Legal Framework for Doing Business of FinTech in India

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TRANSACTION | ADVICE | LITIGATION

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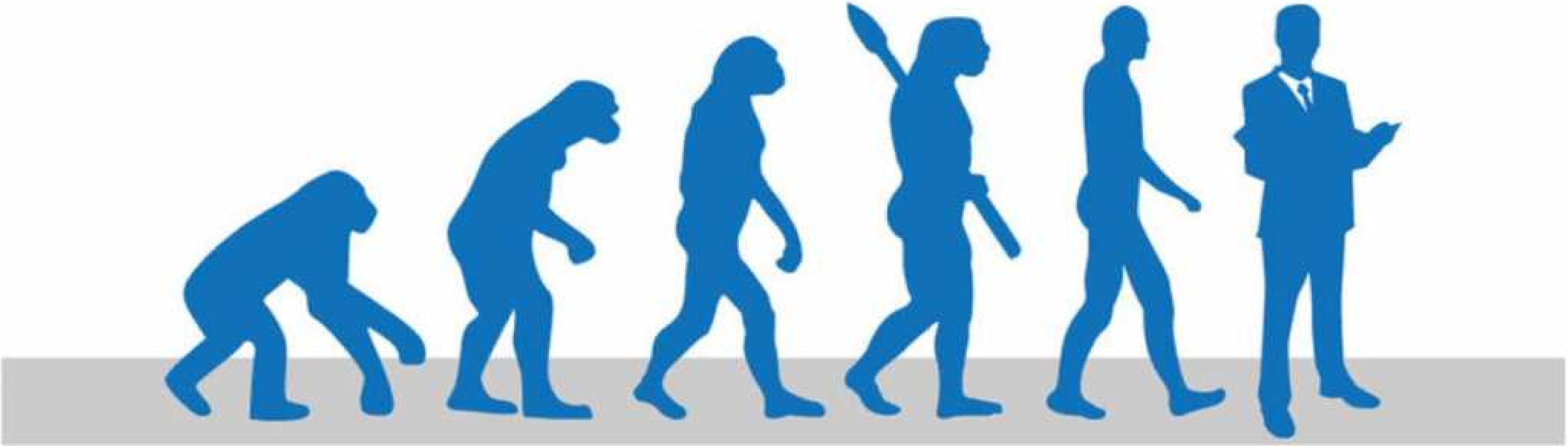
Introduction to Fintech

The Fintech sector has grown rapidly in last few years and is on track of ever evolving track. Prior to 2008 financial crisis, the traditional banking sector was the only playground available for financial needs. The financial crisis collapsed the traditional banking & financial mechanism and paved the way for more secure and updated financial transaction which led to emergence of Fintech, which has altered the economic viability of traditional banking sector participants to originate loans, translating into contraction of the credit supply for individuals and SMEs.

Fintech is an umbrella term coined in the recent past to denote technological innovation having a bearing on financial services. Fintech is a broad term that requires definition and currently regulators are working on bringing

*According to Financial Stability Board (FSB), of the BIS, "**Fintech is technologically enabled financial innovation that could result in new business models, applications, processes, or products with an associated material effect on financial markets and institutions and the provision of financial services**". This definition aims at encompassing the wide variety of innovations in financial services enabled by technologies, regardless the type, size and regulatory status of the innovative firm. The broadness of the FSB definition is useful when assessing and anticipating the rapid development of the financial system and financial institutions, and the associated risks and opportunities.*

FINTECH: THE EVOLUTION



In 2008 there was a global financial meltdown. Cloud technology emerged and increased access to open source software, which in turn triggered a revolution in financial services technology.

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FINTECH GLOSSARY

ANALYTICS
The tool used to measure patterns or trends in data

CROWDFUNDING
Projects funded buy the public

DATABASE
A program that allows you to organise your information in an efficient manner on one platform

CRYPTOCURRENCY
Virtual currency thatis thoroughly protected from hackers

ENCRYPTION
Is the most effective way to achieve data security. To read an encrypted file you must have access to a secret key or password

BENCHMARK
A point at which activity and perfrmance are measured and compared

API
Application Programming Interface. Software tat allows two different sources to communicate with eachother instantly

BLOCKCHAIN
A record of all public bitcoin transactions updated in real-time

BIG DATA
An immense supply of data, and often the analysis of said data

BOOTSTRAP
An individual or group starting a new bussiness venture with minimal amoutn of seed investment or capital

CLOUD
A virtual infrastructure that holds an unlimited amount of data and information

COGNITIVE COMPUTING
Self-learnig computer systems that attempt to mimic human thinking using data mining, pattern recognition and natural langauage processing

DATA
Information used to analyse or evaluate a possible outcome or trend

DISRUPTIVE INNOVATION
The establishment of a new market, product or service that disturbs a pre-existing market or status quo

DIGITAL NATIVE
Young people who have grown up with the availiability and use of dgitial technology

BITCOIN
A new form of independent currency that is held completely virtually

IOT
Internet of Things (IoT) refers to development of everyday internet-connected objects that have the ability to record, recieve and send data

DIGITAL WALLET
Refers to any electronic device or application that allows individuals to make electronic transactions.

