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Joint European Supervisory Authority response

to the European Commission's February 2021 Call for Advice on digital finance and related issues: regulation and supervision of more fragmented or non-integrated value chains, platforms and bundling of various financial services, and risks of groups combining different activities

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Abbreviations

AI	Artificial Intelligence
ADR	Alternative Dispute Resolution
AML/CFT	Anti-Money Laundering/Countering the Financing of Terrorism
AMLA	Anti-Money Laundering Authority
AMLR	Proposal for an Anti-Money Laundering Regulation, COM/2021/420 final
API	Application Programming Interface
ASU	Ancillary Services Undertaking
CCD	Consumer Credit Directive (CCD), Directive 2008/48/EC
CDD	Customer Due Diligence
CfA	Call for Advice
CRD	Capital Requirements Directive, Directive 2013/36/EU
CRR	Capital Requirements Regulation, Regulation (EU) 2013/575
DFS	Digital Finance Strategy
DLT	Distributed Ledger Technology
DMA	Proposal for a Digital Markets Act, COM/2020/842 final
DMFSD	Distance Marketing of Consumer Financial Services Directive, Directive 2002/65/EC
DORA	Proposal for a Digital Operational Resilience Act, COM/2020/595
DPA	Data Protection Authority
DSA	Proposal for a Digital Services Act, COM/2020/825 final
EBA	European Banking Authority
EEA	European Economic Area
EFIF	European Forum for Innovation Facilitators
EIOPA	European Insurance and Occupational Pensions Authority
EMIR	European Markets Infrastructure Regulation, Regulation (EU) 2012/648
ENISA	European Union Agency for Cybersecurity
ESA	European Supervisory Authority
ESG	Environmental, Social, and Governance
ESMA	European Securities and Markets Authority
EU	European Union
FICOD	Financial Conglomerates Directive, Directive 2002/87/EC
FinTech	Financial Technology
FoS	Freedom to provide services
GDPR	General Data Protection Regulation, Regulation (EU) 2016/679
ICT	Information and Communication Technology

IDD	Insurance Distribution Directive, Directive 2016/97/EU
IFD	Investment Firms Directive, Directive 2019/2034/EU
IFR	Investment Firms Regulation, Regulation (EU) 2019/2033
IGT	Intra-Group Transaction
IHC	Insurance Holding Company
InsurTech	Insurance Technology
IORP	Institutions for Occupational Retirement Provision
JC	Joint Committee of the ESAs
KYC	Know Your Customer
MAG	Mixed Activity Group
MAIHC	Mixed Activity Insurance Holding Company
MCD	Mortgage Credit Directive, Directive 2014/17/UE
MFHC	Mixed Financial Holding Company
MiCA	Proposal for a Markets in Crypto-Assets Regulation, COM/2020/593
MiFID	Markets in Financial Instruments Directive, Directive 2014/65/EU
ML/TF	Money Laundering/Terrorist Financing
MoU	Memorandum of Understanding
NCA	National Competent Authority
OECD	Organisation for Economic Co-operation and Development
ORSA	Own risk and solvency assessment
P2P	Peer-to-peer
PAD	Payment Accounts Directive, Directive 2014/92/EU
PEPP	pan-European Personal Pension Product Regulation, Regulation (EU) 2019/1238
POG	Product Oversight and Governance
PRIIP	Packaged Retail and Insurance-based Investment Products Regulation, Regulation (EU) 2014/1286
PSD2	Payments Services Directive 2, Directive 2015/2366/EU
RoE	Right of Establishment
ROFIEG	Regulatory Obstacles to Financial Innovation Expert Group
SFDR	Sustainable Finance Disclosure Regulation, Regulation (EU) 2019/2088
SFTR	Securities Financing Transactions Regulation, Regulation (EU) 2015/2365

Executive summary

1. In February 2021, the European Commission (Commission) published its Call for Advice on digital finance and related issues,¹ among other things, requesting the European Supervisory Authorities (ESAs) to carry out an analysis of (i) the fragmentation of the financial services value chain, (ii) the growth of digital platforms, and (iii) mixed activity groups, and to set out such recommendations as appropriate in order to ensure the EU's financial services regulatory and supervisory framework remains fit for purpose.
2. This report sets out the findings and advice of the ESAs in response to the Commission's request. It covers cross-sectoral and sector-specific market developments in the three key areas identified in the Call for Advice, and the risks and opportunities posed by digitalisation in finance. It goes on to present ten cross-sectoral and two insurance-specific recommendations for actions to ensure the EU regulatory and supervisory framework remains fit for the digital age.
3. In summary, these recommendations relate to: (i) the need for a holistic approach to the regulation and supervision of the financial services value chain; (ii) strengthening consumer protection in a digital context, including through enhanced disclosures, complaints handling mechanisms, mitigants to prevent mis-selling of tied/bundled products, and improved digital and financial literacy; (iii) promoting convergence in the classification of cross-border services; (iv) promoting further convergence in addressing AML/CFT risks in a digital context; (v) ensuring effective regulation and supervision of mixed activity groups; and (vi) strengthening supervisory resources and cooperation between financial and other relevant authorities, including on a cross-border and multi-disciplinary basis; and (vii) the need for the active monitoring of the use of social media in financial services.
4. With digitalisation, financial institutions increasingly rely on third-party providers for the provision of services through outsourcing and other arrangements, which creates specific supervisory challenges as National Competent Authorities (NCAs) may be limited in their assessment of the risks and/or exercise of supervisory powers on the entirety of the value chains. Concentration risks, and hence financial stability risks, may also arise in case of critical third-party providers. The Digital Operational Resilience Act² (DORA) is an important initiative that will address the information and communication technology (ICT) risks in the financial services value chain. However, DORA is not intended to address other risks that may arise from the reliance of financial institutions on third-party providers. **Recommendation 1** proposes that the Commission take a holistic approach to the regulation and supervision of fragmented value chains, as further outlined under Recommendations 2, 3, 7 and 8 (including in relation to digital platforms, and mixed activity groups), and to conduct regular assessments to determine whether financial institutions exhibit dependence on certain providers that may not be captured by DORA and represent a risk to financial stability.
5. New financial services business models may harm consumers, especially those with lower levels of financial and/or digital literacy. **Recommendation 2** highlights main points for attention for the

¹ European Commission (2021a), [Request to EBA, EIOPA and ESMA for technical advice on digital finance and related issues](#), Ref. Ares(2021)898555, 02 February.

² Proposal for a regulation of the European Parliament and of the Council on digital operational resilience for the financial sector and amending Regulations (EC) No 1060/2009, (EU) No 648/2012, (EU) No 600/2014 and (EU) No 909/2014, COM/2020/595, 24/09/2020.

Commission to ensure that disclosures requirements in EU law are fit for the digital age and brings forward recommendations for the review of the Distance Marketing of Consumer Financial Services Directive³, bearing in mind that the ESAs may provide more specific sectoral recommendations on those matters as part of other ongoing calls for advice from the Commission. In addition, Recommendation 2 calls on the Commission to enhance consumer protection to address risks of mis-selling (in particular for tied and bundled products) and to overcome potential weaknesses in complaints-handling processes at EU level. **Recommendation 3** highlights the need to prevent financial exclusion and to promote further a higher level of digital and financial literacy to help consumers make effective use of financial services provided via digital means and responsible choices that meet their expectations, raising confidence and trust in the digital financial system as well as their personal financial outlook. This could include further analysing the use of data in AI/Machine Learning models and potential bias leading to discrimination and exclusion.

6. Digital financial services are inherently borderless, which raises questions about when the obligation to notify of ‘cross-border provision of services’ is necessary and if so, how to classify these services under the ‘right of establishment’ or ‘freedom of services’. This in turn creates supervisory challenges, but also difficulties for consumers in establishing which authority is the relevant authority e.g. in the event of a complaint or need for redress. **Recommendation 4** draws on previous recommendations prepared by the Joint Committee (JC), and joint-ESA and EBA proposals to address this issue, and again calls on the Commission to provide further guidance on the definition of cross-border services in a digital context.
7. Because of the rapid pace of change and complexity observed in digital financial markets, NCAs may lack the necessary expertise and resources to effectively monitor the market. In **Recommendation 5**, the ESAs advise the Commission to consider possible ways to strengthen skills and resources available to relevant authorities. In that respect, the ESAs welcome the Commission’s work on the Digital Finance Supervisory Academy⁴, which will help regulators and supervisors to better understand, identify, and address the risks and challenges arising from digitalisation through enhanced skills and resources.
8. Notwithstanding the possible benefits, fragmentation of financial services might complicate AML/CFT compliance for financial institutions, especially when they outsource some or all of their compliance tasks to external service providers. Some participants in the digital financial services market might also lack adequate AML/CFT systems and controls. **Recommendation 6** highlights the need to clarify data protection obligations in the customer due diligence (CDD) and wider AML/CFT context and to assess as a matter of priority whether to subject all crowdfunding platforms to EU AML/CFT legislation. It also calls for the Anti-Money Laundering Authority (AMLA) to issue guidelines on outsourcing and governance arrangements in close cooperation with the ESAs, and to undertake a thematic review of best practices.
9. Digital finance has unlocked new synergies between financial and non-financial activities that potentially introduce systemic risk into the market for financial services. To manage prudential risks posed by mixed activity groups performing financial and other services, the ESAs in

³ Directive 2002/65/EC of the European Parliament and of the Council of 23 September 2002 concerning the distance marketing of consumer financial services and amending Council Directive 90/619/EEC and Directives 97/7/EC and 98/27/EC, OJ L 271, 09/10/2002.

⁴ European Commission, “[EU Supervisory Digital Finance Academy: Strengthening Supervisory Capacity in innovative Digital Finance](#)”, EC website.

Recommendation 7 suggest updates to and the potential expansion of consolidation rules in order to ensure effective coverage. Additionally, the ESAs recommend that consideration be given to the creation of new supplementary supervision structures, drawing inspiration from the Financial Conglomerates Directive⁵.

10. The growing digitalisation and datafication of financial services necessitate closer cooperation between financial and relevant non-financial authorities. The ESAs see merit in the Commission exploring possible ways to foster an enhanced cooperation framework between financial data, cyber, consumer protection and competition authorities. **Recommendation 8** proposes three complementary frameworks for structured cooperation that would promote information-sharing on policy developments in each authorities' respective sector and strengthen market monitoring coverage.
11. Finally, **Recommendations 9 and 10** are addressed to the ESAs. Considering the ESAs' role in supporting supervisory convergence, **Recommendation 9** provides for the ESAs to look into possible ways to enhance cooperation between home and host authorities, for instance, through additional guidance on notification requirements, discussions of practical cases in supervisory forums, or procedures to follow in situations in which a financial firm infringes on the rules of other Member States. Enhanced coordination with third-country authorities may also be necessary in the form of a review of existing Memoranda of Understanding (MoUs) to ensure they reflect specific issues related to digital finance.
12. **Recommendation 10** acknowledges the growing use of social media in relation to financial services and the need to actively monitor this phenomenon. In securities markets in particular, the growth of digital trading platforms has coincided with new trends, such as 'social trading', or investment advice shared over social media—which brings new opportunities but risks as well. ESMA recently clarified certain aspects of the applicable rules to the phenomenon.⁶ Meanwhile, the ESAs will continue to monitor these developments and assess where regulatory action may be warranted, including as part of the Commission's calls for advice regarding certain aspects relating to retail investor protection.⁷ This includes considering the need to communicate more effectively with consumers who seek information predominantly through digital channels, including social media.
13. The report includes also two insurance-specific recommendations. **Insurance-specific Recommendation 1** covers the Solvency II⁸ restriction in the scope of (re)insurance activities, a topic which has often come up in light of digitalisation and which can be seen as related to all parts of the Call for Advice. EIOPA will consider further analysis of what is and is not considered as 'activities directly related to insurance' in different Member States to bring more clarity (e.g.

⁵ Directive 2002/87/EC of the European Parliament and of the Council of 16 December 2002 on the supplementary supervision of credit institutions, insurance undertakings and investment firms in a financial conglomerate and amending Council Directives 73/239/EEC, 79/267/EEC, 92/49/EEC, 92/96/EEC, 93/6/EEC and 93/22/EEC, and Directives 98/78/EC and 2000/12/EC of the European Parliament and of the Council, OJ L 35, 11/02/2003.

⁶ See ESMA (2021): [Guidelines on marketing communications under the Regulation on cross-border distribution of funds](#), ESMA34-45-1272, 02 August, and [Statement on Investment Recommendations on Social Media](#), ESMA70-154-2780, 28 October.

⁷ European Commission (2021): [Call for advice to the European Securities and Markets Authority \(ESMA\) regarding certain aspects relating to retail investor protection](#), Ref. Ares(2021)4803687 and [Call for advice to the European Insurance and Occupational Pensions Authority \(EIOPA\) regarding certain aspects relating to retail investor protection](#), Ref. Ares(2021)4805409, 27 July.

⁸ Directive 2009/138/EC of the European Parliament and of the Council of 25 November 2009 on the taking-up and pursuit of the business of Insurance and Reinsurance (Solvency II), OJ L 335, 17/12/2009.

through issuing guidelines for enhancing supervisory convergence) in this issue, taking into account the potential impact for consumers, the insurance sector and its supervision, and any unintended consequences and additional risks. Legislation change is most likely not needed. However, this will also depend on the outcome of the further analysis. **Insurance-specific Recommendation 2** covers peer-to-peer (P2P) insurance. EIOPA has analysed P2P insurance in its previous work. Due to the current relatively low market penetration of P2P insurance business models, and the fact that most of the business models seem to fall under existing regulation, EIOPA does not see a pressing need for special regulatory approaches or changes in relation to P2P insurance, but will continue to monitor market developments.

14. The ESAs remain at the disposal of the Commission, including for assistance on how to introduce the proposals into law and the production of any necessary guidance. Additionally, the ESAs observe that financial services and business models continue to evolve quickly with digitalisation and the use of innovative technologies and that there may be a need to re-assess the issues that these developments raise in due course.

Background and methodological approach

15. The Digital Finance Strategy⁹ (DFS) adopted in September 2020 sets out the Commission's intention to review the existing financial services legislative frameworks in order to protect consumers and safeguard financial stability, protect the integrity of the EU financial sectors and ensure a level playing field.
16. To prepare these actions, the Commission requested technical advice from the ESAs regarding digital finance and related issues. It calls on the ESAs to provide advice on the regulation and supervision of more fragmented or non-integrated value chains (see section 3.1), platforms and bundling of various financial services (see section 3.2), and groups combining different activities (see section 3.3) by 31 January 2022. In addition, it calls upon the EBA to provide advice on (i) non-bank lending and (ii) protection of client funds and the articulation to the Deposit Guarantee Schemes Directive¹⁰ by end of March 2022 (and on which the EBA will report separately).¹¹
17. According to Article 16a(1) of the Founding Regulations for each of the ESAs, they may, upon a request from the European Parliament, the Council or the Commission, or on their own initiative, provide opinions to the European Parliament, the Council and the Commission on all issues related to its area of competence. Article 56 of the Founding Regulations provides that ESAs shall, within the scope of their tasks, "*reach joint positions by consensus with, as appropriate, [the other ESAs]*". Based on the above-mentioned legal provisions, the ESAs are competent to assess opportunities and risks related to digitalisation of financial services and provide the requested advice to the Commission.
18. The three ESAs welcome the opportunity to provide the Commission with technical advice regarding digital finance and related issues. While digitalisation is not new in finance, the ESAs believe that recent developments in relation to the fragmentation of the value chain for financial services, digital platforms and mixed activity groups raise specific regulatory and supervisory issues. This Report outlines the ESAs' positions on possible ways to address these issues, including, where appropriate, recommendations for the Commission.

Background

19. The growing digitalisation of financial service activities has contributed to the fragmentation of the value chain for financial services. This fragmentation occurs for several reasons, including as a result of the growing reliance of financial institutions on services provided by technology companies or with the emergence of FinTechs that occupy niche positions in the market. Value chain fragmentation is neither a new phenomenon, nor is it a direct result of the Covid-19 pandemic. For instance, cloud computing and dependencies on specialist technology companies for data and data analytics tools were gaining widespread adoption prior to Covid-19—though the pace of adoption has accelerated due to the pandemic.
20. Capitalising on greater fragmentation while simultaneously contributing to it, digital platforms have emerged to serve as new venues for financial (and non-financial) products or services—sometimes even bundling these products from a range of different service providers operating in the EU and beyond. Digital platforms have grown in popularity in recent years because of the convenience they offer. Another enabling factor has been the growing adoption of relatively

⁹ European Commission (2020), [Digital Finance Strategy for the EU](#), COM/2020/591, 24 September.

¹⁰ Directive 2014/49/EU of the European Parliament and of the Council of 16 April 2014 on deposit guarantee schemes, OJ L 173, 12/06/2014.

¹¹ See footnote 1 for the reference.

new technologies, such as Application Programming Interfaces (APIs) or Artificial Intelligence (AI), which make physical interactions less relevant and facilitate the development of enhanced front and back-office processes.

21. Fragmentation of financial value chains incentivise firms to pursue new forms of cooperation (or consolidation) in the form of '*mixed activity groups*' (MAGs) that offer customers both financial and non-financial services. Some of these groups, including BigTechs, already have a relatively strong presence in the payments sector, which can be traced to the introduction of the PSD2,¹² and have the potential to gain market share quickly in other financial services because of their large consumer base. These same groups, whose core competencies lie mainly outside of financial services, may use partnerships to create additional layers on top of existing financial infrastructures, leveraging their network effects and data collection superiority to create 'one-stop-shops' for retail products and services.
22. These developments are creating new opportunities for consumers and businesses. Outsourcing to tech companies allows financial institutions to focus on their core services, which brings flexibility and efficiency gains. Digital platforms enhance convenience for users of financial services by facilitating 24/7 access to a wider range of financial products and services. Platform-style offerings enable financial firms to tap into a broader customer base, including cross-border, and capture efficiencies of scale. MAGs can leverage on network effects to reach a wide range of consumers, including some that may be underserved.
23. Yet, these developments are bringing new risks and regulatory/supervisory challenges. The growing reliance on tech companies by financial institutions may create risks to financial stability, e.g. if the same small number of companies are being used by many firms across the financial sector. New digital distribution channels, coupled with sometimes aggressive marketing techniques or leveraging on social media to reach a wide consumer base may exacerbate certain risks to consumer protection. The entry of BigTechs into financial services may create concentration risks and raise level playing field issues relative to incumbent financial groups, because the existing prudential and consolidation frameworks were not designed with these developments in mind.
24. Against this fast-changing environment, the Commission's request for technical advice is a timely and relevant exercise that aims to ensure the regulatory framework remains fit for purpose in the digital age.

Scope of the Call for Advice

25. The Commission's request for technical advice is part of a wider package aimed at embracing digital finance for the good of consumers and businesses.
26. On 24 September 2020, leveraging on the prior work carried out in the context of the 2018 FinTech Action Plan¹³, the Commission adopted a **digital finance package**¹⁴, which sets four key priorities, namely (i) removing fragmentation in the Digital Single Market; (ii) adapting the EU regulatory framework to facilitate digital innovation; (iii) promoting data-driven innovation; and

¹² Directive 2015/2366/EU of the European Parliament and of the Council of 25 November 2015 on payment services in the internal market, amending Directives 2002/65/EC, 2009/110/EC and 2013/36/EU and Regulation (EU) 1093/2010, and repealing Directive 2007/64/EC, OJ L 337, 23/12/2015.

¹³ European Commission (2018), [FinTech Action plan: For a more competitive and innovative European financial sector](#), COM/2018/0109 final, 8 March.

¹⁴ European Commission (2020b), [Digital Finance Package](#), 24 September.

- (iv) addressing the challenges and risks attached to digital transformation. The package includes strategies for digital finance and retail payments along with legislative proposals on digital operational resilience and crypto-assets, namely the proposed Digital Operational Resilience Act¹⁵ (DORA), the proposed Markets in Crypto-Assets regulation¹⁶ (MiCA) and the proposed pilot regime for DLT market infrastructures regulation¹⁷ (DLT pilot regime).
27. The DORA proposal will strengthen and harmonise rules on cybersecurity across the EU financial sector, ensuring that firms address digital operational risks effectively, that they report incidents in a complete and consistent way and that they carry out appropriate testing. DORA also introduces new oversight powers in relation to critical third-party providers of ICT services, recognising the integral role that technology providers increasingly play in the financial system.
 28. MiCA and the pilot regime form a comprehensive framework for the regulation of crypto-assets. MiCA brings clarity to the regulatory position around crypto-assets. With MiCA, previously unregulated services relating to crypto-assets will come under the purview of financial regulators, ensuring that important risks to investor protection are mitigated. Meanwhile, the proposed DLT pilot regime will promote the use of the technology in securities markets, bringing potential gains in efficiency and reliability.
 29. Relatedly, although not targeted at financial services specifically, in December 2020, the Commission put forward two legislative initiatives to upgrade rules governing digital services in the EU: the Digital Services Act (DSA) and the Digital Markets Act (DMA).¹⁸ The DSA¹⁹ and DMA²⁰ have two main goals, namely to (i) create a safer digital space in which the fundamental rights of all users of digital services are protected; and (ii) establish a level playing field to foster innovation, growth, and competitiveness, both in the European Single Market and globally.
 30. Finally, on 2 February 2021, and with a view to make the necessary remaining adaptations to the existing regulatory framework by mid-2022, the Commission published the request for technical advice addressed to the ESAs on digital finance and related issues, namely (i) the fragmentation of value chains, (ii) platforms and the bundling of services and (iii) groups combining different activities. Two additional requests for advice, on prudential risks related to non-bank lending and protection of clients' funds, are directed to the EBA only.
 31. All the above initiatives are instrumental for supporting the uptake of digital finance in the EU in a secure environment for the good of consumers and firms, and will address some of the risks highlighted in this report. The ESAs stand ready to further support the Commission's work on these areas as needed.
 32. Consistent with the Commission's request for technical advice, the report sets out the ESAs' recommendations for addressing regulatory and supervisory challenges brought by the fragmentation of value chains, digital platforms, and MAGs.
 33. Importantly, the ESAs take a balanced approach to digital finance, recognising both the need to unlock potential benefits but also address possible risks that the phenomenon raises. The ESAs

¹⁵ See footnote 2.

¹⁶ Proposal for a regulation of the European Parliament and of the Council on Markets in Crypto-assets, and amending Directive (EU) 2019/1937, COM/2020/593, 24/09/2020.

¹⁷ Proposal for a regulation of the European Parliament and of the Council on a pilot regime for market infrastructures based on distributed ledger technology, COM/2020/594, 24/09/2020.

¹⁸ European Commission (2020c), [The Digital Services Act package](#), 15 December.

¹⁹ Proposal for a regulation of the European Parliament and of the Council on a Single Market For Digital Services (Digital Services Act) and amending Directive 2000/31/EC, COM/2020/825 final, 15/12/2020.

²⁰ Proposal for a regulation of the European Parliament and of the Council on contestable and fair markets in the digital sector (Digital Markets Act), COM/2020/842 final, 15/12/2020.

also consider it important to take a technology-neutral approach to ensure that similar activities are subject to the same or very similar standards regardless of the business models or technologies underpinning them.

Structure of the document

34. The report is organised as follows. Chapter 1 sets out the market developments, Chapter 2 sets out risks and opportunities, and Chapter 3 sets out the ESAs' recommendations.

Joint ESA work and methodological approach

35. The ESAs have cooperated closely on all matters set out in the Commission's Call for Advice on digital finance and throughout the preparation of this report. To inform their work and better understand key market developments, the opportunities and risks attached to them and whether some regulatory action was required to unlock and/or address them, the ESAs have used a number of tools, including existing analysis previously conducted at individual ESA level, surveys to NCAs, public consultations and engagement with external stakeholders, including representatives from the industry (academia, incumbent financial firms, BigTechs, FinTechs, consulting firms, think tanks and consumer associations). Relevant ESA experts and working groups and ESA stakeholder groups were also consulted at various stages of the works at each ESA. On 30 July 2021, ESMA Securities and Markets Stakeholder Group published advice to ESMA on those matters²¹, which has been duly considered as part of the ESAs' work.
36. In addition, on 10 September 2021, the ESAs held a joint-ESA public workshop (online) to present and seek feedback from external stakeholders on their interim findings. The workshop attracted more than 500 participants from the banking, insurance and securities markets sectors, technology companies and consumer and investor representatives, who took the opportunity to raise questions and comments on the joint-ESA interim findings and indications for potential recommendations. The slides presented during the workshop were made publicly available in the aftermath²², and attendees given additional time to provide written feedback.
37. Further details on the work undertaken at each ESA are provided below:

i. EBA additional work

In connection with the development of the EBA's September 2021 digital platforms report²³, the EBA carried out a detailed assessment of market developments, including assessing the role of BigTechs in the EU banking and payments sector. As part of the information-gathering to inform this report, the EBA survey issued a survey to the NCAs on the regulated financial services activities carried out by BigTech group companies in the EU. The EBA has also carried out extensive analysis with NCAs on the scope of the current prudential

²¹ ESMA Securities and Markets Stakeholder Group (2021), [SMSG advice to ESMA on digital finance](#), ESMA22-106-3473, 30 July.

²² See ESAs (2021), [presentation of the joint-ESA workshop on the Call for Advice on digital finance](#), virtually held by the ESAs on 10/09/2021.

²³ EBA (2021e), [Report on the use of digital platforms in the EU banking and payments sector](#), EBA/REP/2021/26, September.

consolidation framework under the CRD²⁴/CRR²⁵ which has helped inform this report, along with the analysis undertaken to fulfil the mandate addressed to the EBA in the Call for Advice on Digital Finance in relation to non-bank lending.

ii. EIOPA additional work

In 2020, EIOPA published a Discussion Paper²⁶ and launched public consultation on the fragmentation of the value chain and new business models to get a better picture of possible fragmentation of the EU insurance value chain and the supervisory challenges related to that. An overview of the feedback received is set out in the feedback statement.²⁷ In 2021, EIOPA published a Discussion Paper on Blockchain and Smart Contracts in insurance²⁸ and a Discussion Paper on Open Insurance: accessing and sharing insurance-related data²⁹, and launched public consultations on both Discussion Papers. The input received from broad range of stakeholders has informed current work.

iii. ESMA additional work

In March 2021, ESMA launched a survey to its NCAs to seek their feedback on the issues set out in the call for advice in relation to fragmented value chains, digital platforms and MAGs. NCAs were invited to provide feedback on a 'best-effort' basis due to the potential limitations in visibility over certain developments in the context of digital platforms or mixed groups outside their supervisory remit. 28 NCAs provided feedback to the survey, the summary of which is available in on ESMA's website.

In addition, in May 2021, ESMA published a call for evidence to the market³⁰ to seek feedback from external stakeholders. The call for evidence brought forward a set of tailored questions for each of the three areas covered in the call for advice, with a specific focus on ESMA's remit. ESMA received a total of 32 responses from a wide range of stakeholders. An overview of the feedback received is available from ESMA's website.

²⁴ Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC, OJ L 176, 27/06/2013.

²⁵ Regulation (EU) 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) 684/2012, OJ L 176, 27/06/2013.

²⁶ EIOPA (2020b), [Discussion Paper on the \(re\)insurance value chain and new business models arising from digitalisation](#), EIOPA-BoS-20-276, 14 April.

²⁷ EIOPA (2021c), [\(Re\)insurance value chain and new business models arising from digitalisation: Feedback statement to the Discussion Paper](#), EIOPA-BoS-21-219, 4 May.

²⁸ EIOPA (2021b), [Discussion Paper on Blockchain and Smart Contracts in insurance](#), 29 April.

²⁹ EIOPA (2021a), [Discussion Paper on Open Insurance: accessing and sharing insurance-related data](#).

³⁰ ESMA (2021d), [Call for evidence on Digital Finance](#), ESMA-50-164-4518, 25 May.

1 Market developments

1.1 Fragmented or non-integrated value chains

38. Relying on **third-party services and particularly outsourcing** is not a new phenomenon in the financial sector. Financial institutions have always cooperated with and engaged services from other financial and non-financial companies.³¹ This has been subject to EU regulatory requirements and supervision for a long time, including through effective governance and risk management requirements and outsourcing provisions.
39. However, technological developments and digitalisation are increasing the extent and ways by which financial institutions rely on third parties within the value chain. Indeed, financial institutions are increasingly relying on technology and data provided by third parties for their digital transformation—a trend that has accelerated in response to the Covid-19 pandemic.³²
40. The ESAs also observe **growing interactions between incumbent financial institutions, FinTechs and BigTechs through a variety of co-operation models**, e.g., partnerships, joint ventures, outsourcing and sub-outsourcing, mergers and acquisitions. These firms are also partnering to co-innovate and provide new products or services leveraging on their complementary competencies. Some technology providers partner with multiple financial institutions.³³ Value chains originated, managed and controlled by technology companies or other third parties are emerging.³⁴ FinTechs and BigTechs compete with incumbent financial institutions to provide regulated financial services. Although the entry of BigTechs into regulated financial services is still relatively limited in the EU³⁵ compared to other jurisdictions, the phenomenon requires monitoring (see section 1.3).
41. These developments are driven by **efficiency, competitiveness and innovation purposes**. Financial institutions may choose to externalise their non-core activities to better focus on their operating models and value-adding activities. Technology firms are demonstrating that certain processes within the value chain can be carried out more efficiently, and effectively as stand-alone services. Indeed, greater fragmentation is associated with more specialisation in the value chain. For instance, outsourcing to cloud infrastructure to replace in-house data centres could produce cost savings for financial institutions.³⁶ Financial institutions also tap into specialised capabilities of third parties to offer relevant and cost-efficient digital solutions to consumers. In securities markets, software companies are offering bespoke solutions to augment trading, settlement, clearing, and collateral management services. Investment advisers and insurers are now using AI to customise portfolios and life insurance policies based on the profiles of their clients.³⁷ In the banking sector, the emergence of new service providers for Know Your

³¹ E.g. insurance undertakings with reinsurance undertakings, investment firms with clearing and settlement services providers, banks with payment service providers and payment card schemes.

³² FSB (2020a), [Regulatory and Supervisory Issues Relating to Outsourcing and Third-Party Relationships: Discussion paper](#).

³³ Examples include cloud providers, innovative payments service providers, data providers.

³⁴ EIOPA (2020b), *Discussion Paper on the (re)insurance value chain and new business models*.

³⁵ In some EU jurisdictions, FinTechs and BigTechs hold licenses for payments, e-money, banking and insurance intermediation.

³⁶ Scott, H., Gulliver J. and Nadler, H. (2019), [Cloud Computing in the Financial Sector: A Global Perspective](#), Program on International Financial Systems, July, pp. 6-7.

³⁷ See [responses to the Call for evidence on Digital Finance](#) on ESMA website.

Customer (KYC) or loan administration services is observed. There is also an expanded range of products and services offers (e.g., crypto assets, on-demand, P2P and parametric insurance, smart contracts, electronic payment services) and the emergence of new data centric business models. Regulatory technology (**RegTech**) **solutions** are also emerging, which can facilitate regulatory reporting and provide solutions for fraud, scams in remote onboarding, operational and cybersecurity risks.³⁸ Collaboration can also reduce time-to-market for new initiatives, enabling economies of scale.

Increased availability of data and capacities to consolidate a wide range of data sources

42. Another driver of these developments is the availability of data³⁹ and the capacity to consolidate or analyse large quantities of data, which has increased exponentially. According to the Commission, the volume of data produced in the world is expected to grow from 33 zettabytes in 2018 to 181 zettabytes in 2025⁴⁰ and increased business applications of data can be expected across the economy, including in financial services.
43. Relatedly, the breadth of available data, including alternative or non-financial data such as behavioural, Internet of Things (IoT), social media, Environmental, Social and Governance (ESG) data is growing quickly, spurred by the development of open data principles.
44. Financial institutions increasingly use **data sourced from third-party data vendors** to calculate creditworthiness or personalised investment advice, although this data is not substituting traditional data sets yet. For example, in banking, core banking data remains the main source for analytics rather than data from external sources such as social media. This may be due to institutions' concerns about the reliability and accuracy of external data⁴¹ as well as aspects related to ethical access and use of data. In insurance, traditional data sources such as demographic or exposure data are increasingly combined (not replaced) with new sources like online media or telematics data, providing greater granularity and frequency of information about consumer characteristics, behaviour and lifestyles. This enables the development of increasingly tailored products and services and more accurate risk assessments.⁴² In securities markets, a growing range of data, including alternative non-financial data, is being used by asset managers to refine their investment decisions. This in turn creates new/increased dependencies between financial institutions and third-party data providers.

Increased computing capabilities

45. **The capacity to store and process data has also** multiplied, including through the use of **cloud computing** which has become a vital infrastructure for financial services. Cloud computing is an enabler of agility and advanced data analytics, providing vast storage space and the ability to

³⁸ See EBA (2021d), [EBA analysis of RegTech in the EU financial sector](#), EBA/REP/2021/17, June and EIOPA (2021b), *Discussion Paper on Blockchain and Smart Contracts*; See Anderberg, A. et al. (2019), [Blockchain Now And Tomorrow: Assessing Multidimensional Impacts of Distributed Ledger Technologies](#), Publications Office of the European Union, Luxembourg, 2019, JRC117255, referring to Kavassalis, P., Stieber, H., Breyman, W., Saxton, K. and Gross, F. (2018), "An innovative RegTech approach to financial risk monitoring and supervisory reporting", *Journal of Risk Finance*, Vol. 19 No. 1, pp. 39-55.

