Regulation 2030

What lies ahead?

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Contents

Executive summary

How might financial regulation develop over the next ten years?

This paper focuses on four key questions:

Will regulation push on, or be pushed back?
What will be the regulatory response to fintech?
Will regulation be used increasingly to deliver social objectives?
What questions does this raise for society to address?

Financial regulation has changed significantly in the ten years since the global financial crisis. Tougher, more detailed and more complex standards now apply to all aspects of regulation. This has extended to capital, leverage, liquidity, recovery and resolution planning, governance, culture, remuneration, retail and wholesale conduct, anti-money laundering and countering terrorist financing, systemic risk and macro-prudential policy. Although banks have faced the fullest force of these reforms, the direction of travel has been similar across insurance, investment firms and financial market infrastructure.

Overall, regulation and supervision are more likely to push on further than to be pushed back over the next ten years. In part this will reflect regulation moving into new areas (or expanding in existing areas) largely unrelated to the financial crisis of ten years ago, including fintech, cyber security, anti-money laundering and counter terrorist financing, retail and wholesale conduct, and potentially a raft of regulation driven by social objectives such as climate change and financial inclusion. And in part the use of technology by supervisors will facilitate the growing intensity of supervision.

These developments will be of critical importance to financial institutions. Regulation is a key element in the landscape (together with the macro-economic environment, changing customer needs and preferences, innovation and competitive pressures) in which they operate and are seeking to develop viable and sustainable medium to long term strategies.

Many financial institutions are focusing on business growth and on customer experience, supported to a large extent by data, data analytics and digital transformation. But financial institutions will need to keep a close eye on regulatory developments as regulation and supervision adjust to the data and technology revolution.

Questions for a wider debate

Some of the issues here are very much for society as a whole to address, not just regulators, since they are central to how financial services should evolve over the next ten years. These wider issues need to be debated and resolved. They are essentially questions of how society wants to strike a balance between:

1. The costs and constraints imposed by regulation — The ability of the financial sector to provide products and services efficiently and effectively.
2. The potential advantages of 'big data' and data analytics — Data privacy concerns and the potential mis-use of data for misleading and inappropriate sales and advice practices.
3. The emergence of dominant technology-enabled platforms as fewer, larger firms exploit the scale economies inherent in many fintech applications — Concerns about a lack of competition, market dominance and financial stability risks
4. The potential advantages of artificial intelligence and machine learning — Risks of adverse outcomes and an inadequate understanding of emerging risks.
5. Consumer responsibility — Potential complexities and information asymmetries in an increasingly fintech dominated financial services sector.
6. Maintaining the risk-sensitive lens of regulation — Use of regulatory interventions to achieve wider social objectives such as supporting small businesses, infrastructure investment, financial inclusion and halting climate change.

Will regulation push on, or be pushed back?

Current focus on both recalibration and the relentless march of new regulation.

Likely future focus on shifts in regulatory approach, shifts in geo-political balance, and the impact of the next crisis.

No major rolling back of regulation.

Risk of greater fragmentation of regulation across countries and regions.

Regulation is more likely to push on than be pushed back. Recalibration is unlikely to make a significant difference, while the relentless march of new regulation will continue. There may however be some shifts in regulatory approach and a greater fragmentation of regulation across countries.

Recalibration underway

Pressures are building for a recalibration of financial regulation.

The Financial Stability Board (FSB) is undertaking a post-implementation evaluation of the effects of the G20 financial regulatory reforms. Working with the IMF, the World Bank and the international sectoral standard setters, the FSB has a specific focus on the unintended consequences of regulatory reforms (including the sharp reduction in some banking services such as correspondent banking) and the spill-over impact of tougher regulation on emerging markets and developing economies (including the reduction in the international activities of many banking groups).

The European Union is conducting various reviews of financial sector legislation, in banking (capital requirements and proportionality), insurance (post-implementation review of Solvency II) and securities (post-implementation review of MiFIII and EMIR).

These are driven by concerns that financial regulation may be holding back growth and employment by constraining the provision of finance to individuals, corporates and infrastructure projects; and by moves to enhance a European capital market (Capital Markets Union). This has already resulted in some adjustments to regulatory requirements.

Financial sector legislation and agency rules are under review in the United States, as part of the new administration's efforts to reduce regulatory burdens more generally.

But limited impact?

