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## The Case for Preempting State Money Transmission Laws for Crypto-Based Businesses

Carol R. Goforth  
*University of Arkansas, Fayetteville*

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# THE CASE FOR PREEMPTING STATE MONEY TRANSMISSION LAWS FOR CRYPTO-BASED BUSINESSES

Carol R. Goforth\*

## I. INTRODUCTION

Few industries are evolving as rapidly or as dramatically as those involving payment systems.<sup>1</sup> The recent advent and spread of cryptocurrencies and associated trading platforms and exchanges,<sup>2</sup> as well as ongoing improvements and innovations in FinTech generally,<sup>3</sup> ensure that this is going to continue for the foreseeable future. Along with this rapid change has come a dynamic increase in the number and range of payment startups,<sup>4</sup> a development that has been recognized as likely to redound to the

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\* \* Carol R. Goforth is a University Professor and the Clayton N. Little Professor of Law at the University of Arkansas, in Fayetteville. She has decades of experience with corporate, securities and business law issues in the U.S., and has recently published a growing interest in crypto. She is the author of *REGULATION OF CRYPTOTRANSACTIONS* (West Academic, 2020).

1. “There is no denying that adoption of mobile payments and banking is picking up speed. Nearly 40% of U.S. consumers have now used at least one digital payment service. . . . and more than 60% of consumers are already regular users of mobile banking app.” Richard Yao, *The Evolution of Payments & What It Means for Financial Services*, MEDIUM (Jun. 14, 2018), [<https://perma.cc/G94P-XMK5>].

2. “Payment businesses have gone through a revolution in the last few years. From blockchain, and FinTech to AI and cryptocurrencies, the world of international commerce is moving faster than ever.” Ilker Koksal, *The Rise of Crypto as Payment Currency*, FORBES (Aug. 23, 2019), [<https://perma.cc/U22F-8NG7>]. A trading platform or crypto exchange is simply an online platform in which one kind of digital asset may be exchanged for another based on the relative market values of the assets being traded. Some exchanges allow crypto to be exchanged for fiat currencies, although most trade only in cryptoassets.

3. Generally speaking, Fintech is technology that impacts the delivery of financial services, and “[i]f you were asked today to name one sector that has evolved so fast in the past few decades, you’d not be mistaken to mention the financial space.” *Fintech – The Evolution of Financial Technology*, FINSMES (Jan. 31, 2019), [<https://perma.cc/JZ33-44KT>].

4. “Within the last couple of years, FinTech and especially Payments has seen some amazing companies emerge out of nowhere. Most notably are of course Stripe and Square, which have been able to amass valuations of \$9.2 and \$18.9 Billion (*valuation Tuesday April 3rd, 2018*) respectively.” Dwayne Gefferie, *The New Business Model of the Payments Industry*, MEDIUM (Apr. 4, 2018), [<https://perma.cc/LJG8-2L5Q>] (emphasis in original).

benefit of consumers and the broader economy.<sup>5</sup> The problem is simply that regulation is not keeping up with innovation.

Historically, money transmitters were businesses designed to help customers get their money from one location to a third party in a different location. The quintessential examples of conventional money transmitters are companies like Western Union and Moneygram.<sup>6</sup> However, regulations that worked well to protect consumers dealing with that kind of enterprise do not always translate well to customers involved in the online world of bitcoin and crypto purchasing and trading. Today, businesses set up to hold virtual assets for the convenience of customers or to help customers exchange virtual assets, and even companies distributing their own cryptoassets, are opening themselves to potential liability for operating as unlicensed money transmitters. Businesses that try to comply with legal requirements are often overwhelmed by the conflicting patchwork of laws and regulations at the state level.

Obviously, when customers entrust a business with their money, expecting it to be delivered to a third party, there is a wide range of possible negative outcomes. The business might abscond with the funds or might fail to deliver them to the correct person as a result of negligence or malfeasance, or even because of bankruptcy.<sup>7</sup> State money transmitter laws were specifically

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5. “[S]maller start-up fintech firms now provide much of the innovation backbone in the payments industry. Better positioned to create new consumer-focused digital solutions, these agile fintech firms are the perfect partners for legacy financial services organizations who need to become more responsive to the digital consumer . . .” Jim Marous, *Top 10 Trends Rocking the Future of Payments*, FIN. BRAND (Nov. 6, 2017), [<https://perma.cc/EL8R-RTC7>].

6. “Western Union and Moneygram are classic examples of money transmitters . . .” Benjamin Lo, *Fatal Fragments: The Effect of Money Transmission Regulation on Payments Innovation*, 18 YALE J.L. & TECH. 111, 112 (2016). Accord Jennifer Windh, *Peer-to-Peer Payments: Surveying a Rapidly Changing Landscape*, 15 ELEC. BANKING L. & COM. REP., Jan. 2012, at §§ 1, 3.2.2, 4.3 (Visa and MasterCard are also longstanding players in the payments industry). See also Kevin V. Tu, *Perfecting Bitcoin*, 52 GA. L. REV. 505, 512 (2018) (using Western Union as an example of a conventional money transmitter).

7. One source, in discussing the historical antecedents to state money transmitter laws, pointed to the need to protect immigrants in the early 1900s, who wanted to send money to their native countries, but were often subject to abusive and fraudulent practices. “Principally, these risks include high fees and the possibility of fraud (i.e., that the transmitted funds may never be received by the intended recipients).” Andrea Lee Negroni, *Risky Business: State Regulation of Money Transmitters*, GOODWIN LAW: CLEAR NEWS (Spring 2003), [<https://perma.cc/BK2W-Z55C>]. This same source pointed to the failure of a regional money

designed to address this kind of risk, typically by imposing licensing, safety, and soundness requirements on businesses interacting with each state's citizens.<sup>8</sup> These requirements generally include things like submitting to an initial and annual examination conducted at the business's expense; providing assurance of good character for the licensee and its principals; posting of surety bonds or maintaining adequate collateral with specified characteristics; maintaining minimum net worth; and submitting regular financial reports, which are often required to be audited in accordance with generally accepted accounting principles.<sup>9</sup>

The internet and exponential growth of e-commerce complicated this scenario dramatically.<sup>10</sup> State money transmitter laws were drafted broadly and have been broadly construed, setting the stage for application of rules to products and businesses that are substantially different from those involved in conventional money transmission. The statutes are so broadly worded that in a number of states, they have been found to cover not only online and mobile payment systems,<sup>11</sup> but also virtual currencies, such as bitcoin (which is also referred to as a cryptocurrency, cryptoasset, or simply as crypto).<sup>12</sup>

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order issuer in the 1980s as another possible “precipitating event for the growth of regulation of money transmitters.” *Id.*

8. “Each state separately licenses and regulates money transmitters that engage in money transmission to their residents.” *Money Transmitter Licensing Law*, BLOCKCHAIN LAW GUIDE, [<https://perma.cc/56US-AHUM>].

9. *See id.* The exact parameters of each state's laws are different, although most of these requirements are present in some form in each state that chooses to regulate money transmitters. For a further consideration of the varying state regulations, see *infra* Part VI.B. of this Article.

10. Businesses that facilitate payments online can work in ways that are similar to conventional money transmitters. Money can be transferred by a customer to an online payment processor, such as PayPal, and that intermediary will then transfer the funds as directed. The primary difference is that the transfers are all conducted over the internet rather than through face-to-face interactions at either end of the transaction. *See, e.g., Who We Are*, PAYPAL, [<https://perma.cc/PR2S-K7X8>] (describing that company's “open digital payments platform”).

11. For example, PayPal is licensed in all 50 U.S. states, plus the District of Columbia, Puerto Rico, and the U.S. Virgin Islands. *See PayPal State Licenses*, PAYPAL, [<https://perma.cc/HVV8-2WZ7>]. Although Montana has no state money transmission statute, PayPal has obtained a Montana Escrow Business License. *Id.*

12. Note that this single sentence mentions “virtual currencies,” “cryptocurrency,” “cryptoasset,” and “crypto.” Banking regulators, including FinCEN and state money transmitter regulators, are obviously most concerned with assets that work like money, and it is therefore natural that they tend to talk about crypto as a virtual currency, using a very broad

The application of state money transmitter laws to crypto is not out of step with federal law, given that cryptoassets such as bitcoin and ether have been classified as virtual currencies by federal regulators.<sup>13</sup> As a result, however, businesses that assist in

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definition to cover as many kinds of digital interests as possible. However, some kinds of crypto are not designed or intended to function as a currency, and so popular usage, especially on the international scene, has tended to move towards speaking about “cryptoasset” or simply “crypto” when a broader meaning is intended. *See generally Cryptocurrency Vs 6 Other Crypto Assets Category Classification Types*, BITCOIN EXCHANGE GUIDE (July 25, 2018), [<https://perma.cc/88AB-DAHG>].

Terminology is especially important in understanding cryptocurrencies and other cryptoassets, but it can also be very confusing. For a general explanation of terms used, including an analysis of some of the ambiguities in current terminology, see Carol Goforth, *The Lawyer’s Cryptionary: A Resource for Talking to Clients About Crypto-Transactions*, 41 CAMPBELL L. REV. 47 (2019). This Article will use crypto, cryptoassets, and virtual currency interchangeably.

13. For the past several years, the U.S. Department of the Treasury Financial Crimes Enforcement Network (FinCEN) has accepted that virtual currency is not “currency” under regulations implementing the Bank Secrecy Act because it is not legal tender, but the bureau nonetheless subjects a wide range of virtual currency businesses to regulation as money transmitters. John L. Douglas, *New Wine into Old Bottles: Fintech Meets the Bank Regulatory World*, 20 N.C. BANKING INST. 17, 42 (2016).

It does this, in part, pursuant to a rule finalized in 2011 that expanded “money transmission services” to include “the acceptance of currency, funds, or other value that substitutes for currency from one person and the transmission of currency, funds, or other value that substitutes for currency to another location or person by any means.” Bank Secrecy Act Regulations; *Definitions and Other Regulations Relating to Money Services Businesses*, 76 FED. REG. 43,585, 43,596 (July 21, 2011) (emphasis added) [hereinafter *2011 Regulations*]. Pursuant to this definition of money transmission services, FinCEN has made it clear that the anti-money laundering (AML) requirements of the BSA apply to persons who facilitate the use of crypto by others. FIN. CRIMES ENF’T NETWORK, FIN-2013-G001, APPLICATION OF FINCEN’S REGULATIONS TO PERSONS ADMINISTERING, EXCHANGING, OR USING VIRTUAL CURRENCIES (Mar. 18, 2013), [<https://perma.cc/D9FD-RTLA>] [hereinafter *2013 GUIDANCE*]. This Guidance applies only to “convertible” cryptoassets, which are defined as those that either have “an equivalent value in real currency, or act[] as a substitute for real currency.” *Id.* This is, however, broad enough that it includes most crypto. Updated guidance from FinCEN confirms this approach. FIN. CRIMES ENF’T NETWORK, FIN-2019-G001, APPLICATION OF FINCEN’S REGULATIONS TO CERTAIN BUSINESS MODELS INVOLVING CONVERTIBLE VIRTUAL CURRENCIES (May 9, 2019), [<https://perma.cc/K5JT-ZSBJ>].

State authorities often take the same approach. For example, the Conference of State Bank Supervisors (CSBS) has determined that, for its purposes, “[v]irtual Currency is a digital representation of value used as a medium of exchange, a unit of account, or a store of value, but does not have legal tender status as recognized by the United States Government.” CONFERENCE OF STATE BANK SUPERVISORS, STATE REGULATORY REQUIREMENTS FOR VIRTUAL CURRENCY ACTIVITIES CSBS MODEL REGULATORY FRAMEWORK 2 (2015), [<https://perma.cc/H9QR-EEHC>] (certain exclusions omitted).

When the New York Department of Financial Services assumed authority over cryptoassets it did so by explaining that “virtual currency means any type of digital unit that is used as a medium of exchange or a form of digitally stored value. *Virtual currency shall be*

the transfer of cryptoassets by issuing them for other forms of crypto or fiat, by accepting payment to hold them for customers, or by assisting in the exchange of crypto, are being regulated as money transmitters.<sup>14</sup>

The reality is that rapid growth is often accompanied by growing pains. In the context of crypto, the need to comply with myriad state money transmitter requirements is proving to be particularly painful. The primary problem appears to be that crypto-based businesses are finding themselves subject to numerous requirements that were not designed with them in mind.<sup>15</sup> This Article suggests that a business focused on the issuance, holding, and exchanging of cryptoassets should not be forced to comply with the fragmented state money transmitter regulations that

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*broadly construed . . .*” 23 N.Y. COMP. CODES & REGS. tit. 23, § 200.2(p) (2019), [https://perma.cc/7MRS-MR22] (emphasis added; limited exemptions omitted).

The Uniform Law Commission’s (the ULC’s) project, the Uniform Regulation of Virtual Currency Businesses Act (the URVCBA), proclaims that for its purposes “virtual currency” means: “a digital representation of value that: (1) is used as a medium of exchange, unit of account, or store of value; and (2) is not legal tender, whether or not denominated in legal tender . . .” UNIF. REGULATION OF VIRTUAL-CURRENCY BUSINESSES ACT, § 102(23) (UNIF. LAW COMM’N 2017), [https://perma.cc/3589-Y5BD] (with certain exemptions) (versions with and without comments are available).

14. The first federal action against a crypto business for operating an unregistered money transmission business occurred in 2015. In that year, Ripple Labs was slapped with a \$700,000 fine by FinCEN for failing to register as a money services business and comply with various federal requirements. See Press Release, Fin. Crimes Enf’t Network, FinCEN Fines Ripple Labs Inc. in First Civil Enforcement Action Against a Virtual Currency Exchanger (May 5, 2015), [https://perma.cc/WMN9-6QP7].

Individuals can also be prosecuted for operating unregistered money transmission businesses. In 2013, Michell Espinoza made three purchases of bitcoins for undercover officers who paid in cash and implied that their funds were derived from, or supporting, illegal activity. See Cali Haan, *Florida Granted Right to Appeal Previously Dismissed Case Against Local Bitcoins Trader*, CROWDFUND INSIDER (Feb. 2, 2019), [https://perma.cc/9UVC-FUQL] (The purchases were for \$500, \$1000, \$500, and \$30,000). The state of Florida prosecuted Espinoza, but the trial court dismissed the action on the grounds that bitcoins were not “money,” meaning that the defendant could not have been operating an illegal money transmitter business. *State v. Espinoza*, No. F14-293, 2016 WL 11613849, at \*5 (Fla. Cir. Ct. July 22, 2016), *rev’d* 264 So.3d 1055 (Fla. Dist. Ct. App. 2019). However, on appeal, the decision was reversed. *State v. Espinoza*, 264 So. 3d. 1055, 1057 (Fla. Dist. Ct. App. 2019).

15. For example, the initial panel discussion at Money 20/20, in 2015, widely acknowledged as the largest payment industry conference in the U.S., was captioned “*State Money Transmitter Licensing Laws: Are They Killing Payments Industry Innovation?*” Lo, *supra* note 6, at 113.

currently exist,<sup>16</sup> and instead should be subject to a single, more comprehensive federal regulatory regime.

Following this introduction, Part II of this Article explores why crypto-based businesses are different from conventional money transmitters, including an examination of crypto's inherently multi-jurisdictional nature. Part III considers the public policy rationales behind the regulation of money transmitters, from both a federal and state perspective. Part IV looks at the definition of "money transmitter" under federal law and examines when this definition is applied to crypto businesses. Part V considers how different states define money transmission and when crypto businesses are subjected to these statutes. Part VI examines the scope of existing regulation, starting with federal requirements and then moving to state laws, focusing on the range of approaches and lack of uniformity across jurisdictions. Part VII makes the case for preemption of state regulation of crypto-focused money transmitters and suggests how federal law could be structured to replace the current set of inconsistent and varying rules.

## II. THE INHERENTLY MULTI-JURISDICTIONAL NATURE OF CRYPTOASSETS

Blockchain, bitcoin, and cryptocurrencies in general have been described and discussed in considerable detail elsewhere,<sup>17</sup> and that information will not be repeated here. Nonetheless, to place the issues discussed in this Article into context, a very general understanding of cryptoassets and the underlying blockchain technology is necessary.

To understand crypto, it is important to start with the reality that there is nothing tangible behind most cryptoassets. In

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16. This Article does not consider other state laws, such as securities laws, or their application to crypto-based businesses.

17. Carol Goforth, *Securities Treatment of Tokenized Offerings Under U.S. Law*, 46 PEPP. L. REV. 405, 412-15, 427-28 (2019); Goforth, *supra* note 12; Rebecca M. Bratspies, *Cryptocurrency and the Myth of the Trustless Transaction*, 25 MICH. TECH. L. REV. 1, 12-15 (2018); Elizabeth Sara Ross, *Nobody Puts Blockchain in A Corner: The Disruptive Role of Blockchain Technology in the Financial Services Industry and Current Regulatory Issues*, 25 CATH. U. J.L. & TECH. 353, 359-64 (2017); Scott D. Hughes, *Cryptocurrency Regulations and Enforcement in the U.S.*, 45 W. ST. L. REV. 1, 3-7 (2017).

contrast to traditional government-backed currencies (fiat),<sup>18</sup> there is no government or central bank, and no corporation or any other person ready to make good on the “value” represented by any cryptoasset.<sup>19</sup> In fact, a cryptoasset is really nothing more than a string of numbers recorded on a blockchain.

In order for this to make sense, you have to know what a blockchain is. In essence, it is a digital record (or ledger) of transactions maintained across several computers that are linked together in a network.<sup>20</sup> Computers in the network may be referred to as nodes.<sup>21</sup> Transactions that take place on the network’s digital ledger are time-stamped and aggregated together in blocks. Blocks are added to the chain of data only after computers in the network have checked the accuracy of the transactions included in each block and, in the case of networks governed by proof of work consensus protocols such as bitcoin, after a difficult

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18. “Fiat” is Latin for “it shall be,” and although technically it could refer to any medium of exchange not tied to something with tangible value, it has come to refer to “money” or “currency” that has value because a government has decreed that it does. Neale Godfrey, *A Few Words About Bitcoin . . . Because Fiat Is Not Just a Car*, FORBES (Mar. 8, 2015), [<https://perma.cc/CXB5-U7U3>].

