

Fintech Institutions

This days, financial technology companies (Fintech) has acquire greater relevance in local and global markets. In essence, Fintech companies are mainly engaged in financial services through the use of digital platforms, technology and/or software.

Mexico became a pioneer country within Latin America by publishing on March 9, 2018, a new law called "Law to Regulate Financial Technology Institutions" ("Fintech Law"), that came into effect the day after its publication. The goal is to provide greater security for users and customers of Fintech platforms, as well as their owners and authorities, granting a legal field to act.

The purpose of this paper is to update and inform about the Fintech market in Mexico and its regulation in the Fintech Law.

I. Fintech in México.

With a 18% net growth, Mexico consolidates itself as the leading country in Latin America, ahead of Brazil, Argentina, Chile and Peru, in the *Fintech* industry. Finnovista, through its "*Fintech Radar México 2019*" report, reveals that Mexico it's about to cross the border of the 400 *Fintech* startups, with a total of 394, slightly ahead of Brazil, which has 380, the latter, according to the report "*Fintech in Latin America 2018: growth and consolidation*" published in November 2018 by the *Banco Interamericano de Desarrollo*. Likewise, the *Fintech* ecosystem in Mexico observed an 18% annual growth, percentage considered high, despite the uncertainty generated by the new *Fintech* Law and its secondary law.

The evolution of the *Fintech* industry in Mexico has been fast; its most predominant segments in the country has been: (i) Loans, with 81 startups (20.6%); (ii) payments and remittances, with 79 startups (20.1%); (iii) business finance management, with 52 startups (13.2%); (iv) business technologies for financial institutions, with 36 startups (9.1%); and (v) crowdfunding, with 29 startups (7.4%).

Although the *Fintech* market in Mexico is relatively young, the growth in the last 5 years has been quite strong, a period in which approximately 70% of the Mexican *Fintech* have been created. Mexico City the leader and center of financial innovation, attributing 53% of Mexican startups, ahead of Monterrey and Guadalajara, with 15% and 11%, respectively.

The *Fintech* Law, together with the visible growth of *Fintech* in Mexico, raises the *Fintech's* development expectations, and keeps Mexico as leaders in the sector in Latin America.

II. Content of the Fintech Law.

With the *Fintech* Law in force and a secondary regulation published on September 10, 2018 at the *Diario Oficial de la Federación*, called "*Disposiciones de carácter general para regular las Instituciones de Tecnología Financiera*", we can indicate, below, the relevant points of both laws and analyze their content.

II.1 The Fintech Institutions.

The *Fintech* Law was aimed to regulate *Fintech* under the name of Financial Technology Institutions (the "FTI"). These are subdivided into Crowdfunding Institutions and Funds Institutions of Electronic Payment.

The first are the companies known as crowdfunding. These companies put in contact, through computer applications, interfaces and/or internet pages, the demand for investment by applicants with the offer of investors.

The Funds Institutions of Electronic Payment are those dedicated to the reception, administration and transmission of funds through electronic mechanisms. Examples of this are online purses, money transfers, among others.

II.2 Virtual Assets.

Virtual assets are all electronic representation of value that people usually use as a way of payment and whose registration and disposal can only be done by electronic means. Virtual assets are not currency and doesn't include the Mexican peso.

Through virtual assets, Mexico began to regulate the so-called "cryptocurrency" and even authorizes its use to the FTI and other financial entities, as long as they have the authorization of the Bank of Mexico.

II.3 Innovative Models.

The *Fintech* Law labeled the so-called sandboxes under the name of innovative models, term used in the *Fintech* field to define a test environment for new business models.

The *Fintech* Law distinguishes between those new models belonging to regulated entities (such as financial entities and FTI) and those new models that may arise from any other non-regulated entity.

This last case, it's about the possibility that a moral person carries out, temporarily, an activity that requires authorization, registration or concession in an innovative way. The development of the business model will be with the purpose of entering for the first time in a certain regulated sector without being subject to full regulation. It's an incentive for companies to start in the sector, looking in the future to be able to get the authorization or corresponding concession.

On the other hand, innovative models for regulated entities assume that they will carry out activities of their corporate purpose through innovative models, as long as such way of providing their services implies exceptions to what is provided by authority's provisions or laws and, it's temporary.

III. Crowdfunding Institutions.

Crowdfunding, as mentioned above, allows the investment demand of entrepreneurs (the "Applicants") to be contacted with the investment offer that exists from third parties (the "Investors"). It turns out to be a great alternative for those entrepreneurs who don't have easy access to capital and an opportunity for investors to generate money outside banking entities.

The Crowdfunding institutions turn out to be one of the most attractive options for those who are not financial entities and those who want to be part of the growing world of *Fintech*.

III.1 Crowdfunding in Mexico.

Reports from Finnovista, mention that one of the five largest areas of *Fintech* in Mexico are the Crowdfunding, having 33% growth last year. In Mexico

Pérez Ferrer Abogados, S.C.

Javier Pérez Ferrer jperez@pfabogados.com

the number of *Fintech* companies dedicated to collective financing is approximately 29; representing 7.4% of the *Fintech* companies in the country.

III.2 Crowdfunding in the *Fintech* Law.

Crowdfunding in the *Fintech* Law is one of the FTI.

The *Fintech* Law requires that the activity be carried through any digital medium (property of the owner of the FTI) where investment Applicants and Investors have the possibility to meet.

It will depend on the system chosen by the Applicant, the type of crowdfunding to which the Applicant and Investors will be subject, namely:

- Debt → The Applicant receives the investment and a direct liability is generated, which the Investor will have in his favor as a creditor.
- Capital → When investing, the Investor acquires titles representative of the social capital of the Applicant.
- Co-ownership or royalties → Derived from an agreement between the Applicant and the Investor, the latter may participate in the profits, royalties and/or project losses.

IV. Evolution of *Fintech* in Mexico.

Most Mexican *Fintech startups* are still operating only in Mexican territory. However, according to Finnovista reports, one in five *Fintech* companies operate outside Mexico. The main destination of internationalization for Mexican *Fintech* is Latin America, with 84% of the total of these, operating mainly in Colombia and the United States. Other major countries to which the Mexican *Fintech* startups are venturing are Chile, Ecuador, Guatemala and Brazil.

Mexico City, June 13, 2019.

If you require additional information or have doubts about the content of this Newsletter, please contact any of the following members of our team, who will be happy to advise you with any questions you may have.

Rodrigo Canales Gutiérrez rcanales@pfabogados.com
Daniel Estrada Lechuga destrada@pfabogados.com
Elías Lisbona Jassán elisbona@pfabogados.com