



FINANSINSPEKTIONEN

FI's role regarding innovation

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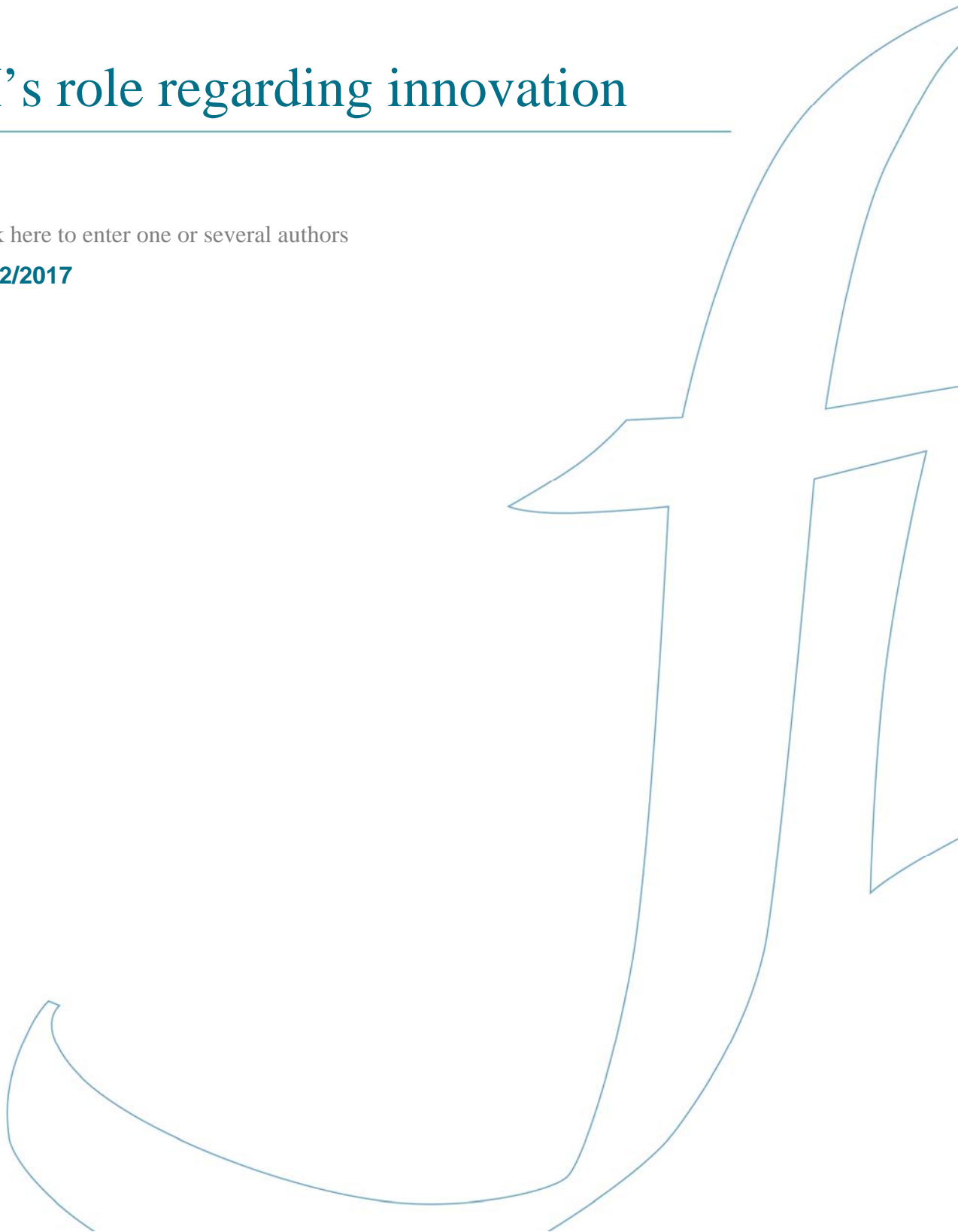


TABLE OF CONTENTS

FOREWORD	3
SUMMARY	4
BACKGROUND	6
Assignment	6
FinTech	6
FI and financial supervision	6
Disposition	8
OVERVIEW	9
Description of the Swedish FinTech sector	9
Payment services	10
Market and infrastructure	11
Loans and financing	12
Advisory services	12
Virtual currencies	13
Insurance policies	13
RegTech	14
QUESTIONS AND NEEDS	15
Roundtable discussions	15
FI's role	15
Information and support	15
Authorisation process	16
Cloud services and technology	17
ACTIONS TO BE TAKEN BY FI	19
More information and guidance	20
ADDITIONAL MEASURES	23
Regulatory sandbox	23
A Swedish regulatory sandbox	24
APPENDIX - ROUNDTABLE DISCUSSIONS, METHODOLOGY	27
Assignment	27
Solution	27
Practical implementation	28
Assessment of the methodology	28
List of participants	29
APPENDIX - REGULATORY SANDBOXES	30
United Kingdom	30
The Netherlands	31

Foreword

New products, new technological solutions and new businesses are fundamentally good - for both the financial sector and other markets. They promote greater competition and efficiency and help products become both more inexpensive and more aligned with customers' needs.

FI has not been given an explicit assignment to promote either technological development or competition in the financial sector, but financial regulation that pursues the goal of promoting well-functioning financial sectors and a high level of consumer protection should not be an obstacle, either. A market with low innovative capacity and poor competition can be called neither well-functioning nor in the interests of consumers. On the other hand, innovation should not be achieved at the cost of weaker financial stability or compromised consumer protection. It is therefore important for FI to closely follow the digitalisation developments in the financial sector.

This report presents the results of the assignment FI received from the Government in March of this year. The report contains a description of several phenomena within the Swedish FinTech sector as well as the challenges the industry is experiencing. In order to meet the needs of the industry and also achieve better consumer protection, FI will be implementing a number of measures. These measures are described in this report.

Stockholm, 1 December 2017

Erik Thedéen
Director General

Summary

Finansinspektionen (FI) received an assignment from the Government to map innovations in the financial sector as well as the questions and needs of market participants in relation to the authority's core activities: supervision, authorisation and regulations.

Finansinspektionen is tasked with safeguarding the stability of the financial sector and sound consumer protection. It is therefore an inherent part of FI's role not to obstruct innovation. However, FI has not been given an explicit assignment to promote innovation.

Innovative activities are initiated either by financial companies themselves or by non-financial firms, and often start-ups. An effort to map the companies that work with financial innovation is more about categorising innovations than categorising companies. The innovative forces within these companies are strong, but the companies are experiencing a considerable need for information about rules, processes and principles in order to be able to realise their innovations.

In order to meet this need, FI will establish an Innovation Center that will provide information for and maintain a dialogue with companies that conduct innovation-based business. The objective of the Center will be to give companies a single point-of-contact that will enable them to more simply and quickly receive the information they need to progress.

The Innovation Center will serve as the natural first point-of-contact at FI for companies that are unsure of the rules, processes and principles that apply in the financial sector to their innovations. The Center will also arrange seminars, informational gatherings and FI participation in external events regarding innovation in the financial sector.

The Innovation Center will provide FI with better conditions for following the development of the financial sector since it makes the authority a natural part of the discussion when it is not clear how regulations and FI's processes apply to an innovation. This contributes to better supervision and further enhances consumer protection.

Existing regulations and FI's risk-based supervisory approach already currently present excellent opportunities for testing new innovative services and products in the market. When these two components are combined with the Innovation Center, it will be possible to achieve the primary functions of a regulatory sandbox – mainly a close and clear dialogue between companies and the authority – while avoiding the limitations of a sandbox, such as selective grouping, which can be considered to benefit some companies at the cost of others, and conflicts of interest if companies perceive the authority to be standing behind or taking responsibility for certain innovations.

FI also intends to adapt the information on FI's website so it is easier for companies to find the information they need. FI will also continue to work with other wishes expressed by the companies, for example a more transparent authorisation process.

FI also intends to issue more guidance on how to use cloud services.

