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The growth of big techs in the financial sector: which risks, which regulatory responses?

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Summary

The major digital players, also referred to as "big techs", still play a limited role in the European financial services sector. However, buoyed by technological innovations that give them a significant comparative advantage, big techs are gradually extending their range of service to areas previously covered by entities subject to prudential supervision. In addition, they have considerable potential for growth, owing to their very large user community, their data-processing capacity and their financial strength.

The fast-paced growth of big techs in finance could pose risks to financial stability. On the one hand, the phenomenon of fragmentation of financial operations, to which this development contributes, may lead to an increase in traditional financial participants' dependency on the services offered by big techs, raising operational resilience concerns for the entire industry. On the other hand, the growth of these groups' activities, particularly in the provision of non-bank lending, whether directly or through distribution, possibly combined with payment activities, asset management activities or crypto-asset services, could open up new vectors for the contagion of financial risk to the rest of the economy, owing to the multiple sources of interconnectedness with the financial world and the real economy.

The EU has been able to provide a swift response to a number of key resilience and competition issues, notably through the Digital Operational Resilience Act (DORA) and the Digital Market Act (DMA). Beyond these essential aspects, however, regulators must ensure that the risks to financial stability posed by the emergence of these players are properly understood and managed. In this respect, several gaps remain in the current regulatory framework that call for adjustments:

- In the case of groups that predominantly conduct non-financial activities, prudential consolidation regimes, where they exist, can easily be circumvented. A fragmented growth strategy can thus prevent supervisors from having an exhaustive view of all the activities

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carried out by a single group, and of the potential interdependencies between financial and ancillary activities. This lack of a comprehensive view makes the conduct of supervisory tasks particularly complex. In particular, it poses challenges for the calibration of potential micro-prudential measures, and it provides groups with opportunities to implement banking maturity transformation schemes without the associated constraints, raising legitimate concerns as regards equal treatment with traditional regulated players²;

- In a digitised world, the lack of a harmonised European regime governing credit granting opens up opportunities for arbitrage that can easily be taken advantage of by these players, who can establish their activities in places where regulatory constraints are weaker. Yet, the failure of big tech players providing credit services on a large scale could affect financial stability, given their numerous interconnections with financial partners and their potential links with savers;
- The current regulatory framework is not necessarily suited to situations in which the balance of power with commercial partners is reversed, which could lead to a loss of control and autonomy for financial institutions in the event that big tech partners become essential to the distribution of financial products and services.

In order to provide a better framework for the development of big techs in the financial sector and reconcile the need to preserve innovation capacity and financial stability imperatives, it would therefore appear necessary to supplement the responses already provided by the EU in terms of operational resilience and competition with a financial component.

As part of the debate that is already underway at both international and European level, this discussion paper sets out **two main avenues for regulatory change** which could be implemented sequentially and proportionately:

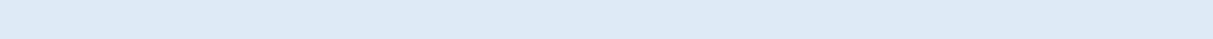
- 1. Strengthening and harmonising the sector-specific rules governing the activities that big techs develop in particular.** This objective can be broken down into two short-term priorities: i) firstly, the introduction of prudential requirements at consolidated level for payment services and electronic money activities, in order to have reliable and up-to-date information available on all these groups and their activities at European level; ii) secondly, the introduction of a European regime covering non-bank lending, which is currently fragmented between various national regimes, in order to bolster the financial soundness of these institutions and limit the potential for regulatory arbitrage as regards the groups these entities belong to.
- 2. Requiring mixed activities groups to cluster their significant financial and ancillary activities within a dedicated structure,** in order to allow for consolidated supervision and, where appropriate, where the combined financial activities of the group presents risks that are similar in nature to those of a credit institution, to allow for banking rules to apply to the entire financial subgroup.

² As banking groups are required to include all the group's financial and ancillary activities in their prudential reporting scope, and given that all these elements will, in turn, be factored in for the calculation of their capital requirements pursuant to the Capital Requirements Regulation.

Far from hampering the capacity for innovation of big tech groups, these regulatory changes are likely to boost them by providing a stable and harmonised legal framework.

This document is divided into four main sections: firstly, it describes how big techs have gradually entered the financial services market, and how this trend could increase in the future. It then outlines the risks to financial stability associated with their growth and highlights the limitations of the existing regulatory framework. Lastly, it sets out a series of regulatory proposals that would contribute to better understand and contain these risks, without stifling these players' innovation capabilities.

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Introduction

In recent years, a number of players specialising in new technologies and digital innovations have entered the world of financial services. Often referred to as fintechs³, a contraction of the words "finance" and "technology", they are defined by the Financial Stability Board⁴ as actors that develop technology-enabled innovation in financial services, that could result in new business models, processes or products with an associated material effect on the functioning of financial markets and traditional financial institutions as well as on the way financial services are provided⁵.

Alongside this emerging population of fintech players, big techs have a distinctive place. This category usually refers to large international technology conglomerates the main activity of which revolves around the management of social networks, e-commerce platforms, internet search engines and the provision of software. These players stand out on account of their size and their impact on society, as well as due to the unique commercial capabilities they have built, thanks to their expertise in data analysis, data processing and data enhancement.

The rise of big techs in the financial sector has been driven by a combination of factors. It notably benefited from new consumer habits associated with the momentum towards the digitalisation of the economy, as users want to be able to access financial services and products quickly, at any time through a single point of entry. Big techs have been able to meet these new expectations, against a backdrop of COVID-19 acting as a catalyst for their growth through the rapid growth of e-commerce during the pandemic. The financial capabilities of big techs also allow them to implement efficient external growth strategies, thereby contributing to their development and possibly to the creation of oligopolistic situations.

These developments brought by big techs paved the way for numerous innovations in the financial sector, and allowed for efficiency gains. However, they also create new risks. The emergence big techs in financial services has the notable effect of fragmenting value chains and thereby the processing of financial transactions. This phenomenon is especially noticeable in the outsourcing by traditional financial firms of an increasing share of certain services, including those deemed to be "essential" or "critical"⁶ for the continuity of their operations. It is also reflected in the emergence of new distribution practices through digital platforms. Big tech players therefore carry out activities as

³https://abc-economie.banque-france.fr/sites/default/files/medias/documents/abc-mot-de-l-actu-fintechs_20190904.pdf

⁴ <https://www.fsb.org/work-of-the-fsb/financial-innovation-and-structural-change/fintech/>

⁵ These fintechs include, for instance, licensed institutions, crowdfunding intermediaries, financing companies offering deferred payment solutions embedded in merchant websites, providers of alternative payment methods (e.g. Apple Pay) and a wide range of digital platforms or interfaces providing financial services on an ancillary or core business basis, either directly or in partnership with other financial institutions.

⁶ In line with the definitions set out in the European Banking Authority's Guidelines on outsourcing arrangements ([EBA/GL/2019/02](https://www.esrb.europa.eu/en/essays-and-articles/2019/02/20190201)).

diverse as intermediation (distribution of financial products, including as “white-label” products⁷), provision of technical services (such as cloud services) and middle office-type services (credit scoring), with the possibility for these various activities to be carried out simultaneously. This value chain unbundling phenomenon leads to an increase in the number of technical participants and intermediaries, which can in turn generate complexity in terms of the sharing of risks and responsibilities. This fragmentation also contributes to blurring the line between purely technical or commercial services and financial activities, making it more difficult for competent authorities to carry out their supervisory duties.

For the time being, the growth of big techs in the financial sector has remained relatively targeted and contained. Yet, it calls for the attention of supervisors and regulators, in view of the far-reaching consequences it could have for the financial sector as a whole. The growing importance of big techs in the technological infrastructure and services sector (telecommunications, software, cloud services, AI, etc.), some of which have already reached systemic importance, coupled with their potential for growth in areas such as the provision of loans or the issuance of crypto-assets, call for the consideration of regulatory adjustments **to ensure that their development can continue in a controlled manner with regard to financial stability imperatives while ensuring a level playing field with other players.** The issue of the suitability of the current regulatory framework appears especially relevant, as it was designed to cover clearly identified players and financial services confined to regulated entities, in respect of which the role of technical or commercial partners was generally limited.

This analysis is not intended to cover all the issues arising from the activities of big techs. Building in particular on recent publications by the Bank for International Settlements⁸ and the International Monetary Fund⁹, this analysis focuses on financial stability issues, dealing only marginally with the equally important issues of consumer protection, money laundering and terrorism financing, data protection and competition.

⁷ In partnership with financial institutions, these intermediaries integrate financial services directly into their service offering through an interface connected to the partner institution’s systems. For instance, this is true of market places or budget or financial management applications that allow users to open and monitor a payment account on their platform and under their own brand, with the funds ultimately being held within the partner financial institution (such arrangements include, for example, [Helios](#) in partnership with the credit institution Solaris, or [PixPay](#) in partnership with the electronic money institution Treezor).

⁸ [Big techs regulation: in search of a new framework](#)

⁹ [Big techs in Financial Services: Regulatory Approaches and Architecture](#)

1. Big techs' foray into financial services

Several studies by the Financial Stability Board¹⁰ and the Financial Stability Institute¹¹ have recently shed light on the emergence of big techs in financial services. The shape and magnitude of this development varies across countries and regions. In the United States and in Europe, the development of financial services (other than technical services) still remains limited, especially when compared with the particular case of China or other emerging countries¹². European authorities offer various explanations for this less advanced stage of development, including the more stringent regulatory framework, the low level of expected profit margins, the already highly competitive environment or societal factors (trust in long-established traditional financial players)¹³.

