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Fintech: how is the world shaping the financial innovation industry?

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Brazil

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1. Fintech regulatory framework: a summary of the most relevant laws and regulations concerning fintech and financial innovation.

Brazil has a cutting-edge regulatory framework applicable, among others, to digital lending (fintechs), payments and acquiring services, foreign exchange and remittances, insurance, asset management and crypto. The Brazilian Congress, the Central Bank and other relevant regulators have built a modern regulatory framework aiming to foster competition and promote entry and adoption of new technologies in those sectors.

It is worth mentioning that the term 'fintech' is widely and indistinctively used in the Brazilian market to describe both payment institutions (which include e-money issuers, credit card issuers, acquirers and payment initiation service providers) and digital lending entities (which include direct credit companies and peer-to-peer lending companies). Even though the regulatory requirements are somehow similar, payment institutions and digital lending fintechs have different regulatory frameworks.

The main regulatory framework applicable both to payment institutions and digital lending fintechs are:

Payment institutions

- Law 12,865 of 9 October 2013;
- National Monetary Council – CMN Resolution No 80 of 2021, CMN Resolution No 81 of 2021; and
- Central Bank – BCB Resolution No 96 of 2021 (as amended).

Payment institutions are legal entities that have as their principal or ancillary activity, the provision of payment services to end-customers. Payment institutions are classified based on the services provided, as follows:

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Issuers of electronic currency (eg, issuers of pre-paid instruments)

Entitled to offer and manage prepaid accounts and allow its clients to make payment transactions with the electronic currency deposited into such accounts.[1]

Issuers of post-payment instruments (eg, issuers of credit cards)

Entitled to offer and manage registered post-paid payment accounts to its clients and allow such clients to make payment transactions with such accounts. These entities cannot lend (such as revolving loans) to its clients.

Acquirers

Institutions that (1) enable recipients (merchants) to accept payment instruments issued by a payment institution or by a financial institution; and (2) participates in the process of settlement of payment transactions as a creditor before the issuer, in accordance with the rules applicable to payment arrangements.

Payment transaction initiators

Entitled to offer payment transaction initiation services but not authorised to offer and manage any payment accounts and may not receive or hold at any time the funds transferred within the provision of the service.

E-currency issuers and payment transaction initiators require prior authorisation from the Central Bank to start operations. Issuers of post-payment instruments and acquirers may start operating without Central Bank's prior approval; once they hit specific volume thresholds, they can continue to operate but must request authorisation from the Central Bank.

Regulated payment institutions (eg, after Central Bank approval is obtained) should comply with certain regulatory requirements including:

- minimum capital requirements;
- prudential requirements;
- reporting and risk administration system requirements;
- data protection laws;
- bank secrecy regulations;
- consumer protection laws, etc.

1 Clients' funds contained in such accounts are bankruptcy remote and cannot be used by the payment institution to fund its operation. In addition, clients' funds, while not being used, must be either deposited at the Central Bank or used to purchase government bonds.

Digital lending fintechs

- Law 4595 of 31 December 1964; and
- CMN Resolution No 4.656 of 2018, as amended.

Digital lending fintechs are considered 'financial institutions' and as such can lend money to third parties and follow a simplified and lighter regulatory regime. This is particularly important to the Brazilian market because, unlike other jurisdictions in Latin America, the activity of granting loans even with its own capital is a regulated activity[2] that requires prior authorisation from the Central Bank. Digital lending fintechs are classified as follows.

Direct credit companies (SCDs)

A financial institution entitled to grant loans and financing to borrowers exclusively by means of electronic platforms and by using its own capital. SCDs are not entitled to offer deposit-taking products and, thus, are not entitled to perform financial intermediation to leverage its lending activity with its deposit-taking activity.

Besides granting digital loans, SCDs are also entitled to offer the following services:

- credit rights acquisition operations;
- credit analysis services for third parties;
- collection of credit rights services;
- acting as an insurance representative in the offering of insurance products related to the services mentioned above;
- issuance of electronic currency (eg, issuer of pre-paid cards) and post-paid payment instruments (eg, credit cards).

Person-to-person loan companies (SEPs)

A financial institution that offers a digital platform that creates a lending marketplace between companies, securitisation vehicles and individuals as lenders and companies and individuals as borrowers. SEPs are also entitled to perform

- credit analysis services for third parties;
- collection of credit rights services;
- acting as an insurance representative in the offering of insurance products related to the services mentioned above; and
- issuance of electronic currency (eg, issuer of pre-paid cards).

2 Lending without a proper licence (as a financial institution) constitutes a crime. Not all financial institutions are allowed to lend money. Commercial banks, multipurpose banks with specific licences, credit, investment, and financing entities, SCDs and SEPs are types of financial institutions that are authorised to lend.

SEPs are not entitled to fund directly the loans offered within its platform and are not entitled to retain the funds disbursed by the lenders within the platform.

As mentioned, both SCDs and SEPs require prior authorisation from the Central Bank to start operations. They should also comply with several regulatory requirements including:

- minimum capital requirements;
- prudential requirements;
- reporting and risk administration system requirements;
- data protection laws;
- bank secrecy regulations; and
- consumer protection laws.

In essence, an SCD is a lighter bank subject to lesser financial regulatory requirements.

