

REGULATORY SANDBOXES: DESIGN AND POLICY CONSIDERATIONS

Dr Anton Didenko
Research Fellow, UNSW Sydney (Australia)

03 SEPTEMBER 2018



THE 2018
AFI GLOBAL
POLICY FORUM

INNOVATION
INCLUSION
IMPACT



Outline

1. Choosing the right ‘sandbox’
2. Regulatory sandbox models
3. A global/regional regulatory sandbox?
4. Regulatory sandboxes in the Pacific
5. Design choices

'SANDBOX' CONCEPT

- Originated in software development
- Testing facility isolated from the rest of the network
- Allows testing of new code in a secure fashion



Source: [Pixabay](#)

SANDBOX ... WHICH SANDBOX?

- Regulatory sandbox
- Industry sandbox
- Sandbox umbrella
- New regulated activity
- ‘Pseudo-sandbox’

REGULATORY SANDBOXES VS INDUSTRY SANDBOXES

- A regulatory sandbox
 - Creates a ‘safe space’ for businesses
 - Developed by the regulator for the industry
 - ‘On-market’ - businesses interact with consumers/clients
- An industry sandbox
 - Creates a ‘safe space’ for businesses
 - Developed by the industry for the industry
 - ‘Off-market’ - businesses do not interact with consumers/clients

REGULATORY SANDBOXES

- Key objectives
 - Improvement of the financial services market (new products, RegTech)
 - Regulators that understand the new technology
 - Firms that understand the regulatory requirements
- 3 models
 - Sandbox umbrella
 - New regulated activity
 - ‘Pseudo-sandbox’

SANDBOX UMBRELLA

- Benefits
 - Eliminates the need for individual firms to obtain authorisation
 - Can be set up by the industry
 - Faster implementation compared to legislative change
- Challenges
 - Could be complex to set up
 - May have limited scope
 - Reduced regulatory oversight over individual firm innovations
 - May obscure deficiencies of tested solutions

NEW REGULATED ACTIVITY

- Benefits
 - Flexibility (regulators can design their own approaches)
 - Regulator's approval of a sandbox application can attract investors
 - Absence of fixed restrictions would be attractive for firms
- Challenges
 - Firms require individual authorisation/waivers/relief
 - Regulator's flexibility may be limited by legislation/international rules
 - Changes to regulations can take time to enter into force
 - Activities outside the scope of a regulator's mandate are not eligible

‘PSEUDO-SANDBOX’

- Benefits
 - Does not require a special ‘sandbox’ regime
 - Requires fewer resources
 - Class waivers do not require regulators to assess the level of innovation of each project
- Challenges
 - Class waivers can be very limited in scope
 - Class waivers are less interactive (no knowledge exchange)
 - Usefulness of individual relief depends on regulator’s efficiency/experience

AUSTRALIA'S SANDBOX

- Existing exemptions from licensing requirements
- Fintech licensing exemptions
- Individual exemptions by ASIC

BUT: only 6 firms using it...



