

REGULATING THE NEW CASHLESS WORLD

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ABSTRACT

Internet and mobile payment volume is growing exponentially. From established technology giants like Amazon, Google, and PayPal to relative newcomers like Square and LevelUp, Internet and mobile payment systems are changing the face of modern commerce. Consumers and merchants have embraced cashless payment options like mobile wallets and mobile credit card readers. Unfortunately, existing laws and regulations lag behind. State money transmitter laws, once a virtual unknown, have become a source of frustration and confusion. These statutes historically regulated money transfer businesses like Western Union with an eye toward preventing consumer harm. The plain language of such statutes, however, purports to broadly regulate the receipt of money or monetary value for the purpose of transmitting it to another place or location by any means. As such, an array of business activity, from bike messengers to app stores, is potentially implicated.

In the absence of clear guidance and inconsistent state enforcement, a number of services that accept customer payments on behalf of merchants, in connection with the sale of the merchant's goods and services, have struggled with the question of whether their unique business models are subject to regulation. Some companies, such as Square, have apparently decided that licensing and compliance with state money transmitter laws is not required for the operation of their payment business. However, doing so comes with very real risks. The Illinois Department of Financial & Professional Regulations recently issued a cease and desist order for alleged violations of the state's Transmitters of Money Act. As a result, those that do not take preventative action to comply may face regulatory enforcement action if a state regulatory agency subsequently decides that a particular business activity falls within the scope of the statute. In the face of such uncertainty, Amazon, Google, and PayPal have all become licensed

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money transmitters under state law. Even Facebook has become licensed in advance of launching a payments product in order to mitigate the risk of sanctions as the development of their payments product continues to evolve. While established companies can afford to comply, the licensing and regulatory compliance costs exist as a barrier to entry for payment start-ups and may stifle continued innovation if left unsettled.

This Article takes the first in-depth look at the intersection of technology and consumer protection in the context of new and emerging payment systems and seeks to resolve the apparent tension between the two, suggesting a framework for modernizing state money transmitter laws to accommodate new technology, innovative business models, and the realities of a cashless world while still respecting the statutory purpose of consumer protection where appropriate. As a result, the framework proposed in this Article will facilitate continued development of new payment services, which benefits merchant sellers (both small and large) by providing them with more efficient and sometimes cheaper options for accepting payments from customers without increasing the risk of harm to the consumer customers who rely on such services to make payments.

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INTRODUCTION

As merchants and consumers increasingly adopt and embrace technological innovations to the traditional channels through which they engage in commerce, established laws and regulatory frameworks must be reassessed for both relevance and applicability. Nowhere is this more evident than with respect to new and emerging forms of payment. The way that consumers pay for goods and services has undergone transformational change in recent years. Where paper-based payment systems such as cash and checks once ruled, and credit/debit cards and stored value cards now dominate, Internet and mobile payments threaten to take over.¹

1. See Colin C. Richard, *Dodd-Frank, International Remittances, and Mobile Banking: The Federal Reserve's Role in Enabling International Economic Development*, 105 NW. U. L. REV. COLLOQUY 248, 253–54 (2011); *A Summary of the Roundtable Discussion on Stored-Value Cards and Other Prepaid Products*, FEDERAL RESERVE (Jan. 12, 2005), <http://www.federalreserve.gov/paymentsystems/storedvalue/default.htm>; Peter Cohan, *Will Square's Starbucks Deal Spark the End of Cash?*, FORBES (Aug. 8, 2012, 8:24 AM), <http://www.forbes.com/sites/petercohan/2012/08/08/will->

The use of Internet and mobile payment technologies to conclude purchase and sale transactions has become commonplace and is expected to grow exponentially. Some forecasts predict that global business to consumer e-commerce sales will top \$1.25 trillion per year by 2013, noting that annual business to consumer e-commerce sales increased by 20% from 2010 to 2011.² Goldman Sachs predicts similar growth, finding that global e-commerce sales will reach \$963 billion by 2013, with an annual growth rate of 19.4%.³ Mobile commerce will likely see a similar upward trajectory with analysts anticipating that mobile payment transactions will grow nearly four-fold over the next five years to more than \$1.3 trillion.⁴

Capitalizing on these changing commerce habits, payment industry innovators have introduced a number of new services that facilitate the acceptance of Internet and mobile payments by merchants when selling their goods or services. Instead of developing the capability to accept Internet and mobile payments directly, merchants may now select from a host of third-party service providers. Those who provide some form of Internet or mobile payment services to merchants include giants such as Amazon,⁵ Google,⁶ Isis (an alliance between T-Mobile, AT&T and Verizon

squares-starbucks-deal-spark-the-end-of-cash/; Suzanne McGee, *End Of Cash: Six Things That Could Take The Place Of Paper Money*, HUFFINGTON POST (May 8, 2012, 11:44 PM), http://www.huffingtonpost.com/2012/05/08/end-of-cash-replacing-money_n_1500885.html#slide=more225166; Deirdre Van Dyk, *The End of Cash*, TIME (Jan. 9, 2012), at 48; D. Steven White, *Predicting U.S. E-Commerce Growth Through 2013*, ALL THINGS MARKETING (Dec. 2, 2011), <http://dstevenwhite.com/2011/12/02/predicting-u-s-e-commerce-growth-through-2013/> (last visited Sept. 30, 2013); D. Steven White, *U.S. E-Commerce Growth 2000-2009*, ALL THINGS MARKETING (Aug. 20, 2010), <http://dstevenwhite.com/2010/08/20/u-s-e-commerce-growth-2000-2009/> (discussing e-commerce growth from 2000 to 2009); David Wolman, *Time for Cash to Cash Out?*, WALL ST. J. (Feb. 11, 2012), <http://online.wsj.com/article/SB10001424052970204136404577209241595751130.html>.

2. Abdul Montaqim, *Global e-Commerce Sales Will Top \$1.25 Trillion by 2013*, INTERNET RETAILER (June 14, 2012, 10:19 AM), <http://www.internetretailer.com/2012/06/14/global-e-commerce-sales-will-top-125-trillion-2013>.

3. Don Davis, *Global e-Commerce Sales Head to the \$1 Trillion Mark*, INTERNET RETAILER (Jan. 4, 2011, 3:02 PM), <http://www.internetretailer.com/2011/01/04/global-e-commerce-sales-head-1-trillion-mark>.

4. Press Release, Juniper Research, *Mobile Payments to Reach \$1.3tn Annually by 2017, as NFC and Physical Goods Sales Accelerate* (Aug. 15, 2012), *available at* <http://juniperresearch.com/viewpressrelease.php?pr=332>.

5. *See* AMAZON PAYMENTS, <http://www.amazonservices.com/services/amazon-payments.html> (last visited Sept. 30, 2013) (describing how sellers can use Amazon Payments to accept payments on the seller's website); AMAZON SERVICES, <http://www.amazonservices.com/selling-on-amazon/how-it-works.htm> (last visited Sept. 30, 2013) (describing how sellers can sell on Amazon.com); *see also infra* Part II.C.

6. *See Google Checkout*, GOOGLE, <http://checkout.google.com/seller/what.html?hl=en&gl=GB> (last visited Sept. 30, 2013) (describing how merchants can use Google Checkout to process payments); *Google Wallet*, GOOGLE, <http://www.google.com/wallet/how-it-works/> (last visited Sept. 30, 2013) (describing how Google Wallet can be used to make online and in-store payments); *see also infra* Part II.C.

Wireless),⁷ Merchant Customer Exchange (a mobile commerce platform created by leading U.S. retailers including BestBuy, Target Corp., and Wal-Mart Stores),⁸ PayPal,⁹ Apple,¹⁰ and Android.¹¹ In addition, upstarts such as Square¹² and LevelUp¹³ clutter the market.¹⁴

While the business model, functionality, and scope of each payment service can vary greatly, the service provider generally offers a mechanism through which it acts on behalf of a merchant in accepting an Internet or mobile payment from a buyer of the merchant's goods or services and facilitates the transfer of the payment to the merchant. Online marketplaces,¹⁵ application stores,¹⁶ checkout or shopping cart services,¹⁷

7. See ISIS, <http://isisforbusiness.com/> (last visited Sept. 30, 2013) (describing how merchants can use Isis to accept mobile payments); see also *infra* Part II.C.

8. See Press Release, Merch. Customer Exch., Leading Retailers Form Merch. Customer Exch. to Deliver Mobile Wallet (Aug. 15, 2013), available at <http://www.mcx.com/images/mcx-press-081512.pdf> (describing a mobile wallet service that can be accepted as a form of payment by participating merchants); see also *infra* Part II.C.

9. See *However You Do Business, PayPal Gets You Paid*, PAYPAL, https://www.paypal.com/webapps/mpp/merchant?intl_cid-main:mktg:personal:sell:overview/business-solutions-x-link (last visited Sept. 30, 2013) (describing the business solutions that PayPal offers for accepting credit card payments); *Sell Overview*, PAYPAL, <https://www.paypal.com/webapps/mpp/selling-with-paypal> (last visited Sept. 30, 2013) (describing how PayPal can be used to accept payments online and in person); see also *infra* Part II.C.

10. See *iOS Developer Program*, APPLE, <https://developer.apple.com/programs/ios/> (last visited Feb. 13, 2013) (describing how app developers can distribute apps via the Apple App Store); see also *infra* Part II.C.

11. See *Developers*, ANDROID, <http://developer.android.com/distribute/googleplay/about/monetizing.html> (last visited Sept. 30, 2013) (discussing how app developers can distribute their apps via the Google Play app store); see also *infra* Part II.C.

12. See *Payments and Receipts in Square Wallet*, SQUARE, <https://squareup.com/help/en-us/article/3906-square-wallet-payments-and-receipts> (last visited Sept. 30, 2013) (describing how Square Wallets facilitates acceptance of mobile payments); *Swipe Card Payments with the Square Reader*, SQUARE, <https://squareup.com/help/en-us/article/5174-swipe-card-payments-with-the-square-reader> (last visited Sept. 30, 2013) (describing the app and mobile card reader that is provided to merchants for purposes allowing a merchant to use their own mobile device to accept credit and debit card payments); see also *infra* Part II.C.

13. See LEVELUP, <https://www.thelevelup.com/how-it-works> (last visited Sept. 30, 2013) (describing how LevelUp facilitates the acceptance of mobile payments); see also *infra* Part II.C.

14. See Margaret Cashill, *Mobile Payment Services Proliferate, Business Owners Save*, TAMPA BAY BUSINESS JOURNAL (Nov. 30, 2012), <http://www.bizjournals.com/tampabay/print-edition/2012/11/30/mobile-payment-services-proliferate.html?page=all> (discussing the proliferation of mobile payment systems); Thomas F. Dapp, *The Future of (Mobile) Payments: New (Online) Players Competing with Banks*, DEUTSCHE BANK (Dec. 20, 2012), [http://www.dbresearch.com/PROD/DBR_INTERNET_EN-PROD/PROD000000000298950/The+future+of+\(mobile\)+payments%3A+New+\(online\)+players+competing+with+banks.PDF](http://www.dbresearch.com/PROD/DBR_INTERNET_EN-PROD/PROD000000000298950/The+future+of+(mobile)+payments%3A+New+(online)+players+competing+with+banks.PDF) (Sept. 30, 2013) (discussing the rise of mobile and online payments and the growth of non-bank competitors in the provision of payment and financial-related services); Leena Rao, *The Mobile Payments Fustercluck*, TECH CRUNCH (Sep. 9, 2012), <http://techcrunch.com/2012/09/09/the-mobile-payments-fustercluck/> (noting that a new way to pay using a mobile phone seems to pop up every week).

15. Online marketplaces like the Amazon Marketplace allow independent merchants (big and small) to sell on Amazon.com. In connection with providing the sales platform, Amazon handles the payment process, receiving credit/debit card information from the buyer and settling with the merchant. See *infra* Part II.C.

mobile wallets,¹⁸ and mobile card readers¹⁹ all involve some degree of Internet or mobile payment acceptance and processing on behalf of merchant sellers. Although the customer pays the service provider (e.g., by providing credit/debit card information), the merchant is in fact the seller of record from whom the purchase is made. As such, the service provider essentially functions as a third-party intermediary who accepts Internet and/or mobile payments from a buyer on behalf of the merchant, subsequently transferring the funds to the merchant (hereinafter referred to generally as “payment services”).

The sheer number of Internet and mobile payment options and speed of adoption highlights the conundrum: how can any legal and regulatory regime possibly keep up with the pace of technological advances and adoption? Internet and mobile payment methods have revolutionized modern commerce, but the law understandably lags behind. As a component part of establishing a comprehensive and consistent regulatory regime for new and merging payment systems, this Article suggests that existing laws, such as state money transmitter laws, must be reexamined in light of technological advances and changes in consumer behavior to clearly define the scope of their applicability to new business models.

Money transmitter laws are essentially “safety and soundness” laws aimed at protecting consumers from suffering losses, and have traditionally governed money transfers services like Western Union. However, the sweeping language of such statutes and the lack of clearly applicable exemptions threaten to subsume a number of innovative business models, including many new and emerging payment systems. Given the burden and expense of state-specific licensing and compliance requirements, this has created real problems for potentially regulated businesses who must struggle to ascertain whether money transmitter laws extend to their activities. In short, businesses are faced with a choice between two

16. App stores depend on independent developers to create apps that are made available for purchase on hosted app stores. The service provider receives payments from those who purchase apps and subsequently settles with the developer/seller. *See infra* Part II.C.

17. Payment services, such as PayPal and Amazon Payments, allow merchants to accept credit/debit cards via the Internet by placing a “check out” button or “shopping cart” on the merchant’s website. Although the buyer visits the merchant’s website instead of a third-party marketplace, the payment process is operated by a third-party service provider who subsequently settles with the merchant. *See infra* Part II.C.

18. Mobile wallets, such as Google Wallet, Isis, Square, LevelUp and Merchant Customer Exchange, allow a consumer to use a smartphone like a credit/debit card. The consumer’s credit/debit card information is stored by the service provider, and in-store purchases can be made by waving the phone in front of a scanner provided to the merchant, which transfers the payment card information with the service provider, subsequently settling with the merchant. *See infra* Part II.C.

19. Payment services like Square and PayPal provide merchants with a mobile credit/debit card reader and a mobile application that allows the merchant to use its own mobile device to accept credit/debit card payments. The service provider receives the payment card information, initiates the payment process, and facilitates settlement with the merchant. *See infra* Part II.C.

undesirable alternatives²⁰: forgo state licensing and risk sanction from a state regulator²¹ or bear the potentially unnecessary cost of compliance.²² While established companies like Amazon, Google, PayPal, and even Facebook have the resources to mitigate the risk by becoming licensed, the cost for start-ups may be prohibitive. Accordingly, the unsettled legal and regulatory environment has the potential to disincentivize the continued development of desirable payment innovations.

This Article attempts to reconcile the apparent conflict between the statutory purpose of consumer protection and the desire for advancements that promote commerce by: (1) setting forth an approach for recasting state money transmitter laws in light of technological advances while respecting the consumer protection purpose of such statutes; and (2) supporting the adoption of an exemption that is tailored to differentiate new payment services in light of their relative risk of consumer loss—extending regulation where appropriate and exempting innovations where little risk exists.

Part I of this Article overviews the laws and regulations that presently govern the business of money transmission. In the absence of an explicit statutory exemption, state money transmitter laws purport to regulate any activity that falls within the statutory definition of “money transmission”²³

20. Complaint at 3–4, *Think Computer Corp. v. Dwolla, Inc. et al.*, No. 5:13-cv-02054-EJD (N.D. Cal. May 6, 2013), available at <http://digitalcommons.law.scu.edu/cgi/viewcontent.cgi?article=1379&context=historical> (describing the dilemma facing payments providers in determining the applicability of state money transmitter laws to new technology along with the inconsistent enforcement of such laws by state regulators).

21. See, e.g., Cease and Desist Order, No. 13 CC 208, State of Ill. Dep’t of Fin. & Prof’l Regulation, Div. of Fin. Inst., available at <http://www.idfpr.com/dfi/CCD/Discipline/SquarePersonifiedCDOOrder13CC208.pdf> (noting the penalties and fines imposed on Square for violations of the Illinois money transmitter law); Letter from Aaron Greenspan, Think Computer Corp. President & CEO, to Roger Dickinson, Cal. State Assemb., Comm. on Banking & Fin. Chairman (Nov. 7, 2012) [hereinafter Letter from Greenspan], available at <https://s.facecash.com/legal/20121107.dficomment.pdf> (noting that Think Computer Corporation shut down its mobile payment product after threats of incarceration from California regulators based on alleged violations of the California money transmitter law); Ken Yeung, *Square Served Cease and Desist Order in Illinois for Violating the Transmitters of Money Act*, NEXT WEB (Mar. 1, 2013, 7:37 PM), <http://thenextweb.com/insider/2013/03/01/square-receives-cease-and-desist-from-illinois-regulators/> (noting that the Illinois Department of Financial & Professional Regulation recently issued Square a cease and desist order for violating the state’s money transmitter law).

22. See, e.g., Brittany Darwell, *Facebook Obtains Money Transmitter Licenses in 15 States*, INSIDE FACEBOOK (Feb. 22, 2012), <http://www.insidefacebook.com/2012/02/22/facebook-obtains-money-transmitter-licenses-in-15-states/> (last visited Oct. 1, 2013); Sean Sposito, *Facebook Fast-Tracks Its Payments Business*, AMERICAN BANKER (Feb. 21, 2012), http://www.americanbanker.com/issues/177_35/facebook-credits-money-transmitter-license-bank-regulation-1046825-1.html (noting Facebook’s election to become licensed under state money transmitter laws in anticipation of potential regulation of a developing payment product).

23. “Money transmission” is often broadly defined as the receipt of money or value for the purpose of transferring it to another person or location by any means. See *infra* Part I.A.1.

and imposes a myriad of state-specific licensing,²⁴ financial security,²⁵ examination,²⁶ recordkeeping,²⁷ and reporting requirements.²⁸

Part II of this Article illustrates how the broad definition of “money transmission” coupled with a limited list of explicit exemptions results in an uncertain regulatory environment where a host of services from bike messengers to app stores could potentially fall within the scope of regulation.²⁹

Part III of this Article explores the growing outcry about the lack of clarity and how it adversely impacts the providers of Internet and mobile payment services.³⁰ The providers of such services face an unappealing dilemma. They can obtain a license and incur the cost and expense of maintaining compliance with a patchwork of state-specific requirements (perhaps needlessly),³¹ or they can elect to forego licensing and run the risk

24. See *infra* Part I.

25. The financial security requirements generally include an obligation to provide a surety bond, which varies in amount depending on the state. See, e.g., COLO. REV. STAT. ANN. § 12-52-107(1)(a) (West 2010). In addition, licensed money transmitters must typically satisfy minimum net worth requirements and may be required to maintain minimum amounts of permissible investments. See, e.g., CONN. GEN. STAT. ANN. § 36a-603 (West 2011); D.C. CODE § 26-1004 (2001); see also *infra* Part I.A.3.

26. Depending on the state, regulators may require audits, investigate a money transmitter’s books and records or conduct an onsite examination. See, e.g., IOWA CODE ANN. § 533C.501(1) (West 2011); MD. CODE ANN., FIN. INST. §§ 12-421, 12-423, 12-424 (LexisNexis 2011); see also *infra* Part I.A.3.

27. Licensed money transmitters must generally maintain certain records for statutorily mandated periods of time. See, e.g., KY. REV. STAT. ANN. § 286.11-029 (West 2011); see also *infra* Part I.A.3.

28. Licensed money transmitters must generally file financial reports with state regulators on a regular basis and may be required to make periodic filings upon the occurrence of specified events. See, e.g., FLA. STAT. ANN. § 560.118(1) (West 2012) (requiring filing of annual financial statements and quarterly reports); *id.* § 560.126 (requiring written notice of significant events); see also *infra* Part I.A.3.

29. See *infra* Part II.

30. Concerns have been expressed over the potential application of federal and state money transmitter laws to new and emerging payment systems, including the chilling effect on innovation by start-up due to the unsettled regulatory landscape and the costs of compliance. See Letter from Greenspan, *supra* note 21; Marie Hogan, *California’s New Money Transmission Law Sweeps Up*, JOSEPH & COHEN (May 19, 2011), <http://josephandcohen.com/2011/05/californias-new-money-transmission-law-sweeps-up>; Brian J. Hurh & Peter Luce, *Regulators Emphasize Importance of Money Transmission Laws, Consumer Protection and Other Regulatory Compliance for Mobile and Other Emerging Payment Innovations*, PAYMENT LAW ADVISOR (Oct. 3, 2012), <http://www.jdsupra.com/legalnews/regulators-emphasize-importance-of-money-65722/>; James Mariani, *The California Money Transmission Act: Boon to Consumers or Bane to Innovation?*, TIMELY TECH (Sept. 26, 2012), <http://illinoisjlt.com/timelytech/?p=1> (last visited Oct. 1, 2013); Owen Thomas, *This Innovation-Killing California Law Could Get a Host Of Startups In Money Trouble*, BUSINESS INSIDER (July 11, 2012, 6:21 PM), <http://www.businessinsider.com/california-money-transmitter-act-startups-2012-7#ixzz2KW3UA2hZ>; see also *infra* Part III.

