



European Financial Services
Round Table

EFR PAPER ON ARTIFICIAL INTELLIGENCE

The European authorities have identified Artificial Intelligence as a promising technology with a high strategic and disruptive potential. For that reason, the European Commission published an AI package on 21 April 2021 proposing actions to maximise Member States' investments on AI as well as the development of an 'ecosystem of trust' through the establishment of harmonised rules on so-called 'high-risk AI systems'.

The financial industry fully agrees on the potential of AI and the need to have a strong leadership in the adoption and development of AI in the EU to stay competitive at global level. This also holds true for financial services, where AI approaches can enable the customization of products to clients' preferences, needs and expectations. Tasks previously done manually can be performed more efficiently and with higher accuracy (for instance, to validate the completeness of the information / documents), improving internal processes by reducing false positives (such as in AML), or enhancing the claims management processes, including improved detection of fraudulent claims. AI can help insurers to refine existing actuarial models or processes, enhancing the availability and innovativeness of insurance for EU customers. While there could be risks related to the development of the AI with misuse, which should be covered by the appropriate regulation, there is also a huge potential for innovation and broader benefits when harnessed correctly that should be fostered. A particularly promising area would be related to risk management, where AI and data analytics can contribute to enhancing financial institutions risk analysis capabilities, both helping more people get access to financing (reducing the number of cases in which a credit is denied to a customer -who might deserve it- due to the lack of 'traditional' credit risk track record), removing unintentional bias in existing processes, while also improving the sustainability and resilience of the financial system (helping to anticipate and manage situations where clients are unlikely to meet their financial obligations).

The Artificial Intelligence Act (AIA) aims to ensure the safety of AI by safeguarding the EU's fundamental rights. While AI systems can vary greatly from one another, it is important that this regulation addresses specific higher risks uses of AI and aims to mitigate these risks for consumers and society at large. Therefore we welcome the risk-based approach followed by the proposed AI Regulation as we think it could support trustworthy AI use cases with embedded EU values.

However, a balance must be struck between ensuring security and raising awareness on potential risks related to AI and fulfilling its innovative potential. We believe that the proposed text must be enhanced to avoid regulatory uncertainties leading to unexpected regulatory burdens and, therefore, hold back the development and adoption of AI in the EU.

As mentioned above, AI provides significant opportunities across different sectors to deliver more suitable products and services to customers. Therefore, educational and awareness raising efforts at member state level would help to build an understanding about the real capabilities and benefits of AI and help to address potential misconceptions, also regarding the Regulation. On the latter, this is particularly important due to the "high-risk" terminology, which could become counterproductive, generating more fear than confidence and trust in users. It would be better to refer to "high-risk" uses of AI systems" instead of "high-risk AI systems". Since this wording is better suited to the objective of the AI Regulation. As a consequence, the EFR argues in this paper that instead of referring to these models as high-risk, once companies comply with this regulation they should be understood by customers as "Trustworthy AI systems".

Three areas where there is room for improvement

The proposed Regulation bans some AI use cases and designates some AI systems as high-risk systems that will have to meet additional requirements on risk management, data governance, transparency and human oversight, among others.

Those requirements will have to be met by at least two AI systems used in Financial Services: (i) creditworthiness assessment and credit score assignment of natural persons, and (ii) AI systems involved in recruitment and employee management.

In addition, the EU Council is considering designating some AI systems used for insurance premium setting, underwritings and claims assessments as high-risk, and the ECB has offered its support for the identification of other financial applications where the use of AI systems could be considered high risk.

Although we believe that the EU authorities have made a great effort to keep the eligible AI systems limited, there are some uncertainties in the Commission's text that, depending on the final interpretation, could significantly increase the final impact of the Regulation.

Those uncertainties can be grouped into three categories: the scope of the Regulation, the requirements imposed and the governance framework.

1. Scope of the Regulation

The high-risk AI systems in the scope of the proposed Regulation are identified according to three criteria: (i) the definition of AI, (ii) the techniques used to develop the system, and (iii) the use case the system is intended to cater for.

There is a risk that the combination of the definition given and the techniques listed in the Regulation can bring into scope any automatic system or system automating even only some basic tasks. For example, at this time many of the standard methodologies typically used in finance and insurance (e.g., linear regression, logistic regression or other statistical methods) could be considered AI and hence would require additional controls. We generally believe this inclusion would be contrary to the purpose of the legislation, which is intended to establish a framework for new and future technology, rather than duplicating the regulation of longstanding financial services activities already covered by a robust regulatory framework.