³⁹ This concerns data in general, not necessarily data relevant to financial services.

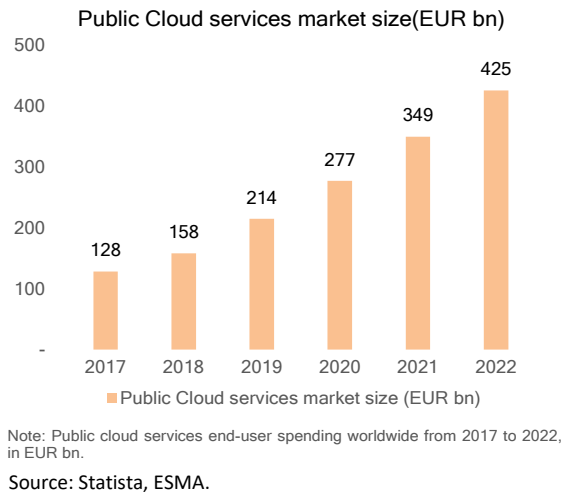
⁴⁰ IDC and Statista (2021), [Volume of data/information created, captured, copied, and consumed worldwide from 2010 to 2025 \(in zettabytes\)](#), Graph, 7 June, Statista website.

⁴¹ EBA (2020c), [EBA report on Big Data and Advanced Analytics](#), EBA/REP/2020/01, January.

⁴² EIOPA (2019b), [Big Data Analytics in motor and health insurance: a Thematic Review](#).

analyse large quantities of data at significant scale, including through easy connectivity to mobile applications used by consumers.⁴³ For example, in the insurance sector, cloud computing services are already used by 33% of motor and health insurance undertakings, with a further 32% saying they will be moving to the cloud over the next three years.⁴⁴

Figure 1: Booming public cloud services



46. Some cloud providers are offering tailored financial services-specific cloud solutions that enable new capabilities such as customer onboarding, profiling and engagement, regulatory compliance assessments, or data encryption that will unlock personal data previously considered too sensitive for analytical purposes. Some insurers are teaming up with cloud providers to build digital healthcare platforms, enabling virtual health and well-being services (e.g., self-assessment and prevention tools, a teleconsultation interface, a digital document vault, home care services) or cybersecurity initiatives aiming to improve the cyber-resilience and reduce the cyber-risk of small and medium sized businesses. While cloud computing has the potential to reduce technology infrastructure costs, **concentration risks are high**.^{45, 46}
47. There is also **growing use of Big Data and AI**. In order to capitalise on the opportunities offered by digitalisation, in recent years many financial institutions have embarked on digital transformation projects where AI plays a pivotal role. More specifically, AI systems are increasingly used to process new and old datasets, launch targeted marketing campaigns or to offer more targeted products and services to consumers. In 2018, already 31% of participating European insurance undertakings were using machine learning and another 24% were at a proof-of-concept stage.⁴⁷ In some jurisdictions the level of adoption is already 100%.⁴⁸

⁴³ EBA (2020c), *EBA report on Big Data and Advanced Analytics*, p. 11.

⁴⁴ EIOPA (2019b), *Big Data Analytics in motor and health insurance*, p. 17.

⁴⁵ Scott, H., Gulliver J. and Nadler, H. (2019), *Cloud Computing in the Financial Sector*, pp. 12-14.

⁴⁶ FSB (2019a), [FinTech and market structure in financial services: Market developments and potential financial stability implications](#), 14 February, pp. 16-17.

⁴⁷ EIOPA (2019b), *Big Data Analytics in motor and health insurance*, p. 6.

⁴⁸ The use of big data analytics tools by insurance undertakings takes place throughout the insurance value chain, predominantly in the areas of pricing and underwriting, claims handling and sales and distribution.

48. While often big data/AI-related services can be developed in-house, **many financial institutions engage external technology providers for big data/AI-related services**⁴⁹ (e.g., tools for model development or robo-advice⁵⁰). AI systems used by financial institutions typically combine the use of data from internal sources (i.e., provided directly from consumers or generated by financial institutions) and/or external sources (e.g., credit rating agencies, public repositories or research centres).
49. **Tech firms are also contracted for other specialised services** beyond cloud and AI/Machine Learning. Examples include KYC/client onboarding, e.g., the development of biometrics and other developments in digital ID/e-Signature used for client authentication and authorisation (increasingly also combined with big data and analytics) or ESG analysis.

Open finance and Distributed Ledger Technology

50. **Open finance** can be seen as another development facilitating both innovation⁵¹ and increasing both competition and fragmentation. The discussion around open finance has been underway for some time, focusing mainly on the banking sector and PSD2 (open banking). Recent EU policy initiatives, such as the Commission's Data Strategy⁵² and Digital Finance Strategy⁵³, clearly recognise the importance of data-driven innovation and data flows within the EU.⁵⁴ Data exchange, both personal and non-personal data, through (open) Application Programming Interfaces (APIs) has expanded beyond the banking sector. Open APIs can facilitate industry-wide innovation and increase the agility of businesses in responding to changes in customer needs and expectations. As part of the push for open finance, institutions are granting more access to their internal APIs to the outside world to offer better services to policyholders and/or greater market competition (e.g. the integration of financial institutions with platforms and other third parties).⁵⁵
51. On the payments side, the **PSD2 framework** has contributed to market evolution by requiring payment service providers (mainly banks) to open up their payment accounts data to authorised and regulated third parties (i.e., open banking), thus enhancing competition in the payments market and creating incentives for further digitalisation. PSD2 also has implications beyond the banking sector. Cross-sectoral open finance solutions have been developed often through strategic cooperation between FinTechs, banks and insurers by leveraging PSD2 data (e.g., using account information for suitability assessments when providing life insurance products).⁵⁶

⁴⁹ EBA (2020c), *EBA report on Big Data and Advanced Analytics*; EIOPA (2019b), , pp. 6, 10, 14.

⁵⁰ Joint Committee of the ESAs (2018), *Joint Committee Report on the results of the monitoring exercise on 'automation in financial advice'*, JC 2018-29, 5 September, p. 9.

⁵¹ McKinsey assessed that opening financial data could increase EU GDP by 1-1.5% by 2030; McKinsey Global Institute (2021), *Financial data unbound: The value of open data for individuals and institutions*, Discussion Paper, June, p.10.

⁵² See the European Commission's communication and factsheet from 19 February 2020, available at: [European data strategy](#), EC website.

⁵³ See footnote 9.

⁵⁴ The Commission announced in the DFS that it will present a legislative proposal for a new open finance framework by mid-2022, building on and in full alignment with broader data access initiatives.

⁵⁵ EIOPA (2021a), *Discussion Paper on Open Insurance*.

⁵⁶ *Ibid*, Section 3, in particular Figure 5 and Box 2, pp. 17-18.

52. **The introduction of PSD2 has also contributed to the growth of FinTechs and BigTechs in the payments market.** Often this takes the form of partnerships with one or more leading financial institutions⁵⁷ to provide ‘customer-facing’ interfaces to facilitate the provision of payment services (and potentially to facilitate access to other products and services offered by the financial institutions). In the future, BigTechs may create additional layers on top of existing services⁵⁸, acting as marketplaces that offer customers the ability to access the products of multiple financial institutions through their distribution channel or platform (known as a ‘one-stop-shop’ model).⁵⁹ Digital or mobile wallet services are also proliferating, as is cooperation with innovative distributors. Increasing development of mobile-based solutions for payments and a general increase in online payments is underway, partly accelerated by the Covid-19 pandemic.
53. **Distributed Ledger Technology (DLT) and smart contracts** are still at an early stage of development in finance, although more practical use cases are emerging in insurance, money remittance and real-time payments.⁶⁰ While it is still early for DLT in the EU financial sector, the number of potential use cases is growing and can influence a number of financial services functions through disintermediation in areas such as IT, operations, product design and development (smart contract-based products), pricing, underwriting, distribution via intermediaries, claims management in insurance, market infrastructure in securities,⁶¹ and inter-bank settlement arrangements. Growth of DLT has also introduced new cooperation models (e.g., industry consortiums working on DLT implementation). As DLT adoption grows, it could potentially cause fragmentation, e.g., in the case of lack of interoperability across DLTs or between DLTs and existing infrastructures. While digitalisation currently seems to rely also on in-house innovation or cooperation with partners that are mostly subject to financial sector supervision, the cooperation with partners not within the financial sector regulatory perimeter is clearly increasing. These developments are expected to continue transforming the way products and services are provided with benefits for consumers and financial institutions.
54. Hence, it is important to prepare for the possibility that fragmentation of the value chain will continue to increase, i.e. monitor developments, identify and analyse risks, and regulate when necessary.

1.2 Platforms and bundling of various financial services

1.2.1 Cross-sectoral

55. Consistent with wider digitalisation trends across the EU economy, financial institutions are increasingly relying on innovative technologies to provide financial products in the digital environment through an improved access point alongside new and improved services to their customers.⁶² As part of this trend, digital platforms are increasingly used to market and

⁵⁷ See further EBA (2021e), Text Boxes 1 and 2, pp. 25-27.

⁵⁸ FSB (2019a), *FinTech and market structure in financial services*, p. 14.

⁵⁹ See footnote 57.

⁶⁰ EIOPA (2021b), *Discussion Paper on Blockchain and Smart Contracts*; See also EIOPA *Consumer Trends Report 2021* (forthcoming).

⁶¹ See footnote 17 for the DLT pilot regime.

⁶² International Center for Monetary and Banking Studies (2019), [Banking Disrupted? Financial Intermediation in an Era of Transformational Technology](#), *Geneva Reports on the World Economy* 22, 24 September.

distribute financial products and services, sometimes bundling different financial and non-financial services and products from a range of service providers.⁶³

56. The ESAs have identified different drivers fostering the rapid uptake of digital platforms in the financial services sector. First, consumer behaviour is shifting towards an increasing search for convenience. Consumers are increasingly demanding access to financial services and products at all times and from different digital devices through a single access point. This behavioural shift towards frequenting online financial services has been accelerated by the Covid-19 pandemic and is expected to become structural, essentially breaking the historic trend of services being provided and accessed locally via physical premises.⁶⁴ Additionally, consumers are increasingly seeking personalised products and experiences⁶⁵ and with this a broader range of tailored financial products and services. Digital platforms can help financial institutions in meeting this demand by boosting convenience, allowing consumers to access financial products and services through almost any digital device and without time restrictions, and by better addressing the specific needs and expectations of consumers. Another enabling factor has been the growing adoption of relatively new technologies, such as APIs or AI, which make physical interactions less relevant and facilitate the development of enhanced front and back-office processes, including through the use of advanced data analytics.
57. As a consequence of the changing consumer behaviour and the Covid-19 pandemic-triggered acceleration of digitalisation, incumbents are changing their business models to remain competitive in the market, and new entrants are leveraging digital platforms as their sole or core interface with customers.⁶⁶ This includes, for example, reaching the new generation of often tech-savvy consumers, expanding product and services offerings towards increased personalisation and enabling consumers to easily gather information about a financial institution's specific products and services online, including via social media (see **Box 1**).
58. Against this background, the ESAs have observed a growing utilisation of digital platforms to bridge consumers and the providers of financial products and services within the EU financial sector. Specifically, four approaches can be observed toward a financial institution's platform development, (i) in-house development by the relevant financial institution or group company, (ii) partnerships among consortia of financial institutions, (iii) partnerships between financial and non-financial institutions, notably technology companies, e.g., FinTechs, (iv) outsourcing to, and reliance on, third-party technology companies. While digital platforms can perform multiple functions, two core functionalities are consistent to facilitate the bridging between consumers and providers of financial and non-financial products and services. First, digital platforms improve the visibility of products and services and consequently related marketing activities. Second, they also facilitate the conclusion of contracts for products and services, either directly or by 'funnelling' consumers to the relevant website of the product and service provider.

⁶³ See further EBA (2021e), *Report on the use of digital platforms*.

⁶⁴ Capgemini Research Institute (2020), [Covid-19 and the financial services consumer: Supporting customers and driving engagement through the pandemic and beyond](#), Research note, April, Sogeti website.

⁶⁵ PwC (2019), ["Shaping consumer behaviour in financial services"](#), PwC website.

⁶⁶ EBA (2021e), p.28.

59. There is no commonly agreed definition of digital platforms, and the term effectively covers a wide variety of set-ups and entities.⁶⁷ Different types of platforms also employ a variety of business models and provide a wide range of financial products and services within the EU market, often sharing attributes of two or more categories. However, four core elements may be used to differentiate between platform types.⁶⁸ First, the platform operator can be either the financial institution, or a technology company or any other third party. Second, the platform can be used by either one or several financial institutions from one or different sectors for the provision of financial services. Third, platforms may provide access to a single or to multiple types of financial products or services or they bundle financial and non-financial products and services. Fourth, platforms can be used for the marketing and/or conclusion of contracts for products and services. Against the background of these core elements, the EBA report on digital platforms has identified an indicative platform taxonomy, spelling out five indicative clusters,⁶⁹ which also serves as background to this ESA technical advice.
60. First, **comparison platforms** enable consumers to compare different sectoral or cross-sectoral financial products and services provided by different financial institutions. For example, consumers can directly compare prices of different products and services or are provided with a ranking based on sample criteria or criteria based on the consumer's preferences. Hence, comparison platforms allow consumers to specifically filter for products and services that address their individual needs. They also typically either redirect consumers to a financial institution's webpage or act as a regulated financial intermediary between financial institutions or consumers. In either way, they may charge fees to financial institutions in return for displaying products and services or receive commissions upon having facilitated a contractual arrangement between consumers and financial institutions. Comparison platforms may be operated by financial or non-financial institutions. Examples of comparison platforms include *deposit brokerage platforms*,⁷⁰ facilitating the placing of deposits with partnering credit institutions by providing a comparison of interest rate offers, investment-related *robo-advisor comparison platforms*,⁷¹ showing a breakdown of relevant quantitative and qualitative information such as fees, account minimums, investment instruments or user experience for different robo-advisors, comparison websites comparing different life or non-life insurance or pension products or multi-sector comparators comparing products across the financial sector (e.g. banking, insurance and/or investment products).
61. Second, **financial institutions** comprise those digital platforms, operated by regulated financial institutions (including regulated intermediaries⁷²), which enable third parties – financial institutions or other firms in case of non-financial products – to market and distribute financial and non-financial products and services to consumers. Again, the platform may either redirect

⁶⁷ In the context of this technical advice, 'platform' means any digital platform that enables financial institutions directly (or indirectly using a regulated or unregulated intermediary) to market to investors, and/or conclude with investors, contracts for, financial products and services. The definition of 'platform' aims to be both 'model' and 'technology-neutral'. Examples of platforms that are relevant for this technical advice include but are not limited to technical infrastructures used by financial institutions to market or distribute different financial products and services that enable investors to access products and services provided by different financial institutions. Those technical infrastructures that have been developed by financial institutions for their sole individual benefit are outside of the scope of this technical advice.

⁶⁸ EBA (2021e), p. 18.

⁶⁹ EBA (2021e), "An illustrative taxonomy of platforms", Section 3.4, pp. 18-19.

⁷⁰ EBA (2021e), Text Box 10 "*Deposit Brokerage Platforms and the DGSD*", pp 56-57.

⁷¹ Robo Advisors Europe (2021), *Robo advisors in Europe*, <https://robo-advisors.eu/>.

⁷² E.g. in cases where insurance platforms could be operated by insurance intermediaries (mostly brokers) falling under the Insurance Distribution Directive.

consumers to a third party to contract a product or service or it intermediates the transmission of funds from the consumer to third party. They may also charge fees to third parties in exchange for granting access to the platform or in relation to products and services contracted following interactions on the platform. Private banking 'lifestyle' apps or digital trading platforms, for example, would typically fall into this category or neobanks offering health, leisure and travel services in addition to banking, insurance and/or investment products. Some insurers are also offering additional e-health services in addition to their insurance products.

62. Third, **platforms with financial services as a side service** are typically operated by non-financial institutions and offer consumers access to third-party financial products and services and third-party non-financial products and services via one platform interface. Again, they may charge fees similar to the ones identified for financial institution+ providers. Examples of these platforms are typically found in e-commerce, travel websites linking travel booking with foreign exchange service providers or automobile and real estate sales, linking credit or insurance services with the purchase of a specific product.
63. Fourth, **ecosystem platforms** serve as marketplaces for a large number of financial institutions and other firms to market and distribute their products and services to consumers, meaning that financial products and services are offered as part of a wide range of products and services available on the platform, and may be operated by financial or non-financial institutions (however, in the EU, typically by non-financial institutions). The platform typically facilitates the marketing of products and services but sometimes also acts as a financial conduit from consumers to third-party providers, including group companies that may be authorised as financial institutions. In other cases, consumers need to contract to product or service directly with the product provider. Current ecosystem platforms tend to concentrate on travel, healthcare, housing and mobility needs but are evolving quickly.⁷³
64. The ESAs expect this type of digital platform to grow rapidly in the next two to five years, with digital commerce continuing to grow and the increasing demand from retail consumers and small and medium-sized enterprises for accessibility to financial services continuing to mirror the ease of access to other types of products and services.
65. Fifth, **enabler platforms** are platforms typically provided by large technology companies offering a suite of software that acts as the interface between consumers, financial institutions and sometimes third parties. Examples include the so-called 'Pays' (e.g. Apple Pay, Google Pay etc) or 'back-office' platforms (e.g., white-label infrastructures offered by financial institutions to other financial or non-financial institutions such as Decentralised P2P insurance platforms). Different to the other platform types, the contractual arrangement between the consumer and the financial institutions typically already exists, with the platform merely being used to facilitate new means of executing a financial service.⁷⁴
66. Where a platform is operated by a financial institution, it will fall under the general governance and risk management requirements applicable to the financial institution dependent on the exact services that it provides. For example, the provision of e-money services will trigger the need for authorisation as an electronic money institution (if the firm is not already authorised

⁷³ McKinsey (2018), [Insurance beyond digital: The rise of ecosystems and platforms](#); See also EIOPA (2019a), [Consumer Trends Report 2019](#), and EIOPA (2020b), *Discussion Paper on the (re)insurance value chain and new business models*.

⁷⁴ For further explanation, see EBA (2021e), Text Box 1, p. 25.

as a credit institution), the provision of lending services may be required to be licenced pursuant to EU or national law (if the firm is not already licenced as a credit institution), and the provision of MiFID⁷⁵ services will trigger the need for a MiFID licence, the associated applicable requirements varying according to the exact type of MiFID services provided. Similarly, the provision of services falling under the Insurance Distribution Directive⁷⁶ (IDD) will require compliance with all IDD requirements.

67. The ESAs observe that financial institutions' growing use of, and collaboration with, digital platforms increase their dependency on third parties. Additionally, the cross-border nature inherent to many digital platforms deepens the interconnectedness of different financial and non-financial sectors across different EEA (and potentially third country) jurisdictions. Yet, as set out by the EBA in its digital platforms report, NCAs have a limited understanding of platform-based business models and need to keep pace with the associated market developments, while securing an appropriate level of visibility of financial institutions' use of and dependencies on digital platforms. Indeed, evidence suggests that NCAs have limited visibility over financial institutions' use of digital platforms both as home and as host NCAs.⁷⁷ Indeed, based on the ESAs' analysis, it appears that the vast majority of NCAs currently have limited visibility over, and understanding of, financial institutions' reliance on digital platforms/enablers, particularly in the context of interdependencies between financial institutions and technology companies outside the perimeter of NCAs' direct supervision.

Box 1: Social media impact on the provision of financial products and services

The ESAs observe a growing reliance on social media in the context of both financial decision-making by individuals and the provision of financial services by firms. Consumers increasingly look to a wider range of sources, including non-traditional sources such as online and social media, to inform their financial decision-making, which can also contribute to the growing disintermediation of financial services and products. A prominent example is the rise of so called *finfluencers* – individuals with a wide social media reach, discussing money-related topics and sometimes offering financial recommendations. The content shared and distributed on social media is broad, ranging from information aimed to boost financial literacy, to general observations about financial market developments and speculations about the profitability of financial products. The interactive character of social media enables one-to-one and one-to-many conversations and content-sharing options which can foster herding behaviour.

Similarly, the range of finfluencers is wide, from retail consumers to financial services professionals. The latter may use social media in their personal capacity but sometimes also as part of their professional activities. Indeed, the ESAs have observed a growing role for social media as part of overall communication and marketing activities for the provision of financial services, ranging from product display to marketing activities and online advice. Through online channels, financial professionals can reach many consumers and provide them with tailored information material, often by segmenting and targeting specific groups through the use of specific hashtags/keywords. They can

⁷⁵ Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61/EU, OJ L 173, 12/06/2014.

⁷⁶ Directive 2016/97/EU of the European Parliament and of the Council of 20 January 2016 on insurance distribution, OJ L 26, 02/02/2016.

⁷⁷ ESMA survey to competent authorities on digital finance (March 2021); EBA survey to competent authorities on financial institution dependencies on digital platforms and regulatory and supervisory issues (November 2020).

also engage in interactive discussions via live-video streaming functions or offer personal advice online via private messenger functions.

1.2.2 Securities markets

Digital trading platforms

68. Consistent with the growth of digital platforms across the financial sector, in securities markets, ESMA has observed an increase in the use of digital trading platforms by retail investors. These platforms, sometimes known as ‘neo-brokers’, ‘on-line brokers’ or ‘zero-commission brokers’, are typically operated by new entrants, rather than incumbent financial firms, and rely on a fully digitalised infrastructure. Through these platforms, investors have online access to a wide range of investment products from different providers, e.g., bonds, shares, ETFs, or more complex or speculative instruments like forex or crypto-assets, and services, including trade execution, portfolio management or investment advice. In addition, many provide market analysis or investor education tools, and sometimes other types of financial services, e.g., banking services, including where they are part of a wider financial group. Most operate cross-border, as their digital features make it easy for them to offer products and services outside of their country of origin. For example, one of the largest trading platforms in the EU, with 20 million reported users, is accessible for investors from all 27 EU member states. Yet, other platforms are present in a few EU countries so far.
69. Mirroring the cross-sectoral drivers for the uptake of digital platforms, the use of digital trading platforms accelerated in the wake of the Covid-19 pandemic and shifts in consumer demographics. The sharp drops in valuations and surges in volatility caused by wider Covid-19 impacts led to a general **increase in stock buying and volume traded** by retail investors across different EU countries in 2020.⁷⁸ In France, purchases of French equities by retail clients increased fourfold in March 2020⁷⁹, while Italy reported considerably higher figures of retail investors’ net equity purchases in 2020⁸⁰, compared to 2019. In Belgium, younger retail investors have increased their purchase of shares in the BEL 20 by ten times during the Covid-19 pandemic.⁸¹ Unsurprisingly, digital trading platforms providing online access to investment products during the national lockdowns imposed in the course of 2020 have benefited from this shift. Yet, the market in the EU is not yet as developed as in the US, where trading platforms are heavily competing for market share and have shown substantial growth recently. One of the largest digital trading platforms in the US saw an 80% jump in its number of users to 22.5 m in the first half of 2021.⁸²
70. At the same time, a new type of **self-directed retail investor**⁸³, often non-sophisticated and adopting a *do it yourself* approach, is turning to digital means to access investment products

⁷⁸ See further details in ESMA (2021a), [Report on Trends, Risks and Vulnerabilities, No. 1](#), ESMA50-165-1524, 17 March, p. 34.

⁷⁹ AMF (2020), [Retail investor behaviour during the COVID-19 crisis](#), 27 April, p.5.

⁸⁰ Consob (2020), [Report of financial investment of Italian households, Behavioural attitudes and approaches](#), pp. 18-19.

⁸¹ FSMA (2020), [“Belgians trade up to five times as many shares during the coronavirus crisis”](#), 27 May.

⁸² Statista (2021b), [Number of users of Robinhood from 2014 to 2nd quarter 2021 \(in millions\)](#), Graph, 17 August, Statista website.

⁸³ Self-directed investors are defined as those who are making investment decisions on their own behalf, i.e. selecting investment types and making trades themselves without the help of a financial adviser.

and services.⁸⁴ Self-directed investors feel more catered for by the new trading platforms, while feeling *'almost like they don't belong'* to traditional investment websites.⁸⁵ These platforms also build on the growing importance of social and emotional factors in retail investors' decision-making. Noteworthy, 38% of investors driven by emotional and social motivation tend to invest in high-risk investment products and only 41% of them believe that the loss of some money is a genuine risk, suggesting that they are not necessarily aware of the risks associated with investing.⁸⁶ Anecdotal evidence also points to an increase in the use of gamification elements, e.g., confetti or rewards upon achieving investment milestones, by digital trading platforms, although there seems to be a growing realisation that some of these features can trigger addictive behaviour by investors and some platforms using them seem to no longer do so.

71. Relatedly, digital trading platforms often facilitate and/or leverage on interactions with online media, especially social media. For example, some digital trading platforms enable investors to directly share their investment activities on social media through embedded links and social media is listed as the second most frequented source out of a list of *'contemporary sources'*⁸⁷ used to inform investment decision-making.⁸⁸ At the same time, influencers can generate traction among followers, thus possibly accelerating trading among retail investors. A recent report⁸⁹ confirms the social media influence on risk-taking by retail investors, highlighting that *'investors can be influenced to invest without the objective and/or fundamental grounds on which an investment decision is normally based'* and links this influence to social media. Indeed, firms are increasingly engaging with influencers to reach a wider range of potential investors.
72. Finally, some of these trading platforms use so-called *'zero-commission trading'* to attract investors, which can give the impression that the services provided are free of charge. In that respect, ESMA reminds *'zero-commission'* brokers of the MiFID II⁹⁰ requirements to provide fair, clear and not misleading information to their clients and to provide information on all costs and charges to the client relating to the service and the financial instrument(s).⁹¹

Fund distribution platforms

⁸⁴ For a more detailed overview of *'self-directed investors'*, please see the survey conducted for the UK Financial Conduct Authority: BritainThinks (2021), [Understanding self-directed investors, A summary report of research conducted for The Financial Conduct Authority](#).

⁸⁵ Ibid, p. 9.

⁸⁶ BritainThinks (2021): the study comprised 517 consumers.

⁸⁷ YouTube, social media, including but not restricted to Instagram, Twitter, TikTok, Influencers/bloggers/vloggers on social media and YouTube, Investing podcasts, Reddit or other forums or blogs.

⁸⁸ BritainThinks (2021).

⁸⁹ AFM (2021), ["Investing and social media in light of GameStop"](#), AFM Market Watch, Newsletter on MAR, MiFID II and transaction reporting, June 2021, Edition 3.

⁹⁰ Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61/EU, OJ L 173, 12/06/2014.

⁹¹ Indeed, clients of *'zero-commission brokers'* will always incur costs (e.g., implicit costs and third-party payments received by the firm): ESMA emphasises that the marketing of the service as *'cost-free'* will infringe the firm's compliance with MiFID requirements. It could also incentivise retail investors' gaming or speculative behaviour due to the incorrect perception that trading is free, see in that respect ESMA (2021e), [ESMA warns firms and investors about risks arising from payment for order flow and from certain practices by "zero-commission brokers"](#), Public statement, ESMA35-43-2749, 13 July.

73. In the asset management sector, digital platforms offering third-party distribution of investment fund products continue to grow. Assets under administration (AuA) at fund distribution platforms in the EU totalled EUR 2.8 tn at the end of 2020, representing a growth of almost 15% in one year.⁹² By way of comparison, assets under management in UCIT funds grew by 5.4% over the same period.⁹³ According to a 2020 survey, 85% of market participants expect the assets supported on fund distribution platforms to increase over the next three years, and 30% even expect a ‘large increase’.⁹⁴ There is also a shift in the range of services provided from a mere intermediary function to a wider set of services, including trade execution, custody, corporate action processing, reporting, compliance and so-called value-added services, such as the provision of data analytics.
74. The market for fund distribution platforms is highly concentrated, with four main B2B⁹⁵ platforms dominating and serving different geographical regions across the EU. One platform alone has a 61% market share. The other three are similar in size, with a 10%, 14% and 15% market share each.⁹⁶ These B2B platforms, which do not interact with end investors directly, typically operate under a MiFID II license and do not undertake fund marketing activities. However, we may expect direct-to-consumer platforms, which are still small in the EU, especially compared to the US and the UK, to gain momentum going forward. It also seems that new actors, outside the financial sector, are forming partnerships with regulated actors to offer fund distribution platform business models with a B2C⁹⁷ component.
75. The phenomenon deserves monitoring as it may have implications for investor protection. In particular, respondents to ESMA’s call for evidence⁹⁸ have reported an increase and a lack of transparency in the fees charged by fund distribution platforms to asset managers, which could in turn affect the cost of investing in funds for end users.

Platforms offering robo-advice

76. Robo-advisors are automated financial advice tools used by consumers to receive advice about the purchase or sale of a financial product or service, with limited to zero staff interaction. Robo-advisors are not new but have grown in size and expanded their service offer over recent years. They offer either fully automated or partly automated processes and their services range from portfolio optimisation through rebalancing to investment selection and retirement planning.⁹⁹
77. Robo-advisors managed client assets of USD 987 bn in 2020 globally, with forecasts suggesting that this figure will increase to USD 1.4 tn in 2021 and USD 2.9 tn in 2025.¹⁰⁰ Figures in Europe remain comparably small, with about EUR 140 bn AuM in 2021 and annual growth estimates of

⁹² Platforium (2021), [Platforms May 2021, European Fund Distribution](#).

⁹³ EFAMA (2021), [Fact Book 2021, Trends in European Investments Funds](#), 19th edition, July.

⁹⁴ Funds Europe (2020), [The global fund distribution ecosystem – The evolution of platform services](#), Survey-based report, Clearstream website.

⁹⁵ Business-to-Business.

⁹⁶ The market share calculation is based on the respective assets under administration reported by these platforms on their official webpages respectively.

⁹⁷ Business-to-Customer.

⁹⁸ See ESMA (2021d) and the [responses to the Call for evidence on Digital Finance](#), available on ESMA website.

⁹⁹ The conceptualisation used for this note is based on the Joint Committee (2015), [Discussion Paper on automation in financial advice](#), JC/2015/080.

¹⁰⁰ Statista (2021c), [Robo-Advisors – Worldwide](#), in [Statista Market Forecast](#).

21% on average over the next four years.¹⁰¹ In the EU, Italy is leading with EUR 13.5 bn AuM¹⁰², followed by France with EUR 11 bn, and Germany with EUR 8.6 bn in 2020 respectively. The number of users in Europe stood at approximately 20 m in 2020.¹⁰³

78. The Joint Committee already conducted substantial work on the topic in 2015, 2016 and 2018 respectively.¹⁰⁴ Additionally, a monitoring exercise performed by ESMA in cooperation with NCAs in 2018 confirmed that the EU market in ‘automation in financial advice’ is growing but at a slow pace. The exercise has also highlighted differences in developments across jurisdictions and across sectors, with the investment services sector as the main area of application of robo-advice. As part of its ongoing work on the Commission’s requests for technical advice relating to retail investor protection aspects, ESMA will perform further analysis on the use and impacts of robo-advisors.

1.3 Groups combining different activities

79. A clarification of the notion of mixed activity group (or MAG) is needed to grasp the scope of the analysis. ‘**Mixed activity group**’ means a group of undertakings (a parent undertaking and its subsidiary undertakings) conducting both financial and non-financial services, for instance a group active in verticals such as cloud, advertising, business software, gaming, food delivery, ride-hailing, streaming combining them with insurance, payments, banking and other financial services.
80. For the purposes of this work, the ESAs have focused on **technology-enabled MAGs** to capture the significance of data and technology on their business models. Groups combining different activities and more specifically BigTechs (‘large technology companies with extensive customer networks; it includes firms with core businesses in social media, internet search, software, online retail and telecoms’¹⁰⁵ (FSB 2020b)) are providing financial services in parallel to other business lines, and this incorporation of financial services (in all financial sectors – banking and payments, insurance, and investment) within their own ecosystems and value propositions has been observed across several jurisdictions, including the EU, and is accelerating.
81. To understand the extent and scale of the MAG footprint in the finance sectors, a look at their global activities is required. Most of the finance markets they have penetrated to date are located in third-country jurisdictions i.e. outside the EU, with these companies concentrating their activities mainly in North America, China, India or Latin America.¹⁰⁶ In these regions, they have brought to the market new value propositions and are mostly active as direct competitors to incumbent financial institutions. Depending on their strategic positioning and partnerships with financial institutions, MAGs can opt for two options. They can either chose to introduce financial products and services outside traditional financial and banking networks, as is practically always the case in emerging markets and developing economies; for instance,

¹⁰¹ Statista (2021d), *Robo-Advisors – Europe*, in [Statista Market Forecast](#).

¹⁰² Assets under Management.

¹⁰³ Better Finance (2020), *Robo-Advice: Can consumers trust robots?*, *Robo-advice Report, 2020 Edition*.

¹⁰⁴ Joint Committee of the ESAs (2016), [Report on automation in financial advice](#), EBA/BS/2016/422 (JC SC CPFI Final Report on automated advice tools); Joint Committee of the ESAs (2018), [Report on the results of the monitoring exercise on ‘automation in financial advice’](#), JC/2018/29.

¹⁰⁵ FSB (2020b), [BigTech Firms in Finance in Emerging Market and Developing Economies; Market developments and potential financial stability implications](#), p.2.

¹⁰⁶ Ibid, pp. 4, 7.