31. See *supra* note 30.

of civil and criminal penalties should a state regulator determine that their business constitutes money transmission.³²

Part IV of this Article illustrates how the statutory purpose of money transmitter laws—to protect consumers from suffering losses at the hands of non-performing money transmitters—is not served by blindly extending regulation to Internet and mobile payment systems.³³ In situations where there is no greater risk of consumer loss, such an approach is overly expansive and needlessly impinges upon commerce while wholly ignoring the evolving habits of merchants and consumers.

Part V of this Article concludes that the continued growth of Internet and mobile payments accentuates the need for legislative action and proposes that state money transmitter laws be amended to include a narrowly tailored “agent of the payee” exemption. Such an exemption would amend the definition of “money transmission” to unambiguously exclude the receipt of a payment for delivery to a merchant in connection with a sale by the merchant so long as: (1) the service is provided to or on behalf of a merchant and not directly to a consumer; (2) the service provider is acting pursuant to a written contract with the merchant; and (3) the contract and terms of service mitigate the risk of loss to the consumer by acknowledging that payment to the service provider constitutes payment to the merchant and that the merchant has no claim against the consumer for the failure of the service provider to transfer the payment to the merchant.³⁴ This approach assures that state money transmitter laws will be fittingly recast in light of technological advances and market realities while upholding the consumer protection goals of such statutes where warranted.³⁵

I. THE LEGAL AND REGULATORY LANDSCAPE OF MONEY TRANSMISSION

United States regulation of money transmission employs a dual-system of both state and federal laws. State money transmitter laws vary by jurisdiction³⁶ and focus on consumer protection concerns.³⁷ As such, state

32. See 18 U.S.C. § 1960 (2006); MD. CODE ANN., FIN. INST. §§ 12-429 to 430 (LexisNexis 2011); Letter from Greenspan, *supra* note 21.

33. See *infra* Part IV.

34. See *infra* Part V.

35. See *infra* Part V.

36. See UNIF. MONEY SERV. ACT, prefatory note, 7A U.L.A. 163–64 (2006), available at http://www.uniformlaws.org/shared/docs/money%20services/umsa_final04.pdf (noting that state laws are “extremely varied”); see also *infra* Part II.A.

37. See, e.g., CAL. FIN. CODE § 2002 (West 2013) (noting that the purpose of the statute is to protect the interests of consumers); VA. CODE ANN. § 6.2-1902(B) (2010) (“This chapter shall be construed by the Commission for the purpose of protecting, against financial loss, residents of the Commonwealth who (i) purchase money orders or (ii) give money or control of their funds or credit

money transmitter laws are essentially “safety and soundness” statutes designed to ensure that consumer funds are protected from loss.³⁸ In contrast, the Bank Secrecy Act (BSA), which regulates money transmission at the federal level, exists primarily as an anti-money laundering statute.³⁹ Despite the differing purpose, state and federal money transmitter laws both opt to define the regulated activity of “money transmission” in broad terms,⁴⁰ relying on a list of explicit statutory exemptions to narrow the scope of regulation.⁴¹ Unless an exemption applies, any person engaging in an activity that constitutes “money transmission” must be licensed under state law⁴² and comply with a host of regulatory requirements involving financial security, recordkeeping, reporting, and examination.⁴³

A. State Regulation of Money Transmission

While the statutory language varies from state to state,⁴⁴ money transmitter laws generally seek to regulate the business of receiving money (or monetary value) for the purpose of transmission to another person or location.⁴⁵ State money transmitter laws require that any person engaging in such activity obtain a license from the appropriate state regulator⁴⁶ and

into the custody of another person for transmission”); *Regulation of Money Transmitters in Texas: An Overview*, TEXAS DEP’T OF BANKING, <http://www.banking.state.tx.us/news/speeches/2004/11-10-04sp.htm#texasregulations> (noting that “the overriding focus is consumer protection”).

38. See UNIF. MONEY SERV. ACT, prefatory note, 7A U.L.A. 163–64.

39. See 31 U.S.C. § 5311 (2006); see also *FinCEN’s Mandate from Congress*, FIN. CRIMES ENFORCEMENT NETWORK, http://www.fincen.gov/statutes_regs/bsa/.

40. See, e.g., CAL. FIN. CODE § 2003(o) (West 2013); WASH. REV. CODE ANN. § 19.230.010(18) (West 1961). But see NEV. REV. STAT. ANN. §§ 671.010, 671.040(1) (LexisNexis 2009) (generally regulating the business of “receiving for transmission or transmitting money” without otherwise defining the scope of such activity).

41. See, e.g., ARIZ. REV. STAT. ANN. § 6-1203 (2007); COLO. REV. STAT. ANN. § 12-52-105 (West 2010); UNIF. MONEY SERV. ACT § 103 cmt. 1, 7A U.L.A. 184 (2006) (noting five exemptions that are typically available).

42. See, e.g., N.Y. BANKING LAW § 641(1) (McKinney 1939); WASH. REV. CODE ANN. § 19.230.030 (West 1961); UNIF. MONEY SERV. ACT § 201, 7A U.L.A. 186 (2006) (setting forth the licensing requirement).

43. See *infra* Part I.A.3.

44. While state money transmitter statutes differ from jurisdiction to jurisdiction, there have been efforts to achieve more uniformity. Recognizing that existing state regulation is “extremely varied,” the National Conference of Commissioners on Uniform State Laws has advanced the Uniform Money Services Act of 2000, which regulates money services business like money transmission. To date, only 6 states have enacted some form of the Uniform act. See UNIF. MONEY SERV. ACT, prefatory note, 7A U.L.A. 163–64 (2006); *Legislative Fact Sheet—Money Services Act*, UNIFORM LAW COMMISSION, <http://www.uniformlaws.org/LegislativeFactSheet.aspx?title=Money%20Services%20Act>. As a result there is little uniformity amongst state money transmitter laws.

45. See, e.g., CAL. FIN. CODE § 2003(s); UNIF. MONEY SERV. ACT § 102(14), 7A U.L.A. 178 (2006).

46. See, e.g., IDAHO CODE ANN. § 26-2903(1) (2000) (requiring a license from the Director of the Idaho Department of Finance to engage in money transmission business); 205 ILL. COMP. STAT. ANN. 657/10 (West 2007) (requiring a license from the Director of the Illinois Department of Financial

comply with other requirements imposed on licensed money transmitters.⁴⁷ Unlicensed money transmission is flatly prohibited unless a valid exemption applies⁴⁸ and is punishable by both criminal and civil penalties.⁴⁹ When analyzing whether a specific activity is regulated under a state money transmitter statute the key considerations are: (1) whether the activity falls within the definition of money transmission; and (2) whether a statutory exemption exists to remove the activity from the ambit of the statute. In the absence of an applicable exemption, any activity that otherwise falls within the definition of “money transmission” is potentially subject to the scrutiny of state regulators.⁵⁰

1. *The Definition of Money Transmission Under State Law*

Most states attempt to define the scope of regulation by way of a broadly inclusive statutory definition.⁵¹ The definitions set forth in the Arizona and Maryland statutes are illustrative of the breadth that is often found. Arizona defines “transmitting money” as “the transmission of money *by any means* including . . . by payment instrument, wire, facsimile, internet or any other electronic transfer, courier or otherwise.”⁵² In Maryland, the term “money transmission” is defined as “the business of selling or issuing payment instruments or stored value devices, or receiving *money or monetary value*, for transmission to a location within or outside the United States *by any means*, including electronically or through the Internet.”⁵³

Institutions to engage in money transmission business); N.Y. BANKING LAW § 641(1) (generally requiring a license in order to engage in the business of receiving money for transmission or transmitting the same); WASH. REV. CODE ANN. § 19.230.030 (requiring a license in order to engage in the business of money transmission or to hold oneself out as providing money transmission); UNIF. MONEY SERV. ACT § 201, 7A U.L.A. 186 (setting forth the licensing requirement).

47. See *infra* Part I.A.3.

48. See, e.g., IDAHO CODE ANN. § 26-2904; 205 ILL. COMP. STAT 657/15; *Money Services Act Summary*, UNIFORM LAW COMMISSION, <http://uniformlaws.org/ActSummary.aspx?title=Money%20Services%20Act> [hereinafter *Money Services Act Summary*] (acknowledging that the act is broadly inclusive).

49. See *supra* note 32.

50. See Hurr & Luce, *supra* note 30 (“Government representatives from both civil and criminal enforcement agencies shared cautionary tales of both new and established companies that learned the hard way about the broad applicability of state money transmitter licensing laws.”); *Money Services Act Summary*, *supra* note 48.

51. See, e.g., IDAHO CODE ANN. § 26-2902(11); 205 ILL. COMP. STAT 657/5. *But see* NEV. REV. STAT. ANN. § 671.010 (LexisNexis 2009); NEV. ADMIN. CODE § 671.005–.100 (2010) (regulating the business of transmitting money or credits without providing a statutory definition or any other guidance as to the intended scope of regulation, which results in ambiguity and the possibility of the statute being narrowly or broadly construed).

52. ARIZ. REV. STAT. ANN. § 6-1201(17) (2007) (emphasis added).

53. MD. CODE ANN., FIN. INST. § 12-401(m)(1) (LexisNexis 2011) (emphasis added).

Instead of narrowly defining the types of businesses that constitute money transmitters (e.g., money transfer services directed toward consumers), the Arizona and Maryland statutes, like many other state money transmitter laws, depend on a sweeping definition that is constrained by few explicit limits.⁵⁴ The definitions do not appear to be concerned with the volume of money transmission or the method by which the transmission is accomplished.⁵⁵ In addition, the statutes do not apply solely to the transmission of money (typically defined as a medium of exchange that is authorized or adopted by the United States or a foreign government).⁵⁶ Instead, the scope has been expanded to encompass the transmission of monetary value (typically defined as a medium of exchange, whether or not redeemable in money).⁵⁷ The only explicit limitation within the definition itself is the requirement that the money transmitter provide money transmission as a business.⁵⁸ Therefore, despite definitional differences between jurisdictions,⁵⁹ money transmission arguably encompasses almost any commercial activity where money is taken from one person or place and delivered to another.⁶⁰ California state regulators have quite literally adopted such an approach, acknowledging the use of a plain language test to guide decisions on whether a particular business model or technology falls within the scope of regulation.⁶¹ Under this test, if a person takes money (or value) from person *A* and pays it to

54. See ARIZ. REV. STAT. ANN. § 6-1201(17); MD. CODE ANN., FIN. INST. § 12-401(m)(1).

55. See ARIZ. REV. STAT. ANN. § 6-1201(17); MD. CODE ANN., FIN. INST. § 12-401(m)(1). *But see* UNIF. MONEY SERV. ACT § 102(14), 7A U.L.A. 178 (2006) (defining “money transmission” broadly as “selling or issuing payment instruments, stored value, or receiving money or monetary value for transmission” but excluding any “delivery, online or telecommunications services, or network access” from its scope, which appears to exclude entities that solely provide delivery services (presumably courier or package delivery services) and entities that act as mere conduits for the transmission of data (such as internet service providers)).

56. See UNIF. MONEY SERV. ACT § 102(11), 7A U.L.A. 178 (2006).

57. See *id.* § 102(12), 7A U.L.A. 178 (2006); see also *id.* § 102, cmt. 10 (noting the expansion of the definition of money such that it is inclusive of anything that (1) serves as a medium of exchange and (2) places the customer at risk of the provider’s insolvency while the medium is outstanding).

58. See *supra* note 55.

59. See, e.g., MICH. COMP. LAWS ANN. § 487.1003(c) (West Supp. 2013) (defining “money transmission services” as “selling or issuing payment instruments or stored value devices or receiving money or monetary value for transmission”); N.J. STAT. ANN. § 17:15C-2 (West 2001) (defining “money transmitter” as “a person who engages in this State in the business of: (1) the sale or issuance of payment instruments for a fee, commission or other benefit; (2) the receipt of money for transmission or transmitting money within the United States or to locations abroad by any and all means, including but not limited to payment instrument, wire, facsimile, electronic transfer, or otherwise for a fee, commission or other benefit; or (3) the receipt of money for obligors for the purpose of paying obligors’ bills, invoices or accounts for a fee, commission or other benefit paid by the obligor”).

60. See Thomas, *supra* note 30 (discussing the use of a plain-English test by California regulators); see also *infra* Part II (providing examples of the wide range of activities and business models that may fit within the plain language definition of “money transmission”).

61. *Id.*

person *B* on behalf of person *A* then the activity is subject to regulation.⁶² A broadly inclusive construction has also been supported by the National Conference of Commissioners on Uniform State Laws (NCCUSL) in its uniform act to address money services business like money transmission.⁶³ Accordingly, money transmitter laws are not strictly limited to regulating traditional money transfer businesses like Western Union. Instead, a variety of business models from courier services to Internet and mobile payment services such as PayPal and Square could conceivably fall within the scope of regulation.

2. Exemptions from Regulation Under State Law

Given the potentially expansive scope of money transmission, each state's list of exemptions exists as the only meaningful mechanism for ensuring that a particular activity is excluded from regulation. The state-specific nature of money transmitter statutes makes generalization difficult. However, there is some minimal level of commonality.⁶⁴ State money transmitter statutes often exempt "money transmission" when conducted by certain categories of persons.⁶⁵ The most common exemptions are for: (1) the federal and state government;⁶⁶ (2) those making transfers on behalf of the government or in connection with government benefits;⁶⁷ (3) regulated banks and financial institutions;⁶⁸ (4) authorized agents or delegates of a licensed money transmitter;⁶⁹ and (5) the United States Postal Service.⁷⁰ As such, only a lucky few—usually the government⁷¹ and those operating in heavily regulated industries⁷²—will be able to take advantage of an exemption.⁷³ Exempt persons generally may engage in what would

62. *Id.*

63. *See Money Services Act Summary, supra* note 48.

64. *See* UNIF. MONEY SERV. ACT § 103, cmt. 1, 7A U.L.A. 184 (2006).

65. *See, e.g.,* N.Y. BANKING LAW § 641(1) (McKinney 1939); WASH. REV. CODE ANN. § 19.230.020 (West 1961).

66. *See, e.g.,* ARIZ. REV. STAT. ANN. § 6-1203(A)(1)–(2) (2007); COLO. REV. STAT. ANN. § 12-52-105 (West 2010); D.C. CODE § 26-1003(a)(1), (3) (2001); FLA. STAT. ANN. § 560.104(2)–(3) (West 2012).

67. *See, e.g.,* CONN. GEN. STAT. ANN. § 36a-609(4) (West 2011); D.C. CODE § 26-1003(a)(5).

68. *See, e.g.,* ARIZ. REV. STAT. ANN. § 6-1203(B)(1); COLO. REV. STAT. ANN. § 12-52-105; CONN. GEN. STAT. ANN. § 36a-609(1)–(2); D.C. CODE § 26-1003(a)(4); FLA. STAT. ANN. § 560.104(1); GA. CODE ANN. § 7-1-681 (2004).

69. *See, e.g.,* D.C. CODE § 26-1003(b); GA. CODE ANN. § 7-1-681; KY. REV. STAT. ANN. § 286.11-003(2) (LexisNexis Supp. 2010); N.Y. BANKING LAW § 641(1); WASH. REV. CODE ANN. § 19.230.030(b) (West 1961).

70. *See, e.g.,* CONN. GEN. STAT. ANN. § 36a-609(3); D.C. CODE § 26-1003(b); GA. CODE ANN. § 7-1-681.

71. *See, e.g.,* UNIF. MONEY SERV. ACT § 103(1), (2), (3), (5), 7A U.L.A. 183 (2006).

72. *See id.* § 103(4), (6), (7), (8), (10), 7A U.L.A. 184.

73. *See id.* §§ 103(1)–(10), 201, 7A U.L.A. 183–86.

otherwise be categorized as “money transmission” without a license and without complying with the regulatory requirements imposed on licensed money transmitters.⁷⁴

Perhaps recognizing the practical implications of a broadly inclusive definition coupled with a limited number of exemptions, certain states have incorporated additional exemptions. While the availability of such exemptions may be limited, they provide additional certainty by explicitly eliminating certain activities from regulation. For example, some states exempt money transmission by: (1) an incorporated telegraph or cable company so long as the money received is immediately transmitted;⁷⁵ (2) a courier service;⁷⁶ (3) an agent or authorized delegate of a person who is exempt from the statute;⁷⁷ (4) an agent of a payee (i.e., someone who is authorized by the principal to whom a payment is made to receive and transfer such payment to the principal);⁷⁸ or (5) money transmissions that are incidental to and a necessary part of a lawful business.⁷⁹

The impact of new technology on the manner in which money is transferred amongst multiple parties by way of bookkeeping entries in lieu of physically delivering a tangible form of payment has also spurred the adoption of additional exemptions. Certain states have recognized the potential for money transmitter regulations to apply in the contexts of: (1) clearing and settling credit/debit card transactions;⁸⁰ and (2) issuing stored

74. See, e.g., ARIZ. REV. STAT. ANN. § 6-1203 (2007); FLA. STAT. ANN. § 560.104 (West 2012); NEV. REV. STAT. ANN. § 671.020 (LexisNexis 2009). In some cases, only limited exemptions are available. For example, authorized agents of a licensed money transmitter are typically exempt from the licensing requirements and must comply with other regulatory requirements. See, e.g., WASH. REV. CODE ANN. §§ 19.230.120, 19.230.130–40, 19.230.180, 19.230.230–40, 19.230.290.

75. See, e.g., COLO. REV. STAT. ANN. § 12-52-105 (West 2010); NEB. REV. STAT. § 8-1003(2) (1997); NEV. REV. STAT. ANN. § 671.020(1)(c).

76. HAW. REV. STAT. ANN. § 489D-4 (LexisNexis2012) (defining “money transmission” as not applicable to courier services).

77. Some states exempt authorized delegates of an exempt person, such as a bank or agents of a licensed money transmitter from the need to apply for and obtain a license. See TEX. FIN. CODE ANN. §§ 151.003(5), 151.302(a)(2) (West 2013). As such, licensed money transmitters may conduct money transmission through authorized delegates by complying with certain additional regulatory requirements designed to ensure that the principal retains responsibility for the acts of the authorized delegate. See *id.* § 151.403. However, agents of licensed money transmitters may be precluded from further delegating to another unlicensed person. See, e.g., WASH. REV. CODE ANN. § 19.230.010(4) (“A person that is exempt from licensing . . . cannot have an authorized delegate.”).

78. See, e.g., NEV. REV. STAT. ANN. § 671.040(2) (permitting agents of a payee to engage in money transmission); N.Y. BANKING LAW § 641 (McKinney 1939) (permitting agents of a payee to engage in money transmission); OHIO REV. CODE ANN. § 1315.01(G) (West Supp. 2013) (defining the term “transmit money” as not including “transactions in which the recipient of the money or its equivalent is the . . . authorized representative of the principal in a transaction for which the money or its equivalent is received, other than the transmission of money or its equivalent”).

79. See, e.g., KAN. STAT. ANN. § 9-511 (2001).

80. These states typically exempt “operators of a payment system” but only to the extent that they provide processing, clearing, or settlement services *between entities exempt from the state’s money transmitter laws*. See, e.g., OKLA. STAT. ANN. tit. 6, § 1512(6) (West Supp. 2013); OKLA. ADMIN. CODE

value devices such as gift cards.⁸¹ To clarify the scope of regulation in these new contexts, some states have adopted limited exemptions that appear to apply where the risk of consumer loss is minimal. For example, the exemption for money transmission in connection with clearing or settling credit/debit card transactions only applies where the person transfers money between exempt persons (i.e., financial institutions) who are otherwise subject to a comprehensive regulatory regime.⁸² Likewise, the issuer of a stored-value device can only take advantage of an exemption in a closed-system where the gift card is redeemable only for goods or services from the merchant who issues the card and not in an open-system where the card is redeemable broadly at a number of different merchants.⁸³ Even so, many states have done little to address the treatment of new and emerging payment mechanisms such as stored value, electronic currency, and mobile wallets under money transmitter laws.⁸⁴

As illustrated by the foregoing, state money transmitter statutes contain state-specific nuances. However, the statutory language is often broadly worded such that they may be deemed to regulate a wide variety of business activities unless a statutory exemption applies. Statutory exemptions vary by state but only apply to a narrow set of enumerated persons, potentially leaving a great deal of activity subject to regulation.