Table 1: licenses granted to big techs for banking, non-bank lending and payment activities at international level

| Financial service offerings by big tech companies | | | | | | | | Table 1 |
|---------------------------------------------------|-----------------------------|----------------------|------------------|----------|---------------|------------------|-----------|---------|
| Big tech | Main business | Banking [%] | Credit provision | Payments | Crowd-funding | Asset management | Insurance | |
| Google | Internet search/advertising | ✓* | | ✓ | | | | |
| Apple | Tech/producing hardware | | | ✓ | | | | |
| Facebook | Social media/advertising | | | ✓ | | | | |
| Amazon | E-commerce/online retail | | ✓ | ✓ | ✓ | | ✓ | |
| Alibaba (Ant Group) | E-commerce/online retail | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | |
| Baidu (Du Xiaoman) | Internet search/advertising | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | |
| JD.com (JD Digits) | E-commerce/online retail | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | |
| Tencent | Tech/gaming and messaging | ✓ | ✓ | ✓ | ✓ | ✓ | ✓ | |
| NTT Docomo | Mobile communications | ✓ | ✓ | ✓ | ✓ | | | |
| Rakuten | E-commerce/online retail | ✓ | | ✓ | | ✓ | ✓ | |
| Mercado Libre | E-commerce/online retail | | ✓ | ✓ | | ✓ | | |

✓ Provision of financial service through big tech entity and/or in partnership with financial institutions outside big tech group in at least one jurisdiction. ✓* Launch expected in 2021. % The core activity of an entity engaged in banking is taking deposits, though regulations vary across countries.

Sources: BIS (2019); Citi GPS (2018); FSB (2019b); IBFED and Oliver Wyman (2020); van der Spek and Phijffer (2020); public sources; FSI.

Source: FSI brief - Big techs in finance: regulatory approaches and policy options - March 2021

¹⁰ Financial Stability Board (FSB), an international coordinating body for the supervision and oversight of financial institutions

¹¹ Financial Stability Institute - FSI, attached to the Bank for International Settlements - BIS

¹² See in particular the study published by the Financial Stability Board in March 2022, [FinTech and Market Structure in the COVID-19 Pandemic](#)

¹³ See paragraph 86 of the following report [Joint European Supervisory Authority response to the European Commission's February 2021 Call for Advice on digital finance and related issues](#)

In Europe, the “financial” activities of big techs are mostly carried out through the provision of technical services to traditional financial institutions (e.g. cloud, digital wallets) and payment services. With the exception of cloud services, to date, big techs primarily opt for partnerships for the distribution of these products and services and have not shown intention of directly offering their own financial services in the EU on a large scale. **These activities are typically carried out by legal persons established outside the EU.** Therefore, they do not trigger the application of a regulated status and do not generally give rise to direct supervision or prudential requirements in the jurisdictions where they are conducted. However, the recent stocktake jointly conducted by the European Supervisory Authorities (ESAs)¹⁴, while indeed finding that development is limited in the financial sector, reveals that a number of big techs are already licensed in the European Union, including in the payment services sector, which would allow them to provide payment services in Europe directly should they wish to do so.

Table 2: licenses granted to big techs for banking, non-bank lending and payment activities in EU Member States

Table 1: Stocktake results: MAGs as electronic money institutions (EMI), payment institutions (PI), credit institutions (CI), insurance intermediaries/undertakings.

| | Group | Subsidiary | Home MS | Host MS |
|----------------------|---------------------------|-------------------------------------------------|---------|---------|
| E-Money Institutions | Alphabet (Google) | Google Payment Lithuania UAB | LT | 12 |
| | Meta Platforms (Facebook) | Facebook Payments International Limited | IE | 14 |
| | Amazon | Amazon Payment Europe SCA | LU | 16 |
| | Alibaba (Ant Group) | Alipay (Europe) Limited S.A. | LU | 4 |
| | Uber | Uber Payments B.V. | NL | 10 |
| | NTT Docomo | DOCOMO Digital Payment Services AG | LI* | 3 |
| Payment I | Alphabet (Google) | Google Payment Ireland Limited | IE | 13 |
| | Tencent | Wechat | NL | 2 |
| Credit I | Orange | Orange Bank | FR | 3 |
| | Rakuten | Rakuten Europe Bank S.A. | LU | 13 |
| Insurance | Tesla | Tesla Insurance ltd (undertaking) | MT | 1 |
| | Vodafone | Vodafone Insurance Limited (undertaking) | MT | 9 |
| | Amazon | Amazon EU Sarl (intermediary) | LU | 2 |
| | Apple | Apple Distribution International (intermediary) | IE | 2 |
| | Orange | Orange Slovensko (Intermediary) | SK | / |

*LI: until 1 June 2022

Source: Joint-ESA Report on 2023 stocktaking of BigTech direct financial services provision in the EU (Home MS - ‘Home Member State’: jurisdiction of registration of the European subsidiary; Host MS -

¹⁴ [Report on joint-ESA 2023 stocktaking of BigTech direct financial services provision](#)

'Host Member State': number of European jurisdictions in which the subsidiary operates, either under the freedom to provide services or through a branch).

This “stealthy” penetration strategy, which takes place outside of the existing regulatory framework, **makes it more complex for supervisors to build a clear and comprehensive view of the financial activities of these players**, of their degree of entanglement with traditional institutions and of the associated risks.

While these activities are not necessarily systemic today when considered individually, the specific characteristics of these groups should also be considered. Given the size of their networks, the amount of data collected from their users, their innovative capabilities and their advance in processing, analysing using and valuing data, they enjoy a significant competitive advantage that could allow them to grow very rapidly in the European financial sector. This is a fundamental feature of big techs that sets them apart from other non-financial conglomerates that have developed an offering of financial services ancillary to their industrial activity, such as car manufacturers, and one that **warrants particular attention from regulatory and supervisory authorities**.

1.1. A gradual, multifaceted and fragmented foray into the European financial sector

The growth of big techs’ financial activities in the EU is gradual and fragmented.

The importance of big techs has increased significantly in recent years, **primarily with the provision of technical services** related to their core business, and in particular through the provision of cloud services. Many traditional financial players have gradually migrated their IT systems and infrastructure to these new solutions as a way to lower their costs, improve agility and user experience and strengthen their own IT security.

In the banking and financial services market, the entering strategy used by big techs can be described as hybrid, insofar as it can be achieved with direct offers¹⁵ or rely on targeted partnerships with established players¹⁶. The financial services offered are mainly aimed at small and medium-sized enterprises or individuals, targeting specific segments of the value chain (mobile payments, consumer credit intermediation).

¹⁵ This is especially true in emerging countries, including China, where groups such as Alibaba and Tencent have established regulated financial institutions (MYBank for Alibaba and WEBANK for Tencent), which can be co-owned with traditional banks, making it possible to provide lending to small businesses and individuals directly, which they record on their balance sheet. In China, the share of credit services directly provided by big techs is estimated at 2-3% of gross domestic product (BIS Working Papers 1084 BigTech credit and monetary policy transmission: micro-level evidence from China).

¹⁶ This is notably true for Apple in the United States, which had partnered with Goldman Sachs to offer loans and savings products associated with owning an Apple Card issued by Goldman Sachs. Under this partnership, loans and deposits are taken out via the Apple application and are assimilated to "Apple" products, but are recorded on Goldman Sachs' balance sheet. However, Apple intends to develop a direct Apple Pay Later offer through a fully-owned financial institution (Apple Financing LLC).

In the EU, **big techs have not, as of yet, opted for significant development in the form of credit institutions, payment institutions or electronic money institutions with a view to offering financial services directly**¹⁷. They mostly carry out single, unbundled investments in the financial sector, as service providers or intermediaries, without bearing the financial risks directly.

Box 1: The financial activities of big techs across the various segments of the value chain

In the payments segment, three main strategies can be identified: (i) the provision of services of a purely technical nature, for example allowing for payment cards to be registered and used for payments directly on someone’s mobile phone (digital wallet, such as Apple Pay or Google Pay); (ii) the creation of customer interfaces for products offered by partner financial institutions (‘white labelling’); (iii) the direct offer of payment services through a payment institution and/or an electronic money institution.

In the credit segment, three entry strategies can be identified: (i) the distribution, through a partnership (either exclusive or not) with a financial institution (e.g. Amazon partnering with various institutions in the Union¹⁸); (ii) the development of an offer for non-bank lending and finance, for instance using a payment by instalments model (‘Buy Now, Pay later’ such as the one Apple Pay Later launched in 2023) or for leasing; (iii) as a credit assessment agency, setting up its own credit scoring system based on collected data on users, possibly in combination with a distribution activity.

In the deposit segment, market entry can also be achieved as an intermediary or distributor of savings products (e.g. the services developed by *Raisin*), or through the development of a direct offer through the establishment of a credit institution (e.g. NTT Docomo Group in Japan).