FINNOVATION
A buzzword referring to financial innovation

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Fintech Business

Indian FinTech Startups
Mobile Payments
P2P Payments, M-commerce
Companies: Paytm, QuikWallet, ZipCash, YPAYCASH, Oxigen, Vodafone m-pesa, Airtel money, MoneyOnMobile, MobiKwik, ItzCash, mRupee, Idea Money, Paychamp, ePaisa, Pyro, MoboMoney, Eko, PayMate, kaypay, Chillr, PayQwik, SBI MobiCash easy, ICICI Pocket, Ruplee, Momoe, PayUMoney, mpurse, iKaaz, atom, Citrus, MobiCash
Financial Inclusion
Branchless Banking Services
Companies: Eko, FINO, Paydome, Integra, A Little World
Lending
Online P2P/SME Lending
Companies: Milaap, Faircent.com, i-lend.in, P2P, MicroGraam, LenDen Club, IndiaLends, InstaPaisa, Vote4Cash, MutualLoans, Capital Float, NeoGrowth, Janta
Credit Score Research
Access & Improving Credit Score
Companies: inVenture, CreditMantri
Remittance
Mobile & Web-Based Remittance
Companies: Remit2India, RemitGuru, BookMyForex, Airtel money, Vodafone m-pesa
Bills & Recharge
Online and Mobile-Based Recharge & Bill Payments
Companies: Paytm, MobiKwik, MoneyOnMobile, Citrus, MoboMoney, ItzCash, Oxigen, ZipCash, YPAYCASH, FreeCharge, EasyBill, BillDesk, BillJunction, Airtel Money, Vodafone m-pesa
Card Acceptance
Companies: Pine Labs, Ezetap, Mswipe, MobiSwipe, Mosambee, Qwikcilver
Others
Bitcoin Trading, On-The-Go Retail Trading
Companies: Unocoin, zebpay, Coinsecure, RKSV
Payment Gateways
Payment Gateway Solutions
Companies: Transerv, PayU, Citrus, Atom, Zaakpay, EMVANTAGE, DirecPay, Airpay
Personal Finance
SAAS-Based Solutions & Platforms
Companies: PaisaGate, MProfit, Aditya Birla MyUniverse, Intuit Money Manager, Perfios
Prepaid & Gift Cards
Multipurpose Prepaid Cards and Gift Cards
Companies: ItzCash, Zaggle
*Boundaries might overlap in case of mobile payments and bills & recharges.
Companies mentioned in lighter grey are part of large conglomerate group

*Today, financial markets & services are flooded with technology driven innovation, whereby new non-depository institutions- referred to as peer-to-peer financing, loan based crowdfunding platform, marketplace lenders (MPL) - providing loans of various types and duration to end users through online and mobile channels. Some of these companies lend from their own corpus/balance sheet, while some serve as brokers between investors and borrowers, commonly referred to as "**Platform Lenders**".*

MPLs are more agile and better able to fill gaps that traditional banks cannot, or are unwilling to address. The traditional banks are hindered by their legacy processes, older systems and branch focused culture.

MPLs flexibility are their ability to provide unsecured lending, source funds from investors with higher risk appetites, apply innovative credit scoring models and operate with lean set up. Most importantly, much of the growth in MPLs is due to many being regulated in the same way as traditional banking participants. Financial & Banking Regulators are becoming increasingly aware of this and recognize that appropriate reform is needed.

To balance the gap, where MPLs do not create future supervisory issues with the benefits of encouraging innovations that will provide borrowers with the necessary liquidity and financing.

Three unique MPL models are currently prevalent in India, depending upon the nature of the services provided by these platforms:

