

BLOCKCHAIN IRELAND

# Cp156 Central Bank Approach to Innovation Engagement in Financial Services

5th February 2024



## **STAKEHOLDERS**

### **Blockchain Ireland Members**

The Blockchain Ireland ecosystem fosters an open innovation approach within a distributed innovation ecosystem to nurture homegrown talent, foster partnerships and support new businesses, by spotlighting disruptive decentralised business models and successful commercial ventures with global ambitions.

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## **STAKEHOLDERS**

### **Central Bank of Ireland (CBI)**

The Central Bank of Ireland, their clients including financial service providers and the customers they serve.

## **OVERVIEW**

This document includes considered responses from members of Blockchain Ireland and the blockchain, DLT, Defi, crypto and Web3 innovation ecosystem in Ireland.

**Q1 What is your feedback on the enhancements underway with the Innovation Hub? Are there other areas that should be developed?**

**INNOVATION**

Blockchain Ireland members welcome the CBI Innovation programme initiative. The proposal to offer an open and adaptive interface to industry clients is hugely beneficial to all, in particular with the commitment to grow and develop services as requirements become better understood. We make this submission in a spirit of collaboration, exercising our right to contribute via consultation and share our concerns from our industry point of view.

Members of Blockchain Ireland find the CBI takes a constrained view of financial innovation. Our view concurs with that reflected in the 10 October 2023 Financial Industry Forum - Innovation Subgroup - Summary Report which highlights a call from industry for an ‘innovation radar’ tool to identify drivers of innovation in financial services and a framework for understanding innovation. This notable gap is not addressed in the Innovation Hub proposals and remains a significant gap in our view.

Blockchain Ireland members understand that innovation happens outside of laboratories, universities and guidance sandboxes; innovation is attempted, succeeds or fails in the global digital marketplace. The proposed Innovation Hub enhancements laid out in CP156 focus on internal fact-finding, informing and upskilling their own and 3rd party experts.

**Q2 What is your feedback on the proposal to establish an Innovation Sandbox Programme? Will the proposal support the Central Bank in meeting our overall objectives, including the needs of consumers and the wider economy?**

While there are multiple references to the current and evolving regulatory context it is not clear what the CBI considers important context for the future of financial services. By way of example, in a recent SEEBLOCKS.eu public

consultation on important emerging blockchain standards the following policy, regulatory and legal references were identified as key:

*Q: Which aspects of EC policy, regulation and law will have the greatest relevance to the implementation of blockchain and DLT technologies in your opinion?*

**The top four most relevant policies, regulation or laws identified are:**

1. Markets in Crypto Assets Regulation (2019)
2. Framework for EU Digital Identity (2021)
3. EU Data Act (2022)
4. ECB Digital Euro (proposed) (2023)

The full selection list is included here for reference.

- EU Data Act (2022)
- EU Digital Finance Package (2020)
- Regulation for digital operation resilience for the financial sector (2020)
- EU Markets in Crypto Assets Regulation (2019)
- ECB Digital Euro (proposed) (2023)
- EU AI Act (proposed) (2023)
- Framework for EU Digital Identity (2021)
- Other

Members of Blockchain Ireland do not see evidence of the most important regulation and policy changes and advances that impact our industry in the proposed enhancements. The framework itself is absent from the discussion document as are indications that frameworks will be tailored to size of enterprise and market.

Indication of concrete connectedness to other European industry research and infrastructures is a gap that needs much greater detail and clarity in the proposed provision of a guidance sandbox.

Will the CB innovation Sandbox Programme have links and share learnings with the [EU Blockchain Regulatory Sandbox](#)?

**Q3 What is your feedback on the operating model of the Innovation Sandbox Programme?**

After carefully reviewing the proposal of the innovation model of the Sandbox Programme, Blockchain Ireland members have identified the following points critical to the success of the program.