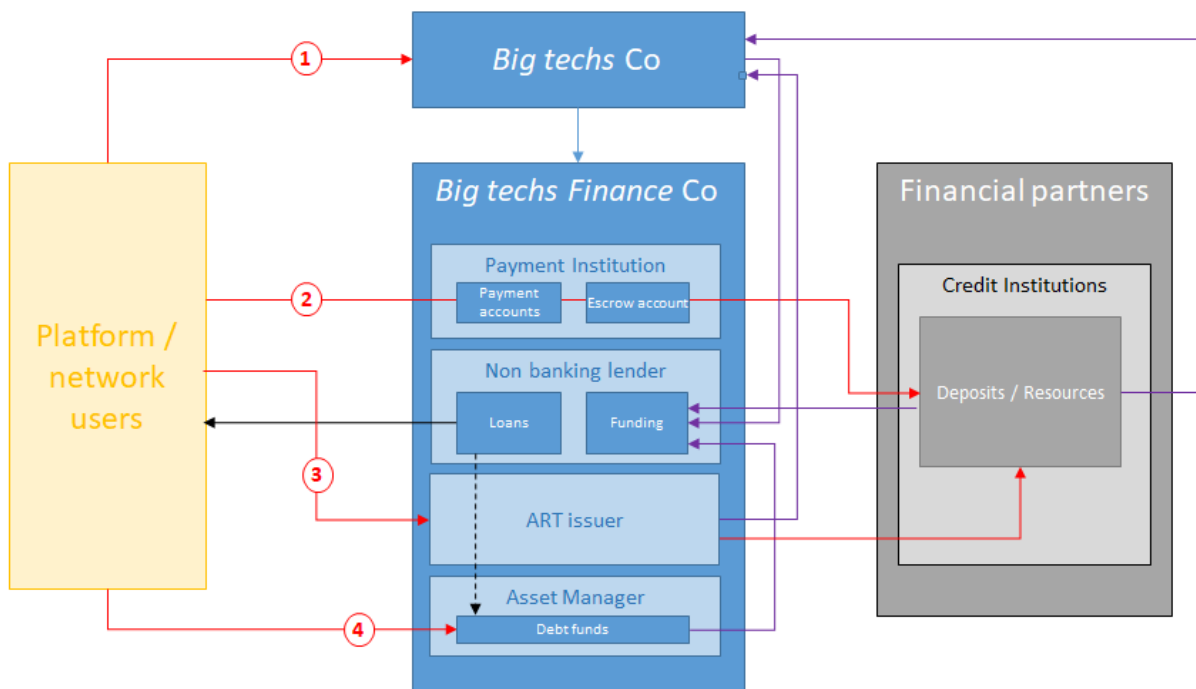
While services currently appear to be “unbundled”, their combination could nevertheless lead to virtual reconfiguration as a bank without the associated constraints, including regulatory and supervisory ones. For instance, a combination of licensed and unlicensed subsidiaries and partnerships would allow for platform users’ funds to be used to finance lending activities, mirroring the traditional maturity transformation schemes used by banks.

¹⁷ Amazon, Meta and Google have established payment institutions and electronic money institutions, but their activities remain relatively marginal and highly specific.

¹⁸ See Section 3.2 of the following EBA report: [Final Report on response to the non-bank lending request from the CfA on digital finance](#)

Figure 1: simplified illustration of the reconfiguration of a bank

- ① Direct or indirect investment in securities issued by the parent tech company by the users, with the parent company funneling the collected funds to finance the credit activities carried out by its financial subsidiaries;
- ② Funding received from partner credit institutions where the deposits from users would be held;
- ③ Issuance of crypto assets in the form of tokens the referenced assets of which would be securities issued by the parent tech company and would funnel the funds collected from users to finance the credit activities carried out by its financial subsidiaries;
- ④ Users' direct or indirect investment in funds invested in loans originated by the financial subsidiaries.



In configurations like this one, big techs mostly remain outside the scope of regulated activities, making it difficult for supervisors to gain an accurate and comprehensive understanding of the interconnections between the various activities and infrastructures within these groups, as well as between these groups and regulated financial institutions.

1.2. The comparative advantages of Big Techs

Initially introduced as “pure players” of the digital economy, big techs have gradually diversified their activities in order to acquire new market shares. Unlike fintechs, **these players enjoy significant comparative advantages to enter and grow rapidly on a large scale in the banking and financial services market.**

First, **network effects** allow these platforms to enter the market by tapping into a large community of customers (nearly 3 billion registered Facebook users in 2023). This network effect also entails self-sustaining, even exponential growth dynamics: the more subscribers the platform gets, the more

services and products are added to its offer, the more attractive it becomes for new users, customers and sellers, with a considerable “lock-in” effect. Moreover, they also derive a competitive edge over traditional players from the data analytics and interwoven activities they provide (a phenomenon also referred to as the DNA Loop, DNA standing for Data analytics, Network externalities and interwoven Activities). Thus, once a Bigtech has attracted a sufficient number of users on both sides of its platform, network effects kick in, allowing that firm to accelerate its growth and generate economies of scale. The more users are using the platform, the more data they generate that can be analysed by the firm, which in turn creates value and attracts new users.

For illustrative purposes, the number of Alipay users grew by 15% in one year, between 2016 and 2017, and by 73% the following year¹⁹. This would go a long way towards facilitating the gradual customer acquisition phase that is commonly associated with the setting-up of a business.

Secondly, large-scale data collection, data analysis and data processing capabilities, coupled with **their advanced expertise in artificial intelligence (AI) and machine learning technologies**, allow big techs to have extensive knowledge of their customers’ profile. Relying on data massively collected through social networks or e-commerce activities, big techs can offer services deemed more tailored to their customers, based on identified customer needs, and therefore capture market shares and generate new sources of revenue²⁰. In addition, these new financial services will allow for the collection of new data which could in turn be monetised and increase the attractiveness of platforms.

These firms therefore combine market entry strengths with a capacity for very fast growth, such as regulators and supervisors may never have faced before. **Hence, the suitability of the existing regulatory framework is worth examining in light of the growth potential of these players, regardless of their current influence in Europe still being limited.**

2. Risks related to the financial activities conducted by big techs

The development of new services by big techs, especially in the areas of payments and loans, can generate positive externalities by fostering financial inclusion²¹, offering services at lower cost and driving innovation. However, **the entry of these new players and the new business models associated with them also create risks with respect to financial stability, consumer protection, personal data protection and competition.**

¹⁹ FSI Insights on policy implementation, Big techs interdependencies, by Juan Carlos Crisanto and al, July 2022.

²⁰ Crisanto, Ehrentaud and Fabian, 2021, cited in Big techs in Financial Services: Regulatory Approaches and Architecture, IMF /2022/002.

²¹ Nevertheless, these positive externalities should not be overestimated, especially those pertaining to financial inclusion, as their sustainability has yet to be established. Indeed, the business model based on large volumes and low profit margins could be materially affected by changes in the economic environment. It is also uncertain whether pricing policies will be maintained over time, as players tend to attract new users with attractive prices and then revise their original offer or tie other payable products to the use of primary services.

2.1. The risks to financial stability

The growth of big techs in the financial sector poses several risks to financial stability. On the one hand, the heavy reliance of financial institutions on a limited number of players and on the technical services they provide raises operational resilience issues. On the other hand, the increased reliance on big techs by the financial sector for the provision of banking services, whether it be for distribution activities or for the provision of non-bank loans, could create bridges between the two sectors and generate new contagion risks. Given the interdependency between financial and business activities within big tech groups, which stems from their use of shared infrastructure, data and resources, issues encountered in the course of business activities or shared infrastructure could in turn make these firms unable to ensure the continuity of their intermediation activities or to carry out their duties related to the offer of financial services.

2.1.1. Risks related to the provision of IT services

Big techs are now leading players when it comes to *cloud* hosting services, with a very high market concentration: the four largest service providers (*Amazon Web Services, Microsoft Azure, Google Cloud, Alibaba Cloud*) hold 70% of the market share²², and financial institutions tend to increase their use of these solutions²³. While big tech investment in infrastructure technology and security are unparalleled²⁴, concentration and dependency levels combined with the limited substitutability of service providers, interoperability and data portability issues create operational vulnerabilities for all the financial institutions that use these services. Such vulnerabilities are further compounded by the fact that these actors are established in jurisdictions located outside the EU, raising digital sovereignty issues. Any disruption or failure of these systems could therefore have repercussions on the entire financial system and pose a risk to financial stability. **It appears that these cloud service providers are carrying a systemic operational resilience risk, and are already “too big to fail”.** The development of certain players in the mobile payment segment (offering “digital wallet” services, such as Apple Pay, Amazon Pay or Google Pay) also raises specific issues in terms of operational risk and fraud prevention or fight against money laundering, with difficulties for supervisors in ensuring compliance with related requirements.

2.1.2. Risks related to distribution activities

The development of partnerships according to which big techs would act as business introducers for credit institutions poses a number of risks, notably including **moral hazard**. These brokerage-related risks are not new, but they could grow to unprecedented levels when combined with other services contemplated by big techs, such as the provision of credit scoring services. Without risk participation, big techs would then have an incentive to generate volume in order to collect commissions without considering or paying particular attention to credit quality. There is also a risk that **situations may arise in which some financial institutions become dependent** on these business-introducing big techs,

²² FSI Insights on policy implementation, Big techs interdependencies., by Juan Carlos Crisanto and al, July 2022.

²³ According to a survey commissioned by Google Cloud, at end-2020, institutions that use “internal” IT infrastructure planned to migrate 40% of their activities to the cloud.

²⁴ Big Techs’ R&D expenses on technology services are three to four and a half times higher than those of the largest banks (G-SIBs) - FSI Insights on policy implementation, Big Techs interdependencies, by Juan Carlos Crisanto and al, July 2022.

forcing institutions to maintain these partnerships regardless of the imposed conditions underlying them.

