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THE DEVELOPMENT OF BIG TECH COMPANIES IN FINANCE: OPPORTUNITIES OR THREATS? WHAT RESPONSE FROM THE AUTHORITIES?

Big Tech companies or tech giants like Amazon, Apple, Facebook/Meta, Google, and Microsoft have grown exponentially over the last two decades. Thanks to their massive customer bases and the resulting data collection and analysis, they have invested in the offering of financial services. For the moment their involvement in this area is limited, they seek to complement or diversify their core businesses, notably helping their customers to buy their main products and services using innovative digital payment methods and/or providing them with insurance cover for purchases made via their platforms.
The European banking sector, for its part, is characterized by its universal, relationship-based banking model that dominates the bulk of financial services and remains largely popular with its customers. In France, five French banks are among the thirty largest in the world.

However, this landscape could change! The banking ecosystem may be severely disrupted by Big Tech companies. Their economic model revolves around their multi-sided online digital platforms while they continue to expand in the financial services sector. The proposal for the establishment of the digital euro creates for them even more potential to increase their presence in the future.
Increased competition between Big Tech companies and banks could rapidly develop, generating benefits for consumers but also risks for financial stability. A first step has been taken with payment management. If financial services are no longer provided by regulated banks but by entities and platforms subject to little or no financial regulation and supervision, the associated risks will also shift. Fair competition must be preserved, both in terms of financial activities carried out and the players themselves, in particular by drawing up appropriate and evolving prudential regulations incorporating the multiple facets of these Big Tech companies.

This debate paper[*] is structured as follow. First, it will highlight the recent development of Big Tech companies in finance, which is modest at this stage but with multiple experiments that could become hegemonic in the future. We will then analyze the specific, idiosyncratic, and systemic risks that these Big Tech companies generate through their original approach to finance, followed by the current efforts of the authorities to strengthen regulation, which are both consistent and still incomplete in terms of financial stability. In this context, the long experience of the European Union (EU) with financial conglomerates can serve as a compass for progress. The paper will conclude with recommendations for concrete and rapid action in this essential prudential area, capitalizing on the acquis of the European legislation on conglomerates.

[*] This Debate Paper was prepared by a dedicated working group (annex) composed of representative's institutional members of the AEFR or not participating in a personal capacity, whose aim is to initiate a discussion on the issues at stake regarding the development of financial services by Big Tech companies. The views expressed in this paper do not necessarily reflect those of the individual members of the working group.

1 Big Tech companies are making progress in finance

1.1 Big Tech companies' presence in finance is expanding

Present for years, Big Tech companies have the capacity to improve the overall attractiveness of their ecosystems through further expansion in financial services sectors of retail banking, in particular payments, savings collection, consumer credit and insurance.

This was confirmed in 2023, when these companies continued to expand.

Funds: In the US, Apple is promoting an Apple Cash card, issued, and supplied by Goldman Sachs, which serves as an electronic cash reserve, facilitates transfers via Apple's iMessage system and, above all, has offered its holders a high-yield fund since April 2023.

Consumer credit: In March 2023, following the Buy Now Pay Later (BNPL) model, that banks and Fintech companies have been offering in Europe for the past two to three years, Apple launched its Apple Pay Later offering in the US, providing direct loans via a program known as Mastercard Instalments. This enables consumers to split their purchases into several payments and repay the loans in their Apple wallet.
Amazon partnered in the US and UK with Bank of America and Marcus (Goldman Sachs) and who act as a broker through which merchants affiliated to the Amazon platform can access loans. In June 2023, it also added a BNPL-type option.

Insurance: Amazon is offering insurance products provided by the London General Insurance Company on its e-commerce site. In late 2022, the company announced the launch of the Amazon Insurance Store, offering consumers a way to find home insurance products from three partner insurers.

Payment: In April 2023, Meta announced that WhatsApp was launching a commercial payments service in Brazil, allowing businesses to sell goods to their customers.

Other: Microsoft entered a ten-years strategic partnership for data, analytics, and cloud infrastructure solutions with the London Stock Exchange Group (LSEG). Microsoft has also acquired an estimated 4% stake in LSEG and sits on its board (Financial Conduct Authority, 2023).

Let's also not forget Elon Musk (former boss of PayPal) who with his company X (ex-Twitter) has just obtained payment licenses in seven US states. "*Its model is the all-purpose (Chinese) application WeChat (...). X would become a universal Swiss army knife, i.e. a mega-platform on which users from all over the world could discuss, obtain information, make a doctor's appointment but also get a loan (...). To start, the platform could give money to its users (10 dollars for example), up to them to send them wherever they want in the system. It would then launch a high-yield savings account*" (Kerdellant, 2024)

Big Tech companies do not share a unique business model or strategy. This heterogeneity is reflected in the variety of ways they enter and expand in financial services, depending on the ecosystem of their original products and services. However, Big Tech companies share certain common characteristics that give them significant competitive advantages:

- They have colossal financial resources. They are far more powerful than the world's largest financial institutions. For example, Apple has a market capitalization of around €3 000 billion, compared to around €100 billion for BNP Paribas, Europe's largest market capitalization.
- They carry out a huge number of transactions with customers all over the world.
- They have access to a very large and unique set of data (e.g. web browsing data, social media data and biometric data).
- They have a naturally fluid and attractive user experience at the heart of their business.

Their success and profitability come from the seamless integration of their products and services into their ecosystems. This is particularly true for Amazon, as payment and consumer credit services are a natural complement to its core business and help to smooth the customer journey. They can offer consumers incentives and discounts for their financial products and services through their existing products and services. They can also create specific financial products such as, car insurance for autonomous vehicles.