19. Julia Finch, *From Silk Road to ATMs: The History of Bitcoin*, GUARDIAN (Sept. 14, 2017), [<https://perma.cc/BPM9-K6JK>]. Note that in the case of some centralized stablecoins, the issuer may actually be maintaining a reserve sufficient to guarantee value. For example, Tether was supposed to be backed by a reserve of U.S. dollars. As of this writing, the Tether website proudly proclaims that “[e]very tether is always 100% backed by our reserves, which include traditional currency and cash equivalents and, from time to time, may include other assets and receivables from loans made by Tether to third parties, which may include affiliated entities . . . .” *Transparency Update*, TETHER, [<https://perma.cc/YXH3-MPWB>]. Not everyone agrees that Tether’s claims about being backed are believable. See, e.g., Frances Coppola, *Tether’s U.S. Dollar Peg Is No Longer Credible*, FORBES (Mar. 14, 2019), [<https://perma.cc/BH49-BBZV>]. Nonetheless, it is certainly possible that such cryptoassets do or will exist, but they are not the norm.

20. See, e.g., Ameer Rosic, *What Is Blockchain Technology? A Step-by-Step Guide for Beginners*, BLOCKGEEKS, [<https://perma.cc/P2VY-VHAF>].

21. In a truly peer-to-peer, decentralized network, any computer running the same protocol can serve as a full node. Many modern cryptoassets use masternodes or limit who can serve as the validator nodes that fulfill the function of validating and adding blocks to the chain, rather than allowing all computers to participate in this process. For a description of masternodes and a list of crypto that follows this process, see William M. Peaster, *What Are Masternodes? Complete Beginner’s Guide*, BLOCKONOMI (Sept. 9, 2018), [<https://perma.cc/3PX7-9P3G>]. Libra plans on allowing members of the Libra Association to serve as validator nodes. See *An Introduction to Libra*, LIBRA, [<https://perma.cc/DJ6Z-7VQV>].



computational problem has been solved.<sup>22</sup> The nodes that perform this verification or validation service<sup>23</sup> automatically check the legitimacy of proposed transfers, and the computers that attempt to solve the puzzle or otherwise validate the block are called miners.<sup>24</sup> A successful miner is typically awarded a predetermined number of coins or tokens (although it is also possible to earn a transaction fee instead), and it is this process that allows the blockchain to function in the absence of a trusted third-party intermediary.<sup>25</sup>

The blockchain is inherently distributed because it exists on many computers and may or may not be decentralized depending on the design of the software (and in particular, whether all nodes or only selected ones are entitled to perform verification or validation services). Data that has been verified and added to the chain is generally immutable because it has been validated by a number of computers, is stored on the blockchain on every computer (or node) in the network, and cannot be changed without the agreement of those nodes.<sup>26</sup>

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22. Checking the accuracy generally means verifying that, at the start of the block, the sender of a particular asset was the owner of those assets, based on the ledger of prior transactions that are already on the blockchain. See Rui Zhang et al., *Security and Privacy on Blockchain*, ACM COMPUTING SURV. (July 2019), [https://perma.cc/3R3C-XX77].

23. These terms have precise meanings for some. For example, one academic article explains validation as involving questions about whether the computer code correctly embodies the intended understandings and agreements, while verification asks if the program is operating properly by doing what it is supposed to do and only what it is supposed to do, without error. See Daniele Magazzeni et al., *Validation and Verification of Smart Contracts: A Research Agenda*, 50 COMPUTER 50, 53 (Sept. 2017), [https://perma.cc/MVH9-DU4Y]. This precision is completely lacking in the popular literature about blockchain. See, e.g., Edzo Botjes, *Pulling the Blockchain Apart.. The Transaction Life-Cycle*, MEDIUM (Aug. 11, 2017), [https://perma.cc/XVP7-UPWX] (using validation to describe all of these functions); Nolan Bauerle, *How Does Blockchain Technology Work?*, COINDESK (Mar. 9, 2019), [https://perma.cc/BC8N-Z3ZP] (using verification to describe these functions). With apologies to computer programmers who use these terms with precision, this Article uses the two labels somewhat interchangeably.

Note also that there are alternatives to the proof of work consensus protocol described in the text. Proof of stake, for example, allocates mining power based on the number of cryptoassets pledged by each miner. For a more detailed explanation of proof of stake mining as contrasted with proof of work, see Ameer Rosic, *Proof of Work vs Proof of Stake: Basic Mining Guide*, BLOCKGEEKS (Mar. 24, 2017), [https://perma.cc/42Q7-3E3N0].

24. See Botjes, *supra* note 23.

25. For a consideration of blockchain consensus protocols, see Amy Castor, *A (Short) Guide to Blockchain Consensus Protocols*, COINDESK (Mar. 4, 2017), [https://perma.cc/MD4Q-L4T3].

26. See Magazzeni et al., *supra* note 23.

As mentioned briefly above, the validation process involves something called a consensus protocol, which is necessary to avoid the problems associated with the inherent untrustworthiness of unknown third parties. The original consensus protocol, in the form of a proof of work,<sup>27</sup> was the innovation of the pseudonymous Satoshi Nakamoto, who ushered in the blockchain era in 2008 with a white paper published in 2008 in an online discussion of cryptography.<sup>28</sup> The focus of that paper was bitcoin, which became the first and most successful cryptoasset to date.<sup>29</sup> In essence, proof of work depends on a node solving a mathematical puzzle, broadcasting the solution to the network, having the other nodes confirm that this is the first correct solution, and then adding the block on which that solution occurs to the chain.<sup>30</sup> This insures that all computers continue to rely on the same chain of data.

As the first successfully established cryptocurrency, bitcoin has been the “de facto standard” for crypto.<sup>31</sup> Following on the heels of bitcoin came a large number of “altcoins,” which were

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27. In essence, a consensus protocol ensures that only blocks that a sufficient number of computers have accepted as legitimate are added to the chain. The proof of work protocol depends on computers serving as nodes in the network verifying the legitimacy of the transactions in the block, solving a complicated mathematical puzzle, and sending the solution for that block to other nodes, which then verify the solution, with the result that the verified block is then added to the chain. Nodes that work at solving the puzzle are said to be miners. This is how bitcoin mining works, and the node that delivers the first solution for each block on the bitcoin blockchain is awarded a number of bitcoins. See generally Goforth, *supra* note 12.

For a more detailed discussion of consensus protocols for decentralized networks, see Ameer Rosic, *Basic Primer: Blockchain Consensus Protocol*, BLOCKGEEKS, [<https://perma.cc/8RT9-MB2H>].

28. See Satoshi Nakamoto, *Bitcoin: A Peer-to-Peer Electronic Cash System*, BITCOIN, [<https://perma.cc/GHP2-S4PY>].

29. As of October 1, 2019, the total capitalization of bitcoin was almost \$150 billion. *Historical Data for Bitcoin*, COINMARKETCAP, [<https://perma.cc/PWC4-M5BP>]. For data for the month ending October 1, 2019, see *Historical Data for Bitcoin*, COINMARKETCAP, [<https://perma.cc/7RQ5-FNZW>].

30. See Nakamoto, *supra* note 28.

31. Sajalali, *The Six Most Important Cryptocurrencies Other Than Bitcoins*, STEEMIT, [<https://perma.cc/KR6M-PH6B>]. While bitcoin may be the most influential, it was not the first attempt to create digital currency with an encryption-secured ledger. See Bernard Marr, *A Short History of Bitcoin and Crypto Currency Everyone Should Read*, FORBES (Dec. 6, 2017), [<https://perma.cc/WGF7-Y427>] (offering both B-Money and Bit Gold as examples of formulations that were never fully developed).

other cryptoassets also designed to be alternatives to fiat.<sup>32</sup> After the initial wave of altcoins, there have been a growing number of cryptoassets designed to serve functions other than or in addition to being a replacement for fiat currencies.<sup>33</sup>

For example, utilizing smart contracts imbedded into a particular software protocol,<sup>34</sup> cryptoassets can be designed to provide a wide range of functionality, such as offering specific applications for particular platforms; serving as developer tools; providing a means for sharing data; improving protocols for establishing authenticity; and/or increasing privacy and sovereignty.<sup>35</sup>

One of the universal attributes of all of these forms of crypto is the lack of any tangible item that exists outside of the blockchain. Cryptoassets are really nothing more than numeric entries on the digital ledger, and as such, they can be said to “exist” anywhere and everywhere there is a computer on which the applicable digital ledger is stored. This necessarily means that bitcoin and every other cryptoasset is, as was intended, global in nature.<sup>36</sup>

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32. Altcoins tend to promote themselves as being “better” than bitcoin in some respect. For a general description of some of the most popular altcoins, see generally Mary Ann Calahan, *Bitcoin or Altcoins: What Should You Invest in?*, FXEMPIRE, [https://perma.cc/5GM9-EL5D]. This is not to say that bitcoin is universally applauded. The vice-chairman of Warren Buffett’s investment firm, Berkshire Hathaway, has said it is “totally asinine,” and a “noxious poison.” Julia Kollwe, *Bitcoin Is ‘Noxious Poison’, Says Warren Buffett’s Investment Chief*, THE GUARDIAN (Feb. 15, 2018), [https://perma.cc/DN4B-GKVY].

33. This was the advent of so-called “utility tokens,” a form of cryptoasset specifically designed with functionality beyond serving as a currency substitute in mind. For a description of how utility tokens might function, see SFOX, *What Are Utility Tokens, and How Will They Be Regulated?*, MEDIUM (Dec. 28, 2018), [https://perma.cc/8VLA-BZ42].

34. A smart contract is a software protocol that executes the terms of a transaction that takes place on a blockchain. See generally Ameer Rosic, *Smart Contracts: The Blockchain Technology That Will Replace Lawyers*, BLOCKGEEKS, [https://perma.cc/D723-FE8U]. Nick Szabo is generally credited with coining the phrase “smart contract” in 1996, prior to the advent of bitcoin. See Magazzeni et al., *supra* note 23.

35. Goforth, *supra* note 12, at 57 n.45 (citing *Tokens, Cryptocurrencies & Other Cryptoassets*, BLOCKCHAIN HUB, [https://perma.cc/349B-FSNA]).

36. “Bitcoin and other crypto-currencies . . . can be accessed on computers throughout the world, not just in modern economies, but also through exchanges and other peer-to-peer networks.” Ed Howden, *The Crypto-Currency Conundrum: Regulating an Uncertain Future*, 29 EMORY INT’L L. REV. 741, 743-44 (2015). As another commentator noted, crypto “is, by design, a borderless medium of exchange.” Jacob Hamburger, *Bitcoins vs. State Money Transmission Laws: Protecting Consumers or Hindering Innovation*, 11 J.L. ECON. & POL’Y 229, 241 (2015) (speaking particularly about bitcoins) (internal quotations omitted).

Pinpointing where an asset is “located” is an impossible and meaningless task. Moreover, the internet allows businesses to interact with customers from anywhere in the world,<sup>37</sup> often on an anonymous or pseudonymous basis.

So when and where are crypto-businesses treated as money transmitters? Remember that bitcoin and all of the initial altcoins were specifically designed to replace fiat and were originally all referred to as cryptocurrencies. It is therefore not surprising that regulatory authorities have been conditioned to treat crypto as “virtual currency.” They are therefore predisposed to regulate businesses that facilitate transmission of crypto as money transmitters.

In order to reach every kind of business that looks like it might serve a payments processing or currency transmission function, money transmitter statutes are often broadly worded and broadly interpreted. This was seen as necessary in order to respond to the policy considerations that the regulatory regimes are designed to address.<sup>38</sup> The result of this is that crypto businesses in the United States find themselves subject to a large number of money transmission regulations, all designed to further legitimate interests.<sup>39</sup> The question is whether the existing paradigm strikes the right balance between the needs of innovators and entrepreneurs (and their customers), and the needs of regulators. To answer this inquiry, it is essential to start with a consideration of the policy justifications and objectives that the existing regulations are intended to address.

### III. WHY ARE MONEY TRANSMITTERS REGULATED?

While it might be convenient if there was consistency in the public policies that have driven the regulation of money

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37. It may not even be possible for a business to know with certainty where customers are located, if they conceal their identities and locations by (for example) spoofing IP addresses and lying on applications. See Mauro Conti et al., *A Survey on Security and Privacy Issues of Bitcoin*, IEEE (Dec. 25, 2017), [<https://perma.cc/3CEF-7FP2>].

38. See *supra* note 13 for the breadth of federal and state definitions of virtual currency. See *infra* Part II of this Article for a discussion of the policy considerations that support the regulation of money services businesses such as money transmitters.

39. See *infra* Part III of this Article for a discussion of some of these regulations and the interests they seek to further.

transmitters, the reality is that there are range of considerations at play. There has long been a divide between the reasons that the federal government seeks to regulate such businesses and the purposes behind state regulation. This might not create insurmountable problems for money transmitters, except that states vary considerably in what they are attempting to accomplish with their regulations, and then in how they have gone about furthering those objectives. The following material in this Part considers first the public policies behind federal regulation of money transmitters and then looks at the objectives that have driven state law.

### A. Federal Policies

When it comes to regulating businesses involved in the provision of money services, including money transmitters, the primary regulatory authority at the federal level is the Financial Crimes Enforcement Network (FinCEN), a bureau of the Treasury Department.<sup>40</sup> Its authority comes from the Bank Secrecy Act (BSA), as that Act has been amended over the years.<sup>41</sup> Pursuant to authority granted in the BSA, FinCEN's mission<sup>42</sup> focuses on

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40. FinCEN was established by Treasury Order 105-08 on April 25, 1990. After the adoption of the PATRIOT Act of 2001, FinCEN was official made a bureau within the Treasury Department. *See* U.S. DEPT. OF TREASURY, TREASURY ORDER 180-01 (2002). This is now reflected in 31 U.S.C. § 310(a), which confirms FinCEN as "a bureau in the Department of the Treasury." The PATRIOT Act is more formally known as the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001, Pub. L. No. 107-56, § 301-77, 115 Stat. 272, 296-342 (2001).

41. The formal name for this act is The Financial Recordkeeping and Reporting of Currency and Foreign Transactions Act of 1970, although it is generally referred to as the Bank Secrecy Act (BSA in this Article). As amended, it is found in Titles I and II of Public Law 91-508, and is codified at 12 U.S.C. §1829b, 12 U.S.C. 1951-1959, and 31 U.S.C. §§ 5311-5314 and 5316-5332. Bank Secrecy Act, Pub. L. No. 91-508, 84 Stat. 1114-24 (1970) (codified as amended in scattered sections of 12 & 31 U.S.C.).

42. As explained on the FinCEN website, the bureau:  
exercises regulatory functions primarily under the Currency and Financial Transactions Reporting Act of 1970, as amended by Title III of the USA PATRIOT Act of 2001 and other legislation, which legislative framework is commonly referred to as the "Bank Secrecy Act" (BSA). The BSA is the nation's first and most comprehensive Federal anti-money laundering and counter-terrorism financing (AML/CFT) statute. In brief, the BSA authorizes the Secretary of the Treasury to issue regulations requiring banks and other financial institutions to take a number of precautions against financial crime . . . .

*What We Do*, FINCEN, [<https://perma.cc/UVC4-PDYM>]. FinCEN's stated mission is "to safeguard the financial system from illicit use, combat money laundering, and promote national security through the strategic use of financial authorities and the collection, analysis,

the prevention of money laundering<sup>43</sup> and funding of illegal activities, particularly the drug trade and more recently, terrorism.<sup>44</sup> Not surprisingly, FinCEN's money transmitter regulations are directed primarily towards solving these problems.

According to the federal government (as set forth on the FinCEN website), “[m]oney laundering is the process of making illegally-gained proceeds (i.e. ‘dirty money’) appear legal (i.e. ‘clean’).”<sup>45</sup> Money laundering became a significant focus of law enforcement efforts during the 1970s, and it increased in priority throughout the 1980s.<sup>46</sup> There was a widespread perception that massive amounts of money were being funneled into and out of the narcotics trade in particular.<sup>47</sup> Thus, anti-money laundering (AML) requirements were geared toward combatting both traditional money laundering and also “reverse” laundering, where clean money was funneled into illegal activities.<sup>48</sup> Since that time, problems associated with money laundering and the financing of criminal and terrorist activities have been a topic of

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and dissemination of financial intelligence.” *Mission*, FINCEN, [https://perma.cc/K7LF-FJJ5].

43. As explained by the Office of the Comptroller of the Currency, money-laundering continues to be a major threat to the American financial system:

Criminals have long used money-laundering schemes to conceal or “clean” the source of fraudulently obtained or stolen funds. Money laundering poses significant risks to the safety and soundness of the U.S. financial industry. With the advent of terrorists who employ money-laundering techniques to fund their operations, the risk expands to encompass the safety and security of the nation.

Office of the Comptroller of the Currency, *Bank Secrecy Act (BSA)*, U.S. DEPT. TREAS., [https://perma.cc/JV52-UW6Z].

44. The Patriot Act, Pub. L. No. 107-56, § 301-77, 115 Stat. 272, 296-342 (2001), specifically expanded the reach of the BSA to include counter-terrorism financing initiatives. See *History of Anti-Money Laundering Laws*, FINCEN, [https://perma.cc/UA7Y-Y8MF].

45. *Id.*

46. The history of efforts designed to combat money laundering in the U.S. is described briefly in Ann Eberhardt, *History and Enforcement of Anti-Money Laundering Laws in the U.S.*, CLAIMS JOURNAL (Jan. 8, 2018), [https://perma.cc/ZW6J-VD7Z]. See also Alina Laumann, *The History of Anti-Money Laundering — Events, Regulations, and Adaptations in the United States*, KROLL (July 16, 2019), [https://perma.cc/65Q2-47ML].

47. See Sabrina Adamoli, *Money laundering*, ENCYC. BRITANNICA (Feb. 13, 2020), [https://perma.cc/K62D-9GYC] (discussing both the international efforts to target profits of unlawful activities as a way of combating drug trafficking, and the implementation of these efforts in the United States).

