

Financial Stability Institute



Fintech regulation: how to achieve a level playing field

PIIE Financial Statement Series: Regulating Financial Activities vs Regulating Entities

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Views expressed are those of the presenter and do not necessarily reflect those of the BIS or the Basel-based standard-setting committees.

1 – Motivation

- “Same activity, same regulation”: a successful slogan
- ...for the industry
 - “Everyone (should be) operating under the same set of rules” (Marcus Scott (City)) in front of the UK parliament (2019)
 - “...same activity should receive the same regulatory treatment, regardless of the entity undertaking that activity” (IIF (2018))
- ...but also for some regulators
 - “Evidence (on non-bank designations) implements an activity-based approach for identifying an addressing potential risk for financial stability” (US FSOC (2019))
 - “EU policies should (...) ensure that the same activity is subject to the same regulation” (European Commission (2017))
- Two main (connected) rationales:
 - Ensuring a level playing field between banks and fintech/big tech players
 - Avoid regulatory arbitrage

2 – This paper

- Is an activity-based regulatory approach consistent with primary policy objectives: financial stability, consumer protection, market integrity and contestability?
- Is it really the most sensible approach to contribute to fair competition between banks and fintech/big tech players?

3 – The current setup

- Big techs do hold licences that allow them to perform regulated activities
- ...particularly in the area of payment services (MT in the US, e-money or p-institutions in the EU)
- ...they rarely hold banking licences
- ...sometimes perform banking functions in partnership with commercial banks

Licences held by big tech companies in selected jurisdictions

Table 2

License held	Licenses and market presence																	
	Brazil			China			European Union			Hong Kong SAR			United Kingdom			United States		
	B	C	P	B	C	P	B	C	P	B	C	P	B	C	P	B	C	P
Amazon									✓						✓			✓
Apple																		
Facebook									✓						✓			
Google									✓						✓			✓
Ant Group			✓	✓*	✓	✓			✓	✓		✓			✓			✓
Baidu				✓*	✓	✓												
JD.com					✓	✓				✓*								
Tencent				✓*	✓	✓				✓		✓						
Mercado Libre			✓															
NTT Docomo							✓		✓						✓			
Rakuten							✓		✓						✓			✓

Market presence in partnership or joint venture with other FIs. (✓) Big tech has entity within group that holds financial licence.

Big tech offers financial services both through partnership or joint venture with other FIs and has entity within group that holds financial licence. (✓*) Shareholding of big techs in these banks is below 50 percent.

B=banking licence. For the EU and UK, CRD credit institution; for Hong Kong, authorised institution; for Brazil, BCB approval under Resolution 4.122/2012 and Circular 3.649/2013; for the US, National Bank Charter or state-level Bank Charters (commercial banks, savings banks, and trust companies). **C=credit licence.** For Hong Kong, money lender licence; for the US, non-bank lender licence (state-level); for Brazil, Sociedade de Crédito Direto or Sociedade de Empréstimo entre Pessoas; for China, internet micro lender or consumer finance licence. **P=payments licence.** For the EU, payment institution or e-money institution; for Brazil, Instituição de pagamento; for the US, money transmitter, sale of checks, money services business (governed primarily by state law); for China, third-party payment licence.

The analysis excludes cases in which payments are made and/or credit is extended for purchasing products and services exclusively within the platform.

Source: EBA Euclid Register; W NMLS® Consumer Access; Encontre uma instituição BCB webpage; HKMA registers; FCA Financial Services Register; various news and reports.

Source: Crisanto, J C, J Ehrentraud and M Fabian (2021): "Big techs in finance: regulatory approaches and policy options", *FSI Briefs*, no 12, March.

4 – A few conceptual preliminaries

- Level playing field is subordinated to other public policy objectives: financial stability, market integrity or, even, fair competition
- Applying same rules to all players only warranted if consistent with those primary objectives
- Seems to be the case in some policy areas: eg AML/CFT, consumer protection
- Not in others (financial stability, operational resilience, competition): risks generated by combination of activities: need for an EB approach
- Unwarranted regulatory discrepancies:
 - If in areas where AB is warranted
 - If in areas where EB rules are required and they are imposed on some but not all classes of entities

5 – The evidence

- Not material regulatory discrepancies for banks and non-banks in policy areas where AB is warranted:
 - AML/CFT rules affect essentially all professional providers of financial services (eg FATF standards, AML Directive EU, BSA in the US)
 - Consumer protection rules apply similarly to all providers of payment services, credit underwriting, wealth management
 - Albeit there could be discrepancies in implementation, monitoring, supervision: a functional rather than a sectoral architecture of supervision would help (eg CFPB in the US)
- No sufficient entity-based rules for large fintech/big techs in areas where EB is warranted
 - On operational resilience: no control of risks generated by combination of activities in big tech platforms
 - On competition: no sufficient ex ante control of possible anti-competitive practices by “gatekeepers”. A major threat to their DNA loop (BIS-AER (2019), Shin (2020))

5 – The evidence (cont)

Recent entity-based initiatives

- To prevent anti-competitive practices
 - US: House antitrust report (Oct 2020)
 - China: SAMAR's guideline (Jan 2021); PBoC's draft rules for payment service providers (Mar 2021)
 - EU: EC proposal for DMA (Dec 2020)
- In the EU, a step forward with EC proposal for DSA (Dec 2020)
 - Controls on operational resilience
 - Requirements on governance and risk management
 - Audit obligations
 - Supervisory regimes

6 – Takeaways

- Need to revise the regulatory framework to accommodate fintechs and big techs
- Contributing to LPF should be an objective but not above others: financial stability, consumer protection, fair competition
- Moving from EB to AB is not, generally, advisable:
 - AB rules already there when warranted (although not always homogeneously applied)\$.
 - Replacing EB with AB may jeopardise financial stability (prudential regulation should remain focused on consolidated balance sheets of banking groups)
- There is a case to rely more on EB rules:
 - To control risk stemming from combination of activities big techs perform
 - Especially in the areas of competition and operational resilience
- That should help:
 - Preserve primary policy goals
 - Limit competitive distortions between banks and fintechs/big techs