§ 85:15-1-3(9) (2012); IOWA CODE ANN. § 533C.103 (West 2011); MICH. COMP. LAWS ANN. § 487.1004(i) (West Supp. 2013); WASH. REV. CODE ANN. § 19.230.020(9). As such, the exemption typically applies to organizations that provide clearing and settlement services, which involve the transfer of funds from one participating financial institution's bank account to another (e.g., the debiting and crediting of accounts). See UNIF. MONEY SERV. ACT, § 103, cmt. 2, 7A U.L.A. 184–85 (2006).

81. See, e.g., IND. CODE ANN. §§ 28-8-4-3.5, 28-8-4-13, 28-8-4-15, 28-8-4-19.5, 28-8-4-20(a) (West 2010); WASH. REV. CODE ANN. §§ 19.230.010(6), 19.230.020(12).

82. See *supra* note 80.

83. See *supra* note 81. For a discussion of the distinction between open-systems such as prepaid cards issued by a financial institution like Visa, MasterCard, and American Express and closed-systems such as gift cards issued by a specific retailer to be used for purchases directly from the retailer, see Philip Keitel, *The Laws, Regulations, Guidelines, and Industry Practices That Protect Consumers Who Use Gift Cards*, FED. RES. BANK OF PHIL. 2–3 (July 2008), available at <http://www.philadelphiafed.org/payment-cards-center/publications/discussion-papers/2008/D2008JulyGiftCard.pdf>. In addition to open and closed systems, there are hybrid systems of stored value such as semi-closed stored value cards that can be used at multiple merchants in a specified location—for example, a mall gift card that can be used at all retailers located in the mall. See Mark Furletti, *Prepaid Card Markets & Regulation*, FED. RES. BANK OF PHIL. 4 (Feb. 2004), available at http://www.philadelphiafed.org/payment-cards-center/publications/discussion-papers/2004/Prepaid_022004.pdf.

84. See UNIF. MONEY SERV. ACT, prefatory note, 7A U.L.A. 164 (2006) (“For the majority of States, [the Uniform Money Services Act] will provide a new approach to the treatment of stored value and electronic currency at the state level.”).

3. *Compliance Requirements Under State Law*

In the absence of an applicable exemption, state money transmitter laws purport to regulate any activity that falls within the definition of money transmission.⁸⁵ Those that engage in money transmission must apply for and obtain a license from the applicable state regulator.⁸⁶ In addition, licensed money transmitters are subjected to state-specific regulatory requirements that primarily seek to ensure the financial security of those who provide money transmitter services to consumer customers.⁸⁷ The failure to obtain a license or otherwise comply may result in both civil and criminal penalties.⁸⁸

In order to obtain a license, a prospective money transmitter must submit an application along with certain personal, business, and fitness-related information regarding the applicant and the business.⁸⁹ The state regulator generally makes the decision to grant or deny the application for a license on the basis of: (1) the application; (2) an investigation of the applicant's financial condition and responsibility, financial and business experience, competence, character, and general fitness; and (3) in some cases, an on-site examination.⁹⁰ In connection with the licensing process, the applicant must also pay various fees, which may include an application fee, an annual license fee, and the costs of regulatory assessments and investigations.⁹¹ While the process is relatively benign, the burdens and costs of obtaining licensure under state laws increase exponentially where a money transmitter must navigate the process in multiple jurisdictions (i.e., subjecting to regulation under every state licensing regime in which the person wishes to engage in the business of money transmission).⁹²

85. See Hurh & Luce, *supra* note 30 (noting that panelists at the annual Emerging Payments Systems conference “reminded participants that ‘money transmission’ is broadly defined to encompass any and all means of transmitting funds, with limited exceptions under various state and federal laws and regulations”); *Money Services Act Summary*, *supra* note 48.

86. See, e.g., IDAHO CODE ANN. § 26-2903(1) (2000); 205 ILL. COMP. STAT. ANN. 657/10 (West 2007); N.Y. BANKING LAW § 641(1) (McKinney 1939); WASH. REV. CODE ANN. § 19.230.030 (West 1961).

87. The financial security requirements generally include an obligation to provide a surety bond, which varies in amount depending on the state. See, e.g., COLO. REV. STAT. ANN. § 12-52-107(1)(a) (West 2010). In addition, licensed money transmitters must typically satisfy a state-specific minimum net worth and may also be required to maintain a minimum amount of permissible investments. See, e.g., CONN. GEN. STAT. ANN. § 36a-603 (West 2011); D.C. CODE § 26-1004 (2001).

88. See, e.g., 18 U.S.C. § 1960 (2006); MD. CODE ANN., FIN. INST. §§ 12-429, 12-430 (LexisNexis 2011).

89. See, e.g., WASH. REV. CODE ANN. § 19.230.040.

90. *Id.* § 19.230.070.

91. *Id.* § 19.230.320; see also 205 ILL. COMP. STAT. ANN. 657/45; KY. REV. STAT. ANN. § 286.11-021 (LexisNexis Supp. 2010).

92. See UNIF. MONEY SERV. ACT § 201, cmt., 3 U.L.A. 192-93 (2006) (noting that state law governs jurisdictional decisions regarding whether a person is engaging in the business of money transmission and that factors such as targeting customers in the state may be relevant).

Licensed money transmitters must also comply with regulatory requirements aimed at protecting the public by ensuring that money transmitters have sufficient resources to honor their obligations to consumer customers⁹³ and giving the state regulator sufficient supervisory power and insight into the licensee's business to identify problems and pursue enforcement actions.⁹⁴ While the specific requirements vary widely from state to state, licensed money transmitters must typically: (1) furnish a surety bond or similar security device;⁹⁵ (2) satisfy minimum net worth requirements;⁹⁶ (3) maintain minimum levels of specified types of permissible investments (e.g., government obligations and other low-risk investments);⁹⁷ (4) retain specified business records for statutorily mandated periods of time;⁹⁸ and (5) file annual and periodic reports relating to financial condition and upon the occurrence of significant events.⁹⁹ In

93. The primary purpose of requiring delivery of a surety bond (or other security), along with the imposition of minimum net worth and minimum permissible investment levels, is to ensure that the money transmitter has sufficient resources to honor its obligations to its customers. *See* UNIF. MONEY SERV. ACT § 204, cmt., 7A U.L.A. 192–93 (2006); *id.* § 207, cmts. 1–2, 7A U.L.A. 196–97.

94. *See, e.g., id.* § 605, cmt. 1, 7A U.L.A. 192 (2006).

95. *See, e.g.,* ARIZ. REV. STAT. ANN. §§ 6-1205(A), 6-1205.01 (2007) (imposing minimum bonding and net worth requirements); COLO. REV. STAT. ANN. § 12-52-107(1)(a) (West 2010) (requiring bond of \$1,000,000, which may be decreased to no less than \$250,000 based on financial condition); CONN. GEN. STAT. ANN. §§ 36a-602, 36a-604 (West 2011) (imposing minimum bonding and net worth requirements); D.C. CODE § 26-1007(a) (2001) (requiring that licensed money transmitters furnish a surety bond of \$50,000 plus \$10,000 per each additional location, not to exceed \$250,000); KAN. STAT. ANN. § 9-509(b)(2)–(3) (Supp. 2012) (requiring deposit of cash or securities with the state treasurer or an approved bank in the amount of \$200,000 which can be increased to a maximum of \$500,000 depending on financial condition, or alternatively the delivery of a surety bond in the same amount); UNIF. MONEY SERV. ACT § 204, 7A U.L.A. 192 (2006) (requiring that each prospective licensee deliver a surety bond, letter of credit or similar security device in the amount of \$50,000 plus \$10,000 for each additional location, not to exceed \$250,000, when applying for a license, and noting that the amount of security can be raised to a maximum of \$1,000,000 if necessitated by the licensee's financial condition).

96. *See, e.g.,* D.C. CODE § 26-1004 (requiring a minimum net worth, at all times, of not less than \$100,000 plus \$50,000 for each additional location or authorized delegate, not to exceed \$500,000); KAN. STAT. ANN. § 9-509(b)(1) (requiring a minimum net worth, at all times, of not less than \$250,000); UNIF. MONEY SERV. ACT § 207, 7A U.L.A. 196 (2006) (requiring that each licensee maintain a minimum net worth of at least \$25,000).

97. *See, e.g.,* CONN. GEN. STAT. ANN. § 36a-603; KY. REV. STAT. ANN. § 286.11-015(1) (requiring a licensed money transmitter to maintain minimum permissible investments of no less than the aggregate amount of all of its outstanding payment instruments).

98. *See, e.g.,* KY. REV. STAT. ANN. § 286.11-029 (requiring licensed money transmitters to maintain and preserve certain books and records for five years); MICH. COMP. LAWS ANN. § 487.1025 (West Supp. 2013) (requiring licensed money transmitters to maintain certain records for three years); UNIF. MONEY SERV. ACT § 605, 7A U.L.A. 214–15 (2006) (requiring that each licensee maintain extensive records for a period of three years).

99. *See, e.g.,* FLA. STAT. ANN. § 560.118(2)(a) (West 2012) (requiring filing of annual financial statements and quarterly reports); *id.* § 560.126 (requiring written notice of significant events); IOWA CODE ANN. § 533C.205(2) (West 2011) (requiring submission of an annual renewal report); *id.* § 533C.503 (requiring filing of quarterly reports, and additional reports upon occurrence of certain material changes and other specified events); UNIF. MONEY SERV. ACT § 206(b), 7A U.L.A. 195 (2006) (requiring that each licensee submit a renewal report, including its audited annual financial statement,

addition, licensed money transmitters must open their business up for audit and investigation by the regulatory agency overseeing compliance.¹⁰⁰ Those who fail to comply face administrative action with both criminal and civil consequences, ranging from imprisonment to monetary penalties.¹⁰¹ In addition to penalties under state law, federal laws regulating money transmission make it a crime, punishable by a monetary penalty or imprisonment, to operate as a money transmitter without complying with applicable state licensing requirements.¹⁰²

The regulatory implications of being subject to state money transmitter laws can be onerous and costly. Licensees must not only bear the direct costs of licensing and renewal, but also bear the expense of establishing a program to ensure compliance with ongoing requirements such as reporting. The state-specific nature of money transmitter laws only increases the burden of compliance.

B. Federal Regulation of Money Transmission

While the primary thrust of this Article centers on state money transmitter laws, a brief overview of federal regulation of money transmission is both enlightening and useful. Federal regulation of money transmission was enacted pursuant to the BSA.¹⁰³ The requirements of the BSA are set forth in the text of the BSA and in the implementing

or submit to an examination when requesting its annual license renewal); *id.* § 603, 7A U.L.A. 211–12 (requiring submission of reports following material changes); *id.* § 604, 7A U.L.A. 213–14 (2006) (requiring that each licensee provide the state regulator with a notice and request for approval of any proposed change in control); *id.* § 606, 7A U.L.A. 216 (requiring that each licensee file all necessary reports under federal and state money laundering laws).

100. *See, e.g.*, MD. CODE ANN., FIN. INST. §§ 12-421, 12-423, 12-424 (LexisNexis 2011) (allowing the commissioner to require an audit by a certified public accountant and permission to conduct an investigation of books and records or an on-site investigation); IOWA CODE ANN. § 533C.501(1) (West 2011) (giving the state regulator the right to conduct an annual examination); UNIF. MONEY SERV. ACT §§ 601–02, 7A U.L.A. 210–11 (2006) (granting the state regulator authority to conduct, at the licensee’s cost, an annual examination and additional examinations if the regulator believes that the licensee is engaging in unsafe or unsound practices or is otherwise violating the statute).

101. *See, e.g.*, MD. CODE ANN., FIN. INST. § 12-429 (imposing a civil penalty of up to \$1,000 for the first violation of the Maryland money transmitter law and \$5,000 for each subsequent violation); *id.* § 12-430 (classifying each knowing violation of the Maryland money transmitter law as a felony punishable by imprisonment for up to five years and a criminal fine of \$1,000 for the first violation and \$5,000 for each subsequent violation); UNIF. MONEY SERV. ACT § 803, 7A U.L.A. 224–25 (2006) (granting the state regulator the power to issue cease and desist orders); *id.* § 804, 7A U.L.A. 225 (granting the state regulator the power to enter into consent orders to resolve any matters under the Act); *id.* § 805, 7A U.L.A. 226 (granting the state regulator the authority to assess civil penalties of \$1,000 per day for each outstanding violation plus costs and attorneys fees); *id.* § 806, 7A U.L.A. 226 (imposing criminal penalties for certain intentional or knowing violations of the Act).

102. 18 U.S.C. § 1960 (2006).

103. *See* 31 U.S.C. § 5311; 31 C.F.R. § 1010.100 (2012); *see also FinCEN’s Mandate from Congress, supra* note 39.

regulations promulgated by the Financial Crimes Enforcement Network (FinCEN), a bureau of the U.S. Department of the Treasury.¹⁰⁴ The BSA seeks to regulate financial institutions and other financial businesses by requiring them to assist U.S. government agencies in detecting and preventing money laundering.¹⁰⁵ Accordingly, the purpose of the BSA is distinct from the statutory purpose of state money transmitter laws because the BSA is wholly unconcerned with protecting consumers from suffering a monetary loss. Notwithstanding the divergent statutory purpose, there are some similarities, including: (1) a broadly inclusive definition of money transmission;¹⁰⁶ (2) the requirement of registration with the proper regulatory agency;¹⁰⁷ and (3) the imposition of regulatory requirements,¹⁰⁸ including civil and criminal penalties for noncompliance.¹⁰⁹

1. *The Definition of Money Transmission Under Federal Law*

Like state money transmitter laws that require licensing, the BSA requires money transmitters to register with the Secretary of the Treasury.¹¹⁰ The regulated activity of money transmission is defined as a component part of the term “financial institution.”¹¹¹ The BSA itself simply provides that the term “financial institution” includes any “licensed sender of money or any other person who engages as a business in the transmission of funds.”¹¹² The implementing regulations of the BSA go a step further and provide that the term “financial institution” includes any money services business.¹¹³ Money transmitters are one of seven different

104. See *supra* note 103.

105. See *FinCEN's Mandate from Congress*, *supra* note 39; see also Glenn R. Simpson, *Easy Money: Expanding in an Age of Terror, Western Union Faces Scrutiny — As Fund-Transfer System Grows in Risky Parts of the World*, *U.S. Questions Oversight — How 9/11 Hijackers Got Paid*, WALL ST. J., Oct. 20, 2004, at A1, available at <http://online.wsj.com/article/SB109823529279550190.html> (discussing how Western Union's money transfer services were used to support terrorism and money laundering).

106. See 31 C.F.R. § 1010.100(ff).

107. See 31 U.S.C. § 5330 (requiring registration of all money transmitters); 31 C.F.R. § 1022.380 (requiring that all money transmitters register with FinCEN regardless of whether or not the money transmitter is already licensed with any State).

108. Due to the BSA's focus on detecting and preventing money laundering, the regulatory compliance requirements naturally focus on reporting and record keeping. See, e.g., 31 U.S.C. § 5313 (requiring submission of reports in connection with certain transactions for the payment, receipt, or transfer of United States coins, currency, or other monetary instruments); *id.* § 5326 (granting authority for the federal regulator to impose additional recordkeeping requirements).

109. See 31 U.S.C. §§ 5321–22.

110. *Id.* § 5330; see also 31 C.F.R. § 1022.380.

111. See 31 U.S.C. § 5312(a)(2)(R).

112. *Id.*

113. See 31 C.F.R. § 1010.100(t)(3).

types of money services businesses.¹¹⁴ Money transmitters are broadly defined in the implementing regulations as: (1) any person that accepts “currency, funds, or other value that substitutes for currency from one person and [transmits the same] to another location or person by any means”;¹¹⁵ or (2) “[a]ny other person engaged in the transfer of funds.”¹¹⁶ Thus, the federal definition, like most state definitions, is broadly inclusive and potentially encompasses any activity where a person accepts and then transfers the money to another place or location.¹¹⁷ While traditional money transfer businesses such as Western Union fall within this definition, a host of other business models also appear to fit within the plain language of the definition (e.g., couriers delivering money or monetary value, the delivery of payments using an Internet-based systems such as PayPal).

2. Exemptions from Regulation Under Federal Law

Given the sweeping definition of money transmission and the use of a facts-and-circumstances test to make the ultimate determination,¹¹⁸ a potentially regulated person must look to the enumerated exemptions for guidance.¹¹⁹ Like state money transmitter laws, the BSA excludes money transmission by categories of persons already subject to regulatory oversight, including banks and any person regulated by the Securities and Exchange Commission or the Commodity Futures Trading Commission.¹²⁰ However, while many state statutes have not yet modernized their money transmitter statutes to address technological advances,¹²¹ the federal regulations contain more robust exemptions.

The exemptions found in FinCEN’s implementing regulations show an understanding of the potential for money transmitter laws to implicate a host of electronic payment and delivery mechanisms. As such, the term money transmitter does not include any person who only:

114. Currency dealers or exchangers, check cashers, issuer of traveler’s checks or money orders, providers of prepaid access, money transmitters, the U.S. Postal Service, and sellers or prepaid access all constitute money services businesses under the BSA’s implementing regulations. *See* 31 C.F.R. § 1010.100(ff)(1)–(7).

115. *Id.* § 1010.100(ff)(5)(i)(A).

116. *Id.* § 1010.100(ff)(5)(i)(B).

117. *Id.* §§ 1010.100(ff)(5)(i)(A), 1010.100(ff)(5)(ii); *see also* Bank Secrecy Act Regulations; Definitions and Other Regulations Relating to Money Services Businesses, 76 Fed. Reg. 43585-01 (July 21, 2011) (codified at 31 C.F.R. pt. 1010, 1021 and 1022) (noting that there is no activity threshold applicable to money transmitters).

118. 31 C.F.R. § 1010.100(ff)(5)(ii).

119. *See id.* § 1010.100(ff)(5)(ii)(A)–(F) (enumerating exclusions to the defined term “money transmitter”); *id.* § 1010.100(ff)(8) (enumerating exclusions to the defined term “money services business”).

120. *Id.* § 1010.100(ff)(8).

121. *See* UNIF. MONEY SERV. ACT, prefatory note, 7A U.L.A. 163–64 (2006).

- (A) Provides the delivery, communication, or network access services used by a money transmitter to support money transmission services;
- (B) Acts as a payment processor to facilitate the purchase of, or payment of a bill for, a good or service through a clearance and settlement system by agreement with the creditor or seller;
- (C) Operates a clearance and settlement system or otherwise acts as an intermediary solely between BSA regulated institutions. . . .
- (D) Physically transports currency . . . or other value that substitutes for currency as a person primarily engaged in such business, such as an armored car, from one person to the same person at another location or to an account belonging to the same person at a financial institution, provided that the person engaged in physical transportation has no more than a custodial interest in the currency . . . or other value at any point during the transportation;
- (E) Provides prepaid access; or
- (F) Accepts and transmits funds only integral to the sale of goods or the provision of services, other than money transmission services, by the person who is accepting and transmitting the funds.¹²²

Thus, federal law appears to take a more progressive approach toward addressing the scope of regulation in light of technological advances in the payments industry. In doing so, federal law specifically exempts any person who simply provides a delivery mechanism that is used by a money transmitter to effectuate the acceptance and transfer of money.¹²³ As such, providing the Internet service used by a money transmitter to accept and transfer currency will not subject the internet service provider to regulation. Federal law also appears to exempt the receipt and transfer of money in certain specified situations, where the money transmission generally supports the operation of a modern payment and financial system.¹²⁴ Specifically, federal law exempts: (1) any seller who receive and transmit money in connection with facilitating the sale of their products or services;¹²⁵ (2) any third party who acts as a payment processor by accepting and transferring a payment in connection with facilitating a purchase via an agreement with the seller;¹²⁶ and (3) any provider of stored

122. 31 C.F.R. § 1010.100(ff)(5)(ii)(A)–(F).

123. *Id.* § 1010.100(ff)(5)(ii)(A).

124. *See id.* § 1010.100(ff)(5)(ii)(B)–(F).

125. *Id.* § 1010.100(ff)(5)(ii)(F).

126. *Id.* § 1010.100(ff)(5)(ii)(B).

value regardless of whether the system is open-loop or closed-loop.¹²⁷ Therefore, federal money transmitter laws have outpaced state law counterparts when it comes to incorporating exemptions to clarify the scope of regulation as applied to new payment technologies.

3. *Compliance Requirements Under Federal Law*

Absent an exemption, any person that constitutes a money transmitter under the BSA must be registered¹²⁸ and comply with additional regulatory requirements. Given the focus on detecting and preventing money laundering, the BSA foregoes regulation focused on financial security in favor of comprehensive reporting and recordkeeping obligations.¹²⁹ Reports must be filed after the occurrence of certain events.¹³⁰ Reportable events include: (1) any transaction in currency in excess of \$10,000;¹³¹ (2) any instance where currency in excess of \$10,000 is physically transported from abroad into the United States or vice versa,¹³² and (3) the occurrence of any other suspicious transaction.¹³³ Money transmitters must also comply with the recordkeeping requirements set out in Subpart D of 31 C.F.R. § 1010 by both making and maintaining appropriate records in connection with certain transactions.¹³⁴ While federal money transmitter regulation does not impose obligations to provide surety bonds and similar financial security devices or involve the burdens of compliance with differing rules across jurisdictions, federal regulation does nonetheless impose arduous recordkeeping and reporting requirements.