FI believes that these measures will be able to remove the obstacles the companies are experiencing in both the short term and the long term.

Background

Financial services and products are currently being offered in different ways, in different forms and by different actors than they were before. As a result, the conditions for competition in the financial sector are changing.

In March 2017, Finansinspektionen (FI) was given an assignment by the Government to investigate how the authority can meet the needs that may arise when financial firms want to offer new, innovative financial services.

ASSIGNMENT

The assignment consisted of four parts that were to be presented in a report to the Government no later than 1 December 2017.

1. Describe the actors that offer new, innovative financial services in the Swedish financial sector and categorise them into the areas where they are active.
2. Provide an overview of the questions and needs of these firms given the authority's core processes: supervision, authorisation and regulation. Report also on the measures the authority has taken to meet these needs.
3. Submit a list of measures the authority could take to meet the needs of these actors in conjunction with offering new services and products for firms and consumers in the financial sector in Sweden. Take into account initiatives by foreign authorities and consider the appropriateness of applying similar initiatives in Sweden. The report must contain a schedule for future work on this matter.
4. Identify any regulatory needs for actors offering innovative services to the benefit of firms and consumers in the financial sector in Sweden.

FINTECH

The word "FinTech" refers to innovations in the financial sectors that are made possible by digitalisation. It is used to describe a phenomenon or specific actors, but there is no commonly accepted definition. The abbreviation derives from the words "financial" and "technology".

There are several similar abbreviations that describe sub areas within the financial sectors where innovations are being offered as a result of digitalisation, for example "InsureTech" for services and products on the insurance market and "RegTech" for regulations translated to digital forms for the control and reporting needs of financial firms.

FI AND FINANCIAL SUPERVISION

Financial regulation and supervision are the Government's most important tools for influencing financial firms and the financial system. In its instruction, the Government has expressed FI's responsibility as follows:

“The authority shall work to ensure the financial system

- is stable and characterised by a high level of confidence and has smoothly functioning markets that meet the needs of households and corporations for financial services, and
- provides comprehensive protection for consumers.”

FI’s assignment was also broadened several years ago to include counteracting imbalances on the credit market that could have a negative impact on both financial stability and consumer protection and primarily create macroeconomic problems.

FI has also been tasked with ensuring that the regulations and procedures at the authority’s disposal are cost-efficient and easy for citizens and firms to understand and follow.

Why has FI received this assignment? In terms of stability, an efficient, stable financial system is necessary for the economy to function and grow. A poorly functioning financial system – or in a worst-case scenario, a financial system in crisis – generates extensive economic and social costs. Because individual firms face neither adequate incentives nor opportunities to fully manage these risks themselves, the Government must step in. This is one of the pillars of FI’s assignment.

The need for the second pillar of FI’s assignment, consumer protection, evolved from the fact that many financial services offered in the financial sector – payment services, savings products, loans and insurance solutions – are often complicated and difficult for the consumer to assess. The objectives of having a financial sector that is “well-functioning” and characterised by a “high level of confidence” can be viewed as both general prerequisites and an expression of stability and good consumer protection.

In order to carry out its assignment, FI must consider and assess how innovative services, products and business arrangements affect the protective interests FI is tasked with monitoring within its core activities: authorisation, supervision and regulation. This can include assessing whether an innovative service is subject to financial regulation, as FI did in its assessment of crowdfunding platforms. By monitoring the financial sector, FI attempts to identify risks, problems and any potential infringements of its rules as early as possible.

This said, however, FI has not been given an explicit assignment to promote either technological development or competition in the financial sector. It can be argued, though, that a financial sector in which products are not developing (or are developing too slowly) as a result of poorly formulated regulation or other reasons can hardly be described as being “well-functioning” or meeting “households’ and firms’ needs for financial services”.

It is therefore FI’s starting point that financial regulation and supervision should not obstruct financial development and innovation, assuming that the fundamental objectives of stability and good consumer protection have not been compromised.

DISPOSITION

This report follows the outline presented in the assignment from the Government and begins with an overview of the market. Thereafter follows a section outlining the companies' questions and needs, a section describing the measures FI has taken and, finally, a section considering additional measures. A description of the method that FI used to identify the companies' experiences and needs has been included as an appendix. This appendix also includes a list of the companies that participated in the four roundtable discussions FI arranged together with Vinnova. A second appendix describes in brief the regulatory sandboxes in the UK and the Netherlands.

This report does not focus on the risks associated with various new, innovative services, products and business models.

Overview

The financial sector in Sweden is changing. Traditional actors are being challenged by new actors, which through technological innovations are gaining market shares and applying pressure to the profitability of firms that have been established in the market for decades. The response from the traditional actors is to invest even more in technological innovation. The innovation is driven either by the financial firms themselves or non-financial companies, and often by “start-ups”. It is therefore better to describe the market by categorising innovations than trying to categorise the companies by type.

DESCRIPTION OF THE SWEDISH FINTECH SECTOR

FinTech in Sweden is more about a general wave of innovation and development in the financial sector than about specific companies. Many actors use or want to use the term, “FinTech”. Therefore, FI believes that “FinTech” is more of a trend within the financial industry at large and does not only refer to a number of new actors. Many of the new services that are today challenging established actors with alternative offers and business models will be tomorrow’s normal behaviour in the market.

Over the past ten years, Sweden has experienced strong growth in companies that create new, innovative financial services. FI considers two important factors behind this growth to be a stable economy and a well-functioning public sector. The Internet penetration rate among Swedish consumers is also high (93 percent - 2016) and there is widespread use of smartphones (81 percent - 2016).¹

In addition, it can also be noted that Sweden, and Stockholm in particular, has a large number of system developers. In 2014, “programmer/system developer” was the most common profession in Stockholm’s municipality.²

The use of digital identification has increased sharply. The most-used form of e-identification is Bank-ID, which according to Finansiell ID-Teknik BID AB has 7.5 million users out of 9.0 million potential users.³ The Swedish Tax Agency and Telia also issue e-identification.

Most of the established actors in the financial sector carry out various initiatives to target and establish, support and promote new, innovative services that complement their existing service offering in various ways. The non-financial actors that work with innovation for the financial sectors include everything from sole proprietorships to large international organisations. This variation creates a demand for differ-

1 Svenskarna och internet 2016, Undersökning om svenskarnas internetvanor, IIS (The Internet Foundation In Sweden), 2016. Available in Swedish.

2 Programmerare – Vanligaste yrket i Stockholmsregionen, Stockholm Chamber of Commerce Analysis 2014:3. Available in Swedish.

3 <https://www.bankid.com/assets/bankid/stats/2017/statistik-2017-10.pdf>

ent types of support in everything from discussion forums to meeting places for various interests. The largest single establishment in Sweden is Stockholm Fintech Hub, which is a contact hub for entrepreneurs, established actors and investors. In January 2017, Swedish Financial Technology Association (SweFinTech) was founded and, according to its website, is an independent, non-profit organisation for companies and individuals working in the Swedish financial technology industry.⁴ The association initiates meetings and cooperation with authorities, politicians and other business organisations.

The media often describes FinTech companies as different types of younger or start-up companies that challenge established actors in the financial industry. The number of new businesses in Sweden in the past ten years indicates that there are currently good conditions for establishing a business in the financial industry. A small but contributory reason is the risk-based supervision conducted by FI, which targets the authority's resources to the parts of the market where the risks are judged to be largest and thus allows for the establishment of new business without major involvement from the authority.

The view of technology has changed over time, and technological solutions are considered by several actors to be the actual driver behind the business in contrast to a more traditional view of technological solutions as system support. Technology is also increasingly being viewed as a source of new business instead of only as a cost.

Among the more than 200 companies registered with Stockholm Fintech Hub and that according to their own definition are associated with FinTech, most are small, relatively young and still generating losses. Among the more established actors, profitability comes from classic financial services such as lending, payments, mediation or advisory services. Many of the FinTech services are basically a development of existing financial services. What is new is the way the services are offered to customers, with the customer experience in focus when forming the services.

