ALLEN & OVERY

Fintech

2017

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“Offers expertise across the TMT sector, and handles mandates spanning multiple jurisdictions. Provides full coverage of key practice areas, including regulatory compliance, competition, litigation, M&A, outsourcing and financings. Notable activity in emerging areas such as financial technology, big data and cloud computing.”

Chambers Global 2015 (TMT: Global-wide)

“They are one of the best in terms of the quality of the work. They are very flexible, experienced and knowledgeable, and are proactive in putting forward solutions.”

Chambers Europe 2017 (Banking & Finance: Europe-wide)

“Ranked Tier 1 for Financial Services Regulatory: Non-contentious”

IFLR1000, UK, 2017

Fintech

Fintech describes the intersection between finance and technology.

Market participants may be providers of technological solutions which bring innovation to traditional financial services companies or they may be companies delivering innovative financial services offerings which disrupt the existing financial services market.

What unites Fintech players is the pursuit of new ideas and business models to bring digital transformation to all aspects of the heavily regulated financial services industry.

Today's Fintech market has been characterised by a period of significant growth. However it is also a crowded space in which participants need to have a clear competitive edge to survive. As the market matures survival or failure can increasingly be ascribed to success in certain key areas. These are:

- Getting regulatory compliance right;
- Making the right partnerships at the right time on the right terms; and
- Driving adoption by ensuring excellent user experience.

With a track record of providing high-quality and innovative legal advice, Allen & Overy is ideally placed to guide market participants through all business and legal issues in this thriving sector. As a recognised banking powerhouse we have a huge knowledge base and extensive experience of advising on financial services regulation. In addition, our strong connections with the leading financial services authorities mean we can support our clients in all their dealings with local regulators. We marry this regulatory expertise with deep and broad experience in the technology sector. We have advised on some of the cornerstone projects in the banking technology market and we also work with some of the most successful technology companies of the 21st century. From growth companies to established market players, we know what it takes to succeed in Fintech.

How technology is transforming finance

Payments

Banks, cards schemes and acquirers and payment processors are the traditional players in the payments landscape. New entrants focus on taking the "friction" out of the payments process and include providers of mobile payments, contactless and eWallets. Trends in this area include further developments with biometric identification and greater use of big data to halt fraudulent payments.

Insurance

One of the slower areas of Fintech to take off, "insurtech" is now gathering steam. Investment is being driven in particular by established insurers investing in new market entrants, and "hot" areas of technology include blockchain and smart contracts, data analytics and Internet of Things applications which can assist with risk identification and mitigation.

Investment management

Cloud and big data have already rung the changes in the investment management industry but a new shift has come with the application of machine learning and artificial intelligence – and thereby the arrival of the robo-adviser.

Fundraising

Crowdfunding (both equity and reward-based) has become an established part of the early stage company market, particularly for consumer facing companies for which engagement with investors is all part of the spectrum of engaging customers. Platform-based tech has also facilitated the rise of syndication of early stage investment, particularly in the angel market where a syndicate typically allows less experienced investors to co-invest with more established leads.

Process efficiencies

For many, Blockchain is the perfect example of the evolutionary power Fintech can have on process optimisation. But Regtech is another subsector of the process efficiencies market to receive significant investment and interest. Regtech applications look to save organisations time and money by automating processes to ensure regulatory compliance. They also offer the possibility of more accurate compliance efforts, and better reporting to supervisory authorities.

Deposits and lending

Peer-to-peer or marketplace lending is the most prominent example of the impact of Fintech on deposits and lending. This part of the market has matured to show a particular symbiosis between established players and new entrants, with P2P lenders, for example, picking up the portion of the SME lending market in which banks on the whole had preferred not to participate since the financial crisis. P2P lenders have turned to established institutions in other ways also, such as by pushing out parcels of loans to hedge funds and other institutional investors via their online marketplaces (something that has arguably given P2P platforms greater exposure to the credit cycle than the "pure" P2P model).

Legal and regulatory issues

Regulatory requirements

Regulatory compliance is fundamentally important to Fintech companies, and can be a key competitive advantage, but navigating the relevant regulatory regimes is a significant headache for many.

Most Fintech companies will have undertaken a detailed analysis of their business model against applicable financial regulation to fully understand what can be achieved without becoming a regulated entity, or, conversely, to help them seek appropriate licences or approvals. However attempts to map regulation can be complicated by the fact that it can be very hard to assess whether innovative new products fall within the regulatory regimes, and if they do, how the various requirements might apply. This problem is compounded for Fintechs scaling internationally, where different regulatory approaches in other jurisdictions can create additional hurdles (albeit the UK's "Fintech Bridges" initiative is one example of attempts to mitigate such problems).

