

Summary of two options for financial requirements

See templates 11, 12, and 13 and the suspension bridge PowerPoint for more details

1. Three-legged stool – traditional net worth, permissible investment, and bonding requirements. Would be applied only to multi-state licensees. Licensees in a single state, or a small number of states, would continue to be subject to the current states' MSB regulations.

Net worth (indication of safety and soundness)

- Tangible net worth must be proven at application and annually with current audited financial statements prepared in accordance with GAAP. This net worth must be maintained at all times.
- Net worth minimum requirement is the greater of \$100,000 OR 3% of total assets.
- Discretion for director/superintendent to increase requirements if needed based on risk.

Permissible Investments (Primary safety element for consumer obligation protection (assets to meet obligations))

- PI must be computed in accordance with GAAP of not less than the amount of the licensee's activity in the United States.
- Types of allowable investments:
 - No limit:
 - cash, deposits, certificates of deposit, or senior debt obligations of an insured depository institution;
 - bank and credit card receivables;
 - receivables less than 7 days old from ADs; and
 - investment security that is an obligation of the US, department, agency, or instrumentality thereof or state, governmental subdivision, agency, or instrumentality thereof.
 - 30%:
 - investment bearing a rating of one of the 3 highest grades;
 - commercial paper; and
 - corporate debt or bonds.
 - Range TBD with additional input
 - savings deposits, demand deposits, or certificates of deposit at a foreign depository.
- The aggregate of investments limited by the percentage is limited to 50% of total outstanding customer payment obligations
- Discretion for director/superintendent to designate any other investment as permissible

Bonding (safety net for consumer loss, cover costs of receivership, etc.)

- \$100,000 minimum (for activity of \$0 to \$5 million).
- Increase of \$100,000 per every \$5 million of activity up to \$45 million. Over \$45 million in activity requires a bond of \$1 million.
- Discretion for director/superintendent to increase the amount of security required to a maximum of \$7,000,000.

2. Suspension bridge - REPLACES the net worth, PI, and Bonding requirements (details TBD):

Ratio-based financial condition requirement (replaces net worth) - tangible assets must be 105% of total liabilities

- Compliance based on relation between assets and liabilities, remains effective with growth
- Proposed ratio: Tangible Assets / Total Liabilities
 - Minimum of \$100,000 and 5% buffer (if lower buffer, prompt corrective action required)
- Conversion to Buffer: $(\text{Tangible Assets} / \text{Total Liabilities}) - 1 = \text{buffer \%}$

Rebrand permissible investments as “**permissible safeguarding**”- assets safeguarding customer funds dictated by financial strength

- Explicitly prohibit comingling and conversion of customer funds
- Conditioning of assets is based on strength of financial condition
 - Some assets are considered risk-free, others are linked to buffer percentage
- Funds are safe if 110% are covered by a surety bond

Use of **surety bonds** – flexible support component

- Minimum Bond: amount required to fund a receivership (will grow with company)
- Maximum Bond: 110% of customer funds → no requirement to convert customer funds to safe assets
- Should start-ups have a different requirement?

Net Worth Requirements

CONCERNS (include source of concern – ex. FIAP, RFI, etc.)

The FIAP suggests a national standard for net worth as well as looking at net worth, permissible investments, and surety bonds together as one overall safety and soundness system. The FIAP further expressed a desire for these three components to not create undue operational challenges, impose unnecessary costs to licensees, or stifle innovation.

AVAILABLE OPTIONS

Individual State laws

Uniform Money Services Act

POLICY CONSIDERATIONS (including risks)

Tangible net worth adds to liquid assets and the greater likelihood of funds availability in the event of insolvency. However, less than ten states currently have a tangible net worth requirement. In the states that require net worth, the minimum and maximum net worth amounts vary greatly among states from zero to \$3,000,000 and in some cases can be increased further at the discretion of the commissioner.

Most states have an audited financial statement requirement.

Transaction volume correlates to the potential exposure of consumer funds and is most often used in net worth calculations by states today. Net worth based on the number of locations is antiquated.

For money transmitters the following net worth standards are applied:

- Tangible net worth must be proven at application and annually with current audited financial statements prepared in accordance with GAAP. This net worth must be maintained at all times.
- Net worth minimum requirement is the greater of \$100,000 OR 3% of total assets.
- Discretion for director/superintendent to increase requirements if needed based on risk.

