

Activity Report of the Innovation Hub and Regulatory Sandbox of Národná banka Slovenska

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Introduction

This is the fifth edition of Národná banka Slovenska's annual report on the activities of its Innovation Hub (the 'Hub'), which since last year's edition has also covered the activities of the Bank's Regulatory Sandbox (the 'Sandbox').

Both tools offer innovators the opportunity to consult the Bank's experts about the application of regulation to financial innovations, thus helping to alleviate legal uncertainty and facilitate the implementation of financial innovation in the Slovak market.

The Hub is generally used for one-time enquiries, and since its establishment in 2019, it has handled 116 enquiries. The Sandbox provides an environment in which firms can, in consultation with the Bank, configure their innovative financial products and services over a longer period. Established in 2022, the Sandbox currently has one participant, who is in the Sandbox's preparatory phase.

Both tools contribute to improving the visibility of innovation topics, to information sharing and to fostering dialogue between the Bank and the private sector. At the same time, they reinforce the Bank's image as an innovator on the domestic and international market.

Across the 30 EU/EEA countries there are a total of 41 innovation hubs and 14 regulatory sandboxes operated by the national supervisory authorities. The national supervisors face very similar experiences and challenges: innovators sometimes come with unrealistic business models that are at a very early stage; some do not do enough prior research using the

information available and ask questions easily answerable on the basis of existing regulation. On the other hand, current legislation is not always relevant for innovative business models.

In response to current trends, various new forms and types of innovation support tools are emerging, including, for example, hackathons, techsprints, virtual sandboxes (e.g. the virtual sandbox of Poland's Financial Supervision Authority), 'green sandboxes' (such as the Green FinTech Challenge and the Digital Sandbox run by the UK's Financial Conduct Authority), and sandboxes designed exclusively for testing artificial intelligence systems.

Aside from the Hub and Sandbox, the Bank is also involved in other innovation-supporting activities. It monitors trends in innovation regulation in Europe and actively participates in discussions on this topic.

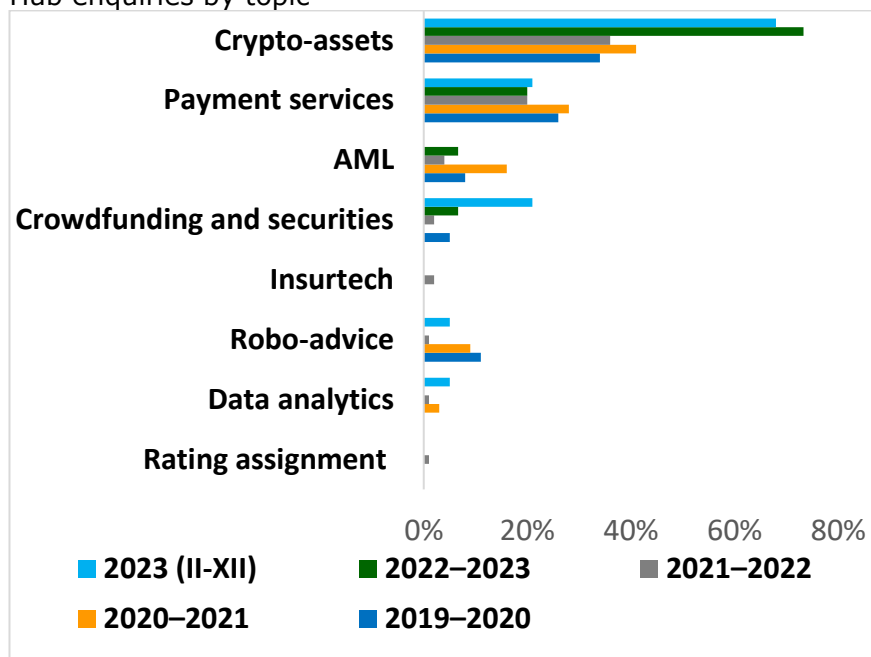
This report summarises the Hub and Sandbox developments, as well as other fintech related activities at the Bank, for the period from 1 February to 31 December 2023.

1 Crypto-assets continued to dominate Hub enquiries in 2023

1.1 Interest in crypto-related issues remains high

During the fifth year of its operation, the Hub handled a total of 19 enquiries, representing a slight increase compared with the previous year (16). The positive trend was driven by innovators' strong interest in crypto-asset issues. Some of these enquiries overlapped with issues such as anti-money laundering and combating the financing of terrorism (AML/CFT), biometrics, outsourcing, and payment services. Those who approached the Hub in 2023 included natural persons and legal entities, smaller and larger market players, law firms, and entities from abroad.

