

Global Financial Innovation Network (GFIN)

Consultation document

August 2018



ABU DHABI GLOBAL MARKET
سوق أبوظبي العالمي



AUTORITÉ
DES MARCHÉS
FINANCIERS



ASIC
Australian Securities & Investments Commission



مصرف البحرين المركزي
Central Bank of Bahrain



Bureau of Consumer
Financial Protection



Dubai Financial
Services Authority



FINANCIAL
CONDUCT
AUTHORITY



Guernsey Financial
Services Commission



HONG KONG MONETARY AUTHORITY
香港金融管理局



Monetary Authority
of Singapore



ONTARIO
SECURITIES
COMMISSION



Contents

1	Executive summary	3
2	Introduction	4
3	Mission statement	6
4	Functions	8
5	Next steps	14
Annex 1		
	List of questions	16
Appendix I:	Regulatory sandboxes in financial services	17
Appendix II:	Summary of ASIC’s regulatory sandbox exemption	19

1 Executive summary

- 1 The major emerging innovation trends within financial services are increasingly global, rather than domestic, in nature. For instance, big data, artificial intelligence (AI), and blockchain based solutions are being developed and deployed simultaneously in different financial markets. Since there is a general trend towards developing these digital solutions, now is a time to consider how to begin building new ways to share experience and manage the questions that emerge. Financial services regulators must re-consider existing ways of working and collaborating, in order to balance potential benefits of innovation (for consumers and the financial sector as a whole) with traditional policy objectives, namely financial stability, integrity, financial inclusion, competition and consumer wellbeing and protection.
- 2 This paper follows a proposition document published by the UK Financial Conduct Authority (FCA) in February 2018 on the idea of a “global sandbox” and provides an update on the next steps of the project. We believe the idea has sufficient merit to continue exploring, with the view to expanding the innovation activities currently undertaken by financial services regulators around the world.
- 3 As the project has evolved, so has the potential operational model. As such, we have revised the name of the group to the Global Financial Innovation Network (GFIN). This reflects the broad nature and scope of the group, and whilst the concept of a sandbox remains a component of the group’s function, this is only one tool available. We also believe there is an opportunity for those regulators currently without sandbox type environments to participate in the different functions listed below.
- 4 The introduction to this paper provides a background to the discussion, including the key themes to emerge in the initial informal consultation. It then sets out a mission statement, which outlines the role we see the GFIN playing in supporting responsible innovation. We believe the GFIN could serve three main functions: act as a network of regulators to collaborate, sharing experience and best practice, and communicate to firms; provide a forum for joint policy work; and provide firms with an environment in which to trial cross-border solutions (business to consumer (B2C) or business to business (B2B)).
- 5 The remainder of the paper then takes each of these areas in turn and sets out the justification for why we feel they constitute an important part of the GFIN, including how we potentially see it operating in practice, in conjunction with industry and other policy making organisations.

Who should read this paper

- 6 We encourage innovative financial services firms, financial services regulators, technology companies, technology providers, trade bodies, accelerators, academia, consumer groups and other stakeholders keen on being part of the development of the GFIN to respond to the questions in the paper.