Regulatory uncertainty makes business planning very difficult, and indeed the financial and compliance cost of regulation has been sufficient to see some new companies exit the market. A clear-sighted assessment of regulatory risk is fundamental to Fintech success.

Dealing with data

Data is central to the business models of many Fintechs, whether they are focusing on retail or investment banking. Companies that are able to derive business insights from financial services data can spot and maximise new opportunities and reduce risk. Unlocking this value is however dependent on far more than clever algorithms and exponential processing power. It is also essential that companies in this space build and maintain the trust of consumers and other stakeholders. As a result, concepts of security and transparency are essential industry principles in the Fintech sector – for both reputational and compliance reasons.

There is significant regulatory activity in this area. Aside from the obvious legislative changes affecting data handling and cybersecurity, such as the implementation of the new General Data Protection Regulation in Europe, a shift to open banking is a further complication on the data horizon. The new European Payment Services Directive (PSD2), the UK's recent retail banking market investigation from the Competition and Markets Authority and the promotion of data sharing by the Monetary Authority of Singapore are all examples of how regulators across the globe are focusing on data as a way to bring change to the traditional vertically integrated banking model.

Such changes require considerable sophistication from data owners and processors. In particular, there is a tension between the concept of open innovation as a route to bringing new players into the market, and the appetite for more control and ownership over data (as a valuable business asset). Intellectual property concerns, as well as privacy considerations, loom large here. The growth of new data handling models may also foster a "co-creation" environment in financial services where partnerships (eg JVs, strategic alliances etc) might be the optimum way to bring diverse parties together.

Protecting innovation

The development of innovative software and technology by Fintech companies has been critical to the rapid expansion in this sector. Legal protection for such innovation is integral to success in the Fintech sector, but the availability of protection varies from jurisdiction to jurisdiction. While business methods were previously thought to be patentable in the U.S. this has become increasingly difficult through recent case law. In Europe, meanwhile, they are per se unpatentable unless they can be shown to solve a 'technical problem'. Given these difficulties, Fintech companies must consider carefully the availability of other IP rights, such as copyright and trade secrets, as well as protecting themselves through contractual arrangements with their customers, employees, suppliers and/or other third parties.

A strategic challenge in areas such as blockchain is how to balance the protection of ideas and technology with the desire to encourage industry-wide adoption. Where there may be so-called "network effects" from new technology, the timing for seeking to register and/or enforce intellectual property rights is critical. Done too soon and the risk is that innovation is stifled, left too late and it is possible to be locked out of the market by peers and competitors.

The importance of intellectual property to Fintech companies may also make them a target for patent trolls, which may cause business disruption unless the Fintech enters into licensing discussions or is prepared to fight a claim in the courts.

Collaborating, investing and acquiring to bring innovation into the business

Many established financial institutions recognise the benefit that financial innovators are bringing to the market. Frequently financial institutions look to partner with emerging technology players to speed up the innovation cycle.

A fundamental question is what form that collaboration might take. The heat in the Fintech market is certainly driving M&A as companies buy in technology and skills or combine with peers to build scale, but commercial collaborations are also a popular route to achieving these goals. Equally, corporate venturing may offer a way to connect with early-stage companies to assess potential technologies, exert a degree of influence on the future direction of the emerging company and be in a good position to acquire or license technology if it looks to be shaping up well.

To make a success out of any of these transactions, both parties need to determine how to accommodate the objectives and needs of what may typically be two very different organisations. This relationship dynamic impacts deal negotiation, the due diligence process (including the all-important regulatory due diligence), and how the commercial aspects of the deal are structured.

Sources of funding

The environment for growth companies is changing. For a start, 2016 saw a slowdown in the number of IPOs that came to the market globally. Meanwhile, a rising number of private companies (and particularly "unicorns" – those with valuations of over USD1 billion) have successfully completed either more private funding rounds or larger private funding rounds (or both). This enables these companies to fund direct growth rather than capital investment from injections of cash from private investors.

The group of investors participating in late stage private company rounds has also expanded. This area is no longer solely the preserve of traditional venture capitalists; we are seeing sovereign wealth funds, asset managers and hedge funds, as well as corporate venture funds, participating in this section of the market. These investors are joining the market for reasons that range from straightforward portfolio diversification through to opportunities to spot and nurture emerging talent and innovation to build research pipelines.

With more companies staying private longer, and with a wider range of investors operating in this segment of the market, how do companies decide which funding option is right for them?
One key criteria is aligning the investor's timetable for exit with the company's growth plans. Another consideration will be planning for a liquidity event in the future – whatever funding options are considered now must not have the effect of making it harder to, for example, gain access to the public markets at a later date.

