Principles of Money Transmission Regulation

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WILMERHALE

WILMER CUTLER PICKERING HALE AND DORR LLP

Agenda

- Why Care about Money Transmission Regulation?
- Licensing and Registration Regimes
- What is a Money Transmitter, Anyway?
- Why is Money Transmission Regulated?
- Money Transmission Analysis
- Compliance Strategies

Why Care about Money Transmission Regulation?

Who might be a money transmitter?

- Any nonbank that handles customer funds, other than as payment for the nonbank's goods and services
- If it's fintech, it may be money transmission

What happens to unlicensed/unregistered money transmitters?

- They get away with it under the radar (maybe)
- They get shut down
- They pay fines
- They go to jail (possible but unlikely, 18 USC 1960)

Licensing and Registration Regimes

Dual Regulation

- Federal: Anti-money laundering – Registration & ongoing compliance
- State: Consumer Protection – Licensing & ongoing compliance

Licensing is No Fun

- It's confusing and onerous
- It's expensive
- It takes a long time

Other covered activities can include, e.g., prepaid, check cashing, foreign exchange

Who Has Multi-state Licensing?

What Is a Money Transmitter, Anyway?

In general, a money transmitter is a person who:

- Accepts funds from one person, and
- Delivers or otherwise transmits funds to another person or the same person at a different location, by any means

But there are many exceptions:

- Agents
- Banks
- Agents of Banks
- Payment Processors
- Agents of Payees
- Integral Activities

Why is Money Transmission Regulated?

Regulation addresses four key risks

- *Bad customers* – The company's service is used for money laundering or sanctions evasion.
- *Bad security* – Funds are stolen by outside parties. The company is solvent, means well, but fails to protect customer funds.
- *Bad companies* – Funds are misappropriated or lost by the company.
- *Broke companies* – Funds are lost through insolvency

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Money Transmission Analysis

How to determine whether a company is a money transmitter

1) Look at the funds flow
2) Look at the funds flow again
3) Look at the bank accounts
4) Look at the policy motivations

Compliance Strategies

Questions?

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Life After *Crawford v. LVNV Funding:* Proofs of Claim and the FDCPA

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ABA Business Law Spring Meeting 2016

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Crawford v. LVNV Funding, LLC

"A deluge has swept through U.S. bankruptcy courts of late. Consumer debt buyers —armed with hundreds of delinquent accounts purchased from creditors — are filing proofs of claim on debts deemed unenforceable under state statutes of limitations."

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Debtor owed debt to furniture company

Account charged off in 1999

LVNV's affiliate acquired account in 2001

Last transaction on account occurred in October 2001

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Alabama limitations = three years

Debt became unenforceable in October 2004

Debtor filed Chapter 13 in 2008

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LVNV filed a proof of claim to collect the debt

The trustee did not object to the proof of claim

LVNV received payment from the trustee

Four years later, in 2012, debtor objected to POC as unenforceable

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Applied least sophisticated consumer standard

Is it "unfair" or "unconscionable"?

A debtor's memory may have faded

A debtor may no longer have records documenting the debt

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"In bankruptcy, the limitations period provides a bright line for debt collectors and consumer debtors, signifying a time when the debtor's right to be free of stale claims comes to prevail over a creditor's right to legally enforce the debt."

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"Similar to the filing of a stale lawsuit, a debt collector's filing of a time-barred proof of claim creates the misleading impression to the debtor that the debt collector can legally enforce the debt."

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"Further, filing objections to time-barred claims consumes energy and resources in a debtor's bankruptcy case, just as filing a limitations defense does in state court."

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Under least sophisticated consumer standard, filing of a time-barred POC was:

unfair,

unconscionable,

deceptive,

and misleading within the scope of the FDCPA

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On remand, LVNV asserted limitations to FDCPA claim

Crawford asserted that FDCPA claim operated as compulsory counterclaim or was a claim in recoupment.