48. Douglas A. Leff, *Money Laundering and Asset Forfeiture: Taking the Profit Out of Crime*, 55 U.S. ATT'Y'S BULL. 36, Nov. 2007, at 42-43 (discussing use of 18 U.S.C. § 1956(a)(2)(A) to combat non-terrorism reverse money laundering).

perennial concern for federal legislators. This has resulted in many federal laws seeking to address these problems.<sup>49</sup>

Although there were a number of legislative enactments throughout the 1990s, it was the USA PATRIOT Act of 2001 (the Patriot Act),<sup>50</sup> enacted in the wake of the September 11, 2001, terrorist attacks that most significantly expanded AML legislation in the United States. The Patriot Act added new record-keeping requirements, expanded reporting and record-keeping requirements to a variety of nonbank financial institutions, such as broker-dealers and insurance companies, and broadened the reach of the already expansive money-laundering laws.<sup>51</sup> These requirements apply, among other things, to money transmitters. Under its expanded provisions, the BSA authorizes the Secretary of the Treasury to issue regulations requiring financial institutions to keep records and file reports necessary to carry out its AML and counter terrorism funding (CTF) missions.<sup>52</sup> This authority has been delegated to FinCEN.<sup>53</sup>

These developments explain why the overwhelming emphasis on money transmitter regulation at the federal level has been on preventing money laundering and the funding of other criminal behavior. Only recently has the federal government evidenced

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49. The list of federal acts addressing money laundering and funding of illegal activities includes all of the following:

- Bank Secrecy Act (1970) (generally referred to as the BSA)
- Money Laundering Control Act (1986)
- Anti-Drug Abuse Act of 1988
- Annunzio-Wylie Anti-Money Laundering Act (1992)
- Money Laundering Suppression Act (1994)
- Money Laundering and Financial Crimes Strategy Act (1998)
- Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001 (known as the USA PATRIOT Act or simply the Patriot Act)
- Intelligence Reform & Terrorism Prevention Act of 2004

See Laumann, *supra* note 46.

50. The Patriot Act, Pub. L. No. 107-56, § 301-77, 115 Stat. 272, 296-342 (2001).

51. The breadth of the reporting and oversight requirements is so great that many criticisms have been leveled at the Patriot Act notwithstanding general sympathy with the need to address money laundering and funding of terrorism. See, e.g., Susan Nevelow Mart, *The Chains of the Constitution and Legal Process in the Library: A Post-USA Patriot Reauthorization Act Assessment*, 33 OKLA. CITY U. L. REV. 435 (2008).

52. See 31 U.S.C. §§ 5311, 5318(h) (2014).

53. See U.S. DEPT. OF TREASURY, TREASURY ORDER 180-01 (2002).

growing concern over the need to protect customers in the money transmitter context.<sup>54</sup>

### B. State Concerns

States have taken a variety of different approaches to the regulation of money transmitters, in large measure because they are concerned with different risks. While FinCEN is focused on preventing money laundering and the funding of criminal enterprises, state law is often predicated on a much broader, sometimes amorphous or unarticulated, set of policy considerations.

In some states, the policies behind state money transmitter laws are clear. For example, some jurisdictions have adopted explicit statements of legislative objectives as part of their money transmitter acts. California's money transmission act includes a specific legislative declaration that the purpose of the act is “[t]o protect the interests of consumers of money transmission businesses in this state, to maintain public confidence in financial

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54. See Brian Knight, *Federalism and Federalization on the Fintech Frontier*, 20 VAND. J. ENT. & TECH. L. 129, 155 (2017) (noting that “the federal government, through the CFPB (the Consumer Financial Protection Bureau), is expressing increased interest in consumer protection regarding the money transmission context”) The CFPB was created on July 2010, as part of the Dodd-Frank Wall Street Reform and Consumer Protection Act. Consumer Fin. Prot. Bureau, *Creating the Consumer Bureau*, CFPB, [https://perma.cc/MF5Q-B8NB].

In general terms “Dodd-Frank authorizes the CFPB to take action against institutions engaged in unfair, deceptive or abusive acts or practices or that otherwise violate federal consumer financial laws.” Sidley Austin LLP, *U.S. Consumer Financial Protection Bureau's Principles for Data Aggregation Services Could Have Broad Implications* 3 (Nov. 9, 2017), [https://perma.cc/4Q6J-3M5X]. Pursuant to this authority, in 2016, the CFPB took action against Dwolla, Inc., an online payment platform that had deceived consumers about its data security practices. See Consumer Fin. Prot. Bureau, *CFPB Takes Action Against Dwolla for Misrepresenting Data Security Practices*, CFPB (Mar. 2, 2016), [https://perma.cc/7E8G-Q8T9] (use the screenshot view). The CFPB has continued to monitor money transmitters with a view to protecting consumers, as indicated in its August 27, 2019 settlement with Maxitransfers Corporation. Consumer Fin. Prot. Bureau, *Consumer Financial Protection Bureau Settles with Maxitransfers Corporation*, CFPB (Aug. 27, 2019), [https://perma.cc/SR3E-WCYH] (use screenshot view).

Keep in mind, however, that there are other federal regulatory authorities that have specific missions designed to protect members of the public. Both the Securities and Exchange Commissions (SEC) and the Commodities Futures Trading Commission (CFTC) recognize the need to protect the public as overarching policy mandates. See, e.g., *What We Do*, SEC, [https://perma.cc/58GU-X86Q] (listing the need “to protect investors” first among its priorities); *Mission & Responsibilities*, CFTC, [https://perma.cc/RK3L-2PKW] (explicitly setting out the goal of lowering the risks of futures and swaps markets to “the public”).



institutions doing business in this state, and to preserve the health, safety, and general welfare of the people of this state . . . .”<sup>55</sup> Similarly, the legislative declaration in Colorado’s Money Transmitters Act states that it is “imperative that the integrity, experience, and financial responsibility and reliability of those engaged in the various types of businesses dealing in the instruments be above reproach . . . [i]n order that the people of this state may be safeguarded from default in the payment of these instruments.”<sup>56</sup> The Kentucky Money Transmitters Act of 2006 also includes an express statement about the underlying legislative objectives:

It is the intent of the General Assembly to establish a state system of licensure and regulation to ensure the safe and sound operation of money transmission to ensure that this business is not used for criminal purposes, to promote confidence in the state’s financial system, and to protect the public interest.<sup>57</sup>

New York includes a number of different policy objectives in its Financial Services Laws, which applies to money transmitters.<sup>58</sup> These include fostering “the growth of the financial industry in New York,” “protect[ing] users of financial products . . . from financial impaired or insolvent providers of such services,” and “eliminat[ing] financial fraud.”<sup>59</sup>

Other states have statutes that lack a specific statement of legislative intent, but the general objectives and guiding policies behind the laws may be gleaned from other sources. For example, a dozen jurisdictions have enacted the Uniform Money Services Act (UMSA).<sup>60</sup> The ULC, which drafted the UMSA, describes it

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55. CAL. FIN. CODE § 2001(d) (West 2015).

56. COLO. REV. STAT. § 11-110-102 (2017).

57. KY. REV. STAT. ANN. § 286.11-067 (West 2006).

58. N.Y. FIN. SERV. LAW § 201(b)(1)-(7) (McKinney 2011).

59. N.Y. FIN. SERV. LAW § 201(b)(1), (4), (6) (McKinney 2011).

60. UNIF. MONEY SERV. ACT prefatory note, pt. A (UNIF. LAW COMM’N 2004) [hereinafter *UMSA*] (commenting on the goal of creating a uniform system of regulation to serve as a larger deterrent to money laundering and to assist law enforcement generally). The UMSA, with comments, can be downloaded from the ULC website at *Money Services Act*, UNIF. LAW COMM’N, [<https://perma.cc/8ES7-DG7T>]. Originally promulgated in 2000, the act was amended in 2004. The text of the amendments as approved at the ULC’s 2004 annual meeting may be downloaded from the ULC website at *Money Services Act: Committee Archive*, UNIF. LAW COMM’N, [<https://perma.cc/8ES7-DG7T>].

As of the date this Article was written, Alaska, Arkansas, Hawaii, Iowa, New Mexico, North Carolina, Puerto Rico, South Carolina, Texas, Vermont, U.S. Virgin Islands, and

as a “safety and soundness law,” designed to promote uniformity while furthering the prevention and detection of money laundering.<sup>61</sup> While none of the UMSA’s provisions explicitly articulate these objectives, states enacting this statute are likely to have been concerned with the same issues that drove the ULC to propose the UMSA, regardless of whether they have explicitly adopted the UMSA’s prefatory note, which is where these objectives are set out.<sup>62</sup>

In Minnesota, the title of the state act gives a fairly clear indication of the legislative priorities. That state’s statute is entitled: “Money Transmission—Protection from Financial Abuse, Financial Exploitation, and Fraud—Requirements.”<sup>63</sup>

In other jurisdictions, there may be other evidence of the goals behind money transmitter provisions. For example, a report detailing the objectives of Florida’s money transmitter regulations noted that Florida has traditionally been concerned with eliminating money laundering (a concern due to international drug trafficking activity in South Florida) and check-cashing businesses that operate as payday lenders.<sup>64</sup>

On the other hand, there are also states where the underlying motives are unclear. For example, both the Texas and Illinois statutes and regulations are silent as to why those jurisdictions have chosen to regulate money transmitters.<sup>65</sup> Even in these cases, discussions with individual regulators may provide some insights into the probable goals of the legislature,<sup>66</sup> although that is not necessarily true everywhere. In very general terms, it appears that most states have a very strong interest in looking out

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Washington had all enacted the statute. No pending legislation was mentioned, and the last enactments listed by the ULC occurred in 2016. See *Money Services Act*, UNIF. LAW COMM’N, [https://perma.cc/M5G7-AKHL] (listing each state that has adopted the Money Services Act along with the year it was enacted in each jurisdiction).

61. See *UMSA*, *supra* note 60, at prefatory note, pt. A.

62. See *id.*

63. Money Transmission—Protection from Financial Abuse, Financial Exploitation, and Fraud—Requirements, 2014 Md. Laws Ch. 421 (2014) (codified as amended at MD. CODE ANN., FIN. INST. §§ 12-401 (West 2014)).

64. See FLA. S. REP. NO. 2008-101, COMM. ON BANKING & INS., *Regulation of Money Services Businesses*, at 1 (2007), [https://perma.cc/8FG4-UD6W].

65. TEX. FIN. CODE ANN. § 151.002 (West 2019); 205 ILL. COMP. STAT. ANN. 657/5 (2004).

66. See, e.g., Lo, *supra* note 6, at 117.

for the interests of consumers located in the state, with many states also expressing concerns about issues such as money laundering and other criminal activities.

Given the breadth of these concerns, how do the federal and state governments go about defining the kinds of businesses that need to be regulated in order to achieve their varied policy objectives? The following material looks first at how federal law determines what businesses are to be regulated as money transmitters, and then considers how states have approached this question.

#### IV. WHAT IS A “MONEY TRANSMITTER” UNDER FEDERAL LAW?

At the federal level, money transmitters are regulated pursuant to authority granted in the BSA. While the title of the BSA might lead one to believe that its provisions apply to “banks,” in fact it includes requirements applicable to a wide range of “financial institutions.” The BSA defines the term “financial institution” to include, among other things, “any person who engages as a business in the transmission of funds . . . .”<sup>67</sup> The businesses included within this definition are generally referred to as money services businesses (MSBs),<sup>68</sup> and they specifically include anyone functioning as a money transmitter.<sup>69</sup> FinCEN’s regulations further explain that “money transmitter” includes anyone who “provides money transmission services.”<sup>70</sup> In turn, “money transmission services” is defined to mean “the acceptance of currency, funds, or other value that substitutes for currency from one person and the transmission of currency, funds, or other value that

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67. “Financial Institution” is defined generally in title 18, which covers crimes and criminal procedure generally, as including banks, depository institutions, and similar organizations. *See* 18 U.S.C. § 20 (2009). The BSA, however, has its own definition of financial institution, so that for its purposes, that term includes any:

licensed sender of money or any other person who engages as a business in the transmission of funds, including any person who engages as a business in an informal money transfer system or any network of people who engage as a business in facilitating the transfer of money domestically or internationally outside of the conventional financial institutions system.

31 U.S.C. § 5312(a)(2)(R) (2004).

68. *See* 31 C.F.R. § 1010.100(ff) (2014).

69. *See 2011 Regulations, supra* note 13.

70. 31 C.F.R. § 1010.100(ff)(5).

substitutes for currency to another location or person by any means.”<sup>71</sup>

Under these definitions, a money transmitter must be doing business on behalf of one or more third parties. As an example of an activity that does not involve money transmission because there was no third party involved, FinCEN concluded in 2005 that a business set up to wire the founder’s personal funds to Columbia for investment purposes was not a “money transmitter.”<sup>72</sup>

In addition, the regulations list six different kinds of activities that will not be enough to cause a person to be subject to money transmitter requirements:

1. Merely providing “delivery, communication, or network access services . . . to support money transmission services”;
2. “Act[ing] as a payment processor to facilitate the purchase of, or payment for [goods or services] through a clearance and settlement system by agreement with the creditor or seller”;
3. “Operat[ing] a clearance and settlement system or otherwise act[ing] as an intermediary solely between BSA regulated institutions”;
4. Acting solely as a custodian and “physically transport[ing] currency” or other value that substitutes for currency “as a person primarily engaged in such business”, on behalf of a customer to an account owned by the same customer at a financial institution;
5. “Provid[ing] prepaid access”; or
6. Accepting and transmitting funds “integral to the sale of goods or . . . services, other than money transmission services.”<sup>73</sup>

Even with these limitations, the federal definition is quite broad. A business can be a money transmitter subject to FinCEN regulations regardless of where it is physically located, whether or not the money transmission activities are conducted on a regular basis, or whether operations are conducted through an organized

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71. 31 C.F.R. § 1010.100(ff)(5)(i)(A).

72. *FinCEN Ruling 2005-4 – Definition of Money Services Business (“Doing Business” as a Money Services Business)*, FINCEN (July 1, 2005), [<https://perma.cc/5DW7-VUY6>].

73. 31 C.F.R. § 1010.100(ff)(5)(ii)(A)-(F).

entity.<sup>74</sup> FinCEN's MSB requirements will apply whenever money transmission activities are being conducted in the United States, in whole or in substantial part, and this can be satisfied with a showing that the money transmitter maintains "any agent, agency, branch, or office within the United States."<sup>75</sup>

In addition, although some other money services businesses have a minimum threshold that they must meet before they are subjected to FinCEN's regulatory requirements,<sup>76</sup> the federal definition of money transmitter does not include a minimum activity level. It does, however, limit applicability of the MSB requirements so that the rules will not apply to banks,<sup>77</sup> a natural person who engages in the activities only "on an infrequent basis and not for gain or profit,"<sup>78</sup> or any person registered with, and functionally regulated or examined by, the SEC or the CFTC.<sup>79</sup> Note that this last exclusion does not apply to publicly held companies simply because they have issued one or more classes of securities registered under the Securities Exchange Act of 1934,<sup>80</sup> or to an issuer conducting an offering registered under the Securities Act of 1933.<sup>81</sup> Registration of securities in and of itself does not subject the issuer to the SEC's control aside from imposing reporting, accounting, and other requirements designed to ensure disclosure of material information.<sup>82</sup> For this reason, "these entities are not intended to be excluded from the rule's definition of money

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74. STEVEN MARK LEVY, FED. MONEY LAUNDERING § 18.04 (2d Ed. 2019 Supp., Aspen).

75. 31 C.F.R. § 1010.100(ff).

76. Money transmitters are the only form of MSB that are subject to regulation even if they do not engage in more than \$1000 in such activities in any day. See BANK COMPL. GUIDE ¶ 101-948 (2011), Westlaw 12877955.

77. 31 C.F.R. § 1010.100(ff)(8)(i).

78. 31 C.F.R. § 1010.100(ff)(8)(iii).

79. 31 C.F.R. § 1010.100(ff)(8)(ii).

80. The Securities Exchange Act of 1934 (the "'34 Act") is codified at 15 U.S.C. §§ 78a-78q (1934). The '34 Act imposes a registration requirement in order for market professionals to use the services of a national exchange. The requirements are set out in § 12 of the '34 Act, as codified at 15 U.S.C. § 781 (2015).

81. The Securities Act of 1933 (the "'33 Act") is codified at 15 U.S.C. §§ 77a-77aa. The registration requirement appears in section 5 of the '33 Act, as codified at 15 U.S.C. § 77e (2012).

82. 64 FED. REG. 45,438, 45,446 (Aug. 20, 1999).

services businesses because the Commission neither regulates nor examines the business activities of those companies.”<sup>83</sup>

FinCEN’s first major guidance on how its money transmitter requirements should be applied to crypto-based businesses came in 2013 (the 2013 Guidance), making the Bureau one of the earliest regulators to address cryptoassets.<sup>84</sup> However, the groundwork for FinCEN’s current approach was actually laid in 2011, when FinCEN finalized a rule that expanded the meaning of the phrase “money transmission services” to include “the acceptance of currency, funds, or other value that substitutes for currency from one person and the transmission of currency, funds, or other value that substitutes for currency to another location or person by any means.”<sup>85</sup> While not explicitly mentioning crypto or “virtual currency,” this expansion of money transmission to cover “other value that substitutes for currency” provided the primary basis for applying AML requirements to actors in the crypto space.<sup>86</sup>

The 2013 Guidance<sup>87</sup> applies only to crypto convertible into fiat currency, either directly or indirectly, and divides persons involved with such cryptoassets into three categories: users, administrators, and exchangers.<sup>88</sup> Users are defined as persons who obtain the currency “to purchase real or virtual goods . . . .”<sup>89</sup> Users are not regulated as money transmitters.<sup>90</sup>

As for the other two categories, the 2013 Guidance stated:

An administrator or exchanger that (1) accepts and transmits a convertible virtual currency or (2) buys or sells convertible virtual currency for any reason is a money transmitter under FinCEN’s regulations . . . . FinCEN’s regulations define the term “money transmitter” as a person that provides money transmission services, or any other person engaged in the transfer of funds. The term “money transmission services” means “the acceptance of currency, funds, or other value that

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83. *Id.*

84. 2013 GUIDANCE, *supra* note 13.

85. 2011 Regulations, *supra* note 13.

86. *Id.* at 43,592.

87. 2013 GUIDANCE, *supra* note 13.

88. *Id.* at n. 6 and accompanying text.

89. 2013 GUIDANCE, *supra* note 13.

90. *Id.*

substitutes for currency from one person and the transmission of currency, funds, or other value that substitutes for currency to another location or person by any means.”

