

**Ref:** EIOPA public consultation on ‘Discussion paper on (re)insurance value chain and new business models arising from digitalisation’.

**Link to consultation:**

[https://ec.europa.eu/eusurvey/runner/EIOPA\\_fragmentation\\_new\\_businessmodels](https://ec.europa.eu/eusurvey/runner/EIOPA_fragmentation_new_businessmodels)

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## **BETTER FINANCE Response to the consultation on (re)insurance value chain and new business models arising from digitalisation**

### ***Executive Summary***

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#### ***Increased fragmentation of the value chain***

The InsurTech wave of innovation introduces and transforms existing business models. The extensive use of third-party providers and outsourcing may lead to both as well as a possible fragmentation of the insurance value chain. Nonetheless, several incumbent insurance-related companies, more or less have become software companies. The degree of this transformation is marked by the level of adoption of technological solutions in their core business processes.

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#### ***Regulatory framework***

We believe that there is the need to extend the regulatory arm to this new business ecosystem. In this respect, scholars<sup>1</sup> noted that “regulation and uniformisation of practices are the best way to protect the economic and financial order, in addition to opening new choices to the market”. Regulation is needed in order to offer investor protection, preserve the benefits of the emerging instrument and its underlying market, remove legal uncertainty, and create the necessary resolution mechanisms in case of a crisis. Deployment of ICT may require rethinking of oversight framework both at EU and national level.

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#### ***Supervision***

One of the main challenges the Authorities are facing is the lack of a complete understanding of AI, ADM and algorithm mechanisms. Due to the use of extremely complex algorithm and automated decision making, most of the time it is impossible to review and challenge the automated decision. This is also true for consumers that do not receive sufficient explanations of the results that the automated decision has provided them thus preventing them to challenge this decision. This increasing complexity reduces the transparency of these technologies preventing an adequate supervision from the authorities.

It is necessary for authorities to have a sound understanding of the technologies and their potential application in the financial sector in order to regulate and supervise effectively. Authorities such as ESAs and ESMA should develop appropriate internal understanding of the use of these technologies in financial services regarding risks and opportunities.

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<sup>1</sup> [https://www.uncitral.org/pdf/english/congress/Papers\\_for\\_Congress/29-DOLES\\_SILVA-Cryptocurrencies\\_and\\_International\\_Regulation.pdf](https://www.uncitral.org/pdf/english/congress/Papers_for_Congress/29-DOLES_SILVA-Cryptocurrencies_and_International_Regulation.pdf)

## About BETTER FINANCE

*BETTER FINANCE, the European Federation of Investors and Financial Services Users, is the public interest non-governmental organisation advocating and defending the interests of European citizens as financial services users at the European level to lawmakers and the public in order to promote research, information and training on investments, savings and personal finances. It is the one and only European-level organisation solely dedicated to the representation of individual investors, savers and other financial services users.*

*BETTER FINANCE acts as an independent financial expertise and advocacy centre to the direct benefit of European financial services users. Since the BETTER FINANCE constituency includes individual and small shareholders, fund and retail investors, savers, pension fund participants, life insurance policy holders, borrowers, and other stakeholders who are independent from the financial industry, it has the best interests of all European citizens at heart. As such its activities are supported by the European Union since 2012.*

**Instructions on how to read this paper:** this document contains the response of BETTER FINANCE to the European Commission's online survey (public consultation) concerning the **consultation on (re)insurance value chain and new business models arising from digitalization** but this is not the actual response form submitted.<sup>2</sup> For each section summaries and explanations (*in italic*) are reported exactly as in the EC consultation document.<sup>3</sup>

## Introduction

*European Insurance and Occupational Pension Authority (EIOPA) is launching a public consultation on ['Discussion paper on \(re\)insurance value chain and new business models arising from digitalisation'](#).*<sup>4</sup>

*Technology continues to evolve, bringing new opportunities, social change and new expectations for consumers. In response, insurance undertakings and intermediaries continue to develop and revise their business models, often in increased co-operation with third parties (e.g. BigTech companies and start-ups), bringing both beneficial innovation and a new set of emerging risks that have to be taken into account.*<sup>5</sup>

*These changes in firms' reliance on outsourcing and third parties bring potential benefits and opportunities. They are expected to transform the way products and services are provided with benefits for consumers (in terms of products and services that are better targeted to consumers' needs, of a better quality or that are more cost-effective) and insurance undertakings (for instance in terms of more efficient processes and decision-making or better fraud detection and management of risks).*<sup>6</sup>

