

CALL FOR VIEWS

INNOVATION



SUBJECT: CALL FOR VIEWS ON ESTABLISHING A REGULATORY SANDBOX

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1. INTRODUCTION

- 1.1. The Cyprus Securities and Exchange Commission ("**CySEC**") is responsible for ensuring investors' protection, market integrity and the smooth functioning of the capital markets.
- 1.2. The emergence and wide-spread adoption of financial technology has become key in shaping the landscape in which our regulated entities operate. This trend has been further reinforced by the new reality that the COVID-19 pandemic has created, namely an increasingly digitalised environment, where most services are accessible online, which in effect results in moving away from traditional face-to-face interactions to non-face-to face online channels.
- 1.3. The aforesaid trend provides new opportunities for financial institutions and end-clients but at the same time it creates new idiosyncratic risks.
- 1.4. In the context of encouraging responsible innovation and addressing the possible risks stemming from innovation, CySEC has been supporting innovative businesses and market participants who are introducing innovative financial products or services, through its Innovation Hub¹. This took place principally through assisting them in building their understanding of any applicable regulations and compliance requirements. CySEC has also been engaging with providers of emerging financial technologies to determine and accelerate their business models, in line with CySEC's commitment to ensuring investor protection.
- 1.5. By means of this call for views, CySEC intends to proceed to an exchange of views with interested stakeholders (including regulated entities and/or other Fintech² or Regtech³ companies, as well as their professional associations from Cyprus or abroad) on establishing a Regulatory Sandbox⁴, its scope and the testing process thereof.

2. OUR APPROACH ON INNOVATION

- 2.1. CySEC takes a '*technologically neutral*'⁵ approach to assessing innovation and Fintech, as the technology itself is not subject to supervision.
- 2.2. More specifically, the end-product or service that the innovative technology in question enables, is analysed to determine whether it is captured by the existing

¹ The CySEC Innovation Hub was established in late 2018 and it is accessible through CySEC's website [here](#).

² A term that encompasses any technology used in the context of providing financial services to clients that disrupts, augments, or streamlines traditional financial services, by way of digitalisation.

³ A term that encompasses any technology used that may facilitate the compliance with the regulatory perimeter or the delivery of regulatory requirements.

⁴ A controlled environment operated by a regulator, enabling the testing of innovative technologies, products, services or approaches, ensuring that appropriate safeguards are in place.

⁵ Such approach ensures that similar activities and assets are subject to the same or very similar standards regardless of their [technological] form.

regulatory framework that falls under CySEC's competence. If the end-product does come under an existing regulatory framework, the relevant sectoral rules triggered apply. The specific risks associated with the technology used, must be evaluated, addressed, and mitigated by interested parties.

- 2.3. CySEC supports responsible innovation, ensuring that the compliance of regulated firms with their obligations under the regulatory framework is not compromised.

3. INNOVATION RELATED STEERS

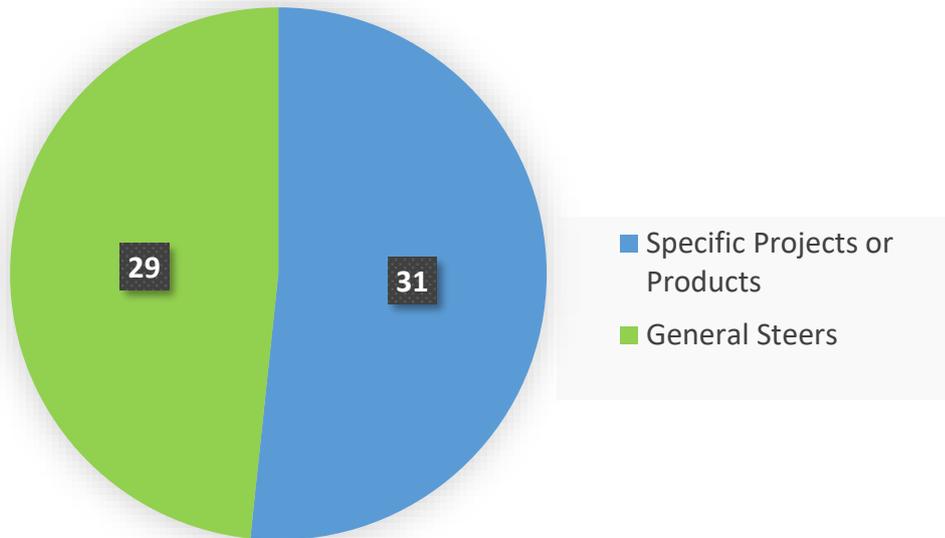
- 3.1. The CySEC Innovation Hub serves as a platform for both supervised and non-supervised entities to get access to regulatory steer and to share knowledge with them, enabling the easy transfer of information on how existing regulation applies to new products or business models and to clearly determine whether their innovative products or services fall within the existing regulatory framework.

