remains limited. For example, blockchain innovations or crowdfunding-type businesses are promising for integrated cross-border handling of securities' transactions and company registry keeping. However, the regulatory environment is still not moving decisively to provide sufficient clarity for the market to develop and even less so to provide clear European dimension to it. True, obstacles might be complex and overcoming them unavoidably time-consuming. But that should not limit the effort.

How to describe the EU digital landscape in the financial area, compared to other geographies globally?

It is seemingly easy to say it is not EU but rather other regions (eg China or Asia-pacific) that have set the global pace on a digital economy, including in cashless payments. However, there is no absolute proof or comprehensive data, which region contributes most with regard to providing most advanced digital financial services.

An estimation of a digital landscape of a region depends on the characteristics which are set as a priority. Europe as a region is versatile but simultaneously uniform: the biggest digital innovators may not be of European origin, but consequently the general level of digitalization and innovation is relatively high. EU single market and common background of regulation could provide a unique starting point for EU technology competence and also smaller countries can play a role in the general status of the region.

EU digital landscape in the financial area is therefore full of potential. Using digital financial services and mobile banking has completely changed our understanding of banking sector and the provision of financial products. But the fact that everything is so comfortable and easy to use also includes dangers, e.g. cybersecurity threats. ●



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The EU FinTech Action Plan is celebrating its first birthday

Digital innovation has increased the pace at which the financial services world is evolving. Financial services have undergone other digital revolutions, but what is unprecedented now is the speed and scale of this transformation. Think a few years back: digital banking was already at your fingertips. Today, your customer's experience has improved, your personalised assistant or robo-advisor helps you with financial and service choices, your payments are ever faster. Tomorrow, one can expect further investments in blockchain, advanced artificial intelligence and machine learning, the Cloud and cybersecurity in the realm that we call FinTech.

Europe is well positioned to reap the fruit from the innovation that the FinTech revolution is delivering to the market. In March 2018, the EU Commission FinTech Action Plan presented a set of actions in FinTech-related sectors such as big data, cybersecurity, blockchain, crowdfunding and cryptoassets, interoperability and standardisation, along with boosting financial and IT skills while ensuring financial stability, protection of consumers and investors, and market integrity.

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>>> One year later, several EU FinTech Labs have been organised with national regulators and supervisors addressing important issues such as cloud outsourcing, artificial intelligence and robo-advice, providing a safe space to put questions to solution providers in regard to technology that is already on the market and ready to be introduced in our financial sector where justified. The next FinTech Lab is expected to address blockchain and other Distributed Ledger Technologies. Standardisation gap mapping activities are being carried out by standardisation bodies at the EU level (CEN-CENELEC, and ETSI being active on blockchain); Europe encourages emerging consortia to avoid market fragmentation and develop PSD2 compliant APIs.

We've seen innovation facilitators, hubs and sandboxes being created in many European countries. ESAs and national regulators have been eager to spread best practice and build expertise across borders. That's the objective of FIN-TECH, an EU-funded project encouraging universities, regulators, supervisors and the FinTechs, to join forces to develop coordinated training support on risk management and new technologies for national regulators and FinTech companies across borders, with the aim of diminishing burden on the compliance side (RegTech) and enhancing converging supervisory practices (SupTech).

Meanwhile, the Commission has rolled out an EU strategy on blockchain based on active stakeholders' engagement through the EU Blockchain Observatory and Forum (1500+ contributors) and the commitment from Member States and EEA countries to build the European Blockchain Service Infrastructure. 27 Member States, Norway and Liechtenstein have formed the EU Blockchain Partnership and are engaging to deploy cross-border digital services on blockchain together starting in 2019. Together with the Member States, the Commission is assessing the regulatory framework with a view to ensuring legal clarity and an enabling environment for technological and other innovation.

The Commission has also witnessed global interest in the International Association for Blockchain Trusted Applications (INATBA), a global multistakeholder association to promote trust and interoperability of blockchain and DLT technologies in different sectors and to enhance regulatory dialogues at the international level. Based in Europe and global from its outset, it already consists of big and small innovative companies and foundations from at least three continents (Europe, Asia and America).

These were just a few examples of the actions in the FinTech Action Plan and Digital Single Market that are progressing. The spirit they share is of policy, innovation and technology moving together, while leveraging EU values to design human-centric services to address our societal needs and to improve our economic competitiveness. ●



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The data battlefield in digital finance

The transformational wave that financial services are experimenting is driven by a number of factors. The main one is the combination of mature technologies like mobile, cloud and big data analytics with new emergent technologies like DLT, AI or IoT. This has a deep impact

on our clients' expectations in terms of convenience, efficiency, customization and security. In addition, other shaping factors appear, greatly facilitated by technology, like the surge of new entrants and new business models mostly based on platform models, and the underlying trend towards decentralization. This context is pushing financial institutions towards a transformation that is much needed to compete effectively in the digital ecosystem.

The entry of brand-new players has been gradual. Fintech startups have first unbundled banking, initially offering niche services like payments and personal finance management, but stepwise entering into lending and asset management. As of today, some >>>

>>> players are rebundling services, turning into integral financial solutions platforms or even getting a license to become fully-fledged banks. We do not need to wait for the future to see significant changes in the industry, because they are already happening. Incumbents, however, must still shift their mindset to make an opportunity out of the unavoidable change. Providing that a level playing field exists, investing, acquiring or partnering with the best fintechs allows to accelerate the digital transformation of the core, and to improve the value proposition to customers by embedding financial services into digital ecosystems.

