ABA Business Law Section
Annual Meeting
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Fintech Compliance and Regulation – Why More Collaboration and Engagement Is Needed
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For over a decade, financial firms have been collaborating with financial technology (fintech) companies on developing options to offer customers quick and convenient access to an array of financial products and services. A primary objective of these partnerships is using technology to deliver cost-efficient services to new customers (particularly tech-savvy ones).

Financial firms engaging with fintech companies have found themselves facing companies at various levels of maturity (from startups to some of the world’s largest corporations). Many fintech companies are technology and data business companies, but others may be banks, asset management companies, and other financial institutions. These collaborations are often financed through a variety of sources leveraging alliances with financial institutions spanning all sectors.

Leveraging new technologies for these collaborations may create more convenience for the customer, but increasingly trigger legal, regulatory, reputational, and other risks. For some time, there was little to no oversight of these engagements. Fintech collaborations were left on their own with most financial regulators unsure about how to regulate them. Fintech products also moved at a pace well beyond what regulators and regulations could address. This imbalance left regulators with limited options other than to oversee these relationships for compliance against traditional regulations (e.g., anti-money laundering, privacy).

Recent developments suggest the regulatory community is stepping up its oversight measures. While existing regulations have not yet fully factored in fintech products they are becoming a focus of rulemaking and enforcement actions. These actions include applying: 1) consumer protection laws regulating credit and debit products; 2) licensing requirements for non-bank entities holding or moving funds; 3) anti-money laundering and know your customer rules and regulations designed to protect our financial system against money laundering and terrorist financing; 4) privacy and data security regulations designed to protect personal information by regulating the handling, storage, transmission, and use of data as well as responses to security breaches; and 5) special considerations involving Blockchain and cryptocurrency.
The increasing focus at both the federal and state level in the United States has created a patchwork of state and federal requirements. The regulatory landscape overseeing fintech relationships is further complicated by the fact that many of these relationships are positioned to provide their products and services to a global consumer base. The global nature of such engagements may trigger a whole host of additional regulations, including complex and often restrictive data protection laws, such as the European Union’s General Data Protection Regulations.

In response, fintech partnerships would be prudent to establish and maintain a strong compliance foundation in preparation for the inevitable increased scrutiny from regulators. They must recognize they can no longer ignore these risks, and must better position themselves to manage them. In facing these challenges, fintech partnerships must establish and maintain robust compliance programs that are responsive to evolving regulatory developments.

Below is an outline of what the panel will cover during this session.

1. The current regulatory environment, risks, and challenges posed by these collaborations, while outlining practical strategies to establish and maintain compliance controls.
2. The panel will also discuss minimum expectations and best practices to help design and implement strong internal controls and
3. How to build a compliance culture around fintech relationships.

The panel will cover the current regulatory environment, risks and challenges posed by these collaborations while outlining practical strategies to establish and maintain compliance controls. The panel will offer best practices for establishing and maintaining compliance programs that are robust and responsive to emerging regulatory developments.
Fintech Compliance and Regulation – Why More Collaboration and Engagement Is Needed

ABA Business Crimes & Investigations Committee Panel (part of Business Law Section Annual Meeting)

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Fintech Compliance and Regulation – Why More Collaboration and Engagement Is Needed

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Outline

Background
  Overview of the U.S. Regulatory Scheme of Financial Firms
  Key Fintech Developments

Challenges
  Financial Regulation Keeping Pace with Fintech Innovation
  Patchwork of Regulation and Oversight

Oversight of Fintech and Financial Firm Relationships
  State vs. Federal Oversight
  Efforts to Improve Engagement, Collaboration and Oversight
  Creating outreach programs to bring together regulators and market participants
  Enhancing the Existing Regulatory Framework to better Manage Innovation (New Products, Practices, and Providers)

Special Issues
  AML
  Third-Party Risk Management
  Privacy
  Cybersecurity

Conclusion
  Final Thoughts

Questions
  Final Thoughts

Reference Materials
Introduction

- Fintech delivers significant benefits
  - Consumers and investors
  - Financial services firms and financial market infrastructure
  - Financial stability and financial inclusion

- Increasing use of fintech solutions is resulting in more risks and more regulatory scrutiny and focus

- More risks and greater regulatory scrutiny is prompting increasing focus on and need for governance, compliance and risk controls
Introduction

WHAT IS FINTECH?