a. MPL Platform as Originator

b. MPL Platform to route to NBFC

c. MPL Platform as matchmaker

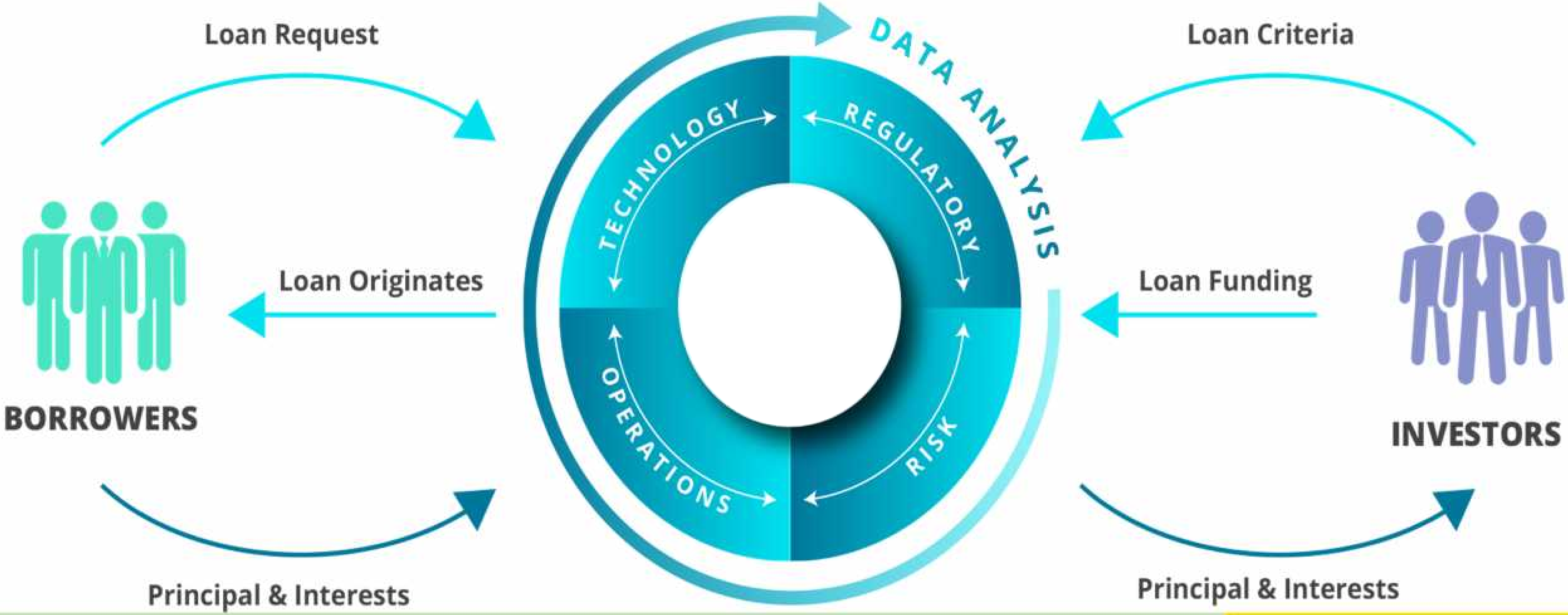
Marketplace Lending Models in India

Platform as Originator: *Act as an aggregation and origination platform to route leads to partner banks & NBFCs*

Platform to route to NBFC: *Act as an origination platform b/w borrowers and in-house NBFC. Also play the role of originator for other banks & NBFCs depending upon the risk profile & nature of loans*

Platform as match-maker: *Has both lenders & borrowers enlisted on a common matching platform. Connects the borrowers & lenders with no/limited role in loan disbursements and repayments*