However, it seems unlikely that these initiatives will result in any major rolling back of financial regulation. There may be an appetite to make modest adjustments to international standards and to their implementation at regional and national level, but there is little evidence of pressure for substantial changes.

Even in the US the currently identified proposals for reducing financial regulation relate mostly to measures taken over the last ten years that were super-equivalent to international standards (such as the Volcker rule on banks' trading activities, the intensity of stress testing, and the structure, governance and capital requirements imposed on foreign banks' activities in the US). In the UK it seems increasingly unlikely that Brexit will lead to any significant 'bonfire of red tape'.

While the flow of new regulation continues

Meanwhile the flow of new regulation continues unabated in many areas.

The Basel Committee has finalised its standards for new standardised approaches for credit risk and operational risk, limitations on banks' use of internal models to calculate capital requirements, and an 'output floor' to limit the extent to which banks' internal models can drive down capital requirements. Although full implementation of these new standards is delayed until 2027, these new standards will require many European banks in particular to retain or raise considerable amounts of capital. The Basel Committee has also initiated a discussion on a revised approach to sovereign risk exposures.

Global systemically important banks and all EU banks subject to a resolution strategy will be required to hold additional loss absorbing capacity, while recovery and resolution planning will extend to other sectors.

The International Association of Insurance Supervisors is developing international capital requirements for insurers.

Conduct of business requirements (in retail and wholesale markets) and anti-money laundering and counter terrorist financing requirements continue to ratchet upwards across all financial sectors.

Financial stability and the use of macro-prudential policy tools remain high on the agenda even at a time of relatively weak macro-economic conditions. This focus is likely to intensify as economic conditions improve, and to extend beyond banking to the insurance and asset management sectors.

Supervisory pressures continue to grow on regulated firms to improve their governance, culture, risk management and other controls.

Alternative approaches will emerge

The overall approach to regulation is also likely to shift over the next ten years, while preserving broadly equivalent outcomes. This will no doubt vary across countries and sectors, and may therefore add a degree of implementation and supervision fragmentation to the fragmentation of international standards. While financial institutions may welcome at least some of these likely developments the 'devil will be in the detail' since each of them could take many different forms.

- A merging of the boundaries between different sectors and a shift away from sector-specific regulation towards more activity-based regulation;
- A more 'principles based' approach under which some detailed rules would be disapplied if a financial institution could demonstrate that it is taking its own tough approach to meeting high level requirements and dealing with issues effectively;
- A more 'outcomes based' approach under which supervisors assess whether (or not) firms and financial systems are safer and whether consumers have on balance benefited from market developments and high level regulatory requirements, rather than focusing on compliance with detailed requirements;
- A trade-off between greater simplicity and basic minimum standards (for example the CHOICE proposal in the US where a firm meeting a tough simple regulatory requirement – such as a high leverage ratio for a bank – would not be required to meet more detailed rules);
- A more proportional approach for smaller firms, differentiated from the international standards applied to larger firms (the EU is exploring this option);
- Having established a tougher set of minimum quantitative standards, a greater focus on 'best' and 'good' practice (depending on the nature and size of a regulated firm) in more qualitative areas such as governance, risk management and internal controls; and
- A more forceful focus on the viability and sustainability of financial institutions, on the financial stability implications of sector-wide issues, and on the possibilities for market restructuring to create more competitive and efficient financial sectors. This may be most marked in Europe, where parts of the financial system suffer from low profitability; an overhang of past problems (non-performing loans for banks, guaranteed interest rate products for insurers, and various mis-selling and misconduct issues); and a lack of competition where a small number of large financial institutions dominate many national markets alongside an inefficiently large number of small firms.

Shifts in geo-political balance and regulatory fragmentation

It has never been easy to deliver global consistency in the development and application of international standards in any financial sector. In insurance and asset management the closest convergence is often between Europe and Asia, with the US pursuing its own agenda. But the convergence between Europe and Asia may prove to be fragile because much of the regulation in the areas of consumer and investor protection, market structure and governance may not be well-suited to Asia, so Asian regulators may to some extent go their own way.

In banking the post-financial crisis consensus is already beginning to fray at the edges and may prove increasingly unsustainable. The rest of the world is growing increasingly tired of following standards crafted in the US and Europe. Some Asian countries may perceive a degree of 'political bias' in the attitude of US and European regulators towards Asian markets, driven by a concern to retain business (and tax revenues) in the US and Europe.