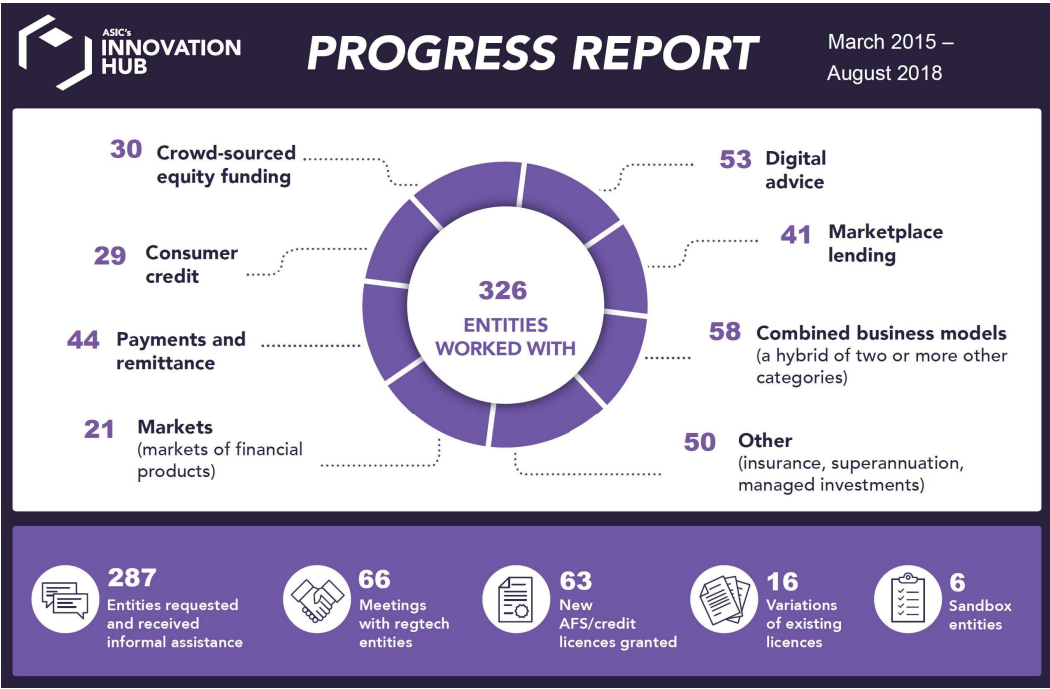
THE 2018
AFI GLOBAL
POLICY FORUM

INNOVATION
INCLUSION
IMPACT

#afiGPF18
#AFITURNS10

10

AUSTRALIA'S INNOVATION HUB



TWO FORMS OF FINTECH FACILITATION

Regulatory sandbox

- **Controlled space** to test innovative solutions with the support of a regulator for a limited period of time
- Tailored supervision, may require legal changes

Innovation hub

- **Institutional arrangement** where firms engage with regulators to **discuss** issues and **seek clarification** on the conformity of business models with the regulatory framework
- Does not require legal change

WHY DO SOME REGULATORS REJECT SANDBOXES?

- France
 - “Although the term sandbox is confusing and misleading, it may **basically mean ‘sound regulation’**, which is actually the proportionate approach French regulators support and implement in France”
- Germany
 - “What we do is **supervision, not business development**. Both are important and sensible. They just should not be mixed up”
 - Regulator should not respond to possible misconduct by providing **“small buckets and spades”** (instead of dialogue)

HARMONISED SANDBOX REGIME?

- Different from current regime - national sandboxes
- Useful for services with cross-border application
- Implies a degree of legal harmonisation
- Early signs of possible harmonisation in the future
 - March 2018 - FinTech Action Plan of EU Commission

