

Re: CP156 - Central Bank approach to innovation engagement in financial services

07/02/2024

FPAI welcomes the enhancements outlined in the Innovation Hub. The proposed developments are recognised as another positive step towards helping the financial services sector (including FinTechs and incumbents) understand the regulatory landscape in Ireland. It is also acknowledged that the new Hub will encourage earlier and more meaningful engagement with new firms entering the financial services sector.

As a FinTech Association deeply embedded in the financial services sector, we recognize the pivotal role that such regulatory frameworks play in enabling sustainable and responsible innovation. The proposed developments in the Innovation Hub, and the introduction of a regulatory sandbox represents a significant step towards creating a more inclusive and dynamic financial ecosystem, and we are eager to engage in constructive dialogue to share our insights and experiences.

Our participation in this consultation is driven by our commitment to advancing the interests of our members and the wider community we serve. We look forward to contributing to the shaping of a regulatory sandbox that reflects the needs and aspirations of all stakeholders involved, and we hope our feedback will provide valuable perspectives to inform the development and implementation of this important initiative.

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Question 1: What is your feedback on the enhancements underway with the Innovation Hub? Are there other areas that should be developed?

- FPAI acknowledges that this is the start of a new strategy and suggests that annual reviews of its effectiveness be conducted, with feedback gathered from industry. FPAI would also encourage the Hub to actively engage with the wider FS sector and especially larger, established FinTech's who may also benefit from the new structure when it comes to innovating their services.
- FPAI believes it is important to consider these proposed developments within the broader context of other activities which are vital to a Ireland maintaining its reputation as a first class jurisdiction for establishing a regulated financial services firm such as continually innovating, refining and enhancing the clarity, predictability, efficiency and proportionality of regulatory authorisation and supervisory requirements and processes.
- De-risking is a major challenge for fintechs and payments firms. We note that de-risking is an area of focus for the EBA, reflecting the fact that this trend is impacting the wider European financial industry. The innovation hub is an ideal means of gathering signals about bank de-risking because firms that cannot open bank accounts may never even get to application stage. We suggest that the innovation hub would monitor for instances of de-risking impacting startups, and share insights about de-risking with the EBA to further inform its work in this area.”

Question 2: What is your feedback on the proposal to establish an Innovation Sandbox Programme? Will the proposal support the Central Bank in meeting our overall objectives, including the needs of consumers and the wider economy?

- FPAI welcomes the establishment of an Innovation Sandbox Programme in Ireland. We are aware that there are many different forms in which a regulatory sandbox programme may take based on existing models in many other jurisdictions
- FPAI members believe that a best-in-class regulatory sandbox is a framework that can allow both FinTech startups and established Financial Service innovators to conduct live experiments in a controlled environment under the regulator's supervision. The goal is to encourage financial services innovation while appropriately managing risks and protecting customers. The sandbox should balance the need for innovation with the necessity of maintaining financial stability and protecting consumers. The services we believe are typically provided by a best-in-class regulatory sandbox include:
 - **Testing Environment:** Which provides a safe space for companies to test their new financial products, services, or business models on a limited scale without immediately incurring all the normal regulatory consequences of engaging in the activity. The tools provided would typically include synthetic data to enable repeated testing of the service by the participants. Our understanding from Central Bank engagement with industry in relation to CP 156 is that the CBI does not propose to include a testing environment in its proposed regulatory sandbox in the initial phase but we believe the CBI should work towards including this in the medium to long term.

- **Regulatory Guidance:** Access to the relevant expertise within the CBI for guidance on compliance matters, helping companies understand how existing regulations apply to their new products or services. We understand that the proposal will provide access to the relevant subject matter experts within the CBI when required and we welcome this as a practical way of helping firms to embed a compliance culture from the earliest stages of their development.
- **Waivers or Modifications:** Some sandboxes allow temporary relaxations of specific regulatory requirements which the new product or service may not fully comply with, under strict conditions and oversight. There would be support for limited testing of live customers - 'friends & family' and staff. There does not appear to be any plan by the CBI to support Waivers or Modifications at least in the initial phase of the proposed sandbox and we consider it important to continue to consider this in the medium to long term given other regulators have found ways to do include this.
- **Support and Monitoring:** Throughout the testing phase, some sandboxes provide ongoing support and closely monitor the progress of the experiment. This ensures that any risks are managed effectively, and consumer protection measures are in place. We understand this is not being proposed by the CBI and our comments regarding a testing environment apply to support and monitoring throughout a testing phase too.
- **Feedback and Learning:** At the end of the testing phase, the sandbox would provide feedback to the participants. This feedback can be invaluable for refining the product or service and preparing for a full-scale launch. By enabling a 'two-way street' it also helps regulators understand emerging innovations and consider necessary regulatory adjustments, ultimately making for a more efficient process. We understand this would not be supported by the proposed sandbox and our comments regarding a testing environment apply to feedback and learning too.
- **Networking Opportunities:** We understand that the proposed sandbox will facilitate networking opportunities with other innovators, investors, and partners, which will be hugely beneficial for business growth and development. We believe the proposal to involve a 3rd Party provider should address this requirement, but our members have a concern that the cost may be prohibitive.
- **International Cooperation:** We would be keen to understand if the intention is to have the proposed sandbox to be part of an international network, to allow for cross-border engagement and understanding of regulatory standards in different jurisdictions.
- Our members are keen that the CBI keeps in close contact with Industry as the sandbox is developed, and as it operates. We suggest an **Industry Council** be formed where the CBI and Industry can meet on an ongoing basis to measure the effectiveness of the sandbox (including the financials) and discuss challenges and evolutions of the service. FPAI is keen to participate in any such Industry Council.
- FPAI recognises that the description above of a best-in-class regulatory sandbox is an ideal '**end-state**'. Our members appreciate there may be several phases required to achieve this. A good first phase might be the CBI granting access to their subject matter experts and grow the service from there. We also understand that the number of firms admitted to the

