

## **New Actors, New Money, New Methods, Same Business: Salvaging Money Transmitter Regulation in Idaho for the 21st Century and Beyond**

Thomas Anderson

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**NEW ACTORS, NEW MONEY, NEW METHODS, SAME  
BUSINESS: SALVAGING MONEY TRANSMITTER  
REGULATION IN IDAHO FOR THE 21ST CENTURY AND  
BEYOND**

THOMAS ANDERSON

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# NEW ACTORS, NEW MONEY, NEW METHODS, SAME BUSINESS: SALVAGING MONEY TRANSMITTER REGULATION IN IDAHO FOR THE 21ST CENTURY AND BEYOND

THOMAS ANDERSON\*

## ABSTRACT

*The rise of the internet age and the exponential advance of technology is rapidly and dramatically changing all aspects of our world. The money transmission industry is no exception to this trend; however, Idaho's Money Transmitters Act was enacted before the implications of these changes were apparent and thus was not designed with the ability to adapt to them. This technological change has also highlighted the problems with the Balkanized state of interstate money transmitter regulation. This article attempts to address the problems with Idaho's current Money Transmitters Act and with the Balkanized national regulatory landscape governing money transmitters resulting from technological change. This article proposes three main changes to address these problems: centralizing regulatory and licensing authority of money transmitters in the Consumer Financial Protection Bureau or implementing interstate licensing reciprocity, matching the degree of regulation to the degree of risk of consumer loss a given entity represents, and finally adopting definitions and statutory language which more broadly conceptualizes the actors and activities involved in money transmission. The goal of these changes is not only to create effective money transmitter licensing regulation for the current state of affairs, but also to enable such regulation to remain effective in the face of the unending and unpredictable changes wrought by technological advancement.*

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\* 2019 J.D. Candidate at the University of Idaho College of Law. I would like to thank my advisor, Professor Wendy Couture. Her guidance kept this article on track and greatly improved the writing quality.

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## I. INTRODUCTION

Money transmitter acts, including Idaho’s Money Transmitters Act (the “Idaho Act” or “Act”), provide for the licensing of entities that engage in the transmission of money, with the purpose of protecting citizens.<sup>1</sup> Money transmitters are playing an increasingly important role in the daily life of the average American, with “[o]ver

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1. *E.g.*, CAL. FIN. CODE § 2030(a) (West 2018); IDAHO CODE § 26-2903(1) (2018).

one-quarter of U.S. households” using services from such entities.<sup>2</sup> Furthermore, the financial crisis of 2008 demonstrated that even established financial institutions involved in money transmission can fail,<sup>3</sup> and thus regulations to appropriately minimize the risk of failure and consumer loss are a necessary safeguard to maintain consumers’ trust in the money transmission industry.

Money transmitter acts were designed with traditional money transmitters, like Western Union, in mind.<sup>4</sup> However, because the rapid emergence of new technologies has changed the actors and activities involved in money transmission,<sup>5</sup> these money transmitter acts need to be updated to continue serving their purpose. In addition, because much of the innovation affecting money transmission is centered around internet-based technologies, which are almost inherently multistate in nature,<sup>6</sup> the challenges created by the Balkanized national regulatory landscape governing money transmitters are brought into increasingly sharp relief.<sup>7</sup> These challenges include stifled innovation, over and under-inclusive regulation, and increasingly ineffective protection for citizens who use money transmission services.<sup>8</sup>

New technology often has a disruptive effect on the industries in which it is adopted, and the money transmission industry is not exempt from this trend.<sup>9</sup> Technological innovations have introduced new actors and activities into the industry.<sup>10</sup>

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2. CONFERENCE OF STATE BANK SUPERVISORS & MONEY TRANSMITTER REGULATORS ASS’N, THE STATE OF STATE MONEY SERVICES BUSINESSES REGULATION & SUPERVISION 3 (2016); Courtney J. Linn, *One-hour Money Laundering: Prosecuting Unlicensed Money Transmitting Businesses Under 18 U.S.C. § 1960*, 8 U.C. DAVIS BUS. L.J. 138, 178 (2007) [hereinafter *One-hour Money Laundering*] (“[P]repaid cards have emerged as a means of delivering financial services to a large segment of the population that is either not served or underserved by traditional banks.”).

