

**DIRECTORATE FOR FINANCIAL AND ENTERPRISE AFFAIRS
COMPETITION COMMITTEE****Digital Disruption in Financial Markets – Note by Mexico****5 June 2019**

This document reproduces a written contribution from Mexico submitted for Item 5 of the 131st OECD Competition committee meeting on 5-7 June 2019.
More documents related to this discussion can be found at
<http://www.oecd.org/daf/competition/digital-disruption-in-financial-markets.htm>

Please contact Mr. Antonio Capobianco if you have any questions about this document
[E-mail: Antonio.Capobianco@oecd.org].

JT03448227

Mexico (COFECE)

1. The development of Fintech in Mexico

1. In 2014, COFECE issued a market study and recommendations regarding competition conditions in the financial sector and its markets. The study identified that, in Mexico, despite a well-capitalized financial system and low late-payment rates:¹

- users display low mobility and financial intermediaries do not have sufficient incentives to attract customers through quality, innovation and lower prices;
- there is a high concentration of suppliers in some products and services, as well as high bank profitability, surpassing that observed in countries with similar income levels;
- both the penetration levels of the financial system and the inclusion of the population remain low;² and,
- financial intermediation levels also remain low, which explains why Mexico is among the countries where least credit is granted.

2. The study found that the structure, performance and competition levels in the financial sector could be modified with the introduction of new technologies that reduce costs and increase the productivity of the sector.

3. During the nearly five years after this study was published, Fintech, through innovative business models and the use of digital platforms, have continued to create new means for the provision of different financial services. The financial technology sector has displayed important growth in Mexico.³ Mexico City is emerging as a “Fintech hub”,⁴ a categorization by the Cambridge Centre for Alternative Finance that considers, among other aspects, Fintech performance and regional influence. Concerning growth,⁵ Mexico had 334 Fintech startups in 2018, an increase of 96 startups since 2017 (a 40% growth), reinforcing the country’s position as the second largest Fintech ecosystem in Latin America.

¹ Research and recommendations on competition conditions in the financial sector and its markets. Available at: <http://bit.do/eS6Le>

² The 2018 National Financial Inclusion Survey shows that 25% of adults in Mexico hold no financial product whatsoever. Available at: <https://bit.ly/2FCSqJP>

³ The Mexican ecosystem is comprised in its majority by young startups, as 45% are less than two years old; 31% were established between three and four years ago; 9% are between four and five years old; and 85% are less than five years old. In 2018, as few as 15% were more than five years old (Finnovista, 2018).

⁴ The Cambridge Centre for Alternative Finance (2018). The Future of Finance is Emerging: New Hubs, New Landscapes, Global Fintech Hub Report. Retrieved from: <http://bit.ly/2JSPwBb>

⁵ Finnovista (2018). México Supera La Barrera De Las 300 Startups Fintech Y Refuerza Su Posición Como Segundo Ecosistema Fintech Más Importante En América Latina. Retrieved from: <http://bit.ly/2WaE628>

4. Among the segments in which Fintech operate in the country are:⁶
- **Payments and transactions.** Providing electronic payment services through direct transactions between individuals. The segment includes services such as currency exchange and foreign exchange hedges, remittances and the use of virtual currencies (cryptocurrencies) as a means of payment.
 - **Credit and financing.** Through the synchronization of the supply and demand of financial resources, by facilitating operations between individuals or between individuals and businesses through electronic platforms,⁷ and are generally carried out through five modalities: 1) collective loans (crowdlending), which consist of direct loans between borrowers and small-scale lenders (through peer networks), in exchange for peer-to-peer interest payments, 2) collective capital financing, which allows to invest in companies or projects in exchange for shares or shares in the company's capital; 3) collective real estate financing, which allows to invest in the real estate sector; 4) collective financing based on donations, in which investors do not receive remuneration for their contributions; and, 5) collective rewards-based financing, where investors receive some form of non-cash remuneration, such as pre-sales rights or products.
 - **Financial consulting and management services.** In this area, Fintech have emerged to offer investment management services through automatic systems based on Artificial Intelligence (known as “*robo-advisors*”) and can serve, for example, to simplify payroll payments or billing. Information banks also stand out in this segment; among other things, Fintech operate platforms through which users access all their financial information (credit history, personal accounts, and other information) and manage their personal finances.
 - **Insurance.** By using technology in the insurance industry to help users purchase and simplify the management of insurance policies.