2 Introduction

- 7 The growth of FinTech in financial services has led regulators from around the world to create initiatives designed to engage with, and respond to, these emerging business models, services, and products. Such activities have aimed at achieving three outcomes: First, bringing about improvements to the broader financial services market that benefit consumers and other market participants. Such improvements could be in the form of new and/or more accessible consumer products, or in the development of new technologies to facilitate the delivery of regulatory requirements (RegTech). Second, ensuring regulatory authorities understand the latest market and technological developments. Third, working with these innovative firms to help them understand what regulatory requirements they need to meet.
- 8 Some regulators have sought to achieve such outcomes by utilising regulatory sandboxes to allow firms to trial new products or services, while other regulators have supported firms through an innovation department or accelerator. Appendix I provides an overview of the idea of regulatory sandboxes in financial services. Other regulators have sought to harness the potential of new technology to improve the way they carry out their supervisory functions (SupTech). Some regulators are engaging in all or a combination of these approaches.
- 9 Following an initial proposition document on the idea of a “global sandbox” issued by the UK’s FCA in February 2018, 50 responses were received which expressed positive sentiment about the idea of regulators collaborating in this respect. Responses also highlighted the benefit it could potentially deliver consumers through the introduction of innovative new products or services, and to the firms looking to bring these ideas to market. Key themes to emerge in the feedback were:
 - **Regulatory co-operation:** providing an environment for regulators to collaborate on common challenges or policy questions firms face in different jurisdictions. It was also highlighted how under the present conditions it can be challenging for a company looking to engage with different regulators on a bi-lateral basis.
 - **Regulatory engagement:** a space where industry can engage with a broader group of regulatory stakeholders on a single topic or policy question.
 - **Speed to international markets:** could reduce the time it takes to bring ideas to international markets. The cross-border potential of emerging technologies (e.g. encryption technology) or business models was also highlighted as important, since firms have ambitions to grow their footprint beyond their domestic market.
 - **Governance:** Must be transparent and fair to those potential companies wishing to apply for cross-border testing. Respondents offered a range of potential models for testing, such as transitioning from a domestic sandbox into a “global sandbox”, or TechSprints similar to those organised previously by the FCA.
 - **Emerging technologies/business models:** A wide range of topics and subject matters were highlighted in the feedback, particularly those with notable cross-border application. Among areas highlighted were AI, distributed ledger technology, data protection, regulation of securities and Initial Coin Offerings (ICOs), know your customer (KYC) or anti- money laundering (AML), and green finance.
- 10 Subsequently, the FCA convened an event during March 2018 with a group of international stakeholders to discuss the opportunities the GFIN could deliver, based on the market feedback from the initial consultation. After the event, a number of stakeholders who attended agreed there was merit in developing the idea further, and committed to take part in a consultation process.
- 11 The objectives of the group were to work towards producing this consultation document, expanding on the initial ideas and to design an operating framework for the GFIN. A wider group of stakeholders expressed an interest

in being kept informed on the main group's progress. This document sets out the views of those organisations listed, however, we would welcome further participation and interest from other regulatory bodies or related organisations, building on the ideas set out in this document.

3 Mission statement

- [Proposed] The GFIN is a collaborative policy and knowledge sharing initiative aimed at advancing areas including financial integrity, consumer wellbeing and protection, financial inclusion, competition and financial stability through innovation in financial services, by sharing experiences, working jointly on emerging policy issues and facilitating responsible cross-border experimentation of new ideas.

Why

- 12** The desired outcome of this initiative is a global financial services system that better serves broader society through harnessing new technology to provide an overall improved level of service and experience, and integrity. It is also to create a new framework for cooperation between financial services regulators, which complements the work of other standard setting organisations who are assessing financial innovation.
- 13** The pace of technological change, including the development of emerging technologies and business models in financial services, requires regulatory authorities to adapt to this new landscape and devise new ways of cooperating. This is because emerging technologies and business models are presenting regulators with questions around how firms can meet the necessary regulatory requirements, whilst harnessing these tools.
- 14** We believe the GFIN offers an agile way for financial services regulators to work collaboratively, to conduct joint work and share their experiences of financial innovation, thereby improving financial stability, integrity, customer outcomes and inclusion, through supporting the responsible adoption of these emerging technologies and business models. We believe the GFIN should be agile in the sense that the network learns through activity and shares this knowledge in order to improve and iterate on existing regulatory approaches.¹
- 15** The GFIN is designed to be an inclusive community of financial services regulators and related organisations. The network will seek to provide a more efficient way for innovative organisations to interact with regulators, helping them navigate between jurisdictions as they consider and look to scale new ideas.

