

November 1, 2019

Via E-Mail to modelpaymentslaw@csbs.org

Attn: MSB Model Law
Conference of State Bank Supervisors
1129 20th Street NW, 9th Floor
Washington, D.C. 20036

Re: Request for Comments: MSB Model Law

Dear Conference of State Bank Supervisors:

Thank you for developing the model language for money services businesses (“MSBs”) laws and providing the opportunity to comment on the draft version of the language. Hunton Andrews Kurth LLP (“Hunton”) is a global law firm that represents banks, MSBs, loan servicers, payment processors, marketplace lenders, start-ups and established financial technology (“fintech”) companies, and a variety of other parties in the financial services market, including money transmitters that range from large entities licensed in all U.S. jurisdictions to small businesses that are seeking their first state licenses. Many of these clients would be directly impacted by the proposed MSB model law, while numerous others would feel the indirect impact. We believe Hunton is uniquely positioned to provide comments on the MSB model law and we appreciate that opportunity to do so. Hunton commends the Conference of State Bank Supervisors (“CSBS”) for its efforts to develop an integrated licensing and supervisory system with uniformity across state lines.

Scope

The first outstanding question asks how the states should bifurcate the applicability of the model law language and existing law. Hunton recommends that CSBS move forward with Option 1 - the model law language is adopted as an overlay of existing state law. It is our reading that this option would allow states to adopt the model law as a new and distinct licensing category, which would sit next to the states’ existing licensing regimes. So, for example, in Minnesota there would then be three license types: the Minnesota Money Transmission License, the Minnesota Currency Exchange License, and the new Multistate Money Transmission License. We believe adding the model law as a new license category, instead of inserting the model law into existing law or replacing existing law with the new model law, will achieve two important goals: (1) it will make

November 1, 2019

Page 2

it clear what requirements do and do not apply to MSBs that only operate in one state, and (2) it will lead to the greatest adoption by states. Money transmission licensing requirements are already difficult to navigate and we believe inserting the new multistate requirements into existing state laws will only make them more confusing.

We suggest the multistate license as a new license type so that MSBs seeking licensure can clearly tell what category they fall under and what requirements apply to their situation. Furthermore, we believe approaching state legislatures with the MSB model law as a new license type will lead to the greatest adoption. We fear inserting the model law into existing law will lead legislators to modify the model law as well as open up existing law for unintended changes. Since the goal is to keep the model law as uniform across states as possible, we believe that will best be achieved by presenting the model law as a stand-alone law and not as something that has to be worked into the various existing state laws, which are already inconsistent in content and form. We also fear that legislators will reject the model law if it requires entirely eliminating existing state licensing regimes. Finally, replacing existing laws goes against CSBS' own stated goal that companies operating in one state should not be subject to the uniform law; if the new model law replaces existing law, entities will have no choice but to apply under the uniform law.

Activity Definitions

The second outstanding question asks how states can ensure consistent interpretation of the new model law definitions. Hunton recommends that the states establish a standing multistate interpretations committee to review novel definitional questions regarding what does and does not constitute money transmission, money, virtual currency, and the other definitions set out in the model law. Currently each state interprets its own definitions, which has led to inconsistencies across state lines, yet which is wholly appropriate as each state should interpret its own law. However, once the model law is adopted in multiple states, it will no longer make sense for each state to interpret the law individually. The law is intended to be a uniform, multistate law and it would be self-defeating if multiple states adopt the model law but then chose to interpret it differently.

The only way Hunton sees to achieve consistency is with a multistate interpretations committee. If a state receives a novel question for interpretation, the state should redirect the inquiry to the multistate interpretations committee. This will ensure one consistent interpretation is agreed upon by a group of states. Furthermore, ensuring the consistent interpretation of definitions will involve ongoing efforts. Technology and the payments industry are constantly evolving, and new issues will continue to arise. Therefore we suggest a standing multistate interpretations committee to address both questions that will arise upon the adoption of the model law and issues that will continue to arise in the future as existing concepts have to be applied to new business models and new technology.