II. THE POTENTIALLY EXPANSIVE REACH OF REGULATION

The sweeping statutory definition of money transmission under state law and the relative lack of exemptions lead to practical problems for any person that is engaged in any activity that involves the receipt of money or a payment for transfer to another person or location. Under state law, money transmission can be reasonably interpreted as extending far beyond traditional money transfer businesses like Western Union who are primarily engaged in the business of taking possession of and delivering money on

127. *Id.* § 1010.100(ff)(5)(ii)(E).

128. *See* 31 U.S.C. § 5330 (2006); 31 C.F.R. § 1022.380.

129. *See* 31 C.F.R. § 1010.300.

130. *Id.* §§ 1010.306, 1010.310–311, 1010.320, 1010.330, 1010.340, 1010.350, 1010.360, 1010.370.

131. *Id.* §§ 1010.310–314, 1022.310–314.

132. *Id.* § 1010.340.

133. *Id.* §§ 1010.320, 1022.320.

134. *Id.* § 1010.400.

behalf of consumers.¹³⁵ While the extension of money transmitter laws to new ways of providing money transfer services (e.g., Western Union's use of the Internet to accept and transfer money on behalf of consumer customers), money transmitter laws potentially encompass everything from bike messengers delivering a check to any number of Internet and mobile payment services that take payment information from a buyer and deliver payment to the merchant seller.¹³⁶ In both cases, the service provider is taking what amounts to money or monetary value under statute (e.g., the check or the credit/debit card information) and transferring it to another person.

A. *Traditional Money Transfer Businesses*

The definition of money transmission clearly covers traditional money transfer businesses like Western Union.¹³⁷ Since there is little doubt that state money transmitter laws regulate such enterprises, money transfer businesses have historically applied for licenses and conformed to the requirements imposed by money transmitter laws.¹³⁸ Money transfer businesses like Western Union provide various money transfer services to consumer and business customers.¹³⁹ As a general matter, customers engage the money transfer business to take possession of funds, which are provided by the customer, and deliver the funds to a person designated by the customer who is located in another city, state, or country.¹⁴⁰ The money

135. See, e.g., *United States v. Cambio Exacto, S.A.*, 166 F.3d 522, 524–25 (2d Cir. 1999) (describing money transmitters in the traditional sense as an entity in the “business of sending money: collecting it from customers and, for a commission, delivering it to a designated recipient, typically in another country” and describing the process by which such transfer occurs as involving reliance “on independent agents at both ends of each transaction.” Specifically, “[c]ustomers give local agents the money they want sent; the agents then notify the money transmitter of the transaction and deposit the funds to be transferred in the transmitter’s bank account. Similarly, to physically turn over the funds to the recipient, money transmitters use entities doing business in the recipient’s vicinity. When performing that function, they are known as correspondents. To expedite the delivery process, correspondents sometimes distribute funds to the recipients before the amount actually arrives from the money transmitter.”).

136. See *infra* Part II.A–C.

137. See *About Us*, W. UNION, <http://corporate.westernunion.com/about.html> (last visited October 1, 2013) (describing the money transfer services provided by Western Union to its customers).

138. See *State Licensing*, W. UNION, <http://ir.westernunion.com/investor-relations/corporate-governance/state-licensing/default.aspx> (last visited October 1, 2013) (listing the various state money transmitter licenses that Western Union currently holds).

139. See *Business Solutions*, W. UNION, <http://business.westernunion.com/> (last visited Oct. 1, 2013) (discussing business solutions provided by Western Union); W. UNION, <http://www.westernunion.com/home> (last visited Oct. 1, 2013) (discussing consumer services provided by Western Union).

140. See *Foreign Exchange Business Solutions*, W. UNION, <http://business.westernunion.com/overview/> (last visited Oct. 1, 2013) (describing how businesses can send payments to suppliers); *Send Money Online*, WESTERN UNION, <http://www.westernunion.com/us/send-money/send-money-online.page?> (last visited Oct. 1, 2013) (describing how consumer can send

transfer business plainly receives and transfers money to another location or person as a service provider for the customer. In exchange for this service, the money transfer business is paid a fee by the customer.¹⁴¹ Thus, traditional money transfer businesses clearly fall within the scope of regulation.

Originally, money transfers were accomplished via a wire transfer through an intercontinental telegraph system, which required that a customer physically go to a telegraph office to deliver the funds for transfer.¹⁴² Likewise, the customer's designated recipient was forced to travel to a telegraph office to receive the funds.¹⁴³ While customers can still travel to a physical location to make a money transfer,¹⁴⁴ technological advances have expanded the available delivery mechanisms. Customers can now initiate a money transfer over the phone or on the Internet.¹⁴⁵ Instead of delivering physical currency, the customer provides the functional equivalent in the form of credit/debit card information or bank account information to the money transfer business, which electronically transfers the value to the customer's designated recipient.¹⁴⁶ Notwithstanding changes in the way that money transfers may be accomplished, the broadly inclusive nature of state money transmitter laws, which explicitly govern transfers by "any means," rightfully allows for the continued regulation of new ways of providing the same old money transfer services.¹⁴⁷

B. Incidental Money Transfer

While the breadth of state money transmitter laws appropriately allows for the regulation of traditional money transfer businesses along with new

money). *But see Get More from Your Billing & Payment Strategy*, W. UNION, <http://payments.westernunion.com/> (last visited Oct. 1 2013) (describing how Western Union now offers payment services to business which facilitates the receipt and delivery of payments from customers to the business).

141. *See supra* note 140; *see also Compare and Price Western Union Services*, W. UNION, <https://wumt.westernunion.com/WUCOMWEB/shoppingAreaAction.do?method=load&nextSecurePage=Y&ShoppingType=2> (last visited Oct. 1, 2013) (describing pricing for certain Western Union services).

142. *See* Salil K. Mehra, *Paradise is a Walled Garden? Trust, Antitrust, and User Dynamism*, 18 GEO. MASON L. REV. 889, 941 (2011) (discussing the development of Western Union's telegraph based money transfer system); Eric G. Roscoe, *Taxing Virtual Worlds: Can the IRS PWN You?*, 12 U. PITT. J. TECH. L. & POL'Y 1, 28 (2011) (noting that the way to wire money historically was to wire it through Western Union).

143. *See supra* note 142.

144. *Send Money in Person*, W. UNION, <http://www.westernunion.com/us/send-money-in-person> (last visited Oct. 1, 2013).

145. *See Send Money by Phone*, W. UNION, <http://www.westernunion.com/send-money-by-phone> (last visited Oct. 1, 2013); *Send Money Online*, W. UNION, <http://www.westernunion.com/send-money-online> (last visited Oct. 1, 2013).

146. *See supra* note 145.

147. *See supra* note 145.

ways of providing the same service,¹⁴⁸ the definition of “money transmission” also implicates other enterprises that may only be involved in the receipt and transfer of money as an incidental part of its primary business. For example, the U.S. Postal Service, United Parcel Service, Federal Express, couriers, bike messengers, and others are primarily involved in providing delivery services to customers. Nonetheless, customers may on occasion request delivery of packages that contain currency or other monetary value such as checks, money orders, and gift cards. Because the service provider receives remuneration for the delivery, the service could be deemed the business of receiving money for the purpose of transferring it to another person or location.¹⁴⁹ While most states exempt the U.S. Postal Service,¹⁵⁰ few states provide an exemption applicable to delivery services generally.¹⁵¹ Moreover, state money transmitter laws typically do not contain a minimum activity threshold before regulation is triggered or otherwise limit regulation to those who have actual knowledge that money is being transported.¹⁵² As such, the breadth of the statute and the lack of clearly applicable exemptions leave couriers and other delivery services that may only occasionally deliver money within the plain language of the statute’s regulatory scope. The foregoing is illustrative of the potential applicability of state money transmitter laws to business models other than the money transfer businesses that have historically been regulated.

C. *New and Emerging Payment Systems*

While the broadly inclusive nature and lack of applicable exemptions has potential implications for delivery services and other businesses that occasionally engage in money transfers, no business sector is more impacted than the burgeoning Internet and mobile payment services industry. The adoption of new technology has changed the way that consumers and businesses send and receive payments in connection with the purchase and sale of goods and services. Increasingly, commerce is shifting from a paper-based payment system reliant on cash and checks to electronic modes of payment.¹⁵³ Credit cards and debit cards have to some

148. *See supra* Part II.A.

149. *See supra* Part I.A.1.

150. *See, e.g.*, GA. CODE ANN. § 7-1-681 (2013).

151. *See, e.g.*, HAW. REV. STAT. § 489D-4 (2012).

152. *See, e.g.*, WASH. REV. CODE ANN. §§ 19.230.020, 19.230.030 (West 1961) (defining money transmission without reference to minimum activity requirements and not providing an explicit exemption for incidental money transmission).

153. *See* Robert J. Samuelson, *The Vanishing Greenback*, NEWSWEEK, June 25, 2007, at 35.

degree replaced paper currency.¹⁵⁴ Gift cards have to some degree replaced paper gift certificates.¹⁵⁵ Consumers can send electronic payments through a variety of providers over the Internet in lieu of sending a check.¹⁵⁶ The advent of mobile payment systems has also enabled the use of smartphones as a payments mechanism.¹⁵⁷ While the business models and functionalities differ, all of the following arguably involve the receipt of money or a payment by a third-party service provider for ultimate delivery to an independent seller of goods or services in connection with concluding a purchase and sale transaction: (1) the provision of stored value and gift cards; (2) the provision of payment processing services for third-party sales on a hosted marketplace like the Amazon Marketplace and various mobile application stores; (3) the provision of shopping cart or check-out functionality, such as PayPal or Google Checkout, for use by a merchant seller in connection with website sales; (4) the provision of mobile wallets, such as Google Wallet and LevelUp, that give merchant sellers the ability to accept payment information from a customer's smartphone; and (5) the provision of hardware and related mobile payment processing services, such as Square and LevelUp, which give merchants the ability to use their own smartphone to accept credit/debit card payments. While some states have started to address the scope of money transmitter laws with respect to stored value,¹⁵⁸ few states have adopted exemptions applicable to new Internet and mobile payment systems, leaving the question of scope undefined and such services potentially subject to regulation.¹⁵⁹

1. *Stored Value and Gift Cards*

Given the potential costs of regulation as a licensed money transmitter, providers of stored value were quick to raise concerns about the lack of

154. See Catherine New, *Cash Dying as Credit Card Payments Predicted to Grow in Volume: Report*, HUFFINGTON POST (June 7, 2012), http://www.huffingtonpost.com/2012/06/07/credit-card-payments-growth_n_1575417.html.

155. See FEDERAL RESERVE, *supra* note 1 (discussing prepaid stored value as a replacement for paper-based payment instruments).

156. See *infra* Part II.C.2–3.

157. See *infra* Part II.C.4–5.

158. See, e.g., WASH. REV. CODE ANN. §§ 19.230.010(6), 19.230.020(12) (West 1961) (providing a limited exemption for stored value). *But see* NEV. REV. STAT. ANN. §§ 671.010, 671.040(1) (LexisNexis 2009) (regulating the issuance and sale of checks and the receipt of money transmission without any explicit mention of applicability to stored value).

159. In promulgating the Uniform Money Services Act, NCCUSL noted that for many states, the uniform act would “provide a new approach to the treatment of stored value and electronic currency at the state level.” See UNIF. MONEY SERV. ACT, prefatory note, 7A U.L.A. 163–64 (2006). Even in states that have adopted the uniform act, technology continues to outpace regulation. The uniform act was drafted in 2004 and while it clarifies, to some degree, the treatment of stored value and internet payments, the question of applicability to newer business models such as mobile payments remains unclear. *Id.*

clarity regarding whether state money transmitter statutes actually applied to prepaid products.¹⁶⁰ The issuer of a gift card, for example, receives money from the person purchasing the gift card. An accounting of the amount paid is then loaded onto the gift card and stored electronically, which allows the holder to use the card to make purchases from any merchant who will accept it as a form of payment. As such, the issuer of the card could be construed as engaging in money transmission by receiving money from the person purchasing the card for the purpose of providing a mechanism (the gift card) that transfers money when the card is used to make a purchase from another place or location.

Because of confusion in the marketplace about whether issuers of stored value were required to become licensed money transmitters, a number of states attempted to clarify the question. States that have addressed the question generally exempt issuers of stored value in a “closed-loop” system where a merchant issues a card that can only be redeemed for goods or services sold by the merchant issuing the gift card (e.g., a gift card issued by Wal-Mart that can only be used to make purchases from Wal-Mart).¹⁶¹ In contrast, stored value in an “open-loop” system can be used to make purchases at many different merchants (e.g., prepaid debit cards issued by Visa that can be used at any merchant who accepts Visa or a mall gift card that can be used at any merchant located in the mall).¹⁶² Although exemptions for issuers of stored value are not available in all states,¹⁶³ it appears that the issuers of “closed loop” stored value may be exempt in certain jurisdictions while issuers of “open loop” remain potentially subject to regulation.¹⁶⁴

160. See FEDERAL RESERVE, *supra* note 1.

161. See, e.g. ARIZ. REV. STAT. ANN. § 6-1201(11), (13) (2007) (excluding instruments redeemable by the issuer in merchandise or services from regulation); CONN. GEN. STAT. ANN. § 36a-596(1), (7), (14) (West 2011); D.C. CODE § 26-1001(5), (10), (12) (2001); FLA. STAT. ANN. § 560.103(11), (15) (West 2012); HAW. REV. STAT. § 489D-4 (2012); IDAHO CODE ANN. § 26-2902(11), (13) (2000); 205 ILL. COMP. STAT. ANN. § 657/5 (West 2007); IND. CODE ANN. § 28-8-4-3.5, 13, 15, 19.5 (West 2010); IOWA CODE ANN. § 533C.102(15), (17) (West 2011); KAN. STAT. ANN. § 9-508(c), (e), (g), (j) (Supp. 2012); KY. REV. STAT. ANN. § 286.11-003(7), (16), (22), (28) (LexisNexis Supp. 2010); ME. REV. STAT. ANN. tit. 32, § 6102(10), (12) (1999); MD. CODE ANN., FIN. INST. § 12-401(l), (n), (p) (LexisNexis 2011); MICH. COMP. LAWS ANN. § 487.1003(c), (e), (i) (West Supp. 2013); MINN. STAT. ANN. § 53B.03(07), (13), (15) (West 1946); N.H. REV. STAT. ANN. §§ 399-G:1(IX), (XIV), 399-G:4 (LexisNexis 2011). *But see* LA. REV. STAT. ANN. § 6:1032(5) (2005) (regulating the sale and issuance of stored value without any exclusions).

162. See Eniola Akindemowo, *Contract, Deposit or E-Value? Reconsidering Stored Value Products for a Modernized Payments Framework*, 7 DEPAUL BUS. & COM. L.J. 275, 281 (2009).

163. See *supra* note 161.

164. *Id.*

2. *Online Marketplaces and App Stores*

While states have started to address the question of whether state money transmitter laws regulate stored value, much less progress has been made toward modernizing such statutes to account for online marketplaces and mobile applications.¹⁶⁵ Money transmitter regulation is potentially implicated when a person: (1) hosts an online marketplace or mobile application store where merchants gather to sell their products; and (2) provides payment processing services to the merchants in connection with sales made. Such a service arguably falls within the scope of money transmitter regulation because the service provider is receiving credit/debit card payment information from customers who wish to make a purchase and subsequently facilitates delivery of the payment to the merchant selling the product.¹⁶⁶

For example, the Amazon Marketplace is a hosted site where merchants congregate to peddle their wares on Amazon.com¹⁶⁷ to over 4 million unique daily visitors.¹⁶⁸ Amazon is not the seller, but instead acts as a service provider to facilitate sales by independent merchants. The merchant agrees to pay Amazon a fee, which may include a monthly subscription fee, a referral fee equal to a percentage of the sale price, and for certain types of products, a fixed fee per item.¹⁶⁹ In exchange, Amazon allows the merchant to sell on Amazon.com and handles all of the payment processing and settlement for the merchant's sales.¹⁷⁰ In doing so, Amazon acts on behalf of the merchant, accepting payments from the merchant's customers (usually via a credit or debit card), and subsequently settling with the merchant for all sales made through the marketplace by paying the merchant an amount equal to the purchase price less any applicable fees.¹⁷¹ Thus, the providers of online marketplaces like the Amazon Marketplace

165. See *supra* note 159.

166. See e.g., MD. CODE ANN., FIN. INST. § 12-401(l).

167. *Sell on Amazon*, AMAZON, <http://www.amazonservices.com/content/sell-on-amazon.htm?ld=AZSOAMakeM#!how-it-works> (last visited Sept. 30, 2013); see also Allison Howen, *Getting Started Selling on Amazon*, WEBSITE MAGAZINE (Jan. 30, 2012), <http://www.websitemagazine.com/content/blogs/posts/archive/2012/01/30/getting-started-selling-with-amazon.aspx>; Kelly K. Spors, *How to Sell on Amazon and eBay*, N.Y. TIMES (Dec. 2, 2009), http://www.nytimes.com/2009/12/03/business/smallbusiness/03marketplaces.html?pagewanted=all&_moc.semityn.www.

168. WEBSITE STATISTICS, <http://stats.website.org/amazon.com> (last visited Sept. 30, 2013).

169. *Start Selling Online—Fast*, AMAZON, <http://www.amazonservices.com/sell-on-amazon/media-fees.htm> (last visited Oct. 1, 2013).

170. See *Sell on Amazon*, AMAZON SERVICES, http://www.amazonservices.com/content/sell-on-amazon.htm/ref=footer_soa?ld=AZFSSOA (last visited Oct. 1, 2013).

171. See *Sell on Amazon: Frequently Asked Questions*, AMAZON, <http://www.amazonservices.com/selling-on-amazon/faq.htm> (last visited Aug. 28, 2013) (noting that Amazon settles with the merchant every 14 days and describing the pricing options available for sellers who wish to sell on Amazon).

arguably accept money in the form of payment card information from the customer for the purpose of delivering to another place or location—to the banks processing the transaction and ultimately to the merchant.

Mobile application stores are similarly susceptible to being covered by the plain language of state money transmitter laws. While Apple, Android, Samsung, T-Mobile, and many others manufacture and sell smartphones on different mobile platforms, they often rely on independent software developers to create apps for use on those smartphones.¹⁷² Everything from games like Angry Birds to photo sharing apps like Instagram is sold via various online and mobile app stores specific to a particular mobile platform like Apple's iOS.¹⁷³ Customers who wish to buy an app pay (usually via credit/debit card or acceptance of a charge to the customer's monthly phone bill) the operator of the app store (e.g., Apple).¹⁷⁴ After receiving payment from the buyer, the app store operator settles with each developer by paying them the purchase price for all of the apps that have been sold minus any applicable transaction fees owed.¹⁷⁵ Like the operator of an online marketplace, the app store operator could be construed as an intermediary who receives payment from buyers on behalf of the developer-seller in connection with the sale of the app, ultimately transferring such payment to the developer-seller. Therefore, like online marketplaces, the activities of app store operators may satisfy the technical definition of money transmission under state law. While such an outcome may seem patently ridiculous in what could be analogous to a reseller/distributor scenario, the application of the broadly inclusive statute and the plain language test advanced by some regulators highlights the potentially wide-ranging types of business models that may be impacted.

172. See David Streitfeld, *As Boom Lures App Creators, Tough Part Is Making a Living*, N.Y. TIMES (Nov. 17, 2012), http://www.nytimes.com/2012/11/18/business/as-boom-lures-app-creators-tough-part-is-making-a-living.html?pagewanted=all&_r=0 (describing how independent developers create and distribute apps); Jenna Wortham, *The iPhone Gold Rush*, N.Y. TIMES (Apr. 3, 2009), <http://www.nytimes.com/2009/04/05/fashion/05iphone.html?pagewanted=all> (describing the successful development and distribution of the iShoot app by Ethan Nicholas, an independent app developer); see also *Android Developers*, ANDROID, <http://developer.android.com/index.html> (last visited Sep. 3, 2013) (providing information to independent developers who wish to design apps for Android).

173. See Doug Aamoth, *50 Best iPhone Apps 2012*, TIME (Feb. 8, 2012), http://techland.time.com/2012/02/15/50-best-iphone-apps-2012/#slide/all/?&_suid=1360964955591021777601781511185; see also Joanna Sibilla Taatjes, Note, *Downloading Minimum Contacts: The Propriety of Exercising Personal Jurisdiction Based on Smartphone Apps*, 45 CONN. L. REV. 357, 361–62 (2012) (noting that apps are downloaded from an app store hosted by the maker of the smartphone).

