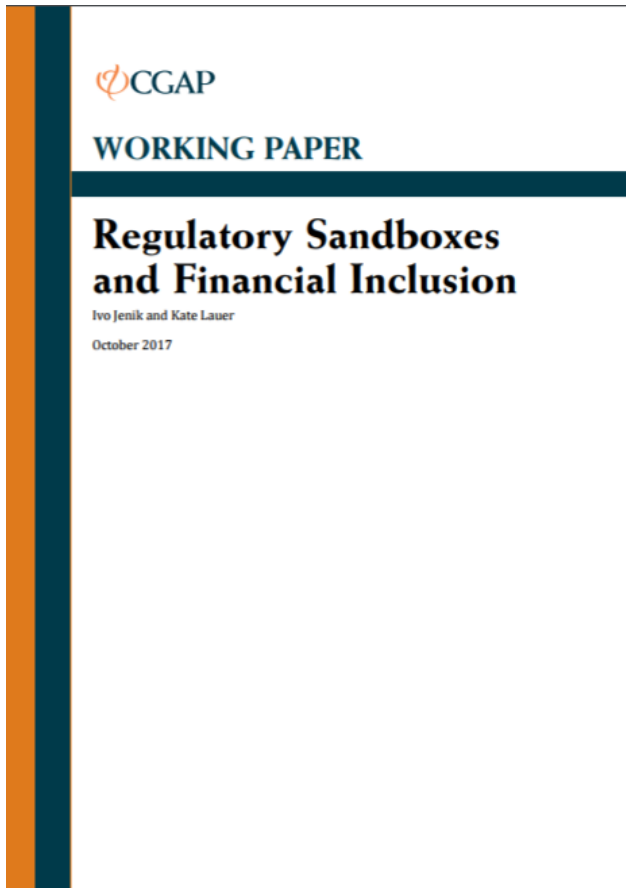


An aerial photograph of three farmers working in a field. They are wearing traditional conical hats and are positioned in a row, working on a field with distinct horizontal rows of soil. The farmer on the left is holding a long-handled tool. The farmer in the middle is wearing a pink shirt. The farmer on the right is wearing a checkered shirt. The field is dark brown, and the sky is not visible.