3. See PHILIP KEITEL, *INSOLVENCY RISK IN THE NETWORK-BRANDED PREPAID-CARD VALUE CHAIN* at 1, 21 (Sept. 2011) (discussing the failure of banks in 2009 and 2010 which had issued prepaid cards and the general risk of insolvency of such entities).

4. Benjamin Lo, *Fatal Fragments: The Effect of Money Transmission Regulation on Payments Innovation*, 18 YALE J.L. & TECH. 111, 112–13 (2016) [hereinafter *Fatal Fragments*].

5. Dong He et al., *IMF, Virtual Currencies and Beyond: Initial Considerations*, SDN/16/03, at 5 (2016); Debra Walton, *Technology is Disrupting the Way People Earn, Save and Spend. How Should Banks Respond?*, WORLD ECON. F. (Jan. 12, 2017), <https://www.weforum.org/agenda/2017/01/technology-is-disrupting-finance-how-should-leaders-respond/>; see M. MacRae Robinson, *Easing the Burden on Mobile Payments: Resolving Current Deficiencies in Money Transmitter Regulation*, 18 N.C. BANKING INST. 553, 554–56 (2014) [hereinafter *Easing the Burden*].

6. See Kevin V. Tu., *Regulating the New Cashless World*, 65 ALA. L. REV. 77, 80 (2013) [hereinafter *New Cashless World*] (internet payment systems are increasingly important); *Fatal Fragments*, *supra* note 4, at 112–13.

7. See *Fatal Fragments*, *supra* note 4, at 117–20.

8. *Id.* at 119; see Lalita Clozel, *When Will Fintech Regulation Grow Up?*, AM. BANKER (Oct. 5, 2016, 6:00 AM), <https://www.americanbanker.com/news/when-will-fintech-regulation-grow-up>.

9. Ron Miller, *Technology is Disrupting Everything*, TECHCRUNCH (Mar. 16, 2016), <https://techcrunch.com/2016/03/16/technology-is-disrupting-everything/>; Walton, *supra* note 5.

10. *Easing the Burden*, *supra* note 5; see *New Cashless World*, *supra* note 6. One clear example is the emergence of virtual currencies like Bitcoin, which rely on blockchain technology to function, which in turn relies on the internet. Ritchie S. King et al., *By Reading This Article, You’re Mining Bitcoins*, QUARTZ (Dec. 17, 2013), <https://qz.com/154877/by-reading-this-page-you-are-mining-bitcoins/>.

Moreover, technological changes that are not directly related to money transmission, including artificial intelligence (“AI”),<sup>11</sup> are likely to have a major impact on the industry in the near future.

In response to these new technologies, some states have been quick to amend their existing money transmitter regulations.<sup>12</sup> Idaho, however, has failed to make any substantive changes to the Idaho Act,<sup>13</sup> resulting in its obsolescence. While the Idaho Department of Finance has extended the Idaho Act to regulate some new technologies,<sup>14</sup> the current problems will continue to grow as new technology continues to emerge and as present technology achieves wider acceptance.

In addition to the issues directly presented by new technology, the current Idaho Act contributes to the Balkanized national regulatory landscape governing money transmitters. This morass of regulatory confusion discourages new companies from obtaining licenses and, to the extent new companies seek to comply, inhibits innovation by creating large barriers to entry.<sup>15</sup> The Uniform Law Commission has attempted to rectify this Balkanization through the Uniform Money Services Act (“UMSA”), but the UMSA has not yet been widely adopted.<sup>16</sup>

This article proposes two solutions to address these issues. The principal solution proposed is the implementation of a unified federal regulatory scheme which would preempt state-level regulation and be administered by the Consumer Financial Protection Bureau (“CFPB”). Alternatively, this article proposes several amendments to the existing Idaho Act designed to alleviate the issues created by the Balkanized regulatory landscape and to make the Idaho Act friendlier to new and innovative money transmitters, while continuing to serve the policy goal of protecting citizens.

This article proceeds in six parts. Part II provides a brief history of the Idaho Money Transmitters Act and the policies underlying it as well as a comparison to the policies underlying similar regulation in other states and at the federal level. Part III discusses the new technologies that are impacting the field of money transmission. Part IV discusses the implications and effects of such technologies on

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11. I use the term AI to include all manner of artificial intelligences and machine learning. For a good discussion of different levels and types of artificial intelligence, see *Artificial Intelligence in the Practice of Law: An Analysis and Proof of Concept Experiment*. Daniel Ben-Ari et al., *Artificial Intelligence in the Practice of Law: An Analysis and Proof of Concept Experiment*, 23 Rich. J.L. & Tech. 3 (2017).