November 1, 2019

Page 3

Exemptions

The third outstanding question asks if businesses that only take payor funds after the business has sent money to the payee at the payor's instruction should be exempt. Hunton believes that these MSBs should be exempt because there is no risk of harm to customers. Since the payee is paid as the first step, there is no risk of harm to the payee. In addition, because the payor only pays the MSB after the funds have been sent to the payee, there is no risk to the payor. The only risk is to the MSB itself in the situation where funds have been sent to the payee and then the payor refuses to reimburse the MSB. While this is a riskier business model for an MSB to adopt, because the activity does not pose a risk to the customers, an exemption is appropriate.

In addition, Hunton believes this activity is already excluded by the proposed definition of "money transmission." The proposed definition of "money transmission" includes "receiving money for transmission" which in turn is defined as "receiving money or monetary value in the United States *for transmission* within or outside the United States by electronic or other means" (emphasis added). In the situation described, where the MSB receives money from the payor only after funds have already been sent to the payee, it is our reading that the MSB is not in receipt of money *for transmission*. Instead, we believe that the funds are received *as a reimbursement* for funds already transmitted to the payee by the MSB. When the payor sends money to the MSB, it is not with the intent that it be transmitted since funds have already been delivered to the payee; rather the intent is to make the MSB whole for funds it has fronted. From past discussions with several state regulators, it is our understanding that this "prefunding" activity is currently not considered money transmission in those states based only on the existing definitions of money transmission in those states. Therefore we believe that this activity will be exempted by just the proposed definition of "money transmission" and that if regulators do intend for this type of activity to be licensable money transmission, then the definition – or at least the interpretation – of "money transmission" would need to change.

Control

The final outstanding question asks how states can leverage the Multistate MSB Licensing Agreement to remove repetitive licensing practices that do not address a corresponding risk. First, we commend the states for their cooperation; Hunton recognizes and appreciates the fantastic progress states have made on coordinating applications and examinations. Second, we appreciate that CSBS recognizes that companies should not be unduly burdened by repetitive tasks that do not address a clear and specific risk. As the working group correctly identified, change of control requirements are ripe for reform as they are currently disparate yet repetitive. States all have the goal of prohibiting unfit persons from controlling an MSB, therefore there must be common ground on who is a control person and what should be a trigger for a change of control application.

November 1, 2019

Page 4

Standardizing change of control requirements such that change of control applications can also be processed through the Multistate MSB Licensing Agreement would remove a significant burden that is currently a repetitive process.

Regarding the Multistate MSB Licensing Agreement itself, we understand that the lead state is already reviewing most common licensing requirements, including the applicant's business plan, background checks, financial information, and compliance with the anti-money laundering provisions of the Bank Secrecy Act. While there may be some other application requirements that are common across states that could be reviewed under the Multistate MSB Licensing Agreement, Hunton believes that the next significant step in coordination requires states to adopt the model law (or otherwise pass more uniform state MSB licensing laws). For so long as states have significant state-specific application requirements, the lead state can only go so far in reviewing and approving an application. We do not expect the lead state to become an expert in every other states' laws. Therefore, until state-specific requirements are reduced or eliminated, we do not see an obvious way for states to remove any additional repetitive licensing requirements using the Multistate MSB Licensing Agreement.

Financial Condition

- *Net Worth*

While Hunton does not have a specific opinion on the Three-Legged Stool or the Suspension Bridge approach to financial condition, we do agree that that a company's financial condition should be measured in relation to the company's balance sheet. In addition, we greatly appreciate the effort to standardize the net worth requirement and we agree with the working group's proposal that licensees have a \$100,000 tangible net worth (or net worth equal to 3% of total assets, whichever is higher). This requirement has long served as a barrier to entry for start-ups, particularly because of the tremendous variance between state minimums. It is difficult to explain to a fintech startup why only \$1,000 in net worth is required in Hawaii, but \$1 million is required in Utah, since there does not appear to be an obvious correlation between those amounts and those state markets or a company's safety and soundness. Having one standard net worth requirement set at a reasonable \$100,000 will be a great improvement over the current regime.