What

- 16** We see the GFIN achieving this through three main functions that complement each other:
 - a. Network of regulators** – a community of regulators and related organisations that promotes information and knowledge sharing on emerging innovation trends, their own local experimentation, tests and initiatives, and the provision of accessible contact information for firms.
 - **Joint policy work and regulatory trials** – collaboration between regulators on key policy questions to inform approach taken by regulators, with the view to support the work of standard setting bodies. This could also include regulators collaborating on RegTech solutions.
 - **Cross-border trials** – support companies in conducting trials across multiple jurisdictions to allow them to navigate multi-jurisdictional regulatory issues, both in the B2B and B2C space.

¹ For a more detailed discussion on the idea of agile governance, see 'Agile Governance: Reimagining Policy-making in the Fourth Industrial Revolution', World Economic Forum, January 2018, available at: http://www3.weforum.org/docs/WEF_Agile_Governance_Reimagining_Policy-making_4IR_report.pdf

How

- 17** The GFIN is designed to be self-sustaining and independent of any wider organisation, with members expected to contribute the necessary staff resources required. Any financial services regulator that wishes to join will have a commitment or interest in working on innovation, FinTech or RegTech related issues. It is a collaborative endeavour aimed at involving regulators, innovative companies and other relevant stakeholders, such as academia.
- 18** A multi-lateral approach would offer a new collaborative framework for regulators to pool knowledge, share their experience of new market developments, while also providing firms the ability to interact and engage with a network of regulators and other relevant stakeholders. This includes the possibility of conducting trials in multiple jurisdictions simultaneously for those firms in a position to do so, or the detailed sharing of the outputs of local tests with the other regulators in the network.
- 19** The GFIN is not designed to replace or duplicate the role of international financial services standard setting bodies or other international organisations, active in monitoring emerging trends, assessing and articulating international standards, and best practices. Nor is it designed to be a regulatory organisation with the responsibility of implementing rules. Instead, the GFIN, whose membership is likely to overlap with the membership of these organisations, is meant to build on and complement the work of those stakeholders through targeted engagement as described below.
- 20** The eventual membership of the GFIN that take this project forward is still to be determined. The named organisations in this document are committed to exploring the idea further, but the consultation process will help inform any future involvement. Similarly, regulators not named in this document may decide to get involved in the future, or after the formal launch of the GFIN.

Questions

- Q1:** *Do you agree with the proposed Mission Statement for the GFIN?*
- Q2:** *Do you agree with the three main proposed functions for the GFIN?*
- Q3:** *What aspects/areas of regulation pose the biggest challenge when it comes to innovating?*
- Q4:** *Do you see any reasons why this initiative may be counterproductive to the outcomes it is seeking to achieve?*

4 Functions

A. Network of regulators

Why

- 21** To date, a number of regulators have signed bi-lateral co-operation agreements with the goal of improving information sharing on innovation related topics. In some instances, these agreements have also contained a referral mechanism to support firms looking to scale their idea internationally.
- 22** The network of regulators would seek to build on existing collaboration and allow information sharing to occur on a deeper, larger and quicker scale, benefiting from a wider range of regulatory perspectives and experiences. Moreover, feedback highlighted that this could fill a current gap, providing a setting for open dialogue on innovation related topics. A network of regulators from around the world that shares knowledge and best practice relating to innovation, technological trends and emerging issues represents an iterative change from the current mode of collaboration in this space.
- 23** Respondents also told us that it can be difficult to initiate a conversation with a regulator in a new market when there has been no prior contact. The network will seek to help rectify this by helping firms navigate international expansion or policy discussions with multiple regulators, building on the existing referral mechanisms in place today under various bi-lateral agreements.

What

- 24** The network of regulators would function as a forum that enables collaboration between members for the advancement of financial innovation, achieving closer ties between the relevant departments in financial services regulators. One area the group could explore together would be the idea of best practice when it comes to assessing the merits of financial innovation in the interests of consumers.
- 25** It would provide a connection to international financial sector standard setting bodies and the relevant activity they undertake related to innovation, explored in more detail below. For the purpose of this document, international financial services standard setting body refers to an international organisation that possess a mandate to develop policy or standards relating to the regulation or supervision of financial services (e.g. International Organization of Securities Commissions (IOSCO)/International Association of Insurance Supervisors (IAIS)/Basel Committee on Banking Supervision (BCBS) Group of International Finance Centre Supervisors (GIFCS)).