Tencent is active accordingly in retail payments via Tenpay, credit and current account provision via WeBank, asset management via LiCaitong and insurance via Shuidihuzhu, all launched outside the traditional finance system, exploiting market niches. On the other hand, MAGs can also operate overlays on top of, or work in collaboration with, existing financial institutions, most notably banks: Amazon opted for the latter when expanding into financial services with Amazon Pay (payments), Amazon Lending and Amazon Protect (Insurance).¹⁰⁷ Other notable examples include Google Pay and Apple Pay.¹⁰⁸

Figure 2: Global footprint of selected MAGs worldwide

HQ	MAG	Main business	Current accounts	Credit provision	Payments	Crowdfunding	Asset management	Insurance
US	Alphabet (Google)	Internet search/advertising	x	x	x			
US	Amazon	E-commerce/online retail		x	x	x		x
US	Facebook	Social media/advertising		x	x			
US	Apple	Tech/producing hardware			x			
US	Microsoft	Tech/producing hardware			x			
CN	Alibaba (Ant Group)	E-commerce/online retail	x	x	x	x	x	x
CN	Tencent	Tech/gaming and messaging	x	x	x	x	x	x
CN	Baidu (Du Xiaoman)	Internet search/advertising	x	x	x	x	x	x
CN	JD.com (JD Digits)	E-commerce/online retail	x	x	x	x	x	x
JP	NTT Docomo	Mobile communications	x	x	x	x		
JP	Rakuten	E-commerce/online retail	x		x		x	x
AR	Mercado Libre	E-commerce/online retail		x	x		x	
UK	Vodafone	Mobile communications		x	x			
KR	Samsung	Tech/producing hardware			x			

Source: EBA, EIOPA, ESMA, FSB (2019b), Padilla, J. and Trento, S. (2019)¹⁰⁹, FSI (2021)¹¹⁰.

82. Some MAGs have even achieved **market leadership** (in the context of the provision of financial services) in some jurisdictions. For instance, Amazon, Google, WhatsApp (Meta (formerly Facebook) group) are active participants on India's real-time payments network Unified Payments Interface (UPI), both PhonePe (Walmart) and Google Pay corner over 79% of UPI's transaction volume, representing over 1.8 billion transactions¹¹¹; this led the National Payments Corp of India to introduce market share-capping guidelines for third-party app providers on UPI in an effort to combat monopoly and competition risks.¹¹² However, UPI apps or third-party app providers, such as Google Pay, PhonePe or Amazon Pay, are treated as third-party intermediaries and not as licensed payment system providers. They are barred from managing customer funds as they are not directly regulated by the Royal Bank of India, their role being to facilitate transactions on UPI.

¹⁰⁷ FSB (2019b), *BigTech in finance; Market developments and potential financial stability implications*, p. 10.

¹⁰⁸ See further EBA (2021e), *Report on the use of digital platforms*, Text Boxes 1 and 2, pp. 25-27.

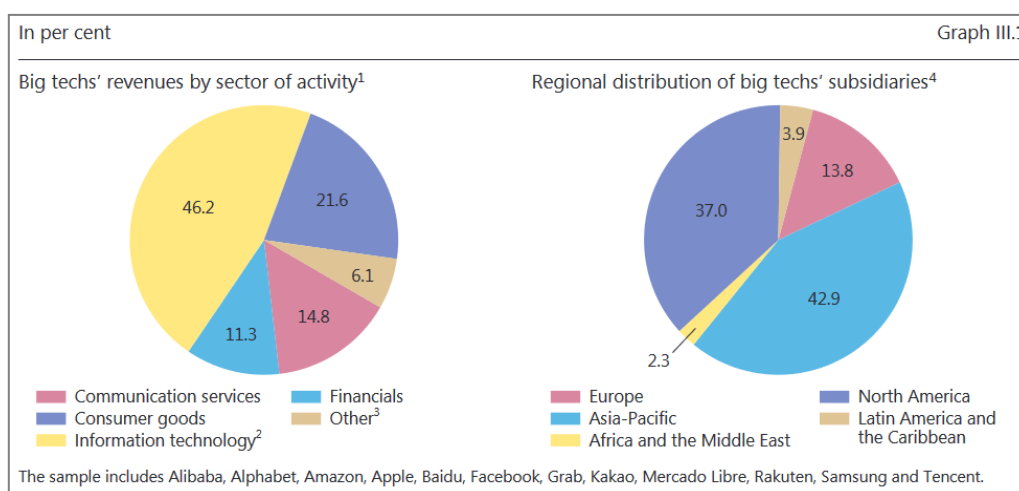
¹⁰⁹ Padilla, J. and Trento, S. (2019), *"No barbarians at the gate? The relatively slow progress of Big Techs in EU and US retail banking"*, *Concurrences*, Vol. 4, 2019, pp. 42-43.

¹¹⁰ Crisanto, J. C., Ehrentraud, J. and Fabian, M. (2021), *Big techs in finance: regulatory approaches and policy options*, FSI Briefs No 12, March, p. 3.

¹¹¹ *The Economic Times* (2021), *"NPCI caps market share for UPI apps at 30% of overall payment volumes"*, 26 March.

¹¹² The National Payments Corp of India (NPCI) — a Royal Bank of India regulated entity, which owns UPI — introduced in November 2020 market share-capping guidelines for third-party app providers on UPI, where no single company could have a volume exposure greater than 30% in any given quarter from 2022 on; <https://www.npci.org.in/PDF/npci/upi/circular/2020/OC-97-Guidelines-for-TPAPs-in-UPI.pdf>.

Figure 3: The share of financial services in big tech business



Source: BIS (2019).

83. When looking at most of MAGs' consolidated revenues distribution on the chart above (left-hand side), the share of financial services amongst their global activities remains relatively small (11.3%)¹¹³ compared to their core business verticals; however it has been constantly increasing over the past few years, showing the appetite of BigTechs to penetrate new markets with a view to enhancing their value propositions.¹¹⁴
84. The financial services-related activities operated by the largest third-country MAGs¹¹⁵ in Europe may not appear at this stage as significant as other markets. In 2019, only 14% of their subsidiaries were active in Europe¹¹⁶ and the MAG footprint in the EU finance markets has been more limited.
85. Technology firms have historically and primarily been active in the EU market as ICT providers to financial institutions (e.g. as third-party service providers, and fall within the scope of the DORA legislative proposal); aside from their core business of tech services like cloud services, they have penetrated selected financial sector market segments, such as retail payments, via the provision of infrastructure as the interface between financial institutions and end users. Overall, only a limited number of BigTech group companies are currently holding licences to carry out financial services activities in the EU, with eight known to have subsidiary companies carrying out regulated financial services.¹¹⁷ In the EU insurance and securities markets, the presence of BigTechs is even more scarce, with only a handful of players having launched

¹¹³ BIS (2019), "[Big tech in finance: opportunities and risks](#)", in *BIS Annual Economic Report 2019*, Chapter III, Graph III.1, left-hand side, p. 56.

¹¹⁴ BIS (2021a), "[Fintech and the digital transformation of financial services: implications for market structure and public policy](#)", BIS Papers No. 117, July, pp. 23-24.

¹¹⁵ The sample studied by the BIS comprised the following mixed activity groups (referred to in the study as "Big techs"): Alibaba, Alphabet (Google), Amazon, Apple, Baidu, Facebook (now Meta), Grab, Kakao, Mercado Libre, Rakuten, Samsung and Tencent.

¹¹⁶ BIS (2019), Graph III.1, right-hand side, p. 56.

¹¹⁷ EBA data gathered to inform the EBA's September 2021 report on digital platforms.

specific products¹¹⁸. It is to be noted that non-bank lending will be addressed in a separate EBA report.¹¹⁹

86. Several reasons may account for a more limited presence of MAGs in the EU financial sector in comparison to other regions to date, among which:
- a. regulatory requirements: it could be said that BigTechs have steered away from more heavily regulated sectors (e.g. due to capital and other requirements that can have cost implications in terms of compliance);
 - b. already low margins across some financial products and services, and therefore low profitability ratios, are not that attractive compared to some jurisdictions outside of the EU where margins are substantially higher due to more limited competition with the relevant sectors;
 - c. the EU financial markets, notably the sector for retail banking products and services, being highly competitive compared to lower levels of online banking penetration in other markets, such as China, India or Brazil¹²⁰;
 - d. socio-demographic differences and consumer preferences, as EU consumers still place a lot of trust in incumbents¹²¹, although the newer generations, grown more familiar with MAG's services and products, may have different inclinations, and a generational gap in the access and use of digital services may be observed;
 - e. insurance risk & data: although BigTechs, FinTechs and InsurTechs are often best placed to provide digital capabilities such as AI, data and analytics, they do not (yet) have the know-how of insurance risks and historical data of insurers to independently monetise their digital capabilities. The unavailability of historical data hinders appropriate pricing and underwriting practices. It may however be overcome, as data is available in the market and can be bought.
87. Market entry, also for the other financial products/services, and potential scaling is possible, given BigTechs' capability to leverage technology, data and large customer bases. The market capitalisation of the bigger MAGs is significantly higher than that of the bigger financial conglomerates and Global Systemically Important Banks (G-SIBs).¹²² Moreover, MAGs' capital and liquidity ratios and funding structures may be relevant to put in parallel with those of financial entities, as a dynamic of liquidity hoarding due to a hyperconservative allocation of free cash flow has been for instance observed with US MAGs.¹²³ Monitoring MAGs is necessary not only due to the interconnectedness risk with the finance sector, but also for their potential to undermine financial stability.¹²⁴

¹¹⁸ International Banking Federation and Oliver Wyman (2020), [Big banks, bigger techs? How policy-makers could respond to a probable discontinuity](#), July, p. 19; BIS (2019), pp. 57, 59-60; Crisanto, J. C., et al. (2021), p. 3.

¹¹⁹ See Chapter 4.1 of the CfA (non-bank lending). The EBA is mandated to respond by end of March 2022.

¹²⁰ Statista (2021a), [Ranking of the online banking penetration by country 2020](#), Graph, 25 May.

¹²¹ BIS (2021a), "Impact on financial services providers" in Section 3.3, p. 20; Carstens, A., Claessens, S., Restoy, F. and Shin, H. S. (2021), [Regulating big techs in finance](#), BIS Bulletin No 45, 02 August, Graph 2, p. 6.

¹²² Frost, J., Gambacorta, L., Huang, Y., Shin, H. S. and Zbinden, P. (2019), [BigTech and the changing structure of financial intermediation](#), BIS Working Papers No 779, April, Figure 1, p. 22; FSB (2020b), Graph 2, p. 7, IBFED and Oliver Wyman (2020), p.16.

¹²³ See Michon, A., Hyppolite, P.-A. (2018), [Les géants du numérique \(1\) : magnats de la finance](#), November.

¹²⁴ FSB (2019b), pp. 23-26; Crisanto, J. C., Ehrentraud, J. and Fabian, M. (2021), pp. 9-10, 12; BIS (2019), p. 55; BIS (2021a), p. 41; Padilla, J. (2020), *Big Tech 'Banks', Financial Stability and Regulation*, 20 April, pp. 8-9.

88. Additionally, BigTechs can leverage their strength in, for instance, the social media industry into the regulated markets. China's biggest tech companies, for example, are diving into the business of insuring motor vehicle accident damage, using insurance undertakings as suppliers. They use artificial intelligence to provide protection against car accidents; although this may seem marginal to financial services, it is the vanguard for China's 'TechFin' companies to reshape insurance, investments and banking in their image.
89. The entrance does not always have to be direct and disruptive. It could be performed through collaborative strategies. These collaborative strategies might allow for lower entry costs, as the traditional regulated company has amongst others practices and policies in place to ensure compliance with the regulatory requirements. The start-up could act as a service provider for an insurer. This is a quite common business model and allows the InsurTech and the insurer, for instance, to focus on their respective strengths in technology and insurance. Additionally, it allows the InsurTech to benefit from the scale, know-how and data from the insurance undertaking.
90. Within an existing group, the availability of new technological solutions might induce (insurance) undertakings to use companies dedicated to an innovative project (e.g. applications of cyber security, IoT, ICT applied to Health) in order to foster speed and flexibility. Alternatively, insurance companies cooperate with or acquire participations in existing 'FinTech' companies to benefit from the digital know-how and capabilities of those parties. In general, although country differences exist, NCAs did not report a significant increase in complexity so far, but they do see the potential for this.

Box 2: Wirecard

Wirecard has been at the centre of an international financial scandal and subject to various allegations since its announcement in June 2020 that EUR 1.9 bn were missing from its escrow accounts. The case effectively demonstrates that the provision of financial services by large technology groups with a complex structure and involvement of third parties outside the EU poses specific risks and challenges for financial supervisors.

Wirecard described itself at the time as a financial institution and a global technology firm providing online payments processing services and linking merchants, banks, and customers. The group has experienced exponential growth and entered the German DAX 30 index in September 2018, becoming one of the largest financial services providers with a valuation of EUR 20.7 bn (as of January 2019). Wirecard processed payments for 250;000 merchants including Aldi and Lidl, two of Germany's biggest retailers, and numerous airlines.¹²⁵ It expanded internationally into Singapore, New Zealand, Australia, South Africa, Turkey, the US and China.

As a company involved in payment process and transaction flow between merchants and customers, Wirecard provided both issuing and acquiring banking services.¹²⁶ The Wirecard Bank, a financial subsidiary of Wirecard group holding a German banking license, provided financial services and was active primarily in the acquiring business in Germany. However, according to Wirecard, neither Wirecard Bank nor any other affiliate in Wirecard group outside the EU had the necessary licenses to

¹²⁵ *The Economist* (2019), "Germany's regulator bans short-selling in Wirecard", 23 February.

¹²⁶ The terms *acquiring* and *issuing* refer to where the banks are in the transaction flow: the acquiring bank is the bank on the merchant end of the transaction (collects and processes card payments on behalf of retailers, merchants or businesses), and the issuing bank is the cardholder or consumer's bank (provides credit and debit cards to customers).

operate the acquiring business and therefore, Wirecard relied on so-called ‘acquiring partners’ (or ‘third-party acquiring partners’), of which the largest three were in Dubai, Singapore and the Philippines. According to some allegations, the revenues of these partners were funnelled into three subsidiaries of Wirecard group (in UAE, Ireland and Germany). Both financial losses and profits of the third-party acquiring partners were accounted for and consolidated as Wirecard losses and profits.

In June 2020, ESMA was mandated by the European Commission to conduct a fact-finding analysis of the events leading up to the collapse of Wirecard AG. In November 2020, ESMA prepared a report in response to this request (‘ESMA Report’)¹²⁷ focusing on the enforcement of financial reporting by German financial reporting enforcement authorities and reflecting the results of ESMA’s fast-track peer review.

While the allegations against Wirecard included malpractices in relation to various issues, including accounting and financial reporting, market integrity (e.g. dissemination of misleading information), short-selling and corporate governance, the ESMA review focused exclusively on assessing the effectiveness of the supervisory system in relation to the Transparency Directive (TD) and more specifically on the application of the Guidelines of the Enforcement of Financial Information (GLEFI) by the national German supervisors (FREP and BaFin).

The ESMA Report provided a description of the Wirecard case and outlined the key allegations against Wirecard. The ESMA Report then analysed the compliance of BaFin and FREP practices with the GLEFI, assessed the effectiveness of the German two-tier supervisory system for financial reporting in the specific context of the Wirecard case, and provided recommendations to address these shortcomings. Overall the ESMA Report highlighted the importance of high-quality financial reporting and effective enforcement of that reporting across the EU.

More broadly, the Wirecard case demonstrated, *inter alia*, that complex arrangements within a group providing both financial and non-financial services with presumably blurred lines between these activities, create specific challenges for supervisors, also considering the lack of visibility on the group’s business model and its activities outside the EU. The case also demonstrated the need for better cooperation arrangements for national authorities and with non-EU authorities, with a view to enhancing the supervision of digitalised group business models (e.g. at some point the Singapore authorities were ‘looking into’ the matter, and a subsidiary of the Wirecard group held an e-money license from the UK Financial Conduct Authority).

Wider supervisory implications of the Wirecard case are discussed in a special study prepared in November 2020 by the Economic Governance Support Unit at the request of the ECON Committee¹²⁸. The report highlighted weaknesses of market and oversight in Germany and in Europe and proposed suggestions on its improvements, such as strengthening the mandatory competencies granted to NCAs under the Transparency Directive and even creating a single, responsible market oversight institution at the European level, which may be called the European Single Capital Market Supervisor.

¹²⁷ ESMA (2020), [Fast track peer review on the application of the Guidelines on Enforcement of Financial Information \(ESMA/2014/1293\) by BaFin and FREP in the context of Wirecard](#), ESMA42-111-5349, 03 November.

¹²⁸ European Parliament (2020), [“What are the wider supervisory implications of the Wirecard case?”](#), Report of the Economic Governance Support Unit, October.

2 Opportunities and risks

91. The aforementioned trends and market developments bring a host of opportunities but risks as well for both users and providers of financial services. Risks and opportunities highlighted in this chapter are often not new but accelerating in digitalisation context. Often they can be also related to digitalisation developments in general. Additionally, the potential opportunities and risks are mixed and dependent upon specific different business models, partners involved, components of the value chain concerned and risk management and governance. The ESAs continue to monitor the application of innovative technologies in the EU financial sector as part of their ongoing and future work, including relating to the appropriateness of the EU regulatory perimeter.¹²⁹

2.1 Opportunities

92. The increasing digitalisation of financial services enhances **convenience for users** by facilitating seamless, 'real-time' 24/7 access to financial products and services, including cross-border, without the need for physical presence. Through digital means, consumers are better able to identify and compare a wider range of financial products and services. They can conclude and administer contracts for financial products and services online more easily and quickly. For instance, digitalisation often allows consumers to sign contracts within a short time-frame and without the need to seek a physical branch location, thus enabling a comparably wider range of the population to conveniently access financial products and services. Consumers may also feel more comfortable engaging with financial institutions less formally and value information provided through more user-friendly digital formats, or via non-traditional channels and sources. For example, the growing trend to seek information from 'like-minded' peers on social media and trends, such as social and copy trading, illustrates the rising demand for a democratisation of investing. Some digital platforms operated by financial or non-financial institutions also bring together a broad range of financial and non-financial products, effectively acting as a convenient 'one-stop' shop for consumers.
93. From a provider's perspective, digital means and innovative technologies can **help more efficiently bridge the demand for and supply** of financial products and services, including across borders. The use of digital distribution channels can allow firms to develop and distribute their products and services to a wider consumer base, potentially faster and at a lower cost, in turn reducing barriers to entry and time to market for new products, and fostering financial innovation. Leveraging on the wide range of consumer data made available through digitalisation and advanced data analytics techniques, such as big data, machine learning, and AI, financial institutions may be capable of better understanding consumers' needs and preferences and customising their marketing approaches and products accordingly, thereby boosting personalisation of financial products and services. Digital means can also facilitate quicker interactions with consumers, including on a one-to-one basis.
94. Similarly, digitalisation and the growing fragmentation of financial value chains that goes with it can enhance **efficiency and flexibility** at financial firms. For example, the outsourcing of in-house data centres to cloud services providers has generated significant cost savings for financial institutions. Business partnerships between specialised or niche financial technology

¹²⁹ For example, the ESAs are continuing to monitor crypto-asset market developments, including the increasing use of so-called decentralised finance (DeFi) and the increasing emergence of decentralised autonomous organisations (DAOs), and AI/Machine Learning use cases in financial services.

providers, including FinTechs, and incumbents can help streamline internal processes or enhance fraud detection and management of risks.

95. In some cases, regulatory developments have also played a major role in fostering competition and as a result innovation, as evidenced by the PSD2 in payments. There is also potential for open insurance, possibly enabling consumers to better compare offerings and switch providers, increasing sector efficiencies and facilitating supervision through more effective and responsive oversight capabilities.¹³⁰ The new opportunities brought up by open architectures and open finance promote both innovation and competition, which can be facilitated for instance by third-party data sharing, use of big data and advanced analytics.
96. All this combined can help foster **greater competition** and an **enhanced Single Market** (e.g. through facilitating cross-border business) for financial services, with beneficial outcomes for users of financial services, both in terms of quality of products and services, enhanced personalisation, seamless experience and potentially costs. Greater convenience for users and lower costs can also help bring higher levels of **financial inclusion**.
97. MAGs have shown that they are able to perform effective creditworthiness assessments and to screen and monitor borrowers' activity leveraging on their consumer data, thereby reducing the need for collateral¹³¹ and potentially facilitating financial inclusion of underbanked consumers and businesses, in particular small and medium-sized enterprises. Similarly, leveraging on data analytics, insurance undertakings can perform more granular risk assessments, which can improve financial inclusion for some high-risk consumers who previously could not access affordable coverage.¹³²

2.2 Risks

98. Notwithstanding the opportunities identified above, the increased digitalisation of financial services also brings about certain risks.

Risks to operational resilience

99. The increased digitalisation of financial services can exacerbate certain ICT and cyber risks and risks in relation to the operational resilience and business continuity of financial entities, especially considering their growing exposure to and dependency on third-party service providers, including unregulated ones, and in cases where the management of third-party and intragroup outsourcing at institutional level lacks robustness¹³³. In the case of MAGs, risks arising from 'core' technological activities may affect the overall value chain, including the provision of financial services. Besides, the rapid growth of platform infrastructures, which typically collect and store vast amounts of personal and financial consumer data, has made digital platforms an attractive target for cyber-attacks.

¹³⁰ EIOPA (2021a), *Discussion Paper on Open Insurance*.

¹³¹ BIS (2019), pp. 65-67.

¹³² See EIOPA (2019b), *Big Data Analytics in motor and health insurance*; EIOPA (2021d), [Artificial Intelligence Governance Practices: Towards ethical and trustworthy artificial intelligence in the European insurance sector; A report from EIOPA's Consultative Expert Group on Digital Ethics in insurance](#), June.

¹³³ E.g. in contractual arrangements, risk identification, risk mitigation frameworks or processes, risk management and risk monitoring.

Risks to consumers

Insufficient disclosures of features and risks

100. In order for consumers to make informed decisions about financial products and services, they must have access to high-quality, clear and easily accessible information that is provided at the appropriate time, via suitable means, and that explains the features and costs across the lifetime of the products and services. This applies to financial products and services that are marketed and/or sold at a physical meeting between the consumer and provider/intermediary, but even more when they are not interacting with each other in the same physical location (i.e. 'distance marketing').
101. Significant work conducted by the ESAs in recent years has highlighted the risk of consumers' poor product understanding due to insufficient information and disclosures, for example in the context of the fragmentation of the insurance value chain and new business models arising from digitalisation¹³⁴ or where the use of digital platforms for the provision, marketing or distribution of banking, payment, investment and insurance services exacerbates the risk of insufficient disclosures.
102. Such inadequate disclosures include for example:
 - a. presentation and format which do not allow easy access to the necessary pre-contractual information;
 - b. product/service terms and conditions;
 - c. the name of the contracting party;
 - d. the applicable complaint-handling mechanisms and redress schemes;
 - e. the applicable deposit/investor protection scheme (if any).
103. Furthermore, customers may face challenges in understanding the business model under which a digital platform operates and there is a lack of clarity about the nature of the services provided by these players, including regarding the pricing structure, the use of customer data.¹³⁵ These challenges can be exacerbated when services are provided cross-border, or for bundled products where the actual provider of each component and their responsibilities toward customers are not clearly stated.
104. Finally, digital disclosures may not always be effective in adequately disclosing relevant information due to technological impediments, difficulties in absorbing information via digital means, and certain consumer biases may be also more easily exploited online.¹³⁶

Risks linked to cross-cross-mis-selling, focusing on tying/bundling of products

105. Cross-selling occurs where a firm groups together one or more products or services and sells them to customers as a distinct package. Such practice is related but also somewhat distinct

¹³⁴ EIOPA (2021c), *(Re)insurance value chain and new business models arising from digitalisation: Feedback statement to the Discussion Paper*.

¹³⁵ For example, the platform provider or third party leveraging the platform to distribute financial products and services may unilaterally terminate the arrangement with the effect of denying customer access.

¹³⁶ For example, providers of financial products and services on their websites often pre-select or highlight their preferred selection, e.g. "accept all".

from tying¹³⁷¹³⁸ and bundling¹³⁹ practices. In today's competitive digital environment, cross-selling often materialises by companies offering additional products or services to target new customers or to retain them. Some products or services may be regulated financial services.

106. Whilst cross-selling may confer benefits for customers in the form of (initial) cost savings or a reduction in time and effort in searching for products, it can create risks as well.
107. For example, risks of cross-mis-selling may occur when digital platforms present to consumers products which may not be in their best interests. It could result in consumers purchasing products that they do not necessarily want, are unsuited to their needs, or they enter into a contractual agreement for a longer time horizon than needed (e.g. locked into the contract for a significant period of time). Additionally, over the lifetime of the product or service, a consumer can end up paying more for the package than he/she would have done, had he/she purchased the products separately. According to some NCAs, risk arising from up-selling¹⁴⁰ may also occur in the digital environment (e.g. a bank offers three different bank accounts (basic, salary and premium account). In the course of the selling process, the consumer is nudged into choosing the premium account although this account exceeds the needs of the customer).
108. In the digital environment, cross-mis-selling can also be observed for example in the context of digital platforms where a number of products or services may be offered in combination, to target new customers or to retain them, or in so-called 'embedded finance' when financial services are 'embedded' into other products/services (e.g. the use of Banking-as-a-Service and API-driven banking and payments services to integrate financial services within other environments and ecosystems). Some products or services in the package may be regulated financial services, while others may not be; the products and services may be offered by the same firm, by firms forming part of the same group, and/or by different firms/groups.
109. Cross-mis-selling practices have also been identified as problematic regarding a number of insurance products: travel insurance, car insurance, payment protection insurance (PPI), credit card insurance, mobile phone insurance and other gadget insurance, etc.¹⁴¹ Discussions with NCAs also highlighted concerns that this practice may be increasing with bank channels exploring different avenues to generate fees (i.e., by also selling non-life products).
110. In general, cross-mis-selling can pose risks (notably by customers being sold unsuitable products), particularly in the event of:
 - a. poor quality disclosures of product fees, terms and conditions and comparisons due to lack of transparency;
 - b. poor product oversight and governance, including inadequate product approval and testing processes;

¹³⁷ Some Member States have introduced stricter rules on tying and bundling.

¹³⁸ A tied package is a package of products and/or services where at least one of the products or services offered in the package is not available separately to the customer from the firm.

¹³⁹ A bundled package is a package of products and/or services where each of the products or services offered is available separately and where the consumer retains the choice to purchase each component of the package separately from the firm.

¹⁴⁰ Sales practice that encourages customers to purchase higher-end versions of that same product or pay for upgrades and extra features.

¹⁴¹ EIOPA's annual Consumer Trends Reports continue to highlight consumer detriment arising from tying and bundling financial products and aggressive sales practices. EIOPA has been further looking into cross-selling issues as part of its conduct supervision in EIOPA (2019c), [Consumer protection issues in travel insurance: a thematic review](#), October, and in its ongoing thematic review on credit protection insurance products sold via banks.

- c. the inability of consumers to limit, control or customise product search functions;
 - d. product bias linked to remuneration incentives/poor remuneration of sales staff;
 - e. differences in products leading to varying quality of professional financial advice;
 - f. limitation of products/services offered by the provider/platform.
111. Such cross mis-selling may result in potential consumer detriment, for example in situations where:
- a. the product purchased is unsuitable and does not meet the needs of the consumer;
 - b. decreased access to a whole range of products/services and providers on the market (e.g. certain commercial comparison websites that only show products of associated firms). The choice is (unduly) limited to products and services provided by certain providers/platforms only, thus consumers forgo the opportunity to buy more suitable products elsewhere;
 - c. in some cases, the consumer pays more for the package than they would have paid if they had purchased the products separately;
 - d. there is a negative effect on consumer confidence to shop around and make informed purchasing decisions in the digital environment;
 - e. the consumer enters into a contractual agreement for a longer time-horizon than needed for their personal needs.
112. In 2016, the ESAs attempted to mitigate the aforementioned risks by issuing Guidelines on cross-selling.¹⁴² However, due to the inconsistent legal provisions in the underlying EU Directives and Regulations (particularly in the banking sector), the ESAs to a large extent stopped the project and instead wrote a letter to the Commission highlighting the legal issues in Level 1 texts that would need to be addressed first¹⁴³ (see more in detail in Recommendation 2b).
113. To date, these issues remain unresolved and there is a risk that due to increased digitalisation, the scale of the issues will be widened.

Complaints handling and redress procedures

114. Consumers may also face challenges in delineating the functions and responsibilities of different parties within the digital platform ecosystem, such as distributors, and their respective rights and obligations vis-à-vis those parties, which in turn may result in end-users being uncertain about which provider they are contracting with or to whom they should address complaints or seek redress.¹⁴⁴
115. This risk is exacerbated in situations where financial services (and potentially other services) from a range of parties are marketed and/or distributed via the same platform. Indeed, the ESAs have noted the challenges in delineating regulated financial services (offered by financial institutions) and non-regulated financial products and services and the relevant measures for complaint handling and redress. These issues may be further exacerbated when financial services are provided cross-border via the freedom to provide services or the right of

¹⁴² ESMA (2015), *Final Report, Guidelines on cross-selling practices*, ESMA/2015/1861, 22 December; ESMA (2016), *Guidelines on cross-selling practices*, ESMA/2016/574, 11 July.

¹⁴³ The Consultation Paper that was published and the joint letter addressed to the Commission can be found under “Guidelines for cross-selling practices”, available at: <https://www.eba.europa.eu/regulation-and-policy/consumer-protection-and-financial-innovation/guidelines-for-cross-selling-practices>.

¹⁴⁴ See for example EIOPA (2021c), *(Re)insurance value chain and new business models arising from digitalisation: Feedback statement to the Discussion Paper*.

establishment, which in turn may raise issues as to which NCA is responsible for supervising compliance with the relevant complaint handling and redress procedures.

Risks of financial exclusion and risks of lack of digital financial literacy

116. While financial innovation in the context of value chain, platforms and MAGs can lower barriers and costs, it can also lead to greater financial exclusion, because access to digital channels and digital infrastructure is often a prerequisite for consumers to make use of digital services or distributions channels, and those digital offerings may become the norm going forward.
117. Such vulnerabilities can manifest themselves in different ways over time and may be exacerbated by digitalisation:
- groups of consumers with less access to, and experience with, the digital environment are increasingly vulnerable¹⁴⁵;
 - some vulnerable groups encounter difficulties when using digital channels, for instance when it comes to new security procedures such as the two-factor authentication for the access to payment accounts; some banks now require their customers to use a smartphone and have no confidence in the security of online and mobile banking when performing everyday transactions¹⁴⁶. In some cases, consumers are incited to use mobile phones or the internet to execute and authorise financial services, otherwise facing the risk that the offering of traditional services might not be as good as the level of digital services. Other consumers may simply not have access to the necessary infrastructure. A ‘fintech gender gap’ may also arise, as women are less likely to use fintech products or services offered by fintech entrants than men¹⁴⁷;
 - price optimisation practices of certain companies and certain types of contractual exclusions could lead to a lower level of financial inclusion, with some consumers not being able to afford or access certain financial products and services, e.g. insurance products.¹⁴⁸
118. The ESA’s analysis has shown that risks exist if increased access to online channels is not coupled with sufficient levels of digital and financial literacy at all stages of financial life and that, in its absence, certain population groups (which could involve people exposed to poverty, physical and mental health disabilities, people of a certain age, gender etc.) are more likely to be excluded from financial services.
119. Several stakeholders also noted the key relevance of digital financial literacy to promote a secure digital environment within the financial sector and to enhance consumer protection. Indeed, consumers with high digital financial literacy can, for example, make better decisions to mitigate security risks when using digital channels.

¹⁴⁵ OECD (2019), [Challenges to consumer policy in the digital age](#), Background Report, G20 International Conference on Consumer Policy, September.

¹⁴⁶ EBA (2021b), [Consumer trends report 2020/21](#), EBA/rep/2021/04, 10 March.

¹⁴⁷ Chen, S., Doerr, S., Frost, J., Gambacorta, L. and Shin, H. S. (2021), [The fintech gender gap](#), BIS Working Papers No 931, March.

¹⁴⁸ EIOPA (2019b), *Big Data Analytics in motor and health insurance*, and the forthcoming *Consumer Trends Report 2021* (forthcoming). EIOPA’s on-going work on exclusions shows that with the increase in more targeted product design, more and more insurers are introducing exclusions where the risks of bearing the costs could be too high – such as not insuring high-risk flooding areas – and this may leave consumers uninsured and as a consequence without access to other financial products and services.

120. Based on the feedback received from the EBA digital platforms report¹⁴⁹, NCAs noted the risk that consumers might not only be exposed to mis-selling practices, fraud risks and risks of over-indebtedness¹⁵⁰, but also to new risks such as misuse of personal financial data, digital profiling, cyber-crime or risks arising from overly complex digital assets and services etc. As such, they highlighted an even greater need to promote digital financial literacy and other digital skills, including cybersecurity risks, also through greater cooperation and coordination between different national authorities involved in consumer protection, financial literacy and financial education initiatives.