12. See, e.g., WASH. REV. CODE ANN. § 19.230.055 (West 2018) (specific regulation of online currency exchangers); WASH. REV. CODE ANN. § 19.230.370 (West 2018) (disclosure requirements for virtual currency licenses); *Fatal Fragments*, *supra* note 4, at 125 (discussing New York’s implementation of a virtual currency regulatory framework).

13. See IDAHO CODE §§ 26-2901–2928 (2018) (no changes to the Act relating to changes in technology since its inception).

14. See *Idaho Money Transmitters Section*, IDAHO DEP’T FIN., <https://www.finance.idaho.gov/who-we-regulate/money-transmitters/> (last visited Mar. 24, 2019) (stating that exchangers of virtual currency are regulated money transmitters).

15. See *Fatal Fragments*, *supra* note 4, at 133–35 (licensing in the five most populous states would require over \$1 million in surety bonds, an upfront cost of about \$180,000, and annual costs of \$140,000); Tim Fernholz, *The Patchwork of Regulations Entangling Square, and Every American Internet Startup that Takes Money*, QUARTZ (Mar. 14, 2013), <https://qz.com/62265/why-square-and-seven-other-finance-start-ups-got-run-out-of-illinois/>.

16. See *Money Services Act*, UNIF. L. COMM’N (last visited Mar. 24, 2019), <https://www.uniform-laws.org/committees/community-home?CommunityKey=cf8b649a-114c-4bc9-8937-c4ee17148a1b> (indicating that the Uniform Money Services Act has only been enacted by a handful of States and territories).

money transmission and the regulation thereof. Part V provides an overview of the current Idaho Act. Part VI reviews other states' money transmission regulations, the Uniform Money Services Act, and current federal regulations. Drawing from the previous parts, Part VII analyzes the problems with the current Idaho Act and proposes several solutions.

## II. THE HISTORY AND UNDERLYING POLICIES OF MONEY TRANSMITTER REGULATION

An understanding of the history of the Idaho Act and the policies underlying it and similar regulation is necessary to appreciate the problems that new technologies present.

### A. The History and Policies of Idaho's Money Transmitters Act

Idaho's Money Transmitters Act was enacted in 1994 with the purpose of protecting Idaho's citizens from insolvent or fraudulent money transmitter businesses.<sup>17</sup> Consistent with this purpose, the Idaho Department of Treasury has ordered money transmitters to cease operation upon the determinations that (1) the transmitter appeared to be acting in a fraudulent manner such that it constituted "an immediate danger to the public" and (2) the order was "necessary for the protection of the public."<sup>18</sup>

Since its original enactment, the Idaho Act has only been amended a few times.<sup>19</sup> The most recent substantive change occurred in 2005, when Section 26-2915 was expanded slightly to require money transmitters to create and retain records required by other federal and state anti-money laundering laws.<sup>20</sup> This amendment indicated a legislative willingness to use the Idaho Act as a tool in the fight against illegal money laundering, especially as it relates to terrorism.<sup>21</sup>

In addition to enacting its own regulation, Idaho is a member of the Money Transmitter Regulators Association (MTRA).<sup>22</sup> The MTRA is an organization of member states with the primary goal of making interstate money transmitter regulation more efficient.<sup>23</sup> The MTRA Cooperative Agreement provides a framework for the

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17. 1994 Idaho Sess. Laws 410.

18. See, e.g., Order to Cease and Desist, at 6, *State of Idaho v. Strong Funds, Inc.*, 2006-12-02 (Idaho Dep't of Treasury Dec. 11, 2006) (order for company holding itself out as a licensed money transmitter in Idaho to cease operation since it was not actually licensed).

19. See H.B. 72, 55th Leg., 1st Reg. Sess. (Idaho 1999) (updating § 26-2906); H.B. 75, 58th Leg., 1st Reg. Sess. (Idaho 2005) (updating §§ 26-2914–2915, 26-2917); H.B. 91, 63d Leg., 1st Reg. Sess. (Idaho 2015) (updating § 26-2916).

