Mexican FinTech Law
and its secondary regulation

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May 2019

SHCP
SECRETARÍA DE HACIENDA Y CRÉDITO PÚBLICO

COMISIÓN NACIONAL BANCARIA Y DE VALORES

Size of the Fintech Sector

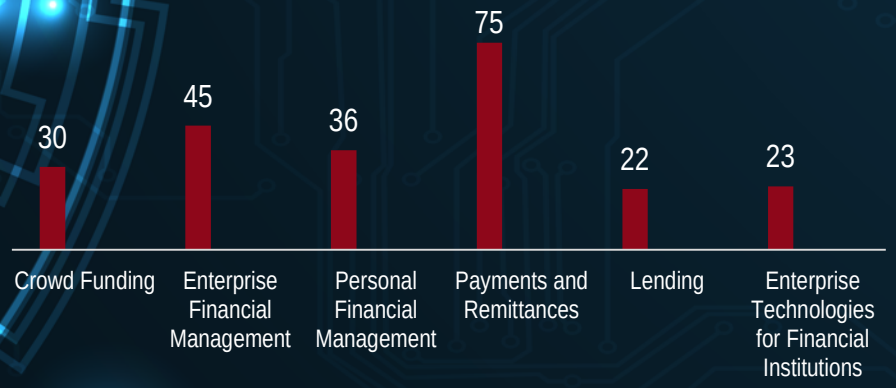
Global-level statistics:

- **Number of firms:** over 8,800 in 2017.
- **Assets:** around $870 USD bn. (1.16% of the global GDP).
- **Investments**: from $15.3 USD bn in 2010 to over $101 USD bn in 2017 *(TCA 37%)*.
- **Funding**: over $105 USD bn
- **Main Hubs:**

USA : California and NY
Mexico
Brazil
UK
France
China
India

Mexico (August 2018)

Fintech main segments



- Number of Fintech firms: 334
- 85% of firms is less than 5 years
- Firm size. 54% of firms has between 1 and 10 employees

- Main firms statistics:
  - **Active users**: more than 540 thousand.
  - **Assets**: Around $400 MMXN.
  - **Transactions**: more than $17,400 MMXN.
  - **Employees**: more than 400.

- Other relevant data:
  - **Startup place of birth**: Mexico City (61%), Guadalajara (9%), Monterrey (9%), Merida (4%), Puebla (2%)
  - **Maturity**: 31% is in *growth and expansión stage*, 47% are ready to *scale*, 22% in *beta version*.
  - **Main technologies**: Big Data and Analytics (25%), APIs and Open Platforms (17%) and Mobile and Apps (15%).

Source: Finnovista 2018

Mexico Fintech Market Segmentation

Source: Finnovista 2018

FinTech sector benefits

Startup Launch

Highly scalable models

Increases the safety and quality of services

Promotes financial inclusion

More efficient and less costly processes

Reduction of systemic risks (TBTF)

… among others.

FinTech sector risks

Money laundering & financing of terrorism.

Financial and systemic risks.

Legal uncertainty.