*However, it may also create new conduct and prudential risks and amplify or relocate significantly old risks (e.g. operational risk, Information and Communication Technology (ICT) risks, security, governance, and reputational risks, consumer protection). It can also lead to legal and compliance issues (e.g. data protection and compliance with outsourcing rules and regulatory perimeter issues). The widespread use of third party providers can also lead to concentration risk if a large number of undertakings become dependent on a small number of dominant outsourced or third*

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<sup>3</sup> [https://www.eiopa.europa.eu/content/eiopa-consults-reinsurance-value-chain-and-new-business-models-arising-digitalisation\\_en](https://www.eiopa.europa.eu/content/eiopa-consults-reinsurance-value-chain-and-new-business-models-arising-digitalisation_en)

<sup>4</sup> [https://ec.europa.eu/eusurvey/runner/EIOPA\\_fragmentation\\_new\\_businessmodels](https://ec.europa.eu/eusurvey/runner/EIOPA_fragmentation_new_businessmodels)

<sup>5</sup> Ibid.

<sup>6</sup> Ibid.

party service providers.<sup>7</sup>

*In this context, a possible fragmentation of the insurance value chain could occur, including, most pertinently, a potential for a reduced regulatory and supervisory 'grip' on the relevant activities in the value chain, or ways in which the 'lengthening' of the value chain 'stresses' existing regulatory and supervisory oversight.<sup>8</sup>*

## **Chapter 1. Introduction and Chapter 2. Increased fragmentation of the value chain**

### ***1. Do you have any preliminary remark or general comment regarding the topic of (re)insurance value chain and new business models arising from digitalisation?***

The Insurancetech wave of innovation introduces and transforms existing business models. The extensive use of third-party providers and outsourcing may lead to both as well as a possible fragmentation of the insurance value chain. Nonetheless, several incumbent insurance-related companies, more or less have become software companies. The degree of this transformation is marked by the level of adoption of technological solutions in their core business processes.

### ***2. Please describe your own co-operation/collaboration respectively with insurance companies/intermediaries/ InsurTech companies, BigTech companies, platform providers. Please describe risks and benefits you see on this co-operation/collaboration.***

N/A

### ***3. What additional issues do you consider relevant for supervisors to understand increased fragmentation and complexity of the market as well as new business models?***

Supervisors should change their vantage point from traditional one to one compliant with the way software companies work. This will allow better understanding of value creation and distribution as well as better mapping of critical points.

One of the main challenges the Authorities are facing is the understanding of AI, ADM and algorithm mechanisms. Due to the use of extremely complex algorithm and automated decision making, most of the time is it impossible to review and challenge the automated decision. This also true for consumers that do not receive sufficient explanations of the results that the automated decision has provided them thus preventing them to challenge this decision. This increasing complexity reduces the transparency of these technologies preventing an adequate supervision from the authorities.

There is as well the question of regulatory perimeter. The recent scandal involving the star of the German fintech industry – Wirecard – constitutes a good example of the risks posed by the alleged failings in the multidisciplinary cooperation between authorities due to, among others, the blurred lines between financial and non-financial sector. Germany's top financial regulator – Bafin - gave a scathing assessment of the failings that led to the scandal at payments processor Wirecard AG and he admitted to errors in control of the fintech company, in particular how his own institution handled allegations of irregularities at the payments provider.<sup>9 10</sup>

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<sup>7</sup> Ibid.

<sup>8</sup> Ibid.

<sup>9</sup> <https://www.bloomberg.com/news/articles/2020-06-22/wirecard-scandal-a-complete-disaster-says-german-regulator>

<sup>10</sup> BETTER FINANCE Response to the consultation on on a new digital finance strategy for Europe / FinTech

**4. In addition to those described in chapter 2 and in Annex 1 of the Discussion Paper, do you see other co-operation/collaboration models (e.g. outsourcing, co-operations, joint ventures) between insurance companies/intermediaries and third parties (e.g. InsurTech companies, BigTech companies, platform providers) to implement and/or enhance the use of innovative technologies that might be worth to look at further from supervisory perspective?**

*Not for the moment.*

**5. In addition to those stated in chapter 3 of the Discussion Paper, are there any other business models that can be seen as related to the fragmentation of the value chain that might be worth to look at further from supervisory perspective?**

One thinkable model could be insurer becoming sort of utility company that has no front end and allows all kind of providers to use the risk bearing capability of the insurance company while pushing forward own products with own labels. Thus, the insurer may become “invisible” to the consumer while facing only the direct product manufacturer.