Risks in relation to the access and use of customer data

121. Financial institutions and third-party providers have been increasingly data-dependent and leveraged innovative tools, such as artificial intelligence and machine learning applications, to facilitate the marketing of products and services to customers and to carry out related processes such as credit/risk scoring or suitability assessments.
122. Risks arising from the access to and use of customer data include:
- a. inadequate or insufficient awareness among consumers of the value of their data for providers (e.g. health data collected from wearable devices).
 - b. ineffective mechanisms to support informed consent to the use of personal data taking into account General Data Protection Regulation¹⁵¹ requirements¹⁵²;
 - c. risks of mis-use and unlawful data access:
 - more granular consumer data combined with AI may increase the ability of undertakings to charge differential amounts to groups of consumers that are similar in terms of risk and cost to serve. Undertakings may be able to understand aspects such as consumers' price sensitivity and their likelihood to shop around and switch at point of renewal. The use of price optimisation practices can lead to potential unfair commercial treatment towards some groups of consumers. The use of new datasets can also lead to unlawful discrimination¹⁵³;

¹⁴⁹ EBA (2021e), *Report on the use of digital platforms*.

¹⁵⁰ As set out in EBA (2021b), *Consumer Trends Report 2020/21*, competent authorities have identified that there is a heightened risk of over-indebtedness as a result of the growing use of digital channels, including digital platforms, to provide and access credit. This could also be attributed, inter alia, to the fact that consumers' credit worthiness assessment may be conducted through automated processes that exacerbate behavioural biases and potentially lead to irresponsible lending decisions. It is also noted that the EBA is carrying out an assessment of non-bank lending activity under section 4.2 of the Call for Advice on Digital Finance. This requires the EBA to consider, among other things, whether the activities are appropriately regulated.

¹⁵¹ Regulation (EU) 679/2016 of the European Parliament and of the Council of 27 April 2016 on the protection of natural persons with regard to the processing of personal data and on the free movement of such data, and repealing Directive 95/46/EC, OJ L 119, 04/05/2016.

¹⁵² Noting that competent authorities within the meaning of the ESA's Founding Regulation are not typically authorities responsible for monitoring GDPR compliance in the Member States (typically Member States have appointed designated data protection authorities).

¹⁵³ New datasets can be closely correlated with protected characteristics such as race, religion, gender or political orientation. For example regarding bank account and credit card data, the purchase of certain pharmaceutical products can be highly correlated with gender. Therefore the use of new datasets, especially in combination with more powerful algorithms such as AI/Machine Learning to identify patterns in data, could increase the risks of unlawful discrimination if there are no adequate governance frameworks in place.

- the wider sharing of data with different parties raises the risks of a data breach, misuse and fraud, including obtaining unauthorised knowledge about facets of consumers' lives, including sensitive data concerning the consumer's health, location, or financial status. Data quality and how it would be measured and enforced might be another possible challenge in this regard. In addition, more openness in relation to the data gathered, processed and exchanged for insurance/financial services purposes could also increase ICT/cyber risks and API security risk, including opening leeway for malpractices, such as phishing or malware/ransomware (this is also linked to data breaches);
- financial crime, fraud or scams may be emphasised due to the increasing importance of dataset and the quantity of shared financial and non-financial data, especially if combined with AI/Machine Learning tools. The accuracy and reliability of external data sources can vary greatly, in particular taking into account that external data sources are often provided by entities that are not subject to regulatory oversight.

123. Risks arising from the access to and use of customer data could impact the supervision of financial products and services by supervisory authorities:

- a high degree of customisation of AI solutions may not always allow for traditional supervisory processes, and require new skills and expertise from supervisory authorities;
- automated decisions, based on complex AI algorithms, may be difficult for consumers and supervisors to understand and scrutinise, notably in relation to the risk of model bias and unlawful discrimination.¹⁵⁴

124. While the ESAs are not the relevant authorities for the purposes of the GDPR, it is worth noting that supervisory authorities face practical issues in relation to data protection when monitoring compliance with requirements imposed in EU financial services directives and regulation, for example where personal data is held and transmitted between various parties utilising a digital platform to market or distribute financial services.

Concerns arising by the provision of services on a cross-border basis through digital means

125. Several issues have been brought to the attention of the ESAs in the area of cross-border provision of services which might require further regulatory action. These issues are not new, but have been further highlighted due to the increased service provision through digital means and particularly through digital platforms. The 'depth' of the issues encountered may also depend on the regulatory frameworks applicable to each financial sector. The concerns identified relate to challenges faced by both financial firms and NCAs in determining whether a cross-border notification obligation is triggered when the service is provided through digital means. Visibility issues around the use of digital platforms to provide financial services on a cross-border basis were also identified by the ESAs.¹⁵⁵

¹⁵⁴ For example, even if the use of new technologies in credit or risk scoring tools may facilitate consumer access to loans or insurance, it may also lead to financial exclusion. If the algorithm was based on factors not directly related to insurance risks/pricing, suitability assessments or creditworthiness (i.e. there is no reasonable causal link) and they are correlated to protected characteristics (i.e. proxies), this could negatively affect conduct risk. In addition, these models raise concerns regarding the explainability and interpretability of their underlying algorithms. The subjects of automated decisions (consumers and businesses alike) are not always able to assess their correctness and appropriateness. This issue is amplified by the increasingly availability of new datasets and data sources in the digital economy.

¹⁵⁵ More detailed information in relation to these issues is outlined in chapter 3 under Recommendations 4 and 9.

Possible concentration and interconnectedness risks (dominant position of certain providers)

126. The dominance of certain providers in value chains raises potential concentration, interconnectedness, competition and systemic risk issues.
127. The widespread use of third-party providers can lead to concentration risk, where a large number of undertakings and intermediaries become dependent on a small number of dominant outsourcers or third-party service providers. This can undermine financial stability in cases of major incidents or failure of a partner. As some outsourcing partners or third-party providers (e.g., cloud providers and BigTech companies) are globally active, the concentration risks and other risks (e.g., risks related to personal data) further increase; furthermore, some critical infrastructure providers are providing services to systemically significant financial institutions, which could lead to interconnectedness risks and potential negative spill-over effects on the financial system. The fact that these providers may be unregulated may also create blind spots in terms of data, and hence assessment of the risks that they may represent.
128. A handful of players may acquire the leverage to impose conditions almost unilaterally on their contractual partners, which could be detrimental to smaller firms, possibly lead to a crowding-out of the market in the future and require firms to accept unfavourable conditions in terms of fees or contractual responsibilities and liabilities.
129. Additionally, 'lock-in' risks can arise, for instance when consumers become increasingly dependent on one provider's product range, with difficulties or without the possibility to switch to other providers, or where large providers acquire gatekeeper status which would make it difficult for smaller players to access the market or change provider.

New forms of ML/TF risks

130. New forms of ML/TF risks have emerged stemming from the lack of clarity regarding respective roles and responsibilities and possible inefficiencies of institutions' AML/CFT systems and controls. The EBA has observed that institutions frequently rely on third parties for Customer Due Diligence (CDD) purposes, outsource some or all aspects of their compliance tasks to external service providers, and are often unsure of the adequate safeguards to put in place. This is more evident in case of outsourcing and can result in the following issues:
 - a. **Fragmentation of the compliance value chain, with insufficient oversight, by institutions, of services provided by third parties or through outsourcing arrangements which impacts the holistic view of ML/TF risks:** evidence collected shows that when the value chains are not entirely controlled by the same institution, these relationships are not always adequately monitored and inherent operational challenges persist. The resulting dispersion of data and information through the various chains, and lack of an end-to-end view of the information and process, can lead to an ineffective overview of the customers' CDD file. At the same time, institutions' management of the different relationships can be weakened by the emergent complexity. This might impact institutions' ability to identify and assess ML/TF risks, including suspicious patterns of transactions, and take the measures necessary to mitigate those risks. As a consequence, their CDD measures might be applied inadequately.
 - b. **Data protection rules, or the perception and interpretation of data perception rules, limit effective information sharing:** it has been identified by this Call for Advice that the relied upon third parties or outsourced service providers, even where are obliged entities¹⁵⁶, often

¹⁵⁶ The range of entities defined as 'Obligated Entities' under current EU AML/CFT legislation and thus subject to EU AML/CFT rules.

misinterpret the data protection requirements that apply to their business relationship with the institutions. This is a result of data protection legislations which may contain perceived unclear provisions that pose difficulties for information sharing or for data retention.

131. In summary, these issues can be the result of either or a combination of the following root causes:
- a. Technological limits, which means that financial institutions cannot integrate information from value chains into their own systems;
 - b. Lack of access to complete data sets as a result of real or perceived legal obstacles, including data protection rules;
 - c. Insufficiently robust outsourcing safeguards;
 - d. Blind reliance on third parties for CDD purposes;
 - e. Lack of understanding of AML/CFT obligations;
 - f. Some services being provided by non-obliged entities.
132. As regards platforms and MAGs, this CfA identified that they might be abused for ML/TF purposes when they do not have adequate AML/CFT systems and controls in place.¹⁵⁷ The risk is increased by platforms' and MAGs' borderless nature and the complexity of the distribution channels, and can be a result of the following:
- a. Under the current AML Directive¹⁵⁸ (AMLD), not all digital platforms are *obliged entities*; the same applies to MAGs, as not all technology companies are *obliged entities*;
 - b. Where considered *obliged entities*, platform providers' as well as MAGs' understanding of AML/CFT obligations can often be considered as insufficiently developed, which hampers AML/CFT compliance efforts;
 - c. New complex business models emerging with digitalisation can present challenges for supervisors to remain updated and have a critical understanding of platforms' or MAGs' AML/CFT control systems. Some supervisors' understanding of the related ML/TF risks can be considered insufficiently mature in that respect;
 - d. Specifically for a MAG, certain parts of the group can run risks with impunity, as shown in the Wirecard case.¹⁵⁹

Risk to integrity of financial markets due to the growing interconnectedness with social media

133. The increasing use of social media, as outlined in **Box 1**, and its subsequent influence on consumers' financial decision-making processes, can pose several risks to consumer protection, the integrity of financial markets and possibly financial stability.
134. As consumers are increasingly seeking information about financial products, services and strategies on social media, they are exposed to a new risk source stemming from the intentional or negligent provision of inaccurate or misleading information, often by other, non-

¹⁵⁷ Certain platforms are known for the lack of, or weaker, compliance controls and therefore more likely to be used for illicit activity.

¹⁵⁸ Directive 2015/849/EU of the European Parliament and of the Council of 20 May 2015 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing, amending Regulation 648/2012 of the European Parliament and of the Council, and repealing Directive 2005/60/EC of the European Parliament and of the Council and Commission Directive 2006/70/EC, OJ L 141, 05/06/2015.

¹⁵⁹ See **Box 2** for further background.

sophisticated, retail consumers. This risk is exacerbated by the anonymity inherent to social media profiles and the network effects that these platforms can trigger. The increasing use of social media for fraudulent activities increases the risk to consumers of becoming subject to scams and maleficent intentions. Network effects by social media platforms are characterised by a rapid speed of information flow, often across different platforms. A key issue here results from the fact that the original piece of information is often altered in the process of this flow, e.g., through the addition of subjective interpretations of the content. Additionally, consumers may find it difficult to trace back the original source of information to verify its accuracy. Relatedly, the impact of *'finfluencers'* on consumer's financial decision-making may be detrimental to consumer protection, if consumers almost blindly follow any recommendations given by the influencer. This may be exacerbated in situations of mass-hype, where a large number of users follow the recommendations, triggering a 'fear of missing out' feeling within individual consumers. Further, the one-to-many conversation nature prevalent on social media makes it difficult for investors to assess if the information provided is suitable to his/her own personal and financial situation.

135. The provision of suggestions and recommendations via social media with the view to animate consumers and investors to make financial and investment decisions may border the scope of market manipulation.
136. The increased use of social media to provide information, sometimes bordering the scope of regulated financial advice, may also lead to an increase in disintermediation and fragmentation in the value chains, and traditional players may risk being crowded out of the market. In light of this, while noting that the use of social media in relation to financial services is already subject to a series of rules, further analysis of the applicability of the current regulatory framework is needed to avoid the risk of creating level playing field issues with advice provided through 'more traditional' channels.
137. In addition, the wide reach of social media platforms can foster increased risk taking, speculation and excessive herding behaviour by retail consumers with a possible spillover effect into financial markets in general. Depending on the impact and scope of the event, this can pose risks to the order and stability of financial markets, for example when the trade execution is impacted due to disruptions in financial market intermediaries, e.g., trading venues, or when the supply and demand equilibrium is substantially disrupted due to high spikes of volatility caused by unforeseen surges in, for example, meme-stock trading.
138. In the insurance area, ongoing behavioural research on insurance distribution and advertising via digital channels being carried out by EIOPA has found that some social media sponsored content appears as content shared by users, while in reality, they are ads that redirect to a third-party website, amounting to disguised ads.

3 Recommendations

139. In light of the market developments and opportunities and risks identified in the preceding chapters, the ESAs identify in this chapter a number of recommendations in order to ensure that the regulatory and supervisory framework remains fit-for-purpose in the digital age. These recommendations are cross-sectoral, except for two that are insurance-specific (see section 3.2 below). Also, while the recommendations are generally addressed to the Commission, Recommendations 9 and 10 are addressed to the ESAs.

3.1 Cross-sectoral

3.1.1 Recommendation 1: Need to consider a holistic approach to the regulation/supervision of fragmented value chains

Recommendation 1a: Consider potential issues in relation to the reliance by financial institutions on third-party providers that may not be addressed by the existing and upcoming rules.

The ESAs welcome the proposed DORA¹⁶⁰, which is an important initiative that will address the ICT risks in the financial services value chain. However, DORA is not intended to address other risks that may arise from the reliance of financial institutions on third-party providers.

The ESAs recommend that the Commission assess and subsequently address where necessary the non-ICT risks that may arise from the use of third-party providers by financial institutions and the growing intertwined relationships between technology companies and financial institutions, as outlined in Recommendations 2, 7, and 8.

Because these dependencies continue to evolve quickly in the digital context, the ESAs also highlight the need to re-assess through time, and after the application of DORA, whether providers of relevance to the financial sector are susceptible to fall outside of DORA's scope and pose significant risks to the financial system, and would therefore require a similar oversight framework in the event of giving rise to concentration (and potentially competition) issues.

140. With digitalisation, financial firms are increasingly relying on third-party providers, including technology companies (including BigTechs), for the provision of their services, through outsourcing or other types of arrangements. This fragmentation of financial value chains and the growing intertwined relationships between financial institutions and unregulated service providers can create a series of regulatory and supervisory challenges, also considering that these providers may not be specific to one financial sector but active in different financial and non-financial sectors and operating cross-border, including non-EU countries.

¹⁶⁰ See footnote 2.

141. Financial institutions are required to identify, assess and monitor the risks that arise from their reliance on third-party providers, as part of their general risk management framework. However, challenges may arise in this context, e.g., because certain providers impose their conditions on financial institutions and/or are not easily substitutable, possibly altering the way in which financial products and services are being provided and bringing new conduct risks. Similarly, financial supervisors may be limited in their assessment of the risks and exercise of supervisory powers on the entirety of the value chains, which may create an uneven playing field between fully integrated and fragmented value chains within the financial sector. There is also the potential for concentration and hence systemic risk in cases where different financial institutions, including across the different financial sectors, rely on the same service providers and these providers become instrumental to financial services. Indeed, some of these service providers could provide technology and other services (e.g. data analytics, advertising, and infrastructure services) at such scale toward the financial sector that they could be regarded as systemically important, but they may fall outside the regulatory perimeter of financial supervisors, save where providing services that are regulated financial services,¹⁶¹ or ICT services to the financial sector.
142. While NCAs usually address possible concentration risk within the scope of the regular supervisory review process (including through offsite and onsite inspections), continuous dialogue with financial institutions regarding their IT operations and management, as well as dialogue with major stakeholders in the FinTech/InsurTech sector, the existing tools may not suffice to effectively identify and deal with an increased concentration risk in the context of digital platforms and ecosystems. In contrast to planned critical or material outsourcings which are typically subject to a supervisory dialogue, financial institutions do not have specific requirements to notify other forms of cooperation arrangements to NCAs.
143. A prominent example of reliance of financial institutions on unregulated service providers is in the area of ICT services, including cloud computing where concentration risk is a particular concern, as a handful of firms dominate the market.¹⁶² The ESAs have issued guidelines to financial institutions and supervisors on the outsourcing to cloud service providers to help them identify, manage and monitor the risks arising from cloud outsourcing arrangements (see EBA Guidelines on outsourcing arrangements¹⁶³, which have incorporated the EBA Recommendations on outsourcing to cloud service providers¹⁶⁴, the EIOPA Guidelines on outsourcing to cloud service providers¹⁶⁵ and the ESMA Guidelines on outsourcing to cloud service providers¹⁶⁶).
144. More recently, the DORA legislative proposal¹⁶⁷ put forward by the Commission aims to strengthen and harmonise the digital operational resilience in the financial sector. It sets out requirements applicable to financial entities in respect of ICT risk management, increases supervisors' awareness of ICT risks and ICT-related incidents, and introduces new requirements for financial entities to carry out cybersecurity digital operational resilience testing. In addition,

¹⁶¹ It is noted that the ESAs conduct regular monitoring of the financial services regulatory perimeter to ensure it remains fit for purpose so that there is an appropriate degree of protection of consumers and to mitigate threats to the integrity and stability of the EU financial system.

¹⁶² See BIS (2021a), p. 35; FSB (2019a), p.16; and Scott, H., Gulliver J. and Nadler, H. (2019), pp. 12-14.

¹⁶³ EBA (2019), [EBA Guidelines on outsourcing arrangements](#), EBA/GL/2019/02, 25 February.

¹⁶⁴ EBA (2017b), [Recommendations on outsourcing to cloud service providers](#), EBA/REC/2017/03, 20 December.

¹⁶⁵ EIOPA (2020a), [Final Report on public consultation No. 19/270 on Guidelines on outsourcing to cloud service providers](#), EIOPA-BoS-20-002, 31 January.

¹⁶⁶ ESMA (2021c), [Guidelines on outsourcing to cloud service providers](#), ESMA50-164-4285, 15 May.

¹⁶⁷ See footnote 2.

DORA sets an oversight framework for critical ICT third-party services providers, with a view to managing the risks posed by the increasingly significant reliance of the regulated financial sectors on ICT third-party service providers.

145. DORA defines ICT services as ‘digital and data services provided through the ICT systems to one or more internal or external users, including provision of data, data entry, data storage, data processing and reporting services, data monitoring as well as data-based business and decision support services’, meaning that the type of ICT services falling within DORA’s scope is inherently broad.
146. Yet, additional issues in relation to the growing reliance of financial firms on third-party providers may require further consideration.
147. First, DORA’s focus on digital operational resilience, and in particular ICT risks, means that the proposal is not intended to address other types of risks that may arise from the growing reliance on (ICT and non-ICT alike) third-party providers by financial institutions. These other risks may arise, for instance, in the context of the use of digital platforms where consumers may not have a clear understanding of the functionalities and role of the platform and/or the complaints handling mechanisms is unclear. There may also be risks in relation to data, especially considering the growth of data-centric business models, e.g., in cases where these arrangements give technology companies unfair advantages in relation to the access and use of data due to the fact that they are unregulated; and more generally, the risk of an uneven playing field between MAGs and financial institutions. Proposed recommendations on possible ways to address these issues are highlighted in the rest of the recommendations, especially Recommendations 2, 7 and 8.
148. Second, some providers of relevance to the financial sector may fall outside of the oversight framework for critical ICT third-party providers provided by DORA (e.g., in cases where the services do not qualify as ICT services and/or the provider does not qualify as critical third-party provider under DORA). Considering that third-party dependencies continue to evolve quickly, the ESAs recognise the need to carry out a gap analysis, after the application of DORA. Examples of providers of relevance to the financial sector that may not be captured by DORA and require further consideration could include providers of certain post-trade services or certain third-party reporting providers for securities markets or providers of specific data or Internet of Things (IoT) devices in the insurance sector, as outlined below. Similarly, documentation requirements for those contractual arrangements that may not qualify as ICT contractual arrangements could require further consideration.

Third-party reporting providers

149. The European Markets Infrastructure Regulation¹⁶⁸ (EMIR) and Securities Financing Transactions Regulation¹⁶⁹ (SFTR) establish very broad reporting obligations. In most instances, the entities that are subject to these reporting obligations delegate their reporting to third-party reporting providers. Third-party reporting providers aggregate reporting flows from small and medium market participants and have emerged as key actors channelling supervisory data to trade repositories. Whereas the supervision of the entities with reporting obligation remains at national level, the third-party reporting providers are largely not supervised. Based on

¹⁶⁸ Regulation (EU) 648/2012 of the European Parliament and of the Council of 4 July 2012 on OTC derivatives, central counterparties and trade repositories, OJ L 201, 27/07/2012.

¹⁶⁹ Regulation (EU) 2015/2365 of the European Parliament and of the Council of 25 November 2015 on transparency of securities financing transactions and of reuse and amending Regulation (EU) 648/2012, OJ L 337, 23/12/2015.

ESMA's experience, an important portion of the data quality issues identified stem from incorrect implementation by third-party reporting providers. This is a similar situation to the one that was observed in the past with Authorised Reporting Mechanisms (ARMs) under MiFID.

150. The set-up of a regulatory and supervisory framework for third-party reporting providers under EMIR and SFTR (either under both regulations or in a self-standing regulation to cover broader activities of third-party reporting providers) would therefore require consideration. This regulatory and supervisory framework could be based on the current organisational requirements for data-reporting service providers. Given that third-party reporting providers are frequently part of integrated groups operating trading venues or providing other investment services, strict requirements on governance, adequate resources and on dealing with conflicts of interest would seem relevant as well.

OTC derivative post-trade services

151. The use of post-trade services (including affirmation, confirmation, compression, margin optimisation, margin call management, etc.) has increased significantly to a point where they may become of systemic importance themselves (for instance risk reduction activities by TriOptima are currently estimated at approx. EUR 1,500 trillion, i.e., more than the outstanding OTC derivative transactions globally). In addition, it is a very concentrated industry with only a few providers, and often one largely dominant provider within a segment. The market is therefore reliant on only a few providers, which are typically not regulated for the provision of risk reduction services, as these services are not usually considered as regulated financial services. Also, compression and margin optimisation are generally not performed by individual financial firms on a standalone basis raising questions as to whether they would fall within the definition of outsourced tasks at all.
152. A potential regulatory and supervisory framework for these services and/or their providers could look into the independence of these third-party service providers, the governance around the algorithms they use to run certain services (in particular post-trade risk reduction services), the operational and systemic risk they may introduce due to the significant volume of trades that they are processing and their concentration, and their handling of client or access requests. In this regard, IOSCO's planned work to assess the possible risks associated with market participants' use of risk reduction services, with particular focus on portfolio compression and counterparty risk optimisation services, operating in the OTC derivatives markets, is welcomed.

EIOPA specific recommendations

Recommendation 1b: Consider adequate minimum approach towards outsourcing in insurance and pensions sectoral rules.

The Commission should consider an adequate minimum approach towards outsourcing in insurance and pensions sectoral rules, including the need to incorporate general and proportionate outsourcing rules in the Insurance Distribution Directive clarifying the responsibility of the insurance intermediaries when outsourcing is used.

153. Outsourcing and risk management rules are the current regulatory and supervisory tool to ensure a proper risk management and monitoring of the third-party risk. DORA builds upon sectoral outsourcing rules. However, within the insurance and pensions sectors outsourcing rules vary:
- a. **Solvency II**¹⁷⁰ - Chapter IV of Solvency II provides for general conditions governing business, including rules on outsourcing, which are supplemented both by Level 2 and Level 3 measures. On top of risk management requirements, Art. 49(3) of Solvency II states that insurance and reinsurance undertakings ‘shall, in a timely manner, notify the NCAs prior to the outsourcing of critical or important functions or activities as well as of any subsequent material developments with respect to those functions or activities’. This covers only the outsourcing of critical or important functions or activities.¹⁷¹
 - b. **EIOPA Cloud Outsourcing Guidelines**,¹⁷² issued to provide clarity on how the Solvency II rules described above apply to this specific type of outsourcing and state that as a part of its governance and risk management system, the undertaking should keep records of its cloud outsourcing arrangements, for example in the form of a dedicated register kept updated over time.
 - c. **IDD**¹⁷³ - No explicit provisions relating to outsourcing by insurance intermediaries exist in the Level 1 text of the IDD, and it is also worth noting that only ‘assistance in the administration and performance of insurance contracts’ is caught by the definition of ‘insurance distribution’ under the IDD, whereas the management of claims on a professional basis on behalf of an insurance undertaking is explicitly excluded from the IDD.¹⁷⁴ It is also worth noting that the Delegated Regulation on Product Oversight and Governance¹⁷⁵ provides that ‘manufacturers designating a third party to design products on

¹⁷⁰ See footnote **Error! Bookmark not defined.**

¹⁷¹ Outsourcing requirements are further clarified in Article 274 of Solvency II Delegated Regulation (Commission Delegated Regulation (EU) 2015/35 of 10 October 2014 supplementing Directive 2009/138/EC of the European Parliament and of the Council on the taking-up and pursuit of the business of Insurance and Reinsurance (Solvency II), OJ L 12, 17/01/2015.

¹⁷² EIOPA (2020a).

¹⁷³ See footnote 76.

¹⁷⁴ It is covered under outsourcing rules if done by an intermediary in the name and on account of an undertaking.

¹⁷⁵ Article 4(5) of Commission Delegated Regulation (EU) 2017/2358 of 21 September 2017 supplementing Directive 2016/97/EU of the European Parliament and of the Council with regard to product oversight and governance requirements for insurance undertakings and insurance distributors, OJ L 341, 20/12/2017.

their behalf should remain fully responsible for compliance with the product approval process¹⁷⁶, meaning, irrespective of the extent to which third parties are involved in the product design process, manufacturers must always maintain effective control over this process.

- d. **IORP 2 Directive**¹⁷⁷ states that Member States shall ensure that IORPs notify NCAs in a timely manner of any outsourcing of the activities covered by the Directive. Where the outsourcing relates to the key functions or management of IORPs, this shall be notified to NCAs before the agreement in respect of any such outsourcing enters into force. Member States shall also ensure that IORPs notify NCAs of subsequent important developments with respect to any outsourced activities. Member States shall ensure that NCAs have the power to request information from IORPs and from service providers about outsourced key functions or any other activities at any time.

154. The EIOPA initial gap analysis indicates that there is room to tailor current and upcoming requirements (Solvency II, IORP 2, IDD) so that rules in the different sectors are consistent and complement each other. In particular, general outsourcing rules within IDD should be considered, also bearing in mind that insurance intermediation is one of the most used (until now) entrance door for tech companies to the insurance sector.

155. More concretely, the following should be highlighted:

- a. Clarify the scope of outsourcing. In fact, Solvency II defines outsourcing as ‘an arrangement of any form between an insurance or reinsurance undertaking and a service provider, whether a supervised entity or not, by which that service provider performs a process, a service or an activity, whether directly or by sub-outsourcing, which would otherwise be performed by the insurance or reinsurance undertaking itself’. In all cases captured by outsourcing definition, the general principle under Solvency II would apply, i.e. ‘Member States shall ensure that insurance and reinsurance undertakings remain fully responsible for discharging all of their obligations under this Directive when they outsource functions or any insurance or reinsurance activities.’ Legal certainty on the definition regarding the different types of arrangements between the parties and the definition of process, service or activity is key to ensure that all relevant activities are captured.
- b. Additionally and if relevant, it could be considered ensuring that tech activities are deemed to be outsourced activities (or, when necessary or automatically, qualified as an outsourcing critical or important activity or function) and that the requirements over the group/the undertaking and the outsourced activity take into account the specificities of tech activities and are sufficient enough to cover them.
- c. Eventually, and when relevant, to grant power to the supervisor over the outsourcing service provider if the service provider is not covered by the DORA Oversight framework, in

¹⁷⁶ Note that POG applies to those manufacturing and distributing insurance products. Products in this context exclude large risks which are exempted from POG requirements. In addition, EIOPA Guideline 61 on the System of Governance states that when an insurance intermediary, who is not an employee of the undertaking, is given authority to underwrite business or settle claims in the name and on account of an undertaking, the undertaking should ensure that the activity of this intermediary is subject to the outsourcing requirements.

¹⁷⁷ Directive 2016/2341/EU of the European Parliament and of the Council of 14 December 2016 on the activities and supervision of institutions for occupational retirement provision (IORPs), OJ L 354, 23/12/2016.

addition to the prerogatives given by Art. 38 of the Solvency II Directive. For instance, it could be relevant to give explicitly the right to the supervisor to formulate any recommendations directly to the outsourcing service provider.

- d. As stated in Guideline 61 of EIOPA System of Governance Guidelines: ‘When an insurance intermediary, who is not an employee of the undertaking, is given authority to underwrite business or settle claims in the name and on account of an undertaking, the undertaking should ensure that the activity of this intermediary is subject to the outsourcing requirements.’¹⁷⁸ It is crucial that insurance undertakings are able to map all their distribution partners;
- e. Given that no explicit provisions relating to outsourcing by insurance intermediaries exist in the Level 1 text of the IDD and to ensure that outsourcing does not lead to material consumer detriment, consideration should be given to incorporating general outsourcing principles in the IDD, clarifying the responsibility of the insurance intermediaries when outsourcing is used. Concrete proposals would need to be further assessed and developed, taking into account rules that would be fit-for-purpose and proportionate.

Recommendation 1c: Consider the need to define clear requirements for financial entities to have internal structured information on all arrangements with third-party providers in the insurance and pensions sector.

The Commission should consider the need to define clear requirements for financial entities to have internal structured information on all arrangements with third-party providers in the insurance and pensions sector, if not yet covered by DORA so as to have adequate information on third parties used to allow a risk-based supervision.

Once DORA enters into force, EIOPA should engage with NCAs to assess if any relevant third-party service provider is not covered by DORA, and depending on the assessment, consider the most adequate way forward to ensure a risk-based supervision of all relevant third-party risk within the supervision of outsourcing requirements.

- 156. As explained before, outsourcing sectoral rules should be the basis for third-party risk monitoring. To fully assess this risk, NCAs need to have access to information on the use of outsourcing. On a case-by-case situation this assessment can be done; in the case of Solvency II (see section on Outsourcing), through the regular supervisory review process, in particular through onsite inspections or requests for ad-hoc information. However, it should be ensured that the information is readily available within the financial entity, and it is clear that any macro analysis of the service providers within the sector by the NCAs or even at European level is not possible today, and in the future it will only be possible for ICT service providers covered by DORA. This situation jeopardises a fully risk-based supervision on this area, an assessment of interconnectedness between regulated and relevant non-regulated undertakings would not be possible.
- 157. Under section 3.3 on Mixed Activity Groups, EIOPA is also proposing an amendment to the definition of Ancillary Services Undertakings so that tech/digital non-financial entities contributing directly to the insurance value chain and/or assuming a material role in the

¹⁷⁸ The discussion could also include exploring how to best capture B2B intermediaries, e.g. Managing General Agents as well as e.g. relationships between insurers and asset managers that can be important from both conduct and prudential perspective.

insurance business model may be classified as Ancillary Services Undertakings. To be able to properly assess which companies could be classified as ASUs, supervisors need information on the types of processes, services or activities that are being performed by those entities and the materiality and types of links to the business model and relevance for the insurance value chain. This could be identified during the business model analysis performed by the NCA or in the supervision of individual ORSAs; however, a more structured source of information would allow for a regular and more efficient process.

158. As DORA will address this challenge for the entities within its scope, it is important to wait for a clear definition of the DORA scope. Once the scope is fully defined, EIOPA should engage with NCAs to assess if any relevant third-party service provider is not covered by DORA¹⁷⁹, and depending on the assessment to consider the most adequate way forward to ensure a risk-based supervision of all relevant third-party risks within the supervision of outsourcing requirements.
159. Possible approaches to address these challenges may include the following, to be considered as a step-by-step approach:
- a. Need to define clear requirements for financial entities to have internal structured information on all outsourcing arrangements in place, if not yet covered by DORA. The structure of the future register of information foreseen in DORA could be used as inspiration;
 - b. After the assessment referred above once DORA scope is clearly defined, consider the need for supervisors to still have an overview of third-party risk not covered by DORA and possible concentration risk and assess possible solutions to improve the efficiency of supervisory monitoring activities, either by identifying relevant processes, services or activities performed by service providers not covered by DORA or by making available more information to supervisors.

Recommendation 1d: Widen the scope of existing tools, when the value chain is fragmented and value chain and/or the business model of the insurance undertaking is materially exposed to a third party while group supervision is not applicable.

EIOPA will review guidelines or other supervisory convergence tools to consider the need to:

- stress the importance of the ORSA at solo level to assess all material risks, including the concentration risk and interdependency risks arising from the fragmented value chain and/or business model. The assessment should include the understanding of the business model and an evaluation of any outsourced services or similar, including data and IT, when such services are strategic and relevant for the business model of the undertaking.

EIOPA will recommend that the Commission consider the need to:

- introduce the power for the NCAs to request from the regulated entity an ad hoc report covering the transactions with relevant third parties/entities, similar to a reporting of Intra-Group Transactions (IGTs) for groups.