The growing importance of China and some Asian markets could also lead to significant changes in regulatory direction. As Asia becomes more important to the global economy/financial system, and as Chinese and other Asian financial institutions increase their global footprint in both lending and capital markets, Asian regulators may take a greater role in formulating global standards and will become increasingly important players in supervisory and resolution colleges.

Moreover, different countries and regions are likely to reach different judgements on the balances to be struck between greater financial stability and consumer protection on the one hand, and the ability of the financial sector to provide products and services efficiently and effectively. The costs of regulation, be it from higher capital requirements or greater consumer protection, ultimately have to be borne by the customers of financial institutions.

Until the next crisis

Major regulatory change tends to follow crises. Since we are unlikely to enjoy a completely smooth ride over the years through to 2030, how might the next crisis shape regulation? Predicting the next crisis may be impossible, but the impact on regulation of actual crises or concerns about potential future crises may be more predictable.

A major cyber security event would lead to increased calls for testing, improved internal controls and information sharing. Any major cyber security event is also likely to test the growing market in cyber event insurance, in terms of both the impact on the insurers in this field and the amount of cover that is actually provided.

Insurance sector losses would lead to greater urgency in the development and implementation of international capital and recovery and resolution standards for insurers.

Another disorderly failure of a systemically important financial institution might force costly restructuring and even break-up on the largest financial institutions to make them more easily resolvable.

A failure to deliver greater cooperation and collaboration among national authorities (on which much of the regulatory reform agenda depends) would lead to an even more pronounced 'revolt' by host supervisors who feel that they are not being listened to, and to a further shift to localisation and fragmentation as national authorities insist on various forms of subsidiarisation and the ring-fencing of local operations.

Regulatory response to fintech developments

Impact of fintech on the financial sector

Risks to firms, financial stability and consumers

Likely regulatory response to these risks

Scope for the use of data and technological developments by supervisors

Fintech developments will have an increasing impact on the financial sector, and will bring not only benefits and opportunities but also risks to regulated firms, financial stability and consumers. These risks will generate a regulatory response in the form of new principles, rules and guidelines. In turn, regulation will constrain and shape the impact of fintech on the financial sector.

Market developments

Fintech covers a wide range of data and technological innovations (see box on page 11). But however it is defined, by 2030 the take-up of fintech is likely to have exploded in multiple directions.

Established regulated firms should be able to provide existing products and services more efficiently (cost reductions), and to provide new products and services through new channels and new customer interfaces (transforming the business model). Fintech-based challenger firms - from within and from outside the financial sector, and including both start-ups and established non-financial firms - will move increasingly into the provision of financial products and services.