How

- 26** The network would be made up of an overarching group containing all GFIN members. The overarching network would share intelligence relevant to the members, highlight key pieces of domestic work, or discuss emerging innovation trends. All GFIN members would be expected to participate in the broader overarching group.

- 27** The network would also contain sub-groups on various topics. Sub-groups will be self-organising and choose their own framework for working together. Members will be able to opt-in depending on their interests. Sub-groups will be asked to feedback to the wider network at key moments, such as at regular meetings.
- 28** The network would be overseen by a steering group made up of a smaller number of members. The steering group would be chaired by one of the members, selected on a consensus basis, defaulting to a voting process of all GFIN members if necessary. The voting system for nominating a chair in this situation would be one vote per jurisdiction. The steering group would act as the secretariat for the network, including organising meetings and member updates.
- 29** The network will meet twice in person each year, with quarterly discussions to discuss key updates. The chair will have first refusal on hosting the in-person meetings. The network would also canvas for feedback from industry, consumer groups, and academia, to understand the major concerns or emerging risks that may require further attention, either through the network or via one of the GFIN functions. Where appropriate, the network would publish external communications to update on its activities.
- 30** The GFIN would seek to complement, and where appropriate, feed into the work of standard setting bodies. The network of regulators would be the main conduit through which this engagement would take place. The relevant standard setting bodies would be invited to participate or observe relevant sub-groups or cross border trials. GFIN would look to avoid unnecessary duplication of standard setting work; however, where relevant it could provide complementary support or input on policy issues.
- 31** For firms, the network of regulators would seek to help them navigate areas such as exploring international expansion or cross-border policy issues. The network would provide easily accessible information about relevant contacts for firms, including sign-posting the opportunities for support and or on-going initiatives within members of the GFIN. This information could be made available through creating common online content or through an online portal for the GFIN.

Questions

- Q5:** *Do you believe the issue of developing a best practice for regulators when assessing financial innovation should be a priority for the network? If not, what other priorities should the network first address?*
- Q6:** *Do you agree with the approach to involve global standard setting bodies as part of the GFIN? How else would you like to see these organisations involved?*

B. Joint policy work and regulatory trials

Why

- 32** Feedback we have received highlighted there is a need to create a setting in which emerging technologies and business models can be discussed with the relevant regulatory authorities. Leveraging expertise from multiple regulatory authorities, and the local knowledge that they hold, provides an opportunity to crowd source solutions to common challenges and promote collaborative thought leadership on emerging issues. Closer policy dialogue and knowledge sharing may also reduce the potential for regulatory arbitrage in the future.

- 33** The first step in this process will be for members to identify common areas of interest, which could emerge from the work of the network, discussions with standard setting bodies, one of the sub-groups, or through consultation with industry, consumer groups, and academia. Equally, the results or findings of cross border trials involving multiple members may highlight potential overlapping policy areas of interest.

What

- 34** Companies have informed us that different regulatory approaches can act as a barrier to realising or scaling new ideas across markets. The GFIN could potentially act as a tool to identify these areas of divergence. Activity would focus on emerging technologies, how they interconnect with emerging business models, and the implications for the direction of regulatory policy. This could also relate to on-going activity around the world that is evaluating the potential of RegTech and SupTech. It would also provide the mechanism by which the future of certain policy debates could be discussed between regulators, industry, academia and other relevant stakeholders.
- 35** Issues relating to AML, counter-terrorist financing (CTF), payments and cross border identity verification are just some of the examples that may require a common approach across jurisdictions for solutions to either be; (1) economically viable/successful, or (2) interoperable.