Value Exchange between Borrowers and Investors

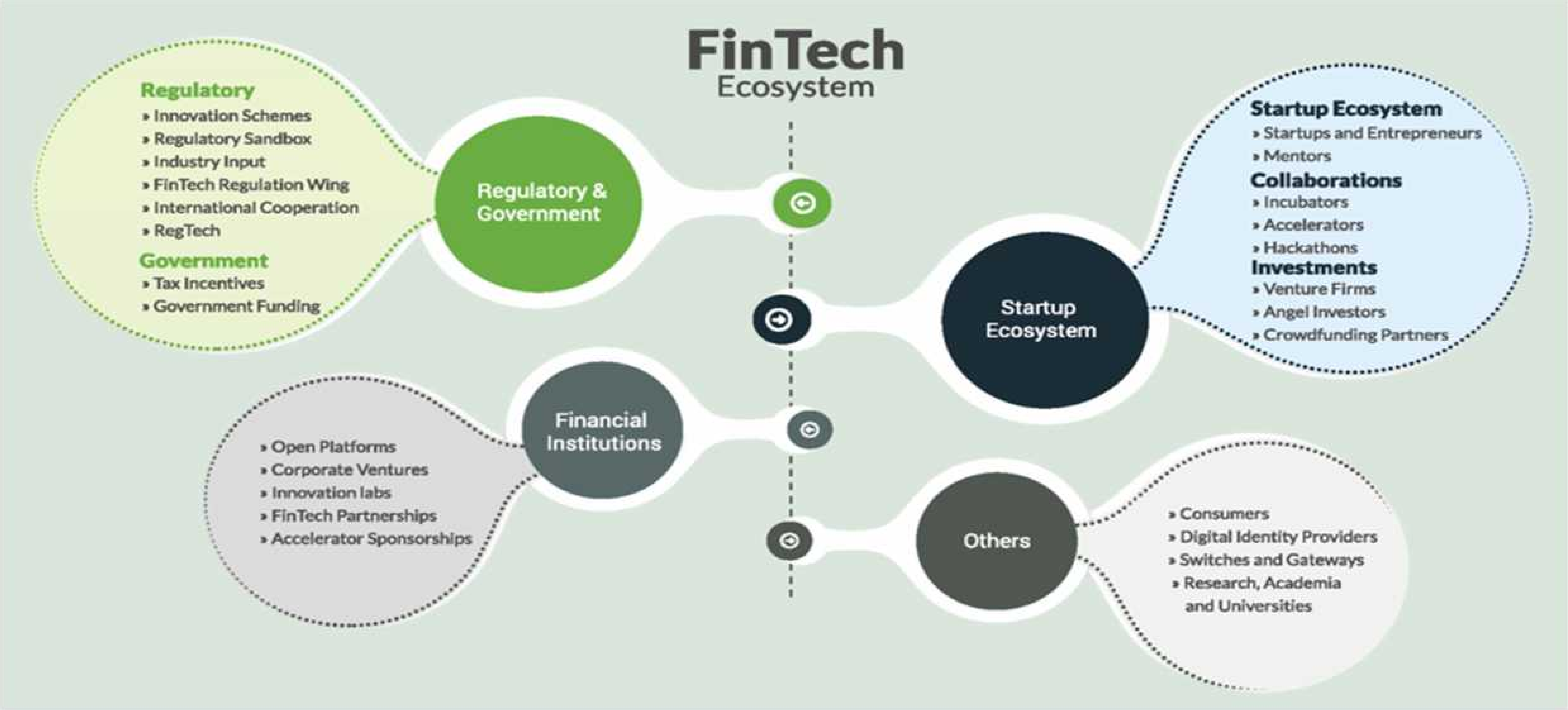


*International standard setting bodies including regulatory authority of different jurisdiction are setting up task forces on Fintech's to have understanding of major innovations, a potential impact of Fintech on the industry & assess risks for banks & any implications on supervision. Fintech or digital innovations have emerged as a potentially transformative force in the financial markets. With the several benefits of Fintech, including efficiency improvements, risk reduction and greater financial inclusion. Some of the key challenges associated with Fintech such as difficulty of regulating an evolving technology with different cases, monitoring activity outside the regulated sector, and identifying and monitoring new risks arising from the technology. Regulatory uncertainty surrounding Fintech could potentially hamper its development. As a result, international standard setting bodies such as Basel Committee on Banking Supervision (BCBS), Financial Stability Board (FSB), Committee on Payment and Market Infrastructures (CPMI) including regulatory authorities of different jurisdictions are taking steps to actively monitor Fintech developments both domestically and in cooperation with international organizations. Strong, proactive policy level support from the government has been providing much needed boost to user adoption. Initiatives such as Jan Dhan Yojna, Aadhar and the emergence of UPI provide a good foundation for Fintech companies to permeate '**last mile**' touchpoints and boost financial inclusion across the country.*

Financial Activity	*Fintech Segments*	*Description*
Credit	*Peer to Peer Lending* *Crowd Funding* *Market Place for Loans* *Online Lenders- NBFC using own capital* *Credit Scoring Platforms*	➢ *All forms of lending market places including Peer to Peer lenders and market places that connect borrowers with both, institutional and lenders.* ➢ *Also include crowd funding and equity funding platforms.* ➢ *NBFCs that use alternative scoring and digital channels for acquisitions.*
Payments	*M-Wallets & PPIs* *Merchant Payments & POS Services* *International Remittance*	➢ *Services that enable transfer of funds for various use cases- P2P (Person to Person), P2M (Person to Merchant), etc.* ➢ *Services targeted at both Payees and Merchants by enabling requisite payment infrastructure through mobile or other technologies.*

Financial Activity	*Fintech Segments*	*Description*
Investment Management	*Robo Advisors* *Discount Brokers* *Online Financial Advisors*	➢ *Wealth advisory services delivered. through technology governed rules and investment strategies.*
Personal Finance Management	*Tax Filing & processing* *Spend Management & Financial Planning* *Credit Services*	➢ *Tools and services for active management of individual financial profiles (e.g. spend, investments, credit profile, etc.)*

Financial Activity	Fintech Segments	Description
Bank Tech	Big Data Blockchain Customer Onboarding Platforms	➢ Services that utilize many data points such as financial transactions, spending patterns to build the risk profile of the customer. This provide an alternate to traditional underwriting methods that are unable to serve people with limited credit data. ➢ There is significant value in unstructured data. However, it is difficult to derive value from unstructured data, owing to challenges in analyzing it. A number of new tools are being developed to derive value from large data sets.
Insurance Tech	Insurance Aggregator	➢ Small Business insurance. ➢ Usage based insurance.


FinTech
Ecosystem
Regulatory
» Innovation Schemes
» Regulatory Sandbox
» Industry Input
» FinTech Regulation Wing
» International Cooperation
» RegTech
Government
» Tax Incentives
» Government Funding
Regulatory & Government
Startup Ecosystem
» Startups and Entrepreneurs
» Mentors
Collaborations
» Incubators
» Accelerators
» Hackathons
Investments
» Venture Firms
» Angel Investors
» Crowdfunding Partners
Startup Ecosystem
Financial Institutions
» Open Platforms
» Corporate Ventures
» Innovation labs
» FinTech Partnerships
» Accelerator Sponsorships
Others
» Consumers
» Digital Identity Providers
» Switches and Gateways
» Research, Academia and Universities