174. See, e.g., ANDROID, *supra* note 11 (describing payment options for customers who wish to buy apps).

175. See, e.g., *Android Developer—Transaction Fees*, GOOGLE PLAY, http://support.google.com/googleplay/android-developer/answer/1112622?hl=en&ref_topic=15867 (last visited Aug. 28, 2013) (providing for monthly payouts and noting that the developer receives 70% with the remaining 30% of the purchase price going to the distribution partner and to pay operating fees).

3. *Shopping Carts and Checkout Services*

States have also neglected to update money transmitter laws to clarify the scope of regulation with respect to third-party service providers who operate the checkout and payment process for a merchant website.¹⁷⁶ Even though a customer may visit the merchant's website instead of a hosted marketplace, money transmitter regulation is potentially implicated where a third party such as PayPal,¹⁷⁷ Google,¹⁷⁸ or Amazon¹⁷⁹ operates the "shopping cart" or "check out" function for the merchant website, or where the merchant directs the customer to pay using a third-party service.¹⁸⁰ In such situations, the service provider (not the merchant) receives and processes the customer's payment in connection with ultimately facilitating the transfer of the payment to the merchant seller.

Services such as PayPal, Google Checkout, and Checkout by Amazon allow merchants to integrate a shopping cart or checkout function with the merchant's website so that a customer can make a payment directly from the merchant's website.¹⁸¹ To make a purchase, customers typically initiate payment by selecting a button on the merchant's website, which directs the customer to provide payment information to the service provider to conclude the purchase.¹⁸² As such, the service provider accepts the payment from the buyer on behalf of the merchant, subsequently transferring the payment to the merchant less any applicable fees.¹⁸³ In addition, many service providers simply give merchants the ability to send invoices and direct customers to make a payment through the service provider (e.g., a seller on eBay directing the winning bidder to pay through PayPal).¹⁸⁴ Given the broadly inclusive definition of "money transmission," checkout services and merchant-facing payment services offered by PayPal, Amazon, Google and others like them could all reasonably be interpreted as falling within the ambit of regulation unless a valid exemption applies.

176. See *supra* Part II.A.1–2.

177. See *Merchant Services*, PAYPAL, <https://www.paypal.com/us/webapps/mpp/merchant> (last visited Sept. 30, 2013).

178. See *Google Checkout*, GOOGLE, <https://checkout.google.com/seller/integrate.html> (last visited Sept. 30, 2013).

179. See *Checkout by Amazon*, AMAZON, <https://payments.amazon.com/sd/ui/sd/ui/business/cba> (last visited Sept. 30, 2013); *Viewing Orders*, AMAZON, <https://payments.amazon.com/sd/ui/sd/ui/helpTab/Checkout-by-Amazon/Managing-Orders/Viewing-Orders> (last visited Sept. 30, 2013).

180. See *Free Invoice Template*, PAYPAL, <https://www.paypal.com/webapps/mpp/free-invoice-template> (last visited Sep. 3, 2013) (allowing sellers to send electronic invoices to customers requesting payment via PayPal); *How to Sell Online*, PAYPAL, <https://www.paypal.com/webapps/mpp/how-to-sell-online> (last visited Sept. 30, 2013).

181. See *supra* notes 177–179.

182. See, e.g., *Checkout by Amazon*, AMAZON, *supra* note 179 (illustrating the payment process).

183. *Id.*

184. See *How to Sell Online*, PAYPAL *supra* note 180.

4. *Mobile Wallets and Mobile Payment*

Like the payment innovations discussed above, mobile wallets and other mobile payment platforms, which allow consumers to use their mobile devices to make payments, could be construed as money transmission. Where a third party provides the application that enables a customer's mobile device to store payment information and the hardware that allows a merchant to accept a customer payment via the mobile device, money transmission regulation is potentially implicated because a third party arguably receives the payment and facilitates transfer of the payment to the merchant-seller.

Some examples of mobile commerce platforms that may constitute money transmission under state law include Google Wallet,¹⁸⁵ Isis,¹⁸⁶ Square Wallet,¹⁸⁷ and LevelUp.¹⁸⁸ In addition, Merchant Customer Exchange is in the process of developing a merchant-owned mobile payment platform for participating merchants.¹⁸⁹ While the business models differ, each mobile payment platform essentially allows a participating merchant to accept payment from a customer's enabled mobile device. When making a purchase, the customer simply uses his or her smartphone to transmit the credit/debit card information to an in-store terminal or scanner.¹⁹⁰ In each case, the operator of the mobile payment platform

185. See *Google Wallet*, GOOGLE, *supra* note 6.

186. See Olga Kharif & Scott Moritz, *Isis Mobile-Payment System to Debut in September After Delays*, BLOOMBERG (Aug. 28, 2012, 2:00 PM), <http://www.bloomberg.com/news/2012-08-28/isis-mobile-payment-system-to-debut-in-september-after-delays.html>; *Learn how to Pay and Save with Isis*, ISIS, <http://www.paywithisis.com/how.html> (last visited Sept. 27, 2013) (describing how Isis allows a phone to be used for payment). At present, only certain merchants in Austin, TX and Salt Lake City, UT are capable of accepting in-store payments via Isis. See Kharif & Moritz, *supra*.

187. See *Square Wallet*, SQUARE, <https://squareup.com/wallet> (last visited Oct. 1, 2013) (describing the functionality of Square as a mobile payment service); Willy Staley, *Starbucks and Square Announce Partnership: But Will Mobile Wallets Work Outside Coffee Shops?*, MY BANK TRACKER (Aug. 8, 2012), <http://webcache.googleusercontent.com/search?q=cache:http://www.mybanktracker.com/news/2012/08/08/starbucks-square-announce-partnership-mobile-wallets-work-coffee-shops/>.

188. See Brian X. Chen, *LevelUp Tries Dropping the Transaction Fee for Mobile Payments*, N.Y. TIMES BITS BLOG (Jul. 12, 2012, 9:00 AM), <http://bits.blogs.nytimes.com/2012/07/12/levelup-zero-scvngr/>; LEVELUP, <https://www.thelevelup.com/> (describing LevelUp's mobile payment app).

189. See Juhi Arora, *Merchant Customers Exchange: Wal-Mart, Target, 7-Eleven, Other Big Retailers May Take to Mobile Payments*, HUFFINGTON POST (Aug. 15, 2012, 9:09 AM), http://www.huffingtonpost.com/2012/08/15/merchant-customers-exchange_n_1777791.html; MERCHANT CUSTOMER EXCHANGE, <http://www.mcx.com/> (last visited Sept. 15, 2013); Jenn Webb, *Commerce Weekly: More Brands Throw in with Merchant Customer Exchange*, O'REILLY (Oct. 4, 2012), <http://radar.oreilly.com/2012/10/merchant-customer-exchange-lemon-qr-codes.html>.

190. See, e.g., Mark Hachman, *Isis Carrier Venture Signs Payment Deals with Visa, MasterCard, Others*, PCMAG.COM (Jul. 19, 2011, 1:49 PM), <http://www.pcmag.com/article2/0,2817,2388712,00.asp> (describing Isis' use of an NFC terminal to obtain payment information from the customer's phone); *Google Wallet*, GOOGLE, <http://www.google.com/wallet/shop-in-stores/> (last visited Sept. 27, 2013) (describing Google Wallet's use of an NFC terminal to obtain payment information from the customer's phone); Olga Kharif, *AT&T-Verizon-T Mobile Sets \$100 Million for Google Fight: Tech*, BLOOMBERG

could be deemed to be receiving money in the form of payment information from the buyer for the sole purpose of delivering it to the merchant seller.

5. *Mobile Card Readers*

One final innovative payment business model deserves mention due to the relative speed of its acceptance in the marketplace and its potential for falling within the scope of money transmitter regulation. The advent of mobile credit/debit card readers has allowed merchants to eschew the terminals provided by the credit card associations in favor of a scanner attached to the merchant's mobile device, which allows the merchant to swipe a customer's credit/debit card for payment.¹⁹¹ Such devices along with the related apps effectively allow a merchant to transform its mobile device into a cash register.¹⁹² Examples include Square, Inc.'s card reader, Square Register (launched in 2010 by Twitter co-founder Jack Dorsey and Jim McKelvey),¹⁹³ and PayPal's more recent introduction of the PayPal Here card reader.¹⁹⁴ Both services arguably involve the receipt of money from a buyer in the form of credit/debit card information for the purpose of payment processing and ultimately the transfer of such funds to the merchant making a sale. Like many of the other payment systems discussed above, Square Register and PayPal Here operate as a kind of third-party intermediary that receives and delivers the purchase price in connection with a purchase and sale transaction between an independent buyer and

BUSINESSWEEK (Aug. 29, 2011), <http://www.businessweek.com/news/2011-08-29/at-t-verizon-t-mobile-sets-100-million-for-google-fight-tech.html>; LEVELUP, *supra* note 13 (describing LevelUp's use of a unique code and scanner system to transfer payment information); Staley, *supra* note 187 (discussing Square Wallet's use of GPS technology to transmit payment information).

191. See *Paypal Here*, PAYPAL, <https://www.paypal-promo.com/here/#welcome> (last visited Sept. 15, 2013) (describing the PayPal Here scanner and app); *Square Reader*, SQUARE, <https://squareup.com/reader> (last visited Aug. 28, 2013); *Square Register*, SQUARE, <https://squareup.com/register> (last visited Sept. 15, 2013) (describing the Square Register scanner and app).

192. See *supra* note 190.

193. Courtney Boyd Myers, *Square Nearing \$1 Billion in Processed Payments Since Launch*, THE NEXT WEB (May 25, 2011, 5:53 PM), <http://thenextweb.com/gadgets/2011/05/25/square-nearing-1-billion-in-processed-payments-since-launch>; Eric Savitz, *Jack Dorsey: Leadership Secrets of Twitter and Square*, FORBES (Oct. 17, 2012, 9:00 AM), <http://www.forbes.com/sites/ericsavitz/2012/10/17/jack-dorsey-the-leadership-secrets-of-twitter-and-square/3/>.

194. See Cliff Kuang, *PayPal Launches PayPal Here, a Competitor to Square Designed by Yves Behar*, FAST COMPANY (Mar. 15, 2012, 9:15 PM), <http://www.fastcodesign.com/1669277/paypal-launches-paypal-here-a-competitor-to-square-designed-by-yves-behar#1> (noting that PayPal Here was announced on March 15, 2012); *Paypal Here*, PAYPAL, <https://www.paypal.com/webapps/mpp/credit-card-reader> (last visited Sept. 15, 2013); Emily Price, *PayPal Takes on Square, Launches 'PayPal Here' Credit Card Reader*, MASHABLE (Mar. 15, 2012), <http://mashable.com/2012/03/15/paypal-takes-on-square-launches-paypal-here-credit-card-reader/>.

seller. Thus, in the absence of clearly applicable exemptions, the service could be deemed money transmission under state law.

III. THE ADVERSE IMPACT OF UNCERTAINTY ON THE PAYMENT INDUSTRY

Uncertainty abounds regarding the scope of regulation under state money transmitter laws because of the broadly inclusive definition of what constitutes money transmission and the existence of few statutory exemptions.¹⁹⁵ As discussed above, a host of activities other than traditional money transfer services potentially falls within the plain language of regulation.¹⁹⁶

While some states have recognized the need for re-evaluation and clarification of money transmitter laws in light of innovations such as stored value,¹⁹⁷ far less certainty exists for the providers of other new and emerging payment services.¹⁹⁸ Nonetheless, the rise of Internet and mobile payment services evokes similar questions and calls for increased clarity.¹⁹⁹ In the absence of certainty, those who provide such services face increased transaction costs. As a result, the unsettled legal and regulatory framework has the potential to stifle ongoing payment innovation.

A. Transaction Costs

The uncertain scope of regulation needlessly increases the search and information costs of any person that currently provides a potentially regulated service or wishes to bring one to market. At present, any person that receives money or monetary value and transfers that money or monetary value to another person or location must evaluate whether his or her actions constitute money transmission under differing state laws.²⁰⁰ An array of Internet and mobile payment services currently in widespread use and those that are still in development effectively involve the receipt of money by person *A* (a service provider) from person *B* (a consumer) for the

195. See Mariani, *supra* note 30; Hurh & Luce, *supra* note 30; Thomas, *supra* note 30.

196. See *supra* Part II.

197. See *supra* Part II.C.

198. See *supra* Part II.C.

199. In addition to the outcry over the lack of certainty and consistency in the application of state money transmitter laws to Internet and mobile payment products, it should be noted that some have challenged the constitutionality of such state statutes. See Complaint at 4, *Think Computer Corp. v. Venchiarutti*, No. CV 11-05496 HRL, 2011 WL 7941050, at *4 (N.D. Cal. Nov. 14, 2011), available at ia600805.us.archive.org/15/items/gov.uscourts.cand.247574/gov.uscourts.cand.247574.1.0.pdf (challenging the constitutionality of the 2010 California Money Transmission Act). While questions of constitutionality are beyond the scope of this Article, the wide-ranging impact of state money transmitter laws on a system of modern commerce utilizing Internet and mobile payments is highlighted by the Think Computer Corporation lawsuit.

200. See Hogan, *supra* note 30; Mariani, *supra* note 30.

purpose of transferring it to person C (e.g., a seller).²⁰¹ Given the lack of clearly applicable exemptions in each state,²⁰² potentially regulated payment service providers are left to navigate an ambiguous legal and regulatory environment when determining whether they are subject to money transmitter laws and perhaps more importantly whether a state regulator enforcing the statute will interpret the scope similarly.²⁰³ As such, potentially regulated payment service providers must wrestle with several wholly undesirable options—either: (1) obtain a money transmitter license and bear the cost of implementing a regulatory compliance program to mitigate the risk of potential regulation and penalties for noncompliance;²⁰⁴ (2) forego licensing and risk the possibility of penalties in the event that a regulator ultimately deems that the person is in fact a money transmitter,²⁰⁵ or (3) stop development or provision of any potentially regulated activity until greater certainty exists.²⁰⁶ Furthermore, the lack of consistency between jurisdictions compounds the problem. Those that operate in multiple states must engage in the same futile exercise of attempting to discern the applicability of each state-specific regulatory regime, including any available exemptions. In the end, it is the potentially regulated person

201. See *supra* Part I; see also CAL. FIN. CODE § 2003(o) (West 2013) (broadly defining money transmission); Thomas, *supra* note 30 (discussing the use of a plain-English test).

202. See *supra* Part II.

203. See Mariani, *supra* note 30; Andrea Lee Negroni, *Risky Business: State Regulation of Money Transmitters*, CLEAR NEWS (Spring 2003), http://www.goodwinprocter.com/~media/Files/Publications/Attorney%20Articles/2003/Risky_Business_State_Regulation_of_Money_Transmitters.ashx (describing PayPal's struggle with money transmission regulation, evolving from an assumption that their business model was unregulated to obtaining state money transmitter licenses in numerous jurisdictions); Thomas, *supra* note 30.

204. See Sean Sposito, *Facebook Fast-Tracks Its Payments Business*, AMERICAN BANKER (Feb. 21, 2012, 3:09 PM), http://www.americanbanker.com/issues/177_35/facebook-credits-money-transmitter-license-bank-regulation-1046825-1.html (noting that Facebook has recently become licensed under several state money transmitter laws). Even though Facebook has obtained licenses, uncertainty remains regarding the applicability of money transmitter laws to Facebook's evolving payments product. See Brittany Darwell, *Facebook Obtains Money Transmitter Licenses in 15 States*, INSIDE FACEBOOK (Feb. 22, 2012), <http://www.insidefacebook.com/2012/02/22/facebook-obtains-money-transmitter-licenses-in-15-states> (Facebook's S-1 filing contains the following statement: "Depending on how our Payments product evolves, we may be subject to a variety of laws and regulations . . . including those governing money transmission, gift cards and other prepaid access instruments, electronic funds transfers, anti-money laundering, counter-terrorist financing, gambling, banking and lending, and import and export restrictions. In some jurisdictions, the application or interpretation of these laws and regulations is not clear.").

205. See Think Computer Corp., *supra* note 20, at 16–17 (discussing its decision to shut down a mobile payment system in light of threats of incarceration by the Department of Financial Institutions for operating without a license); see also Hurh & Luce, *supra* note 30 (Regulators warned conference participants of "both new and established companies that learned the hard way about the broad applicability of state money transmitter licensing laws.").

206. See Mariani, *supra* note 30 (concluding that startups may be dissuaded from innovating in light of the unsettled legal environment and potential costs of regulation); Thomas, *supra* note 30 (noting the chilling effect of broad money transmitter laws on innovation).

that bears the risk of the imprecise and ambiguous nature of state money transmitter laws.

The following examples show how potentially regulated persons can opt to deal with the uncertain scope of state money transmitter laws. PayPal long struggled with the question of money transmitter licensing,²⁰⁷ but ultimately became licensed under state law.²⁰⁸ Other companies such as Facebook have also opted to become licensed in anticipation of offering payment products that may evolve in a way so as to fall within the potentially sweeping scope of money transmitter laws.²⁰⁹ Those that mistakenly determine that their business model does not constitute money transmission or who are not aware of the money transmitter regulation can face significant risk. The case of Think Computer Corporation's ("Think") FaceCash mobile payment system is illustrative. Think operated the system until it was forced to shut down due to the California Department of Financial Institution's threatened enforcement actions and penalties, including incarceration.²¹⁰ Think claims that it shut down the business because of its inability to secure the information necessary to apply for a license, highlighting a perception that state regulatory discretion in the license application process results in inconsistent results for applicants.²¹¹ Most recently, Square's payment service was scrutinized by the Illinois Department of Financial and Professional Regulation, which issued a cease and desist order alleging violations of the state's money transmitter law.²¹² Despite the potentially broad application of money transmitter laws, the foregoing instances of regulatory enforcement actions at the state level appear to be isolated events rather than a component part of an attempt to clearly define the scope of such laws and consistently enforce regulatory requirements either at the state level or nationally.

As evidenced by the foregoing examples, state money transmitter laws increase transaction costs by virtue of an unsettled legal and regulatory

207. See Negroni, *supra* note 203.

208. *Paypal State Licenses*, PAYPAL, https://www.paypal-media.com/state_licenses.cfm (last visited Sept. 30, 2013); see also MISS. DEP'T OF BANKING, CONSUMER ACTIVE COMPANIES WITH DATE LAST EXAMINED—SORTED BY REGION—COMPANY TYPE: MONEY TRANSMITTER (2013), available at <http://www.dbcf.state.ms.us/documents/lists/moneytransmitter.pdf>.

209. See Darwell, *supra* note 204; Sposito, *supra* note 204.

210. See Think Computer Corp., *supra* note 20.

211. *Id.*

212. See Cease and Desist Order, No. 13 CC 208, State of Ill. Dep't of Fin. and Prof'l Regulation, Dep't of Fin. Inst., available at <http://www.idfpr.com/dfi/CCD/Discipline/SquarePersonifiedCDOrder13CC208.pdf> (noting the penalties and fines imposed on Square for violations of the Illinois money transmitter law); Ken Yeung, *Square Served Cease and Desist Order in Illinois for Violating the Transmitters of Money Act*, THE NEXT WEB (Mar. 1, 2013, 7:37 PM) <http://thenextweb.com/insider/2013/03/01/square-receives-cease-and-desist-from-illinois-regulators/> (noting that the Illinois Department of Financial & Professional Regulation recently issued Square a cease and desist order for violating the state's money transmitter law).

environment. In addition to the costs and burdens of complying with state-specific regimes, potentially regulated persons suffer from greatly increased information and search costs when trying to independently evaluate the applicability of state laws. This is due to the lack of clear guidance regarding their scope. Moreover, there are real risks for failing to “properly” interpret the statutory scope because regulatory enforcement actions and penalties may follow. In the absence of clear guidance, it is the potentially regulated that unfairly bear the burdens and risks.

B. *Stifling Innovation*

While the problems of ambiguity stemming from state money transmitters affect all persons engaging in activities that fall within the definition of money transmission, the providers of Internet and mobile payment services are particularly sensitive to the need for clarity regarding the scope of regulation. Given the exponential growth of Internet and mobile payment volume²¹³ and the stream of new payment services that may fall within the plain language of regulation,²¹⁴ it is not surprising that the payments industry, attorneys advising potentially regulated payment services, and business media have expressed concerns over the potential impact of an uncertain regulatory environment on continued development of innovative business models and called for greater clarity on the scope of state money transmitter laws.²¹⁵ Those who recognize the failings of state money transmitter laws to clearly address new payment innovations question whether the lack of clarity will stifle ongoing innovation.²¹⁶ The costs of evaluating whether compliance is necessary, the actual costs of becoming licensed and otherwise satisfying the regulatory requirements, and the risks of operating without a license may all act as a deterrent to those who wish to develop payment innovations. Large companies may have the resources needed to: (1) investigate and gather information before making an informed decision on licensing; (2) become licensed and comply with ongoing regulatory requirements; or (3) simply mitigate risk by becoming licensed.²¹⁷ However, start-ups may not have the same resources

213. See *supra* notes 2–4.

214. See *supra* Part II.

215. See *supra* note 30.

216. *Id.*; see also Thomas P. Brown, Lecturer, Berkeley Law Sch., Univ. of Cal. & Partner, Paul Hastings LLP, Before the Banking and Finance Committee, California State Assembly (March 11, 2013), available at [http://www.law.berkeley.edu/files/bclbe/TPB_Banking_Finance_Committee_Testimony_\(final\).pdf?utm_source=March+2013+Update&utm_campaign=February+2013+Update&utm_medium=email](http://www.law.berkeley.edu/files/bclbe/TPB_Banking_Finance_Committee_Testimony_(final).pdf?utm_source=March+2013+Update&utm_campaign=February+2013+Update&utm_medium=email) (discussing the California Money Transmitter Act and its effect on innovation).