The definition of a money transmitter does not differentiate between real currencies and convertible virtual currencies.<sup>91</sup>

The federal determination of who is a money transmitter is thus very inclusive, turning on the very broad definition of money transmission services, which specifically includes not only currency and funds, but also other value that substitutes for currency.<sup>92</sup>

### V. WHAT IS A “MONEY TRANSMITTER” UNDER STATE LAW?

When it comes to the definition of money transmission under state law, there is considerable variation, both in the wording of the state statutes and in the determination of whether the applicable statutory language applies to virtual currencies.

Prior to the advent of cryptoassets, there was already considerable variation in state approaches. Many state statutes were broad in their approach, covering not only the transmission of fiat currency but also other items of “monetary value,” or “substitutes” for currency. For example, the UMSA<sup>93</sup> defines money transmission as the “selling or issuing payment instruments, stored value, or receiving money or monetary value for transmission. The term does not include the provision solely of delivery, online or telecommunications services, or network access.”<sup>94</sup> A comment to this section specifically acknowledges that this definition “subsumes several activities or functions,” and notes that “[t]he grouping of funds transmission and the sale or issuance of payment instruments and stored value is consistent with existing state practice.”<sup>95</sup> As of the date this Article was written, Alaska, Arkansas, Hawaii, Iowa, New Mexico, North Carolina, Puerto

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91. *Id.*

92. *See supra* note 85.

93. *UMSA*, *supra* note 60, at prefatory note, pt. A

94. *Id.* at § 102(14).

95. *Id.* at § 102, cmt. 9.

Rico, South Carolina, Texas, Vermont, U.S. Virgin Islands, and Washington have versions of the UMSA.<sup>96</sup>

Other states have alternative language that is just as broad. For example, Georgia's statute says:

“Money transmission,” “transmit money,” or “transmission of money” means engaging in the business of receiving *money or monetary value* for transmission or transmitting money or monetary value within the United States or to locations abroad by any and all means, including, but not limited to, an order, wire, facsimile, or electronic transfer.<sup>97</sup>

In Maryland, “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.”<sup>98</sup> Other states use similar language in their definitions.<sup>99</sup>

At the other end of the spectrum are the two states that have chosen not to regulate domestic money transmitters. Montana has no money transmission statute at all, and Massachusetts regulates only foreign money transmitters, having no provisions that apply to domestic businesses.<sup>100</sup>

Also complicating the picture are jurisdictions like Nevada, where there is a money transmission statute that lacks any helpful definitions, leaving the interpretation and breadth of the statutory requirements for the courts to determine.<sup>101</sup>

There are some common themes in the definitions of money transmitters or money transmission businesses employed by most states. Generally speaking, there are few explicit limitations on what kind of business can be regulated as a money transmitter.

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96. See *UMSA*, *supra* note 60. No pending legislation was mentioned, and the last enactments listed by the ULC occurred in 2016.

97. GA. CODE ANN. § 7-1-680(13) (2016) (emphasis added). Closed loop transactions are exempted from this otherwise expansive definition.

98. MD. CODE ANN., FIN. INST. § 12-401(m)(1) (West 2014) (emphasis added).

99. See, e.g., MICH. COMP. LAWS §487.1003(c) (2019) (defining “money transmission services” as “selling or issuing payment instruments or . . . prepaid access devices or vehicles or receiving money or *monetary value* for transmission”) (emphasis added).

100. See, e.g., MASS. GEN. LAWS ch. 169, §§ 1-16 (2020).

101. See NEV. REV. STAT. § 671.010 (1985) (regulating the business of transmitting money or credits without providing a statutory definition of money transmission or any other guidance on what this entails). See generally NEV. ADMIN. CODE §§ 671.005-.100 (2016).



Most statutes do not include any minimum activity threshold to trigger the statute, do not require the business to focus on consumer-oriented services, and do not seem concerned about the method used to accomplish the transmission of value.<sup>102</sup> In addition, most statutes are not limited by their terms to “money,” although this does not automatically mean that crypto-based businesses will be covered by the state requirements.<sup>103</sup>

To borrow a pun based on terminology common in the crypto space, there is a lack of consensus about how crypto should fit into the regulatory regime.<sup>104</sup> This Article does not purport to provide an exhaustive listing of the different state approaches to the issue of whether crypto businesses can be money transmitters. The following material does, however, describe enough variation to provide a basis for understanding the difficulty that a crypto-based enterprise is likely to have if it intends to do business in the United States.

#### A. States that Have no Clear or no Definitive Guidance

There are a number of states that have yet to issue official guidance on the issue of whether crypto-based businesses fit within the state’s money transmitter provisions or where the existing guidance is ambiguous. As of the date this was written, the list of states with no published guidance and a money transmitter statute that does not clearly mention crypto or virtual currency includes all of the following: Arizona, Indiana, Iowa, Kentucky,

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102. To illustrate this, consider Idaho’s statute which covers transmission “by any and all means including, but not limited to, payment instrument, wire, facsimile or electronic transfer.” IDAHO CODE § 26-2902(11) (1994). Illinois uses the same language, although its official statute is formatted differently. 205 ILL. COMP. STAT. 657/5 (2004). Kansas’ provision covers transmission “by wire, facsimile, electronic means or any other means, except that money transmission does not include currency exchange where no transmission of money occurs . . . .” KAN. STAT. ANN. § 9-508(h) (2017); *see also* N.J. STAT. ANN. § 17:15C-2 (West 1998) (covering “transmission . . . 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”).

103. See *infra* notes 105-79 and accompanying text for a consideration of the range of state reactions to this question.

104. Matthew E. Kohen & Justin S. Wales, *State Regulations on Virtual Currency and Blockchain Technologies*, CARLTON FIELDS (Aug. 29, 2019), [<https://perma.cc/AK2D-HRD6>].

Maine, Michigan, Minnesota, Mississippi, Nebraska, Nevada, Ohio, Oklahoma, South Dakota, and West Virginia.<sup>105</sup>

Some states have no official guidance, but there is some indication of how regulators intend to apply the state laws. In Arkansas, for example, the state Securities Department has issued no action letters in response to inquiries from crypto-based businesses, determining that the Securities Department will not recommend that the businesses be penalized for failing to procure money transmitter licenses.<sup>106</sup> Unfortunately, these opinion letters may not be relied upon by anyone other than the persons to whom they are directed, although they do provide an indication of how the state currently views its money transmitter statute.

Similarly, there is no official guidance in Wisconsin, but that state has refused to issue money transmitter licenses to virtual currency businesses and requires an agreement, if a company deals in virtual currency, stating that the company will not use virtual currency to transmit money.<sup>107</sup>

Idaho's money transmitter statute does not define virtual currency or include monetary value,<sup>108</sup> and there are no official regulations that consider whether crypto-based businesses are subject to its requirements. However, the Idaho Department of Finance, which administers the state money transmitters act, has opined that a crypto exchange that accepts legal tender for later delivery to a third party in connection with the purchase of crypto is a money transmitter.<sup>109</sup> On the other hand, the Department has also issued several "No Action & Opinion Letters" on money

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105. *See id.* This list comes in part from the Kohen & Wales article, although online searches confirm the lack of official guidance in these jurisdictions as of September 2019.

106. *See, e.g.*, CEX.IO LTD, Ark. Sec. Dep't No-Action Letter No. 18-NA-0006 (July 18, 2018), [<https://perma.cc/C3UG-YUPB>] (agreeing that a virtual currency purchase and sale and exchange product should not need a license under the state's Uniform Money Services Act).

107. *See Sellers of Checks*, STATE OF WIS. DEP'T OF FIN. INST., [<https://perma.cc/FB33-VHNY>] (stating that the law does not currently give the Department authority to regulate virtual currency, but this may be changed at any time by new regulations or interpretations).

108. IDAHO CODE § 26-2902 (1994).

109. *Idaho Money Transmitters Section*, IDAHO DEP'T OF FIN., [<https://perma.cc/2ZL3-3YX3>] ("If you act as a virtual/digital currency exchanger and accept legal tender (e.g., government backed/issued 'fiat' currencies) for later delivery to a third party in association with the purchase of a virtual currency, then you must be licensed as a money transmitter with the Department of Finance.").

transmitters addressing how the state's money transmission laws apply to virtual currency operations.<sup>110</sup> A typical letter was posted July 5, 2019. In it, the Department wrote, “[a]n exchanger that *sells its own inventory* of virtual currency is generally not considered a money transmitter . . . [but] an exchanger that holds customer funds while arranging a satisfactory buy/sell order with a third party, and transmits the virtual currency . . . between buyer and seller, will typically be considered . . . a money transmitter . . . .”<sup>111</sup> This letter does not clarify the meaning of “customer funds.” Under the prior guidance, if the funds are fiat currency, the exchange will be a money transmitter.<sup>112</sup> The question of what happens if an exchange only deals in various forms of crypto issued by others is not specifically addressed, leaving open the question of how broadly the state might apply its money transmitter requirements.

On the other hand, a number of states have clearly indicated how they intend to apply their money transmitter requirements. The clearest guidance is available in those states that have new legislation specifically dealing with crypto. A number of jurisdictions have amended their state statutes to clarify this issue, but the approaches that these states have taken vary widely.

### **B. States with New Provisions Exempting Crypto Businesses**

In 2017, New Hampshire amended its money transmitter statute to exempt “[p]ersons who engage in the business of selling or issuing payment instruments or stored value solely in the form of convertible virtual currency or receive convertible virtual currency for transmission to another location.”<sup>113</sup> Wyoming has similarly exempted virtual currency businesses from its money transmitter statutes,<sup>114</sup> a decision that is not surprising for the state that

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110. See *Money Transmitters*, IDAHO DEP'T OF FIN., [https://perma.cc/U2Q2-YGMQ].

111. Idaho Dept. of Fin. No-Action Letter Re: Idaho Money Transmitter License Inquiry (July 5, 2019), [https://perma.cc/GKY9-3JM5].

112. See *id.*

113. N.H. REV. STAT. ANN. § 399-G:3(VI-a) (2017).

114. WYO. STAT. ANN. § 40-22-104(a)(vi) (2020) (specifying that the act shall not apply to “[b]uying, selling, issuing, or taking custody of payment instruments or stored value in the form of virtual currency or receiving virtual currency for transmission to a location within or outside the United States by any means”).

is regarded as being the most pro-crypto jurisdiction in the country.<sup>115</sup>

Most states that have enacted new provisions have gone in the other direction, specifically amending their statutes so that they clearly include crypto within the ambit of money transmission.

### C. States with New Provisions Regulating Crypto

Effective August 2017, the Alabama Monetary Transmission Act defines “monetary value” as “[a] medium of exchange, including virtual or fiat currencies, whether or not redeemable in money.”<sup>116</sup> The act therefore requires every person engaging in the business of monetary transmission in Alabama (including the receipt of virtual currency for transmission) to obtain a license from the state.<sup>117</sup> North Carolina similarly expanded its act to define virtual currency traders as money transmitters and, as a result, requires they obtain a license.<sup>118</sup>

In 2017, Vermont added “virtual currency” to the list of defined terms in its money transmission act,<sup>119</sup> although it appears that this did not mark a substantive change in the way the state interpreted its money transmitter requirements.<sup>120</sup> Connecticut took similar action, amending its money transmitter act in 2018 to add a specific definition of virtual currencies.<sup>121</sup> To some

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115. Wyoming’s pro-crypto bent has been widely observed. *See, e.g.*, Gregory Barber, *The Newest Haven for Cryptocurrency Companies? Wyoming*, WIRED (June 13, 2019), [<https://perma.cc/LMG8-XE9B>]; Benjamin Bain, *Wyoming Aims to Be America’s Cryptocurrency Capital*, BLOOMBERG BUSINESSWEEK (May 15, 2018), [<https://perma.cc/C2LF-KKKX>].

116. ALA. CODE § 8-7A-2(8) (2017).

117. ALA. CODE § 8-7A-5(a).

118. *See* N.C. GEN. STAT. § 53-208.42(13)(b) (2018).

119. Vermont’s Money Services Act defines “money transmission” to include “selling or issuing” stored value and “receiving money or monetary value for transmission to a location within or outside the United States.” VT. STAT. ANN. § 2500(9) (2019). As used in the act, monetary value means a medium of exchange “whether or not redeemable in money.” VT. STAT. ANN. § 2500(6). And as of 2017, “virtual currency” is defined as a “medium of exchange, unit of account, or a store of value” that can be exchanged for “money or other convertible virtual currency.” VT. STAT. ANN. § 2500(13).

120. *See, e.g.*, Poloniex, LLC, Docket No. 19-006-B, 2019 WL 2491641 (Vt. Sec. Div. May 22, 2019) (specifically noting that the state “always” interpreted its money transmitter act to cover virtual currency).

121. CONN. GEN. STAT. § 36a-596(18) (2018).

extent, this was not necessary because, by October 1, 2017, Connecticut had already subjected any person “in the business of money transmission in this state by receiving, transmitting, storing or maintaining custody or control of virtual currency on behalf of another person” to regulation.<sup>122</sup> Similarly, in 2017, Washington amended its money transmission statute, the Washington Uniform Money Services Act,<sup>123</sup> to include virtual currencies.<sup>124</sup> “Money transmission” is now defined in that state as “receiving money or its equivalent value (equivalent value includes virtual currency) . . . .”<sup>125</sup> Although the statutory language is new, the position taken is consistent with interim guidance that had been in effect in Washington since 2014.<sup>126</sup>

Georgia has also amended its money transmitter act to add virtual currency.<sup>127</sup> However, in the spring of 2016, the Georgia legislature authorized the state’s Department of Banking and Finance “to enact rules and regulations that apply solely to persons engaged in money transmission or the sale of payment instruments involving virtual currency,”<sup>128</sup> in order to “[f]oster the growth of businesses engaged in money transmission or the sale of payment instruments involving virtual currency in Georgia and spur state economic development.”<sup>129</sup> This raises the possibility that the state might at some point exempt such businesses from typical money transmission requirements. To date, this is not the direction the agency has taken, and on July 26, 2018, the Department issued a cease and desist order to a crypto company, on the basis that it was engaging in unlicensed money transmission.<sup>130</sup>

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122. CONN. GEN. STAT. § 36a-603(b) (2017) (requirement that the company have sufficient minimum assets).

123. *See generally* WASH. REV. CODE § 19.230 (2017).

124. WASH. REV. CODE § 19.230.010(30).

125. WASH. REV. CODE § 19.230.010(18).

126. Memorandum from Deborah Bortner, Dir. of the Div. of Consumer Serv.’s of the Dep’t of Fin. Inst.’s of Wash. on Virtual Currency Activities Under the Uniform Money Services Act to Virtual Currency Companies Operating or Wishing to Operate in Washington State 1-2 (Dec. 8, 2014), [<https://perma.cc/ZB5Y-J3SA>] (providing interim regulatory guidance).

127. GA. CODE ANN. § 7-1-680(26) (2016).

128. GA. CODE ANN. § 7-1-690(b).

129. GA. CODE ANN. § 7-1-690(b)(1).

130. Press Release, Ga. Dep’t. of Banking & Fin., Department of Banking and Finance Orders CampBX, Bitcoin Trading Platform, to Cease and Desist (July 26, 2018), [<https://perma.cc/7BQZ-CB4Z>].

The state with the most notoriously aggressive regulation of crypto is New York. In 2015, the New York State Department of Financial Services established a comprehensive regulatory framework requiring businesses that engage in transactions involving any form of virtual currency to obtain a new license, called the “BitLicense,” from the state.<sup>131</sup> There are a number of requirements that must be met before a business will be granted the license, including not only AML and cybersecurity policies, but also strict compliance and supervisory procedures.<sup>132</sup> The requirements are so onerous that there have been widespread reports of crypto businesses “fleeing” the state.<sup>133</sup> It is so difficult and time-consuming to comply with the regulations that when the state granted a new license in March 2019, the total number of BitLicenses in the state only reached a total of 18.<sup>134</sup>

While legislation may be the most definitive way to determine whether virtual currency is covered by a state’s money transmitter laws, other forms of guidance are also possible.

#### D. Interpretive Guidance Excluding Crypto Businesses

Alaska is one jurisdiction with no blockchain, cryptocurrency, or virtual currency references in the state statutes or regulations. However, the state’s Division of Banking and Services has issued guidance to the effect that it is not authorized to regulate virtual currencies as only transactions involving fiat currencies are subject to the state’s money transmitter law.<sup>135</sup>

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131. See generally N.Y. COMP. CODES R. & REGS tit. 23, § 200 (2015); Sarah Jane Hughes & Stephen T. Middlebrook, *Advancing a Framework for Regulating Cryptocurrency Payments Intermediaries*, 32 YALE J. OF REG. 495, 536 (2015) (explaining that the “proposed framework for regulating cryptocurrency businesses [was] dubbed the ‘BitLicense’”); Press Release, N.Y. Dep’t. of Fin. Serv.’s, NY DFS Releases Proposed BitLicense Regulatory Framework for Virtual Currency Firms (July 17, 2014), [<https://perma.cc/8N39-L4DL>].

132. See N.Y. COMP. CODES R & REGS tit. 23, §§ 200.3, 200.4, 200.7, 200.15, 200.16 (2015).

133. Daniel Roberts, *Behind the “Exodus” of Bitcoin Startups from New York*, FORTUNE (Aug. 14, 2015), [<https://perma.cc/G2BC-B5WZ>].

134. See Jessica Klein, *New York Just Granted Its 18th BitLicense*, BREAKERMAG (Mar. 28, 2019), [<https://perma.cc/5KAV-EULG>] (also noting that “[m]any of these companies had to wait a while between the time they applied for their BitLicenses and the time they were granted them. In May 2018, Fortune reported that Genesis Global Trading (the fifth BitLicense grantee) had to wait close to three years for approval.”)