GLOBAL SANDBOX

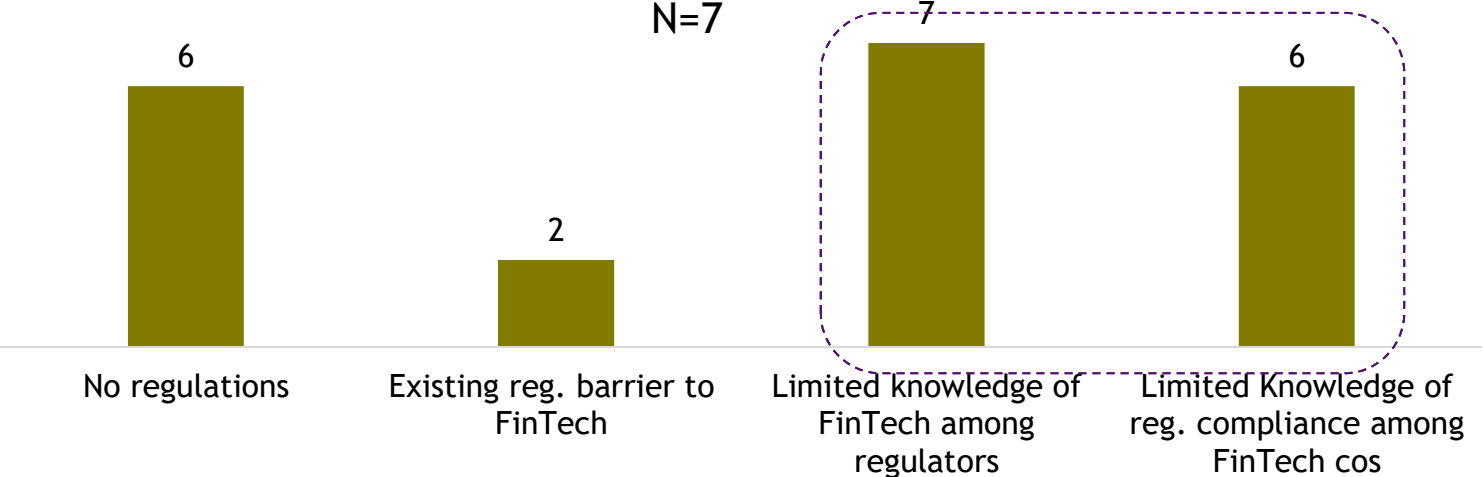
- February 2018 - proposal by FCA for a “global sandbox”
- August 2018 - GFIN (Global Financial Innovation Network)
 - Network of regulators to collaborate/share experiences
 - Forum for joint policy work/discussions
 - Environment for firms to test cross-border solutions

REGIONAL SANDBOX

- Regional sandbox or international cooperation?
 - Memoranda of Understanding by Abu Dhabi, Australia, Kenya, Singapore, UK
 - Referrals by regulators
 - Techsprints to produce prototype solutions
- Level of uniformity?
- A single model?

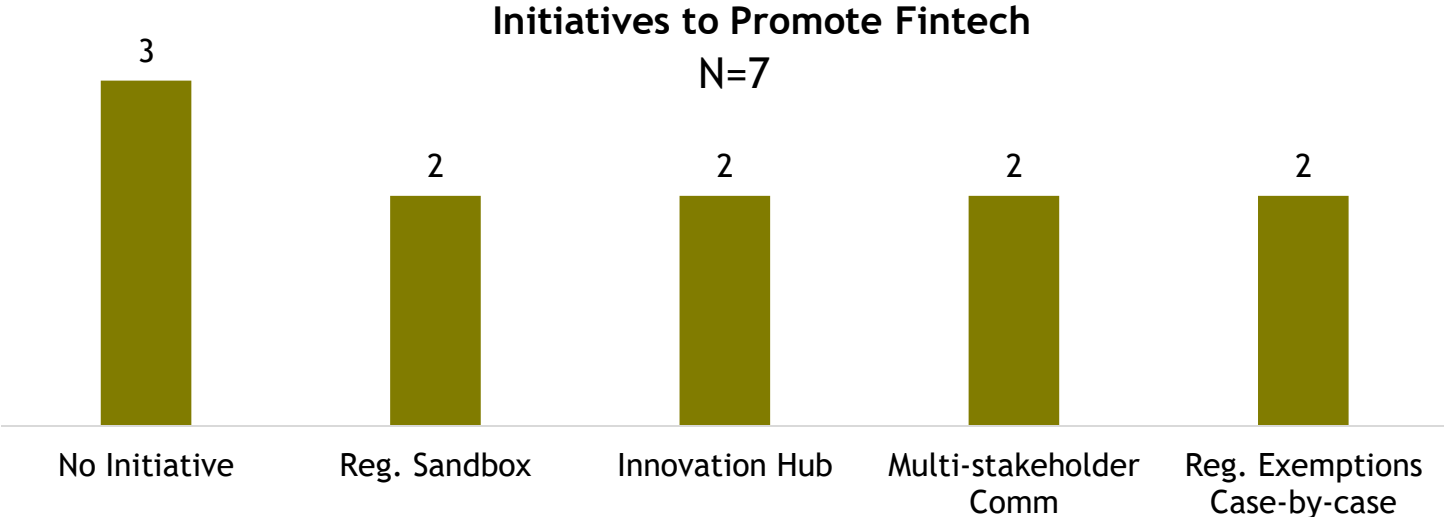
KEY REGULATORY CHALLENGES IN PROMOTING FINTECH4FI (PIRI SURVEY 2018)