- 3.2. More specifically, CySEC's Innovation Hub has been providing developers and users of Fintech and Regtech solutions, with unofficial perimeter steer as to whether the solution in question amounts to a licensable service or product (e.g. tokenised financial instruments); or whether it constitutes a non-licensable tool assisting in the provision of a regulated service or compliance with applicable rules (e.g. client onboarding by regulated entities by means of a '*contactless-selfie*'). In the context of the '*soft-law*' nature of the Innovation Hub, unofficial feedback had also been provided to applicants as regards the merits of the solution in question, following a relevant presentation to the Innovation Hub's team, aiming, inter alia, at:

- Optimising the operations of supervised entities to enhance investor protection;
- Helping firms deploy new technologies that streamline the compliance burden;
- Improving the efficiency of the market by reducing costs and time for supervised entities and investors to conclude transactions;
- Fostering market competition.

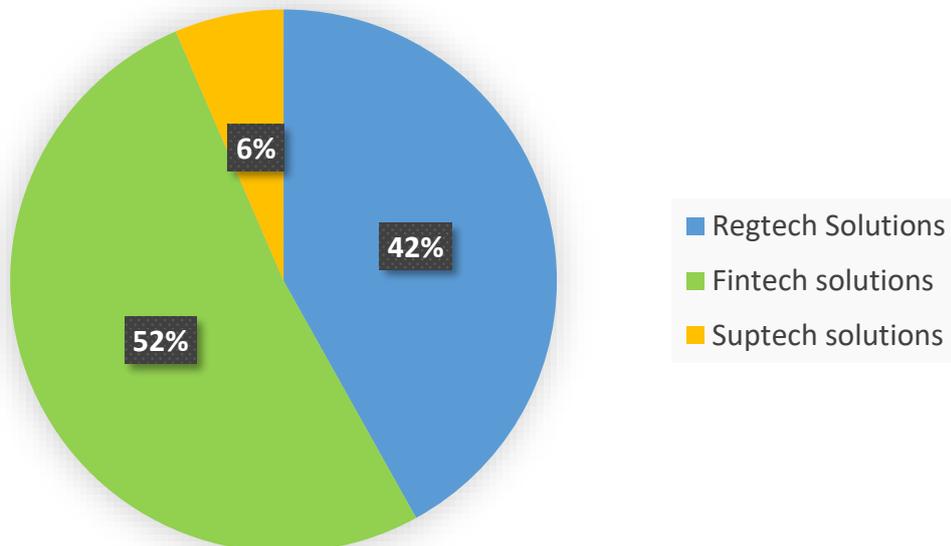
- 3.3. Since its inception in October 2018, CySEC's Innovation Hub has received several applications for assessment of innovative projects and for providing guidance on '*regulatory perimeter*' queries. The applicants were both regulated entities as well as unregulated innovative solution providers from Cyprus and abroad. As to applications for assessment of innovative projects submitted, these related to **31** projects in total, involving Artificial Intelligence, Big Data and Distributed Ledger Technology ('**DLT**'). In addition to the aforesaid, general steer in relation to CySEC's approach on Innovation was provided in **29** cases:

GENERAL OVERVIEW



3.4. The firms and stakeholders who interacted with the Innovation Hub around specific projects or products could be classified into the (sub)categories of Regtech⁶, Fintech⁷ and Suptech⁸ as follows:

BREAK DOWN OF SPECIFIC PROJECTS AND PRODUCTS



⁶ Regtech solutions as described under footnote 3 above herein, including in particular those related to the AML/CTF framework.

⁷ Fintech solutions are described under footnote 2 above herein.

⁸ Solutions aiming at enhancing the regulator's potential for ongoing supervision.

- 3.5. In addition to the work undertaken by the Innovation Hub since its inception, CySEC's Policy Department (under the responsibility of which the Innovation Hub operates) assessed from September 2021 up until today **62** queries relating to crypto-assets, as consequence of the issuance of the CySEC's Policy Statement on the Registration and Operations of Crypto Asset Services providers in September 2021⁹.

4. ESTABLISHING A REGULATORY SANDBOX

- 4.1. The recent factual and legislative developments, such as the COVID-19 pandemic, the registration of Crypto-Asset Service Providers (CASPs), pursuant to the 5th AML Directive, the upcoming pilot regime for market infrastructures based on distributed ledger technology (DLT)¹⁰ and the upcoming regime on digital operational resilience for the financial sector known as DORA¹¹, suggest that financial innovative solutions should be assessed from an operational perspective as well.
- 4.2. Therefore, CySEC intends to proceed to an exchange of views with interested stakeholders (including regulated entities and/or other fintech companies as well as their professional associations from Cyprus or abroad) as to the merits of establishing a Regulatory Sandbox, its scope and the testing process thereof.
- 4.3. To this end we invite interested parties to indicate their interest in participating in the aforesaid exchange of views, **by 28 March 2022** the latest. Interested parties are kindly requested to express their interest by emailing us at innovationhub@cysec.gov.cy, providing a brief paragraph in relation to their background and their innovation related activities.

⁹ See [here](#).

¹⁰ See [here](#).

¹¹ See [here](#).