Insurance Europe response to EC targeted consultation on AI in the financial sector

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Introduction

1.3 Challenges and risks when using AI applications in financial services

> **Question 12.** *AI may affect the type and degree of dependencies in financial markets in certain circumstances, especially where a high number of financial entities rely on a relatively small number of third-party providers of AI systems. Do you see a risk of market concentration and/or herding behaviour in AI used for financial services?*

The European Central Bank (ECB) has recently acknowledged[1] that the widespread adoption of AI in the financial services industry could lead to increased market concentration. This recognition highlights the potential for a small number of AI providers to dominate the sector, raising concerns about systemic risk and market resilience.

The financial services industry's adoption of AI solutions and architecture from well-known third-party providers, driven by their trustworthiness and reliability, might unintentionally have an impact on competition and increase concentration in the market. However, ease of access to AI development, due to lower entry barriers, may well balance out the risks of concentration, nurturing a competitive landscape that champions diversity and innovation.

It should be added that market concentration risks can arise across a diverse range of ICT-related services but may be particularly significant with cloud solutions. Given that cloud solutions and access to computational resources are essential for deploying AI models or systems, and that these solutions are largely offered by a small number of international providers, introducing EU-wide schemes or requirements that would limit the number of cloud offerings available to the financial sector would further reduce the number of potential suppliers and exacerbate the potential for any market risk.

To address any potential risks of market concentration, regulatory bodies could play a role in promoting competition in AI systems and raising the awareness of financial institutions about the potential risks related to the excessive dependence on a single AI provider. Additionally, financial institutions could take proactive steps

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[1] [The rise of artificial intelligence: benefits and risks for financial stability](#). ECB, May 2024

to diversify their AI strategies, such as using multiple AI providers, regularly evaluating AI systems or developing in-house capabilities where feasible.

Another challenge faced by the financial sector is the skills gap. While there is a high demand for AI development, there is a shortage of skilled professionals in this area. Additionally, financial service providers encounter integration challenges. Integrating AI technologies with existing systems and processes can be both complex and costly.

1.4. AI and compliance burden

Question 13. *Can AI help to reduce the reporting burden?*

AI may be able to help with the creation of narrative report sections or the consolidation of different aspects of reporting obligations. In this respect, it can offer certain time-saving benefits. However, the fundamental scope and responsibility of reporting obligations will not change as a result. It is important to ensure that the use of AI to support the fulfilment of reporting obligations does not lead to further reporting obligations due to the use of AI. This would run counter to the positive effects of using AI (minimising time and effort).

Question 14. *Do you think AI can facilitate compliance with multiple regulatory standards across the EU and thus facilitate market integration or regulatory compliance? For example, would you consider it feasible to use AI for converting accounting and financial statements developed under one standard (e.g. local GAAP) to another standard (e.g. IFRS)? Please elaborate.*

The insurance industry does not believe that it would be feasible for AI to convert accounting and financial statements developed under one standard (eg local GAAP) to another standard (eg IFRS). Similarly, it would not seem feasible that AI itself would be able to perform recalculations, as it lacks the necessary insight into the deep granularity of internal data required for such a purpose.

1.5. Data access

Question 19. *Should public policy measures (e.g. legislative or non-legislative) encourage the exchange of data between market participants, which can be used to train AI systems for use cases in finance?*

Any initiative in this field should be aligned with other EU legislative approaches to data sharing, such as the Data Act, where clear provision has been made for a right of compensation for the original data holder. AI developers would clearly be obtaining an objective benefit from access to stores of data that could be used to train AI systems and allow them to fine-tune their uses, protocols and knowledge. This should therefore have a consequence in terms of compensation.

It is critical, however, that any such measures are carefully crafted to balance the benefits of data exchange with the protection of business-sensitive information, the safeguarding of intellectual property and the maintenance of fair competition in the market. In the insurance area in particular, it is of critical importance to duly protect customers' data privacy, with a particular focus on sensitive issues such as health status and information.