Regulatory Sandboxes & Financial Inclusion



CGAP Working Paper



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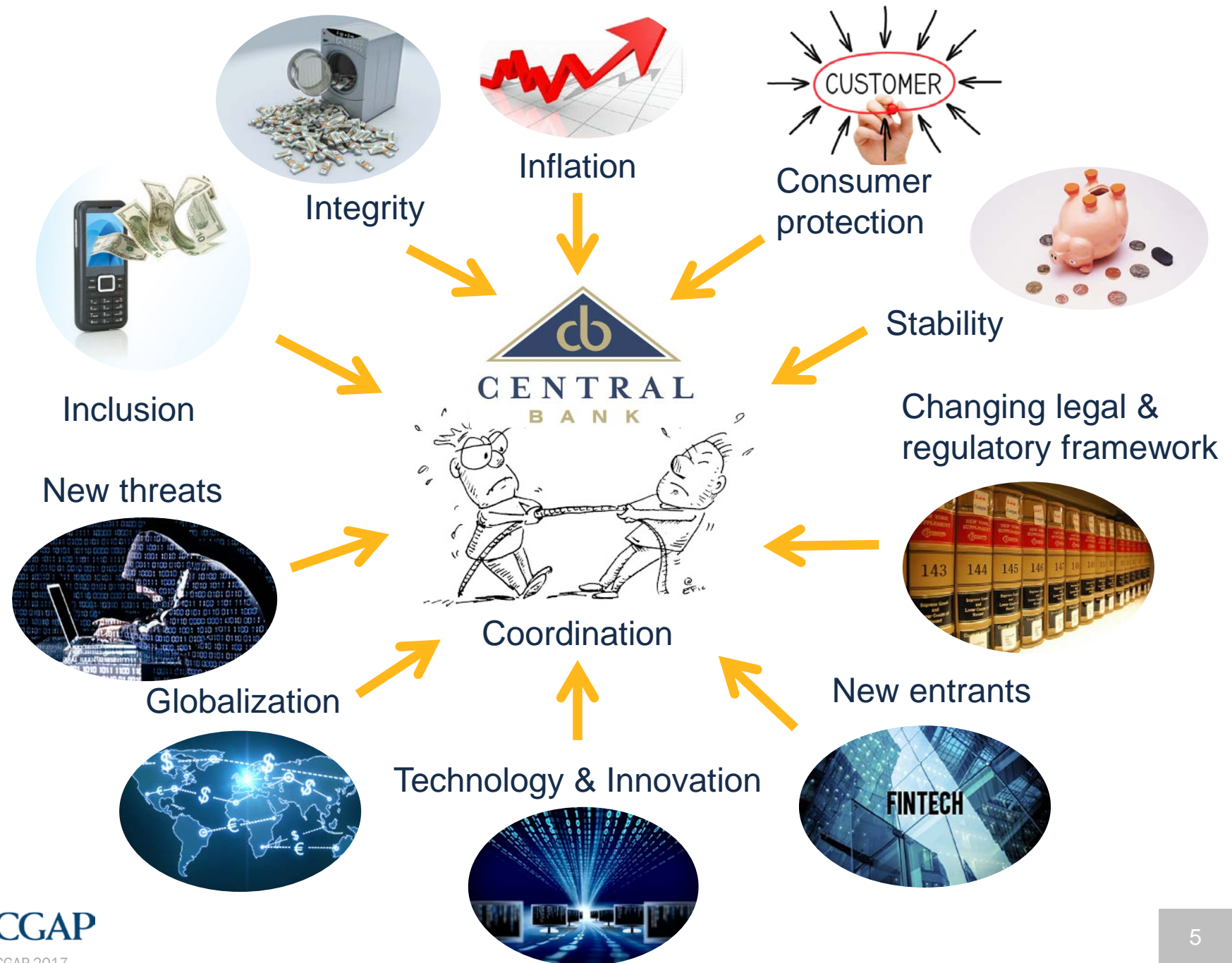
To download the paper, click [here](#).

Summary

1. One out of several other options
2. Not an exclusive point of entry for innovation
3. Too early to evaluate real impact

For more information click [here](#).

The Importance of Regulatory Adaptation is Increasing



Regulators Need to Adapt

Ability to adapt is proportionate to regulator's flexibility, which is constrained by:

- Degrees of discretion allowed by laws
- Resources (staff, time, money)
- Liability (incentivizing risk aversion)
- Political support (incentivizing risk aversion)

Regulation Needs to Adapt

The rules of game for the financial sector were framed when the game was played by handful of players on a desk board. Now the game is played online and in a multiplayer mode.



Problem Statement

Regulators need to find ways to safely leverage the opportunities offered by innovation to expand and deepen the reach of financial services.



What Can A Regulatory Sandbox Do?

A Regulatory Sandbox...

- Is a space for testing of new ideas in a live environment with regulatory permission
- Brings down the cost of innovation and generates insights into regulatory work
- Is one among other regulatory tools...

One Tool Among Others

	Wait-and-See (liberal)	Test-and-Learn (bespoke)	FinTech License (legislative)	Regulatory Sandbox
Structured (a defined process to deal with innovations)			✓	✓
Permanent (a permanent framework)			✓	✓
Objective-driven (implementation driven by defined objectives)			✓	✓
Open access (objective and transparent criteria determine access)			✓	✓
Parametrized test (restrictions and safeguards in place)		✓		✓
Mutual learning (intense dialogue between the regulator and innovators)		✓		✓