135. See Kohen & Wales, *supra* note 104.

A number of other states where finance and money transmitter laws do not mention virtual currencies or crypto have reached the same or similar conclusions. For example, the Illinois Department of Financial and Professional Regulation has issued guidance concluding that virtual currencies are not “money” under the Illinois money transmitters act, and therefore “[a] person or entity engaged in the transmission of solely digital currencies, as defined, would not be required to obtain a . . . license.”<sup>136</sup> North Dakota’s Department of Financial Institutions has issued guidance under that state’s law to the effect that: “The purchase, sale, or exchange of virtual currency does not in and of itself require a money transmitter license.”<sup>137</sup> Tennessee takes the same position, having issued guidance explaining that it does not consider virtual currency to be money under its money transmitter act and therefore, no license is required.<sup>138</sup>

Kansas is slightly more nuanced in its approach, although its approach is generally consistent with that taken in the preceding states. The Kansas Bank Commissioner has issued general guidance to the effect that most types of cryptocurrency transactions are outside the scope of the state money transmitter laws, although the relevant opinion does carve out transmission activities involving centralized virtual currencies,<sup>139</sup> saying that those kinds of operations are so complicated and varied that a general statement applicable in all cases is not possible.<sup>140</sup> With this caveat in mind, the conclusion of this guidance is that decentralized “cryptocurrencies as currently in existence are not considered ‘money’

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136. See Ill. Dep’t of Fin. & Prof’l Reg., Regulatory Guidance on Digital Currency Under the Ill. Transmitters of Money Act at 2, 5 (June 13, 2017), [<https://perma.cc/QAA5-JC26>].

137. *Frequently Asked Questions - Non-Depository*, N.D. DEP’T OF FIN. INST., [<https://perma.cc/BT7M-HFJB>] (providing the answer in response to: “Do I need a money transmitter license to purchase, sell, or operate an exchange for virtual currency?”).

138. Memorandum from Greg Gonzales, Comm’r of Tenn. Dep’t of Fin. Inst.’s on Regulatory Treatment of Virtual Currencies Under the Tenn. Money Transmitter Act to All Virtual Currency Co.’s Operating or Desiring to Operate in Tenn. 1 (Dec. 16, 2015) (2015 WL 10385047).

139. Office of the State Bank Comm’r of Kan., Guidance Document MT 2014-01 on Regulatory Treatment of Virtual Currencies Under the Kansas Money Transmitter Act at 1-2 (June 6, 2014), [<https://perma.cc/5BVE-MP9U>].

140. *Id.* at 1.

or ‘monetary value’” and therefore are not subject to the money transmitter act.<sup>141</sup>

Massachusetts’ regulations on money servicers do not mention virtual currencies, and the state’s Division of Banks has no official guidance on whether money servicers require a license under the state’s Money Transmitter act.<sup>142</sup> However, in replies to inquiries by virtual currency businesses, the Division has noted that under Massachusetts law, only “foreign transmittal agenc[ies]” require a license from the State, and under that provision, domestic crypto-based businesses are not money transmitters.<sup>143</sup>

Pennsylvania’s approach is similar to that taken by Kansas. In 2014, the Pennsylvania Department of Banking and Securities provided informal guidance that “virtual currencies *like Bitcoin* are not ‘money’” and therefore transmission of them would not require a license.<sup>144</sup> In January 2019, the same department published additional guidance clarifying that, generally, virtual currency trading platforms are not money transmitters under state law.<sup>145</sup> Thus, like Kansas, Pennsylvania does not generally include crypto-based businesses within the scope of its money transmitter statute but has noted that some cryptocurrencies (those that are not “like Bitcoin”) may be so regulated.

Texas also agrees that crypto is generally outside the scope of its money transmitter laws but notes that some crypto business will be regulated. Unlike Kansas and Pennsylvania, the Texas authorities have provided more specific advice about the kinds of

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141. *Id.* at 3.

142. *See, e.g.*, Receipts of Deposits for Transmittal to Foreign Countries, MASS. GEN. LAWS ch. 169 §§ 1-16 (1991).

143. Mass. Division of Banks, Opinion Letter 18-003, Do Business Activities, as Described, for Purchase, Sale and Exchange of Virtual Currency Require a License from the Division of Banks, (June 14, 2018), [<https://perma.cc/YK9E-L8G7>]. *See also* Mass. Division of Banks, Opinion Letter 18-002, Do Business Activities Involving the Sale of Cryptocurrency, as Described, Require Licensure from the Division of Banks, (Mar. 9, 2018), [<https://perma.cc/T9G4-PSPY>].

144. *See* Pa. Dep’t of Banking and Sec., *Bitcoin Update*, 6 QUARTER 11 (2014), [<https://www.dobs.pa.gov/Documents/Newsletter/Newsletter%20Volume%206/Quarter21vol6FINAL.pdf>] (emphasis added).

145. This guidance concludes bluntly that “these [virtual currency] Platforms are not money transmitters.” PA. DEP’T OF BANKING AND SEC., MONEY TRANSMITTER ACT GUIDANCE FOR VIRTUAL CURRENCY BUSINESSES (2019), [<https://perma.cc/VZJ5-6CSG>].



crypto that are potentially within the statute. The Texas Department of Banking first issued a supervisory memorandum regarding the legal status of virtual currency under the Texas Money Services Act in 2014.<sup>146</sup> Under the position taken in that document, virtual currencies were simply not considered money and crypto-based businesses fell outside the reach of state money transmitter laws.<sup>147</sup> However, that document was updated and revised in 2019.<sup>148</sup> Under the approach set forth in this memorandum, Texas continued to opine that, speaking generally, under the Texas Finance Code, “neither centralized virtual currencies nor cryptocurrencies are coin and paper money issued by the government of a country, [and therefore] they cannot be considered currencies . . . .”<sup>149</sup> In addition, the department reached the same conclusion under the state money services act.<sup>150</sup> However, as revised, the state has now concluded that the state finance and money transmission laws do apply to stablecoins backed by a sovereign currency where holders have a redemption right.<sup>151</sup> In addition, in Texas, the exchange of crypto for sovereign currency can involve money transmission.<sup>152</sup>

California has also concluded that virtual currency is generally outside its current money transmission requirements, but the path to this conclusion was far from straightforward. In fact, California originally appeared to interpret its state money transmitter act very broadly. On May 30, 2013, the state Department of Financial Institutions issued a cease and desist letter to the nonprofit Bitcoin Foundation warning that it could be subject to fines of up to \$1000 per day or per violation by acting as an unlicensed

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146. TEX. DEP’T OF BANKING, SUPERVISORY MEMORANDUM 1037, REGULATORY TREATMENT OF VIRTUAL CURRENCY UNDER THE TEXAS MONEY SERVICES ACT (Apr. 3, 2014), [<http://perma.cc/5WKA-N6K7>].

147. *Id.* at 3.

148. TEX. DEP’T OF BANKING, SUPERVISORY MEMORANDUM 1037, REGULATORY TREATMENT OF VIRTUAL CURRENCY UNDER THE TEXAS MONEY SERVICES ACT (rev. Apr. 1, 2019), [<https://perma.cc/XSC4-RNGT>].

149. *Id.* at 3.

150. *Id.* at 4.

151. *Id.*

152. *Id.* at 4-5.

money transmitter.<sup>153</sup> Criminal penalties were also threatened.<sup>154</sup> However, eighteen months later, the California Department of Business Oversight took a more thorough look at the question of how digital currencies should be treated under existing state law.<sup>155</sup> That Department eventually concluded that the state's current money transmitter laws would not be applied to crypto and instead suggested that the state legislature should consider the issue.<sup>156</sup> As of March 2020, California is considering the ULC's Uniform Regulation of Virtual Currency Businesses Act, but the state currently has no money transmitter requirements applicable to crypto businesses.<sup>157</sup> Previous efforts at imposing state regulatory requirements on crypto businesses as money transmitters, including an effort to adopt something akin to New York's controversial BitLicense,<sup>158</sup> failed, and there is substantial opposition to the current bill.<sup>159</sup> As of the date of this writing, therefore, California's most recent pronouncement is an opinion placing crypto outside the existing money transmitter framework.

### E. Interpretive Guidance Including Crypto Businesses

Naturally, given the widely divergent approaches taken toward crypto by the states, not every interpretive decision or guidance agrees that crypto generally falls outside conventional money transmissions provisions. Although most states have found that traditional money transmitter statutes are not broad enough to reach crypto, thereby necessitating a legislative

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153. Danny Bradbury, *California Issues Cease and Desist Letter to Bitcoin Foundation*, COINDESK (June 23, 2013), [https://perma.cc/JG98-WCRU].

154. *Id.*

155. Katie Orr, *California Considering Virtual Currency Regulations*, KPBS (Dec. 8, 2014), [https://perma.cc/5QQJ-Y9BR].

156. James Nash, *California Agency Ends Plan to Regulate Digital Currency*, BLOOMBERG BUSINESS (May 22, 2015), [https://perma.cc/Q2QN-VABS].

157. Paddy Baker, 'Innovation Crushing' Crypto Law Could Sneak Through California Legislature, CRYPTO BRIEFING (Sept. 30, 2019), [https://perma.cc/C8SM-HQQD]; updated per list of states with pending acts, ULC, *Regulation of Virtual Currency Businesses Act*, [https://perma.cc/AGZ2-KXP3] (archived on March 24, 2020).

158. *See, e.g.*, Charlie Richards, *California Considers US\$5,000 BitLicense-Style Scheme for "Virtual Currency,"* COIN TEL. (Mar. 16, 2015), [https://perma.cc/JM7K-3EEY].

159. Baker, *supra* note 157.

response, some states disagree and have interpreted existing provisions to include cryptoassets.

Colorado is illustrative of this approach. This state has concluded that crypto is covered by Colorado's conventional money transmitter statute notwithstanding the lack of express language applicable to virtual currency or cryptoassets in the act itself.<sup>160</sup> In Interim Guidance issued in 2018, the state concluded "[i]f a person is engaged in the business of transmitting money from one consumer to another within an exchange through the medium of cryptocurrency, that act would constitute money transmission and would be subject to licensure under the Colorado law."<sup>161</sup>

Louisiana has also interpreted its state money transmitter act expansively. The Louisiana statute defines "money" or "monetary value" to mean "currency or a claim that can be converted into currency through a financial institution, electronic payments network, or other formal or informal payment system."<sup>162</sup> "Currency" is limited to "the coin and paper money of the United States or another country that is designated as legal tender . . ."<sup>163</sup> Despite this limiting language, the state's Office of Financial Institutions has issued public guidance concluding that persons who would be classified as "exchangers" by FinCEN will be subject to licensure as money transmitters in Louisiana.<sup>164</sup> As mentioned earlier,<sup>165</sup> FinCEN has concluded that "a person is an exchanger and a money transmitter if the person accepts convertible virtual currency from one person and transmits it to another person as part of the acceptance and transfer of currency, funds, or other value that substitutes for currency."<sup>166</sup> This means that a person

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160. COLO. REV. STAT. § 11-110-103 (2017) (defining a number of terms, but not referencing virtual currency or monetary value).

161. DIVISION OF BANKING, COLO. DEPT. OF REG. AGENCIES, INTERIM REGULATORY GUIDANCE, CRYPTOCURRENCY AND THE COLORADO MONEY TRANSMITTERS ACT (Sept. 20, 2018), [<https://perma.cc/DL43-BQDD>].

162. LA. STAT. ANN. § 6:1032(12) (2008).

163. LA. STAT. ANN. § 6:1032(6).

164. *See* LA. OFFICE OF FIN. INST., CONSUMER AND INVESTOR ADVISORY ON VIRTUAL CURRENCY (Aug. 2014), [<https://perma.cc/DKN9-MRH7>].

165. *See supra* Part IV.

166. FIN. CRIMES ENF'T NETWORK, U.S. DEP'T OF THE TREASURY, FIN-2014-R011, REQUEST FOR ADMINISTRATIVE RULING ON THE APPLICATION OF FINCEN'S REGULATIONS TO A VIRTUAL CURRENCY TRADING PLATFORM (Oct. 27, 2014), [<https://perma.cc/H6KP-WLE4>] (citing 2013 GUIDANCE, *supra* note 13).

is subject to the Louisiana money transmitter act if it is in the business of accepting and converting a real currency into virtual currency, or vice versa, or converting one form of crypto into another, on behalf of third parties.

New Mexico takes a similar position. As is the case with other conventional money transmitter laws that have not been recently updated, the state's statute does not explicitly mention "virtual currencies."<sup>167</sup> Nonetheless, the New Mexico Regulation and Licensing Department has determined that "any entity engaged in the business of providing the exchange of virtual currency for money or any other form of monetary value or stored value to persons located in the State of New Mexico must be licensed . . . as a money transmitter."<sup>168</sup>

Oregon's Money Transmitter Act also lacks any explicit reference to "virtual currency" or "monetary value."<sup>169</sup> Regardless of that fact, the state has concluded that the statute includes virtual currencies:

Persons selling or issuing payment instruments or receiving money for transmission or transmitting money are required to be licensed as money transmitters. The purpose of licensing is to ensure that consumers receive money services in a secure manner. The definition of "money" is defined in statute to cover the ever changing landscape of virtual currency, including Bitcoin.<sup>170</sup>

Florida also has a broad interpretation of its money transmitter requirements, although the guidance in Florida comes not from an administrative agency but from the courts. The Florida money services businesses statute<sup>171</sup> does not specifically reference crypto or virtual currency, applying by its terms only to a business that receives "currency, monetary value, or payment instruments

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167. New Mexico is one of the jurisdictions that has adopted the UMMA, and it is codified in that state's laws at N.M. STAT. ANN. § 58-32-102 (2019).

168. *Money Service Business: FAQ's*, N.M. REG. & LICENSING DEPT., [https://perma.cc/M472-85AP].

169. OR. REV. STAT. § 717.200 (2015) (defining money, money transmission, and payment instrument, and several other terms, but not mentioning "virtual currency" or "monetary value").

170. *Money Transmitters Definition*, OR. BUS. XPRESS LICENSE DIRECTORY, [https://perma.cc/2ELC-NLRS].

171. This legislation is codified at FLA. STAT. §§ 560.103-.144 (2012).

for the purpose of transmitting the same.”<sup>172</sup> The statute does include any “medium of exchange, whether or not redeemable in currency” in the definition of “monetary value.”<sup>173</sup>

The issue of whether this language covered crypto-based business was at the heart of *Florida v. Espinoza*,<sup>174</sup> a case brought by the state against Michell Espinoza for money laundering involving bitcoin. The trial court dismissed that criminal information, under the rationale that bitcoin was not “money” as defined by the state money laundering statute.<sup>175</sup> In response to this decision, Florida House Bill 1379 was adopted and went into effect July 1, 2017. That legislation added the term “virtual currency” to the definition of “monetary instruments” under Florida’s Money Laundering Act.<sup>176</sup> As amended, the state’s money laundering statute now defines virtual currency as “a medium of exchange in electronic or digital format that is not a coin or currency of the United States or any other country.”<sup>177</sup> The legislature did not amend the state money transmission statute, suggesting under the rationale of *Espinoza* that crypto would not be “money” under its provisions.

Complicating matters, in February 2019, the Third District Court of Appeal’s reversed the trial court’s decision in *Espinoza*, deciding “that selling bitcoin requires a Florida money service business license.”<sup>178</sup> The appellate court held that bitcoin is a “payment instrument,” apparently bringing crypto within the scope of Florida’s money transmission laws.<sup>179</sup> Whether other courts or administrative agencies in Florida will concur is unclear, but the latest guidance from the state (in the form of an appellate court’s opinion) suggests that crypto is covered by the money transmission statute.

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172. FLA. STAT. § 560.103(23).

173. FLA. STAT. § 560.103(21).

174. See *Florida v. Espinoza*, No. F14-293, 2016 WL 11613849 (Fla. Cir. Ct. July 22, 2016), rev’d 264 So. 3d 1055 (Fla. Dist. Ct. App. 2019).

175. *Id.*

176. FLA. STAT. § 896.101 (2017).

177. FLA. STAT. § 896.101.

178. See Justin S. Wales, *Bitcoin Has a Florida Problem*, COINDESK (Feb. 24, 2019), [<https://perma.cc/2ATP-BYUM>].

179. *Id.*

## VI. SCOPE OF EXISTING REQUIREMENTS

The preceding discussion focuses on why governments regulate money transmitters and the range of businesses potentially impacted by money transmitter requirements. By itself, this might not be worrisome, but the incredible range of requirements, particularly at the state level, makes these results problematic for crypto-based businesses. Crypto businesses dealing in digital assets are particularly likely to do business in multiple jurisdictions and therefore will be faced with a number of differing requirements because states do not have consistent rules regarding how money transmitters should be regulated.

### A. Federal Regulation

The federal requirements for money transmitters are relatively easy to describe. Once a business is found to be a money transmitter under the BSA,<sup>180</sup> it will be regulated as a money services business (MSB) and must adopt policies to ensure that it does not facilitate criminal conduct. In essence, MSBs are required to register with FinCEN and renew that registration every two years; they must maintain an agents list; they must establish a written AML program; they must report certain transactions; and they are required to retain records of various transactions.<sup>181</sup>

While this may seem like a lot, the federal registration process is performed by completing an electronic questionnaire.<sup>182</sup> The required responses focus on basic information about the registrant, and ongoing compliance is not intended to impose significant costs on the businesses. Obviously, MSBs must adopt a risk-based AML program, which may entail substantial adjustments to the company's business operations, and the company must satisfy recordkeeping and reporting obligations. On the other hand, FinCEN has explicitly announced that although

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180. FinCEN has issued regulations implementing recordkeeping, reporting, and other requirements consistent with the BSA with respect to money services businesses, including money transmitters. *2011 Regulations*, *supra* note 13.

181. For a list of regulatory requirements for MSBs, see *BSA Requirements for MSBs*, FIN. CRIMES ENF'T NETWORK, [<https://perma.cc/EKC9-B7FP>] (the live page for this contains links for each required action with additional details).

182. *Money Services Business (MSB) Registration*, FIN. CRIMES ENF'T NETWORK, [<https://perma.cc/6V65-BT5C>].

covered businesses must establish an independent audit function to test their anti-money laundering programs, they “are not required to hire a certified public accountant or an outside consultant to conduct a review of their programs.”<sup>183</sup>

Because safety of the customer’s funds and soundness of the business are not primary motivations behind the federal law, at the current time there are no minimum capital requirements, no minimum net worth standards, no security or bonding obligations, and no licensing fees assessed at the federal level.<sup>184</sup> A strong case can be made that the existing federal requirements are a reasonable and appropriately targeted reaction to the need to minimize AML risks and problems associated with the potential funding of illegal enterprises.<sup>185</sup>

### B. The Range of State Responses

As mentioned above, most states are more concerned with consumer protection, and as such they have devised money transmitter requirements that focus on safety and soundness. This is a natural response to concerns that money transmitter businesses might abscond with the funds or otherwise fail to deliver them in accordance with customer instructions.<sup>186</sup> There are therefore a number of similar requirements for money transmitters in most states—although with regard to each issue, the details vary significantly.