20. See H.B. 75, 58th Leg., 1st Reg. Sess. (Idaho 2005) (updating §§ 26-2914–2915, 26-2917).

21. H.B. 75, 58th Leg., 1st Reg. Sess. (Idaho 2005).

22. *Members*, MONEY TRANSMITTER REGULATORS ASS'N, <https://www.mtraweb.org/about/members/> (last visited Mar. 24, 2019) (listing Idaho as a member State).

23. *Article 2: Statement of Purpose*, MONEY TRANSMITTER REGULATORS ASS'N, <https://www.mtraweb.org/about/cooperative-agreement/> (last visited Mar. 24, 2019). It is worth noting that the mere existence of such an organization, having over fifty member states and U.S. territories, indicates that interstate money transmitter regulation is problematic.

interaction of states “that have concurrent jurisdiction over a regulated entity.”<sup>24</sup> While the agreement identifies a “lead state” for overseeing a given transmitter, the lead state’s role is merely to “assist state supervisors in fulfilling their own regulatory responsibilities.”<sup>25</sup> Further, the agreement does not create any type of reciprocal licensing agreement.<sup>26</sup> While the Cooperative Agreement facilitates coordination of money transmitter regulation enforcement, it adds another layer of regulatory complexity and fails to mitigate the underlying Balkanization of the national regulatory landscape governing money transmitters.

#### B. The Underlying Policies of Money Transmitter Regulation in Other States and Federally

Almost every other state has enacted money transmitter regulation similar to Idaho’s Money Transmitter Act.<sup>27</sup> However, the purposes underlying other states’ regulations vary and sometimes even conflict.<sup>28</sup> For example, California’s underlying policy of protecting “the interests of consumers of money transmission businesses in [California]” may conflict with New York’s underlying policy of fostering “the growth of the financial industry in New York.”<sup>29</sup> A money transmitter with a new and risky business model that would expand the financial industry in New York may be allowed to operate there pursuant to the state’s aforementioned policy. However, that same money transmitter may not be allowed to operate in California due to the risk it poses to consumers. Such variations in policy further exacerbate the difficulty of creating a cohesive regulatory landscape as various state legislatures seek to achieve different ends with the same type of regulation.

At the federal level, the focus of money transmitter regulation has traditionally been on preventing money laundering.<sup>30</sup> The principal regulations governing money transmitters at the federal level are contained within the Bank Secrecy Act

24. *Id.*

25. Section 2.2 *Responsibilities*, MONEY TRANSMITTER REGULATORS ASS’N, <https://www.mtraweb.org/about/cooperative-agreement/> (last visited Mar. 24, 2019). See also Article 6: *Applicable Laws*, MONEY TRANSMITTER REGULATORS ASS’N, <https://www.mtraweb.org/about/cooperative-agreement/> (last visited Mar. 24, 2019) (explicitly stating that the laws of each with jurisdiction over an entity may not be waived).

26. See Article 6: *Applicable Laws*, MONEY TRANSMITTER REGULATORS ASS’N, <https://www.mtraweb.org/about/cooperative-agreement/> (last visited Mar. 24, 2019); Article 7: *Application*, MONEY TRANSMITTER REGULATORS ASS’N, <https://www.mtraweb.org/about/cooperative-agreement/> (last visited Mar. 24, 2019) (explicitly stating that each state will retain authority of licensing application approval).

27. See Thomas Brown, *50-State Survey: Money Transmitter Licensing Requirements*, [http://abnk.assembly.ca.gov/sites/abnk.assembly.ca.gov/files/50%20State%20Survey%20-%20MTL%20Licensing%20Requirements\(72986803\\_4\).pdf](http://abnk.assembly.ca.gov/sites/abnk.assembly.ca.gov/files/50%20State%20Survey%20-%20MTL%20Licensing%20Requirements(72986803_4).pdf) (last visited Mar. 24, 2019) [hereinafter 50-STATE SURVEY]; *Money Services Act*, UNIF. L. COMM’N, <https://www.uniformlaws.org/committees/community-home?CommunityKey=cf8b649a-114c-4bc9-8937-c4ee17148a1b> (last visited Mar. 24, 2019) (listing 12 states and U.S. territories that have adopted the Uniform Money Services Act).

28. See *Fatal Fragments*, *supra* note 4, at 117–18 (identifying consumer protection, money laundering prevention, and protection of the financial service industry among the policy reasons underlying their regulation).