Intermediation in savings products or in investment products and in payment services (especially payment accounts) can also generate new risks for users and partner institutions, regardless of these products and services being white-labelled or not. The use of a third-party interface allowing users to access their accounts, assets and services adds complexity to processing chains and poses an additional risk to business continuity. In the event of disruption or failure, users could be deprived of access to services or even to their funds, without any possibility for the partner institution to take remediation measures. In the most extreme scenarios, the partner institution could also incur significant costs to in-source the management back or provide support to the intermediary (so-called “step in” measures), with the aim of maintaining the interface and ensuring business continuity. In addition, a reputational risk also exists for the partner institution in the event of operational issues encountered by the provider or in the event of fraud, which could lead to mistrust among users causing them to withdraw their assets (run risk), with a potentially systemic impact in cases where many institutions rely on a limited number of platforms.

The development of big techs engaged in intermediation of financial products and services through their digital interfaces could thereby reverse traditional intermediation patterns, making these new players the main financial services “originators”. In extreme scenarios, these financial services would be directly embedded in platforms, with financial institutions acting as secondary service providers, with no control over financial flows, despite the fact that they would still bear the financial risks on their balance sheets. In such a scenario, the sudden discontinuation of a partnership could deprive the partner institution of resources and generate liquidity risk. The dependency of institutions could also include many support functions, such as client credit scoring or anti-money laundering monitoring tools, for instance, either directly or through the use by the institution of data provided by big techs pursuant to partnerships entered into with them²⁵, and could extend as far as the definition of the terms and conditions of products being imposed on partner institutions by intermediaries²⁶. In situations of dependency such as these, financial institutions remain solely responsible for ensuring the compliance of their activities with regulatory requirements, but they could encounter difficulties in the effective implementation of compliance, where compliance would run counter to the interests of their partners or big tech providers. Moreover, the profitability and expertise of institutions are likely to be affected by this new division of responsibilities. All in all, the issue of risk sharing between distributors and banks could prove to be crucial in an environment in which the balance of power is reversed.

²⁵ For instance, in the case of Amazon’s partnership with “Marcus by Goldman” to open liquidity lines to sellers that are active on the platform, Amazon shares, among other things, information and analyses on sales and customer satisfaction to identify eligible borrowers.

²⁶ For illustrative purposes, according to recent press reports, Goldman Sachs is seeking to terminate its partnership with Apple, whose profitability model is not ensured for the bank, in the absence of account management fees and commissions. In our view, this case sheds light on the powerful negotiation levers that big techs can use to dictate their terms.

2.1.3. Risks related to the provision of non-bank lending

In a more forward-looking perspective, given current practices in the EU, big techs could also take advantage of exemptions from banking monopoly rules stemming from the various national regimes to develop a direct non-bank lending offer. Such activities could, for instance, emerge within the scope of deferred payment or in other forms of non-bank lending, such as factoring. In the event that the entity retains those exposures on its balance sheet, the use of an unregulated or low regulated status would not ensure sufficient loss absorbing capacity. In the event of significant losses, a risk of transfer to creditors could materialise, but it could also present a risk for business continuity and customer user viability, as the latter could potentially be deprived of a non-substitutable source of financing. These contagion risks between low regulated or unregulated financial companies and the regulated financial sector were recently highlighted with the failure of Greensill²⁷; the magnitude of these risks could increase significantly in the event of the failure of a big tech firm, given the number of users potentially involved.

The risk initially borne by big techs could also be transferred, for example, to debt mutual funds or securitisation special-purpose vehicles, under an originate-to-distribute model. In such a scenario, if the conditions under which these payment facilities are granted are not rigorous, especially when assessing customers' repayment capacity, the associated defaults and losses could spread to the financial sector.

Although they do not hold customer assets directly, these entities are connected to the financial sector. Their bankruptcy can lead to spillover effects, with material repercussions for the economy or financial stability, in view of the volumes potentially at stake.

These growing interdependencies between big techs and traditional players are creating contagion risks that, although they remain contained today, especially as far as Europe is concerned, could quickly increase magnitude. Yet, big techs remain largely **outside the scope of supervisors' oversight**, in the absence of an appropriate regulatory framework, and are **not subject comprehensive prudential requirements in respect of their financial activities**.

2.2. Competition, consumer protection and data protection issues at stake

The growth potential of big techs in the financial sector raises issues concerning competition, consumer protection and personal data, which are not the main focus of this paper and as such are only briefly mentioned.

²⁷ Greensill was a UK-based financial company specialised in short-term lending to firms and reverse factoring that used securitisation as a way to finance its business. Following the emergence and subsequent confirmation of concerns regarding management and the quality of exposures, their financial partners divested, leading to Greensill's bankruptcy. The failure of Greensill created serious challenges for the industrial groups that used its financing services, leading to government support measures. In addition, some financial institutions incurred significant losses, in connection with their investments in Greensill issuances, or indirectly, as a result of their marketing of Greensill products to their customers.

2.2.1. Competition issues at stake

The network effect on which big techs capitalise can contribute to self-sustaining growth dynamic and raise competition issues. The more users turn to the services offered by these platforms, the more personalised and therefore attractive these services become. A "lock-in" strategy could ensue, that would make it more difficult for users to migrate to a competing platform. These circumstances can make it easier for big techs to engage in anti-competitive practices and abuse their dominant position. Legal proceedings have been or are currently being brought against such practices in France and the EU²⁸. Similar issues could arise where financial services are concerned.

2.2.2. The protection of consumers and personal data

The protection of consumers and their personal data is one of the main issues raised by the expansion of big techs. Several studies show that the practice of data sharing between departments within the same entity or group is widespread²⁹. The use of personal data makes it possible, for instance, to develop credit scoring systems that assess the creditworthiness and credit risk of borrowing customers. Using artificial intelligence, big techs are able to define an accurate and granular risk profile based on a user's digital footprint, thereby increasing risk measurement sensitivity. However, the widespread use by financial institutions of ratings provided by a few players, for their small and medium-sized businesses and retail customer segments, could lead to the exclusion of certain customer groups. In addition, the concentration of offers on a single platform may lead intermediaries to engage in tied selling practices or to act in breach of their duty to provide information or advice on the risks associated with the various products as well as on complaint and redress mechanisms. It may prove necessary to strengthen requirements in this area in order to adapt them to new digital consumer patterns.³⁰

3. Analysis of regulatory methods and limitations of the current framework

3.1. Entity-based regulation or activity-based regulation?

The unique configuration of big tech groups, which operate at the borderline of the banking and financial system, raises questions about the suitability of the current prudential framework. This framework essentially relies on an entity-based approach, as opposed to an activity-based approach³¹.

²⁸ See for example the [ruling](#) issued in September 2022 by the Court of Justice of the European Union against Google for imposing unlawful restrictions on Android mobile device manufacturers and mobile network operators; see also, concerning wallet services, the [commitments](#) made by Apple to allow the use of competing wallets on their iPhone, following preliminary findings made by the European Commission.

²⁹ FSI Insights on policy implementation, Big techs interdependencies, by Juan Carlos Crisanto and al, July 2022

³⁰ See recommendation 2 of the following report [Joint European Supervisory Authority response to the European Commission's February 2021 Call for Advice on digital finance and related issues](#)

³¹ See the following BCBS FSI publication No 19 - [Entity-based vs activity-based regulation: a framework and applications to traditional financial firms and big techs \(bis.org\)](#) - for an in-depth analysis of the differences between these two regulatory methods and the benefits and constraints associated with them.

Activity-based regulations impose restrictions on the conduct of specific activities, without examining the entity that carries them out or any other activities that may be carried out by that entity, thereby allowing for a particularly wide scope. For example, the European Directive on credit agreements for consumers³² covers a scope that extends to all types of credit, including crowdfunding credit and “buy now, pay later” schemes for the acquisition of goods and services, irrespective of the entity offering them. Similarly, certain rules relating to market integrity, such as the ban on the use of insider information, or the rules on the protection of personal data, follow the same line of reasoning.

Entity-based regulations govern the conduct of specific activities through requirements applied to the entities that conduct them. These regulations make it possible to cover a range of activities within the same entity. One example of entity-based regulation is the capital or liquidity requirements set out under (EU) Regulation 575/2013 (CRR).

When it comes to the financial activities conducted by big techs, an activity-based approach, while seemingly effective in addressing both data protection and consumer protection concerns, **could prove more complex in terms of the implementation of prudential requirements**, which are essential to ensure the resilience of entities engaged in financial activities. Indeed, in the absence of any effective legal segregation, it would be very complex in practice, and surely not very efficient, to impose requirements only on a subset of financial activities carried out within the same entity or group³³. This is because the liquidity or own funds that would be required to cover these regulated financial activities could not, by definition, be “allocated” to these activities, and would remain available for unregulated activities as well.

When applied to big techs, the activity-based approach can also raise other implementation issues. Firstly, in the specific cross-border context of big techs’ activities, the monitoring compliance with requirements and the enforcement of any potential sanction in the event of non-compliance becomes complex, or even impossible to implement without sufficient international cooperation. In this case, courses of action would be restricted to the ability to prohibit a player from engaging in a given activity, a ban that may be difficult to enforce once a practice has become established, and one that is likely to be circumvented in a highly digitised world. Secondly, these regulations presuppose a very specific definition of the activities covered. Yet, given the way practices evolve in the big tech sector, regulations could quickly become obsolete or struggle to adapt to new players, activities and practices. This would increase the risk of circumvention and opportunistic arbitrage.

Conversely, a regulatory approach based on entities offers two main advantages to capture the financial risks borne by big techs: firstly, it facilitates the implementation of prudential requirements and allows for the level of requirements to be aligned with the level of risk, through the use of Pillar II-type tools; secondly, it can provide supervisors with an overall view of the group and its risks, as well as of any channels of contagion between its various activities.