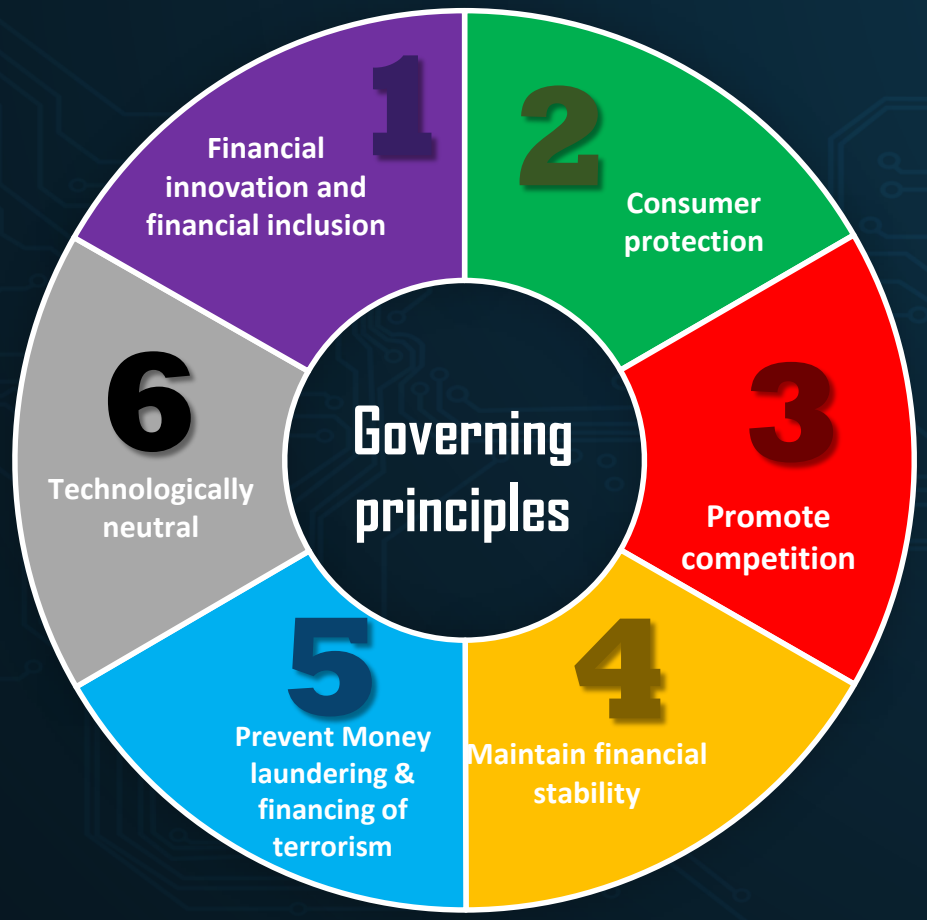
Lack of consumer protection.

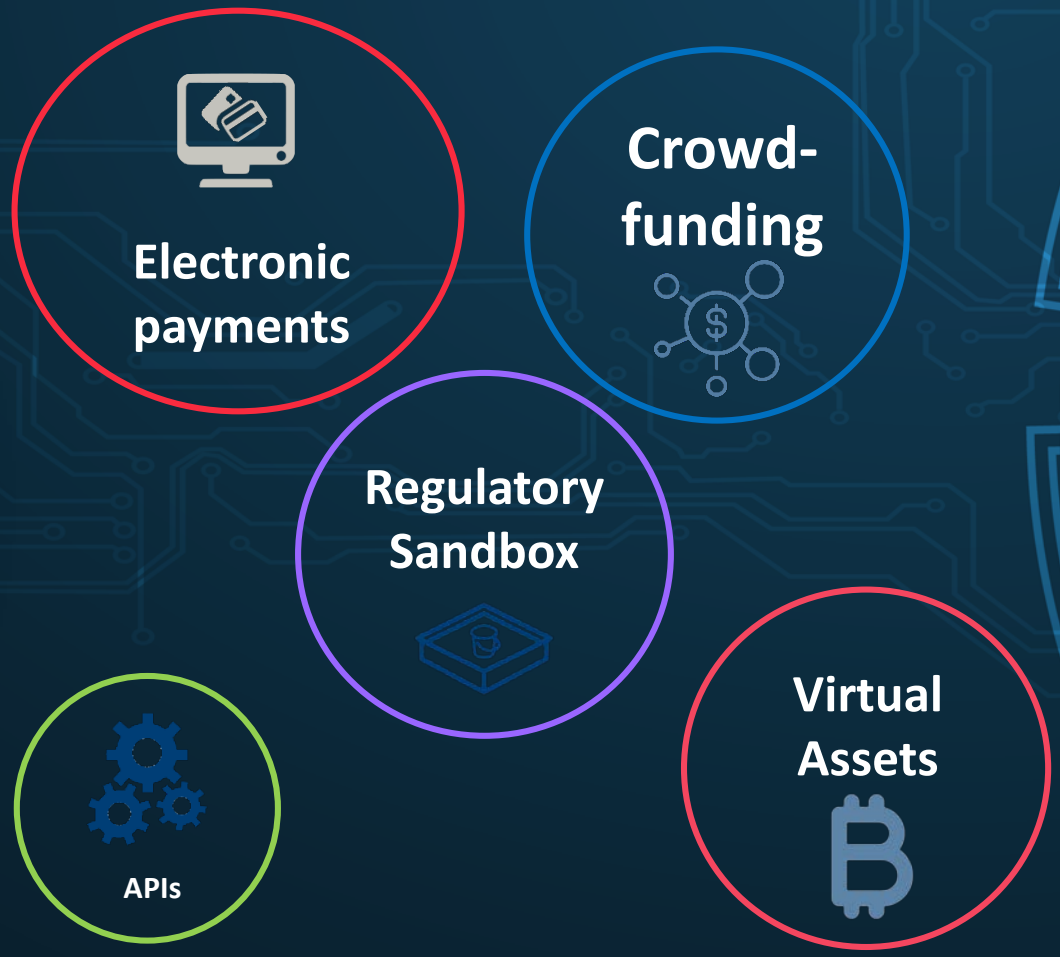
Technological risks.