29. CAL. FIN. CODE § 2001(d) (West 2018); N.Y. FIN. SERV. LAW § 201(b)(1) (McKinney 2018).

30. See *Fatal Fragments*, *supra* note 4, at 114; 31 U.S.C. § 5311 (2012).



(BSA), which is enforced by the Financial Crimes Enforcement Network (FinCEN).<sup>31</sup> However, after the 2008 financial crisis, the federal government increased focus on financial regulation protecting consumers, as evidenced by the establishment of the Consumer Financial Protection Bureau (CFPB) and the implementation other financial regulations.<sup>32</sup>

### III. NEW AND EMERGING TECHNOLOGY CHANGING MONEY TRANSMISSION

To have a meaningful discussion about the problems with the current Idaho Act caused or highlighted by certain new technologies, a basic understanding of those technologies is required. The proliferation of computers and the rise of the internet underlie the technologies that currently have, or present the greatest potential to have, the most disruptive effect on the money transmission industry. This article focuses on several of these technologies while recognizing that other technologies that do not seem important now may have a dramatic impact in the future.

#### A. Blockchain

The technology with perhaps the greatest potential to disrupt the current money transmission industry is blockchain-based technology.<sup>33</sup> A blockchain is essentially an immutable distributed ledger that eliminates the need for trust in transactions.<sup>34</sup> It is blockchain's ability to remove the need for trust from transactions that makes the technology valuable.<sup>35</sup> Blockchain technology thus impacts money transmission, among other ways, by allowing new forms of currency and by fundamentally changing the manner in which entities using the technology can be effectively regulated.<sup>36</sup>

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31. *Fatal Fragments*, *supra* note 4, at 114–15; 31 U.S.C. § 310(b)(2)(I) (2012) (charging FinCEN with administering the BSA).

32. *E.g.*, Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank), 15 U.S.C. § 1693 (2012); *see Bureau*, CONSUMER FIN. PROTECTION BUREAU, <https://www.consumerfinance.gov/about-us/the-bureau/> (last visited Mar. 24, 2019).

33. This is based on the fact that blockchain technology has not only already caused disruption, but also that, like the internet, it has the potential to be a “foundational technology.” Marco Iansiti & Karim R. Lakhani, *The Truth About Blockchain*, 95 HARV. BUS. REV. 118, 120 (2017).

34. *See* Nolan Bauerle, *What is Blockchain Technology*, COINDESK, <https://www.coindesk.com/information/what-is-blockchain-technology/> (last visited Mar. 24, 2019).

35. TEDx Talks, *Blockchain: Massively Simplified | Richie Etwaru | TEDxMorristown*, YOUTUBE (May 15, 2017), [https://www.youtube.com/watch?v=k53LU\\_ZxUF50](https://www.youtube.com/watch?v=k53LU_ZxUF50) [hereinafter TEDx Talks] (starting at 4:35).

36. *See* Madhvi Mavadiya, *Blockchain, Bitcoin and Ethereum Explained*, FORBES (Aug. 22, 2017, 9:00AM), <https://www.forbes.com/sites/madhvimavadiya/2017/08/22/blockchain-bitcoinethereum/#6ff762b76df9> (discussing the importance of blockchain technology's removal of intermediaries); Marco A. Santori, *Governor Jack Markell Announces Delaware Blockchain Initiative*, GLOBALDELAWARE (June 10, 2016), <https://global.delaware.gov/2016/06/10/delaware-to-create-distributed-ledger-based-share-ownership-structure-as-part-of-blockchain-initiative/> (discussing the possibility of blockchain based technologies eliminating all intermediaries in the validation and settlement of transactions).

Perhaps the most well-known implementations of blockchain technology are blockchain-based virtual currencies.<sup>37</sup> The most popular of these currencies is Bitcoin.<sup>38</sup> These virtual currencies have become increasingly popular and have started to see mainstream acceptance as a form of currency.<sup>39</sup> Both individuals and large companies are starting to invest in virtual currencies.<sup>40</sup> The increasing interest has also spawned a veritable tsunami of different blockchain-based currencies.<sup>41</sup> Some are similar to Bitcoin,<sup>42</sup> while others, like STEEM or Ethereum, have purposes beyond merely serving as a currency.<sup>43</sup>