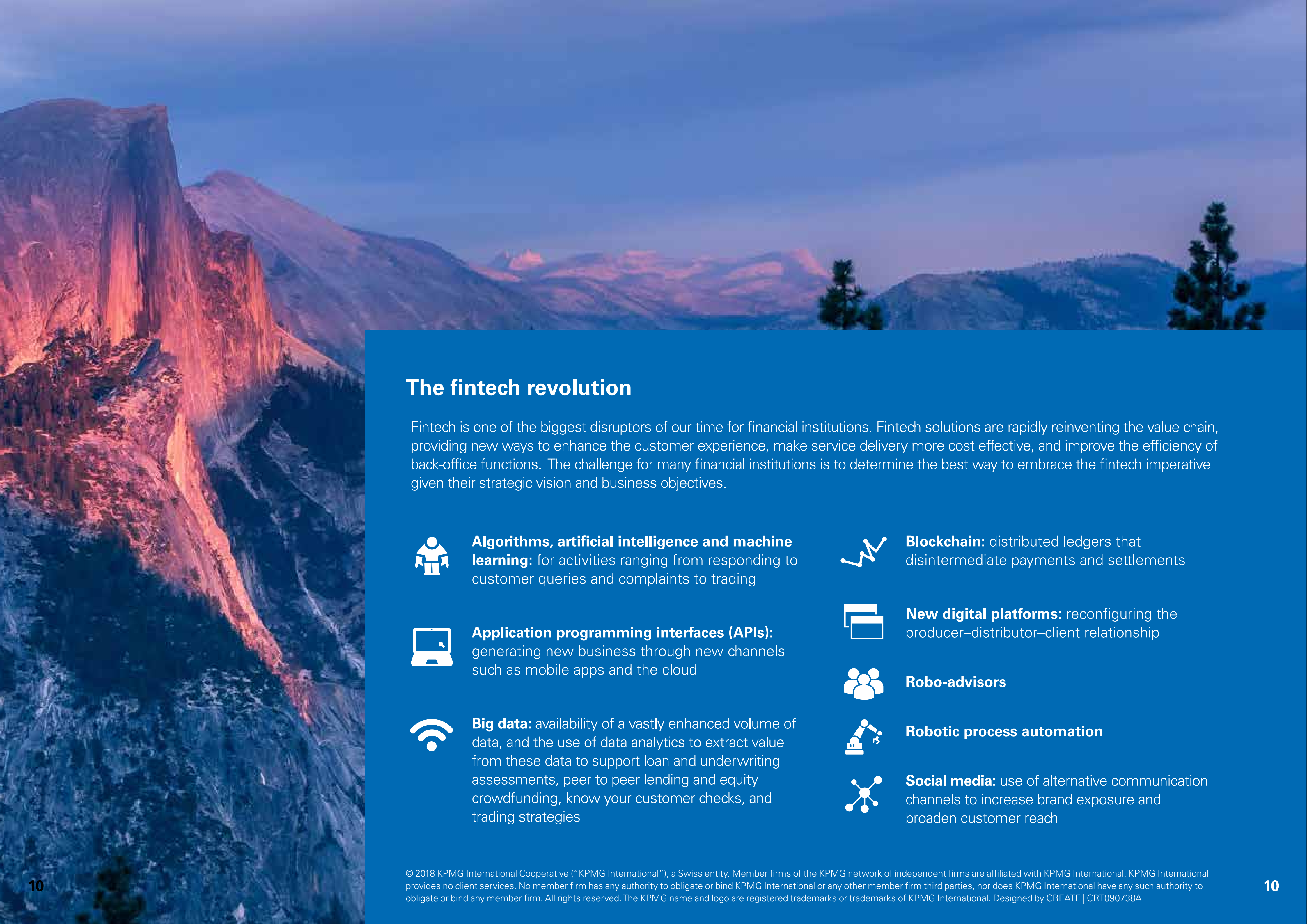
As in other sectors such as retailing, telecommunications and internet searching, we may see the emergence of a platform-based technology revolution in which a small number of platforms dominate the customer relationship, leaving other firms to provide products and services into these platforms.

Established and newly-regulated firms will enhance their compliance, regulatory reporting and stress testing capabilities through fintech (RegTech), including through the development of more effective, accurate and timely data management capabilities, automated 'dashboard' systems for compliance management, biometric approaches to customer identification and more efficient client on-boarding.

These market developments will be driven by various forms of disruption – internal disruption as established financial institutions use fintech to drive cost savings and business model transformation; joint disruption as established financial institutions collaborate (through partnerships, joint ventures, etc) with fintech firms; and external disruption as new entrants build market share.

The initial regulatory response to fintech developments was supportive. The emphasis was on encouraging innovation; using regulatory sandboxes, accelerators and innovation hubs; and taking a 'technology neutral' approach.

However, we are now clearly entering a much trickier phase for regulators, who have to identify, assess and respond to the risks (not just the benefits and opportunities) posed by fintech developments to regulated firms, to financial stability, and to consumers.



The fintech revolution

Fintech is one of the biggest disruptors of our time for financial institutions. Fintech solutions are rapidly reinventing the value chain, providing new ways to enhance the customer experience, make service delivery more cost effective, and improve the efficiency of back-office functions. The challenge for many financial institutions is to determine the best way to embrace the fintech imperative given their strategic vision and business objectives.

- **Algorithms, artificial intelligence and machine learning:** for activities ranging from responding to customer queries and complaints to trading
- **Application programming interfaces (APIs):** generating new business through new channels such as mobile apps and the cloud
- **Big data:** availability of a vastly enhanced volume of data, and the use of data analytics to extract value from these data to support loan and underwriting assessments, peer to peer lending and equity crowdfunding, know your customer checks, and trading strategies
- **Blockchain:** distributed ledgers that disintermediate payments and settlements
- **New digital platforms:** reconfiguring the producer–distributor–client relationship
- **Robo-advisors**
- **Robotic process automation**
- **Social media:** use of alternative communication channels to increase brand exposure and broaden customer reach

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Risks to regulated firms

Risks to regulated firms from the growing use of fintech include:

- The potential impact of new risk assessment methodologies and data analytics on credit and underwriting risks;
- New product development running ahead of internal control processes;
- A failure of Boards, senior management and risk management to understand fully the fintech applications being used by a financial institution - for example the use of artificial intelligence - and thereby a failure to manage the risks effectively;
- Vulnerability to money laundering, cyber attacks and the opportunities for insiders or cybercriminals to manipulate market prices by exploiting advanced optimisation techniques and predictable patterns in the behaviour of automated trading strategies;
- The creation of 'black boxes' in decision-making (for example, decisions on know your customer, credit scoring, insurance underwriting, trading or investment);
- Operational and outsourcing risks, including an inability to understand fully the fintech services provided by a third party and a lack of clarity about responsibilities between regulated firms and third party providers when something goes wrong;
- Data protection;
- Constraints on recovery and resolution preparedness as data, data analytics and digitalisation become critical services supporting the critical functions of financial institutions;
- Greater competitive pressures, including the ability of customers to switch between providers more easily;
- Following non-viable business models;
- Failing to adopt the right balance between fixing the past (fintech places increased pressures to address legacy systems, to facilitate the use of 'big data' and to provide a more robust base from which to develop and apply fintech solutions) and investing in the new; and
- Understanding and addressing the risks arising from the use of distributed ledger technology (DLT) in payment, clearing and settlement systems, and more generally in the storing and validation of transactions data. These risks include operational and security risks, the lack of interoperability with existing processes and infrastructure, the ambiguity relating to settlement finality and the legal underpinning of DLT, and the risks to data integrity, immutability and privacy.

Risks to financial stability

Fintech could lead to risks to financial stability from:

- Greater concentration - perhaps even to the point of single dominant operators - in some market segments, arising from economies of scale in the application of new technologies;
- New and unexpected forms of interconnectedness among financial markets and institutions (for example from the correlations arising from the use by various institutions of previously unrelated data sources);
- The opaqueness of artificial intelligence and machine learning methods and models;
- The potential failure of systemically important firms and market infrastructure relying on fintech;
- Third-party dependencies (possibly leading to the emergence of new systemically important players that could fall outside the regulatory perimeter); and
- Large and unstable funding flows on fintech lending platforms (with the potential for volatility to arise from lower lending standards, untested risk assessment processes, exposure to cyber security risks, and the likely strong pro-cyclicality of fintech-based lending).

Risks to consumers

New products and services, and new ways of advising on and distributing both existing and new products and services, give rise to various risks to consumers:

- Fintech offers the opportunity of financial institutions becoming more customer-centric and providing customers with better products and services, better value for money, more personalised service, and better access, distribution and communication channels. However, at the same time the profit motive and an unchanged culture may lead some financial institutions (advertently or inadvertently) to use the opportunities provided by fintech as new ways to extract money from unsuspecting consumers by selling them (or advising them on) products and services that do not meet their needs or that are poor value for money;
- Firms may find it difficult to meet conduct of business requirements as the digitalisation of the consumer interface and the growth in the use of artificial intelligence (to handle customer enquiries and complaints, and the provision of automated advice) become embedded in the relationships between financial institutions and their customers;
- The use of machine learning and artificial intelligence could result in greater complexity and a lack of transparency to consumers – it becomes more difficult to provide consumers with an explanation of how a credit or insurance decision was reached;
- Without adequate testing and 'training' of tools with unbiased and accurate data and feedback mechanisms, applications may not deliver what they are intended to do;
- Digitalisation may disadvantage older and other vulnerable consumers who have limited access to, or understanding of, digital delivery channels. Fintech carries the potential for increasing the financial inclusion of some groups of consumers while at the same time excluding other groups;
- The increasing use of 'big data' by financial institutions creates the scope for the unfair treatment of some consumers and for conflicts of interest between firms and their customers. For example, insurance has traditionally worked on the basis of a pooling of risks, but technology enables bespoke risk profiles to be determined and individually priced more accurately (fintech will give insurers access to far more information about lifestyle and health risks). Some risks may then become uninsurable or prohibitively expensive;
- Some data sources could introduce race, gender and other biases into credit and insurance underwriting decisions, even if these characteristics are not themselves included in the data sets, because other data points may act as proxies for these biases; and
- Data privacy and data protection issues may arise from the growing volumes of customer data, access to and storage of these data, and the flows of data (often across national borders) between financial institutions and third party service providers. Consumers are likely to become increasingly aware of the value of their data, and of the ways in which it is being used, leading to denial of access issues and possibly data manipulation by consumers.