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Bankruptcy court said claim was subject to 1-year SOL

There is no recoupment savings clause in FDCPA mirroring the clause in TILA

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Issues Raised by *Crawford*

Is filing a proof of claim an act of debt collection?

Is filing a proof of claim the equivalent to filing a state court collection action?

Is a debtor in the bankruptcy context really the "least sophisticated consumer?"

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Circuit Courts of Appeal

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U.S. District Courts

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Bankruptcy Courts

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CFPB & Data Security
In re *Dwolla*

Shara Chang

April 6, 2016
ABA Business Law Section
Spring Meeting

Affirm

In re *Dwolla*, Inc.

- On March 2, 2016, CFPB announced its enforcement action against online payment platform Dwolla, Inc. (“Dwolla”) for “deceiving consumers about its data security practices and the safety of its online payment system”
  - Fined $100,000 in civil money penalties
  - Ordered to fix security practices and cure misrepresentations in data security practices
- CFPB never alleged a data breach occurred

Consumers entrust digital payment companies with significant amounts of sensitive personal information. With data breaches becoming commonplace and more consumers using these online payment systems, the risk to consumers is growing. It is crucial that companies put systems in place to protect this information and accurately inform consumers about their data security practices.

- CFPB Director Richard Corday on the *Dwolla* Consent Order

Key Takeaways

- CFPB's first data security enforcement action
- Sharpened regulatory focus on fintech
- Dodd-Frank Act transferred to the CFPB rulemaking, supervision, and enforcement authority of the privacy provisions of the GLBA, but not the data security requirements
  - Could the FTC have brought the same enforcement action?
  - Any coordination with the FTC?
- UDAAP extends to data security claims … and more!

UDAAP

- UDAAP Definitions under Dodd-Frank
  - **“Unfair”**
    - Causes “substantial” consumer injury
    - Is not outweighed by consumer or competitive benefits, and
    - Could not have been reasonably avoided
  - **“Deceptive”**
    - Representation, omission, or practice that:
      - Is likely to mislead a consumer acting reasonably
      - Is material in impacting consumer decisions and behavior
  - **“Abusive”**
    - Materially interferes with consumer understanding, or
    - Takes unreasonable advantage of consumer’s
      - Lack of understanding
      - Inability to self-protect
      - Reliance on the provider to act in the consumer’s best interest

CFPB's Findings & Conclusions

- Representations about Dwolla's encryption and data-security measures include:
  - "All information is securely encrypted and stored"
  - "100% of your info is securely encrypted and stored"
  - Dwolla encrypts "all sensitive information that exists on its servers"
  - Dwolla "encrypt[s] data in transit and at rest"
  - Dwolla encrypts data "utilizing the same standards required by the federal government"
  - Dwolla's data-security practices "exceed industry standards" or "surpass industry standards"
  - Dwolla is "PCI compliant"

CFPB's Findings & Conclusions

- CFPB alleged Dwolla failed to:
  - Use appropriate measures to identify reasonably foreseeable security risks
    - No written data-security plan for the first ~4 years of operation
  - Ensure that employees who have access to or handle consumer information received adequate training and guidance about security risks
  - Use encryption technologies to properly safeguard sensitive consumer information
    - Consumer personal information includes: first and last names; mailing addresses; 4-digit PINs; social security numbers; bank account information; digital images of consumer ID
  - Practice secure software development, particularly with regard to consumer-facing applications developed at an affiliate website

Dwolla Consent Order Requirements

The Consent Order, which will remain in effect for 5 years, requires Dwolla to:

- Implement appropriate data security policies and procedures
- Implement a comprehensive data security plan
- Conduct data security risk assessments twice annually
- Designate a qualified individual to be accountable for data security issues
- Implement an appropriate and precise method of consumer identity authentication before any funds transfer
- Adopt specific procedures for the selection and retention of service providers capable of maintaining security practices
- Conduct regular and mandatory employee data security training
- Obtain an annual data security audit from an independent, third party acceptable to the CFPB's Enforcement Director

QUESTIONS?