As it is increasingly being acknowledged by authorities like the BIS or the FSB, BigTechs are a totally different issue. Although it might seem that this is a competition based on new technologies and business models, the real battlefield has to do with the most valuable asset when retaining and improving the

relationship with clients: data. Data is the glue that allows the creation and nurturing of digital ecosystems. BigTechs use them to link their increasingly diversified services around every customer. Data also fuels two-sided marketplaces, accelerating the transition to the uberisation of services, which in financial services is initially manifested in P2P lending or crowdfunding platforms.

“A cross-cutting regulation on user-requested data sharing would be desirable.”

- EDUARDO ARBIZU

In this battle, regulatory asymmetries unlevel the playing field. As an example, PSD2, which forces to open transactional payments customer data to

third parties and applies only to financial institutions, poses a clear case of uneven playing field. A cross-cutting regulation on standardised, secure data sharing based on requests by users would be desirable in order to empower users, increase innovation and ensure a fair competition.

Regulatory authorities in Europe and other progressive jurisdictions have sent clear signals that consumers should have greater control over their data. To the extent that a company is able to gain the trust of its customers, and therefore their consent for the lawful and proper use of their data, it is their responsibility to ensure the protection of such data, something especially relevant in a world of information sharing.

Regulation must ensure that all sizeable actors comply with these obligations and that liabilities are properly allocated even in decentralized environments in which data flows can become difficult to monitor. ●



Levin Holle

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EU regulation as an enabler for a European Digital Single Market

One of the great successes of European integration has been the creation of a strong single market which has also proved to be competitive internationally, while at the same time preserving the

diversity and values of the many people who make up the European Union within a common and mutually agreed legal and economic framework.

Digitalisation could be an enabler for an even closer and stronger European Union, as it is a cross-border phenomenon by its very nature.

Digitalisation brings an increase in cross-border services, including significantly lower transaction costs. Unilateral responses by Member States to address some of the effects of digitalisation should therefore be carefully weighed against the fact that such responses tend to hamper cross-border services and could create barriers within the single market.

The European Supervisory Authorities have recently addressed several areas where this effect is already materialising. In the area of crypto-assets, for example, a harmonised European approach is not yet in place. At the same time, the ESMA Advice on Crypto Assets has discovered a number of gaps and issues in European capital market regulation. Consequently, individual Member States are considering unilateral ways to address this issue mainly for two reasons, namely to foster innovation and to protect their investors. An agenda for creating a single digital financial market should be a key priority for the next European Commission.

A European approach to another digital phenomenon, crowdfunding, is

currently under discussion. The new EU rules on crowdfunding are intended to facilitate the cross-border provision of certain crowdfunding services within the European Union and increase investor confidence in such services by implementing appropriate investor protection requirements. These rules should fit in with the overall regulatory and supervisory approach that is aimed at achieving stable, transparent financial markets and comply with the principles of proportionality and subsidiarity.

“A swift response addressing the most urgent issues is key to staying competitive.”

- LEVIN HOLLE

These developments show that the European Union is well-placed to address and embrace digitalisation and stay ahead of international competition. With regard to the tokenisation of capital markets, harmonised European rules could put the EU in a pole position internationally.

In a digitalized market environment where minimum viable products, time to market and winner-takes-all markets have become paradigmatic, a swift response addressing the most urgent issues is key to staying competitive internationally. ●



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Important steps after the fintech action plan - priorities for the Commission

The Fintech action plan is a good starting point for harnessing the opportunities of fintech and for accelerating the adoption of new technology. It will be the important duty of the next Commission to make conclusions based on studies and assessments that are carried out according to the action plan.

Supervisors' role in fostering innovation is one of the key items discussed in the action plan. Today, nearly each European supervisor has an innovation hub to provide a dedicated point of contact for firms to raise enquiries and to seek guidance on regulatory requirements. There are only a few European regulatory sandboxes i.e. schemes to enable firms to test innovative financial products or services.

Sandboxes are open for only a limited number of firms based on pre-defined entry criteria. This raises several questions. Does the entry into a sandbox programme provide the selected firms competitive advantage compared to other firms? Does it indicate that companies providing similar products are less innovative? Do companies that are admitted to sandbox programmes gain easier funding from venture capitalists?

Supervisors' primary role is to evaluate whether a service is compliant with regulatory requirements - not to indicate, which service it finds the most innovative. Going towards EU level sandboxes would be too premature when taking into consideration all of the unresolved issues. Instead, everyone would benefit from yet increased cooperation between all types of innovation facilitators and discussion on lessons learned.

"Going towards EU level sandboxes would be too premature."

- HANNA HEISKANEN

Detailed technical regulation or product harmonization through technical standardization have not typically been among the tasks of financial supervisors. But will they be in the future? Today, supervisors are receiving an increasing number of requests to enhance the harmonization of technical interfaces and even products. It will be an important role of the next Commission to facilitate discussions regarding financial supervisor's role in technical regulation. Will supervisors keep their principles-based approach or should they move into a more detailed direction?

Adoption of new technology is another key item in the action plan. The question when to adopt new technology is challenging. Firms and supervisors learn from new technologies through experiments and trials. But in critical functions, such as payments systems, you simply cannot experiment with evolving technology. The technology has to be mature enough. Therefore the questions is, where and when to experiment. It is crucial to find controlled ways of testing new technology, such as distributed ledger technology. The next Commission could foster discussion on identifying potential technology trials.

Finally, when working with innovations, it is vitally important to ensure a level playing field for all firms. Each supervisor should interpret directives and regulations identically. Same type of authorisation should be required for similar activity in all member states. It is important that the Commission ensures that the ESA's are empowered to tackle cases where supervisors' approaches differ in a too large extent. ●

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