160. When there is a tech firm heavily impacting the value chain of an insurance undertaking, but group supervision does not apply, solo supervisors should also be able to maintain a

¹⁷⁹ If the contractual arrangement is with the third-party provider, it is not captured within DORA's subject matter.

comprehensive understanding of the risks posed to the undertaking from the increased reliance on third parties for parts of the value chain. This stresses the importance of the ORSA supervision at solo level to assess all material risks, including the concentration risk and interdependency risks. The assessment should include the understanding of the business model and an evaluation of any outsourced services or similar, including data and IT, when such services are strategic and relevant for the business model of the undertaking. Additionally, the NCAs could be granted the power to request an ad hoc report of the regulated entity covering the transactions with relevant third parties/entities of the group, similar to a reporting of IGTs for groups

161. In such a scenario, the regular supervisory review process should apply with added focus on Pillar 2 tools such as the ORSA, supervision of outsourcing requirements (and DORA in the future), and emphasis on operational risk and its potential spillage on other risks. In addition, supervisors could assess if the standard formula adequately captures the risks posed by digitalisation.
162. The ORSA at solo level should include an assessment of all material risks, including the concentration risk and interdependency risks arising from the fragmented value chain and/or business model. The assessment should allow an understanding of the business model and an evaluation of any outsourced services or similar, including data and IT, when such services are strategic and relevant for the business model of the undertaking. EIOPA will consider drafting guidelines or other supervisory convergence tools on such integration in the ORSA (e.g. including any additional content related to digitalisation and how it should be addressed in ORSA).
163. More than risk assessment and management effectively driven by the ORSA process and the IGT reporting, it could also be necessary to reinforce the outsourcing provisions and to extend supervisory powers over the outsourced activity. Indeed, groups and undertakings often have recourse to digital service providers as intermediaries for their activities or as experts to fulfil their regulatory requirements, and there remains uncertainty about the correct level of requirements under those outsourced activities to ensure that they are supervised correctly. EIOPA's Guidelines on outsourcing to cloud service providers published in 2020¹⁸⁰ seems to be a good example of a specific treatment of such problems if not solved by DORA Oversight framework.

¹⁸⁰ EIOPA (2020a).

3.1.2 Recommendation 2: Update current disclosure requirements in EU law as relevant to make them fit for the digital age and enhance consumer protection and conduct of business rules to address risks of mis-selling and overcome potential weaknesses in complaints-handling processes

Recommendation 2a: Update current disclosure requirements in EU law and make them fit for the digital age to allow consumers to make informed decisions about products and services.

To ensure that disclosures are fit for the digital age, to allow informed decision-making and avoid mis-selling, the ESAs recommend that the European Commission pay particular attention to specific points in any future review of the disclosure requirements in various legislations, such as the presentation and format of the disclosures, the definition of ‘durable medium’, the timing of disclosures, the use of behavioural insights and the need to explore the benefits of open data.

With a particular focus on the DMFSD¹⁸¹ currently under review, the ESAs recommend that the European Commission take into account the general proposals made by the ESAs on how the disclosure rules should be revised to fit the digital age, in relation to:

- a. Time period of disclosure
- b. Presentation and format
- c. Provision of information
- d. Advertisements
- e. Right of withdrawal
- f. Dispute resolution and redress procedures
- g. Post-sale information and periodic disclosures
- h. Accessibility and effectiveness of the information
- i. Monitoring effectiveness

164. New technologies are transforming financial products and services offers and how information is provided to consumers. Respondents to the surveys and to the interviews commonly identified that the EU legal framework could potentially be outdated regarding disclosure requirements. According to them, it could negatively impact consumers when it comes to making informed decisions about products and services and firms that are willing to provide financial services in the digital environment. From the supervisory side, ensuring the digital transition occurring in society and the marketplace is appropriately reflected in existing disclosure requirements is of paramount importance.
165. EU product-specific and sector-specific financial legislations contain disclosure requirements, for example in the MiFID II¹⁸², IDD, PRIIPs, SFDR, Solvency II, PEPP, CCD, MCD, PSD2 and PAD legislations, and horizontal directives are partially covering these aspects, such as the DMFSD, the e-Commerce Directive¹⁸³ (ECD) and the Unfair Commercial Practices Directive¹⁸⁴ (UCPD).

¹⁸¹ See footnote 3.

¹⁸² In particular Article 24 of MiFID II; Articles 3 and Articles 44 to 52 of the MiFID II Delegated Regulation.

¹⁸³ Directive 2000/31/EC.

¹⁸⁴ Directive 2005/29/EC.

166. The deadline for the ESAs to respond to the Call for Advice does not allow the ESAs to analyse sectoral legislation provisions to check how they could fit better for the digital age.
167. Therefore, as a starting point, the ESAs have decided to first provide concrete recommendations on the disclosure requirements that need to be adapted to the digital age which could be taken into account by the European Commission as part of its current review¹⁸⁵ of the DMFSD and could potentially be reflected in any sectoral legislation's reviews that the European Commission is to/will undertake. The DMFSD which was intended to act as a safety net for financial services not covered by product-specific legislation and new unregulated products that may come onto the market, applies indeed horizontally to any service of a banking, credit, insurance, pension, investment or payment nature, and sets out information obligations to be provided to the consumer prior to the conclusion of the distance contract (pre-contractual information), grants for certain financial services a right of withdrawal to the consumer, and bans unsolicited services and communications from suppliers. The ESAs are, however, not taking a position regarding whether the DMFSD should be revised or repealed; there are some arguments for repealing the DFMSD altogether and others to simply revise the DMFSD, but the ESAs have not had the time to assess this, given the limited time available.
168. With regard to the requirements applying to sectoral legislations, work is however ongoing from the ESA perspective and more specific recommendations will be provided as part of European Commission Call for Advice as follows:
- a. for the financial instruments under the scope of MiFID II and insurance-based investment products under IDD, ESMA and EIOPA are currently preparing their advice to the Commission on a number of areas concerning investor disclosures and digital disclosures, following the receipt of a call for advice regarding certain aspects relating to retail investor protection in July 2021¹⁸⁶. ESMA and EIOPA are looking at identifying any significant overlaps, gaps, redundancies and inconsistencies across investor/consumer protection legislation that might have a detrimental effect on investors and are also assessing how regulatory disclosures and communications can work best for consumers in a digital age.
 - b. following a Call for Advice from the Commission¹⁸⁷ on the review of the PRIIPs Regulation¹⁸⁷, the ESAs are analysing the extent to which the Key Information Document (KID) for PRIIPs is adapted to digital media.
 - c. the Mortgage Credit Directive will soon be reviewed by the Commission, a separate call for advice might be sent to the EBA in the process, and the EBA may then provide an opinion covering also the need to adapt the legislation, including on the European Standard Information Sheet disclosure document.
169. For the reasons explained above, the ESAs are therefore focusing only on the following issues as part of this Call for Advice on digital finance:
- a. Main points of attention to ensure disclosures fit for the digital age;

¹⁸⁵ The Commission's 2020 Work Programme lists this Directive under the REFIT Initiatives as subject to a possible revision.

¹⁸⁶ See footnote 7.

¹⁸⁷ European Commission (2021c), [Call for advice to the Joint Committee of the European Supervisory Authorities regarding the PRIIPs Regulation](#), Ref. Ares(2021)4803662, 27/07/2021.

- b. Recommendations for the review of the DMFSD.

Main points of attention to be considered to ensure disclosures and choice architecture are fit for the digital age in any horizontal and sectoral legislation:

170. New business models, increased fragmentation, and the use of platforms for the sale and distribution of financial services require the regulators to consider new approaches to disclosures.¹⁸⁸ Both disclosure requirements and the broader contexts in which disclosures operate could benefit from an evidence-based approach and contribute to better outcomes for consumers. Choice architecture designed in the best interest of the consumer is a valuable addition. In line with the responses which will be provided by respective ESAs as part of the ongoing or future CfA on sector-specific legislations¹⁸⁹, the ESAs believe that in order to adapt the existing disclosures requirements framework to the digital age, some key orientations could be considered by the European Commission when reviewing disclosure requirements in any horizontal or sectoral legislations:

- a. **Presentation and format of the disclosures:** information to consumers of a potential agreement that will be concluded via digital means should be concise, focused to serve its intended purpose, and presented in a clear and understandable format. Consumers should be able to easily access and navigate through the information provided by the financial institutions: in a digital context, it is of paramount importance to ensure that consumers and potential consumers are able to easily identify particularly relevant sections or access the disclosure in a way that is meaningful to them.
- This can be achieved, for example, through a menu feature in an app, chapters in a video or a contents sidebar or similar on a webpage, which the consumer can use to immediately go to sections of the disclosure (e.g. to benefits and risks, the cost of the product, factors affecting returns, or how to complain etc.).
 - It can also build on the layering approach, already provided for under the PEPP Regulation¹⁹⁰. This allows the structure of the information to be presented in different layers of relevance: from the information ‘at a glance’ that is essential for all audiences, to the more detailed information (e.g. on the breakdown of costs) being readily available in a subsequent layer for those interested, and so forth. Layering can also help explain technical terms (e.g. use of glossaries) or facilitate engagement by the consumer with interactive tools (e.g. QR codes, signposting to a pension calculator). It would help to allow *per se* under EU legislation for the use of visual

¹⁸⁸ Some regulators have already been reassessing their approaches, see e.g. ASIC and AFM (2019), [Disclosure: Why it shouldn't be the default](#), A joint report from the Australian Securities and Investments Commission (ASIC) and the Dutch Authority for the Financial Markets (AFM), 14 October; FINRA (2019), [Regulatory notice on Disclosure Innovations in Advertising and Other Communications with the Public](#), 19 September; ASIC (2016), [Regulatory guide 221: Facilitating digital financial services disclosures](#), March.

¹⁸⁹ For example, the CfA to the ESMA and EIOPA regarding certain aspects relating to retail investor protection (see footnote 7).

¹⁹⁰ Regulation (EU) 2019/1238 of the European Parliament and of the Council of 20 June 2019 on a pan-European Personal Pension Product (PEPP), OJ L 198, 25/07/2019.

dashboards at the start of disclosure documents. Layering allows disclosure to cater to different types of consumers with heterogeneous information preferences.

- Several sectoral financial services EU directives provide that pre-contractual information provisions have to be provided on paper or on another durable medium if the consumer agrees. EU financial regulation should not prevent financial institutions from providing pre-contractual and/or contractual information in electronic format (e.g. e-mail, a dedicated webpage or an electronic mailbox, or mobile applications)¹⁹¹ unless the consumer or potential consumer has requested receiving the information on paper, in which case that information shall be provided on paper, free of charge. This option for consumers to receive the information on paper if they so wish will preserve financial inclusion of non-digital-savvy consumers, disabled consumers etc. For example, if the disclosure requirements in existing regulations (such as on costs, fees, risks, etc.) were to be complemented by requirements that set out how the disclosure should be presented when services are provided via digital means (mobile, internet, etc.).
- b. **Time period of disclosure:** Enough time should be provided to the consumer to consider the relevant information/documents provided by the financial institutions via digital means. This is particularly pertinent when financial services are marketed through digital means, given the potential aggressive marketing practices and expedited way in which consumers might be made to proceed swiftly through user interfaces, e.g. via check boxes, radio buttons or similar features.
- c. **Definition of ‘durable medium’:** The definition of ‘durable medium’ should be adapted to fit better technological evolutions: despite the fact that definitions of ‘durable medium’ exist in several directives, including the DMFSD and PSD2, the definitions are usually too generic and therein may not keep up with the speed of innovation in the technology that is available to store information. The definition should be technology-neutral and future-proof.
- d. **Use of behavioural insights:** Further consideration should be given by the European Commission to behavioural insights when including new disclosure requirements in EU financial legislations (e.g. regarding the content, presentation and format of disclosure, they should be evaluated on their effectiveness in fostering an informed choice process). Firms need to understand the behavioural aspects of choice architecture and consumer biases to improve consumer decision making. Firms need to apply these behavioural insights to designing the choice architecture in such a way that it promotes informed decision making and improves consumer outcomes (e.g. cooling-off period during which a consumer can withdraw from the sale without major legal or financial consequences could be seen as good practice). EU institutions and regulators should, for example, monitor the latest research techniques and consider how they can be best leveraged¹⁹². Valid consumer testing should be integrated to the Level 1 regulatory process before the legislation is finalised and published in the Official Journal. Testing in a controlled setting makes it possible to check

¹⁹¹ CMRP for MiFID II requirements (Art. 24 para. 5a of Directive 2014/65/EU) and the PEPP Regulation (Art. 24 of Regulation 2019/1238/EU) both introduced ‘electronic format’ as ‘default format’.

¹⁹² For example, eye-tracking technology can now be used as part of consumer testing methods.

whether consumers are objectively able to make the correct choices. As best practice, designs are also pilot-tested outside the controlled testing environment. It is crucial that the results of consumer testing meaningfully influence the final design of the disclosure. Without such testing, there is a risk that the disclosure requirements are not adapted to consumers' needs in practice. This might also impact the level 2 requirements the ESAs would have to develop.

- e. **Exploring the benefits of open data:** Without prejudice to GDPR requirements, it is recommended that the European Commission further explore risks, costs and benefits of providing all public disclosure information (including information included in standardised key information documents) in a dedicated space and in machine-readable form so that third parties such as FinTech companies can develop tools for better comparison of financial services and products, and innovation in the area of robo-advice.¹⁹³

Recommendations for the review of the DMFSD

- 171. Because of their intangible nature, financial services are particularly suited to distance marketing. This is why in the EU, a 2002 Directive, the DMFSD, established a legal framework governing the distance marketing of financial services. According to the Directive, when concluding a distance marketing contract, all the contractual terms and conditions and the prior information are required to be communicated to consumers, on a durable medium, and be accessible to them in good time before they are legally bound by any distance contract or offer¹⁹⁴.
- 172. In line with the EBA opinion on disclosures to consumers¹⁹⁵, the ESAs' recommendations present a number of proposals on how the disclosure rules should be adapted to the digital reality, with a particular focus on the DMFSD¹⁹⁶. The proposals consist of general proposals applicable to any information that is being made available to consumers, such as its timing, the presentation format, and accessibility, as well as specific proposals applicable to particular stages of the information to be provided, without prejudice to existing EU legislations targeting specific financial product and services that have a different objective than the DMFSD and only aim to supplement sectoral financial services legislation and not replacing them.
- 173. In addition, as part of the DMFSD review, the ESAs recommend that the European Commission ensure that the provisions related to disclosure requirements in the DMFSD are consistent with the provisions mentioned in sectoral legislations to avoid any overlap and contradictions.

(a) Timing of disclosure

- 174. The DMFSD requires that providers of financial services (hereafter 'providers') make available to consumers relevant information at an early stage in the buying process, and in particular before the consumer commits to a specific financial product or service. More specifically, Article 3(1) of DFMSD requires information to be provided in good time before consumers are bound by a contract, so as to provide them with the opportunity and ability to act on the information.
- 175. This is particularly pertinent when financial services are marketed through digital means, given the expedited way in which consumers might be made to proceed swiftly through user

¹⁹³ ESMA and EIOPA might further look at this in their work on the Retail Finance CfA (see footnote 7).

¹⁹⁴ Article 3(1) of DMFSD.

¹⁹⁵ EBA (2019b), [Opinion of the European Banking Authority on disclosure to consumers of banking services through digital means under Directive 2002/65/EC](#), EBA-Op-2019-12, 23 October.

¹⁹⁶ In line with the opinion referred to in footnote 195.

interfaces, e.g. via check boxes, radio buttons or similar features. A frictionless customer journey is positive, unless it steers too much towards products or services that are less suitable for the customer in question.

176. At the pre-contractual stage before the point of sale, the DFMSD provides that the consumer should be given information on the supplier, the financial services, the contract and the redress procedures before making a choice. Enough time should be also provided to the consumer to consider the relevant information/documents before being bound by any contract or offer. In cases where financial services are marketed via digital means, these issues are, again, particularly important given the speed with which consumers are led, and often encouraged, to make buying decisions.

(b) Presentation and format

177. In general, information should be fair, clear and not misleading. More specifically, it means that information to consumers on a potential agreement that will be concluded via digital means should be concise, focused to serve its intended purpose, and presented in a clear and understandable format. This should be done so as to increase the likelihood that consumers notice and understand the key information (e.g. on fees and charges, level of risk, cover in case of insurance products, or the right of foreclosure when it comes to credit secured by a mortgage) and what the agreement implies in terms of financial commitment.
178. Providers should further be required to use short and direct sentences, key words, boldface, bullet points, comparative tables or other such features so as to highlight relevant information and improve clarity. The information should be provided in clear and understandable language and technical jargon should be avoided, whenever possible. Where such use cannot be avoided, a glossary for reference should be available in a visible place (e.g. through mouse roll-over or pop-up). Without prejudice to any requirements set out in sectoral legislation, providers should be required to use at least the official language(s) of the country where they are marketing the service, unless the consumer agrees to use another language.
179. In addition, the use of digital means of communications should not result in information that is overly restrictive for consumers (e.g. because of the format leaving out key information) and, hence, unclear, ambiguous or misleading. A revision of the DFMSD should take care to spell out explicitly requirements for this marketing channel and the online sale distribution.
180. Providers should be required to draw attention to relevant information and display disclosures prominently on the app, website etc., giving also further consideration to the format imposed by some existing sectoral requirements. Information should be presented in a plain and readable font size, which should easily adapt to work on any kind of device. Ideally, providers should also enable the option for consumers to increase the default font size. In addition, most relevant information for consumers should not be displayed in a smaller font size than the rest of the disclosure, in particular charges and withdrawal conditions, if applicable.
181. Providers should be required to design disclosure material such that it is noticeable, paying particular careful attention to the size, colour, icons or graphics used to disclose relevant information, as these may affect its prominence in relation to other content displayed in the screen (for instance, information in a colour that blends in with the background is likely to be missed). Where colours are used in the design of mandatory disclosures, such as standardised pre-contractual information, they should not diminish the comprehensibility of the information provided if printed or photocopied in black and white. If audio or video is used, speed of speaking and volume of sound shall be adjusted to make the information noticeable and understandable.

182. The provision or availability of information can lead to information overload on the part of the recipients. Information documents should therefore be limited to the information that is most essential for consumers, with straightforward references to additional information at logical points. Consumers will not then be overwhelmed. The key information should in any case clearly state the choices available to consumers on the basis of the information. Consumers wishing to know more can then click through to additional information. This principle is known as 'layered communication'.
183. Finally, an evaluation of the effectiveness of the various solutions proposed should be put in place by providers. It could be adapted to the communication channel used and take into account of possible customers behavioural biases.

(c) Provision of information

184. The DFMSD requires providers to make available pre-contractual information such that they enable consumers to assess whether the product is appropriate for their needs and financial situation.
185. The Directive should make clearer in Art. 5(1) how pre-contractual information should be provided on a durable medium, in a way appropriate to the particular device and the specific type of digital communication channel. The providers should check that the delivery mechanism fits the objective of effective disclosure.
186. For example, in line with the PEPP Regulation, it could be stated that pre-contractual information shall be located in an area of the website or a mobile application where it can be easily found and accessed, and it shall be provided in a stage of the purchase process where the prospective or current consumer is allowed enough time to consider the document before being bound by a contract or an offer.
187. Information to be disclosed to the consumer through standardised pre-contractual information documents on a durable medium should take into account the practicality of the relevant standardised form, and be downloadable in its entirety as a stand-alone document.
188. For example, when access to relevant information is provided through a hyperlink, providers should be required to ensure that hyperlinks are:
 - a. not used in a way that misleads consumers away from the relevant information, for example, by fragmenting the information provided into separate pieces in different locations;
 - b. noticeable and presented consistently, for example regarding style, prominence, positioning, etc., to ensure that consumers can navigate easily through the additional information available;
 - c. labelled appropriately to convey the importance, nature, and relevance of the information they refer the consumer to. For example, when a hyperlink leads to a mandatory pre-contractual information document, the name of the document should be reflected in (name of) the hyperlink. This should prevent hyperlinks from having different names than the documents they refer to;
 - d. referring consumers directly to the relevant information on the click-through page; and

- e. periodically tested by the providers for proper functioning, keeping in mind that a medium can be qualified as a 'durable medium' if the transmitted information is not submitted to an 'any unilateral modification of its content'¹⁹⁷.
189. Where the length of the information is such that cannot be shown within the display area in its entirety, leading to the implementation of a scrolling mechanism to view different parts of the document, providers should ensure that consumers cannot conclude the contract before scrolling down the entire information to the very end.
190. With regard to scrolling through information, providers should use different techniques to encourage consumers to scroll including, but not limited to,
- a. using text or visual cues;
 - b. adjusting navigation for scrolling, for example by keeping abreast of empirical research about where consumers do and do not look on a screen while at the same time recognising and adjusting to any technological limitations on the consumer's device; and
 - c. using jump-to-section options to enhance long-scrolling.
191. Finally, it could be useful for consumers to receive a notification when the contractual conditions have been modified since the subscription. These changes can often concern important clauses, such as pricing, order execution venues, etc. This notification should explain the main changes in an educational manner.

(d) Advertisements

192. As a complement to relevant provisions on advertising contained in a number of Directives, the DFMSD should be amended so that when advertising retail financial products and services through digital means, providers are required to clearly label the promotional nature of the communication in order for marketing messages to be clearly identifiable (for example in line with MiFID II (Art. 13(d) paragraph 2 Sentence 2, Art. 24 para. 3 sentence 2) requirements).

(e) Right of withdrawal

193. Consumers should easily be able to exercise their right of withdrawal from the relevant contract, so the procedure concerning digital financial services should not be more burdensome than the procedure to sign the contract. A dedicated space should be made accessible to consumers on the providers' website and mobile phone applications to allow the consumer to access without difficulty such key information and be informed about the procedure. Such space should, for example, be accessible to the consumer and located on the provider's home page or main menu on a permanent basis.

(f) Dispute resolution and redress procedures

194. According to the DMFSD, with a view to protecting consumers, there is a need for suitable and effective complaint and redress procedures in the Member States with a view to settling potential disputes between suppliers and consumers by using, where appropriate, existing procedures.

¹⁹⁷ Judgment of the Court (Third Chamber) of 25 January 2017, BAWAG PSK Bank für Arbeit und Wirtschaft und Österreichische Postsparkasse AG v Verein für Konsumenteninformation, Request for a preliminary ruling from the Oberster Gerichtshof - C-375/15 – BAWAG.

195. In line with existing requirements applicable to Member States under Art. 13 of the Directive 2013/11/EU for the setting up of Alternative Dispute Resolution Regimes (ADR), providers should set up a dedicated space on their website, app, digital platforms etc. to enable consumers to use ADR procedures, and to be informed on alternative ADR procedures with which the provider complies.
196. This information should explicitly explain the steps to be followed, e.g. who the consumer should contact, and should provide direct links to ADR webpages, and give information on the relevant NCA and national courts where the consumer could take legal action.
197. In addition, where more than one provider is involved in the provision of the financial service, the provider(s) should clarify to which provider(s) a complaint should be addressed and in respect of which provision(s) in the contract.
198. Such space should be accessible to the consumer and located on the provider's home page or main menu on a permanent basis.
199. For completeness, the ESAs note that, according to the provisions of the proposed Digital Services Act, all platforms, except for the smaller ones¹⁹⁸, will be required, inter alia, to set up internal complaint-handling systems¹⁹⁹ in respect of decisions taken in relation to alleged illegal content or information incompatible with their terms and conditions and engage with out-of-court dispute settlement bodies to resolve any dispute with users of their services²⁰⁰. According to the proposal, online platforms shall inform complainants without undue delay of the decision they have taken in respect of the information to which the complaint relates and shall inform complainants of the possibility of out-of-court dispute settlement and other available redress possibilities to resolve any dispute with users of their services.
200. Therefore, in the context of the review of the DMFSD, measures could also be considered to ensure that internal complaint-handling arrangements and engagement with Alternative Dispute Resolution bodies are required for non-financial institution digital platforms to ensure that adequate and effective digital resolution procedures are put in place and apply where these platforms facilitate the distribution of financial services. Appropriate arrangements would also need to be put in place to ensure effective oversight and enforcement of any resulting obligations. Following careful review, measures may also be considered to ensure effective complaints handling and sufficient and effective information.²⁰¹

(g) Post-sale information and periodic disclosures

201. When communicating through digital means, providers should be required to mitigate risks for consumer of not paying sufficient attention to important communications after the sale of the product, such as statements of changes to terms, conditions, fees or charges, and other forms of communication, unawareness of which could be detrimental to consumers.
202. Where appropriate, providers should be required to do so by using instant communication channels, such as emails, Short Message Service (SMS) or push notifications, including the

¹⁹⁸ As proposed, those platforms qualifying as micro or small enterprises within the meaning of the Annex to Recommendation 2003/361/EC will not be required to comply with the obligations set out in Section 3 (additional provisions applicable to online platforms) of Chapter III of the proposal for the DSA (see further from EBA (2021e), Text box 3, pp. 31-32).

¹⁹⁹ Article 17 of the proposed DSA, see footnote 19.

²⁰⁰ Article 18 of the DSA.

²⁰¹ In addition to non-financial platforms, other areas where the line is blurring between regulated and non-regulated financial services might require similar analysis.

seeking of prior consent by the consumer. Consumers should be able to opt out of these communication channels, and financial institutions should also be able to provide suitable communication channels for consumers to access legally mandated communications. However, using instant communication channels should not lead to a possibility for the financial institutions to unilaterally change, at any time, the content of the message transmitted via the aforementioned channels. The financial institution should also ensure that it does not create challenges regarding the long-term storage of the information.

203. The DFMSD, and Art. 5(3) in particular, should be reviewed to assess the merit of amending that provision in order to ensure that, where a contract has been signed via digital means, the terms of the contract should specify the extent to which the consumer can switch to a non-digital provision of the service (if applicable) and, if so, under what conditions.

(h) Accessibility and effectiveness of the information

204. In order to improve the effectiveness of disclosure, providers should be required to better communicate with all types of consumers (e.g. including with disabilities etc.) when concluding contracts via digital means, by considering not just the required message, but the best means of communicating that message, based on the type of financial product or service, the respective stage in the marketing and sales process. Providers should be required, for example through consumer testing, to ensure that information is easily accessible, understandable so as to allow consumers to enter into an active and informed consent. For example, it can be by presenting key information in a clear and prominent manner, separately from the complete suite of information that is being provided, and in a format that is clearly linked to any 'click-to-buy' button that the provider may have used, so that the information cannot be overlooked by the consumer.
205. Providers should be required to move away from a pre-ticked box approach as a means of obtaining evidence of the consumer's understanding and consent; they should also be required to use communication means that are proportionate to the complexity of services provided, such as live chats, chatbots, Q&As, infographics, guides, interactive tools or similar approaches, to ensure that consumers are adequately assisted in their interaction and commercial relationship with the firm in the digital environment.
206. To that effect, providers should be required to use behavioural insights to create effective product and service information, and should include communications to consumers as an integral part of the product or service design process, taking into account the needs of all type of consumers including vulnerable consumers (e.g. a phone number contact should also be made available if consumers would like to access complementary information). Using behavioural and communication insights also entails testing and monitoring whether or not the communications with consumers function effectively and as expected for each specific context.

(i) Monitoring effectiveness

207. Providers should be required to monitor the design and prominence of relevant disclosures by analysing consumer behaviour, for example by gathering feedback from consumers, monitoring their activities and following up on complaints to ensure their effectiveness in the commercialisation of retail financial products and services through digital means. The provider should take the results of the monitoring into account to decide on potential changes required.
208. Providers should periodically review their pre-contractual information to ensure that its content and format are kept simple and easy to understand.

Recommendation 2b: Enhance the level of consumer protection and conduct of business rules to address risks of (cross) mis-selling and overcoming potential weaknesses in complaints-handling processes regarding the provision of financial services in a digital context.

The ESAs recommend that the European Commission address the risk of (cross) mis-selling in particular for tied or bundled products by considering a package of remedies, to give further consideration to the existing Product Oversight and Governance (POG) rules to address any risks of (cross)-mis-selling practices, to prohibit the use of pre-ticked boxes by default and finally address the inconsistencies in relation to cross-selling practices across existing legislative instruments for the three sectors in scope.

The ESAs recommend that the European Commission ensure greater harmonisation at Level 1 legislation to overcome potential weaknesses in digital complaints-handling processes, in particular in relation to disclosure requirements imposed in host jurisdictions and the allocation of responsibilities for the supervision of complaint handling (see also Recommendation 4 which aims to 'Address the lack of convergence in classifying cross-border services in a digital context').

Addressing the risk of (cross) mis-selling in particular regarding tied or bundled products

209. In 2016, the ESAs' work on developing Guidelines on cross-selling practices that was carried out in the context of the Joint Committee of the ESAs revealed some legal issues in the existing regulatory framework between the three financial sectors. At the time, the ESAs were of the view that these issues prevented the ESAs from establishing the desirable degree of consumer protection, exposed consumers to the risk of detriment, and prevented the JC from achieving its objective of ensuring a level-playing field across the three sectors. As stated in the letter addressed at the time by the ESAs to the European Commission²⁰² the ESAs believe that a consistent approach across the three financial sectors is deemed to be beneficial for consumers, who do not always distinguish between the three sectors when buying financial products; to financial institutions, who would be subject to the same requirements irrespective of the products that are cross-sold; and to NCAs, who would have to supervise only one set of requirements irrespective of which constellation of cross-selling occurs.
210. In line with the above, the ESAs reiterate those points and recommend that the European Commission have aligned legislative provisions in different pieces of legislation falling in the regulatory remit of different ESAs (e.g. MiFID II – ESMA; IDD – EIOPA; PAD, MCD, CCD – EBA), regarding for example the wording, scope, and level of granularity in order to help NCAs and financial institutions understand and consistently apply cross-selling guidelines in all three sectors.
211. In addition, the Commission should consider a package of remedies that can be complementary and reinforce each other to address consumer protections issues stemming from online tying and bundling practices.²⁰³ The remedies can cover both the demand and supply side, as well as address the inconsistencies across existing legislative instruments at the EU level.
212. On the demand side, more specifically for the insurance sector, an example of a remedy that is not as intrusive as a ban, but that can have a significant impact is the concept of a 'deferred sale', where the 'add-on' product (which represents usually an optional service) cannot be sold

²⁰² ESAs (2016), [The cross-selling of financial products – request to the European Commission to address legislative inconsistencies between the banking, insurance and investment sectors](#), ESAs 2016 07, 26 January.

²⁰³ Note that proposed remedies are applicable to both online and offline tying and bundling practices.

at the same time with the main product and a deferral period (e.g. several days to weeks) could be respected before the consumer buys a product. When considering such remedy, the Commission should analyse the different scenarios, as there may be instances where it is appropriate for the add-on product to be sold jointly with the main product.

213. On the supply side, providers may be required to provide a transparent overview of the bundle value and the price for each bundled product as well as the product characteristics for comparability reasons.
214. The Commission could give further consideration to the existing POG rules to address any risk of cross-mis-selling practices when it comes to the design and distribution of the products in scope in the digital context. It means for example that manufacturers would have to define the target market for products bundles that are created by cross-selling and specify how the bundle meets consumer needs.
215. Providers should also be prohibited from using pre-ticked boxes through which the consumer is, by default, being opted into buying additional or ancillary products or services. Where such products or services are offered during the contracting process, these should be clearly framed and presented separately from the information about the main underlying product. Instead, providers should ensure that consumers exercise active and informed consent.
216. Finally, also in the digital context, the Commission should address the inconsistencies in relation to cross-selling practices across existing legislative instruments for the three sectors in scope: banking, insurance and investments (MCD, CCD, MiFID, PAD, PSD2 and IDD). EIOPA would suggest further addressing insurance-related cross-selling issues as part of the future IDD review.
217. Mis-selling in the digitalisation context goes beyond cross-selling. Digitalisation could also potentially increase the use of price discrimination practices, i.e. when different consumer groups are charged different prices for reasons other than cost or risk. Hence it is also important to update current disclosure requirements in EU law and make them fit for the digital age to allow consumers to make informed decisions about products and services (see **Recommendation 2a**). More specific recommendations might be provided by the ESAs as part of different European Commission Call for Advices, for example regarding certain aspects relating to retail investor protection, PRIIPs or MCD.

Overcoming potential weaknesses in digital complaints-handling processes

218. The ESAs recommend that where more than one provider is involved in the provision of the financial service, the provider(s) should clarify to which provider(s) a complaint should be addressed and in respect of which provision(s) in the contract. Such links should be accessible to the consumer and located on the digital platform provider's home page or main menu on a permanent basis. In addition, the consumer should be provided with information relating to complaints handling by the respective provider in the language of his/her country of residence or in the language agreed between the consumer and the provider and should have the possibility to use this language to complain.
219. Current rules and procedures for customer complaints handling are currently not fully harmonised in EU legislation. Only some EU directives include specific requirements for

complaints handling and redress mechanisms to leave scope for divergence at the national level.²⁰⁴

220. Turning first to promoting awareness of applicable requirements, in 2014, ESMA and the EBA published complaint-handling guidelines for the investment and banking sectors²⁰⁵ that are also identical to the EIOPA guidelines of the same name for the insurance sector adopted in 2012 and 2013.²⁰⁶ In 2018, the Guidelines were extended in their scope of application to the authorities supervising the new financial institutions established under the PSD2 and the Mortgage Credit Directive²⁰⁷, both of which came into effect after the original Guidelines.²⁰⁸
221. The objective of the Guidelines is to provide EU consumers with a single set of complaint-handling arrangements, irrespective of the type of product or service and of the geographical location of the firm in question.
222. In line with the ESA JC report on cross-border supervision of retail financial services²⁰⁹ and the EBA Report on potential impediments to the cross-border provision of banking and payment services²¹⁰, the ESAs highlight that more clarity should be provided by the EU co-legislators on the application of consumer protection requirements, especially in the light of the growing phenomenon of the digitalisation of financial services and the growth of digital platforms. As stated in the aforementioned reports, greater harmonisation at Level 1, particularly related to disclosure requirements imposed in host jurisdictions and the allocation of responsibilities for the supervision of complaints handling, would be required to mitigate challenges faced by firms when seeking to provide financial services cross-border. Host NCAs and ESAs should be provided with adequate regulatory instruments and responsibilities so that they can effectively assume their conduct supervision responsibilities.
223. In the ESAs' view, should the EU Commission arrive at the view that digital platforms need to be regulated in the context of the provision of financial services, and to the extent that they are not already within the scope of EU law and the scope of action of the ESAs, such as MiFID, IDD and Solvency II, the digital platforms, and any national authorities potentially designated by the Member State as competent to supervise them, should be brought into the scope of action of the three ESAs. This would be to allow the ESA, inter alia, to extend the scope of these existing Guidelines to said platforms.