However, applying this kind of standards to groups conducting mixed activities, and especially to big techs, raises specific challenges, relating in particular to the level at which these rules are applied, and

³² Directive 2008/48/EC on credit agreements for consumers

³³ The allocation of own funds and liquidity to business lines can be complex and lacking in substance, since the liability of shareholders is not divisible; similarly, a globalised asset/liability management strategy makes any attempt to “allocate” balance sheet items according to business lines artificial.

the scope they should cover. In line with the discussions currently underway within international institutions (see Box 2), it seems essential to identify the right level of application of these rules, at group-wide level, or only over the scope of financial activities, depending on the level of risk and the potential for contagion between the various activities conducted.

Box 2: The position of international organisations

In order to address the complexity of big tech groups, and to strike a fair balance between the need to control the risks associated with their development and the need to avoid imposing excessive barriers to innovation, and having acknowledged the inadequacies in the current regulatory framework in force in the home countries of the main big tech groups³⁴, the Bank for International Settlements (BIS) and the International Monetary Fund (IMF) have taken position in favour of an approach that would combine both the so-called “segregation”³⁵ and “inclusion”³⁶ approaches (the “prohibition” approach, consisting in denying big techs access to the provision of financial services, being deemed too drastic). These approaches presuppose the implementation of entity-based financial soundness requirements, the level of application of which may vary.

The Financial Stability Institute (FSI), a research body co-founded by the BIS and the Basel Committee, distinguishes between (i) the requirements in terms of governance, compliance and resilience that should apply at group level and cover all financial and non-financial activities, notably in order to prevent any harmful interdependencies between the various sectors that could generate risk to financial activities, and (ii) the prudential requirements aimed at ensuring financial soundness, which should only apply to financial activities. **Regarding prudential requirements, the FSI suggests that the financial part of the group be sub-consolidated at the home and host country level.** This approach aims to allow big tech groups to cross-use data and thus avoid losing the associated efficiency gains, subject to appropriate competition and data protection safeguards, while specifically ensuring the resilience of financial activities.

³⁴ In its analysis ([Big tech regulation: in search of a new framework](#)), the FSI finds that in both the United States and the EU, the scope of the financial authorisation and supervision regimes does not satisfactorily address the scenario of non-financial groups that develop substantial non-bank financial activities (i.e. there is currently no “bank holding company” supervisory regime with prudential requirements that can be applied based on consolidated financial activities).

³⁵ **This approach would require that the financial services of Big techs be grouped together under a financial holding company that would be subject to prudential rules at its level.** This ring-fencing practice would reduce the potential for contagion effects from non-financial activities to financial activities. This could be achieved by prohibiting the use of shared technology platforms used across a group as well as any form of data sharing between the financial and non-financial components of the group. This approach is conceptually straightforward, increases the transparency of Big techs’ organisational structure and facilitates supervision. However, pushed to the extreme, this would prevent Big techs from achieving synergies and economies of scale, and it could in time lead to crowding Big Techs out of financial services.

³⁶ **This approach would impose governance, business conduct, operational resilience and, as needed, financial soundness requirements on Big techs conducting significant financial activities at group-level and/or on Big techs as absolute requirements.** This is because most of the risks associated with Big techs are not strictly related to their financial soundness, but rather to their data-driven business model. The requirements would be imposed on the entire group, including to parent undertakings in the big tech industry. This approach is adapted to existing business models and recognises the fundamental role of data within the largest technology groups and their tendency to leverage data to secure dominant market positions. This would not prevent Big Techs from making effective use of the data they collect for different activities, as with the two previous approaches, provided that they comply with principles for good data governance and with effective competition rules group-wide. However, the inclusion approach is more complex than the segregation approach, as it requires effective monitoring of global groups carrying out a wide range of activities.

The application of prudential requirements at group level for a whole group would only be provided for in the event that financial activities become dominant at group level (i.e. where the parent undertaking would in fact be considered a financial holding company).

Notably concerned about the issues around competition, the IMF recommends an international approach in the long term, with a division of responsibilities between home and host authorities, favouring the implementation an entity-based framework at the level of the home country. Therefore, notwithstanding the framework applicable to subsidiaries that would be regulated legal entities in the host countries concerned, the IMF recommends that the home country jurisdiction be responsible for applying the global framework on a consolidated basis (a framework that has yet to be defined and that should cover the various risks at global level, potentially with an authorisation mechanism specific to big techs). The home authority would be responsible for coordination with all sectoral, domestic and foreign authorities. The host authorities would rely on the home authority, and focus an activity-based approach to the regulation on competition, consumer protection and data protection.

In both cases, however, it is acknowledged that, if the home authorities do not take the necessary measures, it would be appropriate for the host authorities to implement national or regional approaches to regulate the growth of big techs at their level if need be.

3.2. The regulatory gaps in the current framework

3.2.1. The initial responses of the European Union and their limitations

The European regulator has been able to react quickly to the new risks associated with increasing digitalisation. Among other things, the European Union has enhanced its regulatory framework to strengthen the operational resilience requirements for financial players (DORA), ensure competition conditions that are beneficial to consumers (DSA and DMA) and to regulate the provision of crypto-asset services (MiCA).

Box 3: The main European initiatives in digital finance

DORA - Digital Operational Resilience Act: this regulation, that aims to harmonise and strengthen the requirements that apply to financial players in terms of digital operational resilience, is based on four pillars. The first one aims at strengthening the governance and risk management requirements in relation to information and communication technology (ICT). The second pillar covers the reporting of major incidents by financial entities to the supervisor, while the third one concerns the implementation of an operational resilience testing program by all financial entities, and more advanced penetration testing for the entities considered the most systemically significant. Lastly, DORA creates a regime for the direct supervision by the European authorities of specific to the providers of so-called critical IT services.

MICA - Markets in Crypto-Assets Regulation: inspired in part by the French example (PACTE Law), the MiCA Regulation will provide a framework for crypto-asset issuers and crypto-asset service providers, who will be required to obtain authorisation and will have to comply with an adequate prudential

regime. The aim of this regulation is to better protect users and to ensure the stability of the financial system.

DSA - Digital Services Act - and DMA - Digital Markets Act: These two regulations aim to provide the European Union with a new liability framework applicable to the major digital platforms. The DMA addresses this issue from a perspective primarily focused on competition, ensuring that digital markets remain innovative and open to competition, and that commercial relationships between the major players (the “gatekeepers”) and their business partners remain balanced and fair. The DSA focuses on protecting consumers using digital services from illegal content, covering advertising rules and online misinformation.

However, while these various regulatory responses provide an initial way to address the operational resilience issues associated with the provision of ICT services, with the implementation of DORA and the introduction of supervision applied to critical service providers, they do not cover all the financial stability issues. In particular, they overlook certain risks posed by the potential for big techs to develop as intermediaries and distributors of services, including using new “white label” models and through non-bank lending offerings. Neither do they provide a consolidated picture of the impact of these groups on the European financial sector.

With the exception of DORA, which provides supervisors with a “direct hook” on ICT services, the existing tools only capture big tech activity indirectly, by imposing additional requirements, under Pillar 2 or with macroprudential instruments, on financial institutions the business of which would excessively rely on one or more big techs. However, in a scenario in which the role of big techs becomes critical and unavoidable for financial institutions, these tools could prove insufficient to meet financial stability challenges. On the one hand, these tools apply only to regulated institutions and not to other private investors; on the other hand, whether they are micro- or macroprudential in nature, these tools could prove particularly difficult to calibrate in the absence of a consolidated view for supervisors of the activity of big tech groups and of their financial circuits. The European supervisory authorities also share the view that there may be shortcomings in the current framework, and have called for more specific measures to be taken to better understand the risks associated with the financial activities that may be developed in big techs³⁷.

3.2.2. The regulatory gaps in the current framework for the supervision of mixed-activity groups

In addition to the aforementioned regulatory gaps, which limit the ability to supervise distribution activities (absence of a regime aiming at aligning interests and share risks, see Section 2.1.2) and non-bank lending activities (no existing harmonised regime covering “non-bank lending” activities at European level, see Section 2.1.3), European financial regulation also presents another major shortcoming in addressing the potential emergence of big techs: it does not provide, in all

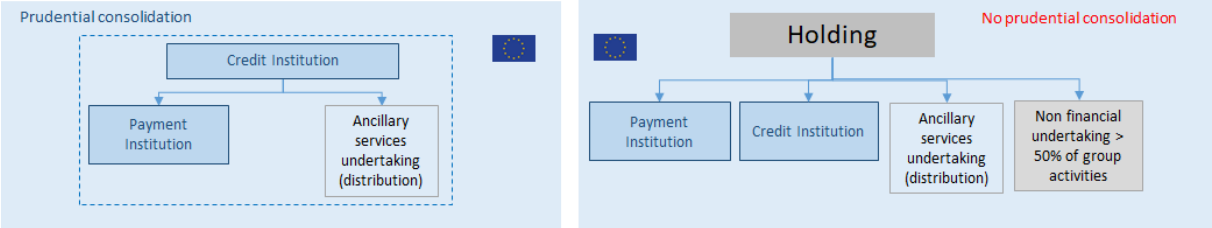
³⁷ See, in particular, the EBA or ESAs’ answers to the Commission’s call for advice on digital finance ([Report on response to the non-bank lending request from the CfA on Digital Finance and Joint European Supervisory Authority response to the European Commission’s Call for Advice on digital finance and related issues](#))

circumstances, a consolidated view of the financial activities conducted by groups the activities of which are mostly non-financial (the “mixed-activity groups”).