Many established actors in the financial sector have invested during the past decade in technology that provides economies of scale, but as technology develops, these investments can now be considered obstacles that hinder a company's flexibility to meet up-and-coming challenges. We are right now witnessing a financial sector in transformation. Traditional business models are being challenged and their profitability squeezed.

PAYMENT SERVICES

In general, payment services are the largest area for innovation within the FinTech area. The innovative services often aim to simplify the user experience, sometimes to the point that the payment becomes only a minor event during the moment of purchase. This can apply to both e-commerce as well as physical purchases.

Klarna is one example of a company that offers a classic financial service in an innovative way; it offers customers the opportunity to

⁴ <http://www.swefintech.se/>

use credit when purchasing goods online. Offering credit (financing) in conjunction with a purchase is nothing new. What is new and innovative is how easily financing is offered at the point of purchase in a web shop. Similar services are also offered by other actors, such as Qliro. Services that entail a credit at the point of purchase are popular among consumers in part because the uncertainty that accompanies online selling is reduced if the consumer does not need to pay in advance but rather can wait until the good has been received. In its supervision activities, FI has also observed that the purchasing pattern between online selling and physical selling is disappearing and payments are becoming increasingly channel-independent.

Another example is iZettle, which makes it possible for businesses to receive card payments during the payment transaction. This is also a well-established type of financial service, but the pricing of the service that is offered and the packaging are innovative compared to many traditional companies that offer card payments. The card transaction is transmitted via the mobile telephone network using a special card reader and an app.

NFC (near field communication)⁵ technology and root codes (QR codes, Quick Response codes)⁶, aim to simplify the customer experience. Several card issuers have begun to apply NFC technology to debit and credit cards, which means that the card can be read remotely without needing to draw it through a card reader, which reduces the amount of wear on the card reader and the card itself. Card technology and NFC technology are both now starting to move into our smartphones, which serve as platforms for content suppliers. We no longer need to bring our plastic card to be able to pay, but we become dependent on functional smartphones and the telephone/Internet infrastructure.

Among the more hyped FinTech services in Sweden are aggregation services. Aggregators obtain information from consumers' bank relationships and then present them in different analyses or compilations. Consumers are more likely than before to use several different banks or credit institutions. A larger number of suppliers of financial services means a more fragmented financial overview for the consumer, and aggregators can bridge this gap and provide consumers with a single user experience. The way consumers experience financial services, such as payment accounts, becomes independent of the number of underlying financial firms. Businesses with aggregation services that are based on payment account information will be boosted by the second payment service directive.⁷ FI is also indications that companies providing aggregation services are actively offering other services, for example payments, transfers, savings or loans. The clearest example of such an aggregator is Tink.

MARKET AND INFRASTRUCTURE

There are many financial infrastructure projects under way that already have, or may have, the potential to offer consumers efficient and

⁵ Transfer method for remote transfer of data over short distances.

⁶ A two-dimensional code for optical scanning.

⁷ Directive 2015/2366/EU of the European Parliament and of the Council.

fast payment and transfer services. The largest example in Sweden is Swish, which enables transfers between two parties in real time using the BIR platform from Bankgirot as the underlying platform. At the European level, the ECB project TARGET Instant Payment Settlement (TIPS) can also be mentioned here.

Sweden is one of the countries experiencing a rapid decrease in the use of cash.⁸ As cash disappears from society, consumers become more dependent on accessing the assets they hold at financial institutions. Effective digital payment methods are a prerequisite for well-functioning day-to-day routines. Most payment methods are associated with the consumer receiving an income and holding assets at the banks. These income and assets are used for direct payment, or for indirect payment when using loans at different institutions. Sveriges Riksbank is investigating the possibility of issuing an electronic payment means, “e-SEK” as an alternative to cash.

Development projects are currently under way at stock exchanges and clearing businesses both in Sweden and abroad with the aim of reducing transaction times and streamlining processes. This includes everything from reducing settlement periods to more radical experiments using block chains as asset carriers.

LOANS AND FINANCING

A number of crowdfunding services have been established in the country in recent years. The services are meeting places for investors/lenders and entrepreneurs/borrowers. The exchange of capital is done through ownership in a company (shares) or through a debt instrument (loan). Examples of such companies in Sweden include Toborrow, Tessin, Sparlån, Svaelend, Pepins and Funded by me.⁹

Established financial actors are also considering the possibility of creating services for crowdfunding. An advantage for them is that such a service would not burden the firm’s balance sheet. The financial actor only provides a platform where lenders and borrowers can meet. The supplier provides a purely administrative service, which generates income for the business. At the time of writing, there is a Government inquiry into crowdfunding, in which FI is participating.¹⁰

ADVISORY SERVICES

Advisory services are also increasingly undergoing automation. This development could mean that consumers will have access to advisory services even for smaller transactions, which otherwise would have been rather expensive in relation to the benefit. Automation creates possibilities for offering independent advice, even if the automation is only one piece of the puzzle in this process. FI has recently noted that several new companies are offering automated advisory services marketed as independent.

⁸ <http://www.riksbank.se/sv/Statistik/Betalningsstatistik/>

⁹ See also Finansinspektionen, Gräsrotsfinansiering i Sverige – en kartläggning, 15 December 2015, Ref. 15-17414. An English translation is available at www.fi.se.

¹⁰ Committee Directive, Crowdfunding, Dir. 2016:70

Advisory services can be related to something other than advice about financial instruments. Digital services that compare loans and offer loan advice have become more popular among consumers for both mortgages and private loans. Different types of automated advice that use information about consumers and their wishes have begun to appear.

VIRTUAL CURRENCIES

There are examples of cryptocurrencies in trade transactions in Sweden, for example bitcoin, even though they are not yet considered a common method of payment. However, mining for bitcoins and trading venues for cryptocurrencies are established activities in the FinTech sector in Sweden.

Internationally, ICO (initial coin offering) has emerged over the past few years as an alternative way for operations to raise capital. ICOs are viewed as an investment product, which in very simplified terms can be described as operations that sell a contractually defined right (token) to investors. This right can then be sold to another investor, and the right can even in the future be realised by the company in accordance with the contract. This topic is frequently discussed in international contexts, and in some countries the supervisory authorities have published information about ICOs. On 7 November 2017, FI published a warning about the risks associated with ICOs as an investment product.¹¹ To the extent of FI's knowledge at the time this report was written, no Swedish company raises capital via ICOs.

INSURANCE POLICIES

So far, Sweden has not had as many InsureTech initiatives (technology-based initiatives within the insurance sector) as in other markets. In the USA, for example, there is a growing trend in the health care sector of sickness insurance policies based on apps that measure a customer's health in real time. However, Sweden ranks relatively high in the number of FinTech initiatives that are offered private equity every year. This may mean that it is only a matter of time before several insurance services will be offered digitally or based on technological innovations.

Services that intend to create an overview of a customer's insurance policies are beginning to appear in the Swedish market, but there is resistance within the insurance industry to provide the level of transparency needed for the services to succeed.

Competition in the market for non-life insurance is obstructed by the high entry thresholds. Motivation to introduce new services is lacking since profitability is already high and development costs for new technology would be high. However, FI is seeing that several companies have initiated simpler insurance policies based on the use of telematics, where sensors scanned in real time determine the cost of the policy based on, for example, driving behaviour. This is achieved via a dedicated piece of equipment, such as a fob in the car, or via smartphone apps. There have been price comparison websites for the past few years where customers can also receive offers for non-life

¹¹ <http://www.fi.se/sv/publicerat/nyheter/2017/varning-for-risker-med-initial-coin-offerings/>

insurance policies. Over time, this should lead to better competition within the non-life insurance sector.

In the life insurance sector, several companies have developed robot advisors to handle basic questions from customers. There is also one Swedish company in this sector that primarily targets customers in development countries and where the customers pay for the insurance policy via their pre-paid mobile telephone card.