217. Mariani, *supra* note 30; Thomas, *supra* note 30.

or ability to mitigate risk.²¹⁸ Accordingly, many may elect to wait until the regulatory requirements are more settled.²¹⁹ Therefore, the impact of uncertainty may disproportionately impact start-ups, acting as a barrier to entry and stifling new payment innovations.²²⁰

These concerns highlight the importance of constantly re-evaluating money transmitter laws to ensure that: (1) businesses engaging in activities potentially subject to regulation have clear guidance as to when licensing is necessary and when it is not; and (2) state regulators consistently apply regulatory oversight to only those activities, new or old, that implicate the same type of consumer protection concerns state money transmitter laws seek to mitigate.

IV. A MODERN APPROACH TO MONEY TRANSMISSION THAT RESPECTS CONSUMER PROTECTION

This Article suggests that state money transmitter laws must be recast in light of new technology in order to provide greater clarity on the scope of regulation. In doing so, the guiding principle should be to uphold the consumer protection purpose of such statutes by regulating only those activities that carry the same risk of loss as traditional money transfer services while leaving other activities unencumbered by the cost and compliance burden of becoming licensed unnecessarily.²²¹ When analyzing Internet and mobile payment services through the lens of consumer protection, it is evident that the extension of state money transmitter laws may be inappropriate in many instances.²²² Internet and mobile payment services that facilitate a purchase and sale transaction between a buyer and merchant seller appear to carry no more risk of loss to the consumer than in any direct purchase transaction between a buyer and merchant seller.²²³ As such, the goal of preventing consumer harm in the event of nonperformance by the money transmitter is not supported by the extension of regulation.²²⁴ Where there are few if any consumer protection gains, the extension of such laws to Internet and mobile payment services would result in a one-size-fits-all regulatory scheme that fails to differentiate between the unique risks of each potentially regulated activity. Such an approach fails to recognize current marketplace realities, specifically how commerce is and will continue to be conducted as technology advances and

218. Mariani, *supra* note 30; Thomas, *supra* note 30.

219. Mariani, *supra* note 30; Thomas, *supra* note 30.

220. Mariani, *supra* note 30; Thomas, *supra* note 30.

221. *See infra* Part IV.A–C.

222. *See infra* Part IV.A–B.

223. *See infra* Part IV.A.

224. *See infra* Part IV.B.

consumer habits change. Therefore, the extension of state money transmitter laws in the absence of a real consumer protection concern would needlessly hinder innovation to payments processes and commerce without materially advancing the statutory goals of such statutes.

A. The Unique Consumer Risks of Payment Innovations

The consumer protection purpose of state money transmitter laws is not well served by extending regulation because many payment services pose little real risk of consumer loss. Because Internet and mobile payment services typically facilitate the purchase of a product or service,²²⁵ the consumer's payment to the service provider is effectively payment to the merchant seller. As a result, the consumer is entitled to the purchased item and often takes possession of the purchased item at that time.²²⁶ Therefore, the failure of the service provider to deliver the money to the merchant will result in a merchant loss rather than a consumer loss.²²⁷ In the event of a dispute between the consumer and the merchant, additional protections are available to give aggrieved consumers avenues for redress.²²⁸ Specifically, payment service providers often provide dispute resolution procedures that supplement the protections that the credit card associations provide to cardholders where a credit/debit card is used to make the purchase.²²⁹ In short, a consumer who makes a purchase via a third-party payment service provider is at no greater risk of loss than a consumer who makes a purchase directly from the merchant.²³⁰ Because the consumer protection concerns are far less pronounced, the statutory purpose of consumer protection is not served by levying additional regulatory compliance requirements on payment services, which do not carry the same risk of consumer harm.

225. *See supra* Part II.

226. *See infra* Part IV.A.1.

227. *See* Amy Martinez, *Amazon Sellers Complain of Tied-Up Payments, Account Shutdowns*, SEATTLE TIMES (Nov. 19, 2012, 11:55 AM), http://seattletimes.com/html/business/technology/2019705292_amazonseller18.html. (describing disputes between merchants and payment service providers such as Amazon and eBay); Amy Martinez, *Small Online Merchants File Suit Against Amazon.com*, SEATTLE TIMES (Mar. 15, 2013, 1:30 PM), http://seattletimes.com/html/business/technology/2020568463_amazonsellersuitxml.html (discussing a class action suit filed by small merchants against Amazon for withholding payments from sales of merchant products and services via Amazon's marketplace). While merchants may be dissatisfied with the payment service provider, it appears that they are not inclined to pursue any claims against the consumer purchaser. This is ostensibly a tacit if not explicit acceptance that such claims are unlikely to be successful where the merchant elects to use a particular payment service provider and directs the customer to make a purchase using such service. In those instances, common sense would indicate that the customer should not be liable for what amounts to be a dispute between the merchant and its service provider.

228. *See infra* Part IV.A.2.

229. *See infra* Part IV.A.2.

230. *See infra* Part IV.A.

1. *Differentiating Risk*

Unlike traditional money transfer businesses that act on behalf of consumer customers in delivering money, consumers face far less risk where the money transfer is a component part of a purchase transaction. With money transfer businesses like Western Union, consumers contracted directly with the service provider, and the service provider was paid by the customer to act on behalf of the consumer in ensuring safe delivery of the customer's money.²³¹ In such situations, state regulators have a legitimate interest in protecting consumers from being defrauded and suffering monetary losses in the event that the money transfer business fails to follow through on its promise to deliver the consumer's money.²³² If left unregulated, insufficiently capitalized businesses without the ability to reliably perform could cause consumer losses. Moreover, those with nefarious intentions could take money for delivery along with any associated fees without any intention of actually performing. Where a service provider does not perform, the consumer will lose the funds trusted to the service provider and might have little ability to locate the funds or otherwise seek a remedy. In such circumstances, consumer protection is an appropriate regulatory concern, and money transmitter laws ably function to reduce the risk of loss by requiring a license from the state, compliance with minimum net worth requirements, and delivery of surety bonds.²³³ Therefore, the imposition of state money transmitter regulations is entirely appropriate where there is a real risk of consumer losses.

In contrast, where the service provider contracts with a merchant to accept customer payments and deliver such payments to the merchant, there is much less consumer risk because the merchant engaging the service provider bears the risk of nonperformance.²³⁴ Instead of contracting with a consumer to provide delivery services on behalf of the consumer, a payment service provider enters into a relationship with a merchant seller and agrees to accept and process customer payments on behalf of the merchant.²³⁵ Here, the payment service provider to merchant relationship is

231. See Negroni, *supra* note 203 (describing the origins of money transmitters as stemming from the early 1900s and the desire of immigrants to have a means of sending money to their native countries).

232. See, e.g., VA. CODE ANN. § 6.2-1902 (formerly cited as § 6.1-371 (2010)) (effective July 1, 2013).

233. See *supra* Part I.A.3.

234. See *supra* note 227.

235. See, e.g., *PayPal User Agreement*, PAYPAL, https://cms.paypal.com/us/cgi-bin/?cmd=_render-content&content_ID=ua/UserAgreement_full&locale.x=en_US (last updated Aug. 20, 2013).

that of agent and principal.²³⁶ While the rights and responsibilities between the service provider and the merchant are set by private agreement,²³⁷ the merchant could be described as engaging the service provider to accept payments on the merchant's behalf.²³⁸ To the consumer making a purchase, delivery of payment to the service provider is effectively delivery of payment to the merchant for purpose of concluding a sale.²³⁹ So long as the consumer receives the purchased item, the consumer will not suffer a loss, even if the service provider does not transfer the payment to the merchant in accordance with the terms of their agreement. Accordingly, the risk profile for a consumer making a purchase through a payment service designated by the merchant seller is wholly different than the situation where a consumer pays a money transfer service to take and deliver money on behalf of the consumer; the failure of delivery in the latter results in a direct loss to the consumer, whereas the failure of delivery in the former does not necessarily result in a loss.

Consumer customers who make in-store purchases via a mobile wallet or mobile card reader face almost no risk of loss because the consumer will often receive possession of the purchased item at the time of payment.²⁴⁰ When a well-heeled gentleman purchases an Emilio Pucci necktie from Bloomingdale's, he simply taps his Google Wallet equipped smartphone to the terminal at checkout to pay and leaves the store with the necktie in

236. See RESTATEMENT (THIRD) OF AGENCY § 1.01 (2006) (defining agency as “the fiduciary relationship that arises when one person (a ‘principal’) manifests assent to another person (an ‘agent’) that the agent shall act on the principal’s behalf and subject to the principal’s control, and the agent manifests assent or otherwise consents so to act”).

237. See PAYPAL, *supra* note 235.

238. See *supra* Part II.C.

239. For example, customers may make a purchase directly from a merchant website that utilizes a third party to accept the payment. See, e.g., *Checkout by Amazon*, AMAZON, *supra* note 179. Likewise, customers often make in-store purchases directly from a merchant who may use a third party to provide payment services such as a mobile wallet or mobile card reader. See, e.g., GOOGLE, *supra* note 190; *Square Register*, SQUARE, <https://squareup.com/register#signature> (last visited Sept. 16, 2013).

240. Even where a customer does not immediately take possession of the purchased item (i.e. delivery at a later date), the risk to the customer is no greater than if the customer paid the merchant directly with the expectation that the purchased item would be subsequently delivered. In both situations, the customer has made a payment on the expectation of future delivery and bears some risk of nonperformance by the merchant seller. The only potential for added risk is if the third-party service provider does not transfer the payment and the merchant withholds delivery as a result. However, in most cases, the credit card is not charged until the merchant has certified shipping or delivery. See *Checkout by Amazon*, AMAZON, *supra* note 179; see also *MasterCard Rules*, MASTERCARD app. B-1 (June 14, 2013), http://www.mastercard.com/us/merchant/pdf/BM-Entire_Manual_public.pdf (noting that merchants generally must not submit transactions until after the products are shipped or services performed). In addition, most merchants do not pursue claims against consumers for failure of a service provider selected by the merchant to abide by the terms of their private arrangement. See *supra* note 227.

hand.²⁴¹ Similarly, when a caffeine-craving CEO stops into Starbucks for a triple venti non-fat no foam vanilla latte, she simply orders at the register and gives her name to pay.²⁴² The GPS technology on the CEO's mobile device allows the barista to pull up the customer's name and picture to confirm the purchase, allowing the CEO to walk out with latte in hand.²⁴³ Thus, the functionality of mobile wallets such as Google Wallet, Square, Level Up, Isis, and Merchant Customer Exchange allows for the purchaser to receive the purchased item regardless of whether there is subsequently a problem with transferring the money from the service provider to the merchant seller.

The same is true of mobile card readers like Square Register and PayPal Here. If a customer wishes to purchase a shrimp po'boy from a food truck utilizing PayPal Here, the merchant simply swipes the customer's card through a card reader plugged into the phone's audio jack.²⁴⁴ The customer then signs on the screen of the smartphone to complete the purchase and can walk away happily with a meal.²⁴⁵ As evidenced by the foregoing, the failure of a service provider to perform the money transmission services or any other contractual obligations agreed upon between the service provider and the merchant is unlikely to result in an adverse impact on the consumer. In such situations, there is little risk of loss because the consumer receives the purchased item at the time of payment and does not expect anything further. Instead, the risk of loss in the event of non-performance lands squarely on the shoulders of the merchant who engages the service provider.²⁴⁶

Where a consumer makes a payment via a third-party Internet or mobile payment service, there appears to be no greater risk of loss to the consumer than if the consumer were to pay the merchant directly. As might be expected, there is an implicit (if not explicit) recognition that the buyer is entitled to the purchased item upon delivery of the payment to the service

241. See GOOGLE, *supra* note 190 (discussing the payment process and identifying Bloomingdale's as a participating merchant).

242. See SQUARE, *supra* note 187 (discussing the payment and checkout process for a hands-free transaction).

243. *Id.*

244. See PAYPAL, *supra* note 194 (noting that a merchant can also manually enter the card number or use the smartphone's camera function to scan the card).

245. *Id.*

246. See *supra* note 227. An allocation of risk that results in the merchant bearing the risk of loss is appropriate because it is the merchant (not the consumer) who elects to engage a payment service provider and has the opportunity to evaluate the ability of the service provider to perform. The merchant will also have the opportunity to contract for and pursue any private rights and remedies in accordance with the terms and conditions of the agreement between the merchant and the seller. Thus, the merchant is not wholly without recourse. Moreover, the consumer protection concerns of state money transmitter laws do not support an extension of protections to merchants.

provider.²⁴⁷ Merchants who sell on online marketplaces like the Amazon Marketplace must often confirm shipment of the purchased item before the consumer's credit/debit card is charged by the payment service provider and funds delivered to the merchant.²⁴⁸ In addition, where the purchased item is an electronic good like an app, the consumer typically obtains the ability to commence downloading the app immediately after payment.²⁴⁹ Therefore, in many cases, the consumer may receive the purchased item at the time of purchase or immediately thereafter, or at least be assured of the purchased item being shipped prior to being charged.

Even if the consumer were charged before receiving the purchased item, there would be no added risk when compared to a purchase directly from the merchant. If a consumer were to make a purchase over the Internet directly from a merchant who does not utilize a third-party payment service, the merchant would have received payment on the promise of subsequent delivery. The potential for non-delivery or delivery of a non-conforming item would still exist. With a third-party Internet or mobile payment service, the situation is no different. The consumer will have delivered payment to the service provider as directed by the merchant seller on the promise that the merchant will subsequently deliver the purchased item, leaving the consumer open to the same risk of non-delivery or nonconforming delivery. Therefore, the involvement of a third-party payment service provider does not appear to materially increase the likelihood that a consumer will suffer a loss in the event of the service provider's failure to deliver the payment to the merchant.

2. *An Added Layer of Consumer Protection*

As noted above, consumers making a payment through an Internet or mobile payment service typically receive the benefit of their bargain (i.e., the purchased item) even when the service provider fails to perform (i.e., delivery of payment to the merchant).²⁵⁰ As such, there is less consumer protection concern than in a traditional money transfer business where the failure of the money transmitter to perform would result in the loss of the funds provided by the consumer. Internet and mobile payment services also mitigate the potential risk of loss with an added layer of consumer

247. See *supra* note 227.

248. See *Checkout by Amazon*, AMAZON, *supra* note 179. While there is no law that prohibits a business from submitting a credit card transaction before delivering the purchase product or performing the purchased services, such a business practice is consistent with credit card rules and regulations that generally mandate delivery before submission. See *MasterCard Rules*, *supra* note 240, at app. B-1.

249. See Taatjes, *supra* note 173 (discussing the downloading of apps); *Visibility for Your Apps*, ANDROID, <http://developer.android.com/distribute/googleplay/about/visibility.html> (last visited Feb. 16, 2013) (discussing downloads of Android apps on the Google Play app store).

250. See *supra* Part IV.A.1.

protection. Where the consumer does not receive the purchased item or is dissatisfied with the delivered item (e.g., it is not as described or arrives damaged), the service provider may also provide a dispute resolution procedure and allow the consumer to recoup the purchase price.²⁵¹ Such dispute resolution procedures supplement the protections afforded to those who make purchases with a credit card or debit card, which may give cardholders the ability to dispute or otherwise challenge charges.²⁵² Therefore, consumers often have an additional avenue for redress that is not available in a direct purchase and sale transaction with a merchant seller, which further mitigates the risk of consumer loss.

251. See, e.g., *A-to-Z Guarantee Process*, AMAZON, <https://payments.amazon.com/sdui/sdui/helpTab/Amazon-Flexible-Payments-Service/Resolving-Disputes/-A-to-z-Guarantee-Process> (last visited Sept. 16, 2013) (describing Amazon's A-to-Z Guarantee); *Buyer Dispute Program*, AMAZON, <https://payments.amazon.com/sdui/sdui/about?nodeId=6025> (last visited Sept. 16, 2013) (describing buyer protections available from Amazon); *Transaction Disputes*, AMAZON, <https://payments.amazon.com/sdui/sdui/about?nodeId=5968> (last visited Sept. 16, 2013) (describing the Amazon transaction dispute process); *Chargeback Process*, GOOGLE, <http://support.google.com/checkout/sell/bin/answer.py?hl=en&answer=134372> (last visited Sept. 16, 2013) (describing how purchase amounts can be charged back to the merchant); *Mediation*, GOOGLE, <http://support.google.com/checkout/sell/bin/answer.py?hl=en&answer=134373> (last visited Sept. 16, 2013) (describing situations where Google will mediate disputes); *Security*, PAYPAL, <https://www.paypal.com/webapps/mpp/paypal-safety-and-security> (last visited Sept. 30, 2013) (describing PayPal's purchase protection program); *Security and Protection*, PAYPAL, <https://www.paypal.com/us/webapps/mpp/security/seller-dispute-resolution> (last visited Sept. 16, 2013) (providing guidance regarding the dispute resolution procedure for sellers); *Square Seller Agreement*, SQUARE, <https://squareup.com/legal/merchant-ua> (last updated June 25, 2013) (describing the merchant's liability for chargebacks for unauthorized or challenged transactions); see also Casey Chan, *How to Get a Refund from the App Store*, GIZMODO (Feb. 20, 2012, 5:40 PM), <http://gizmodo.com/5886683/how-to-get-a-refund-from-the-app-store> (describing how to pursue a refund from the Apple App Store notwithstanding terms providing for all sales to be final).

252. Credit card transactions benefit from greater protections under Regulation Z than are available for debit card transactions under Regulation E. See Truth in Lending (Regulation Z), 12 C.F.R. §§ 226.12(c)(1), 226.13(d)(1) (2012) (giving credit cardholders the right to: (1) assert against the card issuer "all claims (other than tort claims) and defenses arising out of the transaction and relating to the failure to resolve the dispute" with the merchant; and (2) withhold "any portion of any required payment that the consumer believes is related to the disputed amount"); see also 15 U.S.C. § 1693g (2006) (only limiting liability to debit card holders for unauthorized transactions); Ichiro Kobayashi, *Private Contracting and Business Models of Electronic Commerce*, 13 U. MIAMI BUS. L. REV. 161, 192–95 (2005) (describing protections for credit cardholders); Daniel M. Mroz, *Credit or Debit? Unauthorized Use and Consumer Liability Under Federal Consumer Protection Legislation*, 19 N. ILL. U. L. REV. 589, 603–08 (1999) (recognizing that debit cardholders benefit from less consumer protection than holders of credit cards); Neil M. Peretz, *The Single Euro Payment Area: A New Opportunity for Consumer Alternative Dispute Resolution in the European Union*, 16 MICH. ST. J. INT'L L. 573, 598–99 (2008) (noting that credit cardholders may have remedies even if the purchase was authorized); David E. Sorkin, *Payment Methods for Consumer to Consumer Online Transactions*, 35 AKRON L. REV. 1, 8 (2001) ("Paying by credit card affords much greater protection to a buyer than do other traditional payment mechanisms largely because of the credit card dispute rights provided by Federal Reserve Regulation Z."); Jane K. Winn, *Making XML Pay: Revising Existing Electronic Payments Law to Accommodate Innovation*, 53 SMU L. REV. 1477, 1491–92 (2000) (noting that Reg. Z "provides a simple and effective alternative dispute resolution process in the event the consumer is unhappy with the transaction").

PayPal,²⁵³ Amazon,²⁵⁴ and Google²⁵⁵ all have dispute resolution procedures that facilitate the resolution of problems between sellers and buyers who utilize such services to send and receive payments. When a customer is dissatisfied with the purchase, he or she has the right to initiate a process whereby the service provider will investigate and refund the money if the customer prevails.²⁵⁶ Therefore, where a seller fails to deliver a purchased item or delivers an unsatisfactory item, the consumer may have a remedy.