Chart 1:
Hub enquiries by topic



Many of the Hub enquiries concerned crypto-asset service providers' basic obligations under the current legislation and their obligations to register and obtain a trade licence pursuant to the Trading Act of the Slovak Republic.

The ongoing interest in crypto-assets is also linked to developments at the European level. June 2023 saw the entry into force of the EU's Markets in Crypto-assets (MiCA) Regulation, which creates a legal framework for business activity in this fintech sector.

Going forward, we foresee a further increase in crypto-asset issues as well as their spillover into other areas of the financial market (intermediation, payment services, capital market).

1.2 Payment services offer diverse opportunities

Another area addressed by a notable number of Hub enquiries was payment services, largely because it relates to a variety of business models. The Bank commented on one interesting model that allowed employees to be paid their wages under agreed conditions. Such a model is already widespread in some Western countries. Another business model discussed through the Hub allows the disbursement of funds in fiat currency or in crypto-assets. In this case, the innovator is already registered as a crypto-asset service provider in the Netherlands. There was also a model that focused on the area of yacht rental and the security deposit that customers are required to provide, which in this case took the form of locking up funds on a specially issued payment card. Another enquiry focused on the development of a shopping centre app and the development of a related mobile app.

1.3 Less demand for other fintech domains

Compared with previous year, the Hub saw less interest in data analytics, regtech, insurance and securities. One innovator that engaged with the Hub in 2023 was developing and integrating IT systems, analyses and interfaces for corporate clients such as insurance and logistics companies and had questions about how its business activities would be affected by current legislation in a number of areas. Another enquiry concerned algorithmic trading on various types of exchanges, with questions relating to robo-advice, regtech, and securities. One innovator asked about the possibilities of digital tokenisation of securities and the implications of the EU's second Markets in Financial Instruments Directive (MiFID II) for this type of financial product. There was also an enquiry about which legislative framework applied to Sandbox participants, especially in regard to a participant's potential infringement of the rules.

The Bank responds to Hub enquiries in Slovak or English, though in 2023 there were notably fewer submissions in English compared with previous years.

2 Guidance and European cooperation in the Sandbox

2.1 An uncertain start and a new promising case

The Sandbox's first participant had his preparatory phase extended by six months in January 2023. Despite several discussions, and the Bank's written responses to his questions and challenges, the participant was unable to meet the requirements of the Bank's experts even a full year after entering the Sandbox, nor after a final in-person meeting that took place in the summer of 2023.

The participant failed to grasp the basic elements of the legislation that applied to his business model. Moreover, the participant made public his Sandbox participation at a time when such disclosure was prohibited under the Sandbox rules – and after being warned multiple times not to do so. As for the testing plan that the participant drew up as a prerequisite for entering the testing phase, it repeatedly failed to meet the required formal and substantive requirements. In this context, the Regulatory Sandbox

Committee decided to terminate the participant's involvement in the Sandbox at the preparatory phase.

A new participant operating in the crowdfunding sector entered the Sandbox in November 2023 following initial informal discussions with the Bank in the summer.

Given the evolution of Hub enquiries focused on crypto-assets, which accounted for 68% of all enquiries last year, it may be expected that the next Sandbox participant will come from the crypt-asset sector.

2.2 Initial experiences and challenges

Capacity utilisation of the Bank's experts. The Bank's experts are limited in the amount of time they can devote to the Sandbox in addition to their primary tasks. This in effect may cap the number of Sandbox participants below the potential market demand for participation.

Participants' incorrect expectations. Some participants expect legal advice from the Bank's experts. The Bank, however, expects participants to have an overview of the relevant legislation and to be prepared for expert discussions. It recommends participants to consult a law firm if they need legal advice.

Compliance with Sandbox rules. If the Sandbox is to operate effectively, it is essential that participants comply with its rules regarding participant preparedness and communication about Sandbox participation.

As the Bank gains further experience in operating the Sandbox, it will modify the rules to make the Sandbox more efficient and to prevent erroneous expectations. Among the key lessons learned from the Sandbox's operation to date is the need for the Bank to stress to Sandbox applicants the importance of their professional and technical preparedness, i.e. that their compliance culture is at a high level, that all necessary contractual relationships are in place (especially B2B, where appropriate), and that the innovation to be tested has a mature technological basis.