REGTECH

RegTech (Regulatory Technology) has grown rapidly in recent years. RegTech is considered the part of FinTech where an attempt is made to use technology to resolve or simplify efforts to comply with regulations, for example to fulfil the obligation to review payment transactions to counteract money laundering, to report to authorities or take measures to manage the companies' risks.

Technological solutions can make some steps of regulatory compliance simpler and more efficient through the use of standardised products and services. Technological support for governance and control mechanisms can make it easier for companies to increase their knowledge about their compliance. It also creates conditions for more efficient governance and control of the operations.

Asset control and internal/external identity management and control are also a growing area for RegTech. This applies primarily to the parts related to due diligence processes, but also to other types of internal identity control and traceability in technological systems.

For companies and international operations, RegTech solutions may make things easier by bridging local conditions, behaviour and laws.

Security solutions for the storage of information, governance and control of access to and handling of information and innovative methods to identify deviations in the information also fall under RegTech.

FI is interested in particular in technology that facilitates supervision of the financial sector. This can include technology that makes it possible for the authority to efficiently control transactions or activities.

Questions and needs

Through its collaboration with Vinnova, FI asked a number of companies about the challenges they are experiencing in their innovation activities. It was clear from the responses that the companies have had different experiences and have different needs. Many of the challenges are related to questions about how the rules should be interpreted for an innovation or what the process is for being able to bring an innovation to the market.

ROUNDTABLE DISCUSSIONS

In June 2017, FI and Vinnova organised a number of roundtable discussions with companies from the financial industry. The objective of these discussions was to identify the challenges the companies perceive as stopping or slowing their ability to innovate due to FI's activities or financial regulations.¹²

Four roundtable discussions were held in June at Vinnova's premises. A total of 84 companies participated. The participants came from both small start-ups and established companies within all areas of the financial industry. The condition for participation was that a company (regardless of size) was only allowed to participate in one discussion with one representative.

The method is described in more detail in the appendix, *Roundtable Discussions, Methodology*, and also includes a list of the participants.

The challenges that were identified during the discussions could be grouped into four main categories: FI's role, Information and support, Authorisation process, and Clouds and technology.

FI'S ROLE

The companies say that they find FI's role and how the authority functions to be ambiguous, which leads to misunderstandings and misconceptions. The companies perceive FI to be reactive and say that this perception is enhanced by advice from external consultants not to contact FI directly but rather to rely on the expertise from third-party representatives.

INFORMATION AND SUPPORT

Companies that have authorisation or are considering whether to apply for authorisation say that they would like to see more clarity about the types of different authorisations that exist and how the companies should apply for them. Several companies that are considering whether to start activities that would be subject to authorisation said that it is

¹² Information about and invitations to these discussions were published first on FI's website, www.fi.se, and then spread via social media. FI also met with Swedish Bankers' Association, Insurance Sweden, Swedish Securities Dealers Association, Association of Swedish Insurance Intermediaries, Association of Swedish Finance Houses, Swedish Financial Technology Association and Swedish Private Equity & Venture Capital Association to inform them about the roundtable discussions and encourage them to spread the information on to their members.

difficult to understand what is expected from them. The companies also said that there are tendencies to try to avoid contact with FI. This is considered to distort competition in the market. Several established companies expressed concern about creating new services since they were not sure how FI would view the services based on existing regulations.

The need for information and support highlighted by the companies included everything from access to public information on FI's website to support initiatives in the form of "regulatory sandboxes". A regulatory sandbox is when a company, after receiving approval, tests an innovation in the market while being monitored by the supervisory authority.

The companies that highlighted the advantages of a Swedish regulatory sandbox were large, established financial companies and private equity firms. They felt that the opportunity to test innovations in a sandbox would lower the threshold for the firms to develop new services and products. For investors, an approval of a test in a sandbox would be a control point for making the decision to contribute more capital before a full launch. Sandboxes are described in more detail under *Considerations about additional measures*.

AUTHORISATION PROCESS

The companies' experiences when applying for authorisation can be broken down into two time periods: "before the application is submitted" and "during the application process".

In general, the experiences reflect the same basic questions identified above under *Information and support*.

Before the application is submitted

The companies consider it to be difficult to understand which rules apply to an activity or service and the type of authorisation that is required. The lack of templates for different types of authorisation applications is perceived as a challenge. The companies say that it is difficult to know what an authorisation application that will be approved looks like and what content and structure FI would like the application to have.

This uncertainty and the fact that the companies say they cannot talk to FI about these questions are stated as one of the reasons for why the companies use consultants (e.g. legal firms) to submit an application. The consultants in turn interpret the requirements from FI and the current regulations and provide their own templates, which, according to the companies, in a worst-case scenario leads to either incomplete or unnecessarily extensive applications. For the companies, this results in the additional challenges of supplemental information for the application and unnecessarily long application periods.

Some internationally oriented companies said they are considering applying in another country where the supervisory authorities are perceived to be more open to innovation and FinTech. In the long run, this could mean that innovation companies would leave Sweden.

The companies would like to see a transparent process from the moment they have an idea for a new business or service, where they want

to be able to find information on FI's website that is relevant for the situation in which the company finds itself, until the application for authorisation is submitted. They want to be able to use application templates that have checklists for the required information. Another request is for documents with FAQs that can be viewed on FI's website. The companies would like to have the possibility of "bouncing ideas" off FI at an early stage, for example via a short meeting, in order to become familiar with the regulations that they should be reviewing. They would also like to have the possibility to meet with FI right before they submit their application to ensure that their application is complete. This will save time later by avoiding requests for supplemental information. The companies also would like to have open informational meetings where FI presents the rules and goes through the application process.

During the application process

After an application is submitted, the companies think it should be possible to clarify simple misunderstandings immediately in order to reduce the unnecessary work for both parties and an unnecessarily drawn-out process.

Even if FI has guidelines for handling times for its authorisation applications, the companies say that it is difficult to know how long the application process will take. There is little communication during the handling process, and delays are not communicated clearly enough. In this context, however, it should be mentioned that companies that have had direct contact with FI during the application process, and not through third parties, say that FI's staff is knowledgeable in their area.

The companies would like to be able to follow their application electronically and clearly see what is happening and what will happen in the future. If it is not possible to do this digitally, they would like to at least receive information from the person responsible for their application. They would like to be informed at an early stage about supplemental information that is needed and not when the specified handling period for the application is about to close. The companies would also like FI to communicate delays and causes for these delays.

CLOUD SERVICES AND TECHNOLOGY

The largest individual challenge by far for innovations is clearly the use of cloud services.¹³ Smaller companies highlight cloud services as the only alternative for their operations, while larger companies view it as an attractive solution to having their own operational solutions. Cloud services allow scalability of operations, which cannot be achieved with in-house IT functions.

Common for all companies is that they express in different ways that they are uncertain about FI's view on cloud services and that they have gotten the impression in different ways that FI does not allow the use of cloud services. The companies would like to have a clear re-

¹³ Cloud services include, for example, processor power, storage and functions provided by suppliers as online services. (Data Inspection Board)

sponse from FI and emphasise the importance of FI understanding how key this question is for the companies.

Regarding technological development in general, it is the perception of the industry that FI lags behind. New technological solutions can be difficult to implement since the companies are not certain how FI would interpret them from a regulatory perspective. The companies find it challenging if FI does not clearly take a position on new technology, for example artificial intelligence and block chain technology.¹⁴

Another challenge for the companies is the relatively large absence of standardisation. The companies say that standardisation would promote their ability to technologically function and communicate between companies.

Several companies said that FI should actively encourage the development of technological solutions that are safe for consumers and drive development forward. Even within FI's own supervision, and primarily within reporting, technological innovation can have a positive impact on the activities of both FI and the companies by facilitating the submission of reports.

¹⁴ Block chain technology can be described as a system for a distributed database for documentation of transactions that all participants in a network can access. Since the documentation is available in multiple places at the same time, transactions need to be verified to be registered and everything is encrypted, it is very difficult for a single party to manipulate the system.