Factors for growth of Fintech Business in India

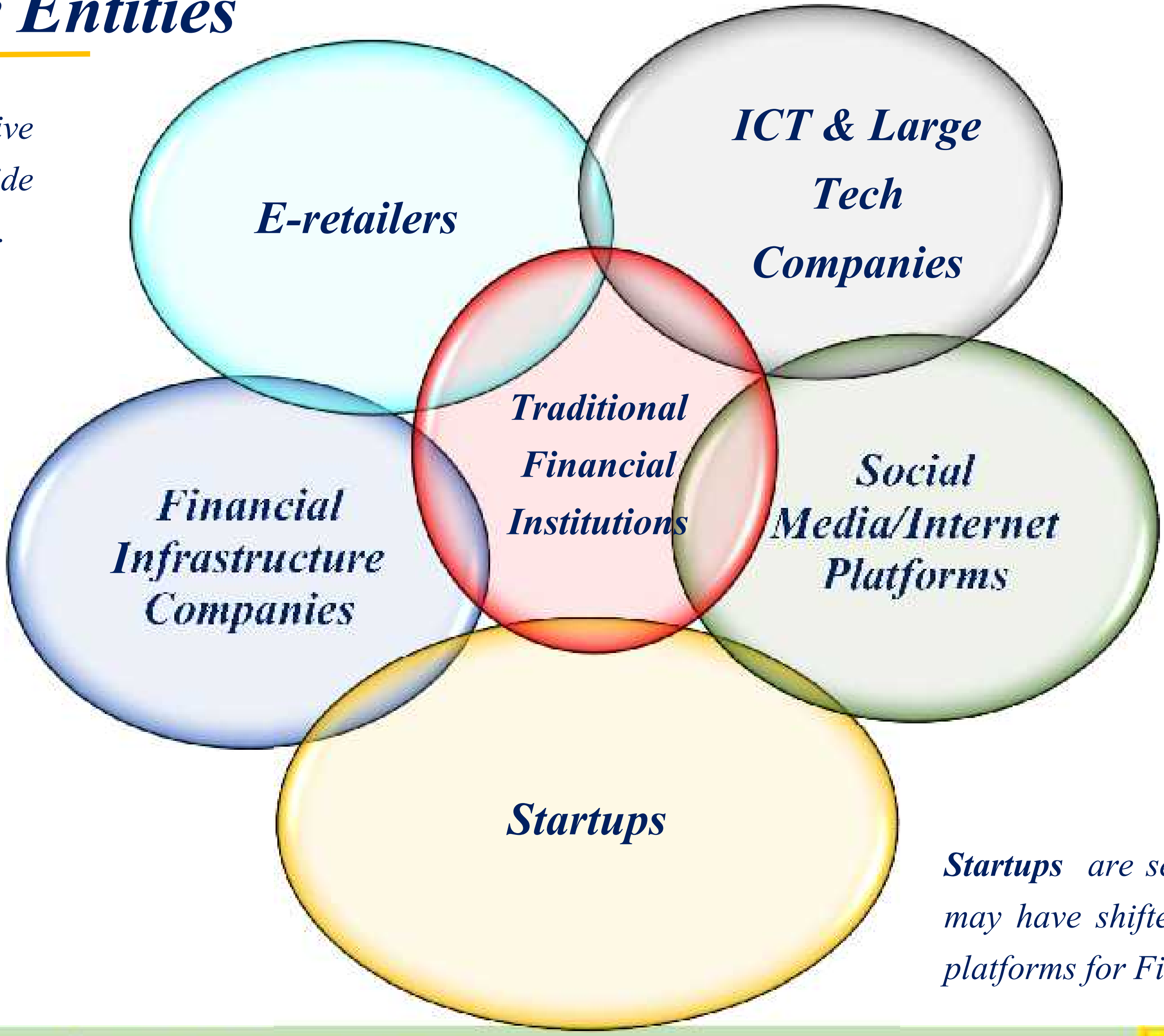
- ***Growing Financial Needs:*** *Traditional service delivery models have not been able to address the financial needs of consumers. Fintech with its ease of usage and access, has allowed consumers to get access to these services, typically at lower costs, driving its active adoption.*
- ***Conducive Environment:*** *Regulatory Authority and legal system in India is interested in driving cashless/digital transactions for financial inclusions as well as control. The spread of broadband/telecom provides a platform for financial services delivery with low delivery costs and high outreach.*
- ***Increasing investments:*** *There has been significant increase in Fintech based startups in India over the last couple of years, primarily in the payment space (driven by regulatory changes and market demand). In addition, there is increased willingness by domestic, as well as international VCs/Pes and incubators to heavily invest in this sector in India.*
- ***Responsive marketplace and incumbents:*** *Globally, Fintech startups are disrupting the business models of incumbent financial services players. In India as in other markets, incumbents are adopting a range of strategies to deal with the risk and opportunity afforded by Fintech paradigms. These include strategic partnerships that provide the Fintech firm with access to bank clients and infrastructure to acquisitions.*

Fintech & Disruptive Entities

E-retailers *are likely to be disruptive using their large data sets to provide consumer focused products and services.*

Traditional Financial Institutions *need to be most concerned as they are not seen as disruptive force, but they are best able to leverage Fintech innovations.*

Financial Infrastructure companies *should be concerned as more Financial Institutions turn to Fintech infrastructure providers but they may be seen as enablers of innovation*



ICT & Large Tech companies *are also seen as potentially disruptors to the financial service sector, as they are able to innovate at a far faster pace than incumbents.*

Social Media/Internet Platforms *are further entrenching their place as disruptors by leveraging their large client reach to provide new channels for customer services and business models.*

Startups *are seen as the main disruptors, but may have shifted to B2B models & providing platforms for Financial Institutions.*

Regulatory Landscape & Fintech Business in India

Indian regulatory authorities including RBI, SEBI & IRDA have adopted an accommodative stance towards an emerging Fintech sector without bringing in prohibitive guidelines to over regulate the sector. Despite catching up with the rapidly evolving eco system, Indian regulators have adopted a consultative approach and have been proactively foreseeing the need for adequate regulations, especially in the areas concerning public funds i.e. peer-to-peer lending, crowd funding and alternative currencies. The multiplicity of firms and mosaic of business models complicate the classification of the various types of activities, products and transactions covered under the FinTech Spectrum. Fintech treads across several activities that are within the scope of different financial sector regulators.