How

- 36** Decisions on the areas of focus will be taken collaboratively to ensure that any joint work is mutually beneficial to members. However, there will be instances where certain regulators may not have the necessary mandate, expertise or resources to take part in a piece of work. Therefore, members would be able to opt-in to activity where they will derive most value.
- 37** Types of policy work that members could collaborate on include publishing the findings from cross border trials and how they have informed evolving policy positions. It could also include comparative market studies on common areas of interest, to understand different regulatory approaches, and future possible areas of convergence.
- 38** We also see potential for members to collaborate on trials involving new approaches to RegTech and SupTech. In May 2018, the FCA hosted its latest in a series of TechSprints, focused on AML and Financial Crime. The event was a collaborative initiative involving international regulators and law enforcement agencies, including Australian Transaction Reports and Analysis Centre (AUSTRAC), Monetary Authority of Singapore (MAS), and Abu Dhabi Global Markets (ADGM). Similar type events in the future involving GFIN members could be one option to explore emerging issues in further detail.
- 39** TechSprints may produce prototype solutions that would be good candidates for further development and testing through the GFIN. Additionally, TechSprint events will help to identify nascent technologies and approaches that may solve international use cases, and it may be appropriate for the GFIN members to articulate challenges/tests for which they would welcome applications.
- 40** Policy work conducted as part of the GFIN should be informed by the views and input from a broad range of stakeholders, recognising the activity of individual firms, partnerships between incumbents and start-ups, and the various industry consortia that have emerged in recent years.
- 41** There would be an expectation that members share relevant policy work with the broader membership of the GFIN, and where feasible also provide a market update on any activity.

Questions

Q7: *What kind of outcomes from the policy work and regulatory trials would your organisation benefit from?*

C. Cross border firm trials

Why

- 42** There was consensus amongst feedback received that the ability for firms to trial and scale new technologies in multiple jurisdictions is important in determining their potential benefit for end users. Feedback suggested this was true for both B2C and B2B business models. As a result, we believe there is demand from industry to offer a new solution to assist firms in this area.
- 43** Under current conditions, innovation initiatives operated by financial services regulators tend to be domestically focused. There is currently no global platform allowing firms to trial new ideas with consumers or other market participants in multiple jurisdictions working with the appropriate regulatory authorities. Facilitating cross border trials is about ensuring the potential benefits of financial innovation are shared across jurisdictions with consumers, regulatory authorities and other market participants. Such a function should also work on an opt-in basis for regulators to allow flexibility and discretion on the part of those involved.
- 44** Innovations that do not fit within the existing regulatory framework could benefit from this function. Likewise, it would provide regulators an opportunity to observe emerging business models and technology up close to help inform policy and supervisory work. We see the potential benefits to regulators as important as the benefits to firms.

What

- 45** Cross border trials would allow firms to test their innovative idea in multiple jurisdictions, gaining real-time insight into how their product or service operated in the market. We see benefits for trialling a single solution in multiple markets, or a business model which has inherent cross-border applications (e.g. international remittances). This would also allow regulators on an opt-in basis to supervise these new ideas closely, and where relevant, potentially inform future policy or supervisory decisions. Trials could also inform the licencing/authorisation outcome of these firms to help facilitate entry into new markets for innovative firms, although they will still be expected to meet the necessary regulatory requirements.
- 46** Over time, such trials could inform regulatory authorities in potential areas of regulatory convergence, although we recognise this is a longer-term opportunity. Trial results could also feed into the broader activity of global standard setting bodies as highlighted above.
- 47** Some responses to the initial consultation mentioned the possibility of a passporting function, whereby firms could trial new ideas in multiple testing facilities if they were licenced in one jurisdiction. Due to differing legal systems, this is likely a long-term project that will require regulatory convergence. Other respondents informed us that the most important thing from a business development perspective was to have clarity on the expectations different international regulators have for emerging technologies or business models.
- 48** The involvement of any regulator in a trial would not constitute an endorsement of that product or service by that regulator. Firms conducting a trial would be expected to meet all the regulatory requirements applicable in the respective jurisdiction(s).