Key Regulatory Challenges in Promoting Fintech



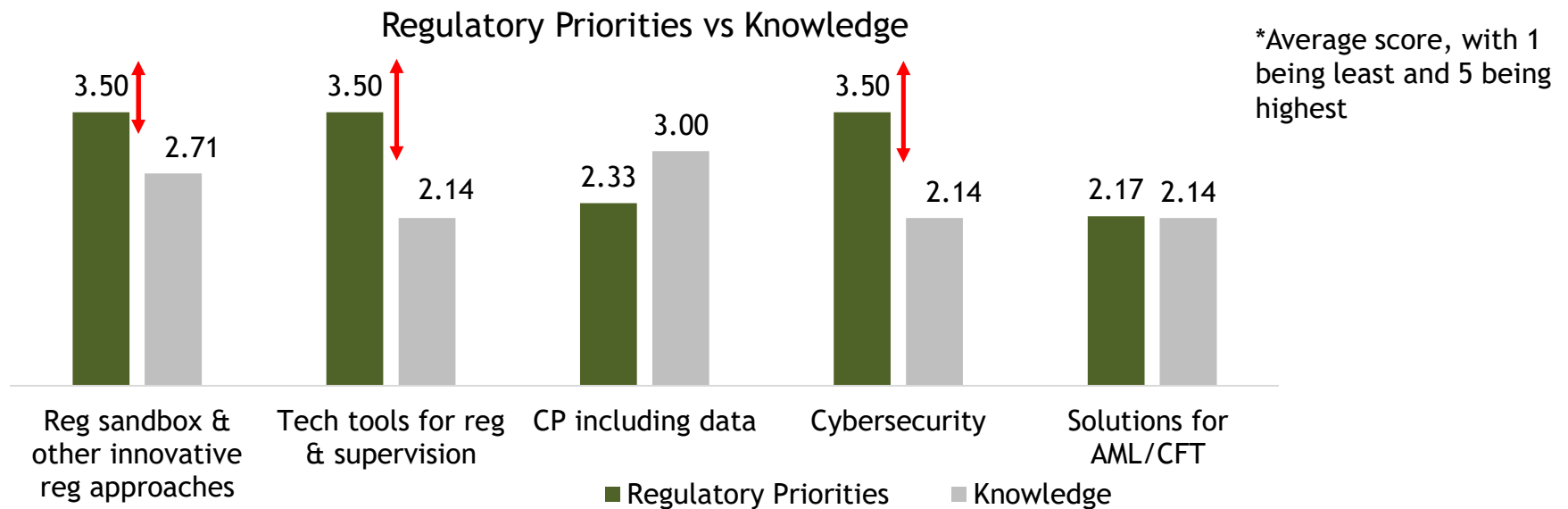
Limited knowledge about fintech among regulators & limited knowledge of regulations/regulatory compliance among fintech companies.

INITIATIVES UNDERTAKEN TO PROMOTE FINTECH4FI (PIRI SURVEY 2018)



Two countries ie, Fiji and Solomon Islands have undertaken a regulatory sandbox initiative along with innovation hubs.