At present, all the traditional financial activities are regulated by the following regulators:

Regulatory Authority	***Traditional/Core Financial Activity***	***Applicable Law/Regulations***
*Securities Exchange Board of India ("**SEBI**")*	*Collective Investment Schemes*	*Securities and Exchange Board of India (Collective Investment Schemes) Regulations, 1999*
	Alternative Investment Funds	*Securities and Exchange Board of India (Alternative Investment Fund) Regulations, 2012*
	Real Estate Investment Trust; *Infrastructure Investment Trust*	*Securities and Exchange Board of India (Real Estate Investment Trusts) Regulations, 2012;* *Securities and Exchange Board of India (Infrastructure Investment Trusts) Regulations, 2014*
	Portfolio Management	*Securities and Exchange Board of India (Portfolio Managers) Regulations, 1993*
	Employee Benefits	*Securities and Exchange Board of India (Share Based Employee Benefits) Regulations, 2014*
	Mutual Funds	*Securities and Exchange Board of India (Mutual Funds) Regulations, 1996*
	Any other schemes or arrangements regulated under SEBI Act, 1992 or its regulations	*SEBI Act, 1992 or its regulations*

Regulatory Authority	***Traditional/Core Financial Activity***	***Applicable Law/Regulations***
*Reserve Bank of India ("**RBI**")*	*NBFC, Residuary Non-Banking Company, Schedules Commercial Banks, Small Finance Banks, Payment Banks, State & District Co-operative Banks, Primary (Urban) Co-operative Banks*	*RBI Act, 1934 or its guidelines or its regulations*
	Any scheme or arrangement under which funds are accepted by individuals or entities engaged as Business Correspondents and Facilitators by banks	*RBI Act, 1934 or its guidelines or its regulations*
	Any scheme or arrangement under which funds are received by a system provider operating an authorised payment system	*Payment & Settlement Systems Act, 2007*
	Any other schemes or arrangements regulated under RBI Act, 1934 or its regulations	*RBI Act, 1934 or its guidelines or its regulations*

Regulatory Authority	***Traditional/Core Financial Activity***	***Applicable Law/Regulations***
*The Insurance Regulatory Development Authority ("**IRDA**")*	*A contract of insurance pursuant to certificate of registration*	*Insurance Act, 1938*
*National Housing Bank ("**NHB**")*	*Housing Finance Companies*	*National Housing Bank Act, 1987*
*Pension Fund & Regulatory Development Authority ("**PFRDA**")*	*Any scheme or arrangement under Pension Fund & Regulatory Development Authority Act, 2013*	*Pension Fund & Regulatory Development Authority Act, 2013*
*Employees Provident Fund Organization ("**EPFO**")*	*Any scheme. Pension Scheme or Insurance Scheme framed under Employees Provident Fund & Miscellaneous Provisions Act, 1952*	*Employees Provident Fund & Miscellaneous Provisions Act, 1952*
Central Registrar, Multi-State Co-Operative Societies	*Any scheme or arrangement for acceptance of deposits from members of Multi-State Co-Operative Societies*	*Multi-State Co-Operative Societies Act, 2002*
*Ministry of Corporate Affairs ("**MCA**")*	*Deposits under Chapter-V of the Companies Act, 2013;* *Nidhi Company or mutual benefits society;* *Producer Company*	*Companies Act, 2013*

Now most of the Fintech provides an associated and related services to the traditional and core financial activities, where they are not requisite to obtain in principal approval from the sectoral regulator, however, for their functional activities, they need to abide and compliance with sectoral regulations and guidelines to the extent as applicable on them. And, some of them have replaced traditional financial activity through Fintech and they are governed by the new evolved legal framework such as peer-to-peer lending as governed as NBFC under RBI Directions via its Mater Directions issued on October 04, 2017 and updated on 09/11/2017 & 23/02/2018.

*Regulations for crowd funding is been proposed by SEBI for public consultations and we may expect a detailed legal framework for the same in the coming months. Similarly, for other Fintech's the sectoral regulators may incorporate applicable regulations and rules. For digital currencies popularly known as "**cryptocurrenices**" are been prohibitive through traditional banking channels for the time being and RBI has framed a committee to understand its complete and detailed legal framework to prevent ponzi schemes and financial frauds.*

Fintech Regulators

*Reserve Bank of India ("**RBI**")- As regulator and supervision of payment systems, RBI has been playing the role as the catalyst/facilitator for innovations in payment systems. In order to ensure that regulations keep pace with the developments in technology impacting the payment space, the global developments in technology such as distributed ledgers, blockchain etc. will be monitored, and regulatory framework, as required will be put in place.*

*The Insurance Regulatory Development Authority ("**IRDA**")- Insurance is typically considered one of the functions within the financial services where the adoption of innovation has been the slowest. However, over the past decade, many innovative practices such as digital channels and process automation have been gradually adopted by many insurers. The rise of online aggregators and the potential entry of technology players could disaggregate the distribution of personal and small commercial policies.*

*Securities Exchange Board of India ("**SEBI**")- The evolution of Fintech in the financial markets, increasing the efficiency of trading systems, reducing overall cost of transactions & most importantly democratizing the reach of financial markets & increasing retail participation. SEBI being the financial market regulator, had made its best efforts to evolve with the changing technological landscapes. In the recent past one of the most pertinent innovations in financial sectors is the adoption of algorithmic & machine based trading. Additionally, tools like robot advisors in the investment advisory space are another innovation gathering speed in recent times. It has also been observed that market participants in other securities markets are exploring the usage of Blockchain or Distributed Database technology to provide various services such as clearing and settlement, trading etc.*

Cyber Security & Data Protection

Cyber Security is an issue that has been growing in importance with the advancements in technology.