For instance: impersonation and identity theft, information privacy and platform or database integrity.

Mexico's FinTech Law

Given the **risks** of the FinTech sector, **Mexico's FinTech Law was built on 6 governing principles** that provide flexibility, and **secondary regulation which will be actively updated** according to the **sector needs**.





Figures regulated in Law

Crowdfunding Institutions (CFI)

- ✓ Connects suppliers and requesters of credit so that they grant financing to each other, through the use of Apps, internet pages, electronic interfaces, etc
- ✓ Crowdfunding can be categorized in: debt (P2P), equity & co-ownership or royalties

Electronic Payment Funds Institutions (EPFI)

- ✓ Issuance, administration, redemption and transmision of electronic payment funds.
- ✓ Electronic payment funds: referred to a monetary value and recorded in transactional accounts (e-money).
- ✓ Main uses: *e-commerce*, funds transfers, P2P payments, payment of services.

Financial Technology Institutions

Virtual Assets Operations

- ✓ Virtual Assets: Representation of value recorded electronically and used as a mean of payment, whose transfer can only be carried out by electronic means.
- ✓ FTI and banks will only be able to operate with the virtual assets authorized by Banxico.

Regulatory Sandbox

- ✓ Temporary authorization so that regulated and unregulated entitites can test innovative models (those that use tools or technological devices with modalities different from the existing in the market).
- ✓ Unregulated entities: laws exceptions up to 2 years (possibility of 1 year extension).
- ✓ Regulated entities: secondary rules exceptions up to 1 year (possibility of 1 year extension).

Application programming interfaces (APIs)

- ✓ Objective is to share data. This type of data can be: open, aggregate or transactional.
- ✓ Obliged entities: financial entities, financial technology institutions, credit information societies, clearing houses, money transmitters and sandbox participants.
- ✓ Charge of comissions is allowed but subject to authorization.

Secondary provisions for Financial Technology Institutions (FTIs), first block

On September 10th, 2018 the following provisions were issued in the Official Gazette:

1. Additional requirements for the application as an FTI:
   - Business plan (operations to carry out); manuals of internal control, operation and risks, corporate governance; certified officer in AML/FT. Detail on shareholders.
2. Minimum capital requirements:
   - It depends on the complexity and risks of the operations (in mexican pesos, only one type of CF, with virtual assets or foreign currency). There are two levels: 150,000 and 210,000 USD.
3. Continuity plan for operational contingencies:
   - The plan has to ensure the continuity of the services and processes, the re-establishment of operations, and to minimize the impact of the contingencies. Plan must be tested anually.
4. FTI's cash inflows & funds transfers:
   - FTI must request authorization to receive/deliver cash from/to clients or to send/receive resources to/from foreign financial entities. In the case of CF, it is only for credits with problems of payment.
5. Financing and investment limits for crowdfunding:
   - Financing caps depending on the type of CF: P2P, 15,000 USD; P2B, real state equity and co-ownership, 500,000 USD.
   - Caps for investments depend on the type of person (an individual or a firm) and the type of financing. Limit per project investment is between 7.5% and 20% of the wealth invested in the platform.
   - For the aforementioned caps there are exceptions (example: for experienced investors).