Actions to be taken by FI

FI makes the assessment that an effort to provide more information and an opportunity for a dialogue regarding regulations, processes and principles will resolve the majority of the challenges the companies say that they are currently facing. FI will establish an Innovation Center, and the authority will also continue to work on several of the proposals suggested by the companies. These actions also fall within the framework governing FI's role as an administrative authority when carrying out its assignment and the administrative legal principles that apply in Sweden.

The companies' needs can be summarised with one word: information! If the companies have all of the information available about regulations, processes and principles, the majority of the challenges the companies say they are experiencing today would probably be reduced.

Even if the companies are experiencing challenges, it must also be noted that innovation in Swedish is strong. Many new financial services and firms have been established in recent years. The stable welfare system and the well-functioning public sector have been mentioned as two contributors. The national financial regulatory framework and the risk-based method that FI applies are also contributors in that they are not too detailed. They can vary between countries, even in Europe. The supervisory authorities in different countries also to some extent have different assignments.

As described in the section about FI and financial supervision (page 6), FI's assignment is to promote a stable and well-functioning financial sector that is characterised by a high level of confidence and meets households and companies' needs for financial services, while also offering a high level of protection for consumers. FI is also tasked with counteracting imbalances on the credit market that could have a negative impact on both financial stability and consumer protection and primarily create macroeconomic problems. As mentioned, even if it is not expressly stated in the assignment, a reasonable point of departure is that financial regulation and supervision should not obstruct financial development and innovation, assuming that the fundamental objectives of stability and good consumer protection have not been compromised.

In addition to FI's specific role and assignment, there are also a number of goals and restrictions that apply to all authorities and naturally must also be considered. The objectivity principle is of particular interest in this context, and it states that authorities must be objective and impartial in their activities. This principle forbids authorities from following interests other than those they have been assigned or basing their decision on circumstances other than those that according to applicable regulations may be considered when assessing a matter, processing a matter or providing a service.

The equal treatment principle is included in the objectivity principle in that the requirement to treat everyone fairly before the law is a consequence of objectivity and impartiality. The equal treatment principle requires that equal matters be treated equally, and unjustified variations in treatment may not occur.

The measures that FI takes in the form of special initiatives must stay within these guidelines unless the authority's assignment is changed.

General measures taken within the framework of FI's assignment naturally do not need to mean that the assignment has to change. These actions constitute a normal part of the development of activities at the authority.

MORE INFORMATION AND GUIDANCE

FI already answers questions from companies and invites companies to meetings to discuss, for example, how new services will be affected by financial regulation. It is therefore worrisome that the perception is still that it is difficult to obtain information from and maintain a dialogue with the authority. Consumer protection does not benefit, either, from the uncertainty the companies are experiencing.

There are different types of actions that can be taken to raise the current level of information and dialogue, including everything from a general increase in the level of communication for all parties to a more targeted increase. The former is preferable over time since it creates greater independence within the organisation, but it also requires a longer adaptation period.

The authority's strategy document – Finansinspektionen 2020 – already states that the authority should be more communicative. A fundamental idea behind this strategy is that a more informed financial sector faces better conditions for delivering a better selection of services to consumers.

A targeted increase in the communication level could achieve results in the short term. Companies on the Swedish market are very innovative, which is positive. In order to avoid having a negative effect on this development, forcing innovation down other roads that would not be as beneficial for the Swedish financial sector, it is appropriate for FI to take measures that already in the short term would result in improvements in its communication. In order to keep this at a reasonable scope, the targeted initiative should be limited to information and guidance in topics where the regulations and standard practices are ambiguous with regard to innovation.

Establishment of an Innovation Center

FI intends during Q1 2018 to establish a point of contact to meet the companies' need for information and an active dialogue regarding perceived ambiguities in the regulations related to innovation.

The point of contact, which will probably be called the Innovation Center, will be where FI gathers experience within the authority.

By freeing up qualified resources to promote information and a dialogue with companies, FI will be able to meet the companies' needs

for information about rules, processes and principles in the financial sector.

The objective of this action is ultimately to create a more efficient and well-functioning financial sector that offers more customer benefits and better consumer protection by ensuring that the companies face better conditions for innovation. Through better access to information and a dialogue, less time will be needed from the idea of an innovation until its launch in the market.

The Innovation Center will serve as the natural first point of contact at FI for companies that are unsure about the regulations, processes and principles in the financial sector that affect innovation. The Center will also facilitate seminars, informational meetings and FI's participation in external events related to innovation in the financial sector. The central role of the Innovation Center with regard to innovation in the market will make it possible to maintain a clear, internal dialogue within FI regarding the challenges the companies in the financial sector are experiencing.

What FI's Innovation Center will do

Dialogue

The Innovation Center is a point of contact for companies and will enable a dialogue with FI. Contact with the Center can take place by telephone, by email or in person. The Center will provide information and guidance, for example regarding tests of innovations.

Information

The Innovation Center will adapt information to the target group. For example, FI can adapt the information on its website and produce podcasts. The Center participates in and arranges seminars and lectures.

Coordination

The Innovation Center is a catalyst within FI's internal discussion about innovation. This raises the authority's knowledge about, for example, new innovative services, which contributes to the supervision activities and enhances consumer protection. The Center also arranges discussions between Swedish and foreign authorities regarding innovation.

The Innovation Center will comprise a number of experienced employees from FI's various sections.

The creation of the Center will provide FI with better conditions for following up on the developments in the financial sector since the authority will become a natural participant in the discussion when regulations and FI processes are perceived as unclear in relation to an innovation. This also improves the supervision activities and further enhances consumer protection.

Even if it is difficult today to appreciate the sector's full need for more information and guidance, FI makes the assessment that there is a considerable need for this type of center. Initially, the authority will use appropriation savings to immediately establish and begin the build-up of the Center. In the long run, and with a higher ambition

level, it is FI's assessment that the appropriations will need to be raised, a topic which FI intends to return to in the budget for 2019-2021.

FI has also considered whether the Innovation Center could also offer various types of support for companies, for instance advisory services or driving market development. These actions tend to fall more towards the "promotion" of development and innovation than "not being a barrier". Such an approach requires different resources than those that have been estimated for the Center that will be established after the start of the new year. These actions would also require a clarification of the authority's assignment to include the promotion of technological development or innovation. The Innovation Center will therefore not support companies in this respect.

Cloud services, more information and more efficient authorisation process

The greatest single challenge the companies mentioned during the roundtable discussions was the use of cloud services. They said that they were not sure about FI's view of such services. FI does not see any reason on principle why financial firms would not be able to use cloud services at external suppliers. The European Banking Authority will soon publish joint EU guidelines for cloud services. FI has participated in this project and plans to issue additional guidance that refer to these guidelines.

The roundtable discussions with companies in the financial industry generated quite a few good suggestions for general measures FI can take that will lead to improvements for all companies. These measures also benefit companies that work with innovation and include templates for authorisation applications, FAQs on FI's website and a simplified digital application process. FI will continue to work with these suggestions, and the establishment of the Innovation Center will serve as a catalyst in this work.

Other implemented measures

A dialogue between authorities – both national authorities and supervisory authorities in the Nordics – has been initiated. The preliminary objective of this initiative was to exchange status reports on the work with innovation at each authority and explore the interest in a continued dialogue. The idea is that such a dialogue could facilitate the work of the authorities in handling questions that arise in relation to innovation in the financial sector. For FI, the next step is to invite the authorities to discuss how to cooperate on innovation-related topics and to facilitate innovation-related activities.

Additional measures considered

Several countries have introduced the possibility of companies testing innovations in the market under supervision of the supervisory authority, which is often called a “regulatory sandbox”. However, FI considers the concept to raise more questions than it answers. FI also notes that innovation has always existed in the financial sector and is already strongly rooted in Sweden. By establishing an Innovation Center, FI believes it will be able to address the uncertainties the companies raised about regulations, processes and principles regarding innovation in the financial area. FI therefore proposes at this time not to introduce a regulatory sandbox.