- As defined by Computer World, FinTech “broadly speaking, is anywhere technology is applied in financial services or used to help companies manage the financial aspects of their business, including new software and applications, processes and business models.”

  https://www.computerworld.com/article/3225515/what-is-fintech-and-how-has-it-evolved.html

WHY IS IT IMPORTANT?

- Because regulators are paying attention: The Reference Materials contain releases from the SEC, CFTC, OCC, FINRA, FICEN, and the NYDFS.
- Because legislators are paying attention: Several states have passes FinTech statutes. Some impose restrictions; some eliminate restrictions.
- Because innovation is a competitive advantage but not without proper controls and oversight.

WHAT DOES IT MEAN FOR FINANCIAL SERVICES COMPLIANCE?

- Listen and learn
Background - Overview of the U.S. Regulatory Scheme of Financial Firms

No single reg framework – Federal, State and Self-Regulatory Authorities

Federal:

- Securities Exchange Commission (SEC)
  - Reg SCI
  - Reg S-P
  - Red Flags Rule

- Commodity Futures Trading Commission (CFTC)

- Consumer Financial Protection Bureau (CFPB)
  - providers of financial services to consumers
  - consumer lending, anti-discrimination, unfair and deceptive practices
Background - Overview of the U.S. Regulatory Scheme of Financial Firms

**Federal:**

- Federal Trade Commission (FTC)
  - Unfair and deceptive practices

- Dept of Treasury Financial Crimes Enforcement Network (FinCEN)
  - Bank secrecy and AML

- Office of the Controller of the Currency (OCC)
  - Primary federal bank regulator
Background - Overview of the U.S. Regulatory Scheme of Financial Firms

State:

• Licenses, including consumer lending, money transmission and digital asset/currency licenses
  – NY Department of Financial Services (NYDFS) “BitLicense”

• Privacy
  – California Consumer Privacy Act

• Cybersecurity
  – NYDFS Cybersecurity Regulation (23 NYCRR 500)
Background - Overview of the U.S. Regulatory Scheme of Financial Firms

Self-Regulatory Organizations:

- Financial Industry Regulatory Authority, Inc. (FINRA)
- The New York Stock Exchange (NYSE)
- Chicago Board of Trade (CBOT)
- Options Clearing Corporation (OCC)
Challenges - Financial Regulation Keeping Pace with Fintech Innovation

- Patchwork of Regulation and Oversight
  - Onerous multi-state requirements

- Federal vs State

- Digital Assets/Virtual Currencies
  - SEC – a security
  - CFTC – a commodity
  - FinCEN – money transmitter subject to BSA/AML
  - NYDFS - BitLicense
Challenges - Financial Regulation Keeping Pace with Fintech Innovation

- Privacy
  - Gramm-Leach-Bliley Act
  - Fair Credit Reporting Act
  - FTC
  - Electronic Communications Privacy Act
  - State privacy laws

- Digital Assets/Virtual Currencies
  - SEC – a security
  - CFTC – a commodity
  - FinCEN – money transmitter subject to BSA/AML
  - NYDFS - BitLicense
Background – Key FinTech Developments

- CFPB – “Project Catalyst”
- CFPB Sandbox
- OCC Office of Innovation
- CFTC – LabCFTC
- OCC - Special purpose national bank charter
Background – Key FinTech Developments

- Banking regulators of [seven] states working towards reciprocity re money service business licenses
- State Regulatory Sandboxes (Arizona, Wyoming)
Oversight of Fintech and Financial Firm Relationships