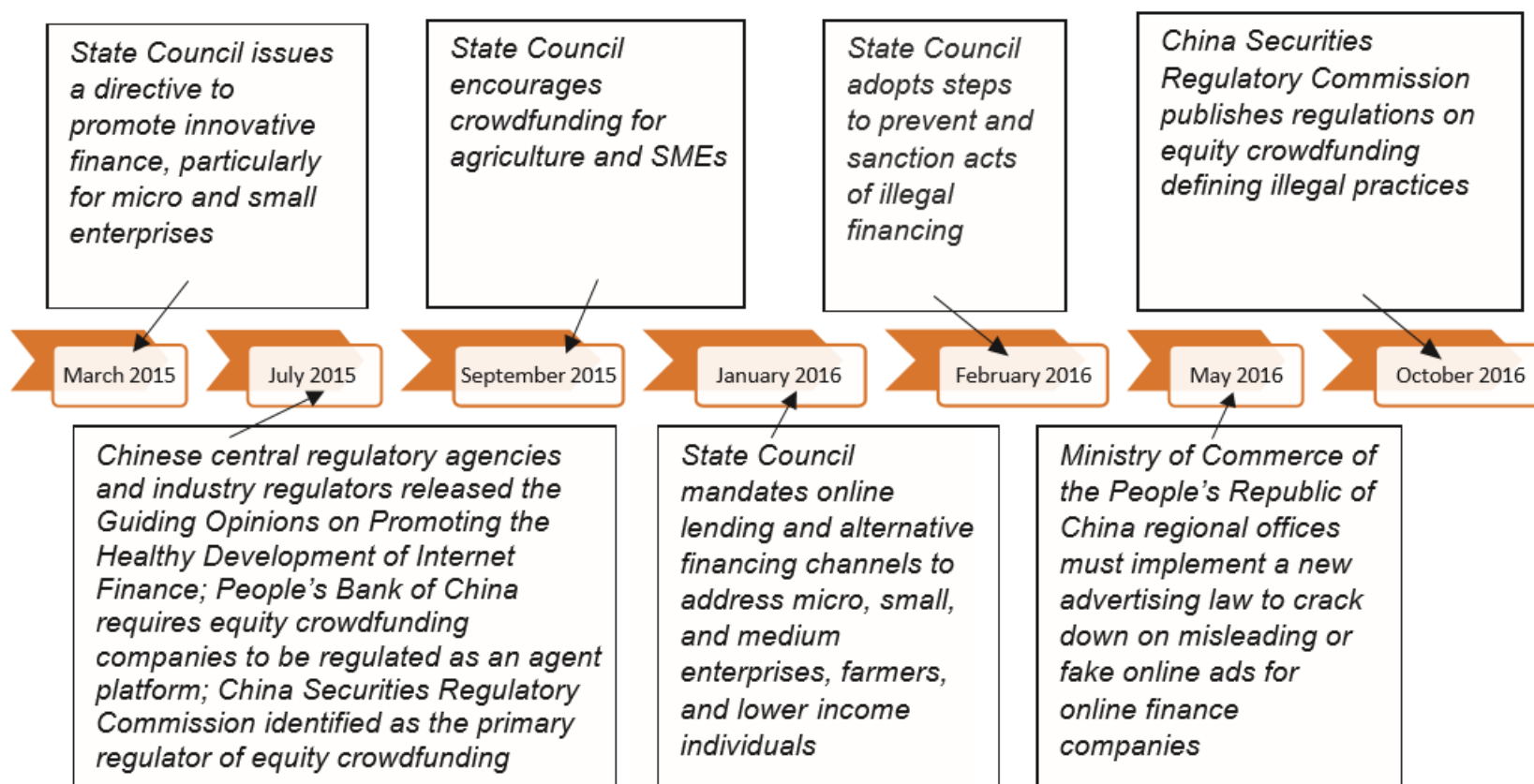
Note: The listed examples of tools are only illustrative and cannot be considered exhaustive.

