7th Annual FinTech and Regulation Conference

Hosted by Afore

Speech: Hanzo van Beusekom, Member of the Executive Board of the Dutch Financial Markets Authority

February 7ty 2023,

Plan for the Future

In dialogue to anticipate the speed of digitalisation

- Thank you for this invitation. Symposia like this one are a must. Supervisory authorities do well to join with market parties in thinking about how we can help each other tackle the challenges ahead.
- Though I would have preferred to do it face-to-face. That's more impactful and effective, if you ask me.
- So, now the challenge for me is to deliver a story that keeps you watching.
- Digitalisation... People like to say time flies, but if that's true, let's take a look at the speed with which digitalisation has unfolded.
- Thirty years ago:
    - Open outcry trading.
    - Telephones were still just bulky boxes with cords.
    - And you would access the Internet via those maddening dial-up modems... 16k6.
- Moreover, 30 years ago, there was no such thing as an online event.
- These days, digitalisation is barrelling ahead, certainly in the financial sector. Some examples:
    - Expansion of financial services by BigTech and FinTech firms.
    - Expanded use of artificial intelligence.
    - Digitalisation has widened and simplified access to advice and products.
- These digital developments has pros and cons
    - Increasing ease of use and easy access are all well and good. But the advantages have to weigh up against risks that customers are willing and able to bear.
    - While AI can help to serve customers more effectively, AI can also lead to exclusion.

    - Partnerships between tech firms and traditional businesses can pay off in cost savings and innovation, but they can also lead to concentration risk and margin pressure.

- Digitalisation has advanced in three waves.
- During the first wave, we got to see the vast potential of digitalisation.
- During the second wave, we staked out a variety of policy initiatives addressing risks and opportunities.
    - These policy initiatives were horizontal and cross-sectoral as well as sector-specific in nature.
    - Horizontal initiatives including DMA, DSA, DGA, DA and AIA, all with one common denominator: they regulate digital markets and players and target digitalisation and data. Impacting market dynamics. Also in the financial sector.
    - Sector-specific initiatives have included DORA, MiCAR, DLT-Pilot Regime and Digital Euro, and we're expecting a proposal for Open Finance.

- We are now in the midst of a third wave, in which rules on paper have to be put into practice. It is supervisory authorities' and market parties' turn to make their moves.

- The main question is: how do we effectuate these laws and regulations in practice?

- That can be quite a challenge. To illustrate, I will give you three examples.

    - AI Regulation
    - Open Finance
    - MiCA

First, the AI Act:

- Talks are still ongoing, and a compromise is likely to come this year. We are starting to see the contours.
- These are cross-sectoral rules with impact beyond the financial markets and on multiple forms of oversight.
- At its core, this Act is concerned with protecting people – specifically, users. Certain specific applications of AI are classified as 'high risk'. Looking at the financial sector, AI

applications for credit scoring, life and health insurance are deemed high risk. Suppliers of those products and services are consequently subject to stringent regulations.

- What's important is that AI doesn't operate on its own. It's always part of existing products or processes. The AI Regulation therefore has to be seen as supplementing existing regulations for those products and processes.
- The challenge is that this technology, these developments and these problems don't align neatly with supervisory structures.
- The consequence? Almost inevitably, this lays the basis for a complex supervisory puzzle, given that various sectoral regulators are charged with supervising AI at both national and European level. And let's not forget coordination... I can already imagine an EU AI Board.
- It all seems logical, but it means the involvement in each sector of a whole diversity of national supervisory bodies that in turn are often associated in European agencies (such as the ESAs, for financial oversight). Plus, yet another EU-level coordinating board, and involvement of the European data protection authority...
- Are you still with me? So, we need strong collaboration.

Open Finance:

- Open Finance is the next step beyond Open Banking, facilitating consumer data access and sharing for even more financial products and services. It allows financial and other market participants to gain and share access to different types of financial data.
- The European Commission is expected to issue a proposal this summer addressing the risks and opportunities of Open Finance.
- The regulatory aim is to expand possibilities for data sharing and the associated benefits.
- Still, it is interesting to think about where we draw the line. Citizens' privacy is valuable.
- Last year, we prepared a discussion document with DNB.
- In it, we zoomed in on the tensions between market forces on the one hand and data protection on the other.
- Also: a single data holder that shares data can also impact others that have not shared their data.
- Some points to consider:

  - Anticipated new opportunities for acquiring data and insights will bring more responsibilities for companies processing those data.
  - The link with the GDPR is clear, and strong partnerships between financial and data protection supervisors will be crucial.
  - Both supervisory authorities and politicians will have to stay attentive to solidarity risks (such as exclusion).

Lastly: MiCA

- A speech that ignores crypto is of course no true speech at all.
- The crypto winter and recent debacles have shown just how global the crypto-assets market is.
- Problems in these markets resemble those in the regular financial sector. That's hardly surprising, as crypto-assets markets are in many ways modelled on the regular system. This means they've also inherited the risks: extreme use of leverage, unlimited lending, no segregation of assets, etcetera.
- The underpinning technology and mystique only heighten the risks.
- The big question, and challenge, is whether MiCAR can bridle the tumultuous crypto markets. Could MiCAR have prevented the FTX debacle? Frankly, I am not sure.
- So, how do we feel about MiCAR?
    - Regulation is an improvement, but it doesn't make the situation watertight. MiCAR is only the first step...
    - The perception of safety is greater, but MiCAR cannot create a fail-safe crypto-land. At best, it offers somewhat more protection.
- What I am certain of is that MiCAR creates handholds for supervision.

- However, existing regulations can be useful too. In the case of a fictitious situation concerning an FTX-type entity with a main presence in the EU, MiCAR would provide a basis. What do I mean by this?

  - First, we need to identify what type of entity we are dealing with. An investment firm as defined under MiFID or a CASP (crypto-assets service provider) that offers multiple services?

- Both frameworks (MiFID and MiCAR) offer means for supervision of: governance, conflicts of interest, segregation of assets, prudential oversight and so forth. With the caveat that MiCAR has been developed to a limited extent, this will lead to challenges, I can tell.
- And what about all sorts of tokens created out of thin air? How should we categorise FTT? I suspect as a utility token. Why is this qualification important? Some of these tokens have no intrinsic value, therefore they are unsuited to serve as collateral (for transactions).
- Being less detailed than MiFID, MiCAR requires interpretations by supervisory authorities. Timely and decisive interpretations.
- Not 27 different interpretations, but rather a clear line laid down by ESMA. What do we need for this? A good grasp of the market and cooperation among 27 Member States.
- A good grasp of the market necessitates constructive dialogue with market parties. Interpretations require cooperation, speed and courage.

Ladies and gentlemen,

- We have witnessed advances over the past 30 years, and in the years to come, digital advances will move even faster. Consider:
  - The evolution of generative AI and even quantum computing.
  - Next generation forms of embedded finance; further integration of financial products into digital interfaces that users interact with daily.
  - New interesting market dynamics will arise between: tech companies (big and small), digital platforms, financial market participants and policy makers.

- Policy makers will do their utmost to develop regulations based on these developments in order to facilitate the use of new opportunities and at the same time addressing risks.
- Regulators and supervisors do their best to translate these new regulatory frameworks into the ever changing and complex reality.

- For that, we need intensive dialogue and intensive collaboration between supervisory authorities and the sector. Precisely as we are doing at Afore.
- 30 years ago, the potential of digitalisation and the speed at which it unfolded may have caught us off guard.
- We must not let that happen again. Plan for the future.

Thank you for your time.