LEARNING ASSESSMENT: REGULATORY PRIORITIES VS KNOWLEDGE (PIRI SURVEY 2018)



REGULATORY SANDBOXES IN THE PACIFIC

- Fiji
 - “[S]andbox will provide a platform to enable existing financial institutions along with interested parties to individually lodge an application or collaborate to explore new products and services for Fiji’s financial sector”
 - Consultations with the industry about the guidelines
 - Knowledge exchange between BSL and RBF

CASE STUDY: SIERRA LEONE SANDBOX

- Financial inclusion objective
- Coordination with ecosystem building
- Dedicated sandbox team and resources from BSL



THE 2018
AFI GLOBAL
POLICY FORUM

INNOVATION
INCLUSION
IMPACT

#afiGPF18
#AFITURNS10

21

CASE STUDY: SIERRA LEONE SANDBOX

- First cohort:
 - “InvestED”
 - “iCommit”
 - “MyPay”
 - “Noory”

CASE STUDY: SIERRA LEONE SANDBOX

Competition: 'FinTech Challenge 2017'

- Co-funded by BSL, FSD Africa and UNCDF
- Selection by 2 panels (UNCDF, FSD, BSL + consumer reps)
- Selection criteria
 - Project feasibility
 - Relevance for the people/businesses in Sierra Leone
 - Impact and potential of the idea



THE 2018
AFI GLOBAL
POLICY FORUM

INNOVATION
INCLUSION
IMPACT

#afiGPF18
#AFITURNS10

CASE STUDY: SIERRA LEONE SANDBOX

- Project feasibility (40%)
- Project relevance (30%)
- Impact potential (30%)
 - How will the product reach:
 - people in need in Sierra Leone
 - people/businesses in key economic areas in Sierra Leone (energy, fisheries, tourism, agriculture)
 - at least one of the following: (i) the unbanked, (ii) the poor, (iii) women, (iv) young people

CASE STUDY: SIERRA LEONE SANDBOX

- 20 applications received
 - 85% from Sierra Leone, others from Ghana, Kenya
- 3 finalists:
 - “InvestED” (*winner*)
 - “Data Pool”
 - “Ace Ltd”

DESIGNING A REGULATORY SANDBOX - IMPORTANT CONSIDERATIONS

- What is the objective?
- Sandbox or innovation hub? Or both?
- Which model?
- What is the scope?

DESIGNING A REGULATORY SANDBOX - IMPORTANT CONSIDERATIONS

- Does the regulator have the required authority?
- Does the regulator have sufficient human resources/funding?
- Is there demand from the industry?

DESIGNING A REGULATORY SANDBOX - IMPORTANT CONSIDERATIONS

- Who is eligible?
- Why would they be interested?
- Who will determine eligibility?
- Are there any spill-over benefits for non-participants?

ADDITIONAL SANDBOX FEATURES

- Mix of positive and negative criteria
- Single point of entry
- Pre-application consultation
- IP protection rules

TYPICAL ELEMENTS OF A SANDBOX REGULATORY FRAMEWORK

- Eligibility requirements
- Application process
- Testing parameters

TYPICAL ELEMENTS OF A SANDBOX REGULATORY FRAMEWORK

- Regulatory flexibility
 - Individual guidance
 - Waivers or modifications of own rules
 - No enforcement action letters
- Limits to regulatory flexibility
 - Consumer protection issues

TYPICAL ELEMENTS OF A SANDBOX REGULATORY FRAMEWORK

- Scheduled exit from sandbox
 - Automatic upon reaching the maximum duration (generally varies between 6 and 24 months and can be extended)
 - Firm submits the final report
 - Regulator reviews the report and decides whether to approve the deployment of the new solution
 - Firm decides whether to launch the new solution

TYPICAL ELEMENTS OF A SANDBOX REGULATORY FRAMEWORK

- Early termination of sandbox privileges
 - Failure to carry out the agreed safeguards
 - Submitting false, misleading or inaccurate information
 - Breach of applicable domestic law
 - Going into liquidation
 - Breach of mandatory rules (eg on data security)
 - Doing business in a manner detrimental to customers or the public at large
 - Failure to address major technical defects
 - Non-compliance with the agreed schedule/process
 - Discovery of a major flaw posing major risks to customers or financial system
 - Firm's voluntary exit
- Appeal against early termination decision



**THE 2018
AFI GLOBAL
POLICY FORUM**
**INNOVATION
INCLUSION
IMPACT**

5 - 7 SEPTEMBER 2018, SOCHI, RUSSIA

THANK YOU