OPEN QUESTION: should there be a small business exemption? Can this be accomplished through director discretion language and/or waivers?

There is no net worth requirement for a currency exchanger regardless of the number of locations or states where the company operates but the company must demonstrate that it has the financial responsibility and condition to justify the confidence of the public and warrant the belief that the

applicant will conduct business in compliance with state and federal law. Audited financial statements are not required.

RECOMMENDATION (model statutory language)

(a) A licensee under this [article] shall maintain at all times a tangible net worth of the greater of \$100,000 or three percent of total assets

(b) Net worth must be proven at initial application and annually with current audited financial statements prepared in accordance with generally accepted accounting principles.

(c) The [superintendent] may increase the amount of tangible net worth required if the [superintendent] determines that a higher net worth is necessary based on criteria specified in rule.

Bond Requirements

CONCERNS (include source of concern – ex. FIAP, RFI, etc.)

FIAP Recommendations: The FIAP included bonding requirements as part of the group prudential regulations for money transmitters. Under UMSA, these were the primary safety and soundness options to consider when evaluating new entrants to the money transmission market. Bonding (along with net worth) is intended to serve as a general proxy for the financial health of an applicant, a minimum barrier to entry, and works to ensure applicants meet basic financial criteria and have viable business models. FIAP stated that the substantive application of the requirements varies significantly, and sometimes are not even established by statute or regulation. The minimum surety bond requirement varies from \$10,000 to at least \$1,000,000. The maximum bond also vary up to \$2,000,000 in a number of states, and one state with \$7,000,000. 12 states have no maximum bond amount.

The basis for determining the bond also varies, with some states using volume (with different volume calculations). Other states use the number of locations of the licensee (and its authorized delegates), and/or whether or not the licensee provides services through the Internet as factors to calculate the bond amount.

FIAP recommends that the surety bond requirements are more consistent and consider the establishment of one or more national standards. FIAP recommends that state regulators identify a principles-based standard for consistent application of the safety and soundness requirements.

The RFI also looked at prudential requirements. For the surety bond, the two fundamental purposes were identified as: (1) mitigates consumer losses in event of failure, and (2) establishes market-based risk analysis. The RFI suggests a review of legislative history of all prudential requirements to determine whether the intent for these requirements is additive. The RFI alternatively asked states to identify a principles-based standard for consistent application of safety and soundness requirements. The RFI also described the significant variance in how both net worth and bond requirements are implemented. There can be broad discretion to require amounts between minimum and maximum ranges set by statute. Industry reports inconsistent application of inconsistent requirements, and want more consistency with the establishment of one or more national standards.

AVAILABLE OPTIONS

- (1) Adopt UMSA as written
- (2) Modify UMSA
- (3) New language

POLICY CONSIDERATIONS (including risks)

Section 204 of UMSA relates to security, and currently has a minimum of \$50,000 plus \$10,000 per location up to \$250,000. UMSA states it must cover claims for as long as the specific statute specifies, but for at least 5 years after the licensee ceases to provide money services. The security may be reduced/eliminated if the amount of a licensee's payment instruments or stored-value obligations outstanding is reduced. The amount of security can be increased to a maximum of \$1,000,000 if the financial condition so requires e.g. reduction of net worth or financial losses. The Comment to UMSA notes that the location refers to physical locations, and that companies who provide services through the Internet will need to be assessed based on other criteria such as volume of business.

It is clear from a review of the various state surety bond requirements that there is great inconsistency in the amounts compared to UMSA, and in the notion of discretion. One apparent flaw in the actual language of UMSA relates to companies only doing business over the Internet. Any statutory model has to consider a bond calculation that more accurately identifies the risk associated with online money transmission. If states deem that an Internet-based licensee only operates out of "one" location, then under UMSA, the maximum bond is limited to \$50,000. Even the section in UMSA related to discretion is only related to financial condition. The Comment appears to suggest this section can be used as a basis to increase the bond amount, but this language appears to be unclear at best as to whether a state would have the authority to raise the bond amount just because they are an online location.