Wait-and-See

Monitoring of a trend to understand it better before any intervention

P2P Lending in China

Examples of policy interventions



Test-and-Learn

A bespoke framework to test a new idea in a live environment

Bangko Sentral ng Philipinas

2004

Permitting non-banks to pilot e-money with safeguards and reporting requirements in place



2009

E-money regulations adopted



Today

T&L approached used to test various innovations from payments agents to e-KYC

FinTech License (not implemented yet)

FinTech License in Switzerland

Main Features

- Deposit-taking up to CHF100 million
- Mandatory compliance with certain rules
- Safeguards in place (scale, leverage)
- Regulatory reporting

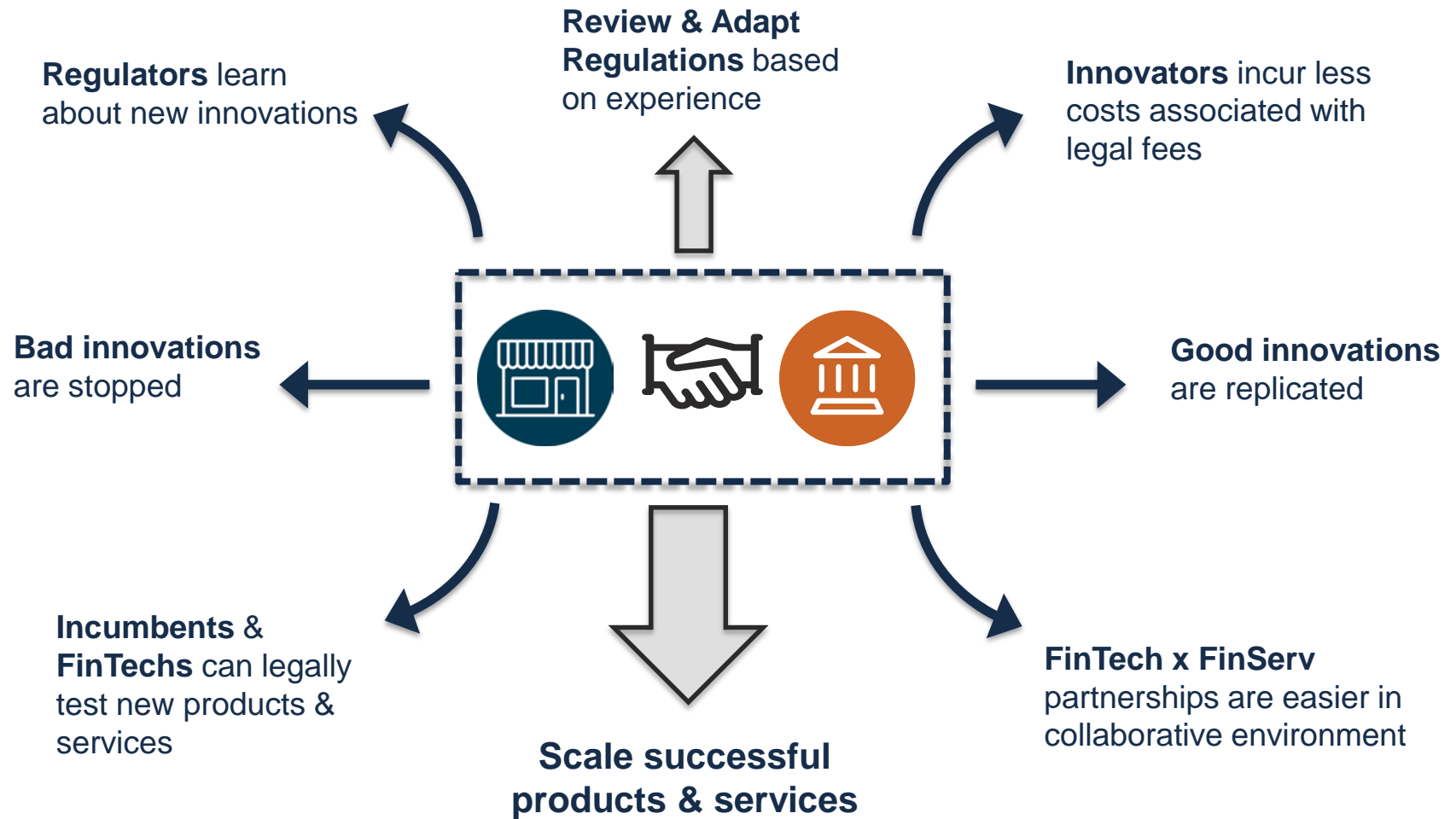
What is a Regulatory Sandbox?