²⁰⁴ Note that financial services provision which falls under national regulation only might not be subject to any alternative dispute resolution procedure.

²⁰⁵ Joint Committee of the ESAs (2018c), [Guidelines on complaints-handling for the securities and banking sectors](#), JC/2018-35, 04 October.

²⁰⁶ EIOPA (2012), [Guidelines on complaints-handling by insurance undertakings](#), EIOPA-BoS-12/069, 14 June; EIOPA (2013), [Guidelines on complaints-handling by insurance intermediaries](#), EIOPA-BoS-13/164, 27 November.

²⁰⁷ Directive 2014/17/EU of the European Parliament and of the Council of 4 February 2014 on credit agreements for consumers relating to residential immovable property and amending Directives 2008/48/EC and 2013/36/EU and Regulation (EU) 1093/2010, OJ L 60, 28/02/2014.

²⁰⁸ EBA (2018), [Final report on the application of the existing Joint Committee Guidelines on complaints-handling to authorities competent for supervising the new institutions under PSD2 and/or the MCD](#), JC/2018-35, 31 July.

²⁰⁹ Joint Committee of the ESAs (2019a), [Report on cross-border supervision of retail financial services](#), JC/2019-22, 09 July.

²¹⁰ EBA (2019c), [EBA Report on potential impediments to the cross-border provision of banking and payment services](#), 29 October.

3.1.3 Recommendation 3: Prevent financial exclusion and promote a higher level of digital and financial literacy

Recommendation 3: Prevent financial exclusion and promote further a higher level of digital and financial literacy to help consumers make effective use of digital financial services and responsible choices that meet their expectations, raising confidence and trust in the digital financial system as well as their personal financial outlook.

The ESAs recommend taking further actions at national and European level to improve digital financial literacy as a continuation of the work already done by the ESAs and the European Commission/OECD-International Network on Financial Education.

Those actions could include promoting the use of those technology-driven financial services as a means of addressing financial inclusion and preventing the use of those technology-driven financial services in ways that exacerbate financial exclusion or cause unfair discrimination, as well as conducting further research to understand better the category of people excluded from the financial systems and the reasons of such exclusion in the digitalisation of financial services context.

224. Financial education represents an essential tool for consumers, as it gives them the knowledge and skills needed to understand the features, risks and opportunities of using financial products and services — and their legal rights and obligations. However, it should be kept in mind that financial education is inherently a long-term endeavour that is not always suited to the delivery of short-term results.
225. Financial education arises therefore as a complement to financial conduct regulation and supervision of the financial system, contributing directly to the greater added value of the instruments regulating transparency and the duties of information of financial institutions and, consequently, to the more efficient functioning of the financial markets. Consumers who are financially well educated, and who choose financial products that are suited to their risk profiles and needs, help to promote greater stability of the financial system, by increasing consumers' sensibility to risks.
226. In line with the recommendations provided by the European Commission Expert Group on Regulatory Obstacles to Financial Innovation²¹¹ (ROFIEG), the ESAs believe that the European Commission should give further consideration to the promotion of the use of technology-driven financial services. The ESAs note that a higher level of digital and financial literacy would help consumers make effective use of digital financial services and make effective and responsible choices, increase their welfare, efficiently enforce their rights, identify and report suspicious products and service providers, and have confidence and trust in the digital financial system.
227. In this light, the ESAs highlight the need for further actions at national and European²¹² level to improve digital financial literacy, for example, by enhancing consumers' understanding of

²¹¹ Expert Group on Regulatory Obstacles to Financial Innovation (2019), [30 Recommendations on Regulation, Innovation and Finance](#), Final report of the European Commission, December.

²¹² E.g. [action 7 \("Empowering citizens through financial literacy"\) of the Capital Markets Union 2020 action plan](#), EC website.

opportunities, challenges and potential risks linked to financial innovation, in particular regarding the use of ‘seamless’ online financial services, including via multi-purpose platforms, and cybersecurity issues. Raising awareness of the risks that consumers may face when choosing online or mobile banking services should be further encouraged on a regular basis.²¹³

228. The ESAs would like to recall that as part of their mandate to ‘review and co-ordinate financial literacy and education initiatives by the competent authorities’, the ESAs have started developing various initiatives on financial education:
- a. In March 2020, the EBA published its second Financial Education Report 2019/20²¹⁴, based on the EBA financial education repository²¹⁵ which consists of more than 120 financial education initiatives taken by national authorities carried out primarily during 2018 and 2019. The Report describes the most common approaches used by national authorities and the lessons learned and experiences gained. Compared to the 2018 edition of the report, the most recent edition includes new aspects such as the interplay between financial education and financial conduct regulation and supervision of the financial system and the growing focus on specific target groups, such as children and youth and elderly. It also identifies a number of developments that could influence future financial education initiatives, including behavioural economics, sustainable finance, and data analytics and big data. In addition, the EBA developed a one-page information sheet providing consumers with tips to protect themselves when choosing online or mobile banking services²¹⁶. This document has been translated into all EU official languages²¹⁷ and been disseminated by the national authorities in all Member States. Finally, the EBA organised a virtual panel dedicated to digital financial education and literacy in the Covid-19 context²¹⁸, which brought together high-level speakers (Member of the European Parliament, Academic, consumer and industry representatives).
 - b. EIOPA published a report on Financial Literacy and Education Initiatives by Competent Authorities²¹⁹, notably presenting the national strategies of EIOPA’s member authorities. It has also published, on its website, links to national authorities that are competent in the area of financial literacy and financial education, and developed a European interactive map.²²⁰ In addition, EIOPA published on its website an interactive page which provides information to customers on the different stages of buying and using insurance and pension products.²²¹

²¹³ For instance, EBA (2020a), “[Key tips to protect yourself when choosing online or mobile banking services](#)”, Factsheet for consumers.

²¹⁴ EBA (2020d), [EBA report on financial education 2019/20](#), EBA/Rep/2020/12.

²¹⁵ A repository of NCAs’ financial education initiatives can be consulted at EBA (2020b), [EBA financial education repository 2019/20](#).

²¹⁶ EBA (2020a).

²¹⁷ EBA, [Personal finance at the EU level](#), in *Consumer Corner*, EBA website.

²¹⁸ EBA virtual panel, [Digital financial education and literacy in the Covid-19 context](#), Highlights of the event, 30/09/2021.

²¹⁹ EIOPA (2011), [Report on Financial Literacy and Education Initiatives by Competent Authorities](#), EIOPA-CCPFI-11/018, 16 December.

²²⁰ EIOPA, [Financial education map](#), EIOPA website.

²²¹ EIOPA (2021), [For consumers](#), EIOPA website.

- c. ESMA has actively promoted exchanges between NCAs regarding their experience and feedback on their financial education initiatives, in particular via the organisation of a financial education day on a regular basis. It also gives priority to actions aimed at achieving its investor protection objective, notably by providing input on some important investor protection topics linked to the MiFID II. ESMA is also engaging on a regular basis with consumer representatives on this issue.
 - d. Further work is expected to be conducted by the ESAs jointly, in particular organising a high-level conference, publishing a thematic report on financial education and digitalisation with a specific focus on cybersecurity, scams and fraud based on a repository collating the NCAs initiatives in that field.
229. Consideration should be also given to the existing OECD core competencies for adults²²² and for youth²²³ which refer to the aspects of knowledge, behaviours and attitudes that form the basis of sound financial decisions and the ongoing work of the Commission and OECD's International Network on Financial Education (OECD-INFE), which jointly develop a financial competence framework for the European Union. The project is developed in the framework of the EU Capital Markets Union Action Plan, which mandates the Commission to work towards the development of a dedicated EU financial competence framework for adults and youth reflecting on recent and emerging issues, including financial digitalisation and sustainable finance.²²⁴
230. In addition, considering the risks of financial exclusion identified by the ESAs and in line with the recommendations provided by the European Commission ROFIEG, further consideration should be given at EU level to promoting the use of those technology-driven financial services as a means to address financial inclusion and prevent the use of those technology-driven financial services in ways that exacerbate financial exclusion or cause unfair discrimination.
231. Further research should be also encouraged to collect further findings to understand the reasons why some people are excluded from the financial system and determine which people run the risk of becoming excluded from it due to the ongoing digitalisation of financial services. This could include further analysing the use of data in AI/Machine Learning models and potential bias, leading to discrimination and exclusion. Financial services should remain accessible also via non-digital means, usable as well as affordable for vulnerable consumers (e.g. disabled people with physical or mental limitations, etc. that prevent them from accessing financial products and services digitally).

²²² OECD (2016), [G20/OECD INFE Core competencies framework on financial literacy for adults](#) (aged 18+).

²²³ OECD (2015), [OECD/INFE Core competencies framework on financial literacy for youth](#) (aged 15 to 18).

²²⁴ See European Commission (2022), "[The Commission and OECD-INFE publish a joint framework for adults to improve individuals' financial skills](#)", 11 January.

3.1.4 Recommendation 4: Address the lack of convergence in classifying cross-border services in a digital context

Recommendation 4: Provide further guidance on the definition of cross-border services in a digital context and strengthen cross-border supervisory coordination.

The ESAs reiterate the previous Joint Committee recommendations outlined under paras. 77 and 78 (concerning the simultaneous exercise of the FoS and the RoE) and 80 (concerning the digital provision of financial services) of the JC report on cross-border supervision of retail financial services.²²⁵

The ESAs also re-state the previous joint-ESA and EBA recommendations to the Commission to update interpretative communications on the provision of cross-border services in a digital context.²²⁶

The ESAs recommend that the Commission consider the need to introduce further guidance on when a digital service is to be regarded as being provided in another Member State (pursuant to the ‘right of establishment’ or ‘freedom to provide services’ cross-border) under sectoral legislations in the banking, payment, insurance and investment sectors and other areas of financial services (e.g. the provision of crypto-asset services).

232. As already highlighted in the cross-sectoral market developments section, and consistent with the wider digitalisation trend across the EU economy, the ESAs have observed an increased use of digital means (including digital platforms) to distribute financial products and services, including on a cross-border basis.
233. The current regulatory framework allows financial entities operating in the banking, insurance and investment services sectors to provide services and/or perform activities throughout the EEA on a cross-border basis, provided that the entity has been authorised under EU rules to operate in one of the Member States. Financial entities can operate on a cross-border basis in line with the respective passporting frameworks that allow either to operate through the ‘right of establishment’ (RoE) or ‘freedom to provide services’ (FoS) provisions.
234. The existing legislative texts applicable in each sector provide for certain requirements for entities passporting across the EEA, including notifications and requirements for the exchange of information between home and host authorities, for example, as regards the arrangements for home-host cooperation pursuant to the PSD2.²²⁷ In some cases, the ESAs have followed up with additional tool measures as Decisions of their Boards of Supervisors to supplement legislation²²⁸. However, several issues have been brought to the attention of the ESAs which

²²⁵ JC of the ESAs (2019a), *Report on cross-border supervision of retail financial services*, pp. 25-26.

²²⁶ For further background, see EBA (2021e), Text Box 5, pp. 38-40.

²²⁷ The framework for cooperation and the exchange of information between competent authorities under the PSD2: <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=OJ:L:2021:343:FULL&from=EN>.

²²⁸ For example, EIOPA’s Decision on the Cooperation of Competent Authorities under the IDD provides for a working definition of when ‘freedom to provide services’ is triggered:

might require further regulatory action. These issues are not new, but they have been further highlighted due to the increased provision of services through digital means and particularly through digital platforms and in fragmented value chains. It should also be noted that the 'depth' of the issues encountered may also change depending on the regulatory frameworks that apply to each sector.

235. More specifically, and as highlighted by the EBA as part of its report on digital platforms²²⁹, NCAs have stated concerns about challenges that financial institutions and NCAs are facing in determining whether a financial service offered by digital means is being provided via the 'cross-border provision of services'²³⁰ and therefore whether a notification obligation is triggered.
236. Additionally, NCAs responding to both ESMA and EBA's surveys have highlighted visibility issues around the use of platforms by financial institutions. In fact, it was highlighted that, even if an obligation is triggered to notify the home NCA of the cross-border provision of services, the notification would not typically include any information about how that service is being carried out (e.g., authorities do not typically receive information about the modalities of the service provision, including the use of digital platforms).
237. Finally, the EBA observed that, due to the above-mentioned uncertainties as to the classification of a service under RoE and FoS, consumers and investors seemingly have more difficulties in identifying the applicable consumer protection measures, and therefore which authority is the relevant authority for specific supervisory purposes and which schemes (e.g., for complaint-handling and redress) are applicable.
238. Many of these issues are not new. Indeed, it should be noted that several issues in relation to the provision of services cross-border had been previously highlighted to the European Commission, inter alia, through work performed by the Joint Committee (result in the report²³¹ published in 2019) and also by the EBA through the publication of a number of reports.
239. Of the issues identified in the report, the ESAs would like to re-emphasise the findings identified in relation to the digital provision of financial services. In fact, the analysis performed by the ESAs has highlighted that it is not always clear whether activities carried out through digital

An Intermediary or Ancillary Intermediary is operating under freedom to provide services ("FoS") if it intends to provide a policyholder, who is established in a Member State different from the one where the Intermediary or Ancillary Intermediary is registered, with an insurance contract relating to a risk situated in a Member State different from the Member State where the Intermediary or Ancillary Intermediary is registered.

In addition, an example is included concerning electronic distance or distance marketing activities:

If the content of the website of an Intermediary or Ancillary Intermediary is general and only in the language of the Member State of the Intermediary or Ancillary Intermediary, if it is not addressed to a specific group of customers or customers in specific Member States and when the customer is not able to directly or indirectly conclude an insurance contract using a website or other media, then the Intermediary or Ancillary Intermediary cannot be considered as actively seeking these customers and therefore cannot be considered as having the intention to do FoS in the Member State, where those customers are established. If an Intermediary or Ancillary Intermediary is contacted by those customers, it will not be considered as an intention to write business under FoS in the Member State of residence or of establishment of these customers.

²²⁹ See further EBA (2021e), pp. 38-40, 42.

²³⁰ This is not withstanding potential issues that may arise in relation to the legal qualification of financial services.

²³¹ Joint Committee of the ESAs (2019a).

means were falling within the remit of the FoS or of the RoE. The ESAs believe that the lack of a clear definition of the cross-border provision of financial services leaves the door open for a range of interpretations that could result in protracted and unsuccessful discussions between NCAs and/or between NCAs and financial institutions as to the applicable regulatory requirements and supervisory powers, and also give rise to confusion for customers.

240. As noted above, this issue has been further evidenced as part of this call for advice. Therefore, the ESAs would like to reiterate the observation outlined under paras. 77 and 78 of the JC report with regard to the simultaneous exercise of the FoS and the RoE that might create uncertainty about responsibilities between host or home NCA and under para. 80 of the JC report regarding the digital provision of financial services, which states the following: ‘The ESAs consider that, under the applicable EU law, it is not always clear whether activities carried out through digital means fall within the remit of the FoS or of the RoE. The ESAs are of the view that more clarity on this issue cannot be provided through Level 3 work and that such clarity should be provided by the EU co-legislators, especially in the light of the growing phenomenon of the digitalisation of financial services’. In insurance distribution, the issue of providing more legal certainty in the IDD over the triggering elements for FoS and RoE activities of insurance intermediaries will need to be considered in the forthcoming IDD Review, not least because some insurance intermediaries no longer need a physical presence (i.e. branch office) in the host Member State, since they can reach consumers situated in the host Member State through digital channels.
241. As noted by the EBA in its 2019 report on potential impediments to the cross-border provision of banking and payment services²³², and the 2021 report on digital platforms²³³, clarity on this important matter will support financial institutions and NCAs in determining how an activity carried out using a digital platform is to be treated under EU and national law, including as regards the application of notification requirements which provide the foundation for better visibility over the cross-border provision of services.

²³² EBA (2019c).

²³³ EBA (2021e).

3.1.5 Recommendation 5: Strengthen skills and resources at supervisors

Recommendation 5: Strengthen supervisory skills and resources to effectively monitor financial firms' digital transformations.

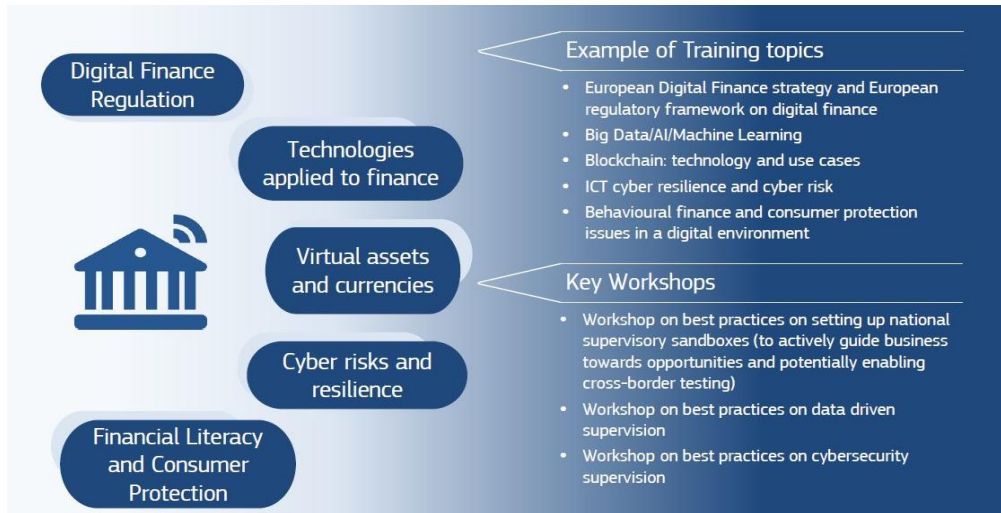
The ESAs recommend that the European Commission consider, in close cooperation with the ESAs, possible ways to enhance resources and skills at national and EU supervisors, with a view to supervise Digital Finance more effectively.

242. Supervised entities are free to explore new technologies, provided their risk management, internal processes and controls systems take fully into account the new risks that these technologies induce. While it remains the sole responsibility of firms to conform with all applicable rules regardless of the technology or business models used, the growing digitalisation of finance, and the increasing use of technologies, such as big data, AI, DLT/blockchain and other emerging technologies, requires supervisors to acquire new skills and enhanced resources in order to understand the benefits of these technologies and to supervise any risks effectively. In particular, these changes demand experts with the necessary technical and digital knowledge to effectively monitor market developments and the application of the rules as well as new/upgraded supervisory tools (commonly known as SupTech). In this fast-changing environment, supervisors need to have relevant resources to engage with firms, both new entrants and incumbents and also technology companies serving the financial sector, as well as understand the emerging business models, front and back-office processes and the technologies involved, assess the associated opportunities and risks and undertake the necessary regulatory/supervisory actions in a timely manner. In particular, understanding changes in relation to the nature, size and risk profile of financial institutions, their interactions with technology providers and the possible displacement of risks between different actors, risk concentrations and systemic relevance as well as the occurrence of new forms of conflict of interests is vital for supervisors.
243. The Commission should consider, in close cooperation with the ESAs, possible ways to enhance resources and skills at national and EU supervisor level, with a view to supervise Digital Finance more effectively. Specifically in respect to AML/CFT, the Commission should consider extending the requirement for training programs to supervisors with a view to ensuring adequate supervision of AML/CFT issues that may arise with disruptive innovations and business models.
244. The ESAs support the Commission's work on the Digital Finance Supervisory Academy which will help address this issue.²³⁴ The Academy is targeted at Member States wishing to strengthen supervisory capacity in the area of digital finance and will be open for participation to supervisors and financial intelligence units from all EU Member States and ESAs' staff as of Q4 2022.
245. Additionally, the ESAs will continue to explore how to strengthen the EFIF (see **Box 5**) for knowledge exchange and share of technological expertise on the regulatory treatment of innovative products, services and business models as well as organising knowledge-sharing and knowledge-building initiatives for the NCAs (e.g. supervisory workshops, roundtables,

²³⁴ European Commission, [EU Supervisory Digital Finance Academy: Strengthening Supervisory Capacity in innovative Digital Finance](#), EC website.

dedicated training sessions, discussions on practical use cases both online and on-premise format).

Figure 4: EU Supervisory Digital Finance Academy: A flagship project under the Technical Support Instrument



Source: European Commission website (2021).

3.1.6 Recommendation 6: Support a convergent approach to ML/TF risks in a digital context

Recommendation 6: The ESAs recommend that the Commission consider the following actions, with a view to supporting greater convergence in the identification and mitigation of ML/TF risks in a digital context:

- a) Mandate the AMLA, in close cooperation with the ESAs, to issue guidelines on outsourcing and governance arrangements for Customer Due Diligence purposes, as foreseen in Article 41 of the proposed AML Regulation;
- b) Clarify the application of the data protection framework in the CDD and wider AML/CFT compliance context;
- c) Mandate AMLA to issue AML/CFT guidelines on crowdfunding and assess as a matter of priority whether to subject crowdfunding platforms licenced under Regulation (EU) 2020/1503 to Union AML/CFT legislation in order to mitigate risks of ML/TF, and to mitigate risks of regulatory arbitrage;
- d) Require ESAs to issue a thematic review of ML/TF risk management in the digital finance context, which identifies best practices.

In addition to the specific recommendations set above and in other cross-sectoral recommendations of this report, it is also relevant to:

- a) Promote a greater understanding of the risks and opportunities posed by digital finance by supervisors, institutions, and external providers (obliged entities and non-obliged entities);
- b) (b) Promote awareness of providers' AML/CFT obligations in relation to the above aspects of digital finance.

246. The ESAs note that ML/TF risks stemming from the growing digitalisation of financial services as highlighted in section 2.2.4 are already largely addressed through:

- a. Existing EBA instruments on AML/CFT:
 - Guidelines on the characteristics of a risk-based approach to anti-money laundering and terrorist financing supervision, and the steps to be taken when conducting supervision on a risk-sensitive basis under Art. 48(10) of Directive 2015/849/EU (amending the Joint Guidelines ESAs 2016 72), The Risk-Based Supervision Guidelines²³⁵;

²³⁵ EBA (2021g), [Guidelines on the characteristics of a risk-based approach to anti-money laundering and terrorist financing supervision, and the steps to be taken when conducting supervision on a risk-sensitive basis under Article 48\(10\) of Directive \(EU\) 2015/849 \(amending the Joint Guidelines ESAs 2016 72\)](#), EBA/GL/2021/16, 16 December.

- Opinion of the European Banking Authority on the risks of money laundering and terrorist financing affecting the European Union’s financial sector²³⁶;
 - Guidelines on customer due diligence and the factors credit and financial institutions should consider when assessing the money laundering and terrorist financing risk associated with individual business relationships and occasional transactions (‘The ML/TF Risk Factors Guidelines’) under Articles 17 and 18(4) of Directive (EU) 2015/849²³⁷;
- b. The European Commission’s 2021 legislative proposals on AML/CFT²³⁸, in which the Commission proposes to:
- Put in place a single AML/CFT rulebook, with more harmonised CDD rules that would be applicable directly in all Member States, which could limit divergence of institutions’ practices and reduce the risks associated with third-party reliance. See in particular a proposal for draft RTS on the performance of CDD in Article 22 of the proposed AMLR²³⁹;
 - Require a future EU-level AML Authority (AMLA) to issue guidelines on the conditions that have to be met to rely on third parties for CDD purposes and to establish outsourcing relationships, as well as the roles and responsibilities of each party to those relationships in Article 41 of the proposed AMLR;
 - Include in the new proposal that an AMLA shall cooperate with various stakeholders from the financial and the non-financial sector and strengthen cooperation between FIUs and AML/CFT supervisors; additionally, an AMLA shall also be responsible for ‘indirect supervision of both financial sector and non-financial sector obliged entities through oversight of supervisors or self-regulatory bodies’;
 - Extend the list of obliged entities to crowdfunding platforms;
 - Introduce a requirement, in Article 13 of the proposed AMLR, that an AMLA should ‘develop draft regulatory technical standards and (...) shall specify the minimum requirements of group-wide policies, including minimum standards for information sharing within the group, the role and responsibilities of parent undertakings that are not themselves obliged entities with respect to ensuring group-wide compliance with AML/CFT requirements and the conditions under which the provisions of this Article apply to entities that are part of structures which share common ownership, management or compliance control, including networks or partnerships’.

247. When considering which recommendations to put forward, EBA staff took into account those existing standards and provisions, as well as the July 2021 AML/CFT Package proposals. EBA staff also considered cross-sectoral recommendations put forward in this response to the Call for Advice. The proposals in this section are therefore designed to address remaining gaps and

²³⁶ EBA (2021c), [Opinion of the European Banking Authority on the risks of money laundering and terrorist financing affecting the European Union’s financial sector](#), EBA/Op/2021/04, 03 April.

²³⁷ EBA (2021a), [Guidelines on customer due diligence and the factors credit and financial institutions should consider when assessing the money laundering and terrorist financing risk associated with individual businessrelationships and occasional transactions \(‘The ML/TF Risk Factors Guidelines’\) under Articles 17 and 18\(4\) of Directive \(EU\) 2015/849](#), Final Report, EBA/GL/2021/02, 01 March.

²³⁸ Currently under discussion: European Commission (2021b), [Anti-money laundering and countering the financing of terrorism legislative package](#), 20 July.

²³⁹ Proposal for a regulation of the European Parliament and of the Council on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing, COM/2021/420 final, 20/07/2021.

serve to strengthen NCAs' understanding of key ML/TF risks and to create a common approach to tackling those risks in Europe.

(a) Amending Article 41 of the proposed AML Regulation to introduce a targeted mandate for an AMLA to issue outsourcing and governance arrangement Guidelines, which it should elaborate in close cooperation with the ESAs

248. Article 41 of the proposed AMLR mandates the AMLA (the new AML/CFT authority) to issue guidelines addressed to obliged entities on the performance by third parties. To ensure consistency of approaches with the existent ESAs Guidelines on outsourcing, the ESAs believe that the AMLA should draft its guidelines in close cooperation with the ESAs.

249. These Guidelines should focus on CDD in particular and respect the principle of proportionality.

(b) Clarify the application of the data protection framework in the Customer Due Diligence (CDD) and wider AML/CFT compliance context

250. As highlighted previously, including in the EBA's response to the Commission's Call for Advice on the future AML/CFT framework²⁴⁰, there is a need to clarify how GDPR provisions interact with the EU's AML/CFT objectives to ensure that ML/TF risk is addressed consistently and in compliance with data protection requirements. A clear understanding of the application of the GDPR to AML/CFT provisions will ensure that expectations are unambiguous.

251. This is also in line with the European Data Protection Board (EDPB) letter to the European Commission on the protection of personal data in the AML/CFT legislative proposals²⁴¹, presented before the proposal, and the European Data Protection Supervisor Opinion on the AML/CFT package of legislative proposals²⁴², issued in September 2021.

252. In respect of the problems identified over this Call for Advice, the current understanding is that the proposals do not sufficiently cover some aspects being recommended by the EDPB and the EBA response to the Commission's Call for Advice on the future AML/CFT framework as follows:

- a. the entities to and the purposes for which the personal data may be disclosed, with specific reference the sharing of information for AML/CFT purposes within a group to other financial market participants;
- b. the categories of personal data to be processed by obliged entities, the processing operations, and procedures, including measures to ensure lawful and fair processing.

253. The ESAs therefore recommend that the Commission clarify the application of the data protection framework in the context of CDD and AML/CFT compliance, as set out in the EBA response to the Commission's CfA on the future AML/CFT framework.²⁴³

²⁴⁰ EBA (2020e), [EBA Report on the future of AML/CFT framework in the EU](#), EBA/REP/2020/25, pp. 54-56.

²⁴¹ European Data Protection Board (2021), [Letter to the European Commission on the protection of personal data in the AML-CFT legislative proposals](#), Ref. OUT2021-0088, 19 May.

²⁴² European Data Protection Supervisor (2021b), [Opinion 12/2021 on the anti-money laundering and countering the financing of terrorism \(AML/CFT\) package of legislative proposals](#), 22 September.

²⁴³ See footnote 240.

(c) Mandate AMLA to issue AML/CFT guidelines on crowdfunding and further assess as a priority whether to subject crowdfunding platforms licenced under Regulation (EU) 2020/1503 to Union AML CFT legislation in order to mitigate risks of ML/TF, and to mitigate risks of regulatory arbitrage

254. It is important to set clear EU-wide regulatory expectations towards crowdfunding platforms, by: a) ensuring all types of platforms are in the scope of relevant AML/CFT legislation; b) mandating the new AMLA to issue AML/CFT guidelines.
255. The new AML Package has expanded the list of obliged entities to other sectors such as crowdfunding platforms, but only the ones which fall outside the scope of Regulation (EU) 2020/1503²⁴⁴. Despite the fact that Regulation 2020/1503 already sets up some AML/CFT requirements in terms of due diligence specifically of some crowdfunding service providers, i.e. those providing services to businesses, not to consumers – in respect of project owners (Art. 5(2)(a)) and within authorisation procedures (Art. 8(3)(a) and Art. 17(1)) – the envisaged mitigation of new and emerging risks is only achieved if there is a transversal and harmonised application of the EU AML/CFT legislation to all crowdfunding platforms, including the ones offering services to project owners that are consumers. The safeguards to be addressed by Regulation 2020/1503 are complementary to the ones being set in the AMLR proposal, but may not be enough per se to effectively mitigate ML/TF risks. Therefore, the ESAs recommend that the Commission assess as a priority whether to subject crowdfunding platforms licensed under Regulation 2020/1503 to EU AML/CFT legislation, in line as well with the *EBA Report on the future AML/CFT framework in the EU*.
256. In addition, Guidelines on crowdfunding platforms (both outside and within the scope of Regulation (EU) 2020/1503) are required to clearly set out what adequate and coherent safeguards would look like, bearing in mind the nature of this activity. The ESAs recommend mandating an AMLA to issue AML/CFT guidelines on crowdfunding. The existing EBA’s ML/TF Risk Factor Guidelines and EBA’s Risk-based Supervision Guidelines already contain some sectoral guidelines for crowdfunding platforms and would, in the ESAs’ view, be a useful basis in this regard.

(d) Request ESAs to issue a thematic review with best practices

257. The ESAs recommend that the Commission request ESAs – to ensure a swift action even before an AMLA is set up – to issue a thematic review with an associated report to identify the solutions in place and best AML/CFT practices to overcome the issues determined in this Call for Advice. This would be in the form of a stock-take analysis, in a different perspective to the work on Call for Advice, with the goal of studying specific AML/CFT solutions being used by market participants to address these issues.
258. The thematic review would be focus on identifying good industry practices and thus akin to guidance for NCAs.

²⁴⁴ Regulation (EU) 2020/1503 of the European Parliament and of the Council of 7 October 2020 on European crowdfunding service providers for business, and amending Regulation (EU) 2017/1129 and Directive 2019/1937/EU, OJ L 347, 20/10/2020.

3.1.7 Recommendation 7: Ensure the sufficient coverage of MAGs by sectoral prudential consolidation/group structured supervision rules

Recommendation 7a: Revise the definitions dealing with the entities to be included in the scope of prudential consolidation.

The ESAs draw particular attention to the need to revise some of the definitions used in the CRD/CRR and in Solvency II (e.g. ‘ancillary services undertaking’) and, in this regard, they welcome the Commission’s recent proposal to revise certain CRR definitions that are relevant for the purposes of the application of the bank consolidation framework under the CRD/CRR.²⁴⁵

Regarding Solvency II and IFR²⁴⁶, the Commission is invited to consider cross-sectoral consistency of such definitions and the proposed adjustment for Article 1(1)(53) of the Solvency II Delegated Regulation²⁴⁷ concerning the definition of ASU:

‘non-regulated undertaking the principal activity of which consists of owning or managing property, managing data-processing services or any other digital services, health and care services or any other similar activity which is ancillary to the principal activity of one or more insurance or reinsurance undertakings, including if the business is performed through insurance intermediaries.’ “non-regulated undertaking the principal activity of which consists of owning or managing property, managing data-processing services or any other digital services, health and care services or any other similar activity which is ancillary to the principal activity of one or more insurance or reinsurance undertakings, including if the business is performed through insurance intermediaries.’

259. EU sectoral rules concerning prudential consolidation rely on concepts such as the definition of financial institutions, the definition of ancillary services undertakings, and the definition of financial holding companies. However, there is a lack of clarity in some of the current definitions, and some are outdated. This might give rise to some loopholes taking account of market developments.
260. For example, as previously identified by the EBA²⁴⁸, the lack of clarity in the CRD/CRR definition of ‘ancillary services undertaking’ (ASU), including the interplay with the activities listed in Article 89(1)(b) CRR, and the limitations in the definition of ‘financial holding company’²⁴⁹ may

²⁴⁵ Indeed, the proposal includes revisions of a wide range of definitions including ancillary services undertaking, financial holding company, financial institution, parent undertaking and subsidiary.

