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TELEPHONIC CREDIT: THE NEXT GENERATION OF BRANCHLESS BANKING IN MEXICO

Tony Godfrey*

“Beam me up.”
—Captain James T. Kirk,
to Lieutenant Commander Montgomery “Scotty” Scott¹

FOR literally centuries now, humankind has been obsessed with transporting information and itself faster and across greater distances than ever before. From Pheidippies’s run at the Battle of Marathon in 490 B.C., to Samuel Morse’s telegraph in May of 1844, to the futuristic depiction of transporting individuals across space in *Star Trek* from the 1960s onwards, the trend and need continues to increase.

Today, that need has turned into a reality in some areas, which can have a profound effect on large swathes of people. No, this article is not about emojis², but banking.

I. FINANCIAL INCLUSION

In 2012, the World Bank published a first-of-its-kind global study on “global financial inclusion.”³ The novel data looked at 148 economies worldwide and found that, overall, 50 percent of the global population has an account at a formal financial institution.⁴ But this is not without its divisions. The study also found that much of this financial inclusion came from developed countries, where individuals reported an 89 percent

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1. *Star Trek: This Side of Paradise* (NBC television broadcast March 2, 1967), available at http://www.startrek.com/watch_episode/15eygMte2BDh (last visited Apr. 12, 2015).

2. Although it should be noted that, at least on Twitter, the prevalent emoticons have become more common than even the hyphen. See Rob Speer, *Emoji Are More Common Than Hyphens. Is Your Software Ready?*, LUMINOSO BLOG (Sept. 4, 2013), <http://blog.luminoso.com/2013/09/04/emoji-are-more-common-than-hyphens/>; see also EMOJITRACKER, <http://emojitracker.com> (last visited Apr. 12, 2015).

3. See Asli Demirguc-Kunt and Leora Klapper, *Measuring Financial Inclusion: The Global Findex Database*, intro. (The World Bank, Working Paper No. 6025, 2012), available at http://www-wds.worldbank.org/external/default/WDSContentServer/IW3P/IB/2012/04/19/000158349_20120419083611/Rendered/PDF/WPS6025.pdf.

4. *Id.*

use of formal financial institutions, compared to just 41 percent in the developing world.⁵ This equates to roughly 2.5 billion people globally that either do not use or do not have access to a formal financial institution, and thus the formal financial market.⁶

In Mexico, an estimated 30 million people, a quarter of the country's population, live in rural areas at least several hours from access to a formal financial institution.⁷ Of this large rural population only 9 percent has access to a formal bank account.⁸ This extremely low access to the formal financial system in rural areas means that only 25 percent of the Mexican population has "access to formal financial institutions."⁹ Compared to similarly situated developing economies such as Brazil, China, and Egypt, all of whom demonstrate financial inclusion of at least 40 percent, Mexico's 25 percent is astonishingly low.¹⁰ Even compared to its geographic region, without regards to size or economic growth, Mexico's 25 percent falls far below the average of 39 percent throughout the rest of Latin America and the Caribbean.¹¹

II. WHAT IS "ACCESS TO A FORMAL FINANCIAL INSTITUTION" AND WHY DOES IT MATTER?

The Mexican National Banking and Securities Commission (CNBV) has defined access to formal financial institutions as "the access and use of a financial product and service portfolio . . . under an adequate regulatory framework."¹² A key component of this definition, "use," generally focuses on financial services and products including "savings, loan, payment and risk management products."¹³ Basic financial services, such as savings, investment, insurance, and financing afford all persons, perhaps especially the poor and the rural, a number of advantages.¹⁴ Through

5. *Id.*

6. *Id.*

7. Martha Casanova, *Unlocking Barriers: Advances in Rural Mobile Banking in Mexico*, CONSULTATIVE GROUP TO ASSIST THE POOR (CGAP), (Aug. 20, 2012) <http://www.cgap.org/blog/unlocking-barriers-advances-rural-mobile-banking-mexico>.

8. Joanna Klimaski, *Cell Phones Can Help End Poverty, Remittance Expert Says*, FORDHAM U. (July 2012) http://legacy.fordham.edu/campus_resources/enewsroom/archives/archive_2477.asp.