With recent development of RBI guideline for storage of sensitive financial data to be stored in India along with Data Protection Bill 2018, which is to be enforce in the coming days has changed the regulatory landscape for Data Protection and Fintech in India.

Moreover, Section 43 A of the Information Technology Act, 2000, provides for the payment of compensation by a body corporate in case of negligence in implementing reasonable security practices and procedures in handling sensitive personal data or information resulting in wrongful loss to any person. In terms of Section 72A of the Information Technology Act, disclosure of information, knowingly and intentionally, without the consent of the person concerned and on breach of the lawful contract has been also made punishable with the imprisonment for a term extending to three years and fine. Hence, that data protection is generally governed by the contractual relationship between the parties and the parties are free to enter into contracts to determine their relationship defining the terms personal data, sensitive personal data, its dissemination, etc.

Classification of Customer/Data

The Fintech entities are heavily dependent on technology for each and every product they offer to their consumers. These entities may collect various personal and sensitive information about the customer and become the owners/custodians of such data. Therefore, the onus of data protection lies with these entities ranging from data preservation, storage, confidentiality, integrity and availability of the same, irrespective of whether the data is stored/in transit within themselves are with customers or with the third party vendors. The confidentiality of such custodial information should not be compromised at any situation and to this end, suitable systems and processes across the data/information lifecycle need to be put in place by the Fintech's. It becomes important to appropriately manage and provide protection within and outside organization borders/network taking into consideration how the data are stored, transmitted, processed, accessed and put to use within/outside the bank's network, and level of risk they are exposed to depending on the sensitivity of the data.

The Fintech entities should acquire industry quality management certifications facilitated by International Organization for Standardization (ISO)/ Payment Card Industry Security Standards Council, etc. as applicable.

Regulation of Payment Systems

Fintech powered business should ideally be undertaken by only regulated entities, e.g. banks and regulated payment system providers. The forms of business which can be undertaken by, say, a banking company are specified in Section 6 of the Banking Regulation Act, 1949 and no banking company can engage in any form of business other than those referred to in that section. This provision however also enables a banking company to do such other things which are incidental or conducive for the promotion or advancement of its business. Banking companies can therefrom from subsidiaries for undertaking any business which supports their main business. Subsidiaries can also be formed for undertaking such other business which RBI may, with the approval of the Central Government, consider to be conducive to spread banking in India or to be otherwise useful for necessary in the public interest (Section 19 (c) of the Banking regulation Act). These provisions give room for banking companies to undertake focused innovative Fintech business relevant to their operations, via a dedicated subsidiary, while remaining within legal framework of the Banking Regulation Act. However, as Fintech innovations are typically multiple-use, with significant applications beyond financial regulation, it may be inefficient and counterproductive to restrict core Fintech activities to only those entities and applications which are covered under financial regulation/supervisions.

The Payment and Settlement Systems Act, 2007 provides for authorisations, regulations and supervision or payments systems by RBI. A payment system is defined in the Payment and Settlement Systems Act, 2007 as a system that enables payment to be effected between a payer and a beneficiary, involving clearing, payment or settlement service or all of them, but does not include a stock exchange or clearing corporation set up under a stock exchange. It is further stated by way of an explanation that a "payment system" includes the systems enabling credit card operations, money transfer operations or similar operations. As the bulk of Fintech innovations do not amount to 'payment system' as defined under that Act, they will not fall under its regulatory framework.

Section 35 A of the Banking Regulation Act empowers the RBI to issue directions to banking companies in public interest and in the interest of banking policies, etc. RBI is also empowered under Section 36 of the Banking Regulation Act to caution or prohibit banking companies generally and generally to give advices to banking companies. As regards payment systems, Section 17 of the Payment and Settlement Systems Act,2007 gives RBI the power to issue directions to payment systems and systems participants. It may be possible for RBI to invoke these provisions in case of Fintech innovations used by these regulated entities require RBI intervention. However, there is scope for developing legal framework that's sets out the broad contours of what principles financial innovations should conform to.

Way Forward- Future Road Ahead

Faced with the profound changes that Fintech is bringing to the banking and financial sectors, regulators need to take care to avoid two pitfalls. The first is overprotecting incumbents by erecting barriers to entry for newcomers. Doing so would discourage financial innovation and stifle competition in the financial sector. The second potential pitfall is choosing instead to unduly favour newcomers by regulating them less stringently than incumbents, in the name of fostering competition. Regulators have a difficult role to play as their decisions have both a direct and indirect impact on competition between incumbent firms and newcomers. They have to provide a level playing field for all participants, but at the same time foster an innovative, secure and competitive financial market. Under present, applicable laws, the banks are not obligated to open to all Payment Service Providers (PSPs) for authorised payment systems.