REGULATORY SANDBOX

At the roundtable discussions, the larger financial companies and private equity firms raised the opinion that there is a need for “regulatory sandboxes”. The assignment from the Government also says that FI should consider if such an approach is appropriate in Sweden.

Several supervisory authorities, both in Europe and in other parts of the world, have introduced regulatory sandboxes to make it easier for innovations to reach the market. Meetings held with the supervisory authorities in the Nordics, the UK and the Netherlands have shown that there is no common definition. What one authority calls a regulatory sandbox can be called an innovation hub by another authority. What all of them have in common, though, is the ambition to remove unnecessary obstacles for financial innovations to enter the market on the condition that the innovation is considered to be of benefit for consumers and not pose risks to the stability of the financial system and consumers.

The methods and forms for reaching this goal vary between countries. The UK opened its regulatory sandbox in June 2016 and the Netherlands in January 2017.¹⁵ Finanstilsynet in Denmark has received an assignment to introduce a regulatory sandbox, but its structure has not yet been determined. There are also regulatory sandboxes in Singapore, Australia and Japan. Lithuania has introduced a public consultation for a potential regulatory sandbox. Some supervisory authorities have also expressed scepticism about this concept, including BaFin in Germany.¹⁶

Providing a regulatory sandbox should not be viewed as an isolated event to contribute to development, but rather must be viewed against a background of the larger projects the authorities are conducting to handle innovation.

¹⁵ The regulatory sandboxes in the UK and the Netherlands are described in the appendix, *Regulatory sandboxes*.

¹⁶ https://www.bafin.de/SharedDocs/Veroeffentlichungen/DE/Reden/re_170926_Hachenburg_p.html

A regulatory sandbox, in brief, is a free zone for the company to test innovations in the market with real customers under strict conditions and supervision of the supervisory authority. The concept itself introduces several fundamental questions for a supervisory authority: Is it reasonable for a supervisory authority to promote one company over another? How is confidence in the authority assured? How are conflicts of interest handled at the authority? Someone needs to decide which companies may and may not participate in the regulatory sandbox. The public expects that the authority will not expose consumer to risks. Someone needs to give the companies instructions to keep risks in the business at a controlled level at the same time as someone needs to exercise supervision of the test operations. Because innovation activities are not new and have always been present in the financial sector, the question can also be raised whether the fact that an authority administers a regulatory sandbox could mean that the sandbox itself could affect competition in the market. Is a company that does not receive authorisation to test its activity in the regulatory sandbox prevented from testing the product on its own?

A SWEDISH REGULATORY SANDBOX

It is not easy to answer the question about whether a Swedish regulatory sandbox is appropriate or not. This is how FI has reasoned.

One argument in favour of a regulatory sandbox is that it would lower the threshold for companies to develop new services and products. It would also give investors a better basis for decisions to contribute capital prior to a full launch.

All of the countries in the EU that have regulatory sandboxes require the companies to first apply for some type of authorisation. A regulatory sandbox, in other words, is not about allowing test products in the market without first fulfilling certain regulations. In the UK, a rapid process is promised for a limited authorisation on the condition that the company meets certain basic requirements.

FI agrees that one condition for providing services subject to authorisation is that the business must meet certain basic criteria to ensure there is no risk posed to confidence in the market or consumers. This requirement also applies to testing activities that require an authorisation on a limited scale.

Some regulations have high barriers of entry for a company to receive authorisation, for example the regulations for securities business, insurance business, banking and financing business and businesses such as stock exchanges and marketplaces for financial instruments. Regulations that steer these operations are deeply anchored in EU law. FI believes that there are very small possibilities for adapting these regulations so an individual company can receive authorisation on simpler grounds.

The legislator could give FI a mandate to decide on exemptions to the regulations. Such a mandate would primarily only be able to apply to national provisions in order not to risk distorted competition on the European financial sector. The Financial Conduct Authority in the UK has such a mandate for rules that the authority has decided on itself. However, Sweden has relatively few national regulations that would

be eligible for such a mandate, and FI has decided itself on even fewer provisions. FI is also doubtful about how such decisions on exemptions from the regulations would be viewed in terms of competition since they would create differences between companies that are in the same market.

Even if EU law and a mandate to exempt companies from applying national regulations is problematic, there are already businesses subject to authorisation and registration obligations where the entry requirements are lower and the regulatory burden is lower. Such regulations could be suitable during an establishment phase. This applies, for example, to payment service operations and lending operations that are not linked to mortgages.¹⁷ By providing information and guidance, companies can be informed about such alternatives to the larger legal framework without needing to establish a regulatory sandbox.

During the test in the regulatory sandbox, adapted requirements are placed on the activities being tested. The degree of adaptation depends on the rules that steer the activities and the supervisory mandate. During the test period, firms would be subject to enhanced supervision.

As mentioned previously, innovation activities have always existed in the financial sector, and it is FI's assessment that the regulations also allow companies to test innovations under controlled forms. Risk-based supervision is also important for not obstructing innovation in that it allows companies to act independently as long as there is not a risk that stability and consumer protection will be circumvented.

The challenges the companies are experiencing, and that lead to uncertainty, are due to a perception that information about regulations and authorisation processes are hard to access. FI can be clearer and provide information, for example, about how the authority views innovation tests. FI will introduce an Innovation Center in Q1 2018 as part of a targeted initiative for information and guidance. The idea is to provide a stepping stone for a development towards companies receiving a more concrete view of the regulatory environment. FI makes the assessment that such an approach, together with other initiatives for clearer information and simpler authorisation processes, is more important than a regulatory sandbox.

It is also possible that the introduction of a regulatory sandbox by the supervisory authority may lead to a perception that innovation testing is not allowed outside of the regulatory sandbox. FI's capacity to facilitate testing will always be restricted. This could hinder innovation. By supporting innovation with information and guidance through dialogues, there is less of a risk of this occurring and should resolve the uncertainty the companies say they are experiencing and that slows their ability to innovate.

If we still were to assume that a regulatory sandbox is appropriate because it fulfils other objectives than those that information and guidance initiatives can fulfil, there are a number of questions that first need to be answered.

¹⁷ Payment Services Act (2010:751), see e.g. Chapter 2, section 3 regarding exemptions from the authorisation obligation and the Certain Consumer Credit-related Operations Act (2014:275).

It has been mentioned above that a regulatory sandbox under FI's responsibility could mean that FI will have an active influence on competition in the market. FI currently does not have an explicit assignment to promote competition. Even if such an assignment could be interpreted from FI's current assignment to ensure that the financial sector is well-functioning, it is doubtful if the task would go to FI to participate in tests of innovations that could challenge other established actors in the market. The mere act of establishing a regulatory sandbox could hinder competition in the market if companies believe that they are not allowed to test activities outside of the sandbox.

The innovation companies that participated in the discussions have not themselves requested a regulatory sandbox. They would like better information and guidelines from the authority. A regulatory sandbox does not really meet this need. The question must therefore be raised - which companies would benefit from a regulatory sandbox? It is undeniable that established financial companies that formally would like to be able to hold their test operations at arm's length would benefit from a regulatory sandbox. However, FI considers it to be possible to test innovations in the market today without major risk, as long as it is done under controlled forms and does not expose consumers to risk. FI can provide guidance for such tests through information and a dialogue without needing to establish a formal regulatory sandbox.

Another question is how the selection process for testing an innovation in the regulatory sandbox would be carried out. As an authority, FI must remain objective and impartial. It is possible to establish objective criteria to be approved for a test in a regulatory sandbox, but the test operations also require resources from the supervisory authority. Objective criteria therefore need to be constructed in such a manner to ensure that there is no risk that the authority's regular supervision assignment would be subordinated at the same time as resource limitations may not counteract innovation.

It can be tempting to establish a Swedish regulatory sandbox, but as a whole the concept raises more questions than answers. FI makes the assessment that the initiative it intends to take to improve information and guidance has greater potential to succeed than the establishment of a regulatory sandbox. An Innovation Center creates a forum for dialogue, and not just for companies that are uncertain about rules, processes and principles. It is available for all companies that plan to test new services. FI is not obligated to intervene if a determined breach is negligible or excusable and the company rectifies the deficiency. The companies' need for support and guidance to test innovations thus can be fulfilled without establishing a regulatory sandbox.