Ultimately, the challenge faced by all those in the Fintech market is how to capture innovation while preserving the stability of the banking network. Facebook's mantra, "Move fast and break things", is a great one for many emerging companies – but perhaps more problematic for companies operating in highly regulated areas such as financial services. Within the Allen & Overy team we have the unique combination of resources to help market participants successfully navigate this path.

Our experience

Worldpay
a leader in global payments, on its IPO.

Deutsche Börse Group
on its investment in Digital Asset Holdings, a venture-stage financial technology company developing blockchain technology to support recording and settling financial transactions.

Funding Circle
Goldman Sachs and Numis on the IPO of Funding Circle SME Income Fund (by way of a GBP150m placing and offer for subscription and placing programme).

Aegon
on the formation of a strategic partnership with Chytrý Honza, a leading Czech Fintech company.

Equiniti Group
Barclays Banks, Goldman Sachs, Credit Suisse and Liberum Capital on the IPO of Equiniti Group.

BACS and Faster Payments
the UK inter-bank payment systems, on their scheme rules, settlement arrangements, technology development and maintenance contracts for processing of payments in the UK.

VEON (fka VimpelCom)
on international laws applicable to mobile payment schemes.

Innovate Finance
the UK trade body for Fintech, on policy issues relating to KYC requirements.

Telenor, Telenor Financial Services and Telenor Myanmar
on the establishment of a mobile financial services provider in Myanmar by way of a joint venture with a local Myanmar bank.

National Bank of Abu Dhabi
on a service agreement with Oxigen Services (India) in relation to mobile banking services to be provided in India by Oxigen for NBAD customers.

Crédit Mutuel Arkéa
on its acquisition of an 86% stake in Leetchi.com, a France-based Fintech group providing a digital solution to collect money for group gifts and events and an API solution to accept online payments and manage e-money for marketplaces, crowdfunding and collaborative consumption (Mangopay).

BNP Paribas Fortis
on the development and roll-out of an innovative mobile payments platform in Belgium. The platform, which is a market-first, was developed together with Belgacom and Accenture.

"We get the wealth of experience the firm has accumulated over the years and the lawyers work well together between their various offices, so we receive a global and seamless service."

Chambers Europe 2016 (Banking & Finance: Europe-wide)

Network International
on the English and U.S. law aspects of its acquisition of a majority stake of TimesOfMoney, the Indian e-payment giant.

SunGard Data Systems Inc.
on the sale of its retail banking software business to Silverlake Axis, a leading provider of digital economy solutions and services, listed on the Singapore Stock Exchange.

Crélan
a Belgian bank, on the sale of Keytrade, its internet bank and broker, to Crédit Mutuel Arkéa, a French bank.

A financial institution
on data protection, intellectual property (including screen-scraping), commercial contract, and financial services regulatory advice in relation to its creation of an innovative banking software product.

A Dutch financial institution
on the negotiation of a software and services agreement with Murex, a global software solutions provider for the financial sector, and leading fintech player.

An international service provider
on an electronic KYC compliance tool.

Discovery Health
on two Fintech joint ventures concerning the integration of data-based technology platforms into its wellness insurance programmes with Sumitomo Life in Japan and Generali in Europe.

A global financial institution
on a loss of sensitive customer data, including advice on appropriate notifications to the data protection and industry regulators and on an internal investigation.

A retail bank
on commercial agreements, including with PayPal, and on exclusive branding and technology arrangements with a transport authority for adding ticketing functionality to payment cards.

Volkswagen Financial Services
on the acquisition of PayByPhone, the mobile cashless parking payments business, from PayPoint for GBP26.5m.

Financière des Paiements Electroniques (Compte-Nickel)
on the disposal of 95% of its share capital to BNP Paribas.

The NAGA Group AG ("NAGA")
on one of Europe's largest Fintech Series A investments in 2017 by FOSUN International, a leading Chinese investment group. Founded in August 2015, Hamburg-based NAGA's mission is to develop, market and grow disruptive applications in financial technology.

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"They are not the type of lawyers that explain risk and provide no solution. They provide us with input, guiding our decision-making and process."

Clients quoted in Chambers Global 2016
(TMT: Global-wide)

"They give you their review on trends, can give a steer in terms of what option to take and are always available: they tick all the boxes."

Clients quoted in Chambers Global 2015
(Banking & Finance: Europe-wide)

GLOBAL PRESENCE

Allen & Overy is an international legal practice with approximately 5,200 people, including some 530 partners, working in 44 offices worldwide. Allen & Overy LLP or an affiliated undertaking has an office in each of:

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