Moreover, the areas of the 'high-risk use cases' identified in the proposal are so broadly defined that it is not completely clear if use cases having similarities to those areas, such as Anti-Money Laundering and fraud controls as well as biometric identification on device, are out of scope of the Regulation. The text on use cases should therefore clearly state that these are out of scope.

As regards insurance, insurance activities do not meet the "high-risk" criteria set in the proposed AIA. Also, the suitability of the current legal framework comprising specific rules at European and national levels (i.e., Solvency II Framework Directive, IDD), as well as horizontal ones (e.g., GDPR, Gender Equality Directive) provide adequate protection to address potential concerns related to the use of AI systems by insurers vis-à-vis EU citizens' fundamental rights but also involves a strong and dynamic supervision. In fact, EIOPA is assessing the need to issue guidelines on the use of AI by 2024, as stated in the Commission's Digital Finance Strategy.

The inclusion of the creditworthiness and credit scoring assessment as a high-risk application does not appear to meet a clearly defined threshold to determine the risk of an AI system. An accurate assessment on a specific use-case basis would be better. This should be corrected adopting a risk-based approach with clear and transparent criteria with clear thresholds, scope and also application domains. Not only would this better determine high-risk use cases when using AI/ML systems to determine access to credit, it would also de-facto better identify lower-risk use cases. For example, this would not only apply to many creditworthiness and credit scoring assessments but also to the AI/ML use-cases for the marketing of credit products, for internal process efficiency or even in capital consumption models. These applications do not introduce the same risks for the health and safety or fundamental rights of potentially impacted persons, and therefore should not be considered "high-risk". As mentioned before, depending on how the AI is used, it can enable more accurate risk analysis which would be beneficial for customers.

This risk-based approach would complement existing strong prudential and conduct regulation and supervision in the financial services sector, which already ensures compliance with consumer protection, risk management and financial stability for all providers of these services, including those involving the use of AI (for example the EBA Guidelines on Loan Origination and Monitoring). Duplication of obligations should be avoided as far as possible.

In any case, the scope of this use case should not be limited to the financial sector. If access to credit is considered a high-risk use case, then it should be regulated as such for all providers, irrespective of the sector of origin.

We are also concerned about the unintended, sociological and psychological consequences on individuals and businesses of using the wording "high-risk AI system", which could hamper the opportunity for the EU to stay globally competitive through the safe application of AI and its social acceptance. In addition, a number of AI systems would cater for both high-risk and low-risk use cases, therefore a use case-based vs system-based definition would be helpful. In particular, AI technologies used for these solutions could be regarded as less safe than other "non-high-risk" AI systems, despite the fact that the given system has undergone stricter controls. We would advise changing the designation for instance to "Tier 1" for use cases requiring the additional regulatory controls, with perhaps "Tier 4" being the lowest tier applied in-line with non-risk use cases.

2. Requirements

Some articles in the proposed regulation raise concerns:

- Some impose new obligations that are overly onerous such as keeping automatic logs for long periods or developing APIs for remote inspection.
- Some others are not sufficiently specific, when requiring human oversight or data to have 'appropriate statistical properties', for instance.
- Other articles set requirements that do not reflect the actual state of the art or lay down criteria that cannot be met at this moment, such as "having testing data free of errors".
- Others would be very hard to implement in practice, such as processing special categories of personal data to detect unfair bias. While detecting and migrating biases is key, just asking for this specific personal data might raise concerns among customers. It would be beneficial to receive additional guidance on how to deal with this.

The issues above could lead to competent authorities and market operators having different expectations and understanding. As a result, AI operators would probably face more compliance costs and could develop non-effective compliance strategies.

The proposed cross-sectoral AI legislation tackles some data-related issues, such as anti-discrimination, conduct or data protection and privacy concerns, that are addressed by existing regulation and other relevant laws. It is therefore key, that the distinct scope of various regulatory efforts will be maintained to ensure legal clarity to the greatest extent possible. That is, for example, the AI Act should not prescribe requirements for insurance models that might interfere with existing insurance laws and regulations.

3. AI Supervision

The oversight and supervision of this regulation will be done at Member State level. This could lead to several different authorities monitoring and enforcing this regulation according to their own expectations and criteria.

It appears that the European Commission is aware of this potential fragmentation in supervision and, therefore, it is proposing the creation of the EU Artificial Intelligence Board, an advisory agency responsible for coordinating national competent authorities and harmonising criteria.

Regarding the financial use case in scope of this regulation, creditworthiness assessment and credit scoring, the regulation acknowledges the strong regulatory framework applicable to financial services, especially to credit activities. As a consequence, some requirements are deemed fulfilled when the provider is a credit institution meeting the obligations in CRD. Other requirements are expected to be incorporated in processes already implemented by financial institutions following the prudential regulation.