This has led to situation where access to payment systems by new non-bank payments services providers, including Fintech firms, is restricted. Most of them can access payment systems only through the banks, which are also their competitors in the payments service industry which has restricted fast-paced expansion of digital payments in India by hindering competition from technology firms. Fintech companies that require to connect to banking systems to serve their customers tend to face restrictive practices. This anti-competitive setting may not be conducive for innovation and consumer interest. Regulators should foster healthy competition between players, regardless of whether they offer conventional approaches or use new technological solutions along with Regulators must act in the interests of end consumers, protecting them in a changing environment that pose new, unanticipated risks.

Banks / Traditional FIs

Advantages

- Large asset base
- Availability of cheap funds
- Perceived stability and trust
- Large customer base
- Brick and mortar presence
- Experience in risk management
- Links to government and regulators

Disadvantages

- Poorly designed for innovation
- Legacy products and systems
- Slow decision making
- Low customer-centricity
- Distributed attention across products
- High cost structures

Collaboration

- Access to customers and markets
- Access to data to test concepts
- Funding
- Understanding of key pain points
- Branding and trust
- Distribution channels
- Risk management expertise

- Low-cost, ad-hoc tech solutions
- Association with young, modern industry and high quality tech talent
- Nimble solutions to key challenges
- Customer-centric, solutions based approach
- Tailored products for segmented markets
- On-boarding new (younger) customers

Fintech companies

Disadvantages

- Limited and expensive funding
- Limited offerings
- Lack of trust/brand recognition
- Small customer base
- Lack of physical presence
- Limited experience in risk management
- Limited exposure to regulatory compliance

Advantages

- Innovation-focussed
- Nimble and responsive
- Customer centric
- Specialised offerings
- Latest digital technology, improved algorithms
- High quality tech talent and creative thinking

The use of technology has been of great help for increasing the reach of the financial services and has also facilitated the ease of doing business. Regulators in India open to considering all these FinTech options and facilitating the same, so long as these serve to subserve their regulatory mandate without compromising on the risk associated with such innovations. It's the Financial Regulator's responsibility to assess the product and its implications for stakeholder, and how to monitor its use.

Regulatory Sandbox- A new approach to evaluate Fintech

Live or virtual testing of new products or services in a (controlled) testing environment, with or without any 'regulatory relief' is termed a 'sandbox'. The testing environment could be available to regulated or unregulated firms, or both. Regulator provides the appropriate regulatory support by relaxing specific legal and regulatory requirement, which the sandbox entity will otherwise be subject to, for the duration of the sandbox. A regulatory sandbox can be used to carve out a safe and conducive space to experiment with Fintech solutions, where the consequences of failure can be contained.

Sandbox should help to encourage more Fintech experimentation within a well defined space and duration where regulators will provide the requisite regulatory support, so as to increased efficiency, manage risks better and create new opportunities for consumers. The proposed financial services to be launched under the sandbox should include new or emerging technology, or use existing technology in an innovative way. The proposed financial service should address a problem, or bring benefits to consumers or the industry.

While innovative player and new technologies are entering the financial industry with impressive rapidity, regulation should not aim for an artificial separation between Fintech's on the one hand and traditional banking on the other. Competition can have a positive impact on integrity in the sector, because customer offered with more options-demand more transparency and integrity.

The key risks emerging across various Fintech are as under:

- *The potential increase of profitability/solvency risk, and of multiple aspects of operational risk (both systematic and idiosyncratic elements).*
- *While incumbent bank's business models are already under pressure in the current low interest rates environment and with more stringent regulations, additional challenges are posed by the Fintech developments.*
- *With the rise of Fintech, IT interdependencies between market players (banks, Fintech and others) and market infrastructures are growing, which increases the potential for an IT risk event at a significant market player to escalate into a wider systematic event.*
- *Additionally, within individual banks, the complexity surrounding the delivery of financial services is expected to increase, making it more difficult to manage and control operational risk.*

Pre-Emptive Actions for hassle free Doing Business of Fintech in India

Obtain the necessary licenses for your fintech Business Model	↳*Check if you qualify for any applicable approvals from the sector specific regulators such as RBI, SEBI, IRDA etc.* ↳*Take steps to make sure your Fintech business meet the necessary requirements to apply for the licenses/approvals, if any.* ↳*If the licenses are too difficult to obtain, then explore partnerships with partners who already have licenses*
Make sure that you are compliant with applicable regulations which includes but not limited to collection of the right information to conduct sufficient KYC procedures, data privacy, anti-money laundering regulations, sectoral regulators guidelines issued from time to time etc.	↳*Determine your Fintech business model's risk of money laundering, ponzi schemes and any other illegal activity.* ↳*If your risk is low, do a simplified customer due diligence.* ↳*If your risk is high, do enhanced due diligence.* ↳*Obtain consent of individuals for collection & use of their personal data.* ↳*Implement a cyber security system to prevent any wrongful loss/theft of personal data stored.* ↳*Keep yourself abreast with latest guidelines, regulations and ever evolving legal framework in Fintech, as any failure to comply may prove to be fatal.*

The emerging and existing guidelines on Fintech's has been evolved on the following principles:

a. *Streamlining the existing regulatory reporting structure across the value chain*
b. *Risk and compliance monitoring*
c. *Protecting Customer interest*
d. *Detecting Financial Crimes*

For legal and regulatory updates on Fintech and further discussion or any clarification, please connect with us at** admin@equicorplegal.com / **08448824659

TIME FOR LEGAL EXPERT?

Let the Professionals at EquiCorp Associates take over the matter

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