Regulatory responses

Regulators will continue to monitor the developing risks to individual firms, to financial stability, and to consumers, and to intervene accordingly. In some cases this will take the form of adapting existing regulation (and supervision) in areas such as:

- Outsourcing (for example where firms rely on common third-party service providers of cloud computing and data services);
- Addressing cross-border legal issues posed by innovations in cross-border lending, insurance, trading and payment transactions;
- Assessing the regulatory perimeter and updating it on a timely basis; and
- Seeking to agree common standards in areas where different regulatory approaches are being taken by national regulators.

There will also be a growing regulatory and supervisory focus on financial institutions' governance and risk management frameworks to ensure that risks arising from fintech developments are properly identified, understood, managed and monitored.

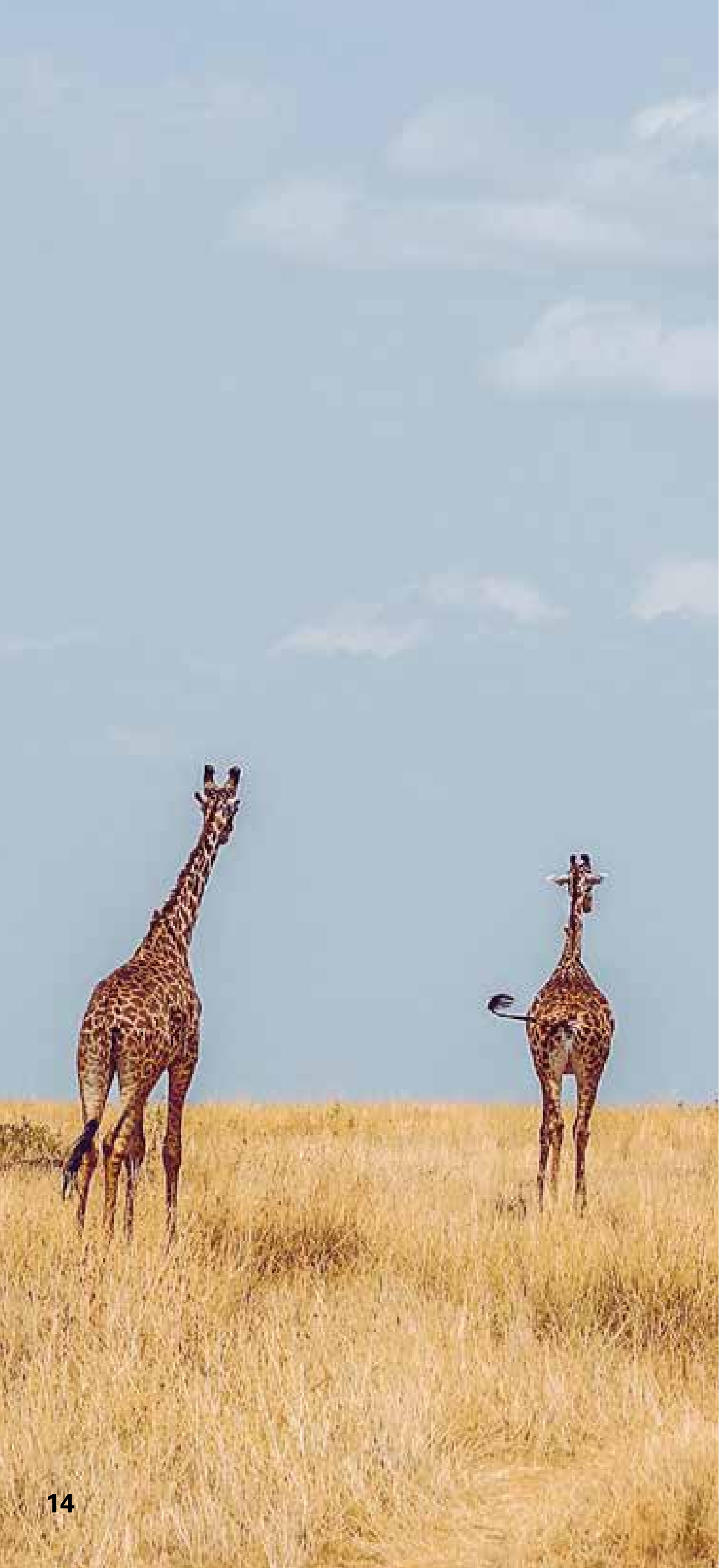
Firms will be expected to embed this in their strategic and business planning, new product approval management processes, and the sound management of operational and outsourcing risks; and to monitor and review the impact of fintech on their compliance with applicable regulatory requirements, including those related to consumer protection, data protection and anti-money laundering.

