

The Risks, Options and Complexity of State Money Transmitter Licensing Laws



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Agenda

- Background on State Money Transmitter Licensing Laws
- Costs and Complexities
- Risks and Enforcement
- Options for new businesses and start-ups
- Troubling trends in Authorized Delegate policies & positions
- Qs & As

Money Transmitter Licensing laws

- Genesis: “Safety and soundness” of non-bank –issuers (Banks are generally exempt)
- Regulates non-bank entities that receive and hold consumer funds, with promise of making funds available later – or sending funds elsewhere.
- 4 primary goals – To make sure entities holding other people’s money:
 - Are financially sound
 - Are not owned or operated by criminals and money launderers
 - Have the knowledge base, systems and resources needed to operate a money transmission business safely and in compliance with laws
 - Are subject to supervision and oversight by a state regulator

Costs and Complexity

Cost –

- Often up to 2 years and \$100,000- \$300,000; net worth \$1million; bonds in each state
- Ongoing compliance, renewals, fees
- Often requires a full-time licensing employee
- And a full time AML Compliance officer

Complexity –

- 48 different state laws – many compliance requirements
- Receipt requirements; posted sign requirements; audit
- Conflicts between state interpretations: prepaid cards; exemptions for banks, processors, agents of payees

Costs and Complexity

Keeping up with changes in the laws

- 19* new bills/regulations impacting money transmitters passed in 2014
 - Significant updating (both technical and substantive) – 5 states
 - NMLS additions – 3 states
 - Agency changes/clarifications – 3 states
 - Fraud-related changes – 2 states
 - “Agent of the payee” exemptions – 2 states
 - Changes to fees – 3 states
 - Other changes – 3 states

* Some state laws impacted multiple areas, hence the list does not total to 19.

Risks and Enforcement

- Risks - - -

- Doing money transmission business without a license – federal crime 18 USC § 1960
 - Reports of unlicensed money transmitters being raided and assets seized.
- States increasingly penalizing non-banks \$10-\$500,000 – reportedly even more than a \$1 million
- States narrowing exemptions and increasing enforcement
- Even companies that are licensed risk penalties for errors in compliance.

Options for New Payment Companies

1. Launch in states without licensing requirements (MT, SC; for some products, NM, MA...)
2. Get licensed.
 - You can start with the easier / faster states
 - But plan on time and expense for the larger, more difficult states: CA, NY, TX, IL, FL, OH, WA, VA...
 - If you've done *any* business prior to licensing, there may be a penalty.
3. Structure products so you don't hold funds, don't hold self out as offering payments, don't issue or sell "prepaid" or other payment instruments. Funds in custodial accounts might help... License your IP – let someone else hold/move the money!

Options for New Payment Companies

4. Partner with a bank as agent - - preferably a national bank
 - Still, some States exempt only “if it does not issue, sell, or provide **payment instruments or stored value** through an agent who is not a bank.” 10 States: [Alaska](#), [Arkansas](#), [Idaho](#), [Kansas](#), [Maine](#), [New Jersey](#), [North Dakota](#), [Vermont](#), [Washington](#), [Wyoming](#)
 - Some States exempts banks only if it is a national bank or a state bank chartered or authorized to do business in their OWN state; out of state, state banks not exempt:
 - [Alabama](#), [Colorado](#), [Mississippi](#), [Nevada](#), [Oregon](#), [Utah](#) (though some of these states waive the requirement)
5. Partner with a licensed money transmitter
 - Unlike banks, this WAS a complete solution across all state laws
 - All states exempt agents or authorized delegates of licensed money transmitters

But: Growing Concern from Regulators

- Can a licensee appoint a third party as authorized delegate if the third party is offering a product or service that the licensee *does not already provide*?
 - Can the authorized delegate be said to be providing services “on behalf of” the licensee if the licensee is not already in that line of business?
 - Does such a relationship = “rent-a-license”?
- Or...can a licensee decide to offer a new service—such as prepaid card reloads or Person-to-Person mobile payments—and do so through a third party?
 - Where and how should the line be drawn?

Changing Trends in the Role of Authorized Delegates

- Change role: Win-Win-Win or a Threat?
- Pros
 - Licensee is responsible & funds are fully protected
 - Gives a option to start-up businesses that want to be compliant
 - Encourages safe and secure innovation
 - Allows Licensees to recoup costs of maintaining licenses
- Cons
 - Could appear to be “Rent-a-License”
 - Licensees may not fully appreciate the additional responsibilities arising out of these arrangements
 - Creates confusion for regulators/examiners
 - “Tail wagging dog”?

Some State responses:

- Washington – A Licensee cannot appoint an authorized delegate in Washington if the authorized delegate does not have a physical location in WA.
- Texas - “Supervisory Memorandum” prohibits any authorized delegate relationship unless the authorized delegate is in the same business as the licensed money transmitter
- Virginia & Michigan – Licensees can only Prepaid Reload Services to their existing authorized delegate networks if the Prepaid Program managers sign directly with each since Reload services are not the “*Licensee’s*” business
- Informal advice that “trend is growing” among states

Alternative Approach

- View as an opportunity to allow for payments innovation while making payments safer, and keeping States in control
- A potential “safety valve” - - reducing calls for a national licensing program
- But to work - - Licensee’s must take on significant responsibility
 - Due diligence and criminal background checks
 - Review AML and anti-fraud compliance procedures
 - Monitoring and reporting of suspicious transactions
 - Reporting of all authorized delegate relationships
 - Permissible investments and bonds cover authorized delegate transactions

Conclusion

- Dark Days for unlicensed emerging payments businesses
- Also more difficulties ahead for licensed payments businesses
- Impact on US payment innovations: calls for a single federal license

Questions?

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