State Regulators Take First Step Toward Nationwide Licensing Standards for FinTechs

Summary: In an effort to address regulatory-related challenges faced by financial technology (FinTech) companies, and to stave off a potential federal law governing money services businesses (MSB) that would preempt state laws covering such entities, seven state financial regulators—Georgia, Illinois, Kansas, Massachusetts, Tennessee, Texas, and Washington—have announced a multi-state compact that standardizes the MSB licensing/regulatory process. More states are expected to join this compact, and similar initiatives are expected to follow.

Overview: As we have covered in previous reports, one of the greatest regulatory challenges that FinTech firms face is complying with the patchwork of state licensing and regulatory requirements that can vary greatly by state. The requirements for MSBs are no different. To date, FinTechs that provide services such as money transmission, stored value, payment instruments, virtual currency, currency exchange, and check cashing, among others, have struggled to determine if and where they need an MSB license and what their corresponding regulatory obligations might be. FinTech firms have also expressed longstanding concerns about the cost and time associated with having to separately secure licenses in multiple states.

In response to these concerns, the Conference of State Bank Supervisors (CSBS)—the nationwide organization of financial regulators from all fifty (50) states and several US territories—recently announced that it would begin working toward a fully integrated 50-state licensing and supervision system for FinTechs, entitled “Vision 2020.” In addition to establishing a FinTech Industry Advisory Panel to provide input on challenges faced by FinTechs in a multi-state regulatory regime, CSBS has launched a redesign of the Nationwide Multistate Licensing System (NMLS), which many state financial regulators use for licensing applications and supervision purposes. The next step in CSBS’s integration plan is to harmonize state requirements by establishing best practices and model approaches for licensing and supervision—a goal that, as of last month, has already begun to bear fruit.

In February, seven states announced that they have entered into a compact to harmonize their MSB requirements. Quite significantly, if any one of the seven states reviews and approves of key requirements pertaining to a FinTech’s MSB license—including the firm’s IT, cybersecurity, business plan, background check, and compliance with the federal Bank Secrecy Act—the other participating states will accept that state’s
findings. State regulators expect the compact to significantly streamline the MSB licensing process within the seven participating states.

What it means and what to expect: The seven states that have entered into the multistate MSB licensing project are expected to launch the program as a pilot later this spring, and state regulators expect additional states to sign-on to the compact in the coming months, with the ultimate goal of having a 50-state program in place.

Through Vision 2020, state regulators have signaled their recognition that the adoption of FinTech solutions continues to gain momentum among consumers and is here to stay, as evidenced by the fact that FinTech firms moved roughly one-third—more than $189 billion—of MSB transmissions in the first two quarters of 2017 alone. Backed by data such as this, state regulators appear increasingly keen to minimize the burden of regulatory licensing and supervision on not only FinTech’s, but also on state resources. Vision 2020 makes clear that state regulators understand that regulatory regimes must modernize alongside the financial services industry, and as additional data findings are revealed, state regulators will likely look to implement additional multistate licensing and supervisory regimes to meet the demands of keeping up with these developments.

Of course, the move by state regulators is also a defensive one, of sorts: there has been increasing speculation that certain MSBs support adoption of a federal law governing MSBs that would preempt state MSB licensing laws and create a single standard for MSB regulation. To date, no such federal legislation has been proposed. However, as the possibility of such a federal law is discussed more seriously in financial services policy circles, state regulators appear to be responding to increasing calls for greater regulatory harmonization for MSBs. The compact described above and the Vision 2020 initiative appear to be an outgrowth of that response.

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