New regulations will be introduced in areas such as consumer protection, cyber security (contingency planning, information sharing, monitoring, and incorporating cybersecurity in the early design of IT systems), data privacy, governance and disclosure frameworks for big data analytics, and the authorisation and regulation of new fintech firms.

Regulation is also likely to spread to firms that are currently outside the regulatory perimeter, for example if they are important as providers of third party services to regulated firms or of potential systemic importance.

The initial 'let innovation thrive' approach is therefore likely to be overwhelmed by concerns about the various risks arising from fintech and by concerns about level playing fields and minimising regulatory arbitrage.

This raises the spectre of more intensive regulation of fintech than might have been expected, and the risk that there may be inadequate analysis of the impact of this on the pace and extent of innovation, on the opportunity provided by fintech to generate greater competition in parts of the financial sector, on the position of incumbent market participants (where regulation may strengthen the oligopoly of existing large players and make it more difficult for new entrants to grow into substantial challengers), and on the availability and pricing of products and services for consumers.



Supervisory technology (SupTech)

Just as technological innovation offers opportunities to financial institutions, there is scope for supervisors to use the same technology and data analytics to enhance (or at least make more efficient through the automation and streamlining of operational procedures) their monitoring of the firms and markets they regulate.

This remains at a relatively early stage of development, but the next ten years should see supervisors making considerably greater use of:

- A more real time approach to analysing data and other information (for example on consumer complaints) to support risk assessments, review exercises and market transaction monitoring;
- Direct and real time access to data and information on a targeted basis through access to firms' own systems, rather than a reliance on out of date and pre-formatted regulatory reporting;
- The use of artificial intelligence to analyse the 'big data' contained in regulatory and statutory reporting by financial institutions, and in other sources of information such as websites, marketing materials, social media and firms' internal documents provided to the supervisor (such as policy document and meeting minutes). This could focus on detecting regulatory breaches and other anomalies in the available data and information, detecting market manipulation and insider trading, and building a capacity to predict problems (early warning systems) based on correlations between observed information ahead of past problems at other firms;
- More preventative ex ante supervisory actions. If supervisors are able to access a firm's data real-time and they have their own predictive monitoring tools, they could be better placed to take earlier actions as soon as supervisors anticipate solvency, liquidity, conduct or other issues; and
- The exchange of real-time information across supervisory colleges.

This has the potential for supervision to become more timely, proactive, predictive, and automated (exceptions or outlier based).

Equally, however, the pace of change here may be held back by concerns within supervisory authorities about the balance of human judgement and automated input to decision-making, the governance and control of supervisory technology, supervisors' own IT capabilities, and restrictions on the cross-border sharing of information and data.

Using regulation to support social objectives

Increasing pressure for regulation to support social objectives

Need to balance this against the risks

Social and political pressures may grow for regulation to be used more actively to promote the achievement of social objectives. Indeed, to some extent this is already happening, for example through the lenient capital requirement treatment of exposures to domestic sovereign risk in local currency, and (at least in Europe) of the funding of SMEs.

The use of regulation to promote social objectives could be extended to more favourable regulatory requirements on financial institutions and financial products supporting social objectives such as carbon reduction and other positive climate change initiatives, financial inclusion and equality of opportunity.

Conversely, less favourable regulatory requirements could be applied to financial activities deemed to be undermining social objectives or deemed by politicians or regulators to be 'less socially useful' (for example certain trading activities, or certain products that are deemed to be too risky to be provided to retail consumers).

Such regulatory incentives and disincentives could take various forms, including adjustments to capital, solvency and liquidity requirements for specific types of lending, insurance and investment; quotas or targets for the performance of regulated firms in areas such as Board and senior management diversity and the provision of financial services to vulnerable and otherwise excluded consumers; disclosure requirements; more active use of climate change scenarios within the stress testing of banks and insurers; and conduct of business requirements (for example making it more costly and difficult to sell, promote or advise on the sale of certain types of product).