Guidance issued by a financial sector regulator to allow small scale, live testing of innovations by innovators in a contained environment under the regulator's supervision.

Note: In reality, a range of practices exists, some of which may not fit neatly under the definition.

For more information click [here](#)

Ideal Scenario: Win-Win



Benefits vs. Risks

Summary of benefits

- Lowering cost of innovation
- Opening access to regulator
- Improving communication between the regulator and innovators
- Formalizing framework for safe, live testing
- Market monitoring
- Signaling

For more information click [here](#).

Benefits vs. Risks

Summary of risks

- Competition issues (winners picking, uneven playing field)
- Limited capacity of regulator to run sandbox
- Liability issues in case of failed testing
- Fragmentation of regulatory regimes nationally and internationally
- Coordination issues

For more information click [here](#).

Diversity of regulatory sandboxes revolves around several design components



Objectives

(promote innovation, competition, consumer convenience, inclusion)



Eligibility

(incumbents, fintechs, innovators)



Safeguards &

other restrictions

(AML/CFT, disclosure, complaints handling, limited scale)



Timing for

applications & tests

(cohorts, rolling, 3 – 24 months)



Costs

(application fees, licensing fees, testing costs)



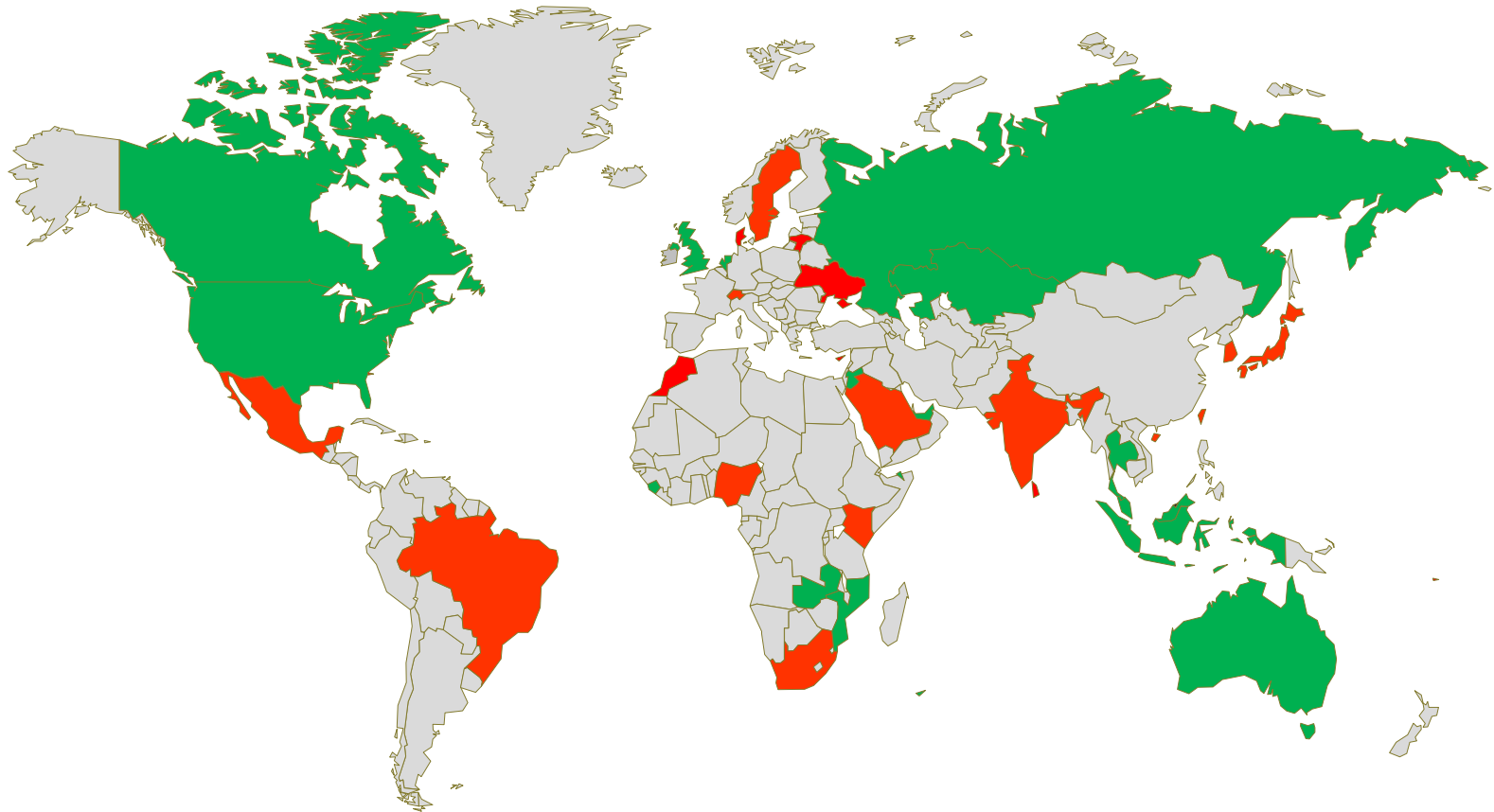
Post-test options

(license, cease-and-desist, regulatory change)