- *Surety Bonds*

Under the discussion of the Suspension Bridge, the working group acknowledges that, for the largest licensees, surety bonds do not provide the kind of protection envisioned in traditional money transmitter laws and that even with a \$100 million nationwide bond requirement, that amount would only cover pennies on the dollar for their liabilities. Therefore, the Suspension

November 1, 2019

Page 5

Bridge proposal repurposes surety bonds for the largest MSBs. Hunton would like to propose its own repurposing of surety bonds. In medical malpractice, some states have introduced the idea of a victim's compensation fund. It is intended to balance the needs of both doctors and patients by placing caps on the amount of damages that a patient can recover from a doctor, but then allowing the victim to be additionally compensated from a state-run patient's compensation fund. The fund essentially plays the role of an "excess insurer" of private healthcare providers. Louisiana is one state with a Patient's Compensation Fund; under that law, doctors have financial responsibility for the first \$100,000 of exposure per claim and then the Patient's Compensation Fund covers additional damages (if the patient's damages exceed that amount). Doctors pay surcharges for the coverage and protection provided by the Patient's Compensation Fund, which in turn provides protection for the healthcare system, keeps insurance costs down, and provides a guaranteed pool of funds to pay patients injured by medical malpractice.

Hunton believes a "customer's compensation fund" could similarly balance keeping surety bond costs down while also guaranteeing that purchasers of money services are able to recover any money that is lost if an MSB fails or is otherwise unable to meet its customer obligations. While maintaining surety bonds is a significant expense for MSBs, the bonds are likely insufficient to make customers whole as the working group itself has noted. Therefore a "customer's compensation fund" could strike the correct balance by keeping the MSBs' costs for surety bonds down – say by capping surety bond requirements at \$100,000 per state as the working group has proposed as the minimum threshold – while at the same time making it more likely that customers will be made whole since they will be able to draw on the compensation fund once the surety bonds (and permissible investments) are extinguished.

Additional Comments

In addition to the issues directly raised by the working group, Hunton would like to comment on the following MSB licensing and uniformity topics:

- *Regulatory Sandbox or On-Ramp License*

While the model law, if adopted, would greatly reduce the barrier to entry, it would still be a significant burden for a new fintech or payments company to obtain all the state money transmission licenses needed to operate as an MSB on a national basis. Therefore, we encourage the CSBS working group to consider including a multistate regulatory sandbox or on-ramp license as part of its model law proposal. As we are sure the working group is well aware, a regulatory sandbox or ramp-up license is a structure set up by a financial regulator with more modest regulatory requirements to allow companies to conduct small scale, live testing of products and services in a controlled manner prior to full-scale public release. Regulatory sandboxes exist all over the world, notably in the United Kingdom and Arizona, which enacted the first U.S. state

November 1, 2019

Page 6

fintech sandbox in 2018. An example of an on-ramp license can be found in the Uniform Regulation of Virtual-Currency Businesses Act. We do not propose any particular structure or requirements for the regulatory sandbox or on-ramp license, but instead simply encourage the working group to consider the concept as part of the model law process.

- *Reciprocity*

Finally, Hunton believes it would be beneficial for the working group to consider adding a reciprocity provision to the model MSB law. State regulators, as evidenced by Vision 2020, are committed to developing a 50-state licensing system and we believe reciprocity is a key component of multistate licensing. As state MSB laws become more uniform, it increases the likelihood that states will be willing to grant reciprocity since they can be assured that other states' MSB laws and licensing requirements are similar if not identical to their own. And once the MSB model law is adopted, there will be little reason for a company to go through the licensing process on a state-by-state basis. If two states have both adopted the model law, a company should be able to get licensed in one and receive reciprocal licensure in the other since the second state can be assured that the company has met its licensing requirements. Without reciprocity, repetitive requirements can be reduced through the model law, but they cannot be eliminated since an entity must still go through the full licensing process in each state. We believe reciprocity is fully in line with CSBS' goal of a regulatory system that is more efficient, coordinated and aligned, therefore we recommend that a reciprocity provision is included in the final model MSB law.

Conclusion

Hunton appreciates this opportunity to comment on the draft MSB model law. We look forward to continuing the conversation on these complex issues, and the next steps in modernizing and improving state regulation of MSBs.

Sincerely,



Erin F. Fonte

Partner
Hunton Andrews Kurth LLP