2. Regulations on crypto assets: a summary of the legal framework regarding crypto assets and how they are regulated.

Like other Latin American countries, until November 2022, Brazil had no specific legal framework applicable to the crypto assets industry. However, on 22 December 2022, Law No 14,478 was published (Law No 14,478/22) aiming at regulating the crypto assets market in Brazil. Although published, the Law will come into force only after 180 days from its publication. Law No 14,478/22 is aligned with global regulatory standards, including the recommendations of the Financial Action Task Force in connection with virtual assets. It focuses on combatting crypto-related crimes, removes crypto assets from the regulatory and supervisory scope of attributions of the Brazilian Securities Exchange Commission (CVM) and creates instruments to reduce the ecological footprint of the mining process through tax incentives.

Therefore, after coming into force, the 'digital assets service providers' (which is the name that the bill grants to those entities involved in a crypto transaction) virtual assets service providers (VASPs) wishing to operate in Brazil will require a regulator prior authorisation. The 'digital assets service providers' that were already operating before the new law was enacted will have at least six months to adapt themselves to the new applicable regulations and may continue to operate until the relevant authorisation is granted. Such digital assets service providers must comply with certain minimum regulatory requirements such as risk management, operational and capital requirements, etc.

Please note that pursuant to the approved text of Law No 14,478/22, a 'digital assets service provider' is defined as a legal entity that performs, on behalf of third parties, at least one of the following digital assets services:

1. trade between digital assets and national or foreign currency;
2. trade between one or more digital assets;
3. transfer of digital assets;

4. custody or management of digital assets or instruments that confer control over digital assets; or

5. participation in financial services and provision of services relating to the offering by an issuer or sale of digital assets.

Despite the above and until Law No 14,478/22 comes into force, the following applies to the crypto assets industry in Brazil:

- No prior licence or prior authorisation is required to operate a crypto exchange in Brazil or to offer crypto assets in the Brazilian market provided that such crypto assets do not fall within the legal definition of a 'security' (*valor mobiliario*). Conversely, if the crypto asset falls within the definition of a 'security', then the following would need to be complied with: (1) the issuer needs to be previously registered with the CVM and the offering needs to be listed and authorised by the CVM; and (2) the offering and distribution needs to be performed by a regulated entity such as a broker.
- Despite the foregoing, any acquisition or sale of crypto assets between a Brazilian individual or entity and an offshore individual or entity requires a foreign exchange transaction to be entered into with a local financial institution authorised to operate in foreign exchange. This means that, in practice, the remittance of funds abroad to purchase a crypto asset needs to be performed with the intermediation of a regulated financial institution.
- In general, according to the CVM's opinions and communiques, depending on the economic essence of the rights granted to their holders and the function assumed thereby, certain crypto assets and tokens may be deemed securities.
- Crypto exchanges need to comply with the general anti-money laundering regime applicable to any non-regulated entity.

3. Payment service providers and digital wallets: a summary of regulations applying to payment service providers and/or digital wallets.

Please refer to Question 1.

4. Special support to fintechs: a description of special programmes supporting the fintech ecosystem, fintech startups (eg, regulatory sandboxes and accelerator programmes) and regulations regarding special support.

The Central Bank has created and implemented a regulatory sandbox to support and foster the entrance of new innovative players to the Brazilian market.

Like other Latin American jurisdictions, the regulatory sandbox is a controlled environment in which companies are authorised by the Central Bank to test, for a limited period, an innovative project related with the financial or payment markets. The purpose of the sandbox is to stimulate innovation and diversity of business models, and foster competition within the Brazilian Financial System (SFN) and the Brazilian Payment System (SPB).

The Central Bank also created the Financial and Technological Innovation Laboratory (LIFT), which is a joint initiative of the Central Bank and National Federation of Associations of Central Bank Servers (Fenasbac). The main purpose of LIFT is to foster innovation by encouraging the creation of prototypes of technological solutions for the financial system. LIFT is truly an ecosystem aimed at innovation.

Finally, other regulators such as the CVM and the Superintendence of Private Insurance have their own regulatory sandboxes with similar purposes and regulations, aiming to foster innovation in their relevant industries.

5. Open banking: a summary of regulations regarding open banking and direct or indirect regulations that affect open banking.

Brazil has a specific legal framework and a highly developed open finance system.

According to the current regulatory framework applicable to the Brazilian Open Finance system contained in Joint Resolution No 1 of 2020 issued by the Central Bank and the CMN, and several normative instructions issued by the Central Bank, the Brazilian open finance system is defined as the system that allows customers of financial products and services to share their information between different financial institutions duly authorised by the Central Bank in order to receive a better financial product or service.

Recently, the Central Bank decided to change the name of the system from open banking to open finance, with the purpose of allowing the sharing of financial information not only related with traditional financial products (savings accounts and loans), but also information related with any financial product such as foreign exchange, acquiring, investment, insurance, etc. The Brazilian open finance system follows the following principles:

- As described above, only regulated entities may participate in the open finance system to guarantee the privacy, due storage, encrypted sharing, and correct processing of confidential personal and transactional data which is subject to bank secrecy obligations. Despite this, the current regulatory framework applicable to the open finance system provides for mandatory and voluntary participants, which will depend on the significance and size of the financial institution in the Brazilian market.
- The open finance system does not modify or alter the Brazilian General Data Protection Law, which needs to be strictly complied with among the participants.
- The main purpose of the open finance system is to foster competition and provide transparency to the users.
- Users are the owners of their data; thus, the open finance system is based on the principle that data sharing is only legally and practicably possible upon a user's express consent.

The Central Bank has regulated the minimum governance and technical standards to be mandatorily adopted among participants in order to be plugged to the open finance system.

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