First, state money transmitter statutes typically condition the granting of a license upon a showing that the applicant, and often a number of its agents or control persons, possess a certain kind of character. For example, under the UMSA, an applicant must show that its “financial condition and responsibility, financial and

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183. *Frequently Asked Questions Conducting Independent Reviews of Money Services Business Anti-Money Laundering Programs*, FIN. CRIMES ENF’T NETWORK (Sept. 22, 2006), [<https://perma.cc/QFW7-6SVA>].

184. FinCEN maintains a list of BSA Requirements. *See BSA Requirements*, *supra* note 181. The listed items relate to registration and renewal, establishing and maintaining an AML program, record-keeping, and reporting obligations. *Id.*

185. *See, e.g.,* Lo, *supra* note 6, at 113-17 (criticizing the state system after concluding that the “federal money transmitter regulation appears reasonably well calibrated to the risk posed by payments startups”).

186. *See supra* Section III.B. for a consideration of state objectives in regulating money transmitters.

business experience, competence, character, and general fitness,” as well as those of its “executive officers, managers, directors, and persons in control of [it]” are such that “it is in the interest of the public to permit the applicant to engage in money transmission . . . .”<sup>187</sup> This language appears in the money transmitter or money services statutes in a number of states, providing wide latitude to inquire into and investigate the applicant’s background.<sup>188</sup>

Other states, while using different language, have adopted the same general requirement. For example, Alabama requires applicants to be investigated for “responsibility, financial and business experience, character, and general fitness.”<sup>189</sup> In order to qualify for licensure as a money services business in Florida, an applicant must “[d]emonstrate to the office the character and general fitness necessary to command the confidence of the public and warrant the belief that the money services business or deferred presentment provider shall be operated lawfully and fairly.”<sup>190</sup> The Hawaii statute says that “[u]pon the filing of a complete application, the commissioner shall investigate the financial condition and responsibility, financial and business experience, character, and general fitness of the applicant. The commissioner may conduct an on-site investigation of the applicant, the reasonable cost of which shall be borne by the applicant.”<sup>191</sup> Tennessee’s Money Transmitter Act states that an “applicant must demonstrate experience, character, and general fitness to command the confidence of the public and warrant the belief that the business to be operated will be operated lawfully and fairly.”<sup>192</sup> Texas says that

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187. UNIF. MONEY SERVS. ACT § 205(a)(2) (UNIF. LAW COMM’N 2004). The UMSA application requires that the application include a list of criminal convictions of all such persons and any material litigation for the prior ten years, as well as information about any bankruptcy proceedings of such persons. UNIF. MONEY SERVS. ACT § 202(b)(2), (b)(6), (c)(5) (UNIF. LAW COMM’N 2004).

188. For example, Arkansas has codified the UMSA requirements at ARK. CODE ANN. § 23-55-205(a)(2) (2011).

189. ALA. CODE § 8-7a-8(a) (2017).

190. FLA. STAT. § 560.1401(1) (2014).

191. HAW. REV. STAT. § 489D-11(a) (2009).

192. TENN. CODE ANN. § 45-7-205(d) (2007).



[T]o qualify for a license under this chapter, an applicant must demonstrate to the satisfaction of the commissioner that:

- (1) the financial responsibility and condition, financial and business experience, competence, character, and general fitness of the applicant justify the confidence of the public and warrant the belief that the applicant will conduct business in compliance with this chapter and the rules adopted under this chapter and other applicable state and federal law;
  - (2) the issuance of the license is in the public interest
- ...<sup>193</sup>

In Utah, an applicant is required to “demonstrate experience, character, and general fitness to command the confidence of the public and warrant the belief that the business to be operated will be operated lawfully and fairly.”<sup>194</sup> Virginia requires that the character of the applicant and its control people is such that there is reason to believe the business will be operated fairly.<sup>195</sup>

Oddly, the Iowa statutes requires the state superintendent of banking to “investigate the applicant’s financial condition and responsibility, financial and business experience, character, and general fitness,” but for money transmitters the statute does not specifically give the banking supervisor authority to withhold the license on grounds of poor character.<sup>196</sup>

In addition to the character requirements, most states rely on what has sometimes been referred to as the “three-legged stool” approach to insuring safety and soundness of money services

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193. TEX. FIN. CODE ANN. § 151.202(a)(1)-(2) (West 2005).

194. 2015 UTAH CODE ANN. § 7-25-203(1)(b) (West 2015).

195. VA. CODE ANN. § 6.2-1906(A) (2014).

196. IOWA CODE § 533C.204(1) (2003). *But see* IOWA CODE § 533C.303(1)(d) (2004) (setting out grounds to deny application to act as a currency exchange, which does include that basis for denying a license).

businesses:<sup>197</sup> surety or bonding requirements; minimum net worth; and limits on permissible investments.<sup>198</sup>

The requirement that a money transmitter maintain a surety bond or an equivalent form of security appears in most state money transmitter or money service businesses statutes. The amount required, however, differs. When the ULC adopted the UMSA, they recognized the range of requirements, and therefore drafted a model provision that lists amounts in brackets, signifying acknowledgement of the reality that the states have not agreed on what a suitable level of security entails. As currently written, UMSA requires “a surety bond, letter of credit, or other similar security acceptable to the [superintendent] in the amount of [\$50,000] plus [\$10,000] per location, not exceeding a total addition of [\$250,000], must accompany an application for a license.”<sup>199</sup> In accordance with the most widely taken approach, the bond or other security must last during the period when the applicant is licensed and must continue for at least five years after services in the state are discontinued.<sup>200</sup> In addition, the model language includes a provision authorizing state authorities to increase the bond requirement up to \$1,000,000 “if the financial condition of a licensee so requires.”<sup>201</sup>

The CSBS, in proposing amendments to UMSA, has suggested that bond requirements should be tied to activity levels of the business. Their proposal would start with a minimum bond of \$100,000, with bond requirements increasing to \$1,000,000

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197. This term is used by various sources in describing safety and soundness requirements. In the context of money services, see *MSB Model Law Executive Summary*, CONF. ST. BANK SUPERVISORS (Sept. 2019), [<https://perma.cc/SP8X-T5SY>] [hereinafter CSBS, *Summary*]. For other uses of the term, see E. Norman Veasey et al., *Delaware Supports Directors with a Three-Legged Stool of Limited Liability, Indemnification, and Insurance*, 42 BUS. LAW. 399, 401 (1987); Becky McCray, *Stop Using “3 Legged Stool” to Describe Any Idea*, SMALL BIZ SURVIVAL (June 24, 2019), [<https://perma.cc/CP5E-47R3>] (“There are dozens and dozens of 3 legged stool analogies. The Three Legged Stool of Retirement Planning . . . of Politics . . . of Sustainability . . . of Accounting . . . of Organizational Architecture.”).

198. See CSBS, *Summary*, *supra* note 197.

199. UMSA, *supra* note 54, § 204(a). “Superintendent” is in brackets to acknowledge that different states give oversight responsibility to different officials or agencies.

200. *Id.*; see, e.g., ALA. CODE § 8-7A-7(d) (2017); ARK. CODE ANN. § 23-55-204(d) (2019); KY. REV. STAT. ANN. § 286.11-013(6) (West 2010); NEB. REV. STAT. § 8-2727(7) (2017).

201. UNIF. MONEY SERVS. ACT § 204(f) (UNIF. LAW COMM’N 2004).

when transaction activity increases to \$45 million.<sup>202</sup> In addition, state authorities would have discretion to increase the required bond amounts up to \$7 million.<sup>203</sup> Current bonding amounts in place at the state level reveal a distinct lack of agreement over how much security should be required, with a minority of states approaching the levels suggested by the CSBS.

At the low end are states that require amounts as low as \$10,000, although in each of these jurisdictions the appropriate authority is authorized to increase that required amount up to a predetermined maximum. For example, Arkansas requires a surety bond between \$10,000 and \$300,000 based on the previous year's transaction volume.<sup>204</sup> The state Securities Commissioner has the authority to increase the amount required to \$1,000,000.<sup>205</sup> In Hawaii, the statute specifies that "[e]ach application for a license shall be accompanied by a surety bond, irrevocable letter of credit, or other similar security device acceptable to the commissioner in the amount of \$10,000," which can be increased to "a maximum of \$500,000 upon the basis of the impaired financial condition of a licensee, as evidenced by a reduction in net worth, financial losses, or other relevant criteria."<sup>206</sup> In Washington, "[t]he minimum surety bond must be at least ten thousand dollars, and [is] not to exceed five hundred fifty thousand dollars."<sup>207</sup> The state Director of the Department of Financial Institutions is to adopt rules implementing this requirement, basing the amount of the bond on the prior year's activity levels.<sup>208</sup>

In the mid-range are a number of states that require a minimum bond of \$50,000, again with increases in the amount either permitted or required under certain circumstances. In Florida, the minimum surety bond is to be specified by rule, but must be between \$50,000 and \$2 million.<sup>209</sup> According to the statute, "[t]he rule shall provide allowances for the financial condition, number

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202. See CSBS, *Summary*, *supra* note 197.

203. *Id.* As of the date this Article was written, the CSBS was still in the process of evaluating and revising its proposal. *Id.*

204. ARK. CODE ANN. § 23-55-204(a).

205. ARK. CODE ANN. § 23-55-204(e).

206. HAW. REV. STAT. § 489D-7(a) (2018).

207. WASH. REV. CODE § 19.230.050(1) (2017).

208. WASH. REV. CODE § 19.230.050(1).

209. FLA. STAT. § 560.209(3)(a) (2009).

of locations, and anticipated volume of the licensee.”<sup>210</sup> Similarly, in Iowa, the state requires money transmitters to include “a surety bond, letter of credit, or other similar security acceptable to the superintendent in the amount of fifty thousand dollars plus ten thousand dollars per location, not exceeding a total addition of three hundred thousand dollars” with their application.<sup>211</sup> If the applicant has no locations in Iowa, the Superintendent of Banking is to set a bond amount not exceeding \$300,000.<sup>212</sup> In addition, the Superintendent can also increase the bond amount up to \$1,000,000.<sup>213</sup> Tennessee also requires applications to be accompanied by a \$50,000 surety bond or equivalent device, with an additional \$10,000 per location, up to a maximum of \$800,000.<sup>214</sup>

Some states require a higher minimum bond. Alabama, for example, requires money transmitters to post a bond in an amount determined by the Alabama Securities Commission, but the minimum bond is set by statute at the higher of \$100,000 or 100% of the average daily outstanding obligations for money received for transmission in Alabama plus 50% of the daily stored value of outstanding payment instrument and store value obligations in the state, to a maximum of \$5,000,000.<sup>215</sup> Texas sets the minimum bond at the greater of \$300,000 or 1% of the “total yearly dollar volume of money transmission business in [the] state” (or projected volume of business in Texas for the first year of operations), up to a maximum of \$2,000,000.<sup>216</sup>

The second leg of the so-called safety and soundness stool is minimum net worth, and again, there is a considerable range among the states as to what net worth is required to operate as a money transmitter.

The UMSA suggests a relatively low minimum net worth, although the recommended amount (“[\$25,000] determined in accordance with generally accepted accounting principles”)<sup>217</sup> is set out in brackets to denote the reality that states disagree on how

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210. FLA. STAT. § 560.209(3)(a).

211. IOWA CODE § 533C.203(1) (2003).

212. IOWA CODE § 533C.203(1).

213. IOWA CODE § 533C.203(6).

214. TENN. CODE ANN. § 45-7-2080(a) (1995).

215. ALA. CODE § 8-7a-7 (2017).

216. TEX. FIN. CODE ANN. § 151.308 (West 2017).

217. UNIF. MONEY SERVS. ACT § 207 (UNIF. LAW. COMM’N 2004).

high to set the bar. The UMSA also includes a comment, explaining the low value in the model act provision:

Only a minimal net worth requirement has been suggested because net worth is used as an additional requirement to make sure that license applicants and licensees have some resources for commencing and operating a money transmission business. Section 207 has been bracketed because some States use net worth as part of the safety and soundness mechanisms whereas other States rely on bonding/security and permissible investment requirements instead. This Act gives States the option of choosing between a combination of security, net worth and permissible investment requirements as prudential measures . . . .<sup>218</sup>

Some states currently impose low minimum worth requirements. The lowest minimum net worth for money transmitters appears in Hawaii, which requires licensees to have “a net worth of not less than \$1,000, calculated in accordance with generally accepted accounting principles.”<sup>219</sup> In Washington State the minimum tangible net worth for money transmitters is to be set by the Director of the Department of Financial Institutions at an amount which is “at least ten thousand dollars and not more than three million dollars.”<sup>220</sup> Alabama requires \$25,000 in net worth, as suggested in the UMSA.<sup>221</sup>

Other states impose net worth requirements that appear to be mid-range. In this category are states like Arkansas, which says that licensed money transmitters must maintain a minimum net worth of the greater of \$50,000 or \$10,000 for every \$1,000,000 of the previous year’s total money transmissions, payment instrument volume, and stored dollar volume.<sup>222</sup> This section of the Arkansas Code does not establish a cap on the required minimum net worth.

At the higher end of net worth requirements are states requiring a minimum of \$100,000 or \$200,000 in net worth in order to obtain a license. For example, a Florida licensee must have a net worth of at least \$100,000, plus \$10,000 for every additional

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218. UNIF. MONEY SERVS. ACT § 207 cmt. 2.

219. HAW. REV. STAT. § 489D-6(a) (2006).

220. WASH. REV. CODE § 19.230.060 (2010).

221. ALA. CODE § 8-7A-10 (2017).

222. ARK. CODE ANN. § 23-55-207 (2019).

location in the state, up to a maximum of \$2,000,000.<sup>223</sup> The required net worth must be maintained at all times. Tennessee requires money transmitters to maintain a minimum net worth between \$100,000 and \$500,000, depending on the number of locations and agents in the state.<sup>224</sup> Texas requires money transmission licensees to maintain a minimum net worth of \$100,000 if the licensee has four or fewer locations, and a minimum net worth of \$500,000 “if business is proposed to be or is conducted, directly or through an authorized delegate, at five or more locations or over the Internet.”<sup>225</sup> (The Texas banking commissioner may also increase the required net worth to a maximum of \$1 million.)<sup>226</sup> Virginia requires licensees to maintain a minimum net worth of \$200,000.<sup>227</sup>

Iowa appears to be on the high end as well, although its net worth requirements for money transmitters are variable. The Iowa statute says:

A licensee shall maintain at all times permissible investments that have a market value computed in accordance with generally accepted accounting principles of not less than the aggregate amount of all of its outstanding payment instruments and stored-value obligations issued or sold and money transmitted by the licensee in the United States.<sup>228</sup>

This appears to be on the high end because the required net worth is calculated based on the outstanding payment obligations sold and transmitted throughout the United States.

Finally, Utah is an outlier, requiring what appears to be a very high minimum net worth for all money transmitters. Utah requires that an applicant must “demonstrate, and a licensee shall maintain, a net worth of not less than \$1,000,000 as demonstrated by a financial statement for the most recent fiscal year that is

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223. FLA. STAT. § 560.209(1) (2009).

224. TENN. CODE ANN. § 45-7-205(a) (2009) (requiring a \$100,000 minimum net worth for the company plus an additional \$25,000 per additional location or agent located in Tennessee, up to \$500,000).

225. TEX. FIN. CODE ANN. § 151.307(a) (West 2017).

226. TEX. FIN. CODE ANN. § 151.307(b).

227. VA. CODE ANN. § 6.2-1906(B) (2014).

228. IOWA CODE § 533C.601(1) (2003).

prepared and certified by an independent auditor and is satisfactory to the commissioner . . . .”<sup>229</sup>

The last of the typical safety and soundness requirements relates to limitations on permissible investments by money transmitters. As noted by the CSBS, limitations on the kinds of investments that are permissible for MSBs “have traditionally served as the primary safety element for consumer funds.”<sup>230</sup> In general, money transmitters are required to invest only in highly secure, liquid assets, such as cash, certificates of deposit, and highly rated investment grade securities.

Some states have statutes that specify the acceptable assets for these businesses. For example, Arkansas limits permissible investments for money services businesses to highly secure assets, such as cash, certificates of deposits, investments rated at one of the three highest grades as defined by a nationally recognized securities ratings institution, government backed obligations, and some receivables and interest-bearing obligations to the extent that they do not exceed 20% of the company’s total investments.<sup>231</sup> Florida includes the same general requirements,<sup>232</sup> as does Tennessee.<sup>233</sup> In Texas, licensees may invest in cash, certificates of deposit, senior debt, investment grade securities, certain receivables valued at 40% of their face amount from delegates resulting from licensed money transmission, and such other assets as the banking commission may permit by rule.<sup>234</sup>

Other states authorize officials in the state to specify what sorts of investments are acceptable. For example, in Iowa, the superintendent of banks has authority to limit the extent to which particular investments are acceptable, except for money and certificates of deposit issued by a bank, which are always permissible.<sup>235</sup>

Outside of these three major components of state safety and soundness regulations, state money transmitter laws also contain

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229. 2015 UTAH CODE ANN. § 7-25-203(1)(a) (West 2015).

230. CSBS, *Summary*, *supra* note 197 (citing *UMSA*, *supra* note 60, at § 701).

231. *See* ARK. CODE ANN. § 23-55-702 (2008).

232. FLA. STAT. § 560.210(1) (2009).

233. In the Tennessee statutes, “permissible investments” are listed in the definitions provision. *See* TENN. CODE ANN. § 45-7-203 (2007).

234. TEX. FIN. CODE ANN. § 151.309 (West 2005).

235. IOWA CODE § 533C.601(2) (2003).

varied filing and renewal fees,<sup>236</sup> and an assortment of additional requirements.

In addition to application and licensing fees, bonding and minimum net worth requirements, and limitations on permissible investments, state money transmitter statutes also impose a range of additional conditions on licensees. For example, there are periodic and ongoing examinations or investigations, which take place at different intervals and on different schedules depending on each state.<sup>237</sup> A range of reports are also required, again with substantial variation among what is required and how frequently the information must be reported.

In Arkansas, money transmitters must file annual renewal reports accompanied by specified licensing fees.<sup>238</sup> In addition, quarterly reports must be made with the number and dollar value

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236. Money transmitters are typically charged an application and/or licensing fee as well as periodic fees or assessments by each state in which they do business. These fees are not particularly large, but they add up for multi-state operations.

