

DRAFT
April 18, 2019

Emerging Payments Task Force
Conference of State Bank Supervisors
1129 20th Street, 9th Floor
Washington, DC 20036

Re: CSBS Models State Payments Law RFI

Dear Emerging Payments Task Force:

The Electronic Transactions Association (“ETA”) appreciates the opportunity to provide comments on behalf of the payments and FinTech industry. ETA encourages states to work together to harmonize requirements for money transmitters and urges all system participants including regulators, policymakers, and money transmitters to move towards a regulatory framework that can promote innovation rather than hamper it. The regulatory framework must allow for innovation and changing expectations of consumers brought on by technology while protecting consumers, providing stability of transactions, and guarding against fraud. Furthermore, ETA encourages CSBS to coordinate with all parts of the policymaking system including legislative bodies and regulatory agencies at the state and federal level to ensure more expedient state adoption of a harmonized money transmitter regulatory framework.

ETA is the leading trade association for the payments industry, representing over 500 companies that offer electronic transaction processing products and services. ETA’s members include financial institutions, mobile payment service providers, mobile wallet providers, and non-bank online lenders that make commercial loans, primarily to small businesses, either directly or in partnership with other lenders. ETA member companies are creating innovative offerings in financial services, revolutionizing the way commerce is conducted with safe, convenient, and rewarding payment solutions and lending alternatives.

Money Transmission Activities & Exemptions

Overview

Money transmitters provide critical services for a large section of the United States population including consumers and small businesses. The services provided by money transmitters help underserved and underbanked consumers have access to financial services through a variety of products including peer-to-peer payments, bill payment services, and mobile wallets.

Technology is changing customers expectations of financial services and companies are looking for the best way to provide those services in all 50 states. However, the current patchwork of state laws, regulations, guidance, and regulatory expectations limits innovation and provides a significant obstacle for both incumbents and new entrants into the market.

Despite many similarities of state money transmission laws, each state defines and interprets money transmission and its exemptions differently. As a result, a significant amount of time and money is spent by stakeholders interpreting how money transmission is defined. These costs - in the form of additional financial spend or in some cases the inability to provide certain services in some states - are ultimately borne by consumers. Uniform adoption of exemptions and definitions across 50 states can help to provide clarity for industry participants and alleviate regulatory burdens.

When looking for guidance regarding standard language, an already adopted definition of money transmitter and accounting framework is available in the Uniform Money Services Act, which has been adopted in large part in certain states.

Agent of the Payee

ETA supports the conclusions of the FinTech Industry Advisory Panel which recommend that the Agent of the Payee exemption be recognized and harmonized across states. The states' disparate views on the "Agent of Payee" exemption has resulted in significant efforts in both time and resources spent working with state regulators and legislators on changes and clarifications.

An Agent of Payee exemption should be adopted in each state because it is consistent with the goals of state money transmission frameworks. State Money Transmission licensure at its core was created to protect the consumers of each respective state. There is no need for consumer protection-focused regulation to apply where there is no likelihood of consumer harm or risk of loss. Accordingly, when determining whether to require a company to obtain a money transmission license, the appropriate question to ask is whether there is material risk of consumer harm. As many regulators have consistently recognized, there is no risk of loss in cases where all consumer obligations are discharged upon receipt of funds by an agent of the payee. Derived from the common law of agency present across the United States, this "Agent of Payee" exemption recognizes that there is no need to apply a consumer-focused regulatory framework to situations where a seller of goods and services has appointed a third-party agent to collect money on its behalf and has agreed that agent has all authority to bind it as the principle. This Agent of Payee structure discharges all obligations on the buyer upon the agent's receipt of funds and protects consumers from any risk of loss the money transmission framework was intended to prevent. This fundamental principle does not change even when the number of merchants or submerchants increase, nor when the types of goods or services sold increase.

In order to allow entities operating in the increasingly important inter-state and international spaces to offer services to customers in all states, it is important not just that each state recognize the Agent of Payee exemption, but that each state similarly define and interpret. An increasing number of states are or have considered limiting the applicability of Agent of Payee to specific industries, prescribed contractual language, limited geographies, and more.¹ However, considering agency