Consideration could also be given to the use of federated learning within the insurance sector, an advanced machine learning technique that enables companies to collaborate on a machine-learning model without having to share their raw data with each other or with a central server. Consolidating aggregated risk information in this way would allow insurers to improve their predictive models while maintaining data privacy, making it useful for applications such as fraud detection models.

1.6. Business model

> **Question 21.** *Which parts of the value chain are being improved with AI?*

AI models have proven the ability to improve several parts of the insurance value chain, such as product definition, underwriting, risk management, customer service, claims handling or fraud detection. AI can improve operational efficiency, speed up internal processes, and improve customer satisfaction through the automation of tasks. It can also enhance risk management and support decision-making by processing large amounts of data and delivering insights.

■ Improved customer experience

Consumers are embracing the use of AI in insurance, particularly where it makes their interaction more convenient and improves communication. With AI-supported text recognition systems, customer requests can be processed much faster. Consumer-facing chatbots, for example, are used by insurers across a range of different platforms. Chatbots can ensure 24/7 availability of customer service and can help to simplify and speed up the interaction between insurers and their customers.

■ More efficient claims handling

The satisfaction of customers with their insurance company often depends largely on claims handling. AI solutions can help insurers automate and speed up the claims settlement process. For example, policyholders can upload images of the damage shortly after an accident via a smartphone application. Thanks to AI-based image recognition, these are analysed automatically so that a decision on repairs or the amount of damage can be made within a few minutes as well as a corresponding cost estimate. Of course, policyholders have the right to a review at any time.

■ More effective fraud detection

AI-driven fraud detection solutions can tackle the problem of fraud by analysing massive amounts of data from multiple sources in order to spot fraudulent claims. These tools can enable insurers to spot and flag unusual patterns that a human might miss, potentially helping to reduce these huge costs, as well as the level of customer premiums.

■ Better risk monitoring and prevention

As the insurance industry focuses more on prevention, AI systems can be used to help monitor and predict risk, as well as to provide advice to customers on how to reduce risk going forward. This can in turn help to reduce the frequency and severity of losses over time. AI applications can also offer the opportunity for lower insurance premiums for customers. For example, in car insurance, AI can monitor and analyse driving behaviour through data collected by smartphone apps or plug-in devices. Customers can then receive a discount on their premium, depending on how they drive, and can also get further insights into their driving behaviour to help them improve over time.

> **Question 22.** *Are there functions that cannot/would not be improved by AI?*

The insurance industry believes that there are certain functions that would not be improved by AI, such as tasks that require strategic thinking or involve expert knowledge about customers, markets or the macroeconomic or regulatory context. Additionally, roles that rely on human attributes such as creativity, empathy, intuition and ethical judgement, as well as positions like client relationship managers, R&D roles, and some leadership functions, are areas where AI may fall short.

1.7. General purpose AI

> **Question 26.** *Compared to traditional AI systems such as supervised machine learning systems, what additional opportunities and risks are brought by general purpose AI models?*

General purpose AI (GPAI) models are currently being assessed by the industry from the point of view of their opportunities and risks. At present, the main observed benefits are linked to supporting employees in their daily

tasks through functions such as cognitive assistants, which help streamline workflows and enhance productivity by automating routine activities.

Additional opportunities brought by GPAI include increased flexibility and scalability, which allow for a broader range of applications while reducing development and integration costs. GPAI also promotes the democratisation of AI, making advanced tools accessible to users who may lack technical expertise.

However, GPAI models may also introduce risks that require careful governance. The main risks include data privacy concerns, lack of transparency regarding training datasets, dependency, improper application, ethical dilemmas, and challenges related to governance, control, and accountability of GPAI responses. To address these challenges, legislators, creators and end-users could better collaborate to develop frameworks and guidelines. These should aim to leverage the positive aspects of GPAI while mitigating its risks, ensuring its integration aligns with collective societal principles and objectives.

