

A new roadmap for European FinTech: Have we gone far enough?

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The European Commission has presented an Action Plan to promote innovation in the financial sector, setting the roadmap for fintech in Europe. Most initiatives are positive for the EU financial market, but more ambition is needed if Europe aims to become a global fintech hub.

On 8 March 2018 the European Commission made public its long-awaited Action Plan on FinTech “*For a more competitive and innovative European financial sector*”. Soon afterwards, the European Banking Authority (EBA) also released its Roadmap for FinTech. Together, these publications set the master lines for the work of European authorities on this front up to mid-2019.

FinTech, understood as technology-enabled innovation in financial services, offers many opportunities for the European market and its consumers. But at the same time developments in technology and new market dynamics might also create challenges and new risks for consumer protection and financial stability and integrity. As a result, European financial authorities are challenged to provide a regulatory framework that balances the promotion of these digital value propositions and protection against associated risks, while ensuring that a level playing field is achieved for all providers throughout the European Union.

Despite acknowledging that both opportunities and risks exist, the European Commission has chosen to follow a pragmatic and cautious approach in defining its next steps. For now, the Commission has focused on deepening the understanding of the new developments in technology and in the market, and their impact in terms of the traditional objectives of financial regulation. While this approach seems reasonable and necessary to avoid over-regulation that might hamper innovation, it might delay concrete measures that could speed up the process of successfully integrating technological innovation to the benefit of consumers in the single market and contribute to European leadership in global financial services. After this exploratory phase, it will be the turn for the next European Commission to speed up the implementation of the necessary measures.

Despite this caution, the Action Plan outlines several measures that work towards the aforementioned objective of achieving a level playing field for all providers of financial services. With that aim, the Commission has defined measures along three lines: (i) facilitating new business models to achieve scale in the single market, (ii) enabling the financial sector to make use of the rapid advances in new technologies and (iii) making the EU financial sector more cyber-resilient. Furthermore, the European Commission has placed great emphasis on cooperation, and as a result has put in place several forums and working groups with the objective of bringing together the private sector and relevant authorities at national and EU level. These can contribute to EU authorities leveraging the technological and regulatory expertise of the financial sector, feeding valuable insights into authorities’ work on the aforementioned three fronts.

Regulation for innovative business models to grow

According to the European Commission, the majority of innovative business models fit within the existing European financial services regulatory framework, hence it has barely proposed any legislative action¹. This contrasts with the EBA's assessment of the status of fintech firms in the EU last year², in which unregulated or nationally regulated fintech initiatives were identified. In response to this evidence, the Action Plan proposes to further analyse national regimes and procedures to assess whether there are unjustified differences and, if possible, to identify best practices. Still, in the digital space changes in technologies and market dynamics happen fast, and it is important for regulation to be able to accommodate this speed. In this context, the introduction of fintech licences that are activity-specific could facilitate a more rapid development of new business models throughout Europe while introducing more security in areas that remain unregulated. The proposal for a regulation on the provision of crowdfunding services for providers that wish to operate across the EU is a good example.

Finally, in order to foster the upscaling of innovative business models in the EU, the European Commission will seek to identify best practices in national approaches to regulatory sandboxes, as a way to mitigate national divergences and promote initiatives to facilitate innovation at national level. Regulatory sandboxes can indeed become a very useful tool for regulators and supervisors to gain an accelerated learning in a low-risk environment. However, if European authorities really want cross-border innovations to flourish in the EU, bolder steps towards the establishment of a true European regulatory sandbox are needed.

Adoption of technological innovation in the financial sector

Measures to enable new business models to grow, such as those covered in the previous paragraph, are only a partial response to the challenge. In order to fully unlock the opportunities of digitization, it is critical for banks and other incumbent institutions to be allowed to conduct their own transformation journeys. These institutions are the muscle of the financial system and a core driver of the European digital economy, but are often constrained by a regulatory and supervisory framework that is not fit for this era. To respond to this challenge, the European Commission has outlined measures to eliminate regulatory obstacles that might hamper the uptake of innovative technologies, such as cloud computing, artificial intelligence or blockchain. These measures start with the creation of several working groups together with relevant stakeholders.

However, these steps to promote public-private dialogue should be accompanied by other actions of regulators and supervisors to update the knowledge, skills and tools of their staff, either through training or a targeted recruitment policy. Similarly to the organizational development in financial services institutions, the organizational structures of regulatory and supervisory bodies should incorporate digital experts, and eventually all the existing departments should make digital knowledge widespread among their professionals.

A more cyber-resilient EU financial sector

Due to the increase in number and sophistication of cyber-attacks, cybersecurity has become a critical issue for financial entities, consumers, regulators and supervisors, and therefore both the European Parliament and the European Commission have placed cybersecurity at the top of agenda. Cooperation in the fight against cybercrime is paramount and therefore the initiatives brought forward by the Action Plan encourage the participation of the whole financial services industry, regulators and supervisors. These initiatives include enhancing information sharing on cyber threats, promoting convergence in supervisory practices and developing a coherent cyber resilience testing framework with the aim of achieving a more resilient financial sector. Finally, cybersecurity is

1: With the exception of a proposal for a regulation on the provision of crowdfunding services by providers that wish to operate throughout the EU.

2: See Discussion Paper on the EBA's approach to financial technology (EBA/DP/2017/02).

global in nature, and therefore every effort should be led at the international level. Thus, it is positive that the European Commission intends to continue engaging with other national and international institutions and actively participating in the G20/G7 work on cybersecurity.

Next steps

The European Commission is now embarked on the implementation of the measures included in the Action Plan, for which it is relying on other national and European authorities, specially the European Supervisory Authorities. However, looking beyond the 18-month horizon of the Action Plan, it is clear that much more needs to be done to really build a regulatory framework that enables innovation by all players. This task will be the responsibility of the European Commission formed after next year's European elections. All in all, Europe needs a decisive, holistic and forward-looking response to the challenge of digitization. In light of the fast pace of change in the new digital economy and the traditional rigidity of the European regulatory reform process, authorities must embark on this process with urgency for the EU financial industry to realize the aspiration of becoming a global hub for fintech.

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