9. LILIANA ROJAS-SUAREZ, ACCESS TO FINANCIAL SERVICES IN EMERGING POWERS: FACTS, OBSTACLES, AND POLICY IMPLICATIONS 8 (2010), available at <http://www.oecd.org/dev/pgd/45965165.pdf>.

10. *Id.*

11. Ximena Peña, *Determinants of Financial Inclusion in Mexico Based On the 2012 National Financial Inclusion Survey (ENIF) 3* (BBVA Research, Working Paper No. 14/15, 2014), available at https://www.bbvaesearch.com/wp-content/uploads/2014/06/WP_1415.pdf.

12. NAT'L BANKING AND SEC. COMM'N (CNBV), FINANCIAL INCLUSION REPORT, Table 1.1 (Dec. 2009), available at <http://www.cnbv.gob.mx/en/Inclusion/Documents/Reportes%20de%20IF/Financial%20Inclusion%20Report%201.pdf>.

13. Peña, *supra* note 11, at 3.

14. CHRISTOPHER SUTTON AND BETH JENKINS, THE ROLE OF THE FINANCIAL SERVICES SECTOR IN EXPANDING ECONOMIC OPPORTUNITY 6 (2007), available at http://www.hks.harvard.edu/m-rcbg/CSRI/publications/report_19_EO%20Finance%20Final.pdf.

risk management, savings, and proper management of assets, maximization of income can be achieved that “ultimately creat[es] paths out of poverty.”¹⁵ There are other, almost too obvious, benefits of access to financial institutions for individuals and small businesses, such as simply the ability to take out cash to make change for small business transactions.¹⁶

Access to financial institutions and services does not only benefit those currently without access, but the country as a whole. Mexican President Enrique Peña Nieto recently spoke about his push for financial reform to tackle this very issue to “reduce the size of the informal economy, foster investment and improve the efficiency and transparency of spending.”¹⁷ Formal financial institutions are in a unique position to provide this macro efficiency of spending by “tak[ing] advantage of economies of scale and scope in information, diversify[ing] risks, and facilitat[ing] economic transactions.”¹⁸ Additionally, Mexico’s tax base is particularly languid at just 10 percent of the country’s GDP.¹⁹ Increasing participation in the formal financial system will make more funds available to the government and lead to a *de facto* increase in its tax base.

III. ACCESS VERSUS USE

A. ACCESS

There is, of course, a wide range of explanations for the low access of Mexico’s population to formal financial institutions. The most obvious for those in rural communities is a lack of physical access to traditional financial institutions. As referenced above, many in rural areas are hours away from banks. Traveling to a branch not only takes a great deal of time, but also requires forsaking work hours to do so with the added cost of transportation itself.²⁰ In addition to the physical distance of branches, the Global Findex survey found that individuals were essentially barred from access to formal financial institutions because they did not have

15. *Id.*

16. Xavier Faz & Martha Casanova, *Vivid Profiles of Mobile Account Users in Rural Mexico*, CGAP (Sept. 10, 2013), <http://www.cgap.org/blog/vivid-profiles-mobile-account-users-rural-mexico>. Mario, one of the top users, is known in these parts as the ‘chicken boy.’ He cooks rotisserie chicken at home and sells it throughout the countryside around Santiago Nuyóo. For him too, cashless payments are important. ‘It’s very complicated to get change. And now [that customers have mobile accounts] they can make mobile payments, we no longer worry about finding change.’ *Id.*

17. Enrique Peña Nieto, *Our Reform Programme Will Build a Better Future for Mexico*, FIN. TIMES (Aug. 20, 2014, 5:28 PM), <http://www.ft.com/intl/cms/s/0/86196824-285c-11e4-9ea9-00144feabdc0.html#axzz3TrwqRRb>.

18. Manuel Sánchez, *Mexico’s Banking System—Opportunities from Reform*, Address Before the BNP Paribas Economic Forum (Mar. 4, 2014), available at <http://www.bis.org/review/r140305b.pdf>.

19. Andres Sada, *Explainer: Mexico’s 2013 Reforms*, AMERICAS SOCIETY (AS) / COUNCIL OF THE AMERICAS (COA) (Dec. 17, 2013), <http://www.as-coa.org/articles/explainer-mexicos-2013-reforms>.