Some sector-specific regulations do not impose requirements on a consolidated basis. This is true, for instance, for payment services governed by the Payment Services Directive (PSD)³⁸, and for digital asset services covered by the MiCA Regulation.

In the case of banking and investment services, while the regulations provide for a framework for consolidation, the latter does have a number of shortcomings as regards mixed-activity groups. As the regulations currently stand, **applying prudential consolidation at the level of a holding company presupposes that the latter qualifies as a financial holding company (FHC) or as an investment holding company (IHC)**. This qualification is based on two conditions: i) at least one subsidiary of the holding company must be authorised as a credit institution (for FHCs) or as an investment firm (for IHCs), and ii) most of the subsidiaries are engaged in financial activities. This makes it easy for a group predominantly non-financial to organise its financial activities in such a way as to avoid consolidated supervision (see Figure 1, right-hand panel). In addition to preventing effective risk supervision, this situation also result in unfair treatment compared with banking groups or investment firms, and constitutes a breach of the “*same business, same risk, same rule*” principle.

Figure 2: the regulatory gaps in the existing prudential consolidation rules



These potential cases of structural arbitrage are further facilitated by difficulties in defining the scope of activities that should be considered as “financial” or “ancillary”, and as such included in the scope of consolidated supervision, in the absence of complete and comprehensive definitions in the Capital Requirements Regulation. These impediments are exacerbated in an environment in constant innovation in which the “unbundling” of financial services has become a hallmark.

This is not a new issue for mixed-activity groups. Industrial groups, such as car manufacturers, have developed offerings for lending and savings products by setting up banking subsidiaries. However, the features of these groups, which rely on a fairly limited range of financial services and having limited links with other financial institutions, while lacking competitive advantages over traditional players, did not warrant changes to the regulatory framework. Conversely, as explained above, big techs are already key players for financial institutions for certain technical services, and they raise systemic concerns, while their growth potential in financial services remains mostly untapped. **It would therefore be appropriate to consider the regulatory responses that could address these blind spots.**

³⁸ (EU) Payment Services Directive 2015/2366. The proposed revision of the Payment Services Directive published by the Commission on 28 June 2023 does not provide for the introduction of consolidated supervision.

4. Enhancing big techs financial activities supervision and risks coverage: few proposals for regulatory responses

It appears necessary to strengthen the regulatory framework in order to ensure that the growth of big techs in the financial sector can proceed in a controlled manner, without excessive risks for financial stability and with a level of requirements comparable to that applied to traditional players, provided that the financial activities conducted and considered in their entirety, are similar. This could be achieved by conducting consolidated supervision for the financial or ancillary activities of these groups, which could be structured around the following proposals:

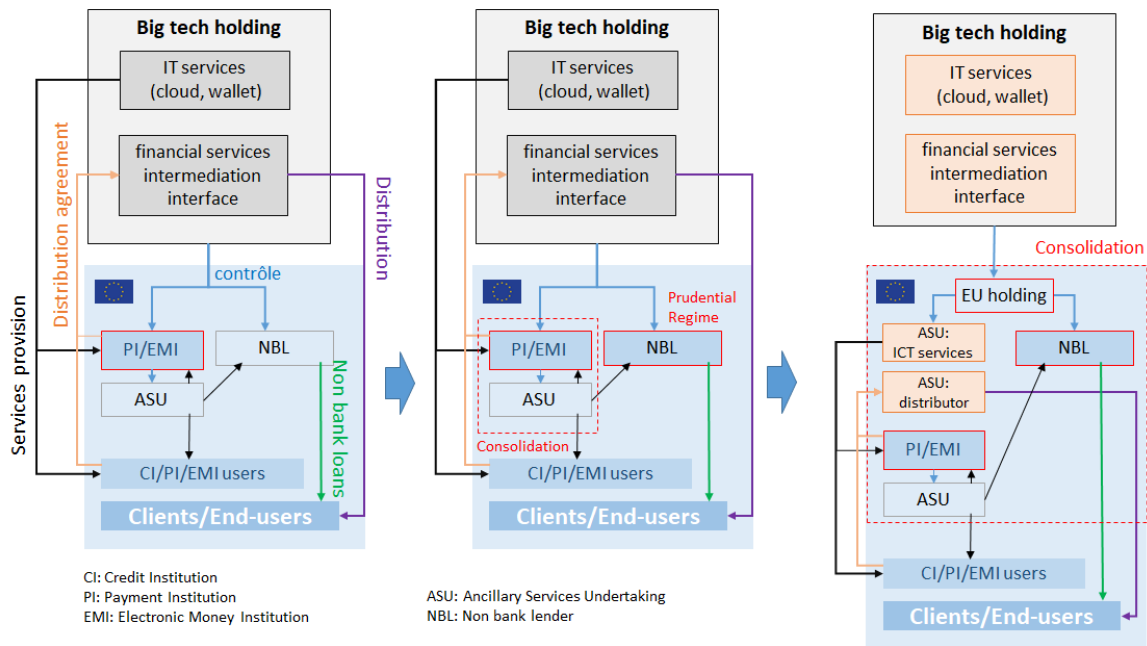
1. The strengthening or introduction, at European level, of a harmonised prudential framework and of consolidated requirements for payment services and electronic money services and for non-bank lending on which the big techs are more specifically focused;
2. The introduction of a new framework for mixed-activity groups comprising two components:
 - a. Adopting further measures to ensure that financial and ancillary activities are grouped together within a single holding company, so as to avoid regulatory arbitrage concerning the legal structure of these groups; and
 - b. In order to prevent scenarios in which big techs would continue to develop their financial activities while at the same time circumventing regulatory requirements, introducing the ability to impose, where the combined financial activities of the group in the EU pose risks that are similar in nature to those associated with the activities of a credit institution, that banking rules apply to the whole financial subgroup, even in the absence of a credit institution within that group³⁹. In addition, and to prevent the risks associated with a model based exclusively on distribution and on the provision of the associated support services, it would appear necessary to be able to require that big techs, in combination with applying banking rules, also share part of the risks associated with the “originated” volumes.

Table 1: overview of the risks associated with the activities conducted by big techs, summary of the limitations of the existing framework and regulatory proposals

³⁹ It should also be possible to impose for groups to apply the banking framework when the group's activities are assessed as presenting a risk to financial stability, and where the requirements applicable to the group's regulated entities in isolation are considered insufficient to mitigate this risk, especially if the measures recommended in proposal 1 are not implemented.

| Activities carried out by big techs | Risks and potential issues | Existing regulatory framework | Key proposals in case of growth to a systemic level |
|------------------------------------------------------------------------------------------------------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| ICT services (cloud, digital wallet) | Resilience of the financial system in the event of a service disruption or failure of a service provider, due to high concentration on a small number of players and low substitutability. | In addition to the requirements imposed on institutions to monitor outsourced services, DORA has introduced supervision for critical IT service providers to ensure their cooperation. | Topic covered by the DORA regulation |
| Origination / distribution in combination with the provision of services (risk management, customer scoring, AML/CTF supervision, etc.), | <p>Situations of dependency are likely to generate moral hazard for financial institutions, as well as a loss of control over flows and the conditions under which services are provided, with ensuing reputational risks, and therefore “step-in” risk in the event of the distributor’s failure. Liquidity risk in the event of overreliance on financing by a specific partner.</p> <p>Concerning the provision of services, there is also a risk of loss of expertise, concentration risk in relation to risk models, and banking exclusion risks.</p> | <p>Institutions are theoretically required to adequately manage their risks in relation to all the services they provide. The supervisor may impose a capital add-on or other Pillar 2 measures (e.g. requiring the termination of contractual relationships), or even use macroprudential instruments on institutions the business of which relies excessively on the services and products distributed by big techs.</p> <p>For the provision of services, institutions remain accountable for all their outsourced activities. In the event of difficulties or shortcomings, the supervisor may impose additional requirements on institutions in relation to outsourced services (e.g. refining recovery plans, amending contractual terms) or terminate the relationship where the aforementioned measures prove ineffective. Certain aspects of these services could fall within the scope of DORA (according to the definition of IT services) and thus allow for cooperation requirements to be imposed on service providers on these matters.</p> | Risk participation and application of NBL rules or banking rules to ensure that loss-absorbing capacity is sufficient to cover the risks retained at originator level and mitigate contagion risks (proposal 2.b) |
| Non-bank lending | Given the lack of a harmonised EU framework, potential regulatory arbitrage, insufficient loss-absorbing capacity, risk of contagion to financial partners and investors. | National requirements apply on an individual basis. Strengthening requirements for financial institutions for exposures to unregulated entities or more specifically on big techs under Pillar II. | Strengthening the PSD and NBL framework through the introduction of a consolidated regime (proposal 1) |
| Various financial activities carried out across several legal structures | Regulatory arbitrage and lack of a consolidated view of activities and associated risks. | Where a credit institution is involved, possibility to use the power to require the consolidation of financial institutions managed on a unified basis (complex to implement). | Consolidation of financial and ancillary activities under a European holding company (proposal 2.a) |

Figure 3: illustration of the proposals and their impact on the supervisory / consolidation scope:



| Current UE framework | Proposal 1 | Proposal 2(a) et 2(b) |
|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <p>Only the PI/EMI is subject to harmonised EU prudential, governance and risk management requirements on an individual basis. ICT services to EU financial institutions and distribution are carried out from abroad</p> | <p>With the strengthening of payment and credit regulation, the PI/EMI shall comply with its requirements on the basis of its consolidated situation (new prudential consolidated scope at the level of the PI/EMI). The NBL undertaking is subject prudential, governance, and risk management requirements.</p> | <p>With the grouping of financial and ancillary activities under an EU holding, a comprehensive consolidated supervision, including prudential requirements, governance and risk management aspects is implemented covering all financial activities in the EU (2(a))</p> <p>If (1) the combined activities and risks of the sub-group are equivalent to those of a credit institution or (2) a material risk for financial stability is identified as insufficiently covered by individual requirements, the authority would be empowered to impose the CRR framework on a sub consolidated basis at the level of "EU holding" (2(b))</p> |

This modular and gradual approach would offer a more comprehensive, proportionate, fair and harmonised supervisory framework, in line with the "same business, same risk, same rule" principle. It would contribute to enhancing the consolidation and autonomy of the European Union by allowing for the activities of these groups, which are often established in third countries, to be supervised on a single, consolidated basis.