1. **Regulatory and Digital Sandbox:** We consider that the current model of non regulatory or non digital sandbox should be only a stepping stone in order to move forward towards a model that will allow participants to fully test real markets and legislation. At the moment, there is no visibility of a road map that will allow this to happen. It is important to mention that, the most successful sandbox programs in the world (Singapore, Dubai, London) have always provided a safety net for companies and entrepreneurs to operate under defined parameters (number of customers, limit is transition value, etc). Dispensations at the regulatory level are critical to boost innovation and create a collaborative environment between regulators and companies regulated.
2. **Timing:** We consider that an annual call for companies to participate in this initiative is not enough. The blockchain, crypto and web3 industry sectors move at a faster pace than most, these early movers are in greatest need of robust development and testing sandboxing from the regulatory perspective e.g. [VASP-registered](#) Defi services, offering peer-to-peer immutable finance, with transparent autonomous transaction execution. The proposed, one year waiting period for a new case study is too constrained. There is a high chance applicants, in particular startups who are highly mobile, will move to a jurisdiction or ecosystem better equipped to cater to their needs. To prevent talent flight or unnecessarily complex new service development, the CBI must support

the ecosystem, meeting the pace and needs of industry and not hamper the product development lifecycle. This can be addressed by running the innovation program on a continuous basis.

3. **Themes:** Following our view on the timing of the program, we have a similar view on the calling for themes. Defining a single topic on an annual basis does not provide enough coverage to the whole financial ecosystem. We consider that a better approach is to understand the real impact some of the solutions will have on the financial ecosystem and the economic benefits they can bring to Ireland. (Please see response to Q4 for a list of what some of these topics might be).

**Q4 Are there specific themes or areas of innovation that the Central Bank Innovation Sandbox Programme should address?**

As per the [EFIF Taxonomy of Financial Innovation](#) - Matrix + Glossary

Blockchain Ireland members call for a focus on cross-sectoral services enabled by DLT (including blockchain) and smart contracts, this includes many areas of financial innovation including crypto asset issuance and exchange. We identify the following topics as defined in the report and referenced as key to financial service innovation and request that the CBI Innovation Sandbox include content, workshops and information sessions that will raise awareness and understanding of the changing socio-digital context for finance.

1. **Crypto asset:** a digital representation of a value or of a right that is able to be transferred and stored electronically using distributed ledger technology or similar technology. Source: [Regulation \(EU\) 2023/1114 \(MiCAR\) Article 3\(5\)](#)
2. **Electronic Wallet:** in the forthcoming EU framework for a pan-European digital

identity, a new EU wallet is foreseen to allow citizens to identify and authenticate themselves online without having to resort to commercial providers - a practice that raises trust, security and privacy concerns. However, electronic wallets can also be used to store payment information, private keys and passwords in a safe and accessible way. Source: Elaborated from [European Digital Identity \(europa.eu\)](#)