2. The need for regulation in Mexico and COFECE's advocacy efforts

5. Mexico's Development Bank in charge of financing international trade (Bancomext) and the federal government agency responsible for coordinating strategies aimed at strengthening Mexico's participation in the international economy (Promexico),⁸ identified the need for a Fintech law since 2015, in response to the emergence of Fintech startups and growing pressure from Fintech entrepreneurs, banks and financial institutions. A crucial moment came about in 2016, when the National Commission for the Protection and Defense of Financial Service Users (CONDUSEF) found itself powerless to defend investors in the Foodies Fintech Fraud⁹ case (to the tune of almost 53 thousand dollars). In October 2017, the Executive branch of the Federal Government sent the Fintech bill to the

⁶ COFECE. OPN-007-2017 in Spanish. Available at: <http://bit.ly/2oIv8qh> and COFECE's Rethinking Competition in the Digital Economy. Available at: <http://bit.do/eS6Rw>

⁷ Typically, Fintech do not directly lend the resources they collect.

⁸ Bancomext & Promexico (2018) México: Nación Fintech, Nuevos negocios y ecosistemas en el sector financiero mexicano. Available at: <http://bit.ly/2JwCfib>

⁹ See *Expansión* article: Müller, N. (2016.10.07) Foodies comete fraude en Fondeadora por un millón de pesos, in Spanish, available at: <http://bit.ly/2HIzxTs>

Senate, with the purpose of regulating: i) collective financing institutions, ii) electronic payment institutions, and iii) transactions with virtual assets.

6. As such, the Commission deemed that, given the environment of constant innovation that exists in the financial sector, and the low levels of financial inclusion in Mexico, it was desirable for Fintech to have an adequate regulatory framework that guaranteed a level playing field to develop, adopt and use technologies and infrastructure to compete in the market, as well as for users to have the certainty necessary to carry out transactions in a secure fashion. Therefore, the Commission carried out two noteworthy advocacy efforts regarding the Fintech bill.

7. First, in October 2017, COFECE submitted procompetitive recommendations to the Senate on the bill.¹⁰ These recommendations addressed issues that could limit competition and pointed out that the Fintech Law should:¹¹

- Explicitly establish that users of financial services are the owners of their information and regulate the considerations for the transfer of data under non-discriminatory conditions. This implies clearly establishing that users' transactional data could be transmitted through networks, with the owners' consent, and that the confidentiality and security of the information should be guaranteed. This is relevant because customer information is a necessary input for Fintech to operate.
- Prevent unreasonable interruption of information from traditional financial institutions to Fintech. Financial entities, credit bureaus and clearing houses should not charge Fintech fees that are higher than the costs associated to the collection, storage, maintenance and transmission of information. Financial authorities must determine and regulate fees for data transmission.
- Stipulate that credit institutions must provide banking services under non-discriminatory conditions. To provide their services, Fintech need access the customers' accounts they want to serve and to access the Mexican electronic inter-bank payment system (SPEI), among others. Therefore, banking services are fundamental for providing and developing Fintech products. If credit institutions grant such services under discriminatory conditions, sanctions should be established.
- Foresee the use of open standards to facilitate the compatibility and interoperability of systems (concerning protocols, interface or other relevant characteristic) to facilitate compatibility and interoperability among systems.
- Establish neutrality, i.e., that Fintech are free to adopt any infrastructure and technology needed to provide their services. In this way, regulation should not constitute a barrier for Fintech to decide how to offer their services as long as they do so in safe conditions for their clients. Regulation applicable to Fintech should not be stricter than that applicable to the rest of the financial entities. Fintech compliance costs should be proportional to the objective pursued. Neutrality is fundamental to avoid unnecessarily diminishing the speed of innovation.
- Include that other (currently unknown) activities will be allowed and stipulate that new business models or activities that authorities determine will be permitted. Also,

