Consultation Response

Inception Impact Assessment - Proposal for a Legal Act of the European Parliament and the Council Laying Down Requirements for Artificial Intelligence

10 September 2020

The Association for Financial Markets in Europe (AFME) welcomes the opportunity to comment on **INCEPTION IMPACT ASSESSMENT - PROPOSAL FOR A LEGAL ACT OF THE EUROPEAN PARLIAMENT AND THE COUNCIL LAYING DOWN REQUIREMENTS FOR ARTIFICIAL INTELLIGENCE** (the "Impact Assessment"). AFME represents a broad array of European and global participants in the wholesale financial markets. Its members comprise pan-EU and global banks as well as key regional banks, brokers, law firms, investors and other financial market participants. We advocate stable, competitive, sustainable European financial markets that support economic growth and benefit society.

AFME is the European member of the Global Financial Markets Association (GFMA) a global alliance with the Securities Industry and Financial Markets Association (SIFMA) in the US, and the Asia Securities Industry and Financial Markets Association (ASIFMA) in Asia.

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We summarise below our high-level response to the Impact Assessment, which is followed by answers to the individual options proposed.

Executive Summary

The capital markets industry is keen to engage with authorities to develop AI in Europe, building understanding and skills and maintaining high standards for its use. Increased public-private partnership should be a key focus.

Regulation should remain technology-neutral and principles-based. Regulation should also avoid creating unnecessary barriers to innovation and the development and adoption of AI by firms. Regulation which focuses on a particular technology (such as a specific AI application) is less effective as it does not address underlying behaviours or practices, for which a technology is simply a tool to perform. Given the speed of technological advances, technology-specific regulation will struggle to maintain pace with developments in its use and risks creating barriers to the adoption of new and innovative technologies.

In relation to the options discussed in the Impact Assessment, we support Option 1, "Soft Law" Approach, since it could effectively take into account existing regulations and developments in sectors that are comparatively mature in their use of AI, rather than imposing a one-size of its all regulatory approach.

As general principles, AFME believes that any additional requirements for AI within the EU should:

- Take into account existing regulation, particularly for highly regulated sectors such as financial services. This would reduce the risk of duplication with existing regulatory requirements;

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- Be tailored to the level of risk of particular uses of AI, such as by being limited to 'high-risk' activities that are not covered by existing regulation; and
- Be applied to the activity being undertaken, regardless of whether the use of the AI application is by a regulated entity in a particular sector, to ensure a level playing field across all firms.

Finally, we encourage the Commission to continue consultation with all industry sectors on its proposals, beyond those which are designated as high risk, to ensure that the resulting framework is suitable and draws on experiences of working successfully with AI.

Comments on the Policy Options

We draw the Commission's attention to our response to its consultation on its white paper 'Artificial Intelligence – A European Approach to Excellence and Trust' (the "White Paper") earlier in 2020.[1] In an appendix to our response, we set out our views, which are also included below in respect to each of the policy option presented in this Impact Assessment.

In that appendix, we also suggested a revised definition of AI, based on the definition[2] provided by the Commission's High Level Expert Group (HLEG) on AI:

> *"Artificial intelligence (AI) systems are systems that act in the physical or digital world by perceiving their environment through data acquisition, interpreting the collected data, reasoning on the knowledge, or processing the information, derived from this data and identifying the best action(s) to take to achieve the given goal. AI systems may adapt themselves or their own algorithms by analysing how the environment is affected by previous actions, knowledge or data."*

Option 0 – No EU Policy Change

Regulation should remain technology-neutral and principles-based, recognising that technologies such as AI are merely tools. Regulation should also avoid creating unnecessary barriers to innovation and the development and adoption of AI by firms. Regulation which focuses on a particular technology (such as a specific AI technique) is less effective as it does not address underlying behaviours or practices, for which a technology is simply a tool to perform. Given the speed of technological advances technology-specific regulation will struggle to maintain pace with developments in its use and risks creating barriers to the adoption of new and innovative technologies.

However, we acknowledge that the Commission may consider that there are gaps in the existing regulatory framework which it wishes to address.

Option 1 – EU "Soft Law" (Non-legislative) Approach

Capital markets is a highly regulated industry and from that perspective AFME would support Option 1. This would limit the creation of unnecessary barriers to innovation and the development and adoption of AI by firms. Those sectors that are highly regulated have already had to develop processes and safeguards for identifying and mitigating a variety of risks. For example, in financial services, firms are under obligations relating to areas such as consumer protection, conduct risk, duty to clients, internal governance, third-party risk management, technology, cloud, outsourcing, operational resilience and data privacy and model risk management. Many of these will already mitigate the risks related to firms' AI use, throughout the lifecycle of any AI application, and will also drive firms' own initiatives to nurture the safe development of AI.