1.2 Big Tech companies have the ability to disrupt the markets they target

They have major assets that may facilitate their expansion in financial services, as they have done successfully in other sectors such as music, books, retail, and travel. Their financial resources allow them to invest massively, including in cutting-edge Fintech start-ups, but also to offer free services thanks to their interconnected platforms ecosystems.
Their empire is built on a large community of users around the world, enabling them to take advantage of different regulatory and tax environments, for example in the UK or in Ireland.
Thanks to their mastery of technology, including IT infrastructure, artificial intelligence, algorithmic tools, machine learning and blockchain technology, they have demonstrated their ability to design

services perfectly tailored to their customers' expectations. In e-commerce, Alipay, Apple Pay, Google Pay and Paypal already account for half of global sales and 32% of in-store sales. Consumer trust in Big Tech companies seems to be amplified by their ubiquitous presence in daily life which creates positive externalities for their products and services.

In financial services, Big Tech companies are attracting customers not because they excel in this area, but because they already offer diversity and good value for money. As a result, customers are using Big Tech companies' financial services without realizing that they may not be best equipped, particularly when it comes to the security objectives of financial regulation.

There are three main reasons why Big Tech companies might invest even more in the banking sector and compete with traditional players of their core businesses:

- Big Tech companies seek to control their entire customer relationship, from service to payment, including the provision of credit and account management.
- They seek to increase their ability to acquire quality personal data, which is a particularly strategic for them. This data enables them to post excellent results in a sector that is worth trillions of dollars. Meta, for example, relies heavily on personal data for its revenues, with over 90% coming from personalized advertising generated thanks to their user's personal data. By analyzing buying behaviour, financial services offer Big Tech companies an effective way of obtaining even more data. This has a multiplier effect: the more data companies have, the more they use it to attract customers, leading to the acquisition of more new data to perpetuate the cycle.
- Big Tech companies have access to different types of data collected by their platforms (on consumer behaviour and preferences) as well as sophisticated software tools that enable them to analyse and use this information to assess risks accurately using highly advanced predictive technologies. This could be particularly relevant and profitable for the consumer credit and insurance sectors.

1.3 Can the development of Big Tech companies in finance generate new opportunities for further innovation, social inclusion and, above all, increased competitiveness?

This is a complex issue. In the short term, the market entry of major technology companies in financial services may benefit consumers. Big Tech companies could generate innovation and incentivise banks to innovate, improving overall quality and reducing the price of financial products and services through increased competition. Big Tech companies can also make a positive contribution to the end-user experiences of digital financial services.

In the longer term, four risks can be identified: the erosion of competitive advantages resulting from the entry of Big Tech companies into financial services if these firms manage to create and take advantage of well-established market power; reduced competition; worsening outcomes for consumers; and an unravelling of the balance between ancillary services and the main risk of keeping the accounts. This development could result in harms arising from the use of data enabling the "cartelisation" of siloed data, barriers to entry once financial data have been "hoovered up", "nonconfidentiality by default" and ultra-precise consumer profiling resulting in increased exclusion and discrimination, especially for vulnerable consumers.

1.4 On the other hand, banks have organized themselves to meet the Big Tech companies challenge

In the European Union, most banking groups are active in bancassurance, highly integrated and organised as conglomerates. They have long-standing financial relationships with a broad spectrum of their customers and offer them a wide range of products and services: savings, loans, insurance, personal protection, pensions, equipment, or car rental, even health, residential real estate, security remote surveillance, etc. They deal with as many of their customers' financial needs and beyond.

The bancassurance model, ubiquitous in France, has led banks to expand their business significantly, generating substantial income and strengthening their resilience, which impacts positively on their ability to cope with crises. This financial conglomerate model has three advantages:

- It benefits customers: it ensures that their main financial needs and interests are taken into account, and it allows for both loyalty in the advice - without referencing specific revenues or attached assets - and support over time.
- It provides banks with a high level of budgetary protection: the profitability of financial conglomerates is fundamentally the result of their customers holding several products over time. In the long run, this choice translates into greater and more consistent financial performance.
- Lastly, bancassurance conglomerates enjoy great balance sheet and long-term stability thanks to the very diverse nature, amounts and maturities of their customers' deposits and loans.

This model confers strength to banks and is a guarantee of security for their customers.

Banks are organising themselves to respond to the threat of competition coming from Tech and Fintech companies by modifying their processes for innovation, digitisation and customer relations. They are developing payment services and extending their range of services to non-banking offerings ("bank as a platform") to continue to position themselves as benchmark players. These relationships generate benefits in terms of knowledge of consumer data, which they use to promote and sell their new services.

1.5 The potential arrival of the digital euro

Big Tech companies excel in digital technology. They are major players across a wide range of uses, but are also in infrastructures, including, for example, the operation of submarine cables (Coehlo, 2023).

If created, the European Central Bank's (ECB) digital euro will provide Big Tech companies with an opportunity to strengthen its ascendancy over financial services, as in the case of central bank money, the question of deposit guarantees does not arise and that one option currently on the table would be to limit ownership of this currency to a single digital wallet per citizen. Big Tech companies could, thanks to their very rich customer databases and financial resources, pre-empt the opening of as many wallets as possible, to the detriment of commercial banks. Their customers could be incentivized to break away from the traditional financial relationships they had with their bank.

Big Tech companies already have a strong presence in the payments sector, offering new services or functionalities at relatively low cost thanks to the network effects of their platforms, which provide easily accessible interfaces for their global customer bases and diversified activities. They also enable direct interaction between many users.