### **Chapter 3. Case studies**

**6. How do you define insurance platforms and insurance ecosystems? Do you distinguish between those two developments/definitions? If so, how?**

The definition from the discussion paper is sufficient from the moment, though it may evolve later on.

**7. Do you see additional examples of national developments in insurance platforms and ecosystems that are not mentioned in this chapter but which might be relevant from consumer/supervisory perspective? Please explain.**

According to one of BETTER FINANCE member organisation, in the Bulgarian market there are attempts to present purely marketing tools as innovative Insurtech solutions which is a misleading practice.

**8. If you are an insurance company/intermediary, are you planning to build your own platform/ecosystem or to co-operate with other platforms/ecosystems? Please explain.**

**9. Are there any other aspects related to platforms/ecosystems that are not covered in chapter 3 of the Discussion Paper but are important from consumer/market/supervisory perspective?**

Another issue is that a significant part of platforms are domiciled outside the EU and may lever local jurisdiction as per lex loci registrationis against consumer friendly legislation.

**10. In addition to those covered in chapter 3 of the Discussion Paper, what related risks and benefits do you see regarding insurance platforms/ecosystems?**

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action plan <https://betterfinance.eu/wp-content/uploads/BETTER-FINANCE-Response-Digital-Finance-Strategy-Final-for-website.pdf>

Ability to create fast new products and interconnect them with other existing products and services. This is both beneficial and dangerous.

***11. Do you consider that changes in existing regulation or further rules (including soft law/guidance) should be introduced both to facilitate platforms/ecosystems and to adequately cover new emerging risks?***

Yes. Platforms in essence are sophisticated marketplaces and should be addressed that way but also taking into account their tendency to evolve.

We believe that there is the need to extend the regulatory arm to this new business ecosystem. In this respect, scholars<sup>11</sup> noted that “regulation and uniformisation of practices are the best way to protect the economic and financial order, in addition to opening new choices to the market”. Regulation is needed in order to offer investor protection, preserve the benefits of the emerging instrument and its underlying market, remove legal uncertainty, and create the necessary resolution mechanisms in case of a crisis. Deployment of ICT may require rethinking of oversight framework both at EU and national level.<sup>12</sup>

***12. Are there other aspects related to on-demand insurance that should be considered from both consumer, market and supervisory perspective?***

The most important aspects of on-demand insurance is its connection with consumer behaviour thus raising privacy concerns.

Non-discriminatory access to data and interoperability. Digitalization is characterized by business models that use data aggregation and analytics, thus becoming the core of innovation. The huge amount of data generated by consumers is a key for these business models to develop products and services. However, the concentration of data in few big market players could be in violation of EU data protection, privacy, consumer law restraining innovation and competition that could be useful for citizens. The EU Commission should complete the regulatory framework for a competitive data economy. Data portability should be at the core of this regulatory framework in which individuals and business should have the possibility to access data but also to provide better protection to individuals on the data that they generate and should clearly own. Therefore, non-discriminatory access to data and interoperability among market players should be considered in the legislative framework.<sup>13</sup> The only way to transfer the benefit of using someone’s data on the generator of data is to introduce payment for that data. This will stifle the misuse since users of data will have to internalize the costs of data into the product’s pricing. This will level the market and cure distortions due to size – if you want to use more people’s data it will be costlier for you, not like now when VW or FB pay much smaller amounts per item due to their huge datapools as compared to let say small data aggregator.<sup>14</sup>

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<sup>11</sup> [https://www.uncitral.org/pdf/english/congress/Papers\\_for\\_Congress/29-DOLES\\_SILVA-Cryptocurrencies\\_and\\_International\\_Regulation.pdf](https://www.uncitral.org/pdf/english/congress/Papers_for_Congress/29-DOLES_SILVA-Cryptocurrencies_and_International_Regulation.pdf)

<sup>12</sup> BETTER FINANCE Response to the consultation on on a new digital finance strategy for Europe / FinTech action plan <https://betterfinance.eu/wp-content/uploads/BETTER-FINANCE-Response-Digital-Finance-Strategy-Final-for-website.pdf>

<sup>13</sup> Better finance is a contributor of the Human-Centric Digital Manifesto for Europe, How the digital transformation can serve the public interest ( September 2019): <https://www.beuc.eu/publications/beuc-x-2019-053-a-human-centricdigital-manifesto-for-europe.pdf>

<sup>14</sup> <https://betterfinance.eu/wp-content/uploads/BETTER-FINANCE-Response-Digital-Finance-Strategy-Final-for-website.pdf>

***13. Are there other aspects related to instant/push insurance that should be considered from both consumer, market and supervisory perspective?***

There is the problem of misuse consumer behaviour and cognitive abilities, especially if bundled with third party perks.

