

Regulatory Sandbox joins other regulatory initiatives and brings optimism to fintechs in Brazil

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Despite the turbulent year, a major movement of regulatory and infrastructure updates planned for 2020 is following its course

* The portuguese version of this article can be found at FEBRABAN's Noomis platform in the link: <https://bit.ly/bdnoomis6>

Over the past 7 years in Brazil, we have witnessed the evolution of the financial market rules in order to expand inclusion, democratize the mechanisms of access to capital and increase competition in the sector - opening space and enabling the activities of new players. Norms were then updated and created, bringing greater legal certainty and expanding the operating conditions of payment institutions, equity crowdfunding platforms and digital credit platforms.

In this movement, some public consultation (call for input) processes were carried out, with counted on the active participation of different stakeholders, in addition to the creation of several working groups and discussion forums involving the presence of regulators and some governmental entities. Among these working groups, there was the launch of the Fintech WG of the Financial Innovation Laboratory (LAB) in December 2017 - a multisectoral interaction forum created by the Brazilian Development Association (ABDE), the Inter-American Development Bank (IDB) and the Brazilian SEC (CVM).

In the period between 2018 and 2020, the Fintech WG dedicated itself, among other themes, to study, discuss and design what would become the basis of CVM's Regulatory Sandbox. I was present in the group throughout these years on behalf of the Brazilian Startup Association, and I was able to witness the advances that occurred in the formatting of the rules of this important experimental regulatory environment, which were published on May 15 through CVM 626 Instruction.

Generally speaking, a Regulatory Sandbox basically allows new startups to test their innovative products, services, business models and delivery mechanisms in the real market, with a restrict number of real consumers, on a trial basis. During a certain period (test phase) the regulator watches and monitors the fintech development and its potential impact on the market. In the end of the period the Fintech can be authorized or not to go live to the broad market, and new regulatory precedents are created upon this experience.

There was a lot of expectation among the fintechs for 2020, a year in which topics such as open banking, instant payments and the Regulatory Sandbox itself were expected to effectively start - after an intense period of previous discussions. With the arrival of the pandemic and the impending global economic crisis, it was questioned whether such steps would still take place within the expected timeframe. However, even within this stress scenario, we see the progress of the agendas related to innovation in the financial segment happening on schedule, bringing hope to innovators in the sector.

The maintenance of these agendas as priorities for the local regulators reinforces their commitment with modernization, and shows that the country is in line with the regulatory innovation movement that is happening in the main global hubs, continuing its implementation, despite the adversities.

About CVM Regulatory Sandbox

CVM's (Brazilian SEC) Regulatory Sandbox is the second to have its operating rules established in the country. The first was Susep's (Insurance market regulator) Sandbox, which had its announcement published on March 20th this year, and the next will be Central Bank's, probably with publication in the coming months.

Unlike the United Kingdom, which has only one Regulatory Sandbox (instituted by the Financial Conduct Authority - FCA) for experimenting new projects in different segments of the financial market. Here in Brazil we will have three different sandboxes, one for each Regulator (Susep, CVM and the Central Bank) dealing with projects aligned with the segment it supervises. According to the regulators, mechanisms will be created to contemplate projects that are within the competence of more than one authority, which would lead to interaction with multiple sandboxes.

Returning to the CVM Sandbox, the final published version had some good surprises incorporated in its text that were not present in the draft placed for public consultation. Among them, I highlight the following (with my comments):

- Replacing the dynamics of sandbox cycles (batches) with participant admission processes, so that it is not necessary to completely end a cycle before new participants can join the sandbox.

Comment: Unlike the British model, which operates with two closed batches of six months each within the year, the CVM model will apparently be more flexible and continuous.

- Inclusion of a preliminary analysis phase of the proposals received to identify any formal defects, giving the proponent the opportunity to present new information or clarifications.

Comment: Good practice that will give fintechs one more chance to detail its solution if any point is not clear after submitting the project to the regulator.

- The participation of foreign legal entities can happen as long as there is a partnership in place with competent regulatory authorities of the jurisdictions in which they are based, and foreign candidates will be evaluated according to the same eligibility, selection and prioritization criteria valid for Brazilian applicants.

Comment: Decision that seems to set a precedent for the practical implementation of agreements such as the one the CVM maintains with a network called GFIN (Global Financial Innovation Network) - a project led by the FCA that has regulators from all over the world and has the objective of creating a Global Regulatory Sandbox, cooperative and interoperable.

- Receipt and analysis of proposals arising from admission processes of other regulatory bodies, even though the deadline defined by the CVM for registration has already ended.

Comment: Inclusion of a possibility that seems to address projects that need interaction with more than one regulator (multiple sandboxes).

- Possibility of submitting a reasoned request, during the period of participation, expanding or altering the regulatory exemptions granted, or reviewing the conditions, limits and safeguards established.

Comment: During the discussions at the LAB (and in the public consultation) we questioned, via ABStartups (the Brazilian Startups Association), how cases of “pivoting” of a startup within the Sandbox could be handled, that is, cases in which the project is modified and ends up following a different course from the one initially proposed. I understand that this section helps to resolve this issue and gives the startup greater flexibility during the process.

- Creation of a section on the CVM page dedicated to the periodic disclosure of information regarding the progress of the Regulatory Sandbox, such as a description of the innovative business models being tested, frequently asked questions and statistics on proposals received, approved and rejected.

Comment: Initiative that gives transparency to the whole process and is in line with good practices followed by the FCA in the United Kingdom, for example.

Next Steps

CVM Instruction 626 came into force on June 1st this year. Subsequently, there should be the publication of a specific ordinance on this topic. The expectation is that there will be the opening of a public notice for the receipt of projects in the second semester (thinking more conservatively, possibly closer to the end of the year) and effective functioning of the Sandbox happening in the beginning of 2021.

A new scenario for the Brazilian capital market is being designed with this initiative, which is added to other important innovation initiatives (such as the local instant payments - PIX - and the open banking) that will change the country's financial scenario.

The current period is stormy and the waters are turbulent, but it is clear that, soon, we will be on a fertile land for financial innovation in Brazil.

About Bruno Diniz



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