As of August 31, 2018



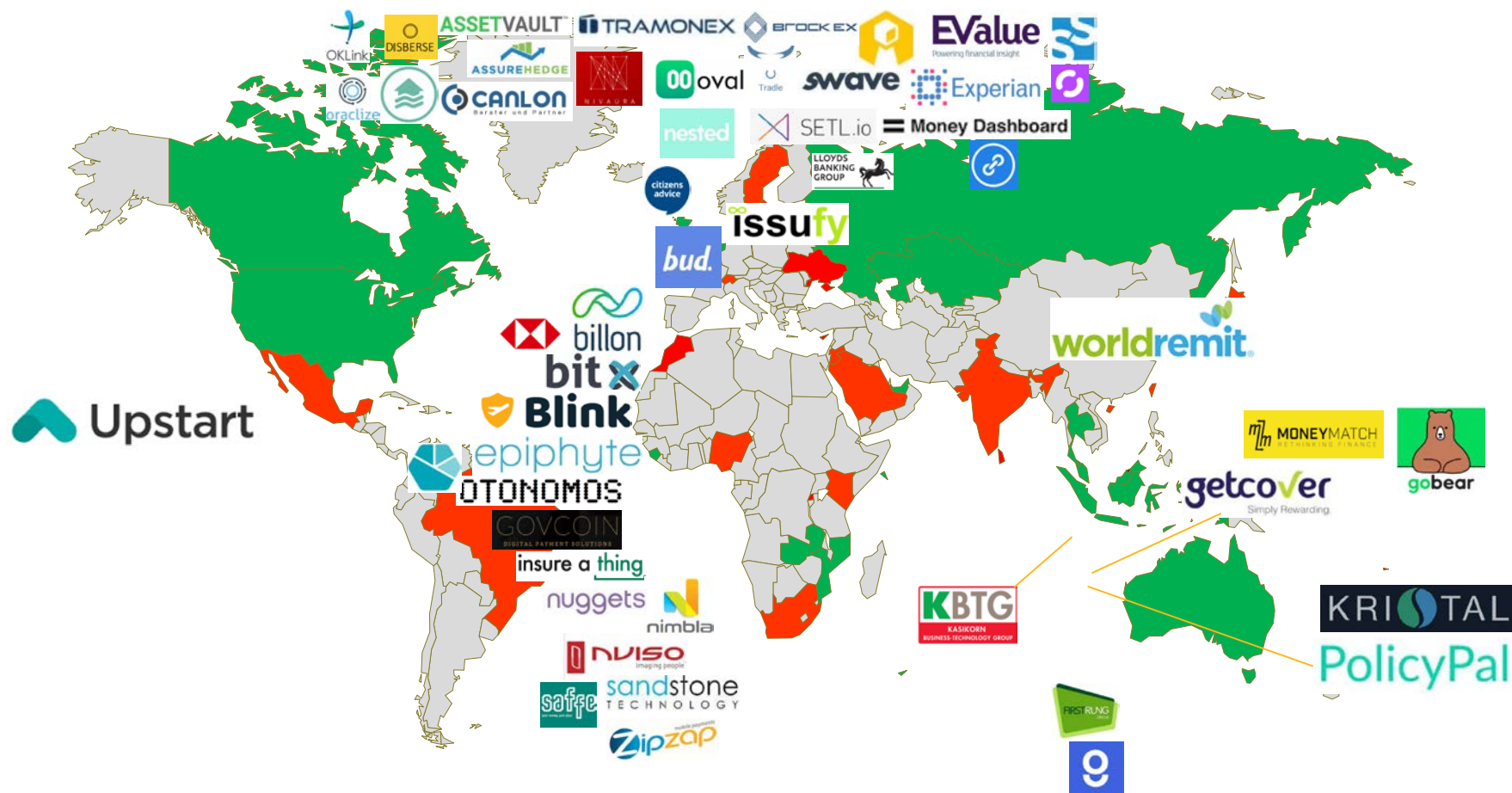
As of August 31, 2018



-  Countries with regulatory sandbox
 Countries considering regulatory sandbox

Regulatory Sandboxes Around the World

As of July 7, 2018



■ Countries with regulatory sandbox

■ Countries considering regulatory sandbox

FinTech Ecosystem in Africa

Snapshot from CGAP FinTech Challenge



Source: [Vidal, M. 2017.](#)