***14. Are there other aspects related to preventive services in insurance that should be -- considered from both consumer, market and supervisory perspective?***

***Chapter 4. Risks and benefits for consumers and for the industry***

***15. Do you consider the potential benefits for consumers and for the industry to be accurately described?***

The potential benefits for the industry are greater than those for consumers since the industry is the main driver behind those transformations. The consumer is more a passive user of certain beneficial side-effects. In any case, attention should be paid at market distortions due to technological dominance and where they occur to remedy them through internalization of external costs.

***16. Do you agree with the description of the risks identified for consumers and for the industry?***

To a great extent- yes

***17. Is the regulatory framework adequately addressing the risks mentioned above? Do you think further regulation is needed? Please explain why.***

Further regulation is needed for sure, since the current regulatory architecture stems from the late 20 century and does not reflect well the transformation effect of ICT. This is even more noticeable taken into account the speedy introduction of AI solution modules.

***Chapter 5. Supervisory implications***

***18. What are the greatest future challenges in the fragmentation of the value chain including the emergence of insurance platforms and ecosystems?***

Data access: due the strong presence of network effects in the digital framework, which is strongly data-driven based, consumers business and especially SMEs are locked in in ecosystem that are controlled by few market players. therefore, there is an entry barrier for data access and restricted competition. Besides PSD2 there is no other regulation for opening the systems of incumbents e.g. in insurance.<sup>15</sup>

***19. This Discussion paper refers to some areas for further work meant to mitigate some of the risks and providing supervisors better tools to tackle with the increased fragmentation***

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<sup>15</sup> <https://betterfinance.eu/wp-content/uploads/BETTER-FINANCE-Response-Digital-Finance-Strategy-Final-for-website.pdf>

*(see Executive summary in page 5). Are other measures and tools needed? If so, what are they and what they should cover (e.g. to ensure compliance with conduct and organisational regulatory requirements; data and consumer protection; better supervisory oversight capabilities; better information about new developments).*

***20. What additional tools could support supervisors to understand increased fragmentation and complexity of the markets as well as new business models?***

Supervisors should support the implementation of software development models in order to understand the increased fragmentation and complexity of the markets as well as new business models.

It is necessary for authorities to have a sound understanding of the technologies and their potential application in the financial sector in order to regulate and supervise effectively. Authorities such as ESAs and ESMA should develop appropriate internal understanding of the use of these technologies in financial services regarding risks and opportunities. In addition, the commission should enhance cooperation with ESAs to develop a cyber resilient testing framework for the financial sector.<sup>16</sup> Also, more effective communication and cooperation mechanisms should be put in place. There is a need is for horizontal tech layer that serves all the ESAS in their present composition. Also, some of the managerial techniques from IT companies should be adopted by the ESAs, especially for that parts that deal with Fintech.

***21. Are there any other comments you would like to convey on the topic? In particular, are there other relevant issues that are not covered by this Discussion Paper?***

Introduction of AI :

If on the one hand, the use of algorithm and Artificial Intelligence (AI) and automated decision making (ADM) produce several advantages as increased accuracy, speed and reduced costs, on the other hand the risk associated to these new technologies can create financial and nonfinancial damages to consumers. The use of these technologies in finance without meaningful human control and oversight can trigger significant loss of transparency, accountability and arbitrary discrimination (as in the use of AI and ADM in the insurance). The EU Commission should propose a legislative framework for AI-powered automated decision making (ADM) to ensure that they are fair, transparent and accountable to consumers and they do not harm their fundamental rights.<sup>17</sup>

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<sup>16</sup>[https://ec.europa.eu/info/sites/info/files/business\\_economy\\_euro/banking\\_and\\_finance/documents/191113-report-expert-group-regulatory-obstacles-financial-innovation\\_en.pdf](https://ec.europa.eu/info/sites/info/files/business_economy_euro/banking_and_finance/documents/191113-report-expert-group-regulatory-obstacles-financial-innovation_en.pdf)

<sup>17</sup><https://betterfinance.eu/wp-content/uploads/BETTER-FINANCE-Response-Digital-Finance-Strategy-Final-for-website.pdf>