How

- 49** Firms applying to conduct a cross border trial must meet prerequisites for entry into a global sandbox, determined by the regulators involved. These criteria will be publicly available to ensure there is transparency around which firms would be accepted. We do not propose drafting a single set of criteria which regulators must adhere to, given the wide range of regulatory mandates involved. The criteria will include what entity status would be required as a minimum for a firm to conduct a trial in a particular jurisdiction.
- 50** In joining the GFIN, regulators would specify whether supporting trials is something they could facilitate. This would be made clear to firms prior to submitting applications. Some regulatory members may wish to focus on the network and joint work, rather than supporting trials. It will be for regulatory authorities to decide the level of their engagement.
- 51** As part of the trial process, firms must demonstrate that they have the capabilities to operate in multiple jurisdictions for the duration of any trial. In cases where a firm may approach the GFIN too early for cross border trials, it may be more suitable for the firm to conduct a trial in one jurisdiction before expanding.
- 52** Cross border trials could start on a cohort and topic specific basis to manage resources, recognising the regulators involved will be learning how to operate trials in the early phase. The first trials could limit firms to the number of jurisdictions in which they want to test, although this could rise in the future once members have more experience in working on cross border trials.
- 53** Alternatively, another option would be to have a rolling application process rather than a cohort approach, whereby firms could submit applications at any time. This could provide greater flexibility for firms wishing to apply.
- 54** Firms would first apply to their domestic regulator, in cases where they are a regulated firm and the regulator is a member of the GFIN. Otherwise, an application would be sent to the chair of the network and distributed to all of the members in which the company has highlighted it wishes to test. The chair would play no role in assessing the application, other than as a co-ordinator of the initial application.
- 55** After an application has been submitted, a discussion would take place between those selected regulators to decide on the merits of the trial, and whether individual members would like to progress the application further based on their own criteria, areas of interest, and ability to support the activity. If a potential trial passed this initial screening, the firm would be informed. At this stage, it would be open to a potentially interested regulator to decline to support the trial under consideration. Successful firms would be asked to submit a trial plan to be discussed with those regulators involved, before commencement of testing.
- 56** During the trial, firms would be required to provide information and other assistance to those regulators involved in order to monitor its progress. The regulators involved would be expected to review this information to test regulatory compliance, and also discuss any broader emerging issues or findings with the other participant regulators.
- 57** The aim, after the trial would be to provide the firm with sufficient information about the merits of the product or service and how it benefited consumers or the wider financial services market. The results of the trial could be shared among GFIN members and potentially inform future licencing decisions of the firm involved, or help provider clarity on how emerging technologies or business models fit within the regulatory framework. Details of successful applicants would be published at the outset and findings may also be published for wider information sharing, depending on the circumstances, following the trial period.

Questions

- Q8:** *Would the cross-border trials be of interest to your organisation? If so, could you provide any potential example use cases?*
- Q9:** *Do you agree with the proposed approach to managing the application process for cross-border trials?*
- Q10:** *[For regulators] Do you anticipate any challenges with the proposed approach to managing the application process, or conducting cross-border trials?*

5 Next steps

- 58** This group are asking for feedback on the consultation questions by **14 October 2018**. Over the course of the next two months we will engage with interested parties across the different jurisdictions involved in the project. This will also include the chance for stakeholders to provide informal feedback through a range of engagement activities the authorities listed in this document will undertake. We are also keen to hear from stakeholders from other jurisdictions not listed in this document.
- 59** In the autumn, we will review feedback and agree on next steps, including a timeline for when we expect to be in a position to launch the GFIN.
- 60** We have set-up an email address GFIN@fca.org.uk for anyone who would like to provide input into the development of the network. Feedback submitted to this email address will be shared among the organisations listed below, unless you specifically state otherwise.
- 61** If you would like to contact a representative from one of the stakeholders involved in the project, please use the appropriate contact email below:

Abu Dhabi Global Market (ADGM)

Contact: Chris Kiew Smith
chris.kiewsmith@adgm.com

**Autorité des marchés financiers (AMF)
(Québec, Canada)**

Contact: Lise-Estelle Brault, Senior Director Derivatives
lise-estelle.brault@lautorite.qc.ca
514 395 0337