In some respects this would mimic the use of both prudential and conduct of business requirements within macro-prudential policy to mitigate risks to financial stability.

Even if regulators 'encourage' certain socially desirable activities, such as green investments, they will need to balance the extent to which they do this with their solvency and consumer protection objectives. This will raise questions about the independence of regulators and the objectivity of their risk-based and risk-sensitive approaches.

A regulated firm that fails because it has lent to or invested in certain types of business in response to regulatory incentives or supervisory encouragement could potentially lead to the regulators being criticised or even sued by the shareholders and creditors of the firm. There is also a potential systemic risk if incentives are pushed to the extent that all firms adopt similar lending or investment strategies. The use of directed lending and lending quotas in some Asian countries already carries such risks.

Wider issues: beginning the debate

Likely developments in regulation, including regulatory responses to fintech-related market developments and the use of regulation to promote social objectives, raise a series of broader issues that need to be addressed. These are matters for society rather than just regulators, and they all relate to the fundamental question of *“what kind of financial services sector do we want in 2030?”*

Regulatory burden

Regulation imposes a burden on regulated firms and constrains the way that many financial markets operate. This in turn imposes costs and restrictions on users of financial products and services.

Have we reached a ‘tipping point’ at which the costs of ever-increasing regulation and more intensive supervision are beginning to exceed the benefits? Specifically in the fintech area, is there a risk that the regulatory response will inhibit innovation and prevent the full benefits of fintech from being realised?

Data

Customer data is being used extensively by product and service providers, often on the basis of sales or exchanges of data among providers. In many respects this can benefit consumers through attractive tailored offerings that meet their needs and through platforms that bring together a wide range of data sources. Even outside financial services some constraints are emerging on the use of customer data, including data privacy legislation and limitations on where data can be held and accessed.

Should financial services be subject to additional constraints, to reflect the highly sensitive nature of much financial data; the risks to consumers and firms if this data were to be used for criminal and fraudulent purposes; and the risks that data may be used to offer products and services to vulnerable or poorly informed consumers that do not meet their needs and do not offer good value for money?

Technology-enabled platforms

Experience outside financial services suggests that scale economies often result in dominant platform providers (such as Amazon, Google and Facebook). This type of technological revolution has not yet hit financial services. This may be because current regulations are discouraging or preventing the emergence of such providers and are protecting the position of incumbent firms.

Should regulation push back against the exploitation of scale economies on the grounds of competition and financial stability? Or should it accept that "winner takes all" outcomes may emerge in some financial services and focus more on the appropriate response to the outcome of strong scale economies in many fintech applications?

Artificial intelligence & automation

An increasing number of processes, including decision-making and the provision of advice, are being handled by robots. In many areas of application this can generate both cost efficiencies and better quality decisions and advice. But in some instances the outputs may not be so beneficial, for example where the 'black box' is designed to lead consumers towards pre-specified outcomes that benefit the provider rather than the customer, and where similar strategies based on similar data sets lead to herding behaviour or ignore situations that are not captured in the data.

What form should the regulation of artificial intelligence take? Is it sensible and effective to focus on control mechanisms (inputs) or should the focus be more on the quality of outcomes and on systemic issues? Should there be a shift from predominantly compliance-based regulation to more outcome-focused approaches? Should regulation focus more on overall benefits rather than the risks to a small number of individual consumers?

Consumer responsibility

The emergence of new products and services as a result of fintech provides an opportunity to redraw some lines around the extent to which consumers should be expected to take responsibility for their decisions and actions. For example, the provision of financial services through digital services enables consumer information and warnings to be delivered in new and imaginative ways.

Is there scope to use fintech-related market developments to draw new and clearer lines between consumer and distributor/manufacturer responsibilities?

Social objectives

Social and political pressures may grow for regulatory incentives and disincentives to be used more actively to promote the achievement of social objectives such as limiting climate change, the provision of finance for infrastructure and SMEs, financial inclusion, and diversity. Indeed, to some extent this is already happening.

To what extent should regulation be used to promote social objectives? Is it sensible and effective to use financial regulation for this purpose, rather than other government interventions such as taxes, subsidies and legislation? How great are the risks that if regulation becomes less risk-sensitive more financial institutions will fail, not least those contributing to desirable social objectives? Is this a price worth paying to achieve wider objectives?

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