Another issue which all states face over time is the inherent decrease in value of the bond amount. Setting a static number can be clear, but over time consumers need to send higher amounts of money as the costs of goods and services increases. A \$250,000 or \$1,000,000 bond may not be sufficient today because of the value of money as well as the ease of sending money through online companies. The presentation at the MTRA conference on "The State of the Money Transfer Industry" stated that the World Bank estimate of remittance inflows in 2017 was \$600 billion compared to \$320 billion in 2006. The CSBS Washington Update at MTRA stated the total market was \$1.1 trillion, with the Fintech market share at 44%.

This leads to the conclusion that sales/volume should be part of the bond calculation. However, as a money transmitter enters a state with no volume, this would require minimum bond amount that could be scaled up based on volume/sales. This does bring into question the same issue that permissible investments analyses raise as to what volume is used: state, US, or global.

Another policy consideration for the amount of the bond is the size and nature of the market in which the money transmitter is operating. For example, in a state such as California, the maximum surety bond of \$7 million may seem reasonable, but then the next highest (where a maximum is stated) is Kentucky at \$5,000,000. This may mean that either state is too low, too high, or just right for the size and nature of the market.

A final policy consideration for bond amounts may also be anticipated business. If the company provides business plans that projects a certain amount of business based on their history in other jurisdictions, then a higher bond amount may be necessary.

The ultimate goal of the bond is to provide some security for claims related to their money transmission activity. The notion of using number of locations may be outdated where the activity and volume is truly the key measure of risk intended to be mitigated against by a surety bond.

RECOMMENDATION (model statutory language)

(a) Except as otherwise provided in subsection (b), a surety bond or other similar security acceptable to the [superintendent] in the amount of \$100,000 must accompany an application for a license.

(b) The licensee shall maintain or increase the amount of security to reflect the dollar amount of all licensed money transmission activity in this state in the preceding calendar year according to the table in this paragraph. A licensee may decrease its security according to the table in this paragraph if the security required is less than the amount of security on file with the [superintendent].

Dollar Amount of Money Transmission Activity	Security Required
\$0 to \$5,000,000	\$100,000
\$5,000,000.01 to \$10,000,000	\$200,000
\$10,000,000.01 to \$15,000,000	\$300,000
\$15,000,000.01 to \$20,000,000	\$400,000
\$20,000,000.01 to \$25,000,000	\$500,000
\$25,000,000.01 to \$30,000,000	\$600,000
\$30,000,000.01 to \$35,000,000	\$700,000
\$35,000,000.01 to \$40,000,000	\$800,000
\$40,000,000.01 to \$45,000,000	\$900,000
Over \$45,000,000	\$1,000,000

(c) Security must be in a form satisfactory to the [superintendent] and payable to the State for the benefit of any claimant against the licensee to secure the faithful performance of the obligations of the licensee with respect to money transmission.

(d) The aggregate liability on a surety bond may not exceed the principal sum of the bond. A claimant against a licensee may maintain an action on the bond, or the [superintendent] may maintain an action on behalf of the claimant.

(e) A surety bond must cover claims for so long as the [superintendent] specifies, but for at least five years after the licensee ceases to provide money services in this State. However, the [superintendent] may permit the amount of security to be reduced or eliminated before the expiration of that time to the extent the amount of the licensee's payment instruments or prepaid access [or stored value] obligations outstanding in this State is reduced. The [superintendent] may permit a licensee to substitute another form of security acceptable to the [superintendent] for the security effective at the time the licensee ceases to provide money services in this State.

(f) The [superintendent] may increase the amount of security required to a maximum of \$7,000,000.

Permissible Investment Requirements

CONCERNS (include source of concern – ex. FIAP, RFI, etc.)

FIAP: There are inconsistent approaches in formulas used to calculate permissible investments (PI) and the manner in which PI may be held. Also, the types of assets which may be used vary, as do the extent to which particular types of funds may be counted toward PI.

AVAILABLE OPTIONS

- 1) Adopt Uniform Money Services Act as written
- 2) Modify Uniform Money Service Act to modernize
- 3) Draft new statutory language

POLICY CONSIDERATIONS (including risks)

Utilizing the Uniform Law Commission's UMSA maintenance of permissible investments section but using global money transmission activity instead of just activity in all states will ensure that a company has adequate assets to cover all customer liabilities. Currently 13 states have no PI requirements; 27 base their PI on outstanding payments in the U.S. (this is the ULC's calculation as well); 6 base it on global outstanding payment obligations; and 3 base it on alternative methods of calculating value. However, if a company has a large amount of liability outside the United States, then it would do little good to require coverage for United States activity only.