In addition to blockchain-based virtual currencies, another blockchain-based technology implicating money transmitter regulation is the smart contract. A smart contract is “computer code that can facilitate the exchange of . . . anything of value,” which, “when running on the blockchain . . . becomes like a self-operating computer program that automatically executes when specific conditions are met.”<sup>44</sup> These smart contracts enable the creation and execution of decentralized applications that can serve an almost unlimited number of functions.<sup>45</sup> One of the most promising applications of smart contracts for money transmitter regulation is the automation of regulatory compliance through the ability of all entities utilizing the same blockchain network to validate and report on transactions occurring over

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37. Many articles have been written discussing blockchain based virtual currency. *See, e.g.*, Sarah Jane Hughes & Stephen T. Middlebrook, *Advancing a Framework for Regulating Cryptocurrency Payments Intermediaries*, 32 YALE J. ON REG. 495 (2015); Jacob Hamburger, *Bitcoins vs. State Money Transmission Laws: Protecting Consumers or Hindering Innovation?*, 11 J.L. ECON. & POL'Y 229 (2015); James Gatto & Elsa S. Broeker, *Bitcoin and Beyond: Current and Future Regulation of Virtual Currencies*, 9 OHIO ST. BUS. L.J. 429 (2015).

38. DAVID LEE KUO CHUEN, *HANDBOOK OF DIGITAL CURRENCY: BITCOIN, INNOVATION, FINANCIAL INSTRUMENTS, AND BIG DATA* 310 (2015).

39. Sean Williams, *5 Brand-Name Businesses that Currently Accept Bitcoin*, THE MOTLEY FOOL (July 6, 2017, 7:41AM), <https://www.fool.com/investing/2017/07/06/5-brand-name-businesses-that-currently-accept-bitc.aspx> (noting that overstock.com, DISH Network, Microsoft, Intuit, and Paypal accept bitcoins for payment).

40. Kazuaki Nagata, *Booming Cryptocurrencies Fire Up Investment Interest*, THE JAPAN TIMES (Aug. 20, 2017), <https://www.japantimes.co.jp/news/2017/08/20/business/virtual-currencies-enjoy-investment-boom-consumers-hesitate/#.WgjRYWIPKUK>.

41. Prableen Bajpai, *The 10 Most Important Cryptocurrencies Other than Bitcoin*, INVESTOPEDIA, <https://www.investopedia.com/tech/most-important-cryptocurrencies-other-than-bitcoin/> (last updated Feb. 9, 2019) (noting that there were over 700 different cryptocurrencies like Bitcoin).

42. *See Frequently Asked Questions*, BITCOINCASH, <https://www.bitcoincash.org/#faq> (last visited Mar. 24, 2019) (describing Bitcoin Cash as “peer-to-peer electronic cash” which is separate from Bitcoin).

43. *See STEEM Blueprint: A Protocol for Enabling Smart, Social Currency for Publishers and Content Businesses Across the Internet*, STEEMIT, INC. 1 (2017), <https://steem.io/steem-bluepaper.pdf> (describing a blockchain based currency aimed at encouraging social media engagement and monetizing online content); *Ethereum Blockchain App Platform*, ETHEREUM, <https://www.ethereum.org/> (last visited Mar. 24, 2019) (blockchain based virtual currency aimed at facilitating the operation and use of the Ethereum network—a decentralized platform for smart contracts).

44. *What Is Ethereum? A Step-by-Step Beginners Guide*, BLOCKGEEKS, <https://blockgeeks.com/guides/what-is-ethereum/> (last visited Mar. 24, 2019).

45. *Id.*

the network.<sup>46</sup> The automation of regulatory compliance validation could dramatically decrease the risk of fraud to consumers by enabling regulators, both government and those within a company, to automatically be notified of potential regulatory violations.

The smart contracts concept can be extended to create a decentralized autonomous organization (DAO) operating on the blockchain.<sup>47</sup> “A DAO is [a] fully autonomous, decentralized organization” that is “run by programming code, on a collection of smart contracts written on the . . . blockchain. The code is designed to replace the rules and structure of a traditional organization, eliminating the need for people and centralized control.”<sup>48</sup> A DAO may even operate independently of its original creators.<sup>49</sup> The projects on which a DAO works are generally determined by a vote of those who have bought into the DAO; however, these people do not necessarily own the DAO itself.<sup>50</sup> Instead, those who have bought in generally have a claim to a certain output product.<sup>51</sup> The net result is that there is no clear owner or party responsible for a given DAO.<sup>52</sup>

#### B. Prepaid Payment Mechanisms

Providers of prepaid payment mechanisms, like gift cards and Visa prepaid cards, are generally considered to fall within the purview of money transmitter regulation at the state level.<sup>53</sup> However, the breadth of entities considered to be such a provider is expanding as new prepaid payment mechanisms are developed. Moreover, as prepaid mechanisms become increasingly important to Americans,<sup>54</sup> ensuring that the issuers of such mechanisms are appropriately regulated to protect consumers also becomes increasingly important.