Innovation is strong in Sweden, and FI makes the assessment that there are no real negative effects from deciding at this point in time not to establish a regulatory sandbox. This means there is also no need at this point to consider any regulatory changes.

Appendix - Roundtable discussions, methodology

ASSIGNMENT

The assignment from the Government states that FI should identify the obstacles companies are experiencing and then implement or propose measures to rectify them.

An important starting point for FI was to gather the opinions of the companies themselves. FI's role as a supervisory authority can be in conflict with the companies' willingness to openly offer their opinion. FI normally obtains information from the industry through industry associations or surveys.

The conditions that were established in this context therefore focused on ensuring that all participating companies would be able to offer their opinion while at the same time being confident that they could state their opinion without risk of countermeasures from FI. The method would offer anonymity and ensure the quality of the information that was gathered.

SOLUTION

Together with Vinnova and a consultancy firm (Transformator Design AB) hired by Vinnova, a method was developed to meet the challenges inherent in the assignment. The method aimed to create a safe environment where the companies felt free to raise the obstacles they have experienced in conjunction with financial regulation and FI. The method would assure the quality of the information discussed while also ensuring that it was easy to obtain the opinions of up to 100 companies in a manageable format.

Two meetings were arranged for the companies that currently have some form of authorisation from FI, one meeting was arranged for companies without authorisation and one meeting was open to all companies. A limit of 25 participants was set for each meeting. At the most, 23 people participated in a meeting.

The meeting was called a "roundtable discussion" in the invitation, but in reality it was more like a workshop for the companies. The participating companies received two preparatory questions in advance:

- Which situations and events/activities in relation to the issuance of authorisation and regulations have been important to establish a FinTech service? Why?
- Which challenges and questions have arisen with regard to, for example, authorisation, supervision and regulation related to these events/activities?

Each meeting lasted 3 hours, and the participants were divided into groups of 4–5, often with similar business interests. Each group also had a host from Vinnova and in most cases a representative from FI. Their assignment was to explain the method and keep the group on track given the focus of the exercise.

The process for the meetings was a semi-structured mapping exercise where the participants list the obstacles they experienced and during which phase of the innovation process. The participants then discussed these obstacles with the others in the group before later describing if and how they had overcome them. The meetings concluded with each group compiling the information from their discussion and presenting it to the other groups.

The material each participant and group created during the meeting was anonymous and consisted of small pieces of paper (Post-it notes) that were hung up on a board for each group. The participants were therefore able to feel safe and anonymous at the same time as the material was left behind without links to individual companies.

PRACTICAL IMPLEMENTATION

The meetings began with opening comments by Vinnova and FI and a review of the assignment from the Government. (15 min)

The participants were thereafter divided into groups of 4–5 and the working method was introduced. (40 min)

Each participant was then invited to write down on Post-it notes the obstacles their company had experienced and the event during which the obstacle arose. (20 min)

Each participant presented their obstacles and events for the other companies in the group. This step often resulted in an interesting and productive discussion between the companies since the recognition factor was often high. (40 min)

Each participant then wrote down how they had gotten around or overcome their obstacle and shared this with the group for discussion. (20 min)

Finally, each group presented the most important obstacles they had discussed for the other groups. (40 min)

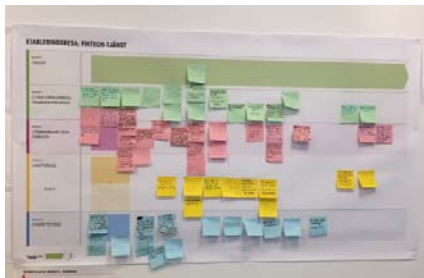
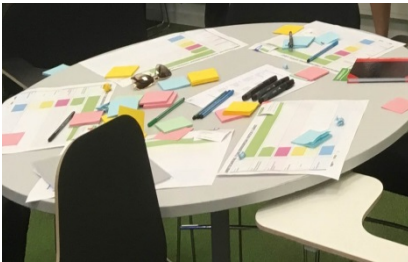
All four days followed the same structure and working method. The participants were primarily senior managers at or the CEO of the company.

ASSESSMENT OF THE METHODOLOGY

FI considers the methodology to have been an effective way of obtaining opinions and receiving feedback from the industry. FI also considered using traditional discussions with industry associations or surveys of the companies. FI's conclusion is that the chosen methodology allowed for a discussion and interaction between companies that would have been otherwise impossible.

Both small and large companies were able to present their experiences and opinions, which were then documented in such a manner as to preserve anonymity. For FI, it was important that the companies be given the opportunity to be as honest as possible about their experiences. As a result, FI also received a wide range of feedback, which has been extremely valuable in FI's subsequent work deciding what the authority can do to contribute to a positive climate for innovation in the financial sector.

Vinnova also conducted a survey of the participants after the meetings. The survey contained a number of questions about their view of FI and the meetings that were held. The responses to the survey indicated that the companies in general felt the meetings were very positive, as was the chosen method. Many companies also went so far as to say that this exercise had positively changed their view of FI.



LIST OF PARTICIPANTS

12 June	13 June	16 June	19 June
AMF Pension	Advisa Ab	2elev8 it ab	Capco
Avanza	Alecta	421	Deloitte AB
Captor Investment Management AB	Avida Finans	City Network	Enigio Time AB
ClearOn AB	Betalo AB	Dreams	EY Law AB
Europeiska ERV	Bliwa	E24 Finance AB (publ)	Ginnungagap AB
Handelsbanken	Collector Bank AB	Europay Sweden Visa Sweden	Goobit AB
Landshypotek Bank	Danske Bank	GRC Watch	IBM
Lysa	Insurance Simplified Europa AB	Instantor AB	Inkassogram
Länsförsäkringar Gruppliv	iZettle AB	MokanTech AB	Itello AB
Nord Fondkommission	KLARNA	NFT Ventures	Kameo svensk Filial
Northmill AB	Kreditbörsen Sverige AB	Norbloc	Kidbrooke Advisory
Monark Finans AB (prev. 24Money Payments AB)	Nasdaq	NOWONOMICS	Lendify AB
Optise AB	Nordea	Omeo Financial Consulting	MAQS Advokatbyrå
Skandiabanken	Pepins	Primepilot AB	Mastercard
Sparplatsen	Savelend Sweden AB	Påmind AB	Movestic Liv och Pension
SPP Pension och Försäkring	SBAB	Småspararguiden	Näktergal Financial Technology
Stabelo 2 AB	Sparlån Sverige AB	Tessin Nordic AB	PEI Development AB
Svea Ekonomi AB	Swedbank	Trapets AB	PwC
Tieless/Stellum	Söderberg & Partners	Wrapp	Sawance AB
Tink AB	Telia Finance	One company under formation	stoEr
Trustly Group Ab	Toborrow		TriOptima AB
Trygg-Hansa	Waizer AB		
	Änke- och Pupillkassan		

Appendix - Regulatory sandboxes

UNITED KINGDOM

The supervisory authority in the UK, Financial Conduct Authority (FCA), describes its regulatory sandbox as follows:

”... a ‘safe space’ in which businesses can test innovative products, services, business models and delivery mechanisms in a live environment while ensuring that consumers are appropriately protected.”¹⁸

The test environment is for companies, both those already with authorisation from FCA and those that could be granted authorisation, that want to test a product or service which does not easily fit into the existing regulations.

There are four eligibility criteria to be approved for a sandbox:

- The service/product must be so innovative that there are no other similar products/services in the marketplace.
- The innovation must offer a good prospect of improved benefit to consumers, either directly or indirectly via heightened competition.
- There is a genuine need to test the innovation. This may mean that the innovation does not easily fit the existing regulatory framework, making it difficult to get the innovation to market, or the full authorisation process would be too costly/difficult for a short viability test.
- The company must be ready to test the innovation. For example, there must be a testing plan, resources, risk assessments, safeguards for consumer protection and a plan for how the attempt can be wound down if it does not work.