Traditional accuracy-metrics are not useable in the case of GPAI models, as answers to the same question can differ for each query. It is not possible to directly measure accuracy in percentage terms for a test dataset – or via random samples – as with traditional AI. This would increase the need for human oversight or at least mean that such models are only used in limited cases. This is an area that is currently receiving a high degree of focus from AI developers, so new technical solutions can be expected to allow for better accuracy and accuracy-measurements going forward.

> **Question 27.** *In which areas of the financial services value chain do you think general purpose AI could have a greater potential in the short, medium and long term?*

The insurance industry believes that GPAI models could demonstrate potential in customer service, where it could assist employees in delivering relevant information efficiently and respond to a wide range of customer queries, regardless of how the questions are formulated. It can also assist in interpreting image and text input from customers. At the individual case level, it could be used to prepare draft decisions to be reviewed further by case handlers, which could potentially happen with greater levels of automation over time once proven.

1.9. Forecasts

> **Question 30.** *What are the main evolutions to be expected in AI in finance?*

Given the high volatility and rapid evolution of AI technology, Insurance Europe would recommend a cautious approach to making forecasts about future AI capabilities. The unpredictable nature of AI development makes it challenging to establish stable, long-term predictions about its future impact on the financial sector.

> **Question 31.** *Which financial services do you expect to be the most impacted by AI?*

The relevance of AI in financial operations is influenced by two key elements. The first is the volume of back-office operations linked to the financial institution's offering, with forecasts suggesting that the initial deployment of AI in finance will primarily target these tasks. The second element is the nature of customer interactions – the more routine and consistent these are, the greater the likelihood that AI solutions will deliver value for both the customer and the financial institution. These elements are pivotal in determining how effective AI will be in the financial domain.

3.2. AI Act requirements

> **Question 40.** *Bearing in mind there will be harmonised standards for the requirements for high-risk AI (Mandates sent to CEN-CENELEC can be monitored here), would you consider helpful further guidance tailored to the financial services sector on specific AI Act requirements, in particular regarding the two high-risk AI use cases?*

Insurance Europe notes that there are several definitions or terms used in the AI Act that are still unclear.

The reference to insurance as high-risk in Annex III refers to life and health insurance, as well as risk assessment and pricing. However, a broad interpretation of each of these individual terms - risk assessment, pricing, health insurance, and life insurance - would mean that many scenarios are included in scope, potentially extending far beyond the original intent of what was meant to be covered. Health insurance, for example, can cover everything related to health, eg health insurance, accident insurance, work-related injuries, critical illness, etc. Life insurance could also be interpreted to overlap with areas such as critical illness or loss of livelihood. Health insurance should not cover work-related injuries, accidents, loss of livelihood, critical illness, etc, while life insurance should only include insurances that come into effect upon death.

Similarly, it would be beneficial to have a clear and harmonised idea of how "risk assessment" should be understood in the context of high-risk AI systems. Insurers engage in numerous risk assessments and calculations that are not directly related to the individual customer, eg of an actuarial, financial, macroeconomic or commercial nature. Models designed for such risk assessments should be clearly excluded from the high-risk scope since they do not affect customers' rights in any way. Risk assessment and pricing should effectively be understood as "premium setting" in an insurance context.

The use of AI for fraud detection purposes has been excluded from the scope of high risk in the AI Act recitals for all financial services. However, due to a difference in the wording of the respective high-risk provisions in Annex III, insurance is not explicitly mentioned, with the focus placed solely on credit worthiness assessments. Clear guidance should be given to confirm that fraud detection in the insurance sector is not captured under the high-risk provisions.