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1 https://www.afme.eu/Portals/0/DispatchFeaturedImages/20200612%20AFME%20EC%20AI%20CP%20Response%20-%20Final .pdf

2 https://ec.europa.eu/digital-single-market/en/news/definition-artificial-intelligence-main-capabilities-and-scientific-disciplines

These processes will be tailored to the needs and specificities of that sector, and (in relation to AI) to the different levels of risk of the AI applications. The imposition of an additional regulatory framework may conflict with the work done to date and would be less effective as a risk mitigation tool.

For these highly regulated sectors, if, following an analysis of existing sectoral regulation (which should also include relevant data and privacy laws/regulations) residual concerns are identified, the Commission should consider its full toolkit of regulatory and non-regulatory measures to determine the most effective solution. This could range from cross-sectoral principles, targeted guidance, and supervisory adjustments, among others, not only legislative amendments.

For example, it may be more helpful in many sectors, where applicable regulation already exists, for existing rules to be applied in a technology-neutral way and for authorities to assist firms in how to meet supervisor's expectations (for example to avoid unjustifiable discrimination or achieve suitable levels of interpretability). A strong public-private partnership, as highlighted in the actions to build an Ecosystem of Excellence, will aid both institutions and public authorities to share information and further understanding on AI techniques and methodologies to address concerns outlined in the white paper.

This may be done in conjunction with a review of the regulatory perimeter, where activity by non-regulated firms may bring new risks. This could assist in creating a harmonized framework of regulators and supervisors' expectations on AI applications depending on the level of risk they pose.

<u>Option 2 – EU Legislative Instrument Setting Up a Voluntary Labelling Scheme</u>

AFME has concerns relating to the proposal for a voluntary labelling system for AI applications and would not support option 2. We discuss this in more detail below.

The awarding of a quality label introduces an element of market discipline; it would be difficult to ensure that such systems would remain market-driven, and therefore truly voluntary, and not become effectively mandatory.

A voluntary labelling scheme also cuts across the principle that the object of trust should not be AI as a technology, but firm using a given AI application. This should be a focus of education about the use of AI in the EU; clearly explaining the benefits and dispelling the myths that may have arisen about the technology.

Practicality

In relation to how such a system would work in practice, it is likely to be disruptive and even a voluntary system imposes disproportionate obligations, such as audit costs. This is also a potential consideration for the High Level Expert Group Guidelines for Trustworthy AI (HLEG Guidelines), for which the Assessment List runs to several pages and more than 50 items; significantly more than is necessary for many low-risk uses of AI. Any firm which decided to certify certain AI applications would need to be assured that it was clearly beneficial for themselves and for their clients.

A voluntary labelling system would also be very difficult to tailor to a specific application or use case. This specificity would be necessary for a truly accurate assessment to be made. This lack of specificity would become apparent in the applicability of the criteria to each AI application, in the definition of each criterion across different participating firms (e.g. how would you define 'accuracy' in a comparable sense), and in that such a system would not be able to take into account the individual risk thresholds and management framework of any participating firm.

Consumer Benefit

Furthermore, it is not clear that enough consideration has been given to how a voluntary labelling system could be useful to consumers, or how it would be presented. For instance, there would be no commentary to explain why any given AI application had, or did not have, the label applied (which would be key in a voluntary, market-driven system). This would be particularly detrimental to those applications for which the labelling system was

inappropriate or insufficiently accurate/specific, or for which it would create disproportionate cost or disruption. It is also unclear what the label would convey to the consumer; there is therefore a risk that an insufficiently specific voluntary labelling system (that under the current proposals would then in effect become mandatory and set the market benchmark) would actually cut across the principle of human autonomy, by misleading or confusing customers with incomplete information.

It is worth noting that the above considerations are in respect of a voluntary labelling scheme as proposed in the White Paper and Impact Assessment. There can be instances where voluntary disclosure on a more general basis is useful for consumers, particularly in instances where disclosing to consumers that they are interacting with an AI system rather than a human.

Option 3 – EU Legislative Instrument Establishing Mandatory Requirements for All or Certain Types of AI Applications

As noted in our comments above under Option 0, we strongly believe that regulation should remain technology-neutral and principles-based, recognising (i) that the risks applicable to the use of AI are also applicable to the use of many other types of technology and (ii) that the object of trust should be the user of the technology (i.e. a firm), not an individual type of technology itself. Regulation or policy which focuses on the specifics of a technology, as opposed to the core obligations and principles to ensure the trustworthiness of the technology provider or user, could negatively and unnecessarily impact the adoption of AI within Europe.

