

# Mexico's Fintech Law initiative: What you need to know

On March 23 2017, the draft bill of the Financial Technology Law (the Law) was published in Mexico. Comments were invited by the Ministry of Finance and Public Credit (known by its Spanish acronym SHCP) from the Mexican banking and financial industry. The bill will also amend other existing financial services laws.

The Law will regulate the organization, operation, functioning and authorization of companies that offer alternative means of access to finance and investment, the issuance and management of electronic payment funds and the exchange of virtual assets or cryptocurrency (the **Financial Technology Institutions**, or **FTIs**).

This FinTech initiative formally introduces several widely used concepts that are in the industry to the regulatory framework, such as big data, crowdfunding, cryptocurrency, e-money, regulatory sandboxes, robo advisory and application programming interface (**API**).

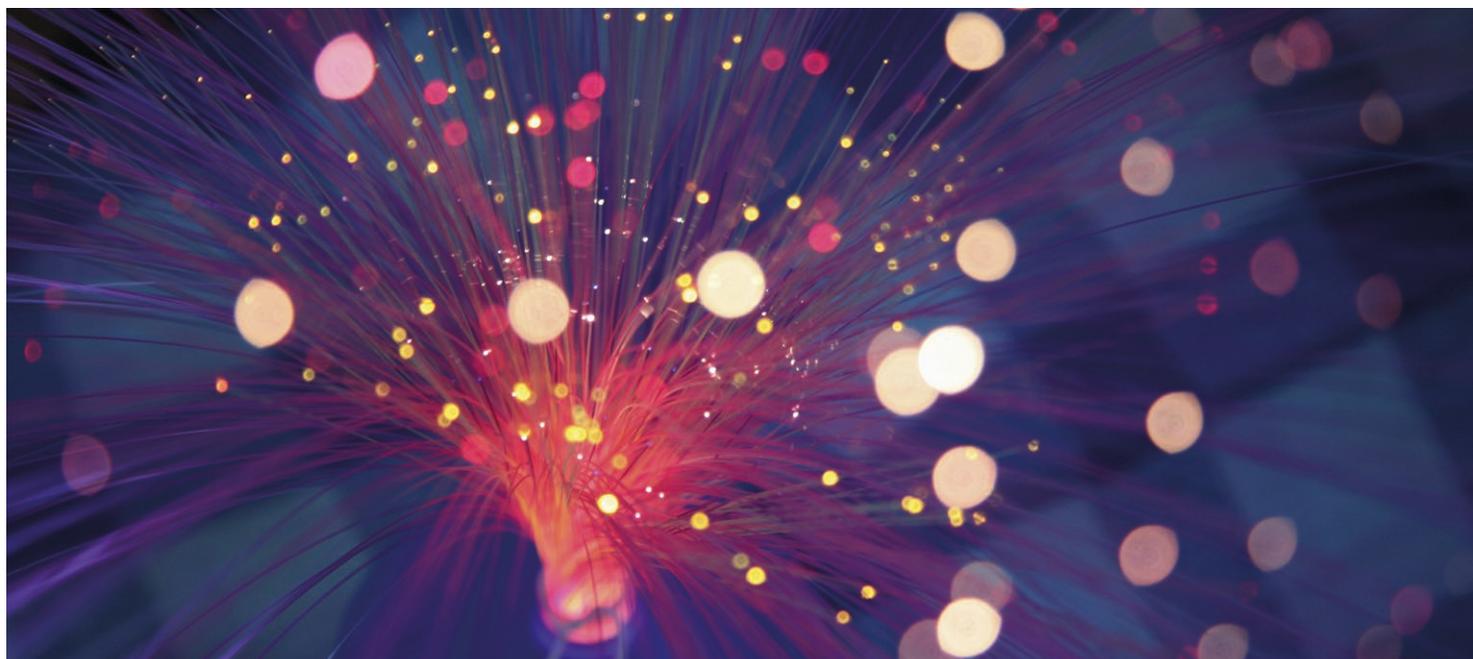
## Why are Mexican authorities taking steps to incorporate FinTech regulation into the legal framework?

Mexico is leading the way in Latin America to implement regulation in this area for several reasons. By establishing the basis for regulation and development of the FinTech industry, Mexican regulators are looking to give legal certainty to industry participants. They are also

hoping to take advantage of the opportunity to expand the financial market by covering segments of the market not covered by traditional banking institutions due to limitations in their infrastructure, cost of services and operational structures. The intention is to encourage products and services that are practical, easy to access and close to the client.

Another objective of this initiative is to provide financial stability, by providing prudential rules in financial risk, operational, technological, marketing, corporate governance and accounting rules, as well as establishing limitations and maximum amounts for transactions. Encouraging healthy competition is also important for the regulators, in order to have greater diversity and reduced costs in the provision of services and new distribution channels for financial services consumers.