20. See Faz & Casanova, *supra* note 16.

enough money to maintain an account, the services were too expensive (such as withdrawal charges and balance fees), and many lacked required documents (such as extensive identification requirements).²¹

Mexico, however, has gone to great lengths to enable transporters to beam potential users of the formal financial system past these barriers. As recently as 2009, Mexico, through CNBV and several private bank partnerships, embarked on a serious overhaul of its banking system to address these barriers to inclusion in the formal financial system. First, CNBV adopted new regulations to allow for “branchless banking,” allowing certified banks to adopt a bank agency model in 2009. From 1993 to 2008, CNBV regulations barred banks from using third party agents, such as retailers, from providing financial services.²² But in 2009, a change in law allowed the formal use of third-party agents to provide limited financial services to low-risk clients.²³ This law severely limited the services provided by third-party agents, and subjected them to governmental oversight to manage risk; but, it nonetheless, worked to break down the geographic barrier to the formal financial system.²⁴ By 2010, just one year after the change in law and regulation, twelve banks operating in Mexico had established 9,000 agents to service previously unserved municipalities.²⁵ Eighteen percent of these municipalities were only served by third-party agents and thus, prior to the regulatory change, had no access to the formal financial system.²⁶

Mexico also further eroded the geographic barrier, as well as the cost of financial services and the need for extensive documentation to access the formal financial system with a unique initiative through its state-operated telecoms company, TELECOMM-Telégrafos, and the country’s third largest bank, Banorte.²⁷

The program began in January 2012 as a pilot initiative in the state of Oaxaca, known as “MiFon.”²⁸ MiFon sought to leverage TELECOMM-

21. Demirguc-Kunt & Leora Klapper, *supra* note 3, at 2.

22. *CNBV Basic Banking Circular*, Chapter XI, Article 317 available at <http://www.cnbv.gob.mx/Normatividad/Disposiciones%20de%20carácter%20general%20aplicables%20a%20las%20instituciones%20de%20crédito.pdf> (last visited Apr. 12, 2015).

23. *Ley de Instituciones de Crédito*, [LIC] [Credit Institutions Law], as amended, *Diario Oficial de la Federación* [DO], May 25, 2010, Art. 92 (Mex.), available at <http://www.inegi.org.mx/est/contenidos/proyectos/aspectosmetodologicos/clasificadoresycatalogos/doc/federal/LDIDC.pdf>.

24. *See id.*

25. ALLIANCE FOR FIN. INCLUSION (AFI), *AGENT BANKING IN LATIN AMERICA*, 4 (2012), available at http://www.afi-global.org/sites/default/files/discussion_paper_-_agent_banking_latam_america.pdf.

26. *See id.* at 5.

27. Javier Alonso, *Mobile Banking in Mexico as a Mechanism for Financial Inclusion: Recent Developments and a Closer Look into the Potential Market* 32 (BBVA Research Working Paper No. 13/20, 2013), available at <http://www.rrojasdatabank.info/mobilebanking4.pdf>.

28. *Id.* at 2; José Maria San Juan and Alessandra Valenti, *TELECOMM-Telégrafos: Connecting the Disconnected Rural Population*, 2 (Inst. for Bus. in the Global Context (IBGC) Working Paper 13-04, 2013) available at <http://fletcher.tufts.edu/~lme>

Telégrafos's mobile telephone infrastructure to provide digital payment and other account services via SMS technologies.²⁹ This was accomplished by providing adults in the area of Santiago Nuyoo free mobile phones and debit cards to conduct mobile-to-mobile payments and deposits.³⁰ Prior to the initiative, the residents of Santiago Nuyoo had to travel at least two hours to get access to cell phone coverage and a bank branch.³¹ The pilot has been labeled an unmitigated success, with 80 percent of phone recipients opening bank accounts, and saving users between 32 and 192 pesos a month in transportation costs.³²