In principle, those specificities could reduce the compliance burden for credit institutions and avoid them having to respond before additional authorities. However, not all firms providing AI systems for the same purpose will be supervised by the same authority (non-financial firms would be supervised by a competent authority to be designated at national level once the regulation is approved) or not even supervised at all (small-scale providers of AI systems intended for creditworthiness assessment or credit scoring are not affected by this Regulation). Therefore, there is a risk that level playing field issues arise between financial and non-financial firms.

Conclusions and policy recommendations

A European AI Regulation that promotes the use and adoption of trustworthy AI embedding EU values should be proportionate and clear. This would avoid creating legal uncertainty or increasing (unnecessary) compliance burden.

In order to achieve these goals, the EFR thinks the EU authorities should take the following recommendations into consideration:

1. Scope of the Regulation

- The definition of Artificial Intelligence should be enhanced to ensure that only systems able to autonomously perform tasks in complex environments without human intervention are in scope of this Regulation.
- The criteria to designate AI use cases as "high-risk" shall be proportionate, clear and stable in order to ease the identification of high-risk uses of AI systems. In addition, both the eligibility criteria and the use cases considered high-risk should only be modified in exceptional and well justified situations.

- AI systems used for insurance activities would not meet the “high-risk” criteria set by the proposed AIA. More precisely, the outcome produced by an AI system in insurance is easily reversible and rectifiable and the policyholders are not reliant on the outcome produced by an AI solution in insurance, since they can decide to opt out. We also question the inclusion of the creditworthiness assessment as a high-risk application, as explained above. The AIA foresees that the proposed list of “high-risk” use cases can be amended (e.g. via delegated acts once the text is adopted). Should emerging insurance and bank use cases be identified and fulfil all the criteria of the proposed methodology, their inclusion to the list would happen in due course, following an appropriate impact assessment.
- Artificial Intelligence use cases having only some similarities with high-risk use cases, without being actually high-risk, shall be unequivocally excluded from the scope of the Regulation. In case this is not possible, some guidance should be developed in order to support the identification of systems in scope by operators and competent authorities.
- The Regulation should refer to “high-risk uses of AI systems” instead of “high-risk AI systems”; or alternatively “Tier 1 use of AI systems”. This new wording is better suited to the objective of the AI Regulation that is not banning the use of AI, but to ensure the application of AI in sensitive use cases does not have unacceptable effects. Following the same logic, the terms “unacceptable-risk AI systems”, “low-risk AI systems” and “minimal-risk AI systems” should be systematically replaced by, respectively, the terms “unacceptable-risk uses (of AI systems)”, “low-risk uses (of AI systems)” or “Tier 2/3” and “minimal-risk uses (of AI systems) or “Tier 4”.

2. Requirements

- Regulatory requirements should be proportionate to the actual risk posed by the system and take into account capacities of modern AI systems.
- The AI Regulation should take into account the cross-sectoral, finance and insurance regulatory frameworks already in place, as well as other legislative initiatives underway, such as the review of the EU liability rules. Any requirement shall be compatible with those in other pieces of legislation. In case of overlap, requirements should be deemed fulfilled for a credit institution or an insurance company if they meet the existing regulatory obligations.
- Regulatory requirements shall be complemented with guidance setting principles that clarify and harmonise supervisory expectations and, therefore, ease compliance with the AI Regulation.
- The transparency requirements (e.g. for the register-Annex VIII) should not hinder the use of fraud detection systems, e.g. for AML purposes. Far-reaching transparency requirements (e.g. for high-risk AI-systems in the future) for fraud detection systems or cyber-attack detection are a concern in the effective use of such systems.

3. AI Supervision

- Level-playing field in supervision and enforcement is essential. The provisions on supervision and enforcement shall ensure that the expectations of supervisors and the enforcement of the regulation are harmonised, i.e. that similar supervision and enforcement is applied to similar activities, and regardless of who engages in them. This harmonisation of practices would be more easily attained if all the competent authorities were subject to the EU Artificial Intelligence Board criteria.
- Authorities supervising Artificial Intelligence should have the resources and capabilities necessary to keep up with the technology and provide well informed oversight.

The European Financial Services Round Table (EFR) was formed in 2001. The Members of EFR are Chairmen and Chief Executive Officers of international banks or insurers with headquarters in Europe. EFR Members believe that a fully integrated EU financial market, a Single Market with consistent rules and requirements, combined with a strong, stable and competitive European financial services industry will lead to increased choice and better value for all users of financial services across the Member States of the European Union. An open and integrated market reflecting the diversity of banking and insurance business models will support investment and growth, expanding the overall soundness and competitiveness of the European economy.