These various “modules” are complementary and can be implemented in a sequenced manner. This way, it would be possible to make headway first on the elements pertaining to the consolidation of the financial activities of mixed-activity groups, should advances in relation to other aspects prove more challenging due to harmonisation issues.

4.1. Better regulation of payment services and the provision of lending by non-bank entities

4.1.1. Implementing a consolidated regime for payment institutions and electronic money institutions

Contrary to the framework applicable to credit institutions⁴⁰, European regulations do not provide for consolidated supervision when it comes to groups of payment institutions or electronic money institutions. **This situation prevents supervisory authorities from building up a comprehensive view of the risks borne by these groups and from ensuring their coverage**, preventing especially from factoring in ancillary activities performed by subsidiaries or “sister” companies, such as the management of IT services and support services required for the execution of transactions or non-banking lending activities.

In order to address this shortcoming, a requirement for consolidated supervision could be introduced in the Payment Services Directive (PSD), which is currently being revised, where a financial group, which would not already be supervised under the CRR, comprises at least one payment or electronic money institution. Such supervision could rely on the introduction of the concept of payment holding company, in the same vein as financial holding companies.

With a view to avoiding hindering the growth potential of fintechs toward banking services, the corollary of this new consolidated supervision may be to not immediately trigger the application of CRR on a consolidated basis at the level of the parent undertaking of a payment institution or at the level of the payment institution where the creation of an affiliated credit institution is planned, and as long as the credit institution’s activity remains marginal and at low levels compared to the payment activities. This is because the parent undertaking of a group the activities of which are predominantly financial is required to comply with CRR on the basis of its consolidated situation whenever that group includes a credit institution. Without prejudice to the fulfilment of CRR requirements at the level of the credit institution subsidiary, triggering the application of CRR at the level of the payment institution or at that of the “parent” holding company can therefore lead to a very significant increase in own fund requirements on a consolidated basis, without the activity (mainly the payment activity), having actually developed, which would be disproportionate given the risk profile of the group.

⁴⁰ Article 18 of CRR lays down the requirement for credit institutions to consolidate their subsidiaries that are ancillary services undertakings, the latter being defined as ‘*undertakings the principal activity of which consists of owning or managing property, managing data-processing services, or a similar activity which is ancillary to the principal activity of one or more institutions*’ (Article 4(1)(18) of CRR).

Table 2: illustration of the impact of moving away from PSD requirements towards CRR requirements following the establishment of a credit institution

| | Before the credit institution is established | After the credit institution is established |
|--------------------------------------------------------|----------------------------------------------|---------------------------------------------|
| Assets of the payment institutions (separate accounts) | 5, 000 | 5, 000 |
| Assets of the credit institutions (outstanding loans) | | 100 |
| Group PSD requirements | 10 | 18 |
| <i>Group PSD requirements (transaction volumes)</i> | 10 | 10 |
| <i>Group PSD requirements (outstanding loans)</i> | | 8 |
| Group CRR requirements | | 153 |
| <i>CRR leverage requirements</i> | | 153 |
| <i>CRR solvency requirements</i> | | 88 |

Beyond consolidation-related aspects, **other ways to strengthen the PSD framework could also be warranted in a context of big techs growth**. This additional tightening of the framework could include additional capital requirements (“Pillar II”) and the introduction of liquidity requirements for payment institutions and electronic money institutions, as well as the regulation of X-Pay type technical services (e.g. Apple Pay, Google Pay) and of the provision of services under a white label, including by requiring greater transparency and measures to ensure the protection of customer funds. Technical services such as X-Pay could also be included in the scope of the security requirements set out in the regulatory framework applicable to payment services (PSD2 and PSD3/PSR).

4.1.2. Adopting a harmonised prudential regime for the lending activities offered by non-bank players

Digitalisation and the widespread use of online payment have led to the development of Buy Now Pay Later (BNPL) payment options and the emergence of new players specialising in these services, as well as in other types of credit agreements (especially factoring and leasing). Due to the fact that they do not collect deposits, these entities do not meet the definition of a credit institution as laid down by the CRR. However, the framework applicable to non-bank lenders (NBLs) is not harmonised across the EU, it is governed by the national legislation of each Member State. In this context, regulatory and supervisory requirement levels may vary substantially from one country to another⁴¹. This situation does not allow for an adequate monitoring of the development of these activities at the level of the EU, and it offers opportunities for regulatory arbitrage, especially against a highly digitised background in which preventing the provision of services on a cross-border basis is more complicated.

As a result, big techs can expand their activities, especially towards low regulated products or niches, depending on the national framework specific to each country, sometimes without any associated prudential constraints, albeit with a potentially significant risk to financial stability (see Section 2.1.2).

France has introduced a scope of supervision applicable to players in the banking sector, understood in a broad sense, in order to safeguard financial stability and protect economic players from risks on

⁴¹ These discrepancies are the topic of an in-depth analysis carried out by the EBA, see Section 5.3 of the [Final Report on response to the non-bank lending request from the CfA on digital finance](#)

an individual basis. For instance, beyond credit institutions, this scope also includes “financing companies”, as a way to ensure the resilience of entities engaged in credit granting but which do not collect deposits. The prudential regime applied to these companies is similar to that applied to credit institutions, it includes own funds and liquidity requirements combined with reporting requirements and consolidation rules. The regime has proved very successful, with more than a hundred financing companies operating and a wide variety of players specialising in factoring, leasing, consumer credit and suretyship, providing the ACPR with a comprehensive picture of credit activities in France. Other European countries have made similar choices (see Section 5.3 of the [Final Report on response to the non-bank lending request from the CfA on digital finance](#)).

Inspired by the French model, the creation of a European prudential regime framing the granting of loans by non-bank entities, at least when the activity becomes material and/or expands in several Member States, could contribute to better address the risks posed by the lending activities of big techs. The introduction of this regime would also make it possible to tighten the legal framework governing third-country entities’ access to the European banking market, as was done under CRD VI for deposit-taking activities, although, contrary to the Commission’s initial wishes, it could not be extended to credit activities in general at the time⁴². The counterpart of this harmonisation at European level would be the ability for these non-bank lending players to take advantage of the **EU passport and therefore benefit from European market integration**. This NBL framework could, as suggested for payment institution groups, include consolidation rules, combined with the same derogation mechanism from the CRR framework in cases where the relative weight of credit institutions is marginal and the weight of NBL entities predominates.

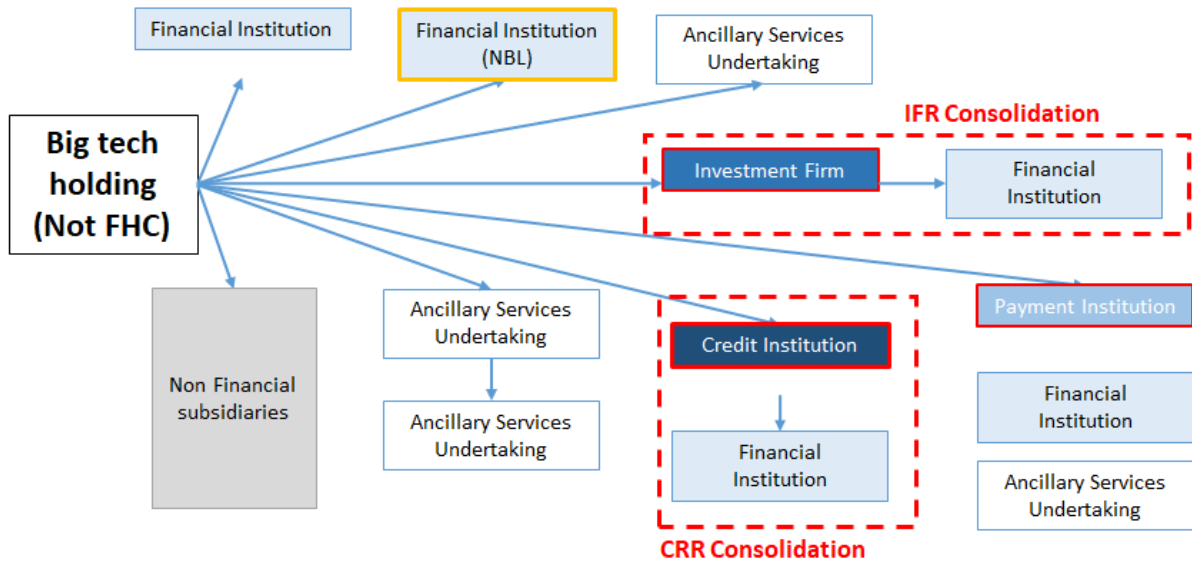
4.2. Revising the supervisory framework applicable to mixed-activity groups

4.2.1. Consolidating the financial activities of mixed-activity groups

The complex structure of major technology conglomerates and, more generally, that of large mixed-activity groups, combined with the predominance of non-financial activities may, as was made clear in the case of the Wirecard group and as detailed in Section 3.2.2, hinder consolidated supervision under the current rules. These players can adjust their organisational structure in such a way as to avoid for requirements to apply on a consolidated basis, even in cases where the group comprises a subsidiary that operates under the credit institution status (see Figure 4).