2.3 Common search for solutions in the European Blockchain Sandbox

In order to take an active part in the development of innovative blockchain solutions at the European level, the Bank last year became a participant in the European Blockchain Sandbox (EBS). This new initiative of the European Commission enables collaboration between private sector innovators and European regulators. The purpose of the EBS is to support blockchain innovation. Within this project, the Bank is currently participating in the evaluation of two cases of blockchain solutions in the financial sector, both focused on the prevention of money laundering.

In the first of these cases, the regulatory dialogue with the firm in question concerns the process of cryptocurrency transaction monitoring with the aim of developing an anti-money laundering (AML) tool. In this case, the standardisation of risk assessment is being examined as are mechanisms for secure, regulated data sharing between financial institutions.

In the second case, the firm has come up with innovative approaches to digital assets and asset tokenisation. Its discussions with the Bank in 2023 concerned the regulatory regime for tokenised assets.

3 Implementation support and innovation popularisation

3.1 The Bank is supporting smooth implementation of the EU's MiCA¹ and DORA² regulations in Slovakia

On 3 October 2023 the Bank held the third annual edition of its **Slovak Financial Market and Innovation conference**, which provided a venue for the sharing of public and private sector perspectives on the regulation of cryptocurrencies and cybersecurity. Putting MiCA into practice implies a considerable cost burden on both the Bank and MiCA-affected businesses. **The Bank is actively engaged in dialogue with the market in preparation for these changes. In 2023 it offered a platform for discussions about the authorisation process and for the preparation of thematic workshops** to help participants better understand how the new rules apply in practice. In addition, the Bank is working with Slovakia's Ministry of Finance to ensure the smooth integration of both MiCA and DORA into the Slovak legal framework.

In 2023 the Bank was closely involved in key domestic fintech events. Among the most important were the **Finweek 2023 Bratislava** conference (24-26

¹ [Regulation \(EU\) 2023/1114](#) of the European Parliament and of the Council of 31 May 2023 on markets in crypto-assets, and amending Regulations (EU) No 1093/2010 and (EU) No 1095/2010 and Directives 2013/36/EU and (EU) 2019/1937.

² [Regulation \(EU\) 2022/2554](#) of the European Parliament and of the Council of 14 December 2022 on digital operational resilience for the financial sector and amending Regulations (EC) No 1060/2009, (EU) No 648/2012, (EU) No 600/2014, (EU) No 909/2014 and (EU) 2016/1011.

October) and regular meet-ups of the Fintech & Insurtech Association of Slovakia (FINAS). At Finweek, the Bank's representative discussed the impact of MiCA. He pointed out that the precise regulatory framework it establishes gives the EU an edge over countries with unclear rules and can also influence the global regulation of cryptocurrencies. MiCA opens up opportunities for traditional financial players to enter the crypto sector and increase confidence in the market. **In 2023 the Bank took a series of measures to support the smooth implementation of MiCA, including the creation of a dedicated section that prepares transparent communication of authorisation requirements and engages in dialogue with prospective crypto-asset service providers.**

On 8 November 2023 the Bank took part in the **Forbes Money Summit** conference in Bratislava, where it was represented in a panel discussion entitled '(Un)attractive crypto? How, why and whether to invest in cryptocurrencies'. In that discussion, the Bank's representative spoke about the MiCA Regulation and its expected impact on the crypto-asset market. The new regulatory regime for crypto-assets is expected to help clean up the market and better inform potential investors. **Even so, crypto-assets will remain a high-risk investment, and the Bank therefore recommends consumers to invest no more in crypto-assets than they can afford to lose.**

At the **Autumn ITAPA 2023** event on 20–23 November, the Bank was represented on a panel discussion entitled 'Crypto – the future of currency or a dead end?', which focused on the future of cryptocurrencies, including the impact of tax cuts, regulation and potential uses of cryptocurrencies beyond (just) investment. **MiCA offers an opportunity to increase consumer confidence, eliminate fraud and enhance market security.** At the same time, cryptocurrencies are far from simply an investment tool. They enable fast and cheap cross-border payments, automate processes thanks to smart contracts and create scope for entirely new business models. There was also an interesting debate on stablecoins and their potential role in the modernisation of international payments and on the prospective digital euro and its impact on the financial autonomy of the European Union.