2 The specific risks of Big Tech companies in finance

With their platforms, Big Tech companies operate in different manner than traditional financial players. They do not generate the same risks as banks and insurance companies, so their balance sheets carry very little credit, counterparty, or market risks. In addition, they are unlikely to become major risk carriers in the years to come because of the banking partnerships they are forging.

However, there are several types of risks that are major for financial stability: risks linked to their platforms; risks linked to Big Tech companies partnerships with financial institutions; more generally, risks linked to the ongoing breakdown of the value chain in finance, which could have serious consequences; the risk of "too big to fail"; risks to data protection and privacy; operational and cyber risks.

2.1 Platform risks

Big Tech companies create value in the financial services sector by providing platforms that bring together supply and demand in as many markets as possible. When the number of players operating via a platform increases, the volumes and variety of data increase in parallel, which increases the value of the platform for the network players.

This concentration of platforms can lead to risks for financial stability, even if these platforms respect competition rules. Three types of risks are particularly relevant.

2.1.1 Data concentration: sovereignty and data sharing

Data is the main driving force behind the growth and concentration of Big Tech companies: more (varied) data paves the way for better service, which in turn generates more data.

For citizen

Big Tech companies currently hold vast and diversified personal data. It is difficult for citizens to determine which organisations have access to their personal data, when they have access, what data they can access and what they do with it.

It is important to act on rules that can give users control over the data-sharing process. This is the purpose of ""permissions dashboards" to allow users to manage their granted open banking access permissions" provided for in the PSR (Payment Services Regulation) proposal (European Commission, 2023 a). It is also important to facilitate data sharing across sectoral boundaries, i.e. not just in the financial sector, as envisaged in the Commission's FIDA (Financial Data Access) proposal (2023 b). Users will then be empowered to ask financial institutions or Big Tech platforms to exchange personal data if this is beneficial to them.

Open banking (and ultimately open finance)

Big Tech companies have significant technological resources, sophisticated algorithms, and the ability to aggregate and combine different categories of data collected on their platforms. They can access Open banking data, but there is no reciprocal agreement for financial services companies to access their data. This leads to asymmetry in data access.
This is particularly important in the consumer credit and insurance sectors, where data is used to assess risk or affordability. Facilitating reciprocity and access to Big Tech companies' data could enable incumbents to provide equally competitive products and services.

2.1.2 Concentration of services

Financial institutions' heavy dependence on a small number of providers for the supply of technological services may create critical external interdependencies. At present, services may not always be adequately covered by outsourcing regulations, which are defined as the performance by an external operator of activities that would otherwise or normally be performed by the financial institution itself.

Changing market conditions require a global vision encompassing all important external contractual relationships for an institution. The EU rules under the Digital Operational Resilience Act (DORA) (European Parliament and Council, 2022b) are an important step in this direction as they introduce oversight of all service providers, whether or not they constitute a form of outsourcing.

Additional requirements may be necessary to ensure effective supervision of service providers. For example, constraints such as operational resilience, outsourcing or risk management, as well as micro or macro-prudential requirements for critical service providers.

2.1.3 Distribution concentration

The nature of these markets, and in particular the indirect network impacts they entail, could lead to a high concentration of distribution on a limited number of Big Tech platforms, even if their role in distribution is currently limited. This type of concentration entails both:

- Reputational risks: risk to financial stability relate to the size and possible concentration of Big Tech distribution platforms themselves. Loss of confidence in a platform due to mis-selling, for example, could compromise the functioning of the financial system when Big Tech companies play a dominant role in the customer relationship.
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- Transfer risks: if distribution channels and customer contacts are concentrated on Big Tech platforms, it will be more difficult for risk-bearing institutions to properly assess and manage risks.

2.2 Partnership and customer relationship risks

Partnership-based models and contractual relationships with large US banks are already - and will probably continue to be - the dominant entry strategy for Big Tech companies. These banks (Bank of America, Citigroup, Goldman Sachs) have an incentive to enter pre-emptive strategic alliances with them, to exploit their expertise in technology and customer experience. This mix can raise specific problems.

In particular, the risk of appropriation of the customer relationship, originally controlled by the traditional financial institution, is then relegated to the background of the customer relationship. This risk is significant in the context of a partnership between a Big Tech company and a financial institution, with the former distributing the products and services provided by the latter to its customers. This is all the truer in case of 'white-labelled' partnership, i.e., as in the case of industrial subcontracting, whereby the Big Tech company puts its brand on the bank's products. The latter's brand disappears in favour of the former, and the customer relationship then becomes controlled by the Big Tech company.

2.3 Overall, a major and growing systemic risk with the potential decomposition of financial services value chains

The expansion of the role of Big Tech companies and the deconstruction of financial services chains in which it is involved could become a real problem in the future.

Increasingly, added value - and profits - will be perceived at the 'periphery' of financial activities, while being conditioned by their 'core' (deposits, credit risk / balance sheets...) which remains in financial institutions. Distribution services can only exist if these "product factories" exist, factories that are generally risk factors and therefore covered by appropriate regulation.

When value chains are integrated, the cost of covering risks is implicitly shared. But by segmenting them into universes of a different nature, the whole distribution of risks is undermined, with links outside financial regulation gradually being able to condition the viability and financial stability of regulated financial institutions.

It could also have system-wide consequences if Big Tech platforms, which often bear no credit or market risks themselves, were to leave all excessive risks to these institutions on a large scale.
In addition, this element gives a distorted view of the risk platforms take on, since it is *a priori* very low, whereas the systemic consequences of the failure of a single Big Tech company in finance would be dramatic, given all the interactions they create with banks.