regulatory sandbox in its initial phase may be relatively small but we trust that this can be expanded as the sandbox becomes more established.

Question 3: What is your feedback on the operating model of the Innovation Sandbox Programme?

- FPAI acknowledges the comprehensive operating model described for the proposed Sandbox. FPAI also notes that Stage 1 will be informed by industry, both on a one-to-one basis through the Hub and through the Innovation Sub-Group.
- FPAI also suggests that:
 - The Value Proposition to Established Firms & Start-ups be clearly articulated at the outset. Members will be sensitive to incremental costs for operating in the sector.
 - For firms who successfully engage with the programme, it would be important that the CBI encourages and monitors incumbent banks to also engage to provide services and support for new products.
 - CBI analysis of the models/features of regulatory sandboxes in other jurisdictions, how these compare with the model/features of the regulatory sandbox which the CBI is proposing, the CBI reasoning for not including models/features of regulatory sandboxes in other jurisdictions which the CBI is not proposing and lessons that can be taken from regulatory sandboxes in other jurisdictions be shared by the CBI as part of its feedback on CP 156.
 - That the importance of clarity, predictability, efficiency and proportionality of authorisation and supervisory requirements and processes remain utmost given their importance to attracting the best new entrants and to maintaining Ireland's reputation as a first class jurisdiction for establishing a regulated financial services firm.
- It is the nature of innovation that priorities/strategies/focus will shift constantly and quickly. FPAI encourages the Sandbox Programme to remain flexible and tolerant of firms who enter the process but may decide to leave early as situations evolve.
- Regionalisation is one of the pillars of the Ireland for Finance strategy for job creation in financial services. It is critical that the CBI ensures its innovation activities are balanced between Dublin and other regions, so regionalisation needs to be part of the design for innovation sandbox programme. When contracting with a third party innovation programme, it's important to ensure that entrepreneurs and start-ups based outside Dublin can have equal access and exposure. FPAI would also ask that CBI expertise remain front and centre of the Sandbox, especially when third-party providers may become involved.

Question 4: Are there specific themes or areas of innovation that the Central Bank Innovation Sandbox Programme should address?

Our members noted that a theme-based approach could act as a bottleneck if themes cannot be run simultaneously.

Some Themes suggested by FPAI members include:

- **Blockchain:** perhaps run as two separate programme themes: (i) tokenisation of financial instruments (e.g. shares or bonds); (ii) crypto-assets, which could include electronic money

tokens or asset-referenced tokens under the Markets in Crypto-Assets Regulation or other types of blockchain projects, e.g. those involving decentralised finance or non-fungible tokens.

- **Embedded Finance:** (Embedded finance refers to the seamless integration of financial services within the offerings of non-financial companies. This means that customers can access banking, payment, insurance, and investment services directly through the platforms or apps they are using, without needing to interact with traditional financial institutions separately. For example, a retail e-commerce platform might offer instant credit at the point of sale, a ride-sharing app might include insurance for each ride, or a social media platform might allow users to send money to each other directly within the app.)
- **Anti-Money Laundering:** (AML refers to a set of laws, regulations, and procedures designed to prevent criminals from disguising illegally obtained funds as legitimate income. AML frameworks require financial institutions and other regulated entities to monitor customer transactions, conduct due diligence to verify customer identity, maintain records of financial transactions, and report suspicious activities to relevant authorities.)
- **Artificial Intelligence:** (AI in financial services encompasses the use of machine learning algorithms, natural language processing, robotics, and other AI technologies to enhance financial processes, decision-making, and customer experiences. AI applications in this sector range from fraud detection and risk management to algorithmic trading, personalized financial advice (robo-advisors), customer service automation (chatbots), and process automation (e.g., in loan underwriting and KYC processes).
- **Fraud** (and use cases around fraud prevention that centre on digital identity).
- **Instant Payments** (drawing on the introduction of SCT Inst and the presence of several major payments businesses in Ireland)
- **Green Finance** (reflecting the fact that sustainable finance is an area of focus in the Government's Ireland for Finance action plan, the Sustainable Finance Centre of Excellence established in Ireland and the growing need for verifiable data to demonstrate compliance with the EU Green taxonomy and to prevent greenwashing).
- **Credit Facilities** on foot of PSD 3