²⁴⁶ Regulation (EU) 2019/2033 of the European Parliament and of the Council of 27 November 2019 on the prudential requirements of investment firms and amending Regulations (EU) No 1093/2010, (EU) No 575/2013, (EU) No 600/2014 and (EU) No 806/2014, OJ L 314, 05/12/2019.

²⁴⁷ Commission Delegated Regulation (EU) 2015/35.

²⁴⁸ See further EBA (2017a), [Opinion and report on regulatory perimeter issues relating to the CRDIV/CRR](#), EBA/Op/2017/13, 09 November.

²⁴⁹ Indeed, to fall under the CRR definition of financial holding company, an undertaking – as a precondition – needs to qualify as financial institution according to Art. 4(1)(26) CRR. However, under the current regulatory framework, the term ‘financial institution’ is defined too narrowly to capture the relevant parent entities of banking groups. Moreover, the quantitative thresholds included in the definition of financial holding company

reduce the effectiveness of the current regulatory consolidation framework to effectively capture emerging risks in mixed activity groups. Additionally, although the provisions of Article 18(8) CRR allow competent authorities to extend consolidation based on step-in risk²⁵⁰ considerations, they are limited to subsidiary undertakings and undertakings in which a participation is held. This means that overall, the current framework does not enable competent authorities to ask for consolidation of all the relevant non-financial entities of BigTech groups and other MAGs.

261. As regards the potential amendments to the EU banking regulation (CRR, CRD) (which also applies in some cases to the securities markets sector²⁵¹), the EBA welcomes the Commission's recent proposal aimed at ensuring that groups headed by FinTech companies and including at least one credit institution are subject to consolidated supervision. This definition should also be modified consistently with insurance and IFR²⁵² definitions and ensure that all non-regulated entities providing essential digital activities to the banking group are scoped in.
262. In respect of the definition of 'financial institution' and 'financial holding company' in the context of the CRD/CRR, which are core to the delineation of the consolidation perimeter, the ESAs have identified cases where the consolidation of entities would not apply because the provided financial services²⁵³ do not represent the predominant activities of the entity, or in the case of the 'financial holding company,' the *relative threshold* of 50%. As such, entities within a group may undertake material financial activities without triggering the relevant definitions and thus escape consolidated supervision regardless of the absolute size of their financial activities where these activities are mixed with non-financial activities. This could give rise to the risk of regulatory arbitrage in the event that new digital actors were to deliberately structure their activities to avoid qualifying as a financial holding company, and merits future consideration (for the avoidance of doubt, it is noted that the proposals in the CRD/CRR III would not fully address this regulatory arbitrage risk).
263. Regarding Solvency II, EIOPA has also identified the need to adjust the definition of ASUs. ASUs are defined in Article 1(1)(53) of the Delegated Regulation as '*non-regulated undertaking the principal activity of which consists of owning or managing property, managing data-processing*

may leave room for groups to structure themselves in a way that would allow them to escape prudential consolidation. Indeed, MAGs/BigTechs may carry out financial activities that although not being their prevalent activity, still may reach important amounts in absolute terms.

²⁵⁰ As defined by the Basel Committee on Banking Supervision, 'step-in risk' is the risk that a bank decides to provide financial support to an unconsolidated entity that is facing stress, in the absence of, or in excess of, any contractual obligations to provide such support. The main reason for step-in risk might be to avoid the reputational risk that a bank might suffer were it not to provide support to an entity facing a stress situation. Indeed, as discussed above, the financial crisis provided evidence that a bank might have incentives beyond contractual obligation or equity ties to 'step in' to support unconsolidated entities to which it is connected. (BCBS (2017)).

²⁵¹ In fact, investment firms (subject to the MiFID framework) or UCITS management companies (subject to Directive 2009/65/EC) can be consolidated in a banking group and investment firms classified under Class 1 of IFR are subject to CRR and CRD.

²⁵² Regulation (EU) 2019/2033 of the European Parliament and of the Council of 27 November 2019 on the prudential requirements of investment firms and amending Regulations (EU) 1093/2010, (EU) 575/2013, (EU) 600/2014 and (EU) 806/2014, OJ L 314, 05/12/2019.

²⁵³ As defined in Annex 1 to the CRD.

services, health and care services or any other similar activity which is ancillary to the principal activity of one or more insurance or reinsurance undertakings’.

264. The reference to ‘data-processing services’ allows for a general interpretation, but EIOPA recommends that the Commission consider a revision of the ancillary service undertakings (ASUs) definition in order to enhance cross-sectoral consistency and to reflect better the reality of the digital economy. This is to ensure that non-regulated entities providing tech/digital activities that become essential for the selling, pricing and management of insurance operations or portfolios of the insurance regulated entities are considered when identifying a group and defining the scope of the group. It would result in capturing risks more adequately in Pillar 1 requirements (for an Insurance Holding Company and a Mixed Financial Holding Company)²⁵⁴ and would also raise (compared to general expectation, see also EIOPA Guideline number 15 on Own Risk Solvency Assessment – ORSA²⁵⁵) the supervisory expectation on how the risks is taken into consideration in the ORSA. This proposal does not impact the power of group supervisors to decide on a case-by-case basis not to include an undertaking in the group supervision, as defined in Article 214(2) of Solvency II.

²⁵⁴ Consolidation will depend on whether it is a subsidiary or a related undertaking, see Article 335 of the Delegated Regulation.

²⁵⁵ EIOPA (2015), [Guidelines on Own Risk Solvency Assessment](#), EIOPA-BoS-14/259, September.

Recommendation 7b: Consider the revision of existing consolidation rules (through adapting the CRR/CRD, IFR and Solvency II) and the creation of bespoke consolidation rules to ensure that the specific nature and inherent risks of MAGs carrying out financial services are adequately captured.

The ESAs recommend that the Commission take action to coordinate the consideration by the ESAs of the revision of existing consolidation rules and the potential creation of consolidation rules (whether through additional amendments to the CRD/CRR, IFR/IFD and Solvency II and/or new bespoke rules) to ensure the adequate capture of the specific nature and inherent risks of new combinations of activities carried out within groups and to mitigate risks of regulatory arbitrage.

In particular, the ESAs note that some MAGs, including BigTechs, do not have entities within their groups to which existing consolidation rules under the CRD/CRR/Solvency II would apply. However, such MAGs may carry out via subsidiary companies a range of financial services, including payments and lending services. Therefore, to effectively mitigate prudential risks and risks of regulatory arbitrage and to protect the level playing field having regard to banking and other groups already subject to consolidated supervision, there is a need to consider whether new bespoke consolidation rules are needed for these new types of MAGs. The ESAs note that the question of whether to introduce consolidated supervision in such cases will be subject to consideration in the context of the review of relevant sectoral measures, notably the PSD2²⁵⁶, and welcome this approach. In carrying out the necessary analysis, the ESAs recommend, in particular, a consideration of:

- the intersection of any new consolidation rules (e.g. if introduced in the context of the revision of the PSD2 or in any future new EU-wide non-bank lending sectoral regime). This would be particularly important in the case of groups that may have more than one relevant financial institution to which sectoral consolidation rules relate – with a need for clear indicators to establish when and how the consolidation rules apply to ensure the most effective risk mitigation (e.g. one possibility could be to introduce a new, limited, exemption to the current obligation of having to consolidate all entities under CRR as soon as there is one credit institution – no matter how small it is – but instead to trigger consolidation under a new sectoral measure reflecting the most predominant financial service carried out in the group – e.g. via a group undertaking that is a payment institution);
- the possibility of requiring the establishment of intermediate parent undertakings and/or of restructuring MAGs in order to ensure the effective capture of risks and application of consolidation rules. This would be particularly crucial where core financial activities such as providing loans and payment services are being performed outside of the bank regulatory perimeter. Prudentially unconsolidated financial activities, above a defined threshold, could hence be ‘grouped together’ under this intermediate holding and would be part of the prudentially supervised group. The conditions for requiring the establishment of an IPU (whether automatic or at the discretion of the supervisor) and the calibration of the relevant threshold(s) would require careful consideration (e.g. taking account of revenues, risks and/or asset size of financial activities);
- enhancing the importance of existing risk management tools (e.g. Own Risk Solvency Assessment) to explicitly acknowledge risks stemming from MAGs and to consider the relation between the regulated undertaking and the tech/digital entities part of the MAG;

²⁵⁶ European Commission (2021f), [Call for advice to the European Banking Authority \(EBA\) on the review of the payment services Directive \(PSD2\)](#), 18 October.

- the availability and scope of crisis management tools such as early intervention powers, recovery plans, and resolution tools.

It is, however, of paramount importance that a thorough prior analysis is carried out to determine what the risks are and what impact prudential consolidation could have, also taking account of the fact that prior experience (in particular in the context of the new investment firm framework) has demonstrated that banking rules do not always fit institutions other than banks.

Note that for the insurance sector, these recommendations are to be read in conjunction with the relevant amendments included in the review of the Solvency II Directive as proposed by the Commission, in particular regarding horizontal groups with no capital links between different undertakings and the power to require the group to restructure.

265. At present, the current sectoral prudential consolidation rules (CRD/CRR, IFR and Solvency II) do not adequately capture the specific nature and the inherent risks of new combinations of activities carried out by MAGs, including BigTechs. For example, unless a relevant qualifying entity exists within the group, the rules do not extend to MAGs carrying out payment, crypto-asset, lending or other financial services via different affiliated undertakings. Although the significance of this point remains to be confirmed by a thorough risk analysis, the situation may evolve quickly and the preliminary view of the ESAs is that this situation could lead to an insufficient capture of risks (resulting in potential prudential resilience risks and ultimately financial stability risks), regulatory arbitrage and level playing field issues compared to groups that are already captured through the consolidation frameworks.
266. More particularly, MAGs can pose financial, reputational, legal, operational, concentration, intragroup and systemic risks that would only be captured by the CRR/Solvency II prudential consolidation rules in the event that the MAG were to meet the necessary structural pre-conditions for a traditional banking group or financial holding group. In this regard, it is worth noting that while the CRR already envisages the possibility for competent authorities to require horizontal consolidation where certain conditions are met²⁵⁷, this provision is only applicable in cases of ‘sister’ entities that are institutions, financial institutions or ancillary services undertakings and, as such, may not ensure the extension of prudential consolidation to all types of MAGs. In addition, as shown by the Wirecard case (see **Box 2**), the positioning of a regulated entity within a group structure (i.e. as a parent or a subsidiary) can have an impact on the scope of prudential consolidation rules (if any) that are engaged. The Commission proposal for CRR III has proposed a number of amendments to definitions relating to prudential consolidation that cater for the Wirecard case (see **Recommendation 7a** above), but these amendments do not necessarily address all possible arbitrage cases under the CRD/CRR. Another regulatory arbitrage possibility stems from the issue identified in the context of the background to Recommendation 7a. MAGs have the capacity to mix an entity’s financial and non-financial activities (e.g. the provision of data, technological infrastructure etc.) in order to arbitrage the principal activity criteria needed to trigger the ‘financial institution’ definition, thereby evading prudential consolidation and supervision.

²⁵⁷ In particular, according to Article 18(6)(b) of CRR: ‘Competent authorities shall determine whether and how consolidation is to be carried out in the following cases:

(a) [...]; and

(b) where two or more institutions or financial institutions are placed under single management other than pursuant to a contract, clauses of their memoranda or articles of association.’

267. To address these issues, the ESAs recommend that the European Commission coordinate the ESAs in carrying out a cross-sectoral ‘gap analysis’ as regards the scope of application of existing prudential consolidation rules vs. new group structures, leveraging insights from the ESAs and NCAs about different types of group structures across the financial sector, and from the work proposed to be carried out by the EBA under the new mandate envisaged in the CRR III proposal (see further below). In particular, it is of paramount importance that a thorough analysis be carried out to determine what the risks to be captured are and what impact prudential consolidation will have, considering that prior experience (in particular in the context of the new investment firm framework) has demonstrated that banking rules are not always fit for entities other than banks. On that basis, should consolidation be a way forward, a determination as to whether banking rules are fit for MAGs and BigTechs will have to be done.
268. The European Commission should require the ESAs to consider potential trigger conditions for the application of any necessary consolidation rules to new types of MAG (e.g. combinations of different financial services in the group, volume/value thresholds/number of Member States in which the activities are carried out by the group and its subsidiaries) taking account of arbitrage risks, notably those identified above.
269. Finally, the ESAs draw attention to the proposal for the CRR III which envisages a specific mandate for the EBA to report to the Commission on the completeness and appropriateness of the new set of definitions and provisions. This would allow the EBA to further investigate, inter alia, whether the empowerments of the supervisors and their ability to adapt their supervisory approach to new sources of risks might be unintentionally constrained by any discrepancies or loopholes in the new regulatory provisions or in their interaction with the applicable accounting framework. In this context, the EBA will reflect further on:
- a. the role and structure of MAGs and how their activities meet the definition of financial institutions or ancillary services undertakings,
 - b. the interactions with the possible set-up of intermediate parent entities, and
 - c. ways to appreciate all the financial activities performed by the different entities within a group.

Box 3: Solvency II Group Supervision and Solvency II Review

There are three group scenarios possible under Solvency II in cases where a non-insurance company is the parent. The type of parent and type of subsidiary determine the exact classification and supervision. In Solvency II, a ‘non-insurance parent’ can be qualified as an Insurance Holding Company (IHC), a Mixed Financial Holding Company (MFHC) or a Mixed Activity Insurance Holding Company (MAIHC).²⁵⁸

In group supervision, it is important to take into account also non-regulated entities as part of a group that contains an insurance or reinsurance undertaking (see also Recital 109 of Solvency II). In the EIOPA Opinion on the 2020 Review of Solvency II, EIOPA identified a ‘lack of clarity in Article 212 of the Solvency II Directive regarding the definitions that support the identification of a group to capture undertakings, which, together, form a de facto group, upon supervisory powers’. This lack has been addressed by the Commission in the review of Solvency II.

²⁵⁸ IHC: mainly holds (re)insurance undertakings; MFHC: holds a financial conglomerate with activities mainly in the financial sector; MAIHC: holds a mixture of regulated and non-regulated activities (please refer to the relevant articles for the full definition).

An IHC or MFHC (Art. 213 (2)(b-c)) is subject to full group supervision in accordance with Articles 218 to 258 (Art. 213(2)) covering the requirements for Group solvency, risk concentration, intra group transactions, risk management and internal control. A tech/digital entity within this group will therefore in principle be included. In the proposal by the Commission regarding the review of the definition of IHC, more quantifiable clarity has been given when a company constitutes as an IHC. Given this and the full scope of group supervision for groups with a MFHC or IHC as a parent, there is no clear need to advise any change to the regulatory framework for these types of groups. The definition of IHC and MFHC, if supported by additional guidance as highlighted in the 2020 Solvency II Review Opinion, is considered as needed and adequate.

A MAIHC (Art. 213 (2)(d)) is subject to group supervision of Intra-group transactions. In this case, where the parent is a tech/digital non-financial entity contributing directly to the insurance value-chain and/or assuming a material role in the insurance business model of the group, the question is whether the supervision of Intra-Group Transactions (IGTs) is enough to address the risks at the level of the group.

The EIOPA opinion also brought up some proposals regarding the scope of application of group supervision; in particular, it highlighted the need to define criteria that could be used to assess whether undertakings are related to each other, if not by capital links. This is also important in dealing with horizontal groups. The Commission proposals for the Solvency II review included amendments in this area in line with the EIOPA proposal, more clearly identifying the possible non-capital links for the purpose of group supervision. This is a crucial element, especially in light of digitalisation moving from the traditional corporate structures based on capital links to non-capital links that are more difficult to define (see paragraph 9.5 and amendments proposed to Articles 212 and 213).

The Solvency II review also sets an important step to ensure that the IGTs capture more broadly the transaction and risk concentrations in the proposed amendments to Articles 244, 245 and 265, extending the list of indicators based on which a group supervisor may define significant intragroup transactions and risk concentrations and clarify the scope of reporting of intragroup transactions. The proposed changes allow for risk concentration and intragroup transactions as indicators, in addition to Solvency Capital Requirement (SCR) and technical provisions, eligible own funds, other quantitative or qualitative risk-based criteria deemed appropriate or a combination thereof. Regarding IGTs, the NCAs may also require groups to report IGTs involving involving companies that are not (re)insurance-related.

Lessons learned since the Solvency II implementation from the supervision of IGTs when the parent is an MAIHC indicate that monitoring of IGTs requires a holistic view, including assessing the system of governance. However, in many cases, the supervisors face challenges in understanding the full scope of the risks. The need for further tools to identify and assess the risks of such groups has been identified but not discussed in detail. This conclusion gains particular relevance when the entity in the MAG performs digital activities that are directly linked to the insurance value chain and/or assume a material role in the insurance business model of the insurance undertakings of the group. The supervision of IGTs is not considered sufficient from a prudential perspective.

270. EIOPA notes that in the cases where the parent is identified as a MAIHC, and where the relations between the insurance undertaking and a tech/digital entity part of the MAG support heavily the insurance business model and/or heavily impact the insurance value chain, enhancing supervision using pillar II requirements, such as the requirement that the ORSA complements the IGT supervision; could also be of added value.

271. The requirement would be on the Insurance and reinsurance undertakings which are not part of a group referred to in points (a), (b) or (c) of Art. 213(2) of Directive 2009/138/EC and the parent undertaking of which is a mixed-activity insurance holding company, and would in practice be a clarification that in these cases; the solo ORSA shall include a specific assessment that adequately captures any operational and concentration risk or any other risk stemming from any undertaking within the group affecting the sustainability and continuity of the business model of the group.
272. Since the ORSA is a crucial tool for the prudential assessment of the group, the group should ensure that the risks arising from the non-financial affiliates of the group and from the specificities of the services provided are taken into consideration, including the concentration risk and interdependency risks, since tech/digital non-financial affiliates are not regulated and supervised at individual level. When such relations and interdependencies are identified, the participating insurance and reinsurance undertakings, insurance holding companies and mixed financial holding companies are responsible for the identification of any material risks and should be able to explain them to the group supervisor under the Group ORSA.
273. The ORSA at solo level should include an assessment of all material risks, including the concentration risk and interdependency risks arising from the fragmented value chain and/or business model. The assessment should allow an understanding of the business model and an evaluation of any outsourced services or similar, including data and IT, when such services are strategic and relevant for the business model of the undertaking. EIOPA will consider drafting guidelines or other supervisory convergence tools on such integration in the ORSA, any additional content related to digitalisation and how it should be addressed in ORSA.
274. To have a convergent application of such approach, EIOPA will consider drafting Guidelines or other supervisory convergence tools on how to assess if the relations between the insurance undertaking and a tech/digital entity part of the MAG are supporting heavily the insurance business model and/or heavily impact the insurance value chain.
275. It should be noted that the recommendations related to this section should not impact the power of group supervisors to decide on a case-by-case basis not to include an undertaking in the group supervision, as defined in Article 214(2) of Solvency II. It is not always appropriate to exercise group supervision. When the tech/digital non-financial entities are pure tech companies, such an approach could lead to a material number of tech companies, including the so-called big tech, to be part of group supervision under Solvency II. Application of full group supervision would be seen as disproportionate. The tech companies might also have similar interconnections with a number of insurance undertakings belonging to different groups. In such cases, a practical approach would be for the analysis and supervision of risks to be captured at solo level.

Box 4: Intermediaries in the scope of group supervision

In the provision of insurance products through a digital channel, the roles and responsibilities are less clear between the insurance undertaking and the intermediary. Gradually the intermediary could gain a key decision-making role in the manufacturing process of an insurance product. The more critical this 'outsourcing' becomes, the more it warrants to be in scope of (group) supervision. Given the link between the ORSA and the POG regarding the manufacturing of an insurance product, inclusion of the risks brought to the business model by such intermediaries in pillar 2 requirements could be advocated.

For the insurance intermediaries, the IDD applies directly to its distribution activities and the Solvency II requirements, to the extent applicable, indirectly as they should be covered by the

outsourcing agreement. In light of the entrance of BigTechs, consideration should however be given to how the risks of insurance intermediaries having a significant influence on the insurance value chain of the undertaking are captured in the insurance groups subject to Solvency II, and if there is a need to highlight any supervisory concerns that a group should also take into consideration from a risk management point of view (Pillar II).

The level of interdependency, with or without capital links, having a significant influence on the insurance value chain of the undertaking could be a trigger for the NCA to consider the entity as part of a group. This is also important from a level playing field perspective. If a similar treatment than ASUs is not applied, as defined above, the tech undertaking could request an intermediary license to be kept out of the scope of group supervision.

Although the digitalisation is highlighting the issue, it is not the main driver. When considering that an outsourced activity as defined in the three cases above can also be performed by an intermediary acting as a tech (or using a tech themselves) heavily influencing the value chain of the insurance undertaking, the cases remain applicable. EIOPA will therefore consider intermediaries not specifically for this document, as it requires further analysis, and the EBA will follow this analysis and take such steps as appropriate to analyse any similar issues in the EU's banking and payments sector.

Recommendation 7c: Consider the creation of a structured regulatory and supervisory framework to extend to MAGs involved in financial services.

The ESAs recommend that as well as requiring the ESAs to consider the scope of consolidation rules (Recommendation 7b), the European Commission should require the ESAs to consider the merits of a new framework that would ensure that there is appropriate group-wide supervision of key risks (especially where consolidation rules are not identified appropriately), notably in relation to governance, intra-group transactions and risk concentration. This framework would apply from the moment the MAG's share in financial services reaches a defined critical level.

The ESAs note that the existing framework for the supervision of financial conglomerates (FICOD) applies to specific types of financial group. However, the FICOD is unlikely to be engaged by MAGs taking account of their typical focus on payments and credit-related financial services and core engagement in non-financial services.

The ESAs do not recommend substantially revising the scope of the FICOD in order to bring new types of group in scope, as this approach could bring undue complexity in the application of the FICOD, which has been shown to work very well against its objectives. However, the ESAs consider that the FICOD should be a source for inspiration for the European Commission in considering the development of any new structure cooperation arrangements between supervisors of mixed activity groups, as well as considering other potential approaches. Regard should also be given to approaches adopted by other jurisdictions, as well as dialogue at the level of international standard-setters in order to mitigate risks of forum shopping and to support the emergence of an internationally consistent approach. For example, several recent BIS reflection papers strongly convey the same message, i.e. to apply a consistent approach to new actors from the digital finance, for financial stability stake.²⁵⁹

276. The emergence of MAGs and specifically BigTechs in financial services emphasises the **need for a revision or clarification in the sectoral prudential consolidation rules**. However, extending and adapting the scope of these group-level prudential rules and the regulatory definitions to new types of groups may not always be appropriate, nor would it address the need for structured cooperation between different supervisors engaged in the supervision of financial services subsidiaries within relevant groups. The ESAs note that existing measures to bridge different types of financial sector supervisors would not typically extend to MAGs. The Financial Conglomerates Directive (FICOD) introduces supplementary supervision for financial conglomerates; however it focuses on the bancassurance model, which was the dominant model for large financial groups when the Directive was adopted in 2002. FICOD identifies financial conglomerates as groups with at least one entity in the insurance sector and at least one entity in the banking/investment sector. The group must carry out significant activities in both financial sectors (where quantitative thresholds are used to establish the significance of

²⁵⁹ Crisanto, J. C., Ehrentraud, J. and Fabian, M. (2021), *FSI Briefs No 12*; Carstens, A., Claessens, S., Restoy, F. and Shin, H. S. (2021), *BIS Bulletin No 45*; BIS (2021b), [Regulating Big Tech Conference](#), 11th BIS Research Network meeting, 6-7 October.

the activities in the group²⁶⁰). However, the notion of mixed activity groups active in the financial sector has evolved in recent years and the bancassurance model is no longer the only business model combining financial activities, nor is it the one adopted by the new generation of MAGs for which the issue is to capture financial activities as well as the new kind of systemic risks they pose.²⁶¹ There is a trend not only across the EU, but also at global level, towards a greater variety of operating models among MAGs. MAGs, and especially BigTech groups, are not likely to fall under the scope of FICOD, either because they are not active in both insurance and banking/investment services sectors, or the direct involvement in financial services only complements their non-financial activities. Moreover, even if a group of financial subsidiaries of an MAG was qualified as a financial conglomerate, then only this part of the MAG would fall in scope and not the whole MAG, therefore the risks inherent to MAGs and BigTechs would not be addressed (see further Recommendation 8). Finally, FICOD is aimed at a very specific type of (stable) mixed activity group, whereas BigTechs often evolve their group structures and blend of activities at pace.

277. This means that complex MAG institutional structures are **not subject to effective oversight** over governance requirements **when multiple participants are involved** in offering regulated financial services. As a result, supervisors might not have, for example, sufficient visibility to monitor group-wide governance issues and conflicts of interests (COI) taking place amongst affiliates within a MAG. Additionally, intra-group financial risks are not subject to oversight, resulting in potentially unmonitored contagion risks from one group company to another, which may be significant depending on the scale/criticality of the services offered by the relevant group company.
278. In line with this assessment that the existing frameworks do not capture the risks pertaining to MAGs, the ESAs jointly propose to the Commission that it requires the ESAs to consider the most appropriate way of ensuring an effective and complete capture of the risks that such groups can pose, drawing on the lessons learned from the application of the FICOD.
279. In line with the principle of proportionality, FICOD highlights that the **existing sectoral rules** (for credit institutions, insurance undertakings and investment firms) ***'should be supplemented to a minimum level, in particular to avoid regulatory arbitrage between the sectoral rules and those for financial conglomerates'***²⁶². This principle should also be preserved if a similar approach is taken for MAGs. Considering the aim of prudential supervision, the supplementary entity-based supervision could use the FICOD regime as a guide for the areas in which **structured supervisory coordination** should be focused and could cover **decisions regarding measures** concerning the following:
 - a. **Governance** requirements – with the aim of ensuring that MAGs have sound risk management and internal control mechanisms;

²⁶⁰ Pursuant to Article 3 (1)-(2) FICOD (Directive 2002/87/EC), thresholds for identifying a financial conglomerate are: “[...] the ratio of the balance sheet total of the regulated and non-regulated financial sector entities in the group to the balance sheet total of the group as a whole should exceed 40 % and [...] for each financial sector the average of the ratio of the balance sheet total of that financial sector to the balance sheet total of the financial sector entities in the group and the ratio of the solvency requirements of the same financial sector to the total solvency requirements of the financial sector entities in the group should exceed 10 %”.

²⁶¹ Noble, E. (2020), [The Next Generation of Financial Conglomerates: BigTech and Beyond](#), 16 September, Butterworths Journal of International Banking and Financial Law, Vol. 35, No. 10, November 2020.

²⁶² Recital (20) of FICOD.

- b. **Intra-group transactions and risk concentrations** – requesting reporting from MAGs on significant intra-group transactions and risk concentrations;
 - c. **Capital adequacy**²⁶³, ensuring that MAGs allocate sufficient capital and liquidity to their financial activities and that the inter-sectoral risks posed are adequately provisioned, including systemic risk.
280. The ESAs consider that for the largest MAGs involved in financial services, the Commission could consider a supplementary supervisory framework addressing the group in its entirety, not only the entities providing financial services, and take account of interdependencies by both financial and non-financial group entities (e.g. those providing critical data services relied on by other group companies).
281. This could be a **supplementary structured group-wide supervision** to the activity-based supervision and to sectoral supervision. The supervision could leverage existing practices and build on financial services law applicable to the relevant financial services carried out within the group, inspired by FICOD’s approach to the supplementary supervision of financial conglomerates²⁶⁴ and could be triggered where specific conditions are met (e.g. blend/volume/value of financial services activities). In addition, but complementary to these elements, the ESAs propose that the Commission consider the **need for cooperation mechanisms** to support open and structured channels of communication and cooperation amongst financial, competition, data, consumer protection, AML/CFT, cyber and possibly other relevant authorities (see further Recommendation 8). This would serve to address the risks posed by MAGs which extend the financial sector, but which can impact the finance sector and vice versa into other sectors.²⁶⁵
282. Additionally, the ESAs note that, similar to the proposed updates of definitions used for the purposes of the consolidation frameworks, the FICOD could benefit from review to assess whether concepts and terms remain fit-for-purpose, noting the previous review took place in 2013. Regard should also be given to emerging financial activities, such as crypto-asset products and services that will fall within the scope of MiCA.

²⁶³ See Articles 6-9 of FICOD.

²⁶⁴ The financial conglomerates falling under the scope of FICOD are identified by the ESAs annually and their list is published regularly by the Joint Committee of the ESAs.

²⁶⁵ The proposals for possible cooperation models are developed in recommendation 8.

3.1.8 Recommendation 8: Consider possible ways to enhance cooperation between financial and other relevant authorities

Recommendation 8: Consider possible ways to enhance cooperation between financial and other relevant authorities, building on existing cooperation models.

The ESAs believe that the Commission should foster stronger cooperation between financial and relevant non-financial authorities (i) to maintain awareness of policy developments happening across relevant sectors; (ii) to better identify and monitor market developments and emerging risks on a horizontal basis; and (iii) in the context of the growing platformisation of financial services and the development of MAGs.

The ESAs propose three possible frameworks for instituting structured cooperation between financial, data, cyber, consumer protection and competition authorities, namely:

- Proposal 1: Creation of a ‘horizontal committee’ of EU sectoral authorities with regular meetings and operating on a voluntary basis;
- Proposal 2: Dedicating staff within each EU sectoral supervisory authority to cooperate on specific areas of digital finance that require a cross-sectoral approach;
- Proposal 3: Use the existing college(s) of supervisors under group supervision and establish new supervisory college(s) on a case-by-case basis involving relevant EU authorities and NCAs.

In the context of proposals 1 and 2, vertical cooperation and engagement with representatives of the national authorities should be an important consideration, as is already the case with the EFIF, for example.

The three proposals should not be considered as mutually exclusive but rather complementary. In any case, the selected cooperation framework should have a very clear mandate conferred upon it to enhance information-sharing, awareness of cross-sectoral policy and market developments, avoiding the creation of undue elements of complexity or new layers of decision-making.

It goes without saying that the authorities that participate in cooperation arrangements should comply with professional secrecy requirements and other data-related rules that may vary from Member State to Member State.

283. The growing digitalisation and datafication of the EU’s financial sector necessitates closer cooperation between NCAs and other relevant non-financial authorities.²⁶⁶ Indeed, a holistic approach to the regulation and supervision of digital finance warrants consideration of issues that extend beyond the exclusive remit of NCAs, for example in cases where the dominant position of certain third-party service providers has negative outcomes on the range or quality of financial products and services being offered to consumers or the stability of the financial system, or in relation to data protection and cyber security issues. Currently practical and legal challenges exist for putting in place cooperation and collaboration between different authorities (e.g. lack of arrangements in place for information exchange between authorities and data protection rules).

²⁶⁶ Suggested relevant authorities are listed in the final section of this recommendation.

284. The 2019 review of the ESAs' powers, governance, and funding made initial steps in supporting enhanced cooperation across relevant authorities. The revised founding regulations²⁶⁷ mandate the ESAs to closely cooperate with the European Data Protection Board (EDPB) to avoid duplication, inconsistencies, and legal uncertainty in the sphere of data protection. The ESAs may also invite national data protection authorities as observers into their committees. Also, the ESAs should promote an effective bilateral and multilateral exchange of information between competent authorities, pertaining to all relevant issues, including cyber security and cyber-attacks, with full respect for the applicable confidentiality and data protection provisions provided for in the relevant Union legislative acts. In addition, the revised founding regulations require each of the ESAs to establish a committee on consumer protection and financial innovation, bringing together all relevant competent authorities and authorities responsible for consumer protection with a view to enhancing consumer protection, and achieving a coordinated approach to the regulatory and supervisory treatment of new or innovative financial activities.
285. Another already established example of a cooperation arrangement between the ESAs, which allows for participation of various sectoral authorities, is the European Forum for Innovation Facilitators (EFIF) (see **Box 5**). EFIF members include representatives of national innovation hubs and regulatory sandboxes established by NCAs and representatives of each of the ESAs. It also foresees 'observer' participation by a range of other authorities, including the EDPB. The EFIF provides a platform for supervisors to meet regularly to share experiences from engagement with firms through regulatory sandboxes and innovation hubs, share technological expertise, and to reach common views on the regulatory treatment of innovative products, services, and business models—all towards boosting multilateral coordination.²⁶⁸
286. Yet, such examples of encouraging cross-sectoral cooperation are still relatively new and limited in scope and/or powers. In particular, the ESAs believe that a closer cooperation framework between financial and relevant non-financial authorities would be beneficial (i) to maintain awareness of policy developments happening across relevant sectors; (ii) to better identify and monitor market developments and emerging risks on a horizontal basis; and (iii) in the context of the growing platformisation of financial services and the development of mixed activity groups as set out in the 'Market developments' chapter.
287. In the following recommendation, **the ESAs have identified three structural frameworks** to facilitate stronger cooperation among the relevant EU level authorities and with NCAs. The ESAs conceived each of the models using efficiency and practicality as criteria. These proposals strike a balance between imposing new structures for cooperation and adapting the already existing tools available to supervisors. They also satisfy both the horizontal needs that are currently lacking at the EU level while incorporating existing vertical cooperation with representatives of national jurisdictions (NCAs). Non-financial authorities that would be relevant for the proposed frameworks are outlined in the final section.