In addition, we added language addressing how to treat virtual currency for those states that will regulate virtual currency under their money transmission laws. This language is in green below. Virtual currency PI should be maintained at a 1:1 like-kind ratio because virtual currency is so volatile. If PI for virtual currency companies could be maintained in cash or other traditional assets the company would have to constantly adjust their PI as the value of virtual currency fluctuated daily, sometimes hourly. Such a model would be impossible to maintain, as would the valuations to USD with the constant fluctuation.

The ULC section on types of permissible investment is modified to keep in line more with modern business models while still protecting consumers. Many licensees transact business globally and may have significant assets on deposit at a foreign institution that previously were not included in ULC's types of permissible investments. In addition, capping the amount of permissible investment allowed based on the amount owed out by the licensee at any given time is safer because it is more restrictive. It is also easier to calculate for the licensee. The calculation will be more straightforward as it will be a percentage of a known number (amount outstanding) versus a percentage of a number (total permissible investments) for which you need many other numbers (all the different categories of allowable permissible investments held) to calculate.

RECOMMENDATION (model statutory language)**Maintenance of Permissible Investments**

(1)[(a)] A licensee shall maintain at all times permissible investments that have a market value computed in accordance with generally accepted accounting principles of not less than the aggregate amount of all of its outstanding payment instruments and prepaid access [or stored value] obligations issued or sold in all states and money transmitted from all states by the licensee.

[Virtual Currency Module – insert if regulating virtual currency (also insert (a) after 1 above):

(b) A licensee transmitting virtual currencies must hold like-kind virtual currencies of the same volume as that held by the licensee but which is obligated to consumers in lieu of the permissible investments required in (a) of this subsection.

(c) A licensee conducting activities in both subsection (a) and (b) must maintain applicable levels and types of permissible investments as described in those subsections.]

(2) The [superintendent], with respect to any licensees, may limit the extent to which a type of investment within a class of permissible investments may be considered a permissible investment, except for money and certificates of deposit issued by a bank. The [superintendent] by rule may prescribe or by order allow other types of investments

(3) Permissible investments, even if commingled with other assets of the licensee, are held in trust for the benefit of the purchasers and holders of the licensee's outstanding payment instruments and stored value obligations in the event of bankruptcy or receivership of the licensee.

Types of Permissible Investments.

(1) Except to the extent otherwise limited by the [superintendent] pursuant to [the section on maintenance of PI], the following investments are permissible under [the section on maintenance of PI]:

(a) cash, bank and credit card receivables;

(b) savings deposits, demand deposits, certificates of deposit, or senior debt obligation of an insured depository institution, as defined in Section 3 of the Federal Deposit Insurance Act [12 U.S.C. Section 1813 (1994 & Supp. V. 1999)] or as defined under the federal Credit Union Act [12 U.S.C. Section 1781];

(c) an investment security that is an obligation of the United States or a department, agency, or instrumentality thereof; an investment in an obligation that is guaranteed fully as to principal and interest by the United States; or an investment in an obligation of a State or a governmental subdivision, agency, or instrumentality thereof; and

(d) receivables that are payable to a licensee from its authorized delegates in the ordinary course of business, pursuant to contracts, which are less than seven days old.

(2) The following investments are permissible under [the section on maintenance of PI] if the investment does not exceed 30 percent:

(a) A short-term (up to six months) investment bearing a rating of one of the three highest grades as defined by a nationally recognized organization that rates securities;

(b) Commercial paper; and

(c) An interest-bearing bill, note, bond, or debenture of a person whose equity shares are traded on a national securities exchange or on a national over-the-counter market

(3) Savings deposits, demand deposits, or certificates of deposit at a foreign depository are permissible under [the section on maintenance of PI] if the investment does not exceed XX percent [percentage needs to be determined].

(4) Any other investment the [superintendent] designates is permissible under [the section on maintenance of PI], to the extent specified by the [superintendent].

(5) The aggregate of investments under subsections (2)-(4) may not exceed 50 percent of the total permissible investments of a licensee calculated in accordance with [the section on maintenance of PI].