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46. This could be achieved two ways. First, by requiring that money transmitters utilizing the network build regulatory compliance into their smart contracts. Second, by creating a regulatory compliance monitoring algorithm which automatically monitors entities acting on the blockchain network and reports violations to the regulatory agency.

47. *What Is Ethereum? A Step-by-Step Beginners Guide*, *supra* note 44.

48. *Id.*

49. *Id.*

50. *Id.* The process of buying into a DAO, which is generally done via participation in the structure or a contribution into such a DAO, has been found to essentially constitute a securities offering, and thus may be subject to regulation under securities law. Timothy B. Lee, *Using a Blockchain Doesn't Exempt You from Securities Regulations*, ARSTECHNICA (July 26, 2017, 1:40PM), <https://arstechnica.com/tech-policy/2017/07/using-a-blockchain-doesnt-exempt-you-from-securities-regulations/>.

51. This claim would arise through the common law of contracts.

52. See Nick Vogel, *The Great Decentralization: How Web 3.0 Will Weaken Copyrights*, 15 J. MARSHALL REV. INTELL. PROP. L. 135, 140–42 (2015) (discussing DOAs and noting the potential lack of liable parties for copyright infringement in the context of a decentralized internet).

53. See *New Cashless World*, *supra* note 6, at 103 (noting that issuers of stored value that may be used to make purchases at merchants other than the issuer are subject to regulation).

54. *One-hour Money Laundering*, *supra* note 2 (“[P]repaid cards have emerged as a means of delivering financial services to a large segment of the population that is either not served or underserved by traditional banks.”).

One of the newest forms of a prepaid payment mechanism is the digital wallet.<sup>55</sup> An example of this is Google Wallet:

[W]hen the customer agrees to purchase a good. . . a payments solution provider under contract with Google . . . issues a onetime, prepaid, virtual MasterCard debit card for the amount of the transaction. Google Wallet debits the single use card and transfers that amount to the merchant and subsequently debits the same amount from the customer's bank account that is stored in Google Wallet.<sup>56</sup>

Similarly, Apple has introduced a peer-to-peer (P2P) payment system that relies on prepaid mechanisms.<sup>57</sup>

Venmo is another example of a digital wallet which constitutes a prepaid mechanism.<sup>58</sup> In addition to being able to debit and credit a user's bank account, Venmo holds currency received from others in a user's account until the customer requests that the funds be transferred to a bank, to a merchant, or to another person using the service.<sup>59</sup>

Both these new takes on prepaid payment mechanisms and more traditional iterations are subject to increasing regulation at the federal level.<sup>60</sup> This increasing regulation sits atop the myriad regulations already imposed on prepaid payment mechanisms by several different federal agencies.<sup>61</sup>

### C. Payment Processors

The current Idaho Act applies to payment processors, a category of financial entities experiencing significant change as a result of new technologies.<sup>62</sup> The rise of the internet and other technologies have allowed new service providers to “facilitate consumer-to-merchant payments” in commercial transactions.<sup>63</sup> These new providers “typically underwrite the payment to the merchant, then later withdraw the money from the consumer's bank account or charge the consumer's credit

55. *Easing the Burden*, *supra* note 5.

56. *Id.* at 556.

57. Fitz Tepper, *You Can Now Send Your Friends Money Inside iMessage*, TECHCRUNCH (June 5, 2017), <https://techcrunch.com/2017/06/05/you-can-now-send-your-friends-money-inside-imessage/>.

58. *See How It Works*, VENMO, <https://venmo.com/about/product> (last visited Mar. 24, 2019) (Venmo allows users to pay anyone instantly “using money you have in Venmo”).

59. *See Purchase Funding Sources – Venmo*, VENMO, <https://help.venmo.com/hc/en-us/articles/217532317-Purchase-Funding-Sources> (last updated Mar. 23, 2019) (Venmo funds transactions from the balance in your Venmo account).