In Arkansas, “[a] nonrefundable application fee of \$1,500 and a license fee of \$375 must accompany an application for a license under this article.” ARK. CODE ANN. § 23-55-402(b) (2019). Only the \$375 license fee is refundable in Arkansas if the application is rejected. ARK. CODE ANN. § 23-55-402(b). Similar rules apply in Iowa, where “[a] nonrefundable application fee of one thousand dollars and a license fee must accompany an application for a license under this article.” IOWA CODE § 533C.202(4) (2013). The Iowa license fee, which like Arkansas’s is refundable, is set at \$500 plus \$10 for each location in Iowa at which business is conducted, to be capped at \$5000. IOWA CODE § 533C.202(4). *See also* TENN. CODE ANN. § 45-7-209 (1995) (requiring an application fee of between \$250 and \$500); V. VA. CODE ANN. § 6.2-1905(A) (2019) (stipulating a \$750 annual fee); VA. CODE ANN. § 6.2-1905(B) (stipulating annual assessment to defray costs of examination). The UMSA suggests an application fee of \$2000 and a license fee of the same amount. *UMSA, supra* note 60, §202(d). The UMSA application fee is nonrefundable, and in addition, a \$2000 annual renewal fee is required. *UMSA, supra* note 60, § 206(a). These amounts appear to be relatively typical.

237. *See generally* Conference of State Bank Supervisors, *Conference of State Bank Supervisors & Money Transmitter Regulators Association*, CSBS 9-10 (May 2016), [<https://perma.cc/7242-SXZM>] [hereinafter *State Bank Regulators Report*]; *see also* Conference of State Bank Supervisors, *The State of State Money Services Businesses Regulation and Supervision*, CSBS (Nov. 16, 2017), [<https://perma.cc/W5NV-YBWX>] (briefly summarizing the State Bank Regulators Report). For a sampling of state statutes explaining this obligation, *see* ARK. CODE ANN. § 23-55-601(a)-(c) (2011) (providing for annual reports and unannounced examinations if the state securities commissioner has reason to believe the licensee is engaged in an unsafe or unsound practice, plus fees for all such examinations); FLA. STAT. § 560.109 (2019) (providing for unannounced examinations and investigations to protect the public as often as warranted, but in no case no less frequently than every five years); TENN. CODE ANN. § 45-7-214 (2007); VA. CODE ANN. § 6.2-1910(A) (2014); WASH. REV. CODE § 19.230.110(1) (2017).

238. ARK. CODE ANN. § 23-55-206 (2019).



of payment instruments, stored value, and prepaid access sold in the state as well as amounts outstanding, and special reports are required from licensees in any quarter in which there is a change in agents or locations in the state.<sup>239</sup> Licensees must also file with the state upon any felony charge or conviction of control persons and certain affiliates, the cancelation of bonds maintained by the licensee, any petition to revoke or suspend license anywhere, and give notice within three days following any bankruptcy filing or petition for receivership, dissolution, or reorganization.<sup>240</sup>

In Colorado, the state bank commissioner has authority to examine books and records, and charge fees set by banking board, and licensees are required to file audited financial statements annually.<sup>241</sup> Licensees are also required to file reports not less often than three times a year on days that the commissioner shall select setting out the resources and liabilities of the licensee on such day, as well as being obligated to make reports on the happening of other specified events.<sup>242</sup>

Florida requires specific quarterly reports and a more detailed annual report containing financial audit information.<sup>243</sup> Tennessee requires annual renewal of licenses and a renewal application with a report of the licensee's financial condition, including financial statements, list of locations and agents, and notification of any "material litigation or litigation relating to money transmission."<sup>244</sup> Virginia and Washington also require annual reports including audited financial information.<sup>245</sup>

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239. ARK. CODE ANN. § 23-55-603.

240. ARK. CODE ANN. § 23-55-603.

241. COLO. REV. STAT. § 11-110-111(1)(a), (2)(a) (2017).

242. COLO. REV. STAT. § 11-110-111(2)(b)(I)-(II).

243. FLA. STAT. § 560.118 (2009).

244. TENN. CODE ANN. § 45-7-211(d) (2013). Tennessee also requires licensed money transmitters to notify the state after certain events, including bankruptcy, felony indictment of certain parties related to the firm, or revocation of the firm's license by any governmental authority. TENN. CODE ANN. § 45-7-212 (2007).

245. VA. CODE ANN. § 6.2-1905(D) (2019) (requiring annual reports, including audited financials); WASH. REV. CODE § 19.230.110(2) (2017) (requiring annual report including audited financial reports, certification that company is maintaining appropriate investments and minimum bond, and description of all material changes to information previously submitted). Virginia also requires money transmitters to notify the state if certain events occur, including material changes to information provided in the firm's application, a filing for bankruptcy, and the indictment of certain parties related to the firm. VA. CODE ANN. § 6.2-1917(A), (C) (2019).

The consequences of failing to comply or in submitting information that the state deems to indicate a that the licensee is not complying with statutory requirements or is operating in an unsafe or unsound manner are severe. In most cases, the state regulator can mandate corrective action or suspend or even revoke the license.<sup>246</sup>

### C. The Failure of Coordination and Uniformity

The problems caused by the complex patchwork of requirements for multi-jurisdictional money transmitters are neither new nor unknown.<sup>247</sup> In 1994, as part of the Riegle Community Development and Regulatory Improvement Act of 1994,<sup>248</sup> Congress adopted the Money Laundering Suppression Act of 1994.<sup>249</sup> That act specifically recommended that states adopt uniform laws for money services businesses such as money transmitters.<sup>250</sup>

In response to this call for action, the Uniform Law Commission (ULC) promulgated the Uniform Money Services Act (UMSA) in 2000.<sup>251</sup> However, despite general recognition that complex and inconsistent state regulation has placed substantial burdens on the industry, adoption has been slow. Since its introduction, only ten states (Alaska, Arkansas, Hawaii, Iowa, New Mexico, North Carolina, South Carolina, Texas, Vermont, and Washington) and two territories (Puerto Rico and the U.S. Virgin

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246. See, e.g., TENN. CODE ANN. § 45-7-217 (2007); VA. CODE ANN. § 6.2-1907(A) (2014); *State Bank Regulators Report*, *supra* note 237, at 10-11.

247. As e-commerce began to take off, calls for reform increased. “Existing laws and regulations that may hinder electronic commerce should be reviewed and revised or eliminated to reflect the needs of the new electronic age.” William J. Clinton & Albert Gore, Jr., A FRAMEWORK FOR GLOBAL ELECTRONIC COMMERCE, Principles § 4 (1997), [<https://perma.cc/76B5-V8RV>]. Accord Kerry Lynn Macintosh, *The New Money*, 14 BERKELEY TECH. L.J. 659, 659-60, 673 (1999). Commentators have continued to push the need for a more uniform approach as new technologies, such as blockchain and crypto, have appeared. See, e.g., Knight, *supra* note 54; Lo, *supra* note 6; Hughes, *supra* note 17; Kelsey L. Penrose, *Banking on Bitcoin: Applying Anti-Money Laundering and Money Transmitter Laws*, 18 N.C. BANKING INST. 529 (2014).

248. Riegle Community Development and Regulatory Improvement Act, Pub. L. No. 103-325, 108 Stat. 2160, (1994) (codified as amended at 31 U.S.C. § 5312 (2004)).

249. This history is recited in the prefatory note to the UMSA. UMSA, *supra* note 60, at 5.

250. *Id.*

251. See *id.* at 1.

Islands) have enacted the Act.<sup>252</sup> No new state has adopted the UMSA since 2016.<sup>253</sup>

This is not to suggest that states are unaware of the problems posed by the lack of consistency in existing regulations. There have been a number of initiatives designed to increase coordination among the states, particularly through the efforts of the Money Transmitter Regulators Associations (MTRA)<sup>254</sup> and the Conference of State Bank Supervisors (CSBS).<sup>255</sup> Both of these groups work to increase consistency, cooperation, and efficiency in the state regulation of money transmitters (although the CSBS is obviously focused on other financial institutions as well).<sup>256</sup>

The primary success to date has been in efforts to coordinate the examination process by which money transmitters are evaluated. In 2012, the CSBS and MTRA together promulgated a nationwide agreement establishing a joint examination for multi-state MSBs.<sup>257</sup> Among other things, the agreement establishes a taskforce known as the MMET (Multi-State MSB Examination Task Force) and sets out an information-sharing arrangement for the signatories.<sup>258</sup> There is also an accompanying protocol for the

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252. A list of states having adopted the Act is maintained by the Uniform Law Commission. *See UMSA, supra* note 60.

253. *Id.*

254. According to the group's website, the MTRA is "a national non-profit organization dedicated to the efficient and effective regulation of money transmission industry" in the U.S. *See Money Transmitter Regulator Ass'n, Welcome to MTRA*, MTRA, [<https://perma.cc/HNV9-9SCC>]. One of the organization's stated goals is to promote "a more efficient and less burdensome state regulatory system that has universal respect and credibility." *Id.*

255. The CSBS is also a nationwide organization of financial regulators, designed to state banking supervisors "a national forum to coordinate supervision and develop policy." Conference of State Bank Supervisors, *What Is the Conference of State Bank Supervisors?*, CSBS, [<https://perma.cc/GZ2U-WHPY>].

256. The CSBS does not limit its reach to depository institutions, and instead also considers non-depository issues, such as those applicable to many money transmitters. *See Conference of State Bank Supervisors, Non-Depository Issues*, CSBS, [<https://perma.cc/2QUS-XB2D>]. The CSBS also maintains a strong interest in FinTech. *See Conference of State Bank Supervisors, Financial Technology*, CSBS, [<https://perma.cc/N383-TW3N>].

257. CONFERENCE OF STATE BANK SUPERVISORS, NATIONWIDE COOPERATIVE AGREEMENT FOR MSB SUPERVISION 1-2 (Jan. 2012), [<https://perma.cc/D9U6-UR6Y>].

258. *Id.* at 2-3.

multi-state examinations.<sup>259</sup> As of October 2018, only three states were not parties to this Agreement and Protocol.<sup>260</sup>

Members of MTRA have also signed a cooperative agreement, which states that its purpose “is to promote a nationwide framework for cooperation and coordination among state money transmitter regulators that have concurrent jurisdiction over a regulated entity in a manner that conserves regulatory resources and minimizes the regulatory burden on supervised entities, consistent with each state attaining its supervisory objectives.”<sup>261</sup> This Agreement focuses on the examination of multi-state money transmitters, setting up a system of lead state supervisors to coordinate the examination process and includes information-sharing and enforcement provisions.<sup>262</sup>

There is also a coordinated system through which companies and individuals are to apply for, amend, renew, and surrender financial services licenses.<sup>263</sup>

Notwithstanding the coordination of the examination process, and the central application process used by several states, most states continue to apply their own standards during the examination process.<sup>264</sup> The substantive provisions of state money transmitters continue to vary widely,<sup>265</sup> and there is no agreement

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259. CONFERENCE OF STATE BANK SUPERVISORS, PROTOCOL FOR PERFORMING MULTI-STATE EXAMINATIONS 1 (Jan. 2012), [<https://perma.cc/DV4Z-DMN4>].

260. See CONFERENCE OF STATE BANK SUPERVISORS, CSBS/MTRA NATIONWIDE COOPERATIVE AGREEMENT & PROTOCOL FOR MSB SUPERVISION (OCT. 2018), [<https://perma.cc/NXF6-4RJL>]. In addition, between implementation and 2016 “state agencies have conducted over 400 multi-state MSB examinations.” *State Bank Regulators Report*, *supra* note 237, at 11.

261. *MTRA Cooperative Agreement* § 2.1, MTRA, [<https://perma.cc/Q669-CUWR>].

262. *Id.* at §§ 2.2, 3.1, 4.1, 5.1.

263. See Conference of State Bank Supervisors, *Nationwide Multi-State Licensing System and Registry (NMLS)*, CSBS, [<https://perma.cc/TEP8-2N89>].

264. In early 2018, the CSBS announced a trial program in which seven states agreed to accept the findings of a single reviewing state, although the details of the experiment were not released. Andrew Bigart & Evan Minsberg, *New Details on CSBS Streamlined Money Transmission License Application Program*, Venable LLP (Mar. 8, 2019), [<https://perma.cc/BP29-GHFV>]. Subsequent reports suggested that as many as twenty-one states were ready to join the experiment (*Id.*), but in April of 2019, the CSBS Progress Report merely stated that the state examination system was still in development, and the pilot program was “underway.” *CSBS Vision 2020: A Progress Report*, CSBS (April 25, 2019), [<https://perma.cc/RG34-5SEE>] [hereinafter *Progress Report*]. The CSBS efforts are described in more detail in Section VI.D., *infra*.

265. See *supra* Part V.

about how these requirements apply to crypto-based businesses.

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#### D. Vision 2020 from the CSBS

Aware that a common application and examination form is only the first step towards a more consistent state-level approach, in 2017 the CSBS launched what it called Vision 2020.<sup>267</sup> Vision 2020 is a series of initiatives aimed at achieving an integrated state licensing and supervisory system for money service businesses such as money transmitters.<sup>268</sup> The express objective of this project is to improve regulatory efficiency and supervision.<sup>269</sup>

As part of its Vision 2020 initiative, CSBS announced in February 2018 that a group of seven states had agreed to streamline the money transmitter application approval process by accepting the findings of the other states regarding certain sections of an application.<sup>270</sup>

On October 1, 2019, the CSBS published a draft of several proposals designed to improve upon the UMSA, suggesting amendments to “language that has been inconsistently implemented or interpreted over time.”<sup>271</sup> A dozen comments from businesses and other organizations were received by the November 1, 2019, deadline.<sup>272</sup> As of the date this was written, this proposal is still being evaluated and modified.

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266. See *supra* Part I.

267. CSBS, *Summary*, *supra* note 197, at 1.

268. *Id.*

269. *Progress Report*, *supra* note 264.

270. Bigart & Minsberg, *supra* note 264. Although state-specific materials will still be required as part of the streamlined process, participating states would accept findings of an assigned state’s review as to matters such as cybersecurity, background checks, and compliance with BSA requirements. The precise list of items that participating states will accept is subject to change, and the list of states willing to participate was later reported to include twenty-one jurisdictions. *Id.* On the other hand, the April 2019 CSBS Progress Report merely noted that this pilot program is underway and the entire examination process is in development. *Progress Report*, *supra* note 264.

271. CSBS, *Summary*, *supra* note 197, at 1. The CSBS draft materials were published in links that can be found at *Request for Comments: MSB Model Law*, CSBS (Oct. 1, 2019), [<https://perma.cc/Y5Q7-BC7R>]. Perhaps the most useful of the draft documents is a model law language chart, which sets out suggested language by topics. *Draft Model MSB Law Language by Topic*, CSBS (July 10, 2019), [<https://perma.cc/SS7Y-A6RG>].

272. CSBS, *Comments: MSB Model Law* (Oct. 1, 2019), [<https://perma.cc/EDP4-XACB>].

Unfortunately, there are limits to what this approach can be expected to achieve. First, individual states will have to accept the proposals without significant modification. Given both past experience with UMSA and the wide variation in current approaches, this appears improbable. Second, even if universally adopted, the updated language still retains a range of state-specific requirements. Thus, while this is a laudable step towards harmonization, crypto businesses are likely to continue to face a confusing maze of requirements and standards.

Major players may have an easier time complying, but smaller innovators are still likely to choose other markets in which to experiment. A reasonable level of regulation is both necessary and appropriate; inadvertent barriers to competition and innovation because of a lack of consistency is neither.

## VII. THE CASE FOR PREEMPTION

If a uniform response at the state level is not forthcoming, preemption by federal action may be the only viable solution to addressing unnecessary complexity and over-regulation. Certainly the federal government has the power to preempt state money transmitter laws that apply to multi-state operations.

In 1992, the U.S. Supreme Court explained that the U.S. Constitution gives Congress the power “to regulate Commerce among the several States.”<sup>273</sup> Moreover, in the event of a conflict between federal and state law, federal law prevails.<sup>274</sup> By virtue of the changing nature of commerce, this means that the federal government now holds the power to regulate activities that were

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273. *New York v. United States*, 505 U.S. 144, 157 (1992) (citing U.S. CONST. Art. I, § 8, cl. 3). A number of the Court’s decisions have noted and upheld the federal government’s exercise of power over a range of topics, some of which had more traditionally been left to the states. This balance exists notwithstanding the corresponding reduction in state power when the federal government preempts state action. *See, e.g.*, *Shaw v. Delta Air Lines, Inc.*, 463 U.S. 85, 103-106 (1983) (preemption of state law by the Employee Retirement Income Security Act).

274. The Constitution’s Supremacy Clause provides that federal law “shall be the supreme [l]aw” of the United States, notwithstanding any contrary state law. U.S. CONST. Art. VI, cl. 2. As the Court has noted, the Constitution’s Supremacy Clause gives the federal government “a decided advantage in th[e] delicate balance” between state and federal power. *Gregory v. Ashcroft*, 501 U.S. 452, 460 (1991).

once considered purely local.<sup>275</sup> Preemption does, however, require an action by Congress, although the Supreme Court has acknowledged that such preemption may be express or implied.<sup>276</sup>

It is true that states have traditionally exercised authority over money transmitter businesses,<sup>277</sup> and it is also true that there is a general presumption against preemption of matters that have

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275. Paul E. McGreal, *Some Rice with Your Chevron?: Presumption and Deference in Regulatory Preemption*, 45 CASE W. RES. L. REV. 823 (1995). As commentators have observed, because of the growth of interstate commerce, activities that once seemed local in nature have had an increasing impact on the national economy, and have therefore come within the scope of Congress' commerce power. *Id.* at 823. *See, e.g.*, *Katzenbach v. McClung*, 379 U.S. 294, 301, 304 (1964); *Wickard v. Filburn*, 317 U.S. 111, 123-25 (1942). *See also* *New York v. United States*, 505 U.S. at 157 ("The Federal Government undertakes activities today that would have been unimaginable to the Framers . . .").