²⁶⁷ Regulation (EU) 2019/2175 of the European Parliament and of the Council of 18 December 2019 amending Regulation (EU) 1093/2010 establishing a European Supervisory Authority (European Banking Authority), Regulation (EU) 1094/2010 establishing a European Supervisory Authority (European Insurance and Occupational Pensions Authority), Regulation (EU) 1095/2010 establishing a European Supervisory Authority (European Securities and Markets Authority), Regulation (EU) 600/2014 on markets in financial instruments, Regulation (EU) 2016/1011 on indices used as benchmarks in financial instruments and financial contracts or to measure the performance of investment funds, and Regulation (EU) 2015/847 on information accompanying transfers of funds, OJ L 334, 27/12/2019.

²⁶⁸ JC of the ESAs (2019b), [Terms of Reference, European Forum for Innovation Facilitators](#), JC/2019-40.

Proposed structural cooperation models:

288. These proposals **should not be considered mutually exclusive from one another**, as they each address specific challenges. Indeed, they should be considered complementary, with interchangeable components that address the three areas for improvement in existing structures for cooperation identified above. In particular, Proposals 1 and 2 may be considered either as standalone models or complementary to each other for the purposes of better maintaining awareness of relevant policy and market developments across sectors. In other words, the ESAs do not foresee any friction that would prevent a combination of the first two models (e.g., having the cross-sectoral staff-level work of Proposal 2 feed into the ‘horizontal’ standing committee structure found in Proposal 1). Proposal 3 is more geared towards addressing the specific issues raised by platformisation and mixed activity groups and considers ‘hands on’ entity-level supervision. Also, the exact details of each proposal are malleable, meaning that they could be refined through time, depending on further suitability tests and structural design preferences.
289. It should be caveated that enhanced collaboration between the different EU and national level authorities may create practical and legal challenges, as it relates to data sharing. At present, there may not be adequate professional secrecy arrangements in place for information exchanges between authorities. From a functional perspective, the gateways for sharing this information would also have to be formalised. It is therefore important that institutional mandates of all authorities involved comply with GDPR and other national data-sharing schemes.
290. ***Proposal 1: Establish a ‘horizontal committee’ of relevant authorities at the EU level***
- a. A horizontal committee of existing EU authorities from the relevant sectors (EDPB, DG Comp, ESAs, ENISA etc.) would be established on a voluntary (non-statutory) basis. The committee would have no formal policymaking role or ability to issue formal guidance to members. Instead, it would function primarily as a coordination mechanism by which committee members would inform one another about policy developments in their respective remits. Cooperation principles could include information-sharing, capacity-building, joint stakeholder engagement, and joint market assessments. Committee members would ultimately define the scope, but such a determination could be flexible in capturing a range of activities native to digital financial markets. New powers would not have to be enumerated to any authority, nor would there be confusion caused by an overlapping scope.²⁶⁹
 - b. This committee could take inspiration from the EFIF model. Similar to the EFIF model (and other joint EU and Member State authority networks such as the Consumer Protection Cooperation (CPC) the European Cooperation Network (ECN), or the EU Agency for Cybersecurity (ENISA)), the committee could also incorporate a sub-EU level structure into its design. Membership status would be open to relevant national authorities (including NCAs) with a common interest in supervision or regulation of digitalisation and platformisation.
291. ***Proposal 2: Allocate dedicated staff for ‘digital markets’ within each relevant EU authority (financial, data, cyber, consumer protection and competition authorities) that would collaborate on issues of common interest (and convene a committee for NCAs when necessary)***

²⁶⁹ Inspiration for this approach can be found in the example of the *Italian FinTech Committee*: Turati, A. (2021) [New Italian regulations on fintech regulatory sandbox](#), 13 July, Fieldfisher, Italy.

- a. This proposal would involve the creation of subsidiary teams (comprised of current staff) within each relevant EU authority which would have formal powers to share data/information and collaborate on areas of common interest in areas specific to digital financial markets. Topics under the teams' purview could include (but not be limited to) the ethical use of AI, encryption, smart contracts, collection of non-financial data, and issues related to platformisation (e.g., network effects, user interface design/gamification).
- b. The value of dedicated 'digital financial markets' staff in each of the relevant authorities (financial, data, cyber, consumer protection and competition authorities) which would collaborate on issues of common interest would be twofold. First, these could be targeted towards a narrowly defined set of digital financial market issues. Second, collaboration on issues that require a range of technical expertise would encourage greater in-house capacity/expertise building at each authority. Noteworthy, at the ESAs level, the DORA proposal already calls for the Joint Committee of the ESAs to continue ensuring cross-sectoral coordination in relation to all matters pertaining to ICT risk.²⁷⁰
- c. Again, structuring vertical cooperation with NCAs could simply entail borrowing the EFIF playbook. In other jurisdictions, policymakers have proposed a separate 'liaison committee' with sub-national authorities, however, this may add complexity when suitable structures already exist.

292. ***Proposal 3: Use the existing college(s) of supervisors under group supervision and establish supervisory college(s) on a case-by-case basis involving relevant EU authorities and NCAs***

- a. In the cases where colleges of supervisors are already in place in the context of group supervision, e.g. as foreseen in Solvency II Directive or CRD/CRR, and when it addresses the supervision of financial groups pursuing a digital business model, especially when there are strong relations with non-financial entities, additional cooperation between supervisory authorities should be envisaged. Existing legislations should be updated so that group supervisors are allowed to invite the relevant supervisory authorities to the colleges for the discussion of dedicated topics. The participating authorities should comply with professional secrecy rules.
- b. Where the criteria set out in sectoral legislation such as CRR/CRD or Solvency II to establish a college are not met, a voluntary supervisory college model would give an opportunity to bring together EU authorities and national level authorities with relevant supervisory jurisdiction into colleges with oversight of certain entities or activities where needed. This will be decided on a case-by-case basis, e.g., in relation to a platform used by multiple financial institutions. EU authorities could participate in the colleges in an advisory role or as a lead member depending on the objectives and circumstances. They would be responsible for the coordination of supervisory actions, sharing of risk assessment techniques and information/data-sharing.²⁷¹ The colleges would involve cooperation among NCAs which often have greater knowledge of local market participants. The addition of specific authorities as members of a college can be based on criteria such as the geographic scope of regulated entities, activities or use cases. In any case, responsibilities

²⁷⁰ Paragraph (60) of DORA, see footnote 2.

²⁷¹ Alford, D. (2018), [The Operation of Supervisory Colleges after the Single Supervisory Mechanism of the European Banking Union](#), September 16.

must remain clearly assigned and reflect the respective competences of the various supervisory and non-financial authorities involved.

- c. In addition, the DORA proposal would mandate the JC of the ESAs to establish an ‘Oversight Forum’ covering critical ICT third-party providers and composed of the ESAs and representatives from relevant NCAs, as well as the European Commission, European Systemic Risk Board, European Central Bank and European Union Agency for Cybersecurity.²⁷² The DMA proposal also includes a provision (Art. 32) on the creation of a Digital Markets Advisory Committee comprised of representatives of Member States which would help to determine firms that would fit the proposal’s criteria for ‘gatekeeper’ status.²⁷³ The European Data Protection Supervisor has proposed expanding this Committee to include data protection authorities.²⁷⁴ MiCA also proposes a supervisory college model for certain issuers of crypto-assets, vesting final jurisdiction with EBA (Articles 99(2), 101(2)) and enabling it to chair a college of issuers who are deemed ‘significant’.²⁷⁵

Relevant non-financial authorities for the proposed enhanced cooperation frameworks

293. Relevant authorities for the proposed new cooperation frameworks could include:

- a. **Data protection authorities** — The European Data Protection Board (**EDPB**) is an independent European body which contributes to the consistent application of data protection rules across the EU and promotes cooperation between the national data protection authorities in the EU.²⁷⁶ Data Protection Authorities (**DPAs**) are independent public authorities that supervise, through investigative and corrective powers, the application of the data protection law. They provide expert advice on data protection issues and handle complaints lodged against violations of the GDPR and the relevant national laws. There is one DPA in each EU Member State.²⁷⁷
- b. **Consumer protection authorities** — The Consumer Protection Cooperation Network (**CPC**) consists of authorities responsible for enforcing EU consumer protection laws to protect consumers’ interests in EU and EEA countries.²⁷⁸ The Commission coordinates the cooperation between these authorities to ensure that consumer rights legislation is applied and enforced in a consistent manner across the Single Market.
- c. **Cybersecurity authorities** — The EU Agency for Cybersecurity (**ENISA**) contributes to EU cyber policy in cooperation with Member States and other EU bodies. It enhances the trustworthiness of ICT products, services and processes with cybersecurity certification schemes.²⁷⁹ The NIS Directive²⁸⁰ (Art. 12) also establishes a network of ‘computer security

²⁷² Article 29 of DORA.

²⁷³ DMA, see footnote 20.

²⁷⁴ European Data Protection Supervisor (2021), [Opinion 2/2021 on the Proposal for a Digital Markets Act](#), 10 February.

²⁷⁵ MiCA, see footnote 16.

²⁷⁶ EDPB, [About us: “Who we are”](#), EDPB website.

²⁷⁷ European Commission, [“What are Data Protection Authorities \(DPAs\)?”](#), EC website.

²⁷⁸ European Commission, *Internal Market*, [Single Market Scoreboard](#), EC website.

²⁷⁹ ENISA website: <https://www.enisa.europa.eu/>.

²⁸⁰ Directive 2016/1148/EU of the European Parliament and of the Council of 6 July 2016 concerning measures for a high common level of security of network and information systems across the Union, OJ L 194, 19/07/2016.

incident response teams' (**CSIRTs Network**), composed of EU Member States' appointed CSIRTs and CERT-EU. The CSIRTs Network provides a forum where members can cooperate, exchange information and build trust. It is intended to improve the handling of cross-border incidents and develop coordinated responses to specific incidents.

- d. **Competition authorities** — At the EU level, **DG Comp** is responsible for the EU competition policy and for enforcing EU competition rules. The Commission and the national authorities in the EU Member States cooperate with one another through the European Competition Network (**ECN**), the objective of which is to build an effective legal framework to enforce the EU competition law against companies that engage in cross-border business practices that restrict competition and are harmful to consumers.²⁸¹ ECN members have also engaged in cooperation and exchange of best practices on merger control issue via the **EU Merger Working Group**.

Box 5: The European Forum for Innovation Facilitators (EFIF) ²⁸²

The Joint Committee of the ESAs established the EFIF in 2019 to promote greater coordination and cooperation between innovation facilitators²⁸³ and thus support the scaling up of FinTech across the single market.

The EFIF provides a platform for supervisors to meet regularly to share experiences from engagement with firms through regulatory sandboxes and innovation hubs, share technological expertise, and to reach common views on the regulatory treatment of innovative products, services and business models, overall boosting bilateral and multilateral coordination.

Members of the EFIF include representatives of national innovation hubs and regulatory sandboxes established by NCAs and representatives of each of the ESAs.²⁸⁴ The EFIF may maintain direct contacts and dialogue with academics, industry experts and relevant authorities (e.g., in the fields of consumer and data protection). The representatives of innovation facilitators established by competent authorities in third countries may be invited to participate in EFIF meetings.

The EFIF is intended to benefit participating authorities and firms in fostering a common supervisory response to technological innovations in the financial sector.

The September 2020 Digital Finance Strategy for the EU ('the EU Digital Strategy') highlighted the role of the EFIF for the digital transformation of the EU financial sector and for 'facilitating the scaling up of digital financial services across the Single Market'.²⁸⁵

The EFIF is a voluntary discussion forum, which does not have regulatory, supervisory or decision-making powers. Its organisation rests with the ESA Joint Committee.²⁸⁶

²⁸¹ European Commission, [European Competition Network \(ECN\)](#), in *Competition Policy*, EC website.

²⁸² JC of the ESAs, [European Forum for Innovation Facilitators \(EFIF\)](#), JC website.

²⁸³ See the definition of "innovation facilitators" in Joint Committee of the ESAs (2019) [Report, FinTech: Regulatory sandboxes and innovation hubs](#), JC/2018-74.

²⁸⁴ See footnote 268.

²⁸⁵ See footnote 9 on the DFS.

²⁸⁶ JC of the ESAs, [Organisational Structure, Composition & Tasks](#), JC website.

3.1.9 Recommendation 9 for the ESAs: Address cross-border supervisory coordination challenges

Recommendation 9 for the ESAs: Address cross-border supervisory coordination challenges.

Consider possible ways to enhance cooperation between home and host authorities (e.g. complementary notification requirements for cross-border activities and/or supervisory forums for enhanced information exchange, processes and measures to be adopted where a firm possibly infringes rules, and with third country authorities (e.g. updating MoUs to reflect specific issues related to digital finance).

294. As already highlighted in the cross-sectoral recommendation section, several issues have been brought to the attention of the ESAs with regards to the distribution of products and services on a cross-border basis, which might lead to further work being conducted by the ESAs.
295. In particular, NCAs responding to both ESMA and EBA surveys have highlighted visibility issues around the use of platforms and other innovative technologies as a means for financial institutions to distribute products and services. It was indeed noted by NCAs that passporting notifications in relation to the cross-border provision of services and distribution of products are often given on an EU-wide basis (rather than specific to the jurisdictions in which the services are actually being carried out) and would not typically include any information about how the service is being carried out (with NCAs not being informed about the means through which services are provided, including the use of digital platforms). Therefore, the ESAs will consider if there is a need to introduce amendments to the relevant sectoral level 2/3 measures and guidance concerning the content of passporting notifications, including more granular information on the means by which services and products are to be provided or distributed (digital platform, other technology etc.).
296. As part of this call for advice, the ESAs have also identified the need to enhance cross-border supervisory cooperation and information exchange in order to ensure a higher level of protection of EU consumers, having considered the increased use of digital means in distributing financial products and services cross-border. In this context, the ESAs will continue the work on supervisory convergence to promote the consistent and effective implementation and application of the relevant rules (e.g. discussing practical use cases in the supervisory community, e.g. in relation to the allocation of responsibilities between home and host NCAs on conduct of business rules, coordinating the collection of data on cross-border activities).
297. Moreover, ESMA restates the need to strengthen cross-border supervisory coordination, particularly in relation to precautionary measures that host authorities can take when they have grounds for believing that a firm acting within their territory under the FoS is infringing requirements of relevant EU financial legislation. ESMA therefore restates its Technical Advice provided to the Commission on the application of administrative and criminal sanctions under MiFID II/MiFIR²⁸⁷.
298. Lastly, the ESAs and NCAs are invited to consider the merit of enhancing cooperation with third country authorities, possibly by reviewing and updating, if necessary, relevant sectoral MoUs to take into account the growing digitalisation trend across the three sectors.

²⁸⁷ ESMA (2021b), [ESMA's Technical Advice to the Commission on the application of administrative and criminal sanctions under MiFID II/MiFIR](#), Final Report, ESMA35-43-2430, 29 March.

3.1.10 Recommendation 10 for the ESAs: Actively monitor the use of social media in financial services and assess whether regulatory action may be warranted as part of forthcoming work

Recommendation 10 for the ESAs on social media: The use of social media in relation to financial services continues to evolve at a rapid pace, especially in securities markets where ESMA has observed an increasing use of social media by individuals and firms to promote financial services and products and by (retail) investors to seek investment and trading ideas. While those practices partly fall under existing rules already, for example MiFID II and the Market Abuse Regulation²⁸⁸ for what concerns investor protection and market integrity aspects, there may be a need to consider further specific issues raised by the growing interconnectedness between social media and the provision of financial services. EIOPA has also observed some social media-sponsored content which appears as content shared by users, while in reality they are ads that redirect users to a third-party website, amounting to disguised ads, which may require further consideration. The ESAs will continue to monitor these developments in all sectors and, in the case of ESMA and EIOPA, will assess where regulatory action may be warranted, as part of the calls for advice received from the Commission in July 2021 regarding certain aspects relating to retail investor protection.²⁸⁹ The ESAs also consider that there may be a need for regulators and supervisors to adapt their external communication to reach financial market participants that seek information predominantly through digital channels, including social media.

299. As already highlighted in the market developments and risk and opportunities sections, the ESAs have observed a growing reliance on social media both by firms promoting financial services and by consumers who are increasingly looking to a wider range of sources, including non-traditional sources such as social media, to inform their financial decision-making. This has been so far predominantly observed in securities markets. In the insurance sector, not so many developments have been observed to date.
300. The use of social media in relation to financial services is already subject to a series of rules. For example, personal investment/insurance recommendations on social media may qualify as regulated ‘investment advice’ under the Markets in Financial Instruments Directive (MiFID II) or “insurance advice” under the Insurance Distribution Directive (IDD) (noting that in some jurisdictions, a mandatory advice regime applies). The provision of regulated financial services without proper authorisation/registration and adherence to the applicable rules exposes firms to the risk of administrative or criminal sanctions.
301. In October 2021, ESMA published a statement²⁹⁰ on investment recommendations on social media. Through the Statement, ESMA highlighted the definition of investment recommendations under EU law, the rules under the EU Market Abuse Regulation that those making investment recommendations need to adhere to and the consequences of possible breaches. In particular, the statement recalls that investment recommendations must be done in a specific and transparent way so that investors, before making any investment decision, can

²⁸⁸ Regulation (EU) 2014/596 of the European Parliament and of the Council of 16 April 2014 on market abuse (market abuse regulation) and repealing Directive 2003/6/EC of the European Parliament and of the Council and Commission Directives 2003/124/EC, 2003/125/EC and 2004/72/EC, OJ L 173, 12/06/2014.

²⁸⁹ See footnote 7.

²⁹⁰ ESMA (2021g), *Statement on Investment Recommendations on Social Media*.

know and assess: 1) the credibility of the recommendation – and how objective it is; and 2) any interests of those making the recommendations.

302. In August 2021, ESMA published guidelines on marketing communication under the Regulation on cross-border distribution of funds.²⁹¹ In particular, the Guidelines clarify that messages broadcasted on social media platforms, when such messages refer to any characteristics of a UCITS or an AIF, including the name of the UCITS or the AIF, may be considered as marketing communication and therefore fall within the scope of the guidelines, which include various disclosure requirements (e.g., in relation to costs, risks and rewards). The guidelines further specify the format for disclaimers to be used on social media platforms, as well as the tone and scope of the marketing communication.
303. Yet, considering that the use of social media in financial services continues to evolve quickly, the ESAs are committed to analysing the growing interlinks and dependencies further, with a view to identifying areas where these are not yet captured by existing rules or where new interactions and business models develop that require further assessment. This will be done through general market monitoring and, in the case of ESMA and EIOPA, where relevant, as part of the calls for advice received by the Commission in July 2021 regarding certain aspects relating to retail investor protection²⁹², especially in relation to the request to ‘assess the risks and opportunities presented by new digital tools & channels selling retail investment products’. In particular, ESMA is looking at whether amendments to the existing regulatory framework (e.g., relevant provisions under MiFID II) are needed to safeguard investor protection. As part of the call for advice, ESMA will consider the need to adapt existing rules on digital disclosures and advertising, including when provided through social media. In this context, ESMA will assess, inter alia, aspects of promoting investment advice in the context of social media and will look at the role of *finfluencers* as well and the possible need to update the existing legislative frameworks. ESMA will also perform an assessment of the general need for additional tools for regulators in order to supervise these new digital channels through which information is provided to retail clients by and through third parties.
304. Depending on the market developments, some regulatory adaptations might be needed in the different sectors going forward, therefore it is important for considerations relating to the use of social media to be taken into account, where relevant, in the context of the review of sectoral measures, notably the PSD2 and the IDD.
305. Additionally, this development illustrates that a new generation of consumers responds increasingly, or even predominantly, to communication and information circulated on social media. This implies a growing need for regulators and supervisors to become better acquainted with different types of social media, to facilitate a comprehensive assessment of the activities taking place in this specific digital context. Regulators and supervisors may also want to consider broadening their communication channels to reach consumers that seek information not through traditional means but predominantly or exclusively on social media.

²⁹¹ ESMA (2021f), *Guidelines on marketing communications under the Regulation on cross-border distribution of funds*.

²⁹² See footnote 7.

3.2 Insurance

3.2.1 Recommendation 1: Solvency II requirement on the scope of (re)insurance activities

306. One topic which has often come up in light of digitalisation and which can be seen as related to all parts of the Call for Advice is the current requirement on the scope of (re)insurance activities. Namely, Article 18(1)(a) of the Solvency II Directive states that Member States shall require every undertaking for which authorisation is sought in regard to insurance undertakings, to limit their objects to the business of insurance and operations arising directly therefrom, to the exclusion of all other commercial business.
307. In practice, it might not be so easy to identify what activities are directly linked to insurance. While this is not a new topic, it seems to be ubiquitous in the digitalisation context, also in light of the move from protection/cover of risk to prevention/advisory models foreseen in the market (e.g. on cyber risk), arguably also driven by digitalisation/increased access to data. Hence, some new digital activities might be classified as ‘non-insurance business’.²⁹³ In addition, the pure IT activities of providing software/API development that directly support the insurance business may not be considered as insurance activities when developed directly by the undertaking or one of its subsidiaries but offered to other insurers/intermediaries.²⁹⁴
308. For those activities not traditionally considered as core insurance business, insurance undertakings may establish, for example, some partnership solutions. In the cases where group supervision does not apply, the risk related to separate entities is limited to the market risk of the investment amount in that entity and reputational risk. In addition, operational risk identified in the group’s ORSA could be assessed differently, depending on the classification of such entities, their inclusion in the group and methods of consolidation and risk management. An adequate computation of operational (including IT) and legal risk for innovative and more complex activities in capital requirements for solo undertakings and groups is also an issue to be considered.
309. In fact, EIOPA stakeholders highlight the application of Article 18 in Solvency II both as an issue of level playing field and a barrier to innovation. In light of the work on barriers to InsurTech, some stakeholders have argued that a restrictive interpretation of this Article could limit the ability of (re)insurance undertakings to experiment with new business models and technologies and develop platforms and ecosystems around them.
310. Under the work on licensing requirements and principle of proportionality in an InsurTech context, EIOPA stated ‘Article 18 provides some flexibility to InsurTech companies as far as the activities are directly related to core business. However, a practical implementation of this provision can vary in different Member States and hence it might be relevant to analyse more

²⁹³ In addition to more traditional examples such as brokering phone contracts and selling cell phones in addition to cell phone insurance against theft / damage to property or granting of credit/loan, different examples that might raise questions include selling an inventory management IT system to third parties, security consultations sold with property insurance, health apps, rehabilitation services, driving style coaching, the use of digital tools for car repair management (in the context of motor insurance claims management), platform for online consultations with doctors to allow for psychological follow-up for claims management purposes, the use of smart tools (e.g. smart smoke detector, smart water sensor, smart security tool against theft) for loss prevention purposes typically connected to an app or in some cases to a security centre, insurance-related data collection, insurance company offering free platforms which bring together volunteers that can offer help to with people with specific needs, offering public online data platform that gives free access to data points to academics.

²⁹⁴ An example could include situations where an insurance intermediary is developing its own comparison tool for internal use, but also offers this as a ‘white label’ solution for other intermediaries.

in-depth the different national approaches (e.g. the application of this provision to different risk prevention activities, which are becoming more widespread in an InsurTech context) as well as the need for possible legislative change’.

311. More recently, Recommendation 24 of the European Commission ROFIEG expert group touched on the same point, stating that the impact of existing activities restrictions for financial institutions’ non-core business (e.g. Art. 18 of Solvency II) should be reviewed to determine whether these restrictions remain proportionate. According to the expert group, this review should pay particular attention to cross-sectoral considerations in order to ensure a level playing field between different types of actor in the financial sector, including BigTechs.
312. EIOPA is of the view that the issue has a convergence angle. The key question is which new services would be allowed under Art. 18, and which would not be. Article 18 states that insurance undertakings are ‘to limit their objects to the business of insurance and operations arising directly therefrom, to the exclusion of all other commercial business’. Indeed, the notion of ‘arising directly therefrom’ may already provide sufficient leeway in theory to allow for a number of new services, but the lack of convergence seems also clear.²⁹⁵ A possible solution should be to make sure that (digital) activities directly linked to insurance activities and insured risks such as risk prevention and customers’ risk management services (health apps, rehabilitation services, driving style coaching) should be considered insurance or ancillary business. This could allow the application of existing governance, resiliency, capital and conduct requirements to such activities.
313. EIOPA will consider further analysis (e.g. deeper analysis of what is and is not considered to be ‘activities directly related to insurance’ in different Member State; Issuing guidelines as relevant) to bring more clarity to this issue, taking into account the potential impact for consumers, insurance sector and its supervision. Legislation change is most likely not needed in order to avoid unintended consequences and additional risks that those new activities could cause.

²⁹⁵ Based on NCA feedback, the following activities are rather considered as falling under Art. 18(1)a: Security consultations sold with property insurance, health apps, rehabilitation services, driving style coaching, the use of digital tools for car repair management (in the context of motor insurance claims management), platform for online consultations with doctors to allow for psychological follow-up for claims management purposes, the use of smart tools (e.g. smart smoke detector, smart water sensor, smart security tool against theft).

3.2.2 Recommendation 2: The treatment of P2P insurance

314. EIOPA has looked at P2P insurance (where a group of individuals with mutual interests or similar risk profiles pool their ‘premiums’ together to insure against a risk) in its Report on Best Practices on licensing requirements, peer-to-peer insurance and the principle of proportionality in an InsurTech context.²⁹⁶
315. European insurance legislation does not provide a definition of what is insurance and what is not²⁹⁷ (either as an activity or as a contract); Art. 13(1) of Solvency II states that insurance undertaking means a direct life or non-life insurance undertaking which has received an authorisation. The IDD, which is a minimum harmonisation directive, provides a broad definition of what should be understood by insurance distribution (Art. 2(1)(1)). The definition of insurance is often (not always) included in national legislation or case law, and therefore there is not a common EU approach in this regard which can lead to diverging views of what constitutes P2P insurance.²⁹⁸ Some NCAs have also reported that it is unclear to what extent the several natural or legal persons typically involved in the setting-up and running of digital distribution channels should be considered as insurance distributors and/or ancillary intermediaries under the IDD.
316. EIOPA has stated in its previous work that from a regulatory perspective, and following an activity-based approach, it can be argued that there are three different types of P2P insurance business models: a) P2P insurance sold directly through a licensed insurer; b) P2P insurance sold via a licensed / registered insurance intermediary backed by a licensed insurance undertaking, and c) service providers/platforms acting solely as administrators for risk-sharing groups, without an underlying insurance carrier and without performing insurance distribution activities (e.g. certain DLT/Blockchain based solutions).²⁹⁹
317. While there is a clear applicable legal framework for the first two types of P2P insurance business models, this is not the case for service providers/platforms purely acting as an administrator for risk-sharing groups. It is also debateable whether the Solvency II and the IDD can be adapted to regulate all new types of P2P insurance business models.
318. Since publishing the report, there have not been any significant developments in P2P insurance. However, some Member States have recently indicated some further developments in their markets, including possible perimeter issues (e.g. how it should be treated). One Member State has issued guidelines on P2P insurance.³⁰⁰ There also seems to be some blockchain-based decentralised business models³⁰¹ in developing phase, sometimes also arguing they do not offer insurance but protection products, hence outside of the insurance perimeter. However, the

²⁹⁶ EIOPA (2019c), [Report on Best Practices on licensing requirements, peer-to-peer insurance and the principle of proportionality in an InsurTech context](#), March.

²⁹⁷ This is also a matter of civil law which is not harmonised.

²⁹⁸ In at least one EU jurisdiction, there is an entity operating a P2P-like insurance business model with a payments license under PSD2 instead of an insurance license/registration.

²⁹⁹ EIOPA (2019c).

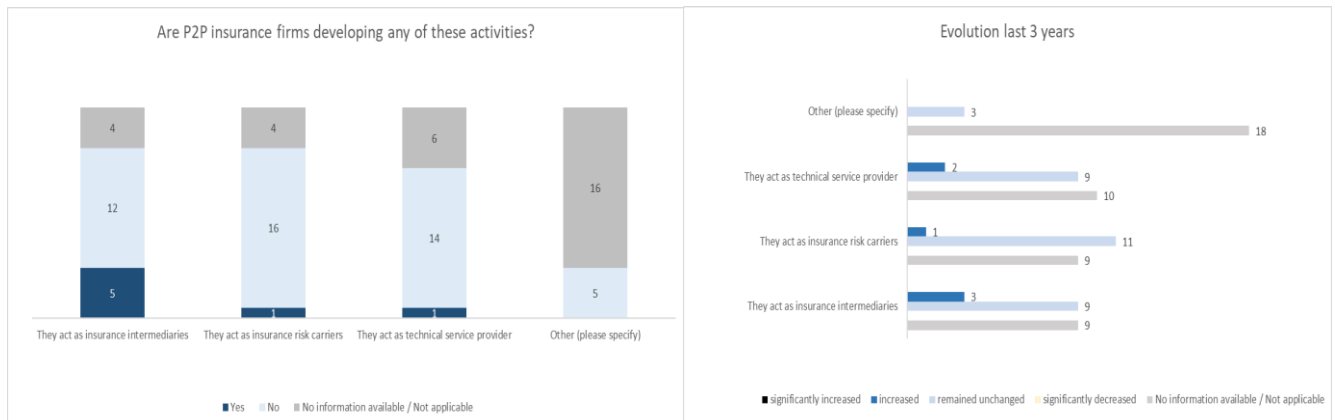
³⁰⁰ The guidelines include recommendations on consumer information, governance, pricing, asset safekeeping, restrictions on activity, financial and statistical disclosures.

³⁰¹ EIOPA (2021b).

scale of those developments is still very limited and most of the models seem to fall under existing regulation.³⁰²

319. Due to the current relatively low market penetration of P2P insurance business models,³⁰³ and the fact that most of the business models seem to fall under existing regulation, EIOPA does not see a pressing need for special regulatory approaches or changes in relation to P2P insurance. EIOPA is also of the opinion that best practices highlighted in its Report are still valid. However, the Commission could consider developing such legislation in the future, in particular if P2P insurance business models or other new business models continue to develop along a similar trajectory, as seen with crowdfunding, car sharing or real estate rentals. This could include setting criteria and thresholds to identify when P2P is an insurance product (i.e. professional activity with offer to a general public) and when service providers are acting as intermediaries. In any case, an in-depth impact assessment would be needed, as highlighted in EIOPA’s report on Best Practices on Licencing Requirements, Peer-to-Peer Insurance and principle of proportionality³⁰⁴. In general, any regulatory responses should be (1) neutral in terms of the way that a product or service is distributed (i.e. the principle of ‘technological neutrality’); and (2) ensure that regulatory responses reflect the business model, risk profile, size, systemic significance, as well as complexity and cross-border activity of the regulated entities (i.e. proportionality).
320. EIOPA will also continue market monitoring on P2P insurance, e.g. through its annual Consumer Trends Report. Additionally, EIOPA will continue to facilitate exchange of different P2P insurance business models and best practices both in its InsurTech Task Force and the European Forum on Innovation Facilitators (EFIF) to promote supervisory convergence.

Figure 5: Focus on P2P insurance developments



Source: EIOPA Committee on Consumer Protection and Financial Innovation – NCAs’ Questionnaire to NCAs (2021).

³⁰² See **Figure 5** below.

³⁰³ Taking into consideration the European Commission's Fintech Action Plan, EIOPA mapped in 2019 current authorising and licencing requirements (both in the light of the IDD and Solvency II), and assessed how the principle of proportionality is being applied in practice specifically in the area of financial innovation. EIOPA also took a more in-depth look at P2P Insurance. The majority of the NCAs didn’t report on licenced P2P insurers. Some NCAs stated that the specific regulation would be useful if such market will start growing – at the moment it is very limited and thus it is too early to determine a need for special legislation. Indeed, an estimate size of the P2P business was considered very limited or even not sizable (compared e.g. with the market size of crowdfunding). NCAs reported no consumer complains on P2P insurance yet.

³⁰⁴ EIOPA (2019c).

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Annex 2. Glossary

BigTech means a ‘large technology company with extensive customer networks; it includes firms with core businesses in social media, internet search, software, online retail and telecoms’ as defined by the FSB (2020b). BigTechs are a type of mixed activity group (see definition below).

Digital Platform means any digital platform that enables financial institutions directly (or indirectly using a regulated or unregulated intermediary) to market to consumers, and/or conclude with consumers contracts for financial products and services. The definition of ‘digital platform’ aims to be both ‘model’ and ‘technology-neutral’. Examples for digital platforms that are relevant for this report include, but are not limited to, technical infrastructures used by financial institutions to market or distribute different financial products and services and enabling consumers to access products and services provided by different financial institutions. Those technical infrastructures that have been developed by financial institutions for their sole individual benefit are outside of the scope of this report.

FinTech refers to technology-enabled innovation in financial services that could result in new business models, applications, processes or products with an associated material effect on the provision of financial services.

InsurTech refers to ‘technology-enabled innovation in insurance that could result in new business models, applications, processes or products with an associated material effect on the provision of insurance products and services’.

Mixed Activity Group (MAG) refers to a group of undertakings (a parent undertaking and its subsidiary undertakings) conducting both financial and non-financial services. For the purposes of this report, the ESAs have focussed on technology-enabled mixed activity groups to capture the impact of the use of digitalisation, technology and large customer base on their business models and on the provision of financial services.