FCA offers a number of tools for sandbox businesses:

- The FCA is able to offer restricted authorisation to business that are not ultimately subject to EU law. All business subject to an authorisation obligation under EU law or national law must also receive authorisation to participate in the sandbox. No exemptions are allowed from the authorisation requirement set out in EU law. Companies that have not yet received authorisation can undergo an adapted authorisation process that results in restricted authorisation in terms of the number of customers and volumes for a limited period of time, with regard to national regulation.
- FCA can provide individual guidance on how rules for the business in question are to be applied. As long as the company follows FCA’s instructions, there is no risk that FCA will intervene. This is primarily adapted to companies that already have authorisation but want to test a new product or service.
- FCA may allow some easements for companies with regard to FCA’s own regulations, but not EU law or national law. A company that would like to test a financial solution for six months, for example, only needs to prepare a business plan and have financing for those six months.

¹⁸ Source: <https://www.fca.org.uk/news/press-releases/financial-conduct-authority-unveils-successful-sandbox-firms-second-anniversary>

- FCA is also able to issue no enforcement action letters, which basically is a promise from the authority that it will not intervene in the event of unforeseen breaches. FCA to date has not issued any such letters.

All companies that conduct business in the sandbox are subject to intensified supervision during the testing period. FCA steers the business actively through informal directives. The authority also requires that the company informs its customers and stakeholders that the business is being conducted during a testing period. The company must also have a plan for winding down the test in an orderly manner, back-up systems, etc. It should also be noted that FCA has an explicit assignment to manage matters related to competition.

In October 2017, FCA published a report on the lessons learned from the sandbox during its first year.¹⁹ FCA says that the sandbox has become important as a learning process for the authority. By following how a test develops, the authority identifies obstacles to innovation. The sandbox does not capture all challenges a company is facing, but it does offer companies access to regulatory expertise, which has reduced the time and the costs of getting innovative ideas to market. The sandbox, which is FCA's own creation, is described as successful in the report. Sixteen of the twenty-four applications that were approved for the first sandbox cohort continue to develop after the test. There were also observations that it was easier to obtain financing from private equity firms if FCA granted a company test authorisation. Another lesson, however, is that it is difficult to test certain business models on a small scale since the basic requirements for authorisation are high. One example is companies without authorisation that want to test insurance products and new marketplaces. These regulations come from the EU, and the FCA cannot offer any easements from their requirements.

THE NETHERLANDS

Supervisory authorities AFM (conduct) and DNB (prudential) have established a joint regulatory sandbox that is briefly described below:

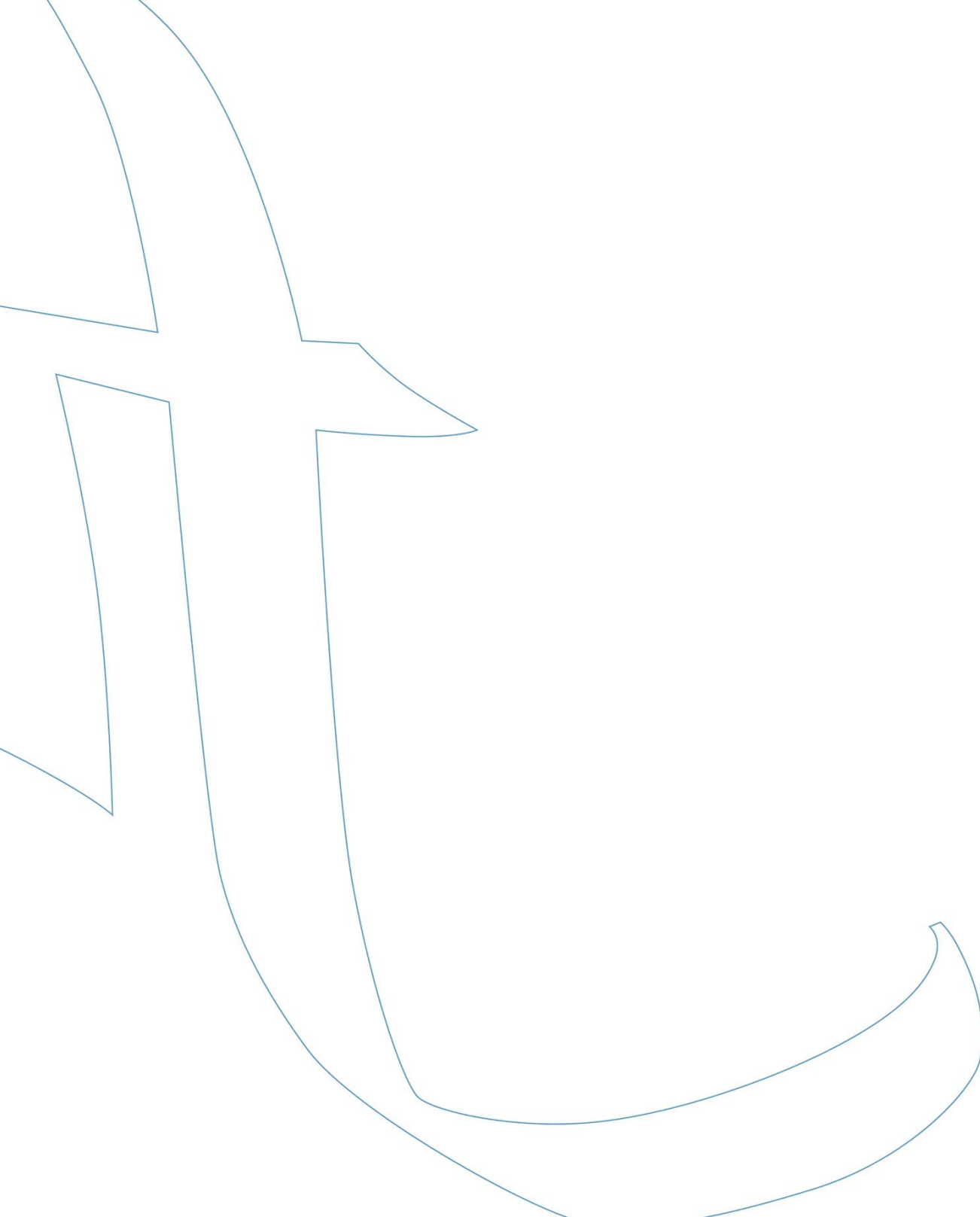
“The core premise of the regulatory sandbox is that supervisors will focus on the real purpose of policies, rules and regulations when assessing innovative products, services or business models. And if these purposes are met, they will use the scope offered by the law to provide a bespoke solution.”

The test environment is for companies which already have authorisation and want to test a product or service that does not easily fit into the existing regulations. A company that does not meet specific rules or policies prior to the launch of a product or service but has alternative solutions for how the current regulations or policies can be met can benefit from the sandbox. AFM or DNB determines if a regulation places unreasonably high requirement on the company in terms of innovation and whether an alternative application of the regulation is possible.

Example: An innovative fund manager makes it possible for its customers to gradually increase the value of their funds with incremental deposits at the same time as the manager gradually maps the customers' finances, knowledge and risk appetite. If the supervisory authority considers such a procedure to be aligned with the spirit of the law, i.e. that the company fulfils its duty of care, the company does not need to apply the procedure that has been established via practice, i.e. create a complete investor profile of a customer at the first meeting.

¹⁹ Regulatory sandbox lessons learned report, Financial Conduct Authority, October 2017.

The Dutch sandbox is ultimately restricted by the regulations a company wants to apply in an alternative manner. Binding regulations such as EU regulations and national law that implement EU law create very restricted, if any, opportunities for alternative applications. It is therefore primarily the authorities' own policies and recommendations that allow for some manoeuvrability. Guidelines from the European supervisory authorities, EBA, ESMA and EIOPA, can allow for alternative procedures that live up to the spirit of the guidelines.



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