60. *See* CONSUMER FIN. PROT. BUREAU, PREPAID RULE: SMALL ENTITY COMPLIANCE GUIDE 1 (2017); Gillian B. White, *The New Rules of Digital Cash*, ATLANTIC (Oct. 5, 2016), <https://www.theatlantic.com/business/archive/2016/10/cfpb-prepaid-venmo/503000/> (noting that the new CFPB rules will impact Venmo and other digital entities).

61. “Currently, five agencies - the Federal Reserve System, the Consumer Financial Protection Bureau (CFPB), the Office of the Comptroller of the Currency, the National Credit Union Administration, and the Federal Trade Commission (FTC) - all have some responsibility in overseeing the regulation of the mobile payments business.” *Easing the Burden*, *supra* note 5, at 558. “[T]he CFPB and the FTC currently assume concurrent responsibility of consumer protection.” *Id.* at 559.

62. *See Idaho Money Transmitters Section*, *supra* note 14 (stating that payment processors are regulated as money transmitters).

63. *Fatal Fragments*, *supra* note 4, at 122.

card.”<sup>64</sup> By underwriting the payments, these providers decrease the risk to the merchant of non-payment and the risk to the payor of the payment processor absconding with their money. Further, these new providers have driven down the cost of payment processing services while making them easier to access and use.<sup>65</sup>

#### D. Incidental Transmitters<sup>66</sup>

A result of the internet making money transmission easier is that more entities have started engaging in money transmission in the course of providing goods or services, and thus the transmission is incidental to their core business.<sup>67</sup> This category encompasses some of the largest internet-based companies, including Amazon.com, Uber, and AirBnB.<sup>68</sup> While federal law excludes such entities,<sup>69</sup> Idaho’s Act does not contain a similar exemption.<sup>70</sup>

#### E. Artificial Intelligence

The last principal technology considered by this article is AI. AI creates the possibility that humans will be entirely removed from the process of creating and operating a money transmitter.<sup>71</sup> While AI technology is not yet so advanced, limited implementations of artificially intelligent learning algorithms, also known as machine learning, are beginning to see widespread adoption in other financial industries.<sup>72</sup>

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64. *Id.*

65. *See id.* (noting that payment processor “startups provide easy-to-use software and hardware that allow small businesses to receive payment from consumers.”); Adam J. Levitin, *Payment Wars: The Merchant-Bank Struggle for Control of Payment Systems*, 12 STAN. J.L. BUS. & FIN. 425, 481 (2007) (PayPal has reduced the transaction costs of processing payments compared to traditional networks).

66. I have adopted this term from Benjamin Lo and his discussion of them in *Fatal Fragments: The Effect of Money Transmission Regulation on Payments Innovation*. *Fatal Fragments*, *supra* note 4, at 121–22.

67. *Id.*

68. *See id.* (discussing how online market platforms which “connect buyers and sellers of goods and services . . . usually offer a native payment function to help sellers get paid”).

69. *See* 31 C.F.R. § 1010.100(ff)(5)(ii)(B) (2017).

70. *See* IDAHO CODE §§ 26-2901–2928 (2018).

71. Gregory Scopino, *Preparing Financial Regulation for the Second Machine Age: The Need for Oversight of Digital Intermediaries in the Futures Markets*, 2015 COLUM. BUS. L. REV. 439, 451 (“Within a matter of time, computers and software programs will essentially act as independent, autonomous artificial agents.”).

72. *See* Daniel Ben-Ari et al., *Artificial Intelligence in the Practice of Law: An Analysis and Proof of Concept Experiment*, 23 RICH. J.L. & TECH. 2, 28 (2017); Tom C.W. Lin, *The New Investor*, 60 UCLA L. REV. 678, 689–93 (2013) (discussing the use of algorithm-based trading and asset management rising rapidly in prominence).

#### IV. HOW THESE NEW TECHNOLOGIES STRAIN THE EXISTING MONEY TRANSMITTER REGULATION

Whereas the implications of some of these technologies on the money transmission industry and consequently on its regulation may be clear, it is worth further exploring some of the specific issues that these technologies operating independently and together present.

##### A. Implications of the Rise of the Internet

Looking at internet-based technologies more generally, their rise has created a money transmitter landscape that is no longer geographically bounded. The internet has enabled companies to offer money transmission services even when they