Tools for Regulatory Adaptation

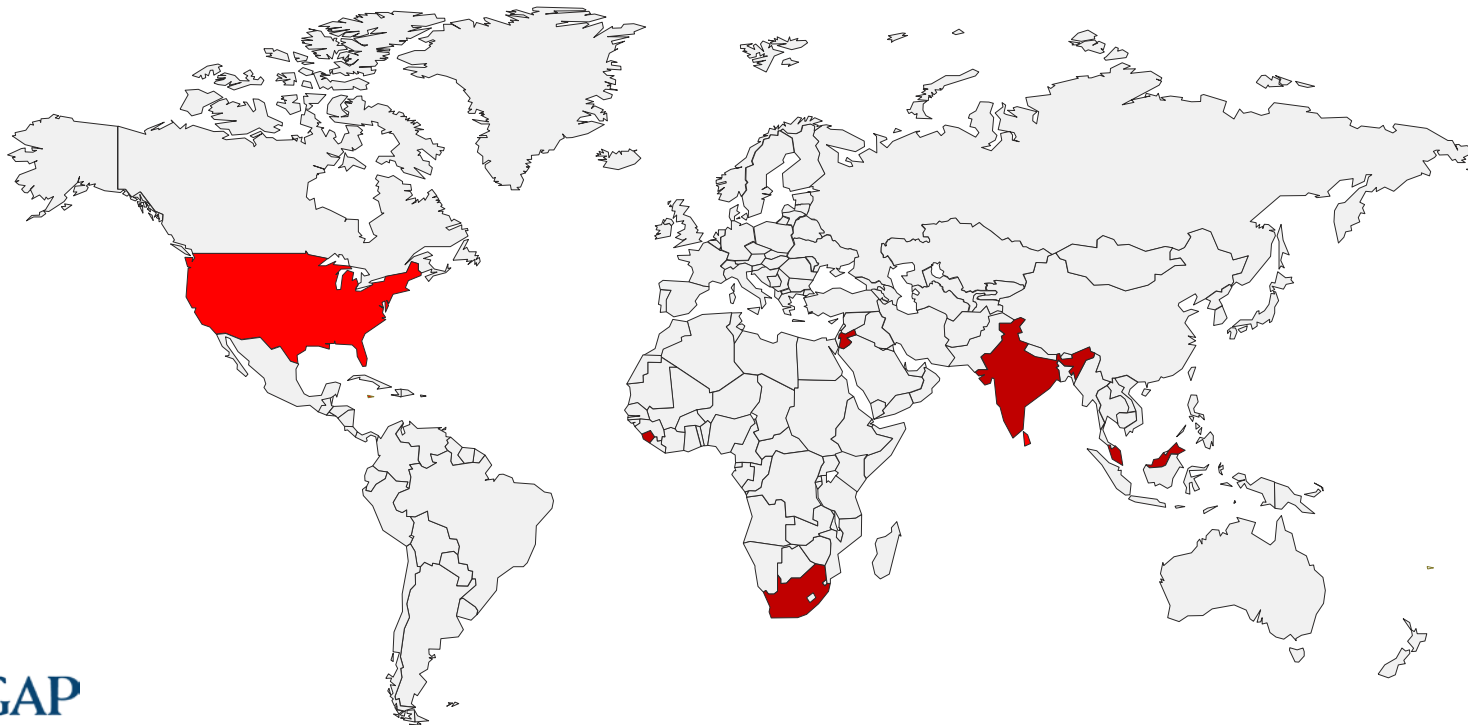
	Liberal (wait-and-see)	Bespoke (test-and-learn)	Legislative (statutory exemption)	Regulatory sandbox
Formality	★	★ ★ ★	★ ★ ★ ★ ★	★ ★ ★ ★ ★
Structure	★	★ ★ ★	★ ★ ★ ★ ★	★ ★ ★ ★ ★
Transparency	★	★ ★ ★ ★	★ ★ ★ ★ ★	★ ★ ★ ★
Flexibility	★ ★ ★ ★ ★	★ ★ ★ ★	★	★ ★ ★
Resources	★	★ ★ ★	★ ★ ★ ★ ★	★ ★ ★ ★
Intervention	★	★ ★	★ ★ ★ ★ ★	★ ★ ★ ★

Note: The listed examples of tools are only illustrative and cannot be considered exhaustive.

What does this all have to do with financial inclusion?

Promoting Financial Inclusion

- Not hard data to make a strong case yet
- No blueprint to copy
- High implementation costs to justify wide-spread application



Pro-Financial Inclusion Benefits

Several hypothesis

- Improving capacity of regulators to balance innovations with I-SIP objectives
- Promoting innovation that improves financial inclusion (as demonstrated by past examples – though not tested in a sandbox)
 - New, affordable products or services (BitPesa)
 - Distribution channels (AliPay)
 - Operational efficiencies (Yu'e Bao)
 - Business models (PayGo)
 - Compliance and risk management (iProov)
 - Increased competition

Leveraging Regulatory Sandboxes for Financial Inclusion

- Segment targeting
 - At the testing stage
 - At the rollout stage
 - KPIs for serving excluded customers
- A preferential regime for pro-inclusion providers

For more information click [here](#).

Implementation Risks

Several hypothesis

- Stretching regulatory capacity
- Regulatory procrastination
- Inadequate institutional arrangements
- New risks associated with products and services
- Disproportionate distribution of benefits to already included segments

For more information click [here](#).

Summary

1. One out of several other options
2. Not an exclusive point of entry for innovation
3. Too early to evaluate real impact

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Outstanding Questions

1. Can regulatory sandboxes harness innovation for financial inclusion?
2. Under what circumstances?

Sources

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