¹ See e.g., Washington regulatory guidance December 2016, limiting it to cases outside the marijuana context, BSA-regulated clearance and settlement systems, and requiring certain timing for funds disbursement between agent and payee; Pennsylvania limiting applicability in the case of non-profit organizations and requiring 7 specific contractual provisions; Kansas, limiting

law and that the objective of Agent of Payee is to prevent regulatory resources from being expended where there is no risk of customer harm, acceptable payment models for the Agent of Payee exemption can include payment processing for any services or offerings when the payment recipient is acting as an agent of a merchant. That includes instances of multiple entities serving as simultaneous agent of the merchant. Under accepted principles of agency law, sub-agents and co-agents can represent the principal in the same manner as the original agent.² Agency law applied to parties involved with money transmission dictates that payments made to a sub-agent/co-agent satisfy the payor's obligation to the payee as if the payment was made directly to the principal – in other words, making a payment to one counts as a payment to all. Just as the payee and the agent collapse into a single party in the transaction (agent stands in the shoes of the principle), so too do co-agents and sub-agents collapse into one. Moreover, an agent-of-payee exemption commensurate to the bounds of agency law does not detract from the goals of a licensure law because consumer protection concerns are satisfied when the consumer's debt is extinguished upon payment to the agent(s).

Given the importance of providing a clear roadmap for industry and the regulators ETA recommends that exemptions for Agent of the Payee be provided through statute, however, if state legislatures are not willing to harmonize their laws, regulators could provide written guidance that makes explicitly clear that agent of the payee exemption be adopted and done so in a uniform fashion across states.

Payment processing

Currently, payment processors must lean on various exemptions, whether established by law or by regulatory interpretation, including, but not limited to exemptions of agents of banks, agents of payees, payment processors, and operators of a payment system. This is not a system that is appropriate for a modern, competitive, innovative, and nationally operating ecosystem. In the interest of clarity and harmonization is imperative that states provide for a specific payment processing exemption from money transmission licensure.

This sentiment is succinctly stated by the FinTech Industry Advisory Panel when they stated. "...one area where all the states may be able to clarify a uniform position based on the existing regulatory landscape and industry practice...concerns certain payment processing activities."

States could look to federal law for guidance as FinCEN issued an administrative ruling making clear that Independent Sales Organizations and payment processors meeting certain requirements are not money transmitters subject to BSA regulations.³ While the federal government does not currently control the states in this space, following that guidance, a number of states have provided

applicability in the case of non-profit institutions; California's recent suggestion that certain types of goods or services should be omitted.

² See Rest. (Third) of Agency § 1.04 ("In a relationship of co-agency, neither agent is the other's agent ... Each coagent owes duties to the common principal.").

³ See U.S. Department of Treasury Financial Crimes Enforcement Network Administrative Ruling "FIN-2014-R009". Also See "FIN-2014-R004" which states that "the acceptance and transmission of funds only integral to the sale of goods or the provisions of services, other than money transmission services will not cause the person that is accepting and transmitting the funds to be deemed a money transmitter."

specific exemptions (through guidance or statute) for payment processing. However, a uniform position across the states is important to ensure that the regulatory framework of the states is open for innovation.

Insured prepaid card

Clear guidance and exemptions on state regulatory oversight of bank issued prepaid cards should be provided. Generally, if these prepaid cards are issued by a chartered financial institution, these products are already under significant regulatory oversight and therefore should be exempt from money transmitter licensing requirements.

Closed loop prepaid access

Many, but not all, states have an express exemption from the definition of payment instrument (or similar term) for payment instruments issued and redeemed by the issue of goods or services. ETA recommends that all states adopt an express exemption from the definition of payment instrument (or similar term) for payment instruments issued and redeemed by a closed network of parties.

Agents and service providers of banks

Banks and other financial institutions are some of the most regulated entities in the world on the federal and states levels. Their agents, through agency law, and their service providers by contract and regulatory requirements are also subject to much of the same regulation. As such, states should adopt express exemptions for agents and service providers of financial institutions.

Business to business activities

ETA supports the recommendations of the FinTech Industry advisory panel to harmonize an exemption for business to business activities.

Control

Control events including biographical requirements

ETA supports the FinTech Industry Advisory Panel's recommendations that states revisit the change in control requirements in order to streamline the process while preserving the shared goals to ensure that only appropriately qualified and vetted parties participate in the money transmitter system.

Change of control requirements across states offer a very disparate approach to what type of investment constitutes a control event the requirements for notification to regulators including a formal application or notice. For example, for the definition of control, 29 states and the District of Columbia use 25% control of outstanding voting shares of an entity as the trigger for control, while, 11 other states use 10%. Nevada, Utah, and New York use 20%, Arizona uses 15%, and

Hawaii uses 35%.⁴ The reality of the current disparate landscape serves as a regulatory hurdle not built for the modern marketplace where startup payment companies often and predictably take on outside investment several times in their early years. These are positive actions which the state of the segmented regulatory landscape makes expensive and time consuming to comply with.