**Australian Securities & Investments
Commission (ASIC)**

Contact: Cuihua Cartwright
cuihua.cartwright@asic.gov.au

Central Bank of Bahrain (CBB)

Contact: yasmeen@cbb.gov.bh

**Bureau of Consumer Financial Protection
(BCFP, USA)**

Contact: Paul Watkins
officeofinnovation@cfpb.gov

Dubai Financial Services Authority (DFSA)

Contact: Elisabeth Wallace
ewallace@dfsa.ae

Financial Conduct Authority (FCA, UK)

Contact: Paul Worthington
paul.worthington@fca.org.uk

Guernsey Financial Services Commission (GFSC)

Contact: Steve Chandler
innovate@gfsc.gg

Hong Kong Monetary Authority (HKMA)

Contact: Henry Chang
FinTech@hkma.gov.hk

Monetary Authority of Singapore (MAS)

Contact: Sopnendu Mohanty
FinTech_Office@mas.gov.sg

Ontario Securities Commission (OSC, Canada)

Contact: Pat Chaukos
osclaunchpad@osc.gov.on.ca

Consultative Group to Assist the Poor (CGAP)

Contact: Ivo Jenik
jenik@worldbank.org

Annex 1

List of questions

- Q1:** *Do you agree with the proposed Mission Statement for the GFIN?*
- Q2:** *Do you agree with the three main proposed functions for the GFIN?*
- Q3:** *What aspects/areas of regulation pose the biggest challenge when it comes to innovating?*
- Q4:** *Do you see any reasons why this initiative may be counterproductive to the outcomes it is seeking to achieve?*
- Q5:** *Do you believe the issue of developing a best practice for regulators when assessing financial innovation should be a priority for the network? If not, what other priorities should the network first address?*
- Q6:** *Do you agree with the approach to involve global standard setting bodies as part of the GFIN? How else would you like to see these organisations involved?*
- Q7:** *What kind of outcomes from the policy work and regulatory trials would your organisation benefit from?*
- Q8:** *Would the cross-border trials be of interest to your organisation? If so, could you provide any potential example use cases?*
- Q9:** *Do you agree with the proposed approach to managing the application process for cross-border trials?*
- Q10:** *[For regulators] Do you anticipate any challenges with the proposed approach to managing the application process, or conducting cross-border trials?*

Appendix I: Regulatory sandboxes in financial services

The origin of sandboxes

The idea of sandboxes was popularised in software development and conceived of as a type of testing facility, one that runs in isolation from the main production environment. This in effect allows new code to be tested in an isolated and secure fashion, with restrictions on what it can and cannot do.

Introduction to financial services

Following their wide usage in computer software, the idea of sandboxes has since been adopted across a number of financial services regulators. Sandboxes in financial services have sought to replicate the key components from software development, namely that it is about creating an environment which allows for limited testing with restrictions on what firms can and cannot do. Testing can be done either on a virtual basis with data sets, or in a live market with real consumers or market participants. This allows regulators to learn about emerging technologies and business models on a limited scale, short term basis.

Sandbox objectives

A number of financial services regulators from around the world have implemented a variety of different regulatory sandbox models, with varying objectives reflecting the different mandates and legal responsibilities regulators possess. Some of the most common objectives for these initiatives include:

- Support financial innovation and FinTech firms who are seeking to offer innovative new products, services or business models.
- Foster a financial services system that is more efficient and manages risks more effectively.
- Understand how emerging technologies and business models interact with the regulatory framework and where it may lead to barriers to entry.
- Promote effective competition in the interest of consumers.
- Promote financial inclusion for consumers.

Similarities

Despite regulators possessing different motives for setting up regulatory sandboxes, they do possess some broad similarities. In general, regulatory sandbox initiatives seek to support and facilitate the introduction of new innovative technologies and business models. These innovations are also likely to pose questions around the current regulatory framework or requirements for firms.