¹⁰ COFECE. OPN-007-2017 in Spanish. Available at: <http://bit.ly/2oIv8qh>

¹¹ COFECE's Rethinking Competition in the Digital Economy. Available at: <http://bit.do/eS6Rw>

avoid including an exhaustive list of activities that can be carried out by Fintech, since this could require legislative changes with the invention of each new business models. Innovation in the financial sector is so accelerated that regulation must be open to new business models.

- Reduce the length of authorization periods and procedures required to begin Fintech operation to avoid disincentivizing potential Fintech investors, who expect short periods.
- Regulation should grant legal certainty without limiting competition. The legal framework should allow firms involved and potential entrants to develop and diversify business models.¹² The authority should not base the design of regulation on the first disruptive technology, since it could inhibit the development of subsequent innovations, which are a relevant source of competitive pressure.

8. Second, COFECE organized a conference to discuss competition-related challenges in the digital economy to launch a debate on the possible regulatory solutions for diverse sectors in the digital era. Relevant stakeholders, including regulators, local authorities, international experts, sector representatives and Fintech representatives, participated. Media coverage fostered by this forum contributed to placing the subject and the authority's views before the public eye. Later, the document "Rethinking competition in the digital economy", was published as an outcome of the conference to add to the understanding of issues competition authorities need to address in the context of digital economy.

9. Conducting the aforementioned advocacy initiatives enabled COFECE to face the challenge of advancing procompetitive regulatory frameworks in a fast-changing market in a digital economy environment, balancing protection of consumers and the stability of the financial system with the promotion of innovation and development of Fintech. The advocacy strategy also enabled the Commission to understand stakeholders' perspectives, and acquire expertise on the topic which is valuable for enforcement of competition law.

10. In March 2018, Mexico's Fintech Law was published in the Official Gazette. Among COFECE's recommendations adopted by the Mexican Fintech Law were: (i) explicitly recognizing financial information is the users' property; and (ii) Fintech's access to users' information under control of traditional financial entities should be facilitated through non-discriminatory fees and conditions established by financial authorities. Fintech will now have greater possibilities to assess the risk level of each potential client and generate products that respond to their needs, presenting themselves as an option different from traditional banking.

11. COFECE will follow the development of secondary regulation which, in line with the Fintech Law, should be favorable to innovation and the entry of new competitors, without generating barriers to competition and free market access.

12. Fintech are not only regulated by the newly enacted Fintech Law. They must also comply with the Federal Economic Competition Law (FECL). COFECE can exercise all its powers for the protection of free market access and economic competition in the Fintech market, as well as to prevent, investigate, combat, prosecute effectively, severely punish

¹² This flexibility can be achieved through the use of regulatory sandboxes. The United Kingdom's Financial Conduct Authority (October 2007) in its Regulatory sandbox lessons learned report, explains that a regulatory sandbox allows firms to test innovative products, services and business models in a live market environment, while ensuring that appropriate safeguards are in place.

and eliminate monopolies, monopolistic practices, unlawful concentrations, barriers to entry and to economic competition, as well as other restrictions to the efficient operation of this market.

3. Benefits of the enactment of the Fintech Law

13. After the enactment of the Law, Fintech have greater regulatory certainty, and specialized private institutions expect that they will increase their presence in the country.

14. The Commission considers financial services in the country will improve as Fintech start competing with traditional financial institutions.

15. Fintech Mexico,¹³ a specialized association, expects Fintech to bring economic benefits of around 265 million dollars a year to families and SMEs, in interest savings due to increased competition.

¹³ Fintech México (2018.03.18) México punta de lanza en regulación Fintech. Available in Spanish at: <http://bit.ly/2Enm8Q6>