One instance of the requirements which are particularly onerous for licensees is the fingerprinting requirements for currently 27 states. Regardless of whether a person has limited or no contact with the state in question, if the company requires licensure in that state, then all control persons subject to biographical requirements must comply. Control persons, including those with only an investment interest must physically appear to fulfill this requirement, creating a significant burden for investment including time, travel, and cost. To help alleviate this burden, university accepted fingerprinting done through a central depository like the CSBS's Nationwide Mortgage Licensing System and Registry ("NMLS") could provide a mechanism to lower the barrier to entry for investment in money transmission companies.

Control persons (including Foreign Control Persons)

ETA supports the recommendations made by the FinTech Industry Advisory Panel to consider recognizing the distinction between passive ownership and control of the investment made in licensees when a VC firm is involved. Recognition in this distinction will provide a better result for licensees who may be considering investment by venture capital firms.

ETA also supports the recommendation that states should have mechanisms in place to facilitate the employment of the world's best and brightest in the payments space. That includes foreign control individuals that meet the same bar for integrity that we expect of local control persons and that they may be evaluated consistently and uniform across the country to ensure that bad actors cannot participate anywhere in the system. Additionally, ETA recommends that states seek to identify relevant providers of the equivalent criminal background checks in foreign countries to establish minimum standards to be met of the provision of financial information for cases where credit checks do not have the same utility as in the states. Ultimately, there needs to be a uniform and accessible approach for vetting foreign control persons.

Prudential Requirements

Net Worth & Surety Bonding

ETA prefers that states adopt a system of uniform surety bond standards. These would help licensees better monitor volumes and agents to determine when bond increases are needed. Additionally, a cap is important to bonding as well because once a licensee grows more complex, review of other factors like capital and liquidity are required.

⁴ Those 25% states include: Alabama, Alaska, Arkansas, California, Colorado, D.C., Florida, Hawaii, Idaho, Illinois, Indiana, Iowa, Kansas, Kentucky, Louisiana, Massachusetts, Michigan, New Jersey, New Mexico, New York, North Dakota, Ohio, Oklahoma, South Dakota, Tennessee, Texas, Vermont, Virginia, Washington, and Wyoming. 10% states include: Connecticut, Georgia, Mississippi, Minnesota, Nebraska, New Hampshire, Maryland, North Carolina, Rhode Island, Wisconsin, West Virginia (which may also require a spouse).

Permissible Investments

It is imperative that states look to harmonize their definitions of permissible investments with a uniform set of principles. Calculation of permissible investments can be difficult when a licensee holds a diverse base of assets. This may also involve moving funds from one account type to another when it really does not impact the safety and soundness of the company. States should align on what is and is not permissible and the percentages of assets that are allowable. This would prevent licensees from constantly having to change their permissible investment portfolio and focus on maintaining adequate balances which should be a priority over which account the funds are held. For example, some states allow FBO funds and others do not. Some states allow the use of MMF funds invested in U.S. treasuries at 100% while other states have 10 or 25% caps. Alignment amongst the states and standardizing of what caps are necessary would also be more beneficial for states. In the current system, where states may require different types of securities, it is difficult for a state to know that its consumers' funds are in the "correct" type of security required by that state. If there were one uniform standard, a state could more easily confirm that all regulated funds were held according to the requirements, and therefore be more assured that its consumers' funds are properly protected. A universal standard would be more beneficial for both the states and licensees and would allow more time to be spent on higher risk areas.

Supervision

ETA is appreciative of the many improvement instituted by state regulators in their supervision practices in recent years. These are well received efforts; however, ETA also agrees with the FinTech Industry Advisory Panel that a number of additional measures could be instituted to help make the supervision and examination practices more efficient.

First, state regulators should encourage states to use the NMLS tool and encourage full adoption of NMLS to eliminate duplicative tasks and inefficiencies. While investments in improving the tool are necessary to make this work for all states, for example, so that confidential correspondence with one state will not unnecessarily be disseminated to all states, this type of investment would save all states time and resources in the future. Second, states should prescribe unified reporting formats, time frames, and parameters. Third, states should find ways to use reciprocity across states with similar requirements to help save time, effort, and money for licensees and supervisors. Fourth, states should provide mechanisms and incentives for industry participants to have real-time conversations with regulators to help drive a positive collaboration between regulators and the industry.

Conclusion

ETA encourages states to work together to harmonize requirements for money transmitters and urges all participants in the marketplace including regulators, policymakers, and money transmitters to move towards a regulatory framework that can promote innovation rather than hamper it.

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We appreciate you taking the time to consider these important issues. If you have any questions or wish to discuss any issues, please contact me or ETA Senior Vice President, Scott Talbott at Stalbott@electran.org.

Respectfully submitted,



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