Concurrently with this pilot program, Mexico's CNBV established a groundbreaking tiered "know-your-customer" requirement that alleviated the documentation demands for opening new accounts for small businesses and individuals.³³ This new regulation established four account tiers with varying requirements: (1) anonymous accounts for which no client data is needed, but caps the monthly deposits at \$280, a maximum balance of \$373, and does not allow money transfers except cash withdrawals; (2) named accounts where clients must self-report their name, date of birth, and address, and monthly deposits are limited to \$1,160; (3) fully documented accounts that require hard copies of identifying information, although the copies need not be kept by the financial institution, and accounts are capped at \$3,860; and (4) full-fledged bank accounts that require face-to-face opening at a branch, hard copies of identifying information, those copies to be kept on file by the institution and filed with the CNBV, and there are no limits to the account.³⁴ These reforms have significantly reduced the barriers of access to clients. Additionally, the costs of conducting business with lower volume clients have decreased dramatically for financial institutions, as evidenced by the pilot program in Santiago Nuyoo, where Banorte saw a 36 percent reduction in the cost of opening and maintaining accounts.³⁵

B. USE

But what good is a transporter if you do not go anywhere with it? Globally, while 36 percent of individuals report saving money, 29 percent

dia/Fletcher/Microsites/Cost%20of%20Cash/IBGC%20WP13-04%20Telecomm.pdf.

29. Alonso, *supra* note 28, at 32; *Mobile Money Explained: Insight from TELECOMM-Telégrafos on New Mobile Money Pilot in Mexico with Banorte, Banamex, and REV*, MOBILE MONEY GATEWAY (last accessed March 8, 2015) <http://www.mobile-money-gateway.com/sites/default/files/Mobile%20Money%20Explained%20interview%20from%20Telecomm%20Telegrafos.pdf>.

30. San Juan & Valenti, *supra* note 29, at 2.

31. *Id.*

32. *Id.* at 3.

33. THE WORLD BANK, MEXICO: NEW TECHNOLOGY-ENABLED CHANNELS TO SCALE UP FINANCIAL ACCESS, 13 - 14 (2013), available at <https://openknowledge.worldbank.org/bitstream/handle/10986/16746/831370FSAP0Mx00ess0379884B00PUBLIC0.txt?sequence=2>.

34. *Id.* at 13-14.

35. San Juan & Valenti, *supra* note 29, at 2.

did so informally.³⁶ As one author put it, “presumably they put the money under the mattress or used it to buy jewelry.”³⁷ Rather than a crass comment on the plight of the poor, this highlights the innate insecurity of operating outside of the formal financial system.

While Mexico has gone to great lengths to increase access to formal financial systems, recent data indicates that those transporters provided by the MiFon pilot program are not being used to their full extent either. Since the regulatory changes allowing for banking agents to spread across the country, agents and the extension banking access points have increased by 59 percent.³⁸ Despite this increase in access, even with banking via telephone, 28 percent of potential Mexican users of the formal financial system continue to use exclusively the mattress money-saving method.³⁹ Since the increase in access, just above 35 percent of the Mexican population has formal bank accounts; however, even half of those confirmed clients use the mattress money-saving method at least in part.⁴⁰

IV. MEXICAN REFORMS TO PROMOTE USE

Thanks to financial reforms and improvements in infrastructure, a much greater percentage of the Mexican population has access to transporters beaming them past access barriers to formal financial institutions, but more are in-store under President Nieto to provide a destination and use of those systems. On December 2, 2012, leadership from Mexico’s three main parties signed the “Pact for Mexico,” which outlined an unprecedented political agreement to achieve ninety-five agreed upon measures.⁴¹ Measures sixty-two and sixty-three focus on comprehensive reform of the financial system to strengthen the Mexican central bank’s ability to extend credit, and amend the legal framework surrounding private institutional lending to provide firmer safeguards and encourage lending.⁴²

On January 9, 2014, President Nieto signed into law a comprehensive fiscal reform package aimed at achieving those two provisions of the tri-

36. J.P., *Banking in the Developing World: The Poor are Different*, *ECONOMIST* (Apr. 20, 2012), <http://www.economist.com/blogs/feastandfamine/2012/04/banking-developing-world>.

37. *Id.*

38. COMISIÓN NACIONAL BANCARIA Y DE VALORES [NATIONAL BANKING AND SECURITIES] & AFI FIN. INCLUSION DATA WORKING GROUP, *USING DATA FOR IMPROVING PUBLIC POLICIES—THE CASE OF BANKING AGENTS AND MOBILE PAYMENTS 3* (2014), available at http://www.gpfi.org/sites/default/files/documents/The%20Use%20of%20Financial%20Inclusion%20Data%20Country%20Case%20Study_Mexico.pdf.

