



REGULATORS KEEPING IN STEP WITH FINTECH GROWTH

IFWG

INTERGOVERNMENTAL FINTECH WORKING GROUP

The rapid development of technology in the financial sector requires South African regulators to be nimble when formulating a regulatory framework that advances responsible innovation.

To that end, the financial sector regulators launched the Intergovernmental Fintech Working Group (IFWG) in 2016¹ to continuously assess financial technology (fintech) developments and provide a space for innovators to test new products and services.

As one of the founding members of the IFWG, the FIC provides fintech firms and other financial sector innovators guidance in terms of the country's anti-money laundering and financing of terrorism (AML/CFT) legislation.

“It is important for regulatory authorities to jointly understand fintech and develop regulatory frameworks in a coordinated and harmonised approach,” said Pieter Smit, Legal and Policy executive manager at the FIC.

“Therefore, it is important for financial sector regulators, such as the FIC, to be part of the IFWG to ensure the continued efficient functioning of financial markets, and the integrity of the financial system.”

THE FIC ACT AND FINTECH

The FIC's role, in general, and within the IFWG, is to ensure that businesses whose products or services are at high-risk for money laundering and terrorist financing comply with the Financial Intelligence Centre Act (FIC Act) obligations.

CONTINUES....

¹In 2016, the IFWG comprised members from National Treasury, the South African Reserve Bank, the Financial Service Conduct Authority and the Financial Intelligence Centre. The National Credit Regulator and the South African Revenue Service joined the IFWG in 2019, while the Competition Commission came onboard in 2020.

In addition, the FIC establishes whether regulators' responses to fintech developments adhere and align to the international anti-money laundering and combating the financing of terrorism standards of the Financial Action Task Force (FATF).

"Many of the risks that may be associated with fintech enabled products and services relate to money laundering and terrorist financing," Smit said.

"This makes it necessary for the FIC, in particular, to play a prominent role in structures such as the Innovation Hub."

Smit added that South Africa adopted an activity-based approach to fintech regulation by focusing on the type of products or services that emerging innovators provide.

"If the new fintech-enabled product or service equates to an existing activity that is already covered by the legislation of the various regulators, then such businesses need to comply with that legislation," Smit said.

"However, if it is something that is not covered by current legislation, the regulators would have to decide whether, and if so what type of regulation is required and then look at putting that in place."

INNOVATION HUB

The IFWG launched the Innovation Hub in April 2020 which serves as the working group's virtual headquarters where fintech innovators can practice development and exchange ideas with regulators.

The hub consists of three primary innovation facilitators – a Regulatory Guidance Unit, a Regulatory Sandbox and an Innovation Accelerator – that aim to clarify the regulatory landscape, provide a space for safe experimentation and actively advance innovation.

The FIC has so far largely contributed in the Regulatory Guidance Unit where fintech companies have sent through queries about regulation. Queries straddle aspects related to different regulatory areas where guidance is, for example, required from the South African Reserve Bank, the Financial Sector Conduct Authority and the FIC. In some cases, a single regulator may provide input if only one piece of a regulatory framework applies, or it could involve multiple agencies and subject matter experts.

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REGULATORY SANDBOX

The FIC also contributed substantially to the Regulatory Sandbox process meeting with participants, albeit without providing regulatory relief from AML/CFT compliance as required in terms of the FIC Act.

If the activity of the Sandbox participant falls under one of the Items listed in Schedule 1 to the FIC Act as an accountable institution, the participant is under an obligation to comply with the Act.

If the activity of the Sandbox participant does not fall under one of the Schedule 1 Items, and the participant is not under an obligation to comply with the FIC Act, there may be specific cases where the type of activity should be regulated in terms of the Act and where a condition to the entity's participation in the Sandbox would be to apply the FIC Act provisions as if they are obliged to do so.

The IFWG screened and accepted the first cohort of six fintech innovators – with more expected to be added – for the Regulatory Sandbox (testing environment). The IFWG received a total of 55 applications from a range of financial services activities including payments, savings and deposits, lending, and investments.

The IFWG has adopted a staggered approach to allow the innovators who are ready to start testing to proceed before the full cohort is finalised. Some of the innovators are at an advanced stage of the testing in the Regulatory Sandbox.

Four out of the six fintech innovators in the first cohort's technology relates to crypto assets or blockchain technology. The IFWG is currently conducting a retrospective assessment of the Regulatory Sandbox, which will determine whether the cohort approach is suited for the South African environment.

CRYPTO ASSETS

In the area of crypto assets, the FIC was integral to the IFWG developing a policy position paper on this subject, which was published for comment on 14 April 2020. The purpose of the position paper was to provide specific recommendations for the development of a regulatory framework for crypto assets, including suggestions on the required regulatory changes to be implemented. **(See story on the regulation of crypto assets...in this newsletter).**

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“The majority of fintech developments are positioned to change the way in which financial services are delivered to customers by using digital platforms to interact with their customers,” Smit said.

“In almost all of these instances the products or services promote non-face-to-face business and create greater opportunities for financial transactions to be carried out anonymously. If we look at, for example, crypto asset service providers that are already operating in South Africa and globally, we have seen instances of their services being exploited for ML/TF purposes. If this sector is not regulated for AML/CFT, we have a blind spot and we will not be able to protect our financial system from ML/TF from exploitation by ill-meaning customers of these types of businesses.”

RECEIVING GLOBAL RECOGNITION

The SARB, and by extension the IFWG, received global recognition when it received the Fintech Policy of the Year award from Central Banking’s 2020 FinTech and RegTech Global Awards.

Through its collaboration with other regulators and policymakers in the IFWG, SARB was recognised as one of the central banks that are leading the way in creating a fintech ecosystem. The fintech policy award, therefore, acknowledges the shared approach to fintech policy making, showing that institutions can work together for greater efficiency.