In autumn 2023 the Bank conducted a survey on the use of innovation in supervised entities, following a previous such survey in November 2022. Each survey focused on banking, payment services, the capital market, insurance, and financial intermediation. Also in 2023, the Bank conducted a repeat representative consumer survey on crypto-assets and the digital euro, with the results due to be released in 2024.

3.2 The Bank is fully engaged in international discussions on digital finance

Since 2019 the Bank has been a member of the European Forum for Innovation Facilitators (EFIF), which provides a platform for supervisors in the EU to discuss and share experiences regarding regulation and different business models in the field of innovation. The EFIF held three meetings in 2023, and the Bank participated in all of them.

The Bank is also involved in the EU Supervisory Digital Finance Academy (EU-SDFA), a European Commission initiative intended to provide technical assistance to supervisory authorities. The EU-SDFA is designed for experts from national supervisory authorities and focuses on current regulatory topics. Last year saw the completion of the EU-SDFA's first foundational training cycle (2022–2023), which consisted of online learning and residential training weeks in Florence, Italy. Topics covered by the EU-SDFA included the MiCA and DORA regulatory frameworks and the sharing of experiences about innovation tools such as innovation hubs and regulatory sandboxes.

In April 2023 the Bank took part in the **Global Banking Innovation Forum** and FinTech Roadmap conference in Prague. This meeting for banking experts focused on various discussions around innovative business models, complemented by discussions on such topics as sustainability, artificial intelligence, cloud and data analytics, and virtual assets.

At the **Seamless Europe 2023** event held on 18-19 October in Berlin, the Bank's representative had the opportunity to speak on a panel about current developments in digital payments, the continuing role of cash, and a future influenced by fintech and crypto-assets. The discussion also addressed two initiatives that have the potential to redefine the payments sector: the digital euro that is envisaged to be introduced by 2027/2028 as a secure and fast electronic payment instrument; and the recently approved MiCA Regulation, which provides legal certainty for issuers of crypto-assets and for crypto-asset service providers. Hence, new opportunities are opening up for stablecoin-based cross-border payments, owing to their speed, low fees and transparency.

The Bank was also represented at the **Markets in Crypto-Assets Regulation Conference** held in Malta on 16 November 2023. Participants agreed that although MiCA strengthens investor protection and brings legal certainty, the crypto-asset sector remains subject to volatility and risks. The supervisors present stressed the need for stringent enforcement, information sharing, and the building-up of a strong compliance culture across the industry. The experience of countries (Malta and France) that had national legal frameworks for the crypto-asset sector in place prior to the

arrival of a common framework points to the need to insist on robust standards to combat cyber risks and money laundering.

By taking part in these foreign events, the Bank was able to:

- share experiences and knowledge with other regulators;
- keep up-to-date with the latest innovation trends;
- strengthen its expertise in digital finance regulation;
- contribute to the development of effective and harmonised regulation at the European level

Conclusion

In the area of fintech, 2023 was a very busy year for the Bank. Through the Hub, the Bank dealt with 19 enquiries, while in Sandbox, two pilot projects were underway.

The fintech topic attracting most attention was crypto-assets, particularly in the context of the MiCA Regulation that the EU adopted in May 2023. Another key issue was the preparation for the EU's Digital Operational Resilience Act (DORA). The Bank cooperated closely with Slovakia's Ministry of Finance to adapt Slovak legislation to both regulations. Most of the Bank's involvement in domestic and foreign fintech-focused conferences was in line with the above regulations.

In addition to the activities mentioned in this report, the Bank is also engaged in other related activities carried out by other public institutions in Slovakia, with these activities being in various areas with a focus on artificial intelligence.

Annex – The handling of Hub enquiries

The enquiries to the Hub during its fifth year of operation were largely in writing. A few of them were conveyed by teleconference or in person, especially where enquiries simultaneously focused on multiple financial areas and the presence of experts from different areas added more value to the meeting.

In 2023, as is usually the case, the number of Hub enquiries were lowest the summer months of July and August.

As regards the number of Hub enquiries, we noticed that their increase reflected the impact of preparations for new regulation at both the EU and domestic level. It may therefore be expected that in addition to an increase in crypto-asset-related enquiries, there will also be an increase in number of questions regarding payment services and open banking (e.g. the new PSR, PSD3 and FIDA framework for open banking).

Chart 2:
Number of Hub enquiries in 2023 and previous periods