Finally, this initiative intends to provide the basis for preventing the use of FinTech activities for purposes of money laundering and terrorism financing, as well as protecting the users of financial services.



### How does this FinTech initiative address money laundering and terrorism financing risks, and consumer protection?

To mitigate the risks of using FinTech companies for money laundering and the financing of terrorism, this initiative proposes establishing both client and investor identification standards, which it considers essential for the integrity and correct functioning of the financial system. Companies that wish to participate in this industry must use bank accounts maintained in authorized financial institutions; the use of cash in transactions is limited only to specific situations as permitted by the authorities.

Without any regulation in place, FinTech operations currently fall outside of the scope of the protection of Mexican authorities. However, by introducing a FinTech regulatory framework, the authorities will supervise the authorized companies and their activities, and establish much-needed defence mechanisms.

To further protect FTI investors and clients, FTIs will not be allowed to make any guaranteed returns on investment, or guarantee the result or success of investments. Also, the initiative prohibits related persons, or those with the power to direct or control an FTI's management or resolutions, from applying for crowdfunding financing, as well as those officers, partners, board directors, managers and other individuals imprisoned for over one year for a financial crime.

### Relevant FinTech authorities

The Law establishes the **SHCP**, the National Banking and Securities Commission (**CNBV**) and the Bank of Mexico (**Banxico**) as the main authorities in the financial technology field.

In addition, it provides that the CNBV, the National Commission for the Protection and Defense of Financial Services Users (**CONDUSEF**), the National Commission System for Retirement Savings (**CONSAR**), and the National Insurance and Bond Commission (known by its Spanish acronym **CNSF**) will have supervision and surveillance powers, and must operate within the scope of their jurisdictions.

The Law also proposes that a Committee on Financial Technology Institutions (the **Committee**), which will be set up, consisting of two representatives from each of the SHCP, the CNBV and Banxico.

The Committee, together with the CNBV, will be responsible for granting the necessary authorizations so that the FTIs can correctly operate within the national territory.

### What types of institutions will be regulated by the Law?

The following institutions that undertake financing, investment, savings, payments or transfer activities through interfaces, the internet or any other means of electronic or digital communications will be considered FTIs pursuant to the initiative:

- **Crowdfunding Institutions:** These serve as mediators to investment seekers and potential investors through digital platforms such as websites or mobile applications, so that prospective investors can fund applicants through such digital platforms.
- **Electronic Payment Institutions:** These offer the services of issuance, management, accountability and transfer of electronic payments. Electronic payment funds include, but are not limited to: (i) the amounts or units of an asset that can be assigned a monetary value and are recorded in an electronic transaction accounting ledger; and/or (ii) those

amounts that are accepted by a third party as receipt of an amount of money or respective virtual assets.

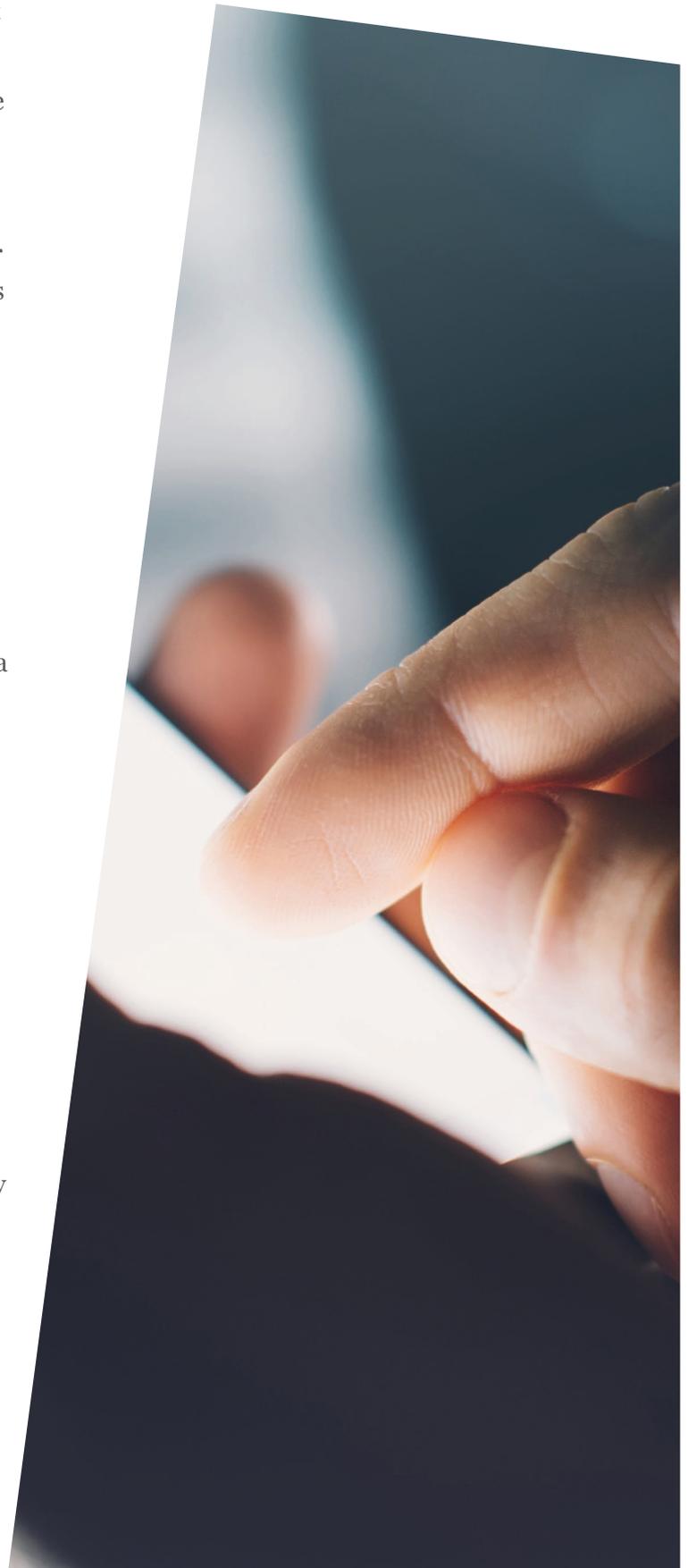
- **Virtual Asset Management Institutions:** These contact third parties through digital means in order to buy, sell or dispose of their own or a third party's virtual assets, and receive virtual assets to make transfers or payments to a person, including another Virtual Asset Management Institution. Virtual assets are those digital units that have similar uses to that of the Mexican peso, as determined by Banxico under certain criteria it will take into consideration.