Consideration of the sub-options

- Sub-option 1, to focus on a limited category of AI applications

Focusing on a limited category of AI applications, , such as biometric identification systems, could be a suitable approach, as the legislative instrument could be tailored to systems that present specific risks.

This would help to narrow the criteria and scope of AI applications to those with the greatest perceived risk to safety, fundamental rights, and discrimination. However, further thought and consultation would be needed on the criteria for determining the category and how these would be kept up to date.

- Sub-option 2, to focus on a limited set of 'high-risk' AI applications

Focusing on 'high risk' AI applications could be a suitable approach, provided that the definition of 'high-risk' is set appropriately within the legislative instrument. We discuss this in more detail below.

Focus on High Risk Applications

AFME supports the Commission's focus on safety and fundamental rights. Limiting any new requirements to those applications that may pose a real and relevant risk to citizens (e.g. on their safety or physical integrity) will prevent these requirements from creating barriers to innovation and inhibiting the broader development of AI in Europe. This focus on safety should be the foundation, to ensure a consistent application of the requirements across any activities to which they are applied, based on comparable risks.

On this basis, and given the highly-regulated nature of financial services noted above in our comments on Option 1, AFME is of the view that financial services is not a high-risk sector, particularly noting the comments below.

However, we also feel that the EU is a leader in protecting consumers and fundamental rights. It is crucial that the regulatory landscape for AI in Europe appropriately balances risk reduction with fostering innovation, allowing firms in Europe to harness the benefits of AI and maintain their competitive position globally; particularly in key sectors for the European economy. In assessing the approach to high risk applications, we recommend the Commission consider the comments made on highly regulated sectors under Option 1 above, as well as the following on unintended consequences.

We note that the designation of a sector as 'high-risk' may also create unintended opportunities for regulatory arbitrage. Where an activity can be performed by a firm from outside the designated sector (or from outside the EU), this firm would be in a position to provide products or services which utilise in-scope high-risk AI applications to consumers, without adhering to the new regulatory obligations intended to ensure trustworthy AI. To ensure that citizens' safety and fundamental rights are well protected, and to avoid creating an unlevel playing field among firms, once an application has been identified as high-risk, the Commission should ensure it is appropriately covered by the regulatory framework regardless of sector, following the principle of "same activity, same risks, same rules."

In addition, we also request clarity on the criteria to be considered to designate high-risk activities (specifically on how to evaluate "that significant risks are likely to arise"), the procedure to follow and the body responsible for making the decision. This assessment would presumably have to be performed by a central authority, rather than on a firm-by-firm basis. It would therefore fall either to the Commission or, given their specialist expertise, to sectoral authorities. The latter would, however, be limited by their own regulatory perimeter in terms of the activities or entities they supervise. We would like to emphasize again that in order to ensure a consistent framework the focus on safety and citizens' fundamental rights should be the foundation to evaluate, including a new activity in this framework, ensuring that the same requirements are applied based on comparable risks.

Further Consultation

Finally, we note that the regulatory approach for high-risk activities as proposed in the Impact Assessment will need refinement via further consultation once the scope has been defined. This will be important not just for any sectors categorised as high-risk, but also more broadly to allow all industry sectors to comment on how the regulatory approach will apply to individual high-risk applications. Furthermore, it will allow the sharing of experiences from sectors that are already highly regulated, such as financial services.

- Sub-option 3, to focus on all AI applications

We believe that focusing on all AI applications would not be a suitable approach. As noted in our comments under Option 0 above, this would create unnecessary barriers to innovation and the development and adoption of AI by firms. We also note that capital markets is a highly regulated industry, and our comments are made from this perspective.

<u>Option 4 – Combination of any of the options above taking into account the different levels of risk that could be generated by a particular AI application</u>

As outlined in our comments under Option 1 above, the Commission should consider its full toolkit of regulatory and non-regulatory measures to determine the most effective solution. This could range from targeted guidance, and supervisory adjustments, among others, not only legislative amendments.

Comments on the Preliminary Assessment of Expected Impacts

Further to our comments above, we strongly support that the following are taken into account in any cost-benefit analysis of a new approach to AI:

- That any new requirements should be risk-based, rather than broadly applied, to prevent unnecessary barriers being placed on the development of AI applications;
- That existing regulatory requirements should be taken into account, to avoid duplication or conflicting obligations being placed upon firms;
- That a level playing field should be created and maintained, i.e. that the requirements should apply to specific activities, regardless of the size, or regulatory status of the firm performing the activity

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