

Five legal trends driving FinTech success

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“FinTech” is shorthand for a wide variety of technologies and companies designed to increase efficiency in the financial sector. Many FinTech businesses (FinTechs) have little in common other than that they seek to apply technological innovation to the financial sector. They include the following:

- start-up and high-growth companies that seek to compete with industry incumbents, in many cases by carving out particular services (e.g., wire transfers and investment management services) out of incumbents’ broader service offerings and in the process providing attractive product features or reduced costs (or both)
- technologically innovative companies that complement and provide services to incumbent industry players by providing augmented services (e.g., chatbots) or are able to expand the incumbent’s reach to new customer populations (e.g., small business services providers and youth-focused app or points providers)
- large technology providers that enhance existing financial service platforms, such as improving trading platforms by incorporating artificial intelligence techniques or enhancing the scalability of platforms using cloud computing
- incumbent players themselves that recognize the need for rapid innovation and that either put in place internal efforts to innovate more quickly or innovate by acquiring products or services provided by the types of companies listed above or by acquiring the companies themselves

The broad range of business types that fall under the FinTech umbrella results in a wide variety of legal factors at play in the sector. In all jurisdictions, financial services are delivered within a web of significant regulatory requirements and business practices designed to reduce risk to customers and maintain the stability of the financial system. Living in a highly legalistic environment is a fact of life for FinTechs.

We have observed the following legal trends while advising some of Canada’s leading FinTech innovators:

- *The most successful FinTechs build legal compliance into their processes early in the formulation of their businesses.* This “compliance by design” approach focuses on the legal compliance risks at the time that the foundational business practices and technological systems are being developed and implemented. A wide variety of compliance requirements can have an impact, including increasingly strict privacy laws; securities law requirements for investment platforms and initial coin offerings (see our Osler colleagues’ blog post “[Failure](#)

to [Coin]Launch – Caution for crypto-asset consultants, advisers and service providers”); anti-terrorist financing and anti-money laundering laws (see our Osler Update on anti-money laundering rules for cryptocurrency dealers); and consumer protection laws and transparency in lending laws. In addition, FinTechs that plan to deal with banks and other financial institutions need to take into account the indirect application of banking regulatory oversight, which in Canada is the Office of the Superintendent of Financial Institutions (OSFI). FinTechs that only account for regulatory factors late in their business planning dramatically increase the risk that regulatory requirements will disrupt their business plans.

- *FinTechs need to have a clear vision of how data will be used in their business.* Data, particularly customer data, is a hugely valuable business asset. Use of data has also become an increasingly sensitive issue with consumers and regulators. Two key issues need to be considered: compliance with data privacy laws and the contractual frameworks required to allocate data rights. FinTechs should have a clear vision of whether they require data to be available across their customer base in order to support the development of technology applications (as is the case in many artificial intelligence applications) or for otherwise generating value (for example, by creating valuable deidentified or aggregated data sets). The desired result then needs to be set out in contracts between the parties exchanging data. Note that simply relying on ownership of data and licensing language treating data as if it is a form of intellectual property is generally not effective given that most data is not treated as property under current intellectual property laws.
- *Good cybersecurity practices are table stakes.* Thoroughly developed cybersecurity policies and practices are essential. This goes beyond simply having a privacy policy and complying with privacy requirements (although exposure to fines and regulatory interventions is increasing), but also involves having in place internal policies and practices that adopt recognized standards and tools to lock down the FinTechs’ data and systems to the extent possible. Appropriate training and breach protocols for when a breach does occur are equally important. Established participants that operate in a financial system that handles and trades in funds and other financial assets are on a constant quest to ensure that security breaches are eliminated and, where they are not, minimize the risk of actual loss by clear action plans. This same attitude needs to be in place among FinTech newcomers.
- *FinTechs need a well-thought-out customer contracting strategy.* The contracting approach can either facilitate business or become a significant impediment to revenue, whether FinTechs offer a consumer-facing application or a service that is provided to existing incumbent players in the financial system. FinTechs should develop standard customer-facing agreements with well-thought-out terms that protect their intellectual property, clearly describe their rights to data and privacy law compliance obligations, address any terms required by the FinTechs’ unique compliance environment, and allocate liability appropriately. Terms differ whether the application is a B2C (business to consumer) or B2B (business to business) offering. FinTechs that have polished template agreements typically have an easier time completing deals and articulating reasonable and consistent positions

related to legal terms. FinTechs should also establish a contracting process to streamline the review and negotiation of their customer contracts. Such processes typically include identifying a lead to co-ordinate the contract review (typically, a sales lead) and should involve internal stakeholders who are responsible for delivering on the key contractual issues (e.g., the FinTech's engineering team would arguably need to review and sign-off on a customer's requested changes to the service level availability or security requirements). Negotiations, which can take several months, can be reduced to several weeks with the right supporting processes.

- *Contracting with financial institutions (FIs) and other incumbents requires thorough preparation.* Where the customer is an incumbent FI, thinking through in advance the anticipated contracting requirements of such a customer is essential. FI incumbents are subject to significant compliance requirements and adopt practices to reduce the risk of loss to as near to zero as possible. FinTechs new to contracting with FIs can often be surprised by both the length and complexity of the required agreements. The process can also involve procurement processes that include completing lengthy and complicated questionnaires on data security practices. Having thoroughly thought through the issues mentioned above in this Update can make the difference between a relatively smooth contracting process and having to go back and reconsider fundamental business practices in order to meet the contract requirements of the FI. Does the FinTech clearly have compliance culture, and can it commit to those practices contractually? Has it clearly thought through its approach to data and can it clearly articulate the rights it needs in order to carry out the service for which it is contracting? If required to build its business, can it justify use and retention of data beyond what is strictly necessary to provide the contracted services? The agreement will be shaped by whether the FinTech is offering a complementary or partner service to the FI's customers (e.g., a new product not currently offered by the FI) or outsourcing a portion of the FI's business (which may be subject to the [OSFI B-10 Guideline](#)) or other similar regulatory requirements.

As their influence grows, FinTechs will require a sophisticated and thorough approach to the legal issues that are inherent when carrying out business in the financial sector. Regulators will respond to new business models, and FinTechs will continue to face one of the most dynamic and complex legal regimes of any sector.