Secondary provisions for Financial Technology Institutions (FTIs), first block

On September 10th, 2018 the following provisions were issued in the Official Gazette:

6. Mandates and commissions contracts by crowdfunding clients:
   - CFI manage different activities on behalf of their clients; automatic reinvestments, extrajudicial collection and representation in shareholders meetings. There are previsions that warrant clients that these activities are properly conducted.
7. Knowledge of risks by the CF investors:
   - CF institutions must obtain from investors an electronic recognition confirming that they know about the risks they are about to take when investing in CF platforms.
8. Accounting and financial information:
   - Rules about accounting criteria, external auditors, virtual assets recording and valuation and financial statements approval, to ensure that the information is accurate, standardized and available for supervision duties.
9. Selection criteria for requesters of credit in CF:
   - CFI must define a methodology to analyze and define the risk grade of the applicants' projects considering quantitative and qualitative criteria. The approved projects in their platforms have to be in clear language that does not bias client decisions.
10. AML/TF:
    - Regulation issued by the Ministry of Finance (SHCP).
    - The regulation in aligned with the applicable to other financial entities and includes: geolocation, risk-based methodology, reporting to the authorities, AML/TF officer, KYC, among others.

Secondary provisions for Financial Technology Institutions (FTIs), second block

On March 25th, 2019 the following provisions for Crowdfunding were issued in the Official Gazette:

Information disclosure on applicant's projects

- Information the CFI must disclose for every project published such as: amount requested, duration of CF, use of resources, risk grade, interest rate; information about the applicant's payment performance; aggregated information by type of CF.

Cibersecurity

- Specification of the necessary internal controls in order to warrant the confidentiality, availability and integrity of the information.
- Framework mandates the development of a master security plan approved by the general manager, hiring a CISO responsible for the supervision of the implementation of the information security policies, vulnerability and penetration tests and reporting security incidents to the authorities with the correspondent mitigation plan.

Use of electronic devices

- Dispositions regarding client authentication (something you know, you have and you are) and session management into the CF platform.
- Rules cover internal IT infrastructure as well as client devices.

Outsourcing

- Rules corresponding to contracting services with third parties necessary for the operation of the FTI (including cloud services)

Regulatory reporting

- Definition of the type of information that must be reported (catalog of fields), the format and the periodicity of it (i.e. cash flow reports, financial statements, claims).

Secondary provisions for Financial Technology Institutions (FTIs). Second block

Also, in-between the issuance of the September 10th and March 25th provisions, the following dispositions were issued:

Self correction programs

Set of activities that the FTIs are obligated to carry out in order to adjust their operation to the regulatory framework that is applicable to them and, where appropriate, to prevent future irregularities or non-compliance.

Regulatory Sandbox

The Financial Entities and other entities supervised by a Supervisory Commission or by the Central Bank, must obtain a temporary authorization, conditional to provide financial services through innovative models.

EFPI's Operations

Issued by the central bank, include: opening of accounts, receipt of resources for the issuance of e-money, as well as its transmission and redemption. Establish the limit to the overdrafts that EFPI´s can grant, the transfers of e-money referred to foreign currency, and the obligation to interconnect to the payment systems.

Currently CNBV is working with the central bank to issue the joint regulation for EPFI's in the following topics: Cibersecurity, use of electronic devices, outsourcing and continuity of operations.

Provisions to be issued for FTI's, third block

CNBV is working in the following dispositions with due date in the second semester of 2019:

Remote onboarding

- Given the risk of identity theft, the rule will be flexible enough to ease the remote onboarding process, but with several controls to ensure the identity of the client.

Dispositions to be issued in March 2020

Application Programming Interfaces (APIs)

- Standards and rules so that financial entities must share their data with third parties in an orderly and secure manner.
- Specifications will detail on the type of data to be shared and the fields that must be included. To share transactional data, a client must grant her consent.

Regulatory capital

- Capital complementary to the mínimum capital, this requirement is needed to mitigate operational risk.

Reflexions about FinTech Law and its implementation in Mexico

The following are some lessons learned from the work we have done in the development of FinTech Law and its secondary regulation:

1. FinTech sector moves faster than regulation:
   - Regulation requires close contact with the regulated institutions, in order to identify improvements to the provisions or even the Law (limits, new models, shareholders, etc.)
2. There is a need for an adequate ecosystem that allows a prudent development of FinTech sector: bring the participants to the regulatory perimeter in order to grant them security and to give powers to the authorities.
3. Regulators require different capabilities: the required profile for FinTech regulation is different.
4. Adequate regulatory burden for FinTech institutions v.s. level playing field with incumbents.
5. Ubiquity of internet: cross-border issue
   - There are no supervisory & regulatory standards worldwide-accepted for FinTech institutions.
   - MOUs among financial authorities around the world should be reviewed.

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