The same goes for the definition of an AI system. Statistical analysis and modelling have for centuries been core to the insurance business model and used for a range of key activities including pricing, reserving, risk management, capital allocation, marketing and product development. Statistical analysis and modelling are also necessary for the calculation of data required under the various reporting obligations for insurers including for Solvency II, financial reporting and sustainability reporting. Such existing statistical analysis and modelling, including Generalised Linear Models (GLMs), can be distinguished from AI tools and methods because they do not operate with autonomy or exhibit adaptiveness after deployment. Therefore, such statistical analysis and modelling (including GLMs) that do not operate with autonomy or exhibit adaptiveness, are outside the scope of the AI Act. Explicit clarification of this fact would help avoid ambiguity and unnecessary burdens for companies and supervisors regarding existing statistical analysis and modelling. This would allow resources to be focused on newer tools that fall within the scope of AI, which may present new risks and thus warrant the consideration of new regulatory requirements.

The AI Act also includes provisions specifying that financial institutions already subject to EU financial services legislation should take these requirements into account when considering their obligations under the AI Act. For example, the obligation in Article 17(4) to put in place a quality management system, or the technical documentation requirements in Article 18(3). Further guidance in these areas, which clearly outlines what is expected of financial institutions, would be welcome.

AI systems used by public authorities, or on their behalf, to assess the eligibility of individuals for essential public assistance benefits and services, as well as to grant, reduce, revoke, or reclaim these services, are classified as high-risk AI systems. In some member states, Motor Third Party Liability (MTPL) and workers' compensation insurance that are provided by private insurance companies are considered part of the social security system. It is unclear if these should be considered as high-risk AI systems. The treatment of such insurance products should be equal across member states, and therefore these should not be considered high-risk AI systems. However, this is not currently clear.

3.3. Financial legislation requirements

> **Question 41.** *Future AI high-risk use cases would also need to comply with existing requirements from the financial legislation. Would you consider helpful further guidance meant to clarify the supervisory expectations for these use cases?*

No.

> **Question 42.** *There are other use cases in relation to the use of AI by the financial services sector which are not considered of high-risk by the AI Act, but which need to comply with the existing requirements from the financial legislation. Would you consider helpful further guidance meant to clarify the supervisory expectations for these use cases?*

No.

> **Question 43.** *Are you aware of any provisions from the financial acquis that could impede the development of AI applications (e.g. provisions that prohibit the use of risk management models which are not fully explainable or the use of fully automated services for the interaction with consumers)?*

Several provisions in the EU financial acquis could impede the development and deployment of AI applications, particularly those focusing on explainability, transparency, and consumer protection. Key regulations include the GDPR, which addresses automated decision-making and the right to explanation; the Insurance Distribution Directive, emphasising product oversight and governance; anti-money laundering and counter-terrorism financing (AML/CTF) regulations, that require Know Your Customer and Customer Due Diligence processes. While these regulations aim to protect consumers and ensure financial stability, they may inadvertently hinder innovation in AI-driven financial services. Balancing the need for consumer protection with the promotion of AI innovation will be a critical challenge for regulatory and financial institutions.

For example, there are currently no clear legal grounds for the training and testing of new IT applications and systems using special categories of personal data (eg health data). Although the provision in Article 10(5) of the AI Act introduces some form of legal basis, it is limited to the development of high-risk AI systems and only applies to the extent that it is absolutely necessary for detecting and correcting bias. Exceptions to the prohibition on the processing of special categories of personal data are set out in Article 9 of the GDPR but these are narrowly interpreted. Depending on the specific purpose of the processing of the special categories of personal data for the preparation of the training of the AI system (eg collection and categorisation of the data) and the application of the AI system, the legal basis pursuant to Article 6(1) in conjunction with Article 9(2) GDPR may vary.

In addition to the requirements of the AI Act, Article 22 of the GDPR must be taken into account for fully automated decisions. According to this provision, fully automated decisions with legal effect are generally prohibited. This provision does not make any reference to the development of AI applications; however, as the use of applications for fully automated decision-making is not permitted under this provision, it also limits the development of AI applications. Unfortunately, the exceptions to this requirement are interpreted too narrowly in an insurance context, as fully automated decisions are generally not deemed to be 'necessary' for the insurance contract within the meaning of Article 22.