In addition, an aggrieved consumer who pays using a credit card or debit card has the benefit of protection under federal law²⁵⁷ and credit card association operating rules.²⁵⁸ Under Regulation Z, consumers have the right to assert claims against a credit card issuer with respect to certain disputes between the seller and a buyer in a consumer goods transaction.²⁵⁹ Accordingly, if a consumer credit cardholder has a dispute with a merchant regarding the purchase of a consumer good, he or she can assert his or her claim against the bank that issued the credit card. Such a remedy would appear to apply regardless of whether the payment was made through a service provider or directly from a merchant. Because the protections for debit card transactions under Regulation E are much more limited, a consumer using a debit card to make a payment through an Internet or mobile payment service may have greater liability if a dispute arises.²⁶⁰ However, the distinctly different treatment of credit/debit cards would appear to impact a cardholder similarly regardless of whether the payment

253. See *PayPal User Agreement*, PAYPAL, *supra* note 235, § 13 (setting forth Protections for Buyers); see also *Buyer Complaint Process*, PAYPAL, <https://www.paypal.com/cgi-bin/webscr?cmd=p/gen/buyer-complaint-outside> (last visited Oct. 1, 2013); *Paypal Security and Protection*, PAYPAL, *supra* note 251.

254. See *Amazon Payments User Agreement*, AMAZON § 3.5, <https://payments.amazon.com/sdui/sdui/helpTab/Personal-Accounts/User-Agreement-Policies/User-Agreement> (last updated July 10, 2013); see also *Buyer Dispute Program*, AMAZON, *supra* note 251.

255. See *Mediation*, GOOGLE, *supra* note 251.

256. See *supra* notes 253–255.

257. See *supra* note 252.

258. See VISA, VISA INTERNATIONAL OPERATING REGULATIONS 832–47 (Apr. 15, 2013), <http://usa.visa.com/download/merchants/visa-international-operating-regulations-main.pdf> (discussing the resolution of cardholder disputes); see also Sorkin, *supra* note 252, at 8–9 (noting that the credit card issuer can chargeback a transaction even if it does not qualify under Regulation Z).

259. Truth in Lending (Regulation Z), 12 C.F.R. §§ 226.12(c)(1), 226.13(d)(1) (2012); see also Jane Kaufman Winn, *Open Systems, Free Markets, and Regulation of Internet Commerce*, 72 TUL. L. REV. 1177, 1236 (1998).

260. Under the Electronic Funds Transfer Act, the consumer has limited liability for unauthorized transactions under Regulation E. See 15 U.S.C. § 1693g (2006). However, the definition of “unauthorized transaction” does not include authorized transactions where merchandise is not delivered or is nonconforming. See 15 U.S.C. § 1693a(12). As such, the protections available for debit cards under the EFTA are not as strong as those available for credit cards under Regulation Z. Specifically, the right to assert claims relating to a dispute with the merchant against the card issuer is much more expansive than limited protections for unauthorized transactions. See Sorkin, *supra* note 252, at 7–9.

was made directly to the merchant or if the payment was made through an Internet or mobile payment service provider.

Notwithstanding the limited remedies of Regulation Z,²⁶¹ consumers may have better luck disputing or challenging a charge directly with the credit card issuer.²⁶² Upon receipt of the complaint, the credit card issuer will temporarily credit the cardholder's account for the amount of the disputed transaction pending the results of an investigation.²⁶³ If the dispute is resolved in favor of the cardholder, the credit remains and the amount is "charged back" to the merchant.²⁶⁴ Merchants that wish to accept credit/debit cards must enter into an agreement with the credit card association (e.g., Visa or MasterCard) and agree to abide by the terms and conditions of their operating rules.²⁶⁵ Included in the terms and conditions are a number of broad chargeback rights. For example, amounts may be charged back to the merchant if: (1) the merchant fails to perform the service or deliver the merchandise; (2) the merchant delivers defective or damaged merchandise; or (3) the merchant delivers merchandise that is not as described on the transaction receipt or is otherwise unsuitable for the purpose sold.²⁶⁶

As illustrated above, a consumer that uses a credit card or debit card to make a purchase via an Internet or mobile payment service at worst benefits from the same protections that are available to all credit/debit card transactions.²⁶⁷ However, certain payment service providers may provide for added consumer protections in the form of buyer protection efforts to supplement those generally available for credit/debit card transactions.²⁶⁸ As such, it appears that in many cases there is no greater risk of consumer loss to justify or otherwise support the extension of money transmitter regulation.

261. 12 C.F.R. §§ 226.12(c)(1), 226.13(d)(1).

262. See Mroz, *supra* note 252 (describing the chargeback process); Sorkin, *supra* note 252, at 8–9; see also *Chargebacks & Dispute Resolution*, VISA, http://usa.visa.com/merchants/operations/chargebacks_dispute_resolution/index.html (last visited Sept. 27, 2013) (discussing the chargeback process generally and noting that a chargeback to the merchant is often triggered by a customer dispute); VISA, CHARGEBACK MANAGEMENT GUIDELINES FOR VISA MERCHANTS 29 (2011), <http://usa.visa.com/download/merchants/chargeback-management-guidelines-for-visa-merchants.pdf> (discussing customer dispute chargebacks).

263. See VISA, CHARGEBACK MANAGEMENT GUIDELINES FOR VISA MERCHANTS, *supra* note 262, at 29.

264. *Id.* at 32.

265. See VISA, *supra* note 252, at 397 (mandating a merchant agreement).

266. *Id.* at 831–34 (describing available chargeback rights).

267. See *supra* note 252.

268. See *supra* note 251.

B. Statutory Purpose Does Not Support Indiscriminate Extension

In the absence of additional consumer risk, the main purpose of money transmitter laws—to protect consumers—is not served by indiscriminately extending regulation to all third-party Internet and mobile payment service providers who accept and transfer payments on behalf of merchants. This Article suggests that a more nuanced approach would better serve the statutory purpose of state money transmitter laws by only extending regulation to those activities that implicate meaningful consumer protection concerns of the sort raised by traditional money transfer business. Instead of taking the one-size-fits-all approach of extending regulation to all activities that fall within the sweeping definition of money transmission, state money transmitter laws should be recast so as to support the statutory goal of consumer protection where appropriate and to clearly exclude other activities from regulation.

As noted above, many payment services do not materially increase the risk of loss to the consumer.²⁶⁹ While the use of such services does not come wholly without risk, many consumers making payments via an Internet or mobile payment system face a risk profile that is almost indistinguishable from any other purchase and sale transaction effectuated directly between a buyer and seller without the involvement of a third-party payment service.²⁷⁰ Where a payment service does not increase the risk of consumer loss,²⁷¹ the extension of regulation would not serve the purpose of state money transmitter laws.²⁷² As such, the regulation of such services would be inappropriate and wholly unsupported by statutory purpose.

It is important, however, to clarify that all payment services should not be wholly excluded from the ambit of money transmitter regulation. Under the approach advocated by this Article, the consumer protection purpose of state money transmitter laws should guide the scope of regulation. To the extent that new or emerging payment systems raise increased risks of consumer loss, regulation under the money transmitter law regime would be fitting. For example, Western Union's use of new technology to effectuate a money transfer on behalf of a consumer customer should continue to be regulated as a money transmission. Perhaps more illuminating is the case of PayPal. As noted above, PayPal provides a number of payment services, such as the mobile card reader PayPal Here and a checkout service for merchants, which do not appear to raise

269. See *supra* Part IV.A.

270. See *supra* Part IV.A.

271. See *supra* Part IV.A.

272. See *supra* Part IV.A.

consumer protection concerns.²⁷³ However, PayPal also offers a consumer-facing product that allows individual consumers to send money to their friends, family, and others.²⁷⁴ Such a service appears to operate as the functional equivalent of a traditional money transfer business and carries with it the same potential for consumer harm. As such, under the approach advanced by this Article, PayPal would need to obtain a license and comply with state money transmitter laws. The distinction, however, is the basis for regulation. PayPal would not be subject to regulation because its varied payment service offerings to merchants can be construed as money transmission. Instead, PayPal would be deemed a money transmitter as a result of the money transfer service it provides to consumers.

In short, the statutory purpose of consumer protection does not compel the indiscriminate application of state money transmitter laws to all Internet and mobile payment service providers. A nuanced approach that focuses on the consumer protection goals of the statute would better serve the purpose of state money transmitter laws by mandating oversight when justified by consumer protection concerns and exempting other activities from needless regulatory burdens.

C. *What About Merchant Protections?*

To the extent that payment services are provided to merchants, they appear to offer a distinctly different risk profile than services provided to consumers.²⁷⁵ In such situations, the risk of loss shifts in large part from the consumer to the merchant seller.²⁷⁶ While state consumer protection laws seek to provide protections for individual buyers of goods and services, it is less clear that such statutes should offer similar protections for merchants who sell goods and services.²⁷⁷ The question of what protections (if any) should be available to merchants using Internet and mobile payment services is beyond the scope of this Article. However, it is clear that forcing merchant sellers to bear the entire risk of loss in the event of nonperformance of a payment service provider may be unappealing.

On the one hand, merchant sellers can be viewed as distinctly different than individual consumers. By acting in a commercial capacity to sell goods or services, merchant sellers could be reasonably expected to exercise care in selecting those who will provide payment services on their behalf. As such, merchant sellers should bear the risk of nonperformance,

273. *See supra* Part III.

274. *See Transfer Overview*, PAYPAL, <https://www.paypal.com/webapps/mpp/transfer-money-online> (last visited Sept. 16, 2013).

275. *See supra* Part IV.A–B.

276. *See supra* Part IV.A–B.

277. *See supra* note 37.

and are in the best position to conduct due diligence on the qualifications of the service provider and negotiate any necessary protections to guard against the risk of nonperformance.²⁷⁸

Unfortunately, not all merchant sellers possess the same level of sophistication or bargaining power. As a result small business owners such as the sole proprietor of a food cart may in fact be viewed as more closely analogous to a consumer. If so, providing merchant protections via statute may be both necessary and appropriate in certain limited circumstances. In the absence of such additional protections, smaller merchant sellers may be particularly susceptible to significant losses (e.g., delivery of goods or services without payment) in the event of that a payment service provider does not perform. As compared to consumers, merchant sellers more appropriately bear the risk of loss.²⁷⁹ Nonetheless, additional statutory protections may be warranted if simply allowing merchant sellers to sue nonperforming payment service providers to enforce contractual rights and remedies is viewed as insufficient.²⁸⁰

D. Indiscriminate Extension Needlessly Hinders Innovation and Ignores Marketplace Realities

Because the indiscriminate extension of state money transmitter laws to all Internet and mobile payment mechanisms is not supported by statutory purpose, doing so would: (1) needlessly hinder continued innovation and competition in the payments industry; and (2) wholly fail to accommodate a societal shift toward conducting commerce over the Internet and mobile platforms and using non-paper-based payment mechanisms. Instead the nuanced approach advanced by this Article clarifies the scope of regulation while appropriately recasting state money transmitter laws to accommodate technological advances and the development of innovative business models. Guidance and support for such an approach abounds. The need to ascertain the scope and applicability of existing laws and regulations in light of new and emerging technologies is nothing new.²⁸¹ In the context of money transmitter regulation at the federal level, regulators have already recognized the need to accommodate previous payment system

278. See *supra* note 222.

279. See *supra* note 222.

280. See Martinez, *supra* note 227 (discussing merchant law suits against nonperforming payment service providers).

281. See, e.g., *Am. Libraries Ass'n v. Pataki*, 969 F. Supp. 160, 161–82 (S.D.N.Y. 1997) (noting that (1) judges and legislators are “faced with adapting existing legal standards to the novel environment of cyberspace,” (2) the “Internet . . . requires a cohesive national scheme of regulation so that users are reasonably able to determine their obligations,” and (3) the “[r]egulation on a local [l]evel . . . will leave users lost in a welter of inconsistent laws, imposed by different states with different priorities”).

innovations.²⁸² Moreover, financial laws, including in the heavily regulated banking industry, have historically been appropriately reinterpreted in light of technological changes.²⁸³ The foregoing supports the proposition that state money transmitter laws can and should be appropriately recast in light of new ways of conducting commerce.

1. *Lessons from the Federal Reserve Board*

In 2005, the Federal Reserve Board addressed the lack of clear and consistent state and federal regulation of prepaid products such as gift cards, including concerns over the applicability of state money transmitter laws.²⁸⁴ At the time, industry participants felt that “uncertain legal and regulatory conditions [could] stifle innovation in the industry, as compliance with an increasing number of laws and regulations, particularly at the state level, [could] make products too expensive to offer.”²⁸⁵ Industry participants also noted that existing regulations failed to adequately differentiate between types of prepaid products, which may have very different risk characteristics for the general public.²⁸⁶ In responding to these concerns, the Federal Reserve Board concluded that: (1) significant changes were taking place in payment systems; (2) payment systems varied widely and a one-size-fits-all regulatory approach may not best fit the needs of the industry or best address the risks associated with prepaid products; and (3) regulation should not unduly hinder innovation.²⁸⁷

Just eight years later in 2013, the discussion of Internet and mobile payment systems is like *déjà vu*. The payments industry is rightfully expressing concern regarding the lack of clear and consistent guidance as to regulation of Internet and mobile payment systems.²⁸⁸ Moreover, the speed of innovation has resulted in different business models with unique risk profiles.²⁸⁹ Nonetheless, existing regulation fails to adequately differentiate Internet and mobile payment services for purposes of regulation.²⁹⁰ Like the providers of prepaid products, the proponents of new and emerging payment systems rightfully fear that the lack of clarity and the costs of

282. See FEDERAL RESERVE, *supra* note 1; see also Financial Crimes Enforcement Network; Amendment to the Bank Secrecy Act Regulations—Definitions and Other Regulations Relating to Money Services Businesses, 74 Fed. Reg. 22,129-01 (proposed May 12, 2009) (to be codified at 31 C.F.R. pt. 103).

283. See *supra* Part IV.D.2.

284. See FEDERAL RESERVE, *supra* note 1.

285. *Id.*

286. *Id.*

287. *Id.*

288. See *supra* note 30.

289. See *supra* Parts II–IV.

290. See *supra* Part IV.

compliance will have a chilling effect on innovation.²⁹¹ Given the similarities, the Federal Reserve Board's 2005 conclusions may very well be an inspired utterance as to the appropriate means for reconciling the tension between potentially sweeping regulation and innovative business models. Transposing the Federal Reserve Board's conclusions to the present situation mandates the recognition of ongoing transformational change with respect to payment systems. As noted by the Federal Reserve Board, a one-size-fits-all regulatory scheme may not fit the needs of the industry or address the risks of new and emerging payment systems. Because the Internet and mobile payment services vary widely in functionality and potential risk to the general public, such an approach would be inappropriate, and would unnecessarily hinder payment innovation. In contrast, the Federal Reserve Board's conclusions support the adoption of the more nuanced approach advanced by this Article. Such an approach is flexible enough to differentiate between payment innovations and address the actual consumer risk that results from each unique payment service. Instead of needlessly hindering the growing e-commerce and mobile payment practices of the modern marketplace, this approach supports continued innovation by eliminating the costs of regulatory compliance where consumer protection is not served and by providing greater clarity as to the potential scope of regulation. As such, the Federal Reserve Board's conclusions regarding prepaid products accentuates the need for recasting state money transmitter laws in light of the real risks of each new payment innovation instead of indiscriminately extending regulation to any new innovation that falls within the plain language of the statutes.

2. *Lessons from Banking and Financial Regulation*

Examples of situations where regulatory requirements have been reinterpreted in light of technological advances abound. The banking industry, in particular, has constantly addressed the regulatory implications of new ways of conducting the very old business of banking.²⁹² As

291. See *supra* note 30.

292. See, e.g., *Indep. Ins. Agents of Am. v. Ludwig, Inc.*, 997 F.2d 958 (D.C. Cir. 1993) (declining to recast a statute permitting banks located in towns having a population of 5,000 or less to sell insurance as limiting such sales to local townspeople where new technologies such as telephones and direct mailing allow for nationwide business and solicitation not contemplated by legislators in 1916); Office of the Comptroller of the Currency, Interpretive Letter No. 875 (Oct. 31, 1999) (setting forth the regulatory agency's opinion that 12 U.S.C. § 24 (2006) authorizes banks to engage in certain new Internet-related services on the basis that such activities are new ways for performing traditional bank functions or are incidental thereto); RICHARD SCOTT CARNELL ET AL., *THE LAW OF BANKING AND FINANCIAL INSTITUTIONS* 198 (4th ed. 2009) (noting that Internet banking holds the potential to eviscerate any remaining limitations on geographic expansion by a bank).

discussed below, the resolution of regulatory uncertainty can be prompted by marketplace demand. In addition, the determination of how to appropriately recast existing laws and regulations can be made on a case-by-case evaluation that takes into account the marketplace demands of both industry participants and the public.

The advent of the automated teller machines (ATMs) is illustrative. Historically, banking laws restricted geographic expansion and branching by banks.²⁹³ In many states, unit banking—a requirement that state-chartered banks have only one place of doing business—was the norm.²⁹⁴ Under federal law, a nationally chartered bank could only have branches in its home state and to the extent that state-chartered banks were permitted to branch under state laws.²⁹⁵ The ATM created a great deal of uncertainty because it was unclear whether an ATM constituted a bank branch. Nonetheless, ATMs were broadly supported by both the banking industry and consumers on the grounds of increased convenience for the public. In the 1970s and 1980s, many state legislatures acted to liberalize branching restrictions in response to both public and industry demands.²⁹⁶ At the national level, the question of whether an ATM constituted a branch remained unsettled until the National Bank Act was amended to specifically exclude ATMs from the definition of the term “branch” under 12 U.S.C. § 36(j) (2006).²⁹⁷ Thus, the spread of both intrastate and interstate banking was, in part, the result of a changing marketplace that pushed for the liberalizing of branching rules to allow the operation of ATMs.²⁹⁸ The case of the ATM illustrates the need to recognize marketplace realities when recasting and clarifying the appropriate scope of existing regulation.

Like the banking industry, the means of conducting commerce and making payments are prone to being impacted by technological change. When recasting money transmitter regulation, care should be taken to

293. See Mehra Baradaran, *Reconsidering the Separation of Banking and Commerce*, 80 GEO. WASH. L. REV. 385, 399–400 (2012) (describing the removal of legal barriers to geographic expansion); Sharon E. Foster, *Fire Sale: The Situational Ethics of Antitrust Law in an Economic Crisis*, 78 MISS. L.J. 777, 784, 786 (discussion geographic restrictions); Roberta S. Karmel, *Is the Public Utility Holding Company Act a Model for Breaking Up the Banks that are Too-Big-to-Fail?*, 62 HASTINGS L.J. 821, 831 (2011) (noting that geographic restrictions prevented concentration in banking); Frederick Tung, *Pay for Banker Performance: Structuring Executive Compensation for Risk Regulation*, 105 NW. U. L. REV. 1205, 1219 (2011).

294. See Kevin J. Stiroh & Philip E. Strahan, *Competitive Dynamics of Deregulation: Evidence from U.S. Banking*, 35 J. MONEY, CREDIT & BANKING 801, 806 (2003); see also *First Nat'l Bank in Plant City, Fla. v. Dickinson*, 396 U.S. 122 (1969) (discussing Florida's unit banking statute, which only allowed banks to have one place of doing business).

295. See 12 U.S.C. § 36(c) (2006).

296. See CARNELL ET AL., *supra* note 292, at 25.

297. *Id.* at 190–91.

298. *Id.* at 25.

accommodate the growing role of Internet and mobile payment services as a preferred alternative to other payment mechanisms. As with the adoption of ATMs, the growing acceptance of such payment services in an ambiguous legal and regulatory environment highlights the importance of providing clarity regarding the scope of regulation. The nuanced approach of recasting state money transmitter laws seeks to ensure that Internet and mobile payment systems are evaluated with a critical eye and a determination made as to whether the purpose of state money transmitter laws is served by regulation. Instead of blindly extending regulation or simply bowing to marketplace demands, this Article seeks to determine the appropriate scope of such regulation in light of the unique nuances of each service and any benefits to the marketplace. Basing the determination of regulation on the extent of consumer protection concerns implicated by each unique payment service accomplishes this goal. Where the extension of regulation is not supported by consumer protection concerns, regulation would needlessly burden commerce by forcing ill-suited regulatory requirements upon innovative payment services that make purchase and sale transactions more convenient for consumers and merchants. In addition, it would needlessly raise the costs of providing such payment services and potentially reduce the incentive for continued innovations. However, if consumer protection concerns are implicated, the statutory purpose of state money transmitter laws is appropriately upheld by extending regulation. In doing so, state money transmitter laws are modernized to account for marketplace realities while simultaneously staying committed to the consumer protection goals of money transmitter regulation.