39. *Id.* at 5.

40. *Id.*

41. See generally PACTO POR MÉXICO [PACT FOR MEXICO] (2012), available at <http://pactopormexico.org/PACTO-POR-MEXICO-25.pdf>.

42. *Id.* at 30.

lateral pact.⁴³ The package altogether consisted of thirteen bills that amended, rescinded, or added to thirty-four separate laws and regulations.⁴⁴ Through the extensive legislation, President Nieto hopes to achieve four goals: (1) promote extensions of credit through the development banks that focus on small and medium businesses;⁴⁵ (2) increase competition in the financial sector; (3) increase availability of credit in the private banking sector; and (4) increase stability of the financial market.⁴⁶ Prior to the reform package Mexican lending accounted for 26 percent of Mexico's GDP, compared to the average in Latin America where lending accounts for 50 percent of GDP, or Chile, which has a 100 percent ratio of lending to GDP.⁴⁷ The reform package first eases capital retention restrictions on the development banks to allow for increased lending to small and medium businesses.⁴⁸ Secondly, the package makes a number of changes to regulation of private banks, prohibiting financial services that are predicated on a customer staying with a particular bank to ease transition from one institution to another and making available to the public in an accessible format the various services and interest rates offered by different institutions.⁴⁹ Third, the package amends existing bankruptcy laws, making it easier for lenders to go after the assets of defaulting borrowers.⁵⁰ In this way, institutions are granted greater security in lending to previously risky projects and customers. Finally, the package, through a number of measures, creates a new regulatory body to oversee the stability of banks operating in Mexico through consistent audits and stress tests.⁵¹

The most immediate impact on new entrants to the formal financial system will most likely be the loosened restrictions on the development

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43. Georgina Olson, *Peña Nieto Promulga La Reforma Financiera [Peña Nieto Promulgates Financial Reform]*, EXCELSIOR (Jan. 9, 2014), available at <http://www.excelsior.com.mx/nacional/2014/01/09/937425>.
44. Decreto por el que Se Reforman, Adicionan y Derogan Diversas Disposiciones en Materia Financiera y Se Expide la Ley para Regular las Agrupaciones Financieras [Decree to Amend, Supplement and Repeal Certain Provisions in Financial Matters and Expedition of the Law to Regulate Financial Institutions], Diario Oficial de la Federacion [DO], 9 de Enero de 2014 (Mex.), available at http://www.presidencia.gob.mx/wp-content/themes/presidencia/assets/frontend/other/reforma_financiera.pdf.
45. *Description of the Development Banking Sector*, COMISION NACIONAL BANCARIA Y DE VALORES [Nat'l Banking and Securities Commission], <http://www.cnbv.gob.mx/en/Supervised-Entities/Development-Banks/Paginas/Development-Banks.aspx> (last updated Oct. 25, 2013).
46. *Peña Nieto Unveils Package to Reform Mexico's Financial Sector*, BUS. MEXICO ONLINE (May 9, 2013), <http://business-mexico-online.com/pena-nieto-unveils-package-to-reform-mexico's-financial-sector/>.
47. Dr. Luis Videgaray Caso, Palabras Del Secretario de Hacienda y Credito Publico [Words from the Secretary of Finance and Public Credit] Presenting on the Financial Reform Initiatives 1 (May 8, 2013), available at http://www.hacienda.gob.mx/SALAPRENSA/doc_discurso_funcionarios/secretarioSHCP/2013/lvc_reforma_financiera_08052013.pdf.
48. *Id.* at 2.
49. *Id.* at 4.
50. *Id.* at 5.
51. *Id.*

banks. The Global Findex survey indicates that the few banking services used in the developing world are focused on personal use—namely family emergencies, tuitions, and home construction.⁵² By more easily opening the market to small and medium businesses, the development banking system in Mexico will have the ability to offer more comprehensive business development to the previously underserved or unserved.

Finally, not only is Mexico on track to increase access to the formal financial system, but provide a wide range of services and risk management beyond monthly deposits and cash withdrawals. Thanks to initiatives like MiFon, much of this will be done through banking agents and mobile SMS technologies.

Beam the economy up, President Nieto.

52. J.P., *supra* note 37.