### What does the enactment of the Law mean for future FTIs, and those FTIs already in existence?

If the Law comes into force in its current form, FTIs will have to be incorporated as a Mexican corporation (sociedad anónima de capital variable) or limited liability company (sociedad de responsabilidad limitada de capital variable) in order to provide services in Mexico. This is something all interested parties from outside Mexico must take into consideration.

All FTIs must obtain prior authorization from the CNBV, together with an opinion from the Committee. FTIs that are already providing services in Mexico will have to obtain the CNBV's authorization in order to continue operating.

To be authorized as FTIs, companies must certify to the CNBV that the transactions they wish to carry out are expressly indicated in their bylaws; (i) that they have the appropriate governing bodies and corporate structure to carry out their operations; and (ii) that they have the necessary infrastructure and internal controls such as operating, accounting and security systems, offices, as well as the respective manuals. The CNBV will publish the authorizations it grants on a public registry and on the CNBV's website.



An important point to keep in mind for both existing and future FTIs is that if a FTI fails to comply with the minimum operating requirements or any of the other conditions established in the Law, the CNBV has the authority to revoke its authorization to operate.

### Introduction of innovative companies (regulatory sandboxes)

Modeled after the regulatory sandboxes in the UK, this initiative enables innovative companies to operate dedicated to using technological tools, models, services or other means through innovative methods or processes.

Innovative companies must obtain a temporary authorization (of not more than two years), during which time they can provide their services to a reduced number of clients. This will be a trial period in which innovative companies can test out their business model. During this time, they must take all necessary steps in order to obtain permanent authorization, registration or concession to continue operating.

### Creation of a FinTech Council

The Law also provides for the creation of a FinTech Council, which shall act as a means of consultation, advice and coordination. The Council's purpose is to create a space for exchanging opinions, ideas and knowledge between the public and private sector, in order to learn about the innovations in the field of financial technology and plan their development and regulation. The Council will be composed of individuals from the public and private sectors.

### Next steps

Once the finance and banking community has provided its feedback on the initiative, the draft bill will be introduced to Congress who of Congress will make any adjustments and if passed, the bill will be enacted. It is therefore important to note that the bill is still in draft form and the proposal may change.

If the draft provisions are enacted without any amendments, as proposed existing FinTech companies will have a six months from the date the Law comes into force, within which to request authorization from the CNBV in order to continue operating. In the meantime, they will need to disclose to the public that the FinTech activities they perform are pending authorization from the CNBV, and are not supervised.

It is expected that the issuance of secondary regulation would be enacted and would cover general provisions such as regarding FTIs acting as attorneys-in-fact or agents of their clients, requirements and methodologies to report client risk and payment behavior to investors, technological infrastructure provided by financial entities with interests in an ITF, the creation of a specialized office for attending claims, and the use of robo advisory.

The Hogan Lovells team will closely monitor the continuing developments regarding this groundbreaking initiative.

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