3. **Next generation Financial Market Infrastructures (FMIs):** Financial market infrastructures include the payment systems used every day, as well as more specialised systems that move money, shares, bonds and other financial assets between banks and financial institutions. Some of these systems are provided by central banks as public goods, while others are provided by nonprofit groups supervised by central banks to ensure their safety and resilience. Source: [BIS Innovation Hub work on next-generation FMIs](#)
4. **Open finance:** In the context of banking, open data has translated into “open banking” regulation, empowering customers to authorise banking institutions to share their personal data with third parties for the purpose of obtaining greater access to finance in a more open and competitive market. Witnessing the evolution of technology-driven business models that make finance more accessible, inclusive and competitive through connecting and analysing data, the concept of open banking is evolving into “open finance”. To reach optimal adoption, open finance in turn calls for the continued evolution of new infrastructures, such as individual and corporate digital identity. Source: [BIS Innovation Hub work on open finance](#)
5. **Payment-related technical services:** services provided by technical service providers, which support the provision of payment services, without them entering at any time into possession of the funds to be transferred, including processing and storage of data, trust and privacy protection services, data and entity authentication, information technology (IT) and communication network provision, provision and maintenance of terminals and devices used for payment services, with the exclusion of payment initiation services and account information services. Source: [Directive \(EU\) 2015/2366 \(PSD2\), Article 3\(j\)](#)
6. **RegTech:** any range of applications of technology-enabled innovation for regulatory, compliance and reporting requirements implemented by a regulated institution. Source: [EBA analysis of RegTech in the EU financial sector \(europa.eu\)](#)
7. **Robo-advice:** refers to the provision of investment advice or portfolio management services (in whole or in part) through an automated or semi-automated system used as a client-facing tool. Source: [Directive 2014/65/EU \(MiFID II\) - Guidelines on suitability \(ESMA35-43-3172\)](#)
8. **Standardisation:** a standard is a voluntary technical or quality specification, adopted by a recognised standardisation body, for repeated or continuous application, with which compliance is not compulsory. Standardisation can cover a product, a process, a service or a system. Source: [Elaborated from Regulation \(EU\) No 1025/2012 Article 2](#)
9. **Blockchain:** is a public ledger consisting of all transactions taken place across a peer-to-peer network. It is a data structure consisting of linked blocks of data, e.g. confirmed financial transactions with each block pointing/referring to the previous one forming a chain in linear and chronological order. This decentralised technology enables the participants of a peer-to-peer network to make transactions without the need of a trusted central authority and at the same time relying on cryptography to ensure the integrity of transactions. Source: [ENISA Glossary](#)

10. **Distributed Ledger Technology (DLT):** a type of technology that supports the distributed recording of encrypted data. A distributed ledger is an information repository that keeps records of transactions and that is shared across, and synchronised between, a set of DLT network nodes using a consensus mechanism. Source: [Regulation \(EU\) 2023/1114 \(MiCAR\) Article 3\(1\)](#)

11. **Encryption:** the encoding of messages in such a way that only intended recipients can understand them. Encryption therefore ensures high levels of data protection. Source: [EDPS Encryption | European Data Protection Supervisor \(europa.eu\)](#)

12. **Extended reality:** refers to technologies that combine advanced computing systems (hardware and software) that can change how people connect with each other and their surroundings and influence or manipulate human actions through interactions with virtual environments. Source: [Enhancing EU legal frameworks for Digital Extended Reality - TechEthos](#)

13. **Privacy Enhancing Technologies (PET):** refers to a collection of digital technologies, approaches and tools that permit data processing and analysis while protecting the confidentiality, and in some cases also the integrity and availability, of the data and thus the privacy of the data subjects and commercial interests of data controllers. Source: [OECD Emerging PET: Current regulatory and policy approaches](#)

14. **Smart contracts:** An automated mechanism involving two or more parties where digital assets are put in and redistributed, at a later date, based on some pre-set formula and triggering event. The contract can run as programmed without any downtime, censorship, fraud or third-party interference. computerised transaction protocol that executes the terms of a

contract. Source: [ICMA FinTech jargon](#) and [EBA Glossary for Financial Innovation \(europa.eu\)](#)

15. **Tokenisation:** refers to the creation of digital tokens representing real assets issued on the blockchain. Source: [OECD The Tokenisation of Assets and Potential Implications for Financial Markets](#)

16. **Web3:** a new paradigm where users control their data and choose who to share it with, and when. By putting data back in the users' hands, Web3 avoids the hoarding of data by just a few platforms. A fundamental change brought about by Web3, when compared to the Web 2.0 model based on BigTech platforms, is the use of technology to achieve automated verification of data which in turn enables the decentralisation of services and the removal of intermediaries. Although Decentralised Finance (DeFi) and other token-based initiatives have been among the first sectors to embrace Web3, the implementation of these principles is becoming a much larger and wider movement that has the potential to transform eCommerce, eGovernment, eHealth, etc. Source: [What is Web3? - EU Verify - \(europa.eu\)](#)

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