Existing laws and regulations do not target the large distribution platforms for financial products and services, which are dominant and concentrated. New financial regulation is needed to prevent platforms from passing on excessive risks to the financial firms with which they work in partnerships and to ensure that these firms will always be able to manage their risks properly. Measures can also be envisaged to guard against the systemic risks associated with the concentration of distribution platforms. Finally, attention must be paid to the continuity and possible long-term resolution of systemically important distribution platforms.

2.4 The "too big to fail" risk linked to the mixing of industrial and financial activities

The combination of financial and industrial activities has been a long-standing concern that has led to more or less strict solutions in the past, even going as far as outright prohibition. Today, this combination is no longer seen as an unhealthy mix, and it is regulated. The notion of core business activities and so-called ancillary activities seems to predominate today. A bank may hold interests in a given industry, even on a long-term basis, but these are subject to conditions. Similarly, a Big Tech company, which is basically a commercial enterprise, should be able to play a role in finance, but in a moderate way. In China, quota rules have been put in place, but they would clash with our Western principles of free enterprise. With the solutions outlined in part 5 below, the European Union and the United States could better control the volumes involved without going to such extreme constraints.

Furthermore, the disproportionate size of a Big Tech parent company active in the financial sphere through its service offerings (even regulated ones) - structurally marginal for it but significant for the financial ecosystem-, represents a severe risk. This risk needs to be better understood, in line with the situation of financial institutions, even of limited size, which guarantee the security and quality of the distribution of financial services.

2.5 Data protection and privacy are major concerns

The General Data Protection Regulation (GDPR) (European Parliament and Council, 2016) limits the use of data that is incompatible with the original purpose for which it was collected. Data sharing agreements between Big Tech companies, insurance intermediaries and insurers are risk areas that warrant regulatory attention to anticipate any detrimental impact on customers or policyholders.

2.6 Operational risk and cyber security

Cybersecurity incidents in non-financial sectors can have an impact on financial services, especially if they are concentrated among a small number of service providers.

In these last areas - data protection and privacy, operational risk, and cybersecurity - there is no international body in charge, unlike in finance areas This makes regulatory action even more of a priority.

3 An evolving regulatory framework for Big Tech compagnies

3.1 Tech companies follow the rules of the financial sector

All banking and bancassurance groups are subject to a strict framework for their activities, given their transactional role, potentially systemic size, the distribution of their services to all individuals and legal entities and, fundamentally, their key position for the economy. International prudential rules impose global requirements on their solo financial entities, such as minimum capital for all their risk exposures, liquidity requirements and a high level of transparency and reliability in their governance. In addition, there are extensive, anti-money laundering, combating financing of terrorism (AML-CFT) and consumer protection regulations.

A risk of unequal competition between players may arise in particular if Big Tech companies provide financial services without been subject to the regulation and financial supervision that applies to traditional players. As a matter of fact, this risk is limited, because if the services are provided illegally in violation of the relevant monopolies (banking, investment services, etc.) the supervisory authorities (ACPR, AMF, etc.) and judicial authorities (in the event of a breach of the law) must then act. This does, however, raise the question of political will and resources, which is dealt with in section 4 below. Or, Big Tech companies benefit from exemptions, generally limited in nature (e.g. services as X Pay, Apple Pay, Google Pay, etc.), relating to providers of technological services under the Payment Services Directive (PSD2) (European Parliament and Council, 2015) which do not allow them to expand the portfolio of services and products offered to customers. Apart from these limited situations, Fintech players wishing to provide financial services are subject to the same constraints as traditional players.

In many cases, the Big Tech companies have had to set up in the EU subsidiaries dedicated to financial services with the appropriate authorisations, so as not to be opposed to the traditional financial institutions whose statutes they have adopted. In the EU, for example, Paypal is a fully-fledged Luxembourg bank. Amazon has had a subsidiary in Luxembourg authorized as an electronic money institution since 2010. Google has had two subsidiaries authorized as electronic money institutions in Ireland and Lithuania since 2018 and 2019 respectively. Alipay has had the same authorization in Luxembourg since 2018. Facebook/Meta has had subsidiary, a payment institution, in Ireland since 2018. The Big Tech companies are also entering into partnerships with banks in the United States, whose banking services they distribute.

3.2 New areas of regulation are underway

European governments and authorities have introduced regulatory measures aimed at providing Big Tech companies with a better framework.

3.2.1 MiCA, DORA, DMA

These new regimes include the Markets in Crypto-Assets Regulation (MiCA) (European Parliament and Council, 2023), which will come into force in November 2024, the Digital Operational Resilience Regulation (DORA) (European Parliament and Council, 2022b), which will strengthen IT risk management and network cyber resilience from January 2025, and most importantly, the Digital Markets Act (DMA) (European Parliament and Council, 2022a).

The DMA establishes obligations for gatekeepers at the entrance to the Internet, in practice the Big Tech companies in the way they provide services on their platforms. Gatekeepers are intermediary professionals in the public space who manage access to information or a service to make it visible to the public and institutions. This is the case, for example, with online shops for mobile applications or online markets for e-commerce. These companies may control the products, services, and participants on their platforms.

This may generate a risk that large technology companies will exploit their very strong market power to impose their conditions of access and use (for businesses and consumers), which may lead to harm in terms of competition given their unbalanced bargaining power, and restricted choice for consumers. This can lead to unconstrained pricing and the manipulation of behavioural biases.