276. Robert S. Peck, *A Separation-of-Powers Defense of the "Presumption Against Preemption"*, 84 TUL. L. REV. 1185, 1189 (2010). Express preemption exists where Congress includes language to that effect in the federal law. This is the easiest case in which to find preemption. *Id.* at 1189-90. Implied preemption can be based on field preemption (which occurs where the federal action is so comprehensive that it can be said to fully occupy the field) (*Id.* at 1189, 1191), direct conflict (where the state provision directly conflicts a portion of the federal law), or possibly obstacle preemption (where the state law presents an obstacle to accomplishing the objectives of the federal law) (*Id.* at 1189, 1193). *Compare* *M'Colloch v. Maryland*, 17 U.S. 316, 319 (1819) ("It is of the very essence of supremacy, to remove all obstacles to its action within its own sphere, and so to modify every power vested in subordinate governments, as to exempt its own operations from their own influence. . . .") with *Crosby v. Nat'l Foreign Trade Council*, 530 U.S. 363, 372-73 (2000) (identifying only express, field, and conflict preemption). For a more complete analysis of whether implied obstacle preemption continues to be a valid theory, see Lauren Gilbert, *Immigrant Laws, Obstacle Preemption and the Lost Legacy of McCulloch*, 33 BERKELEY J. EMP. & LAB. L. 153 (2012); Caleb Nelson, *Preemption*, 86 VA. L. REV. 225 (2000). Nelson's article appears to have influenced Supreme Court Justice Clarence Thomas's thinking on preemption. *See, e.g.*, *Wyeth v. Levine*, 555 U.S. 555, 582-83 (2009) (Thomas, J., concurring); *Pliva, Inc. v. Mensing*, 564 U.S. 604, 621-22 (2011). This Article will not attempt to address the varying types of preemption, given that the suggestion made here calls for federal action expressly preempting state money transmitter legislation insofar as it would otherwise reach crypto-based businesses.

277. As noted in 2018, "[t]he several states rather than the federal government are the primary regulators of money transmitters." Peter Van Valkenburgh, *The Need for Federal Alternative to State Money Transmission Licensing*, COIN CTR. REP., *Abstract* (v.1, Jan. 2018), [<https://perma.cc/2HK6-3ALC>]. This has also been the subject of comment by the Chairmen of both the SEC and CFTC.

Check-cashing and money-transmission services that operate in the [United States] are primarily regulated by states. Many of the internet-based cryptocurrency-trading platforms have registered as payment services and are not subject to direct oversight by the SEC or the CFTC. We would support policy efforts to revisit these frameworks and ensure they are effective and efficient for the digital era.

Jay Clayton & J. Christopher Giancarlo, *Regulators Are Looking at Cryptocurrency*, WALL STREET J. (Jan. 24, 2018), [<https://perma.cc/2B8W-2Q35>].

long been regulated by the states. As the Supreme Court has explained, when Congress legislates in a field which has been “traditionally occupied” by the states, courts “start with the assumption that the historic police powers of the States were not to be superseded by the Federal Act unless that was the clear and manifest purpose of Congress.”<sup>278</sup> There is also precedent suggesting that the presumption against preemption “is not triggered when the State regulates in an area where there has been a history of significant federal presence,”<sup>279</sup> such as exists in the case of national banking.<sup>280</sup> Because cryptoassets are designed to be multi-jurisdictional, there is certainly an argument that could be made that any presumption against preemption of state law should not apply.<sup>281</sup>

This Article recognizes the risk that implied preemption would not be available, and therefore the suggestion posited here is that Congress should expressly and clearly removed interstate<sup>282</sup> crypto-based money transmitter activities from the purview of state money transmitter statutes.<sup>283</sup> In deciding how to do this, the federal government might, for example, choose to borrow language from one of the states that has removed crypto from the scope of state money transmission requirements.

One such state is Wyoming, which specifically amended its Money Transmitter Act to make it clear that the act does not apply to “[b]uying, selling, issuing, or taking custody of payment instruments or stored value in the form of virtual currency or receiving virtual currency for transmission to a location within or outside

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278. *Rice v. Santa Fe Elevator Corp.*, 331 U.S. 218, 230 (1947).

279. *United States v. Locke*, 529 U.S. 89, 108 (2000); *see also* Peck, *supra* note 276, at 1195 (“The presumption does not apply where there has been a history of significant federal presence . . .”) (internal quotations omitted).

280. *Cuomo v. Clearing House Ass’n*, 557 U.S. 519, 554 (2009) (Thomas, J., dissenting).

281. *Bank of Am. v. City & Cty. of San Francisco*, 309 F.3d 551, 589 (9th Cir. 2002) (quoting *Locke*, 529 U.S. at 108). *See also* *Wachovia Bank v. Burke*, 414 F.3d 305, 314 (2d Cir. 2005) (“The presumption against federal preemption disappears, however, in fields of federal regulation that have been substantially occupied by federal authority for an extended period of time. Regulation of federally chartered banks is one such area.”) (quoting *Flagg v. Yonkers Sav. & Loan Ass’n*, 396 F.3d 178, 183 (2d Cir. 2005)).

282. A purely intrastate business would remain subject to state law, but given the nature of cryptoassets, this is not likely to affect many crypto-based business operations.

283. The purpose of this preemption would not be to eliminate regulation, but to establish a unified regulatory regime at the federal level instead.



the United States by any means . . . .”<sup>284</sup> That statute also defines “virtual currency” to mean “any type of digital representation of value that: (A) Is used as a medium of exchange, unit of account or store of value; and (B) Is not recognized as legal tender by the United States government.”<sup>285</sup> This is in accord with FinCEN’s treatment of virtual currencies as “a medium of exchange that operates like a currency in some environments, but does not have all the attributes of real currency.”<sup>286</sup> The missing attribute identified by FinCEN is that virtual currency is not currently recognized as legal tender which could easily be added if and when it becomes likely that the U.S. would choose to recognize a virtual currency as legal tender.

Essentially the same exemption and definition could be used in the BSA, precluding states from regulating such businesses as money services or money transmitter businesses. Because the purpose of preemption is to avoid inconsistent state regulation, and not to avoid all regulation of such businesses, the language at the federal level would also need to limit the exemption from state law to businesses licensed pursuant to federal law to the extent that they are involved with the listed activities. A rogue business operating outside the scope of federal regulation should not be exempt from state oversight.

Since preemption begins with the inquiry as to whether Congress intended to preempt state law, an unambiguous statement such as the foregoing should make it clear that states would not retain the authority to regulate virtual currency businesses as money transmitters, so long as they are licensed at the federal level. This would naturally necessitate increased federal oversight, since the current federal approach focuses on registration of these businesses with AML and CTF compliance in mind, rather than with the goal of licensing to ensure adequate safety and soundness for consumer protection. The switch to federal licensing would require a more detailed application process at the federal level, a substantive review of the materials provided, and a decision at the federal level about appropriate bonding or security

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284. WYO. STAT. ANN. § 40-22-104(a)(vi) (2020).

285. WYO. STAT. ANN. § 40-22-102(a)(xxii) (2018).

286. 2013 *Guidance*, *supra* note 13.

requirements, minimum net worth obligations, and any limitations on permissible investments (keeping in mind the nature of the underlying business).

Rather than suggesting that Congress should establish these standards, it would seem preferable to delegate such rule-making authority to an appropriate agency. While FinCEN currently oversees these very same businesses for compliance with AML and CTF requirements, it may not be the logical agency for safety and soundness review. Instead, the federal Consumer Financial Protection Bureau (CFPB),<sup>287</sup> whose creation was authorized by the Dodd-Frank Wall Street Reform and Consumer Protection Act in 2010, is a more logical choice.<sup>288</sup>

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287. It should be noted that various challenges have been made to the legitimacy of the agency in the years since its creation. *See, e.g.*, Barbara S. Mishkin, *D.C. Federal Court Dismisses Morgan Drexen Lawsuit Against CFPB*, BALLARD SPAHR, [https://perma.cc/4H2A-78H8]. *See also* Consumer Fin. Prot. Bureau v. Morgan Drexen, Inc., 60 F. Supp. 3d 1082, 1086 (C.D. Cal. 2014); PHH Corp. v. Consumer Fin. Prot. Bureau, 881 F.3d 75, 110 (D.C. Cir. 2018) (upholding the CFPB against a challenge that its for-cause removal provision for commissioners violated the constitutional separation of powers). Notable in *PPH Corp.* is a dissent by now-Supreme Court Justice Brett Kavanaugh, who would have invalidated the for-cause termination provision, instead allowing the President to remove the Director of the CFPB at will. *Id.* at 200 (Kavanaugh, dissenting). *Cf.* Consumer Fin. Prot. Bureau v. RD Legal Funding, LLC, 332 F. Supp. 3d 729, 785 (S.D.N.Y. 2018) (finding that the CFPB “lack[ed] authority to bring [an] enforcement action because its composition violate[d] the Constitution’s separation of powers,” and declining to sever the for-cause termination provisions) (internal quotations omitted). On May 6, 2019, the Ninth Circuit Court of Appeals concluded in *Consumer Fin. Prot. Bureau v. Seila Law LLC* that the structure of the CFPB did not violate the Constitution, even though “the agency is headed by a single Director who exercises substantial executive power but can be removed by the President only for cause.” 923 F.3d 680, 682. Although agreeing that the argument against the structure was “not without force,” the court nonetheless concluded that Supreme Court precedents required the court to find the structure to be permissible. *Id.* at 983. The Supreme Court granted certiorari to decide the issue on October 18, 2019. *Id.*, *cert. granted*, 140 S. Ct. 427 (2019). The Court might have signaled a willingness to strike down the provision relating to the removal of a Director only for cause, by broadening the scope of certiorari beyond the narrow issue raised by appellants. It did this by directing the parties to brief and argue the issue of whether, 12 U.S.C. § 5491(c)(3) can be severed from the Dodd-Frank Act if the Court determines that the CFPB is unconstitutional on the basis of the separation of powers. 140 S.Ct. 427 (Mem). This same language also suggests that the Court might be willing to uphold the CFPB with a change in the removal powers of the President. In any event, the suggestions made in this Article are based on the assumption that the CFPB will continue in effect, either in its current form, or with a Director who is subject to at will removal by the President.

288. *See* Eric J. Mogilnicki & Melissa S. Malpass, *The First Year of the Consumer Financial Protection Bureau: An Overview*, 68 BUS. LAWYER 557, 557 (2013).

The CFPB is a governmental agency responsible for consumer protection in the financial sector.<sup>289</sup> Its jurisdiction includes banks and other financial companies operating in the United States, making it a reasonable choice to oversee safety and soundness of crypto-based businesses. The bureau has a history of consulting industry, consumers, and other external stakeholders when considering new regulations and works to “carefully assess the benefits and costs” of new requirements.<sup>290</sup> Because small businesses and entrepreneurs would undoubtedly be impacted by safety and soundness requirements such as minimum net worth and bonding obligations, the CFPB will be obligated to organize a Small Business Review Panel in order to insure that there is a strong justification for choices that the agency makes.<sup>291</sup>

This suggestion will necessitate a change to the reach of the CFPB’s authority. As of June 2019, the CFPB’s authority was limited to banks, thrifts, and credit unions with assets over \$10 billion, and larger participants in the consumer reporting, consumer debt collection, student loan servicing, international money transfer, and automobile financing markets.<sup>292</sup> This scope of authority would need to be broadened in order to cover money transmitter businesses that deal in cryptoassets.

The actual regulations that the CFPB should impose in order to replace the myriad state safety and soundness requirements

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289. According to its own website, “[t]he CFPB implements and enforces federal consumer financial laws to ensure that all consumers have access to markets for consumer financial products and services that are fair, transparent, and competitive.” *Rulemaking*, CONSUMER FIN. PROTECTION BUREAU, [https://perma.cc/EYF7-KSUF].

290. *Id.*

291. The obligation to consult with this kind of group is derived from the Regulatory Flexibility Act, which applies to the CFPB. “When any rule is promulgated which will have a significant economic impact on a substantial number of small entities, the head of the agency . . . shall assure that small entities have been given an opportunity to participate . . . .” 5 U.S.C. § 609(a) (2010). Under the policies adopted by the CFPB, this includes formation and consultation with a Small Business Review Panel:

Each Small Business Review Panel consists of representatives from the CFPB, the Small Business Administration’s Chief Counsel for Advocacy, and the Office of Management and Budget’s Office of Information and Regulatory Affairs. The panel holds an outreach meeting with a representative group of small businesses . . . . [The CFPB will] use that feedback to inform the rulemaking process.

*Small Business Review Panels*, CONSUMER FIN. PROTECTION BUREAU, [https://perma.cc/7VKL-R8XM].

292. *Institutions Subject to CFPB Supervisory Authority*, CONSUMER FIN. PROTECTION BUREAU, [https://perma.cc/R3LJ-4XDR].

should be based on discussions with current state regulators and groups such as the CSBS, as well as with the small business panel described above. After considering the range of fees, character standards, bonding requirements, minimum net worth obligations, limitations on permissible investments, and other safety and soundness regulations currently being applied to various money transmitters, a single application and examination based on a uniform set of standards should be implemented at the federal level. For multi-jurisdictional entities conducting their “money transmission” activities through cryptoassets, compliance with these federal standards should preempt inconsistent state requirements. States, should however, be allowed to require filing of a reasonable fee and notice that would include the name of the money transmitter, and a list of agents and locations operating in each state.

Given the reality that states have shown no tendency towards uniformity in their approach to regulation of payment transmitters, it does not make sense to wait for them to adopt changes to their statutes and regulations. Notwithstanding efforts by groups such as the ULC and CSBS to encourage consistency and cooperation, vast differences in ideology and approach make it almost inconceivable that uniformity will be achieved by the states acting alone.

In this instance, the benefits of allowing states to experiment with approaches to regulation appear to be outweighed by the problems posed by inconsistent regulation. First, state-by-state regulation means that interstate operations may be forced to comply with the most stringent state’s regulation or forego doing business in that jurisdiction (and potentially in all U.S. markets if it becomes impossible to insure that residents of a particular jurisdiction are not served).<sup>293</sup> Even if most states would welcome a particular product or service, a single state (particularly one with a lucrative market and a powerful lobby by existing market

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293. When it comes to online transactions, it is not always easy to know where a customer is actually located. For example, there are plenty of sources offering advice on how to hide I.P. addresses. See, e.g., Max Eddy, *How to Hide Your IP Address*, PCMag, [https://perma.cc/SJU9-DBRC]; (4 Super Easy & Fast Ways To (REALLY) Hide Your IP in 2020, VPNMENTOR (Feb. 13, 2020), [https://perma.cc/CY27-RJG5]; *How to Hide Your IP Address*, WHATISMYIPADDRESS, [https://perma.cc/EYD3-L35T].

participants) might have the effective power to preclude that option from being available anywhere.<sup>294</sup>

Secondly, inconsistent regulations place new entrants into the payment services market at an unfair disadvantage. Certain market participants, particularly banks, already have a relatively uniform regulatory framework,<sup>295</sup> and it seems particularly unfair to subject new entrants into a market specifically designed to serve the unbanked<sup>296</sup> to more difficult standards.

### VIII. CONCLUSION

Hopefully, the preceding materials offer a general basis for understanding how crypto-based businesses differ from conventional money transmitters even though they may provide similar services. In addition, the discussion of crypto business should also provide a framework in which to evaluate both the potential risks and benefits of the new technology in the sphere of money transmission.

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294. For a discussion of this possibility, see J. Parker Murphy, *More Sense Than Money: National Charter Option for FinTech Firms Is the Right Choice*, 18 N.C.J.L. & TECH. ONLINE 359, 388 (2017), [<https://perma.cc/Q6XE-T7NZ>]. “If lucrative markets are allowed to functionally dictate stringent requirements across the country, the overregulation could reduce the financial products available in small states. This outcome would reduce competition in those markets as well as ensure that unbanked consumers remain unbanked.” *Id.*

295. For example, “[s]tate money transmittal statutes, which are otherwise extremely broad, often exempt banks.” Knight, *supra* note 54, at 155. Accordingly, non-bank entities seeking to offer money transmitter services “may find themselves under a different—and much less consistent—regulatory regime than their bank competitors.” *Id.*

296. Although it has not been a primary focus of this article, one of the original justifications for crypto was to help the unbanked. “It’s going to prevent wars, help the unbanked and bring honesty to financial systems.” Kirsten Grind, *Let Me Tell You Some More About Bitcoin Hello? Hello?*, WALL ST. J. (Jan. 19, 2018), [<https://perma.cc/9C4M-H6UF>] (internal quotations omitted). The Federal Deposit Insurance Corporation (FDIC) reported in 2017 that as of that year, approximately 8.4 million U.S. households (or 14.1 million adults) were unbanked, and an additional 24.2 million households with 48.9 million adults were underbanked. FED. DEPOSIT INS. CORP., 2017 FDIC NATIONAL SURVEY OF UNBANKED AND UNDERBANKED HOUSEHOLDS 1 (Oct. 2018), [<https://perma.cc/HN84-WGAE>]. This is one of the most vulnerable populations in the U.S., and it seems particularly pernicious to limit services that might benefit them, or to restrict competition that might result in lower costs and better services for them. For a further consideration of the plight of the unbanked, and the correlation between banking status and race, age, and employment status in the U.S., see generally Catherine Martin Christopher, *Mobile Banking: The Answer for the Unbanked in America?*, 65 CATH. U. L. REV. 221 (2015).

The extended discussion of federal and state regulatory approaches is designed to explain, if not justify, the range of requirements applicable to crypto businesses that may be classified as money transmitters. This background is necessary to appreciate the extent of the barriers to entry that the current system imposes on entrepreneurs that might find themselves regulated as money transmitters. The lack of uniformity, despite efforts to promote a more consistent approach and widespread recognition of the problems that the current patchwork regulations have caused, appears certain to continue for the foreseeable future, unless there is federal intervention.

The case for preemption of state regulation turns both on the success of the federal approach to AML and CTF requirements as administered by FinCEN, and the failures of the state approach, which appear to stifle innovation and competition at the state level in a way that unfairly protects conventional businesses and potentially harms the unbanked who have not been able to afford conventional banking services. Admittedly, the suggestion of this Article, that the CFPB should be given preemptive authority to regulate inter-state crypto-based businesses for safety and soundness requirements, requires a Congressional mandate for preemption, a determination that the CFPB's authority and structure is constitutionally sound or an amendment to that structure; and an expansion of the CFPB's jurisdiction to include crypto-based money transmitter businesses. Nonetheless, the successes of that agency in advancing consumer interests and FinCEN's successes in developing a reasonable approach to protect against money laundering and funding of criminal enterprises suggest that this is the optimal direction for regulatory reform.