V. THE FRAMEWORK FOR A MODEST PROPOSAL

Because law and regulation often lag behind innovative business models, the need to consistently re-evaluate and adapt existing regulatory schemes is nothing new.²⁹⁹ Given the rise of Internet and mobile payment systems,³⁰⁰ it is high time that state regulators and legislators look critically at state money transmitter laws and unambiguously address the extent to which such laws apply to new methods of transferring money and making payments over the Internet and mobile networks.³⁰¹ This Article has

299. See FEDERAL RESERVE, *supra* note 1; see also Financial Crimes Enforcement Network; Amendment to the Bank Secrecy Act Regulations—Definitions and Other Regulations Relating to Money Services Businesses, 74 Fed. Reg. 22,129-01 (proposed May 12, 2009) (to be codified at 31 C.F.R. pt. 103).

300. See Richard, *supra* note 1, at 262 (“In five to ten years, the remittance industry will change greatly because of increases in the variation of service providers and transfer business models.”).

301. See UNIFORM MONEY SERV. ACT, prefatory note, 7A U.L.A. 163–64 (2006).

advocated for state money transmitter laws to be modernized to account for technological changes while respecting the consumer protection purpose of such statutes.³⁰² Given the distinctly different risks between money transfer services provided to consumer customers and payment services provided to merchant sellers, an appropriate line of demarcation could be made by extending regulation to the former (and any new ways of conducting the former) while exempting the latter from regulation in the absence of an equivalent consumer protection rationale. To do so, this Article advances a framework for a narrowly tailored statutory exemption that builds on the “agent of a payee” exemption available under Nevada,³⁰³ New York,³⁰⁴ and Ohio³⁰⁵ law that would supplement other more specific exemptions that states may enact to clarify the scope of regulation to technological advances such as stored value or payment processing. The adoption of such an exemption would provide added certainty for the payment industry while simultaneously upholding the consumer protection goals of state money transmitter laws and addressing the unique characteristics of Internet and mobile payment services.

A. *The Agent of a Payee Exemption*

Each of Nevada,³⁰⁶ New York,³⁰⁷ and Ohio³⁰⁸ have money transmitter laws that contain express statutory language that could be construed as precluding regulation of payment service providers who take and deliver customer payments on behalf of a merchant seller where certain conditions are satisfied.³⁰⁹ These states provide for a so-called “agent of a payee” exemption. In these states: (1) no person may engage in the business of money transmission without a license; and (2) no person may engage in the business of money transmission as an agent “except as an agent of a

302. *See supra* Part IV.

303. NEV. REV. STAT. § 671.020 (2011).

304. N.Y. BANKING LAW § 641(1) (McKinney 1939).

305. OHIO REV. CODE ANN. § 1315.01(G) (West 2013).

306. *See* NEV. REV. STAT. § 671.020 (appearing to exclude agents of a payee).

307. *See* N.Y. BANKING LAW § 641(1) (appearing to exclude agents of a payee).

308. OHIO REV. CODE ANN. § 1315.01(G) (defining the term “transmit money” as not including transactions in which the recipient of the money or its equivalent is the authorized representative of a principal in a transaction for which the money or its equivalent is received, other than transactions for the transmission of money or its equivalent).

309. Unlike the Nevada, New York, and Ohio statutes, the Texas money transmitter law does not contain express statutory language that exempts agents of a payee from regulation. However, the Texas Department of Banking is of the opinion that payment processors who act as agents of a merchant by temporarily holding merchant funds at the end of the settlement process are exempt from licensing under the money transmitter law. *See* Tex. Dep’t of Banking, Op. No. 06-01 (May 15, 2006), available at policy.ctspublish.com/txdob/; *see also* Tex. Dep’t of Banking, Op. No. 03-01 (June 4, 2003), available at policy.ctspublish.com/txdob/.

licensee or *as agent of a payee*.”³¹⁰ The foregoing requirements are somewhat unclear. However, the language regarding money transmission as an agent appears to expressly allow “agents of a payee” to engage in money transmission without a license and without otherwise being subject to the regulatory requirements of the state’s money transmitter statute.³¹¹

The New York statute and associated regulations provide additional detail regarding the application of this exemption. Under New York law, agents of a payee include “any person authorized by a payee to receive funds on behalf of the payee and to deliver such funds received from the payor to the payee.”³¹² The key to qualifying for the exemption is the presence of a contractual agency relationship between the service provider and the merchant seller. According to the New York Banking Department, factors that indicate a valid agency relationship include: (1) a contract between the agent and the payee; (2) authorization for the agent to receive payments on behalf of the payee and deliver such payments to the payee; (3) a receipt from the agent to the customer indicating that payment to the agent constitutes payment to the payee; (4) the absence of risk of loss to the customer if the agent fails to remit the payment to the payee; and (5) the payee treats customers as if the payee received the payment whether or not the agent actually delivers the funds to the payee.³¹³ The New York Banking Department has also emphasized that the exemption only applies where delivery of funds to the agent results in no greater risk to the customer than if payment were delivered directly to the payee.³¹⁴

While the “agent of a payee” language is not listed in the statutory exemptions section of the New York and Nevada statutes, it appears to function as such, and could be available to Internet and mobile payment service providers where the service is: (1) provided to a merchant pursuant to a valid agency agreement and (2) steps are taken to ensure that the buyer faces no greater risk of loss in delivering a payment to the service provider instead of paying the merchant directly.

310. See NEV. REV. STAT. § 671.020 (emphasis added); N.Y. BANKING LAW § 641(1); see also OHIO REV. CODE ANN. § 1315.01(G).

311. See N.Y. Banking Dep’t, Interpretive Letter (Jul. 9, 2007), available at http://www.dfs.ny.gov/legal/interpret_opinion/banking/lo070709b.htm.

312. N.Y. COMP. CODES R. & REGS. tit. 3, § 406.2(1) (2013).

313. N.Y. Banking Dep’t, Interpretive Letter (April 24, 2007), available at http://www.dfs.ny.gov/legal/interpret_opinion/banking/lo070424.htm; see also N.Y. BANKING LAW § 640(10) (McKinney 1939) (defining the term agent as requiring a written agency contract, albeit in the context of agents of a licensee as opposed to agents of a payee).

314. N.Y. Banking Dep’t, Interpretive Op., *supra* note 299 (determining that agent of a payee exemption was inapplicable where a company that received student payments for prepaid meals at a secondary school did not give a receipt indicating that payment to the agent was deemed payment to the payee, and emphasizing that there “ought to be no greater risks than if the funds were delivered directly to the payee”).

B. *The Federal Approach*

In addition to the minority of states that have adopted an agent of a payee exemption, federal laws regulating money transmission have been quick to adapt to payment innovations. In 2009, amendments clarifying the application of the BSA's money transmitter regulations to payment services were initiated.³¹⁵ The term "money transmitter" was amended to specifically exclude any person that "[a]cts as a payment processor to facilitate the purchase of, or payment of a bill for, a good or service through a clearance and settlement system by agreement with the creditor or seller" from the definition of money transmitter.³¹⁶ This exclusion is most likely applicable to third-party payment services offered to merchant sellers. However, it only applies to payment processors, which may be narrower than the New York and Nevada approach of exempting any agent of a payee. It is unclear whether all Internet and mobile payment services provided to a merchant would be deemed payment processors. In addition, the term "money transmitter" was amended to exclude any person that "[a]ccepts and transmits funds only integral to the sale of goods or the provision of services, other than money transmission services, by the person who is accepting and transmitting the funds."³¹⁷ This second exclusion appears to be focused on sellers themselves who may directly engage in money transmission when selling their own goods or services. As such, it is unlikely to be of benefit to third-party payment services not acting as sellers themselves.

When compared to the agent of a payee approach, the federal amendments provide more certainty in clearly excluding certain activities from the definition of money transmission and thus, the scope of regulation. However, because the federal approach opts to exclude very narrowly defined payment activities, any business model that does not clearly fit the description may be resigned to the same unsettled legal and regulatory landscape.

C. *A Mash-Up of the State and Federal Approaches*

This Article suggests that the best framework for amending state money transmitter laws to accommodate payment innovations while continuing to protect against consumer losses requires a mash-up of the "agent of a payee" approach and the amendments to the BSA. Specifically,

315. See Financial Crimes Enforcement Network; Amendment to the Bank Secrecy Act Regulations—Definitions and Other Regulations Relating to Money Services Businesses, 74 Fed. Reg. 22,129-01 (proposed May 12, 2009) (to be codified at 31 C.F.R. pt. 103).

316. 31 C.F.R. § 1010.100(ff)(5)(ii)(B) (2013).

317. 31 C.F.R. § 1010.100(ff)(5)(ii)(F).

state money transmitter laws should be amended to unambiguously exclude any agent of a payee from the definition of money transmission. In determining the availability of the exemption, the key factor would be whether the receipt and transmission of money by the agent to the payee results in any greater risk of loss to the purchaser of the good or service than a purchase and sale transaction where the payment is made directly to the seller.³¹⁸ As such, the exemption would depend on: (1) a valid written agreement with the payee/seller; and (2) enforceable terms and conditions between the agent/service provider, confirmation that the receipt of funds by the agent/service provider is deemed receipt by the payee/seller and that the payee/seller has no recourse against the purchaser for any failure of performance by the agent/service provider.³¹⁹

This framework combines the substantive inclusiveness and consumer protection focus of the “agent of a payee” approach with the clarity and drafting finesse of the amendments to the BSA. By basing the exemption on the more inclusive “agent of a payee” approach, the exemption is better able to account for the variations between different payment services and innovations while allowing consumer protection to remain the driver for regulation. In contrast to limiting the exemption to specific types of payment services like the BSA amendments, or attempting to explicitly list each and every type of exempt service, this framework allows consumer protection to exist as a guiding principle on questions of regulatory scope instead of focusing on the underlying technology, the type of service, or business model nuances. In addition to being better suited to differentiating between existing services, the “agent of a payee” approach allows for ongoing guidance with respect to new payment innovations by not being too narrowly focused.

The foregoing notwithstanding, the New York and Nevada approach suffers for not clearly exempting agents of a payee from regulation via an explicit statutory exemption or amendment to the definition of money transmission. Instead, New York and Nevada have inserted the agent of a payee language into the licensing mandate, which may result in some confusion. Therefore, this Article suggests that, like the amendments to the BSA, the agent of a payee language should be incorporated by amending the definition of “money transmission” to exclude the activity, or otherwise provide for an explicit exemption. Doing so provides for a more clearly articulated position on the scope of regulation.

It should be noted that this Article does not mean to suggest that there is no benefit to adopting activity-specific exemptions that narrowly address

318. See *supra* Part IV.

319. See *supra* notes 313–314.

defined types of payment services such as stored value,³²⁰ payment processing,³²¹ and money transmission by sellers where it is necessary and integral to the sale of the seller's goods and services.³²² To the contrary, targeted exemptions can and do provide added certainty regarding the question of whether regulation applies to specific payment innovations and new business models. However, such narrowly focused exemptions will be of little benefit in clarifying the scope of regulation more broadly with respect to new and emerging payment systems. As such, the agent of a payee exemption would be an ideal supplement to targeted exemptions dealing with new business models or technological advances.

D. Benefits of the Proposed Framework

The adoption of the agent of a payee framework for an exemption would not only address the uncertain regulatory scope of money transmitter laws, but also modernize such laws to account for new and emerging forms of payment activity. Such an approach is narrowly crafted to ensure that the consumer protection purpose of state money transmitter laws is served by continuing to apply regulatory compliance requirements on those services that pose a real risk of loss, and only exempting activities that will not run afoul of the purpose of such statutes. Moreover, clarifying the scope of regulation will allow for the continued development of innovative payment mechanisms and the use of such mechanisms to facilitate the growth of commerce in a modern cashless world without burdening those in the payment industry with: (1) the cost and expense of complying with inappropriately scoped regulatory requirements; (2) the transaction costs of evaluating the scope and applicability of a statute that has yet to catch up to technological advances; and (3) the risk of uncertain application of such statutes by state regulators.

1. Providing Much Needed Clarity

The adoption of an exemption that clearly defines the compliance obligations of third-party payment services providers that receive funds on behalf of sellers will greatly reduce the risks facing such businesses by virtue of an uncertain legal and regulatory landscape.³²³ The intentionally broad definition of "money transmission" under most state laws leaves open the very real possibility that a state regulator could elect to broadly

320. See, e.g., WASH. REV. CODE ANN. §§ 19.230.010(6), 19.230.020(12) (West 2013).

321. See, e.g., UNIF. MONEY SERV. ACT § 103(9), 7A U.L.A. 184 (2006).

322. See, e.g., 31 C.F.R. § 1010.100(ff)(5)(ii)(F).

323. See *supra* Part III.

interpret the scope of the statutory language and seek to require licensing and regulatory compliance of a number of businesses, including Internet and mobile payment systems.³²⁴ Because few states currently have express statutory exemptions that clearly apply, there is little certainty.³²⁵

In Nevada, New York, and Ohio the agent of a payee exemption appears to apply to exempt these services from regulation.³²⁶ In one other state, Texas, these types of payment businesses may take some comfort in the presence of an interpretive opinion that may be construed to indicate the state regulator's present position that payment processing is exempt from money transmitter regulation.³²⁷ In other states, uncertainty over potential regulation remains. Providers of Internet and mobile payment service to merchant sellers must at a minimum bear the transaction costs of evaluating the risk of potential regulation and deciding whether or not to obtain a license.³²⁸ In addition, any person that elects to obtain a license and comply with the regulatory requirements will bear the costs of maintaining a money transmitter license and the compliance costs as an added expense of doing business.³²⁹ Because these types of services do not result in added consumer protection concerns, the added regulatory burdens are both unnecessary and ineffectual.³³⁰ If a license is not obtained, the risk of potential regulation and liability for noncompliance remains and may compound over time.³³¹

Those who elect not to obtain a license and comply with regulatory requirements may have an argument based on statutory interpretation that money transmitter laws are inapplicable to their services. At its most basic level, the argument is that by acting as an agent for a seller of goods or services, the agent is not in fact receiving money for transmission. As an agent of a seller, receipt of funds by the agent is the equivalent of receipt of funds by the seller. Therefore, receipt of payment by the agent and subsequent delivery of funds to the seller who acts as principal is not money transmission. While this is both a reasonable and perhaps even appropriate interpretation, the possibility of regulation remains due to the breadth of most state statutes and the lack of a clearly applicable exemption

324. See Think Computer Corp., *supra* note 30; see also Hurh & Luce, *supra* note 30.

325. See *supra* Part II.

326. See *supra* Part V.A.

327. See Tex. Dep't of Banking, Op. No. 06-01 (May 15, 2006), available at policy.ctspublish.com/txdob/; see also Tex. Dep't of Banking, Op. No. 03-01 (June 4, 2003), available at policy.ctspublish.com/txdob/.

328. See *supra* Part III.

329. See Sposito, *supra* note 204 (quoting Brian Riley that "[t]he pain in the neck is when you do it in all 50 states").

330. See *supra* Part IV.

331. See 18 U.S.C. § 1960 (2006); MD. CODE ANN., FIN. INST. §§ 12-429 to 430 (LexisNexis 2011); see also Think Computer Corp., *supra* note 30.

or other guidance indicating that compliance is not required.³³² As evidenced by the foregoing, providers of such payment services are left in the unenviable position of having few good options when it comes to money transmitter regulation and compliance.

Given this uncertain legal and regulatory backdrop, state money transmitter laws would benefit by clarifying the scope of money transmitter regulation and answering the question of whether a host of new payment services must become licensed money transmitters.³³³ As advanced by this Article, the agent of a payee framework for a new exemption succeeds in resolving this question by drawing an appropriate distinction between payment services provided to merchant sellers pursuant to a contractual arrangement that protects consumers and traditional money transfer services provided directly to consumers. The former category of services would be exempt while the latter would continue to be regulated under state money transmitter laws based on a case-by-case assessment of the risk of consumer loss.³³⁴ Accordingly, the adoption of the proposed regulatory framework would provide the benefit of added certainty for those who provide such services, those who seek to develop similar services, and the state regulators who are tasked with enforcing the mandate of state money transmitter laws.

2. *Upholding Consumer Protection*

In addition to providing certainty, the proposed agent of a payee framework strikes an appropriate balance by allowing the breadth of state money transmitter regulation to reach new services that raise the same consumer protection concerns as traditional money transfer businesses while leaving those without the same risks free to operate without licensing and oversight.³³⁵ The consumer protection purpose of state money transmitter laws is upheld by continuing to require licensing and regulation of traditional money transfer businesses like Western Union that provide money transfer services directly to consumer customers.³³⁶ This would be true regardless of whether the money transfer service is provided from a brick and mortar location or electronically via the Internet or a mobile application.³³⁷

For example, where Western Union receives money from an individual consumer through the Western Union website and the consumer engages

332. *See supra* Part II.

333. *See supra* Part IV.

334. *See supra* Part IV.

335. *See supra* Part IV.

336. *See supra* Part IV.

337. *See supra* Part IV.

Western Union to deliver the funds to a designated person or place, a money transmitter license and compliance with the state regulatory regime would be required. In such instances, the agent of a payee exemption would not apply because Western Union would not be receiving and delivering funds as an agent of a merchant seller in connection with facilitating the sale of the seller's goods and services.³³⁸

In contrast, where a merchant seller contracts with a third party to receive and deliver payments from the seller's customers and complies with the requirements for mitigating consumer loss, the activity would be exempt from regulation.³³⁹ For example, if a book store contracts with Amazon Payments or PayPal to provide a mechanism for accepting online payments from a customer who wishes to purchase a book, Amazon Payments and PayPal would not be engaging in regulated money transmission so long as there were a valid contractual agreement with the book store that eliminates any risk of loss to the buyer of the book after a payment is made to Amazon Payment or PayPal, as the case may be.³⁴⁰ However, Amazon Payments and PayPal can both be used by individual consumers to effectuate money transfers to designated individuals in the absence of a purchase and sale transaction.³⁴¹ In those instances, the receipt and delivery of money is no different than the use of the Western Union website. Therefore, licensing and regulation would be necessary for services like Amazon Payments and PayPal for the latter activity, but not the former.³⁴²

The foregoing examples illustrate how the proposed framework for an agent of a payee exemption is narrowly tailored to not only maintain regulation and licensing where appropriate due to the continued risk of consumer harm, but also to clarify the scope of the statute in light of technological advances. In doing so, the proposed framework would more appropriately respond to the risks of these activities by acknowledging and distinguishing between money transfer services provided to a consumer customer and payment services on behalf of a seller pursuant to a contractual agreement, which is inherently different. Therefore, the agent of a payee exemption operates so as to support the consumer protection purpose of state money transmitter laws.

338. *See supra* Part V.C.

339. *See supra* Part V.C.

340. *See supra* Part V.C.

341. *See Send & Receive Money*, AMAZON, <https://payments.amazon.com/sdui/sdui/personal/money> (last visited Aug. 21, 2013); *Transfer Overview*, PAYPAL, *supra* note 268.

342. *See supra* Part V.C.

3. *Accommodating Innovative Business Models, Modern Technology, and Commerce*

Finally, the proposed framework recognizes innovative business models in the payments industry and new technology while appropriately adapting existing laws to society's growing e-commerce habits instead of trying to force new payment systems into an incongruous regulatory box. By differentiating between payment services and recognizing the unique risks that each poses to consumers, the proposed framework promotes continued innovation in the payments industry, which supports the realities of a system of commerce that now relies heavily on non-cash payment methods. The providers of Internet and mobile payment services and those who continue to develop services will benefit by having an understanding of the scope of regulation and not having to unnecessarily bear regulatory burdens and costs. As such, money transmitter laws would be modernized and appropriately scoped to regulate the actual consumer protection risks implicated by changing technologies and advances in payment technologies without needlessly hindering the development of services that help to drive commercial growth in an increasingly cashless world.

CONCLUSION

State money transmitter laws, like many other statutes, suffer from an inability to predict and account for technological advances that occur in the years following enactment. Given the way that Internet and mobile payment technologies have been embraced, it is high time that state regulators and legislators look critically at state money transmitter laws and unambiguously address the extent to which such laws apply to the ever expanding ways that a person can electronically transfer money and make payments. In modernizing state money transmitter laws, it is imperative that we: (1) carefully consider and continually re-evaluate the scope of regulation in light of new services and technological innovations; (2) make an individualized determination of whether each new activity rightfully ought to be regulated as money transmission; and (3) adopt new amendments, as appropriate, to provide for clear and explicit exemptions where the consumer protection purpose of state money transmitter laws is not served.

Assuming that the consumer protection purpose of state money transmitter laws should inform decisions regarding regulatory scope, the agent of a payee exemption framework advanced in this Article strikes an appropriate balance between the potentially divergent interests of consumers and commerce. The framework provides guidance and clarity to potentially regulated persons. In addition, the framework upholds the

integrity of consumer protection that underlies state money transmitter laws by extending regulation to technological advances only where appropriate. Perhaps most importantly, the framework alleviates concerns about the chilling effect on innovation by embracing and exempting payment innovations that do not implicate overt consumer protection concerns. Thus, the agent of a payee framework will assist states in taking an important first step toward appropriately modernizing existing laws to accommodate new and emerging payment systems and developing a cohesive regulatory scheme for such systems.