

Executive summary

The establishment of a regulatory sandbox by Czech Authorities could foster innovation in the financial sector while allowing supervisors to observe and address emerging risks associated with the deployment of innovative technologies in finance with potential benefits extending to all stakeholders involved. Enhanced communication and interaction with FinTechs through constructive dialogue and customised guidance, clear guidance as to the license category corresponding to the innovative business model, and support in preparing a licensing application are some of the potential benefits for FinTechs who can make more informed decisions, develop tailored strategies, and ensure compliance with applicable regulations. Czech Authorities can enhance their understanding of how such innovative mechanisms may alter the risk profile of certain financial activities, and, in turn, facilitate the development of adequate policy responses, if required. Visible efforts to improve the dialogue between the supervisor and FinTechs can increase the confidence of investors about the viability of local FinTechs and the attractiveness of the domestic FinTech market and signal an openness towards safe innovation in finance, encouraging FinTech start-up activity.

Legal certainty can be enhanced by a regulatory sandbox without the need for bending rules for FinTechs when existing rules and regulations continue to be applied within the framework of such facilitator. Additionally, a regulatory sandbox can benefit supervisors by enabling them to better monitor the activities of FinTechs and ensure compliance with new regulatory frameworks (e.g, Markets in Crypto-assets (MiCA) Regulation, Distributed ledger technology (DLT) pilot regime), while also allowing them to consider any necessary tools and resources needed to ensure proper enforcement of regulations in such new areas.

The recommended design for a Czech regulatory sandbox is based on the feasibility study for its implementation in the Czech Republic and is tailored to the specificities of the Czech ecosystem, considering relevant opportunities and limitations of the domestic environment. The key design recommendations for the Czech Regulatory Sandbox are as follows.

Definition of “innovative financial product”: a new or improved financial product, service, or business strategy that leverages novel/emerging technologies to provide innovative/enhanced financial services.

Objectives of the proposed regulatory sandbox for FinTechs: facilitate innovation and speed up productive innovation; promote competition and financial inclusion in the financial sector; facilitate the adoption of new technologies; and attract FinTechs.

Recommended scope: cross-sectoral with no restrictions concerning the sector of activity, if it falls under the remit of the financial authorities, directly or indirectly. In this context, ‘indirectly’ refers to financial activity that may not fall under the existing definitions of activities requiring a license from Authorities but may still have an impact on the financial sector. Applicants must comply with the eligibility criteria in all cases.

Limits of the testing environment: The recommended structure advises against the provision of any waivers, restricted authorisations or other relaxation of existing applicable rules, which would anyway be against EU rules. It is recommended that a proportional application of existing regulatory and supervisory requirements, as embedded in EU financial services regulation, is used as appropriate, and at the discretion of the supervisor for firms participating in the Czech regulatory sandbox. Such proportionality can apply to the governance process and system and control requirements, board composition; financial

soundness; reputation; management experience and track record. Proportionality should be applied on a case-by-case basis by the supervisor, depending on the business model and the applicable rules.

Regulatory and supervisory oversight: The recommendation for the Czech regulatory sandbox to maximise operational benefits and improve the dissemination of regulatory clarity on the one hand, and understanding of business models by the supervisor on the other hand, is to have the sandbox set up by the Authorities. The practice in all EU regulatory sandboxes has been for regulatory sandboxes to be established at the supervisory authority. Since the suggested testing framework will not offer exemptions to participating firms in the sandbox beyond those provided by national and European law, there is therefore no need for legislative changes for the establishment of a regulatory sandbox. The Czech Authorities could establish the regulatory sandbox by an internal act or by designating which posts will be dedicated to co-ordinating its operation within the relevant Authorities.

Standard regulatory vs. data sandbox: The recommendation for the Czech sandbox is to commence with the establishment of the 'standard' regulatory sandbox and, to the extent feasible, provide data-sharing when the conditions allow it. The feasibility of this option will be based on (i) the availability of datasets and ability to make these available; (ii) the capacity of the authorities participating in the regulatory sandbox. It could also be envisaged that a data sandbox without a regulatory component to it could be outsourced and/or be established outside the Czech Authorities, although even in this case the Authorities would need to participate *inter alia* by means of providing data. The two types of sandboxes, regulatory and data, are not mutually exclusive.

Types of data in the data sandbox: The recommendation about the Czech data sandbox will depend on the feasibility analysis of such endeavour, which, in turn, will depend to a large extent on the datasets that can be made available, taking under consideration legal and technical limitations with respect to companies participating in such facilitator, while it will also depend on the allocation of capacity to operate such a sandbox, both in terms of numbers and in terms of technical skillsets, to allow for its operation.

Synthetic data in the data sandbox: It is recommended to avoid this option at the first stages of development of the data sandbox, unless there is a willingness to deploy important resources, both internally / pre-existing and externally in terms of providers of specialised services that may not be available within the Czech authorities. In the future, depending on the availability of resources and the experience of the sandbox, Czech authorities can consider engaging in a more resource-intensive phase of the data sandbox, involving synthetic datasets.

Participants: Categories of firms that may participate and would find it useful include companies that already have a license but wish to test a new technology and/or business model; companies that do not have the required license within the financial legislation to provide the desired activity; companies where it is uncertain whether the activity requires a license within the financial legislation.

Eligibility criteria: It is recommended that participants in the regulatory sandbox hold the appropriate license for the regulated activity undertaken or are ready to apply for a license in order to have it before the start of the testing phase, if the supervisor deems that the activity falls within the perimeter of regulated financial activity. In case the supervisor deems that a license is not necessary, the Czech Authorities have the discretion to allow the company to perform the testing or not. This could be beneficial for both the Czech Authorities and the service provider, for example, if regulation in this area is being negotiated and co-operation is assessed as beneficial for familiarisation with this type of product.

Authorisation model: Participants are preselected by a special Advisory Board based on enclosed eligibility criteria, which provides a non-binding recommendation. This will then be validated or rejected by the Czech Authorities, and this does not apply to the CNB, as the CNB has no legal basis to issue such a decision. The Authority operating the sandbox would issue a decision regarding the selection upon considering the recommendation of the Advisory Board.



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