[State vs. Federal Oversight]

**Federal**
- Securities/commodities – SEC, CFTC
- Banking – Federal Reserve, OCC, FDIC, NCUA
- Anti-Money Laundering – FinCEN
- Tax – IRS

**State**
- Corporate and contract law – Delaware, Wyoming
- Blue sky laws
- Money transmitters, other non-bank financial services (MSBs)
- Banking/Anti-Money Laundering – New York DFS
Oversight of Fintech and Financial Firm Relationships

[Efforts to Improve Engagement, Collaboration and Oversight]

- Special virtual currency license: New York Bitlicense
- Conference of State Banking Supervisors – Vision 2020
  - Nationwide Multistate Licensing System & Registry (NMLS) for nonbank financial services
  - Model MSB law
- Regulatory sandboxes
Oversight of Fintech and Financial Firm Relationships

[Creating outreach programs to bring together regulators and market participants]

- State regulatory sandboxes
  - Arizona, Wyoming, Utah, Nevada
  - Insurance sandbox (Kentucky, Vermont)

- Federal
  - LabCFTC
  - SEC Strategic Hub for Innovation and Financial Technology
  - OCC Office of Innovation / Special Purpose Charter
  - CFPB Office of Innovation / Disclosure Sandbox
Oversight of Fintech and Financial Firm Relationships

[Enhancing the Existing Regulatory Framework to better Manage Innovation (New Products, Practices, and Providers)]

- New York DFS – Research and Innovation Division announced 7/23
  - Consolidates Bitlicense issuance and supervision, financial inclusion, consumer data protection, encouraging innovation

- State digital currency and blockchain working groups
  - Delaware, Illinois, North Carolina (by governor)
  - California, Florida, New York, Texas (by legislature)

- Federal – Facebook Libra Working Group (?)
Special Issues

Managing Special Issues - Anti-Money Laundering

- Myriad entities under the name “Fintech”
  - Are Fintechs “financial institutions” under BSA - 31 USC 5312? (MSB, etc)?
  - Future Regulatory Focus (z) “any other business designated by the Secretary…”

- Cost of Compliance – regulatory focus for future?
  - December 2018 Joint Statement on Innovation – impact?
  - Impact of new pending AML legislation, e.g., “Counter Act”
  - Regtech

- Federally or state regulated?
  - State law AML requirements (and other applicable laws) may differ
  - Financial Institutions may require Fintech BSA/AML programs for access to bank
  - Solving KYC issues

- FinCen Guidance – May 2019; “Innovation Hours”
- International Regulations (ECIN “Sandbox”, EU 5th Directive)
Special Issues

Managing Special Issues: Third-Party Risk Management

- Regulatory focus on Third Party Risk Management
  - Impact of Capital One
- Fintechs should expect heightened reviews from regulators and financial institution partners
- OCC Guidance 2013-17
- Cybersecurity focus
- New Legislation
Special Issues

- Managing Special Issues - Privacy
  - CFPB
  - FTC
  - Graham Leach-Bliley
  - GDPR
    - New Comprehensive requirements
    - Policy, Procedure and Contract Issues
  - New US Privacy Legislation? – e.g., Committee on Banking, Housing and Urban Affairs, May 7th 2019
  - Electronic Communications Privacy Act
  - State Law/California Consumer Privacy Act
Special Issues

- Managing Special Issues - Cybersecurity
  - Capital One impact
  - Interagency Guidelines establishing Information Security Standards 12 CFR Part 30
  - FFIEC IT Examination Manual and CAT
  - DFS Cyber Security Regulations
  - NIST and Best Practices
  - Treasury Report – Non-bank Financials, Fintech and Innovation
Practical Guidance

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Practical Guidance

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Fintech Compliance and Regulation – Why More Collaboration and Engagement Is Needed

Practical Guidance

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Conclusion

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Thank you.
Questions?
Reference Materials
- See attached Inventory