Big Tech companies have to comply with a series of obligations or bans on the use of these platform services in the European Union since March 6, 2024. Identical antitrust bills are also being examined by legislators elsewhere in the world. This new DMA regulation (European Parliament and Council, 2022a) aims to act before abusive behaviour destroys competition and gives rise to a de facto quasi-monopoly, such as that of Google in search engines.

At the same time, in November 2023, the European Banking Authority (EBA) published its recommendations for updating AML-CFT standards (EBA, 2023). This authority hopes that Crypto Asset Service Providers (CASPs) and their cryptocurrency wallets will be subject to verification protocols as rigorous as those imposed on banking entities and their accounts.

However, the current EU regulations on these platforms have no impact on prudential standards. Their aim is not so much to combat this concentration of platforms as to prevent the abuse of market power by the major platforms, including the possible blocking of customers or users. In the context of the financial sector, as we have seen above, large, concentrated platforms can entail major risks for financial stability.

3.2.2 The ongoing strengthening of competition and prudential rules

This is why new prudential regulatory requirements are gradually being introduced (Capital requirement directive 6 - CRD6 (European Commission, 2021a) and Capital requirement regulation 3 - CRR3 (European Commission, 2021b)) to ensure a more level playing field considers the risks common to banks and Big Tech companies. These requirements are all the more urgent that Big

Tech companies have already led to concerns about alleged breaches of competition law both within the European Union and in the United States. Regulation had to and must continue to be tightened.

The scope of regulation is evolving to capture the new services that fall outside the scope of PSD2 (European Parliament and Council, 2015), precisely to provide a framework for account aggregators who were able to take advantage of a blind spot in PSD1. This is also the case for crypto-asset service providers, which will be regulated under MiCA (European Parliament and Council, 2023) in substantially the same way as investment service providers, just as issuers of stablecoins referring to a single official currency will have to be authorised as banks or electronic money institutions.

4 But this is not enough

Although these new standards are welcome, there are still significant gaps in the regulatory framework:

- Big Tech companies have access to multiple markets in multiple jurisdictions. This poses problems for their international competitiveness, as they can take advantage of non-harmonized national rules, even within the European Union. Moreover, future regulatory proposals of varying degrees of stringency could have a negative impact on investment decisions in European financial services compared with other regions.
- They clearly prefer to operate outside or at the edge of financial services perimeter as this minimizes the degree of regulatory oversight imposed on them and are seeking to remain outside the scope of banking supervision particularly when it comes to the consolidation status of financial entities.

There are two key issues here.

4.1 Which activities should be considered financial activities?

Are products such as BNPL a form of credit? The answer to this question was positive, but many others remain or will emerge.

For example, are Amazon and Apple providing payment services by placing themselves between the bank card provider and the customer? As part of the review of PSD2 (European Parliament and Council, 2015), EBA and European Commission's Directorate General for Financial Stability, Financial Services and Capital Markets Union (DG FISMA) recommended that X Pay applications should fall within the scope of the PSD. However, the draft PSD3 (European Commission, 2023a) provides for these applications to remain outside the scope, following lobbying by the Big Tech companies.

The basic question is whether Big Tech companies provide regulated services that trigger an authorisation requirement without an exemption being applicable.
Furthermore, sectors such as payments are only gradually being regulated, and at this stage there is no obligation to consolidate.

It therefore seems essential that the Basel Committee, or at least the European Union, should keep a regularly updated list of activities and services considered to be financial. This would ensure uniform, high-quality regulation.

4.2 What is the scope of monitoring for a group engaged in these financial activities?

Big Tech companies with mixed activities deploy these financial businesses without necessarily triggering supervision of all their financial activities. An inadequately covered combination of activities can lead to a risk of contagion between entities and to the financial system.

The development of distribution by platforms, which have become essential for the routing of financial products and services, bank loans or services, is also continuing without consolidated supervision.

GE Capital famously collapsed in 2015, before being sold at a loss by the US conglomerate General Electric in 2021. More recently, some entities such as Wirecard were not subject to appropriate supervision and others are outside the prudential consolidation scope of banking groups. Finally, the failure of Bahamas-headquartered FTX, with businesses on a platform combining crypto (an exchange), traded delivery, crypto issuance and market making, shows that aggressive Fintechs can be bank-headquartered or hold a banking licence as was the case with Greensill Capital.

To achieve this, it seems essential to ensure a clear consolidated perimeter for any financial conglomerate. The supervisory authorities must be able to exercise their powers at the level of this legal entity to be able to implement any sanctions, a function without which any supervision is null and void.

Currently, activities of Big Tech companies are only subject to a regulation based on the activities they carry out (e.g. payment services, electronic money), with no framework for broader supervision of the consolidation of their entities or conglomerates (ESA, 2024).
This regulatory approach therefore does not consider:

- The risks that may arise from interdependencies between these activities, essentially the risks associated with intra-group interconnectivity which arise from the common use of technological infrastructures (the well-known platform), internal structural financing and/or intra-group financial transactions and risks relating to customer data. Segregation rules between financial and non-financial entities could therefore be imposed.
- Risks of financial contagion, potential conflicts of interest and reputational risks that could result from difficulties experienced by one of the group's entities.
- Lastly, the risk of insufficient attention or expertise on the part of management with regard to risks outside the core business, accentuated by the often-opaque organizational structure of Big Tech companies, with subsidiaries operating in several sectors and in different jurisdictions.

This prudential area has evolved positively since 2019 with the CRD5 Directive (European Parliament and Council, 2019), which introduces the concept of a "mixed financial holding company" ((M)FHCs).