Another similarity of regulatory sandboxes is the limited scale, restricted nature of activities firms can conduct in the sandbox environment. The types of restrictions vary depending on the sandbox, but the restrictions and limited scale of the sandbox environment means that firms testing as part of regulatory sandboxes eventually look to scale their solution outside of the restricted environment.

Sandboxes also possess criteria for entry, to determine the type of firm eligible for sandbox type support. Although the criteria differ between regulators, on a broader level sandboxes operate in a way that requires firms to meet certain criteria as a condition of entry.

Differences

As highlighted above, the objectives of regulatory sandboxes conceived by financial services regulators vary depending on the mandate of individual regulators. The three other differences between sandboxes are the type of support available to firms, the way in which sandboxes are run, and the difference in regulatory or legal regimes.

The type of support available to firms can vary on a sector basis, with certain sandboxes focused on specific areas of financial services, or in certain situations unable to provide the necessary support as part of a sandbox environment for the type of activity the firm has in mind.

The tools available to firms differ across sandboxes. For example, ASIC has created a regulatory sandbox licencing exemption for firms (see Appendix II). In contrast, in the UK, firms wishing to test in the FCA's sandbox must be authorised for the purpose of the activity they wish to test. This involves firms applying for a restricted authorisation, whereby firms must meet the FCA's regulatory conditions in order to receive the necessary authorisation, which will allow the firm to test their ideas as agreed with the FCA for a time limited period.

The operational differences of regulatory sandboxes determine the way in which firms interact with regulators. For instance, some sandbox models function on a cohort basis, whereas others have a rolling application process. The duration of time firms can spend within a sandbox environment also differs between sandboxes, with common ranges from six months to two years.

Appendix II: Summary of ASIC's regulatory sandbox exemption

In December 2016, ASIC released Regulatory Guide 257 Testing FinTech products and services without holding an AFS or credit licence (RG 257), which contains information about ASIC's regulatory sandbox exemption.

ASIC has statutory powers to exempt a person (or class of persons) from:

- (a) the requirement to hold an AFS licence under the Corporations Act; or
- (b) the requirement to hold a credit licence under the National Credit Act.

ASIC refers to these powers as 'relief powers'. ASIC has used these relief powers to provide FinTech licensing exemption (also known as the 'regulatory sandbox exemption') that allows eligible firms that are not currently authorised to provide the services covered by the exemption to test these services for up to 12 months without an AFS or credit licence.

The exemption allows eligible firms to provide advice on and deal in (other than acting as a product issuer):

- (a) listed or quoted Australian securities;
- (b) debentures, stocks or bonds issued or proposed to be issued by the Australian Government;
- (c) simple managed investment schemes;
- (d) deposit products;
- (e) some kinds of general insurance products; and
- (f) payment products issued by authorised deposit-taking institutions (ADIs).

The exemption also allows eligible firms to act as an intermediary or provide credit assistance for certain types of credit contract.

The exemption is subject to a number of conditions, such as client and exposure limits, consumer protection measures, adequate compensation arrangements, and dispute resolution systems.

ASIC has taken a whitelist approach, meaning ASIC does not review each proposed product or service, and ASIC is not involved in selecting applicants and negotiating individual testing terms for people using the exemption in the instruments. ASIC's FinTech licensing exemption allows eligible firms to notify ASIC and then commence testing without an individual approval process. However, customers of these FinTech firms will still have fundamental protections under the law, such as access to dispute resolution systems and the firms's professional indemnity insurance.

Within ASIC's remit, this is the result of balancing the benefits of concept validation testing against the risks of consumer harm from poor conduct by unlicensed firms that have not demonstrated their competence to deal with consumers.

Note on the Australian Government's Enhanced Regulatory Sandbox

The Australian Government consulted on exposure draft legislation and regulations for the enhanced regulatory sandbox exemption in October 2017 and is working to make relevant regulations in coming months. The proposed enhanced regulatory sandbox will extend the scope of the class waiver beyond that under the ASIC sandbox licensing exemption in a number of key areas. This proposed exemption, if implemented in a materially similar form, would supersede the need for ASIC's FinTech licensing exemption.