⁴² Concerning credit, the requirement to establish a branch, as laid down in Article 21c of CRD6, applies only to third-country entities that would qualify as credit institutions (Article 47(1)(a) CRD6), with each Member State retaining the ability to open its national market to non-bank entities that are not established locally.

Figure 4: illustration of the regulatory gaps in the current consolidation framework

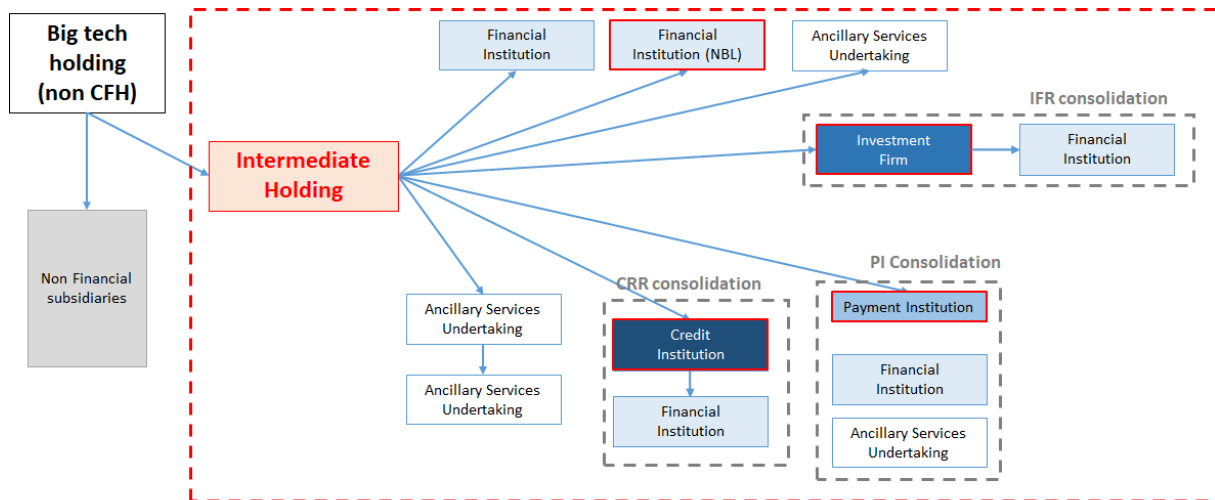


Under the current applicable regulation, in a situation where the holding of the group do not qualify as a financial holding company (FHC) as it is located outside the EU or it predominantly carries out non financial activities, **only two fragmented sub-groups are supervised separately, and several financial institutions are not at all part of such supervised scopes. The Payment Institution and, depending on applicable national law, the Non Bank Lending undertaking are supervised on an individual basis.**

Another limitation lies in the fact that undertakings providing ancillary services are not factored in when calculating the thresholds for qualification as a financial holding company. This potential for arbitrage should however be resolved in the context of the revision of the CRR, by including these entities in the definition of financial institution.

In order to close these arbitrage channels, it appears advisable to strengthen consolidation requirements in order to be able to **require groups that carry out significant financial activities in the EU to aggregate all such activities, including ancillary services (distribution, back-office, etc.), within an intermediate holding company** (see Figure 5).

Figure 5: illustration of the proposal to aggregate all the financial activities of big techs within an intermediate holding company



Following the introduction of a consolidation regime for mixed-activity groups, grouping of all financial undertakings under a dedicated structure and application of an appropriate prudential regime to this sub group on a consolidated basis.

Depending on the nature of the institutions to be included in this structure and on their relative importance, and subject to the adoption of the recommended strengthening of the framework applicable to payment institutions, electronic money institutions and non-bank lending institutions, the aggregation of all financial activities would automatically trigger consolidated prudential supervision at the level of the intermediate holding company, in line with, as appropriate:

1. The CRR, where a credit institution exists and provided that the other subsidiaries (investment firms, payment institutions, electronic money institutions or non-bank lending institutions) would not be deemed to conduct predominant activities; or
2. Where there is no credit institution or where a small credit institution exists, pursuant to the Investment Firms Regulation or the new Payment Services Directive or Non-Bank-Lending framework depending on the respective importance of each of the activities sectors involved.

The establishment of this type of holding company would enable supervisors to gain a better understanding of the activities conducted by each group, of their interconnectedness with non-financial activities and, in turn, of their systemic nature, without impacting the exercise of supervisory tasks concerning the entities on an individual basis. This solution would **only require a limited revision of the consolidation rules**. It also appears well **suited to the principle of proportionality**, as it was implemented in the sector-specific regulation applicable to investment firms, which lays down rules that are differentiated and graduated according to the activities and size of the undertaking considered. Additional adjustments could be considered as regards proportionality. For example, in light of supervision as provided under the DORA Regulation, IT services (especially cloud-type services) might not be taken into account in cases where authorities are satisfied with the level of cooperation and resilience of entities.

One of the challenges of this approach lies in the ability to assess the materiality of a group's activities, as such an assessment would require the implementation of minimum reporting requirements covering all financial and ancillary services targeting European customers or users, end-customers or

end-users or financial and partner users (including for instance intermediated volumes, operations for which the group is involved at the processing stage - e.g. X-Pay wallets, issuance of crypto-assets, etc.), regardless of these activities and services being carried out by regulated or unregulated entities, and whether these entities are EU entities or not. The definition of such a materiality threshold in relation to a given geographical market could be based on revenue, on risks, on outstanding financial assets and on volumes on which the group is involved in a fragmented manner. It would also be advisable to provide for supervisor judgement. It should be possible for this assessment to be carried out at European level, through coordination between the national authorities concerned and the European Banking Authority.

To ensure that all risks and interdependencies are appropriately taken into account, especially concerning the group's non-financial activities, strengthened governance, internal control and risk management requirements may also be appropriate.

4.2.2. Implementing banking rules

In an environment characterised by constant innovation, it would be advisable empowering supervisors to require that banking prudential rules apply across a financial sub-group where the combined financial activities of the group pose similar risks to those incurred by credit institution⁴³ activities or where a risk to financial stability is identified that is not sufficiently covered by the individual requirements that apply. The use of this power would notably be necessary where the consolidation of activities as set out in Section 4.2.1. would not result for the intermediate holding company to be qualified as a financial holding company due to the lack of a credit institution within the group.

These intermediate holding companies would therefore be required to comply with the entire prudential regime applicable in the banking sector, which are based on the standards developed by the Basel Committee and shared at international level, in all its components (governance and internal control, quantitative requirements, Pillar 3 disclosure requirements, additional Pillar 2 requirements, as well as the components concerning risks self-assessment and risks review by the supervisor in a structured process, with gradual and proportionate supervisory powers).

Some of the quantitative own funds and liquidity requirements may not seem well-suited to big techs, as these groups typically do not include subsidiaries authorised as credit institutions and usually enjoy very healthy capital and liquidity levels. However, **applying consolidated supervision based on banking rules at the level of the financial subgroup would have the added benefit of providing a common, robust reference framework within the supervisory community, and it would equip supervisors with graduated and proportionate means of action⁴⁴ should these groups pose risks to financial stability.**

Furthermore, this approach would also make it possible to better regulate the financial activities of big techs and to facilitate extensive cross-border coordination in the future through the use of a common language, particularly in the event that the non-European jurisdictions hosting these companies also decide to strengthen their own regulatory frameworks in the future. Setting up dedicated colleges could also be a stepping stone towards more integrated supervision for these groups, along with the establishment of complementary international colleges, building on the experiences acquired in the context of the international supervision of systemically important banks.

⁴³ For example, if the group includes entities that are stablecoin issuers or entities that conduct non-bank lending activities.

⁴⁴ Especially thanks to the range of additional "Pillar 2" measures.

Conclusion

In view of the fact that the risks associated with the concentration of players providing specific ICT services are addressed by the recent EU regulatory initiatives, the risks posed to financial stability by other initiatives from big tech players appear limited in the short term. However, given the nature of these players and the fast pace at which they are likely to develop in the financial services market, it appears necessary to put in place a regulatory and supervisory framework suited to this new configuration, and, where appropriate, to give the EU in a pioneering role at international level.

The introduction of a European legal instrument allowing supervisors to impose that financial activities be consolidated and appropriate consolidated requirements be applied would have the benefit of taking into account the rapid growth of these players. This tool, which may or may not be activated, depending on the direction taken by big techs, would also make it possible to force these players to be more transparent about their financial activities and their development strategy. Ultimately, such a framework could be instrumental in paving the way for a direct and mutually beneficial dialogue between players and regulators on planned financial services projects, as well as on the level of requirements and structuring expected by European authorities, which could then be better anticipated by players.

The recommended approach, designed to be proportionate and flexible, aims to provide an initial response to these various challenges, contributing to improvements in the resilience of the financial sector without stifling innovation. It seeks to strike a fair balance between the need to safeguard competitiveness, innovation and growth, while addressing the new risks and challenges posed by these players in terms of financial stability and, by extension, of sovereignty.