This is a regime for the approval of mixed financial services undertakings. These (M)FHCs are subject to the same capital and liquidity requirements as banks. The Single Supervisory Mechanism (SSM) supervises their activities by ensuring that they comply with these prudential standards, carrying out regular checks and imposing sanctions in the event of non-compliance. Groups with significant financial activities must, when appropriate, set up an "Intermediate Parent Company", i.e. a parent undertaking located between the financial subsidiaries and the ultimate parent undertaking of a conglomerate group. CRD6/CRR3 (European Commission, 2021a and b) further clarifies, from 2025, these standards on certain key concepts: for example, the notion of "ancillary service undertaking". These are companies within a consolidated financial group, often regulated differently or not at all, which provide support services to the bank, such as data processing, portfolio management, clearing and settlement, record keeping, custody and custody services, advisory services, and research services.

Subsidiaries that are considered non-financial today and therefore not included in the consolidated scope of the group will have to be included. For Fintech and similar companies, the European Commission is also trying to include those that operate closely with banking groups or, a fortiori, those that are part of them. CRR 3 also brings several improvements, including a revision of the concept of financial holding company.

Greater control over major international groups is thus gradually taking shape, and this regulatory action is clearly a step in the right direction. By way of illustration, Apple's new financial services are managed by Apple Card and the company has also created a new subsidiary, Apple Financing, responsible for overseeing credit assessments and loans.

However, much remains to be done to understand and follow the nebulous and complex structures of Big Tech companies. Yet this is the first step towards effective control. In particular, the complex forms of partnership with certain traditional financial players, which have been developed in the United States, make their group structures complicated and difficult to understand. As already mentioned, the size of the platforms means that the financial risk is considered negligible compared with the core of their activities, even though it may entail major underlying systemic risks for the financial sector.

5 Our proposals based on the European Directive on conglomerates

Big Tech companies are expanding into retail financial services, which will increasingly bring them into competition, particularly in France, with the six financial conglomerates. It is essential therefore to be forward-looking and proactive in developing right now a comprehensive and effective regulatory and supervisory approach that allows fair competition among all players consistent with the wider international regulatory landscape, including regulation of digital currencies, the security and efficiency of global payment systems, artificial intelligence (AI) in financial services.

The threat posed by Big Tech companies is clear. The authorities are sounding the alarm, but often conclude that they need to monitor the situation and reflect on the next steps (ESA, 2024). On the contrary, we believe it is urgent to act because things can develop exponentially.

How can we ensure a level playing field? The Basel Committee's mantra is well known: "same business, same risks, same rules". The basic principle that must guide any prudential approach is clear: all companies, whether they are traditional banks or Tech companies, must be subjected to the same regulatory and supervisory requirements.

This may seem easy to implement, but in practice it is not. International prudential regulation is risk-based. It covers several long-established areas, such as financial stability, market integrity and consumer protection (depositors and policyholders). But the existing regulatory frameworks and their supervision pose major practical difficulties when it comes to applying them to Big Tech companies. Although the subject is well-defined, and warnings are multiplying, the solutions proposed to remedy the situation are few and far between.

This is where European regulations on conglomerates can help. European Union has had regulation and supervision of financial conglomerates in place for more than twenty years: the FICOD, known as the Conglomerates Directive (European Parliament and Council, 2002). It has proved its effectiveness during the many crises we have experienced. It is aged, but it should be revised, in particular to broaden its scope and include Big Tech companies active in finance; it should be the compass and the framework for the future of regulation and supervision to map out the right path to follow.

The Conglomerate Directive defines prudential requirements based on three essential and complementary conditions:

- The existence of defined financial sector entities (credit institution, insurance undertaking, reinsurance undertaking or insurance holding company, parent financial holding company, parent mixed financial holding company), with prudential consolidation at the highest level of the group.
- Supervision by the National Competent Authorities (NCA) with a lead coordinator.
- Competent authorities responsible with ensuring that the financial entities have an appropriate level of integrated management, risk management and internal control mechanisms, and that the processes are applied consistently on the long term.

To this end, three main controls are put in place by supervisors at the level of European financial conglomerates:

- Intra-sector relations, i.e. those between the banking entity and other sectors such as the insurance company (ies) or asset management company (ies) for bancassurance groups, and vice versa, to monitor the potential risk of contagion induced.
- All concentrations at the highest level.
- The existence of an overall solvency ratio at the highest level of the conglomerate, monitored by the supervisory authorities to ensure that it is properly capitalised.

On this basis, Big Tech companies would have to:

- Create a consolidated legal perimeter for all financial conglomerates, covering all financial activities carried out, with a particular focus on transactions between regulated and non-regulated entities of the group.
- Be monitored for concentration risks at the highest level and inter-business risks.
- Be monitored to ensure sufficient capital against systemic risks and, if possible, a global ratio of the conglomerate type at the upper limit of the group.

5.1 We propose the creation of a consolidated legal perimeter covering all the financial activities carried out by a conglomerate and its compulsory supervision by the competent authority, recognized by its peers, of the host country of the group's head office.

5.1.1 Regulation should require the consolidation of financial and ancillary activities.

Regulation must cover all financial activities, particularly with a view to controlling systemic risks.

For example, this could systematically include BNPL services. The provision of critical IT and cloud services to banks may equally be affected. Where Big Tech companies provide technologies that enable digital payment services or digital credit solutions, these need to be appropriately regulated.

The immediate challenge relates to payment institutions: it is important that banking prudential regulation applies to all non-bank payment and credit players carrying out systemic activity for the financial market.

5.1.2 The scope of entities should be complete

Today, banks, insurance companies and market infrastructures are under greater pressure than non-banks. Big Tech companies sometimes operate at the frontier or outside the regulatory perimeter and generate potential supervisory challenges. There are three shortcomings to be considered:
- The relative thresholds, which still give large, diversified groups considerable leeway in setting up mandatory financial holding companies.
- The location within the legal structure.
- What is or is not considered to be "ancillary services".

It is critical that all entities/activities considered as financial activities are grouped together within a homogeneous and impervious financial conglomerate to be regulated. As indicated in Part 4, progress has been made since 2019 in CRR2 and will be made in CRR3 (European Commission, 2021b) along these lines. This effort must be pursued.

5.1.3 Effective localisation in the European Union

Location of Big Tech companies in the European Union must be made compulsory (to avoid so-called "reverse solicitations"), as well as a very strict framework for delegations outside the European Union to combat "mailbox" locations.

In addition, the concentration of Big Tech financial entities in certain "small" EU Member States (Ireland, Lithuania, Luxembourg) is a cause for concern, as they could offer their services to the whole of the EU from these countries. Supervision by ECB-SSM, or even Anti-Money Laundering Authority (AMLA), should systematically replace national supervision.

5.2 All interactive and concentration risks should be monitored

5.2.1 Interactive transactions should be monitored

Within a financial conglomerate, certain entities may not be covered by the CRD/CRR. Already, with the CRD6/CRR3 legislation (European Commission, 2021a and b), the number of non-regulated entities will be reduced, and some will (re)become regulated entities (leasing in particular). But others may remain unregulated or regulated differently. The lesson of FICOD (European Parliament and Council, 2002) is that it requires reporting to the supervisor of transactions between regulated and non-regulated entities (above a certain size threshold) for supervisory control.

In addition, banks are sometimes encouraged, over and above their contractual obligations or their capital links, to "step in" to provide support to non-Group/non-consolidated entities to which they are linked. This notion of "step in risk" must also be well understood by the regulation.

Because, finally, the existence of partnerships between Big Tech companies and certain banks often makes the issue particularly complex, here too the relationship needs to be closely monitored.

The regulatory perimeter for financial services must be dynamic and regulators must seek to integrate financial activities into the regulatory perimeter over time. Although Amazon and Apple claimed that they did not provide payment services and that they were somewhere between the bank card provider and the customer they were obliged to have a payment license.

5.2.2 Concentration risks to be monitored

As mentioned above, there are concentration risks that need to be closely monitored, particularly concentrations in the distribution of financial products and services, volume limits per contracted player could be imposed on platforms in this respect.

5.3 Big Tech companies can operate at the boundaries of standards. A control along the lines of the FICOD conglomerates ratio could be introduced.

The International Monetary Fund (IMF) has warned that the rapid and significant expansion of Big Tech companies in financial services and their interconnection with financial services companies potentially create new channels of systemic risk (Bains & al, 2023).

Activities are interdependent. The difficulty lies in detecting when a group's activities can produce an overall risk that exceeds the sum of the risks associated with its activities. In this respect, the close links between the financial and non-financial activities of Big Tech companies justify close monitoring to detect any potential contagion that may come from or even impact their non-financial activities. Risks can be transmitted, so it is important for supervisory authorities to have visibility of the potential channels through which risks linked to Big Tech's non-financial activities are transmitted.

Big Tech companies could be subjected to additional regulation along the lines of that which governs systemically important financial institutions (G-SIFIs) around the world and that which controls the absence of double counting of capital for financial conglomerates in the European Union. This is achieved through a solvency requirement based on all quantifiable risks generated by financial activities at the level of the consolidating group (including new risks and step in risks), compared with the actual own funds that capitalizes it. All other risks, even those difficult to assess with respect of capital requirements, should also be controlled as far as possible, in particular by setting maximum losses in relation to the consolidated group's own funds at the level of its largest financial entity.

This proposal works well if there is a credit institution, an investment firm, and/or an insurance company within the conglomerate, which then makes it possible to impose such consolidation on a prudential basis with all the attributes of banking rules (systemic, pillar 2, step-in risks, etc.).

It is more complicated in cases where conglomerates have entities for which no European regulation triggers consolidated supervision: payment institutions, asset management companies, non-bank credit companies depending on the country and issuers or providers of crypto services, etc. However, the core business of these groups generally concerns payment and/or non-bank credit activities. A first step within the European Union would be to rapidly introduce a regulation to ensure that the payment system is supplemented by a consolidated system of the payment holding company type, to which consolidated supervision would then apply; and similarly for non-bank lending, with the creation of a European finance company.
There would be an entity that would trigger consolidation with a conglomerate aspect in pillar 2, which is admittedly more flexible than with a pure conglomerate ratio, but based on conglomerate rules that would then provide this alternative monitoring. The issuance of crypto to finance a credit channel supported by another entity with tokens issued to the public would, for example, fall within this consolidation framework.

Finally, it would be even trickier with entities that exclusively carry out activities that are distinct from banking-type activities, such as the use of a platform without any form of payment (activities based solely on technical services and the platform itself). One solution could be to recover the desired consolidation loop via an authorization requirement triggering consolidation. In the case of partnerships with other institutions, this could take the form of an obligation to implement a minimum of controls over the volumes and conditions of offers, or directly through a risk-sharing requirement imposed on the platform which would then have the capacity to absorb losses. It would be considered as granting credit through the acquisition of these receivables, and therefore as having the regulated status of a financial company, and the requested consolidated supervision could be implemented.

Beyond these adjustments, consolidated supervision is needed.

5.4 The urgent need to improve supervision of Big Tech companies in finance

Adequate supervision of Big Tech companies proves difficult:

- The supervisory authorities do not necessarily have all the expertise, or the means and resources required to understand, assess, and monitor their risks, nor do they have the authority to do so. As mentioned above, effective regulation requires the ability to hold management accountable, and the structures of Big Tech companies are often opaque in this respect. The implementation of consolidated perimeters must therefore be systematically pursued.
- Big Tech companies have considerable technological resources, offering a wide range of products and operating across several sectors. They operate wherever they see the greatest added value in their core products and services and are therefore perfectly mobile.
- The wide variety of services provided by Big Tech companies and the sophisticated forms of partnership between these companies and banks make the overall structure difficult to understand and, as a result, complicated and hard for the authorities to supervise.

5.4.1 A balanced approach is essential

Considering their business models and cross-sector presence, the activities of Big Tech companies in financial services within and outside the current regulatory perimeter need to be monitored in a comprehensive manner. Supervisors must take an evidence-based approach that protects consumer interests without undermining incentives to innovate.

As the business models and strategies for Big Tech financial services develop, supervisors will need to continually adjust supervision, including the regulatory perimeter. If all banks migrate to the cloud, it would be for those cloud providers to bear the operational systemic risk.

5.4.2 At the very least, create hubs within the European Union

The Basel Committee is making slow progress in this area, hesitating between entity-based and/or activity-based supervision (Carstens et al., 2021). The Bank for International Settlements (BIS) is gradually making headway, arguing that a rethink is warranted given the blind spots and inadequacies of current regulations Big Tech companies are subjected to, leading it to reflect on a new regulatory framework or approach to Big Tech in finance (Ehrentraud et al., 2022). Both the IMF and the BIS have recently put forward a "hybrid approach" that attempts notably to reconcile entity- and activity-based supervision (Villeroy de Galhau, 2023). However, Big Tech regulation and supervision remains piecemeal and holistic actionable insights on these should be expedited. Conclusions in this area clearly need to be speeded up.

In the absence of progress at the international level, the European Union will have to set up regional hubs, with the obligation to establish a regulated entity grouping all financial activities for any service provided to Europeans/within the European Union and which would aggregate loss-absorption functions in the event of distribution.

5.4.3 International cooperation is also essential

The presence of Big Tech companies across industries and regions of the world makes the supervisory landscape particularly complex. Supervisors need to be able to monitor them effectively and enforce rules, even if these companies are based in other international jurisdictions.

NCA and European authorities have little experience cooperating with each other in this area. To develop cross-border and cross-sectoral cooperation, it is essential to overcome current obstacles. In some Member States, there is even still a struggle between banking and insurance authorities, particularly over the issue of digital rights, which are sometimes particularly sensitive and/or confidential. In the EU, frictions or challenges may also arise from the increasing interaction of financial regulation with competition policy and data regulation, which have "*evolved in distinctive non-interactive legal silos, based on very different underlying principles and policy objectives*." (Zetzsche et al., 2019). The very recently recommended measures by the European Supervisory Authorities (ESA) to improve the Big Tech companies' oversight, however, are a welcome step in the right direction.

Greater coordination between national and international regulators and supervisors - where the BIS, the Financial Stability Board (FSB), the ECB, the EBA/ESMA/EIOPA and the NCAs should have a role to play - will improve supervisors' ability to identify trends, assess market-wide competition issues, and consider how best to supervise and enforce the regulatory perimeter. This coordination should be very broad, covering IT, data protection, competition, etc.

6 This is new territory!

A new generation of financial conglomerates is on its way: it will take advantage of synergies across data analysis, analytical capabilities, and innovative delivery mechanisms to design new types of products more quickly and easily for distribution to a greater number of customers. A tsunami may be approaching, encouraged by the potential launches of digital currencies such as the digital euro.

It is difficult to determine exhaustively how the new players should be understood, regulated, and supervised. However, we do know the direction of travel, thanks to the FICOD Directive.

The development of Big Tech companies will depend on two key factors.

- Consumer behaviour: tech giants such as Google, Apple, Amazon and Meta have transformed the way people search for information, communicate with each other and buy products online. It's not surprising that they are taking an interest in financial services. For their part, customers, particularly in retail banking, are increasingly demanding an 'integrated customer experience' and are increasingly managing their finances online. Digitalization and customer expectations are creating a new environment. Digital payments, for example, have accelerated sharply, particularly in the wake of the Covid pandemic.

- Regulatory environment, both prudential requirements and consumer protection standards: the BIS has emphasized that the role of Big Tech companies in finance raises issues that go beyond traditional financial risks. To address these issues, a balance needs to be struck between financial stability, competition, and data protection. Public policy must embrace a comprehensive approach that draws on financial regulation, competition rules and the regulation of private data.

Regulation is therefore essential. Authorities must ensure fair competition, considering the extent of the Big Tech companies' customer base and the specificities of their business models. They must coordinate to sharpen and develop their regulatory tools.

We do not have much time and we must do so quickly and with courage in terms of regulation and supervision. The network economy is tending towards a "winner takes all" situation. Without an appropriate prudential framework for this new market, it would be the Wild West.

Regulation is not just a question of prudence; it is also a question of models. We also need politicians to take a firm grasp of these issues, because the harmonisation of international rules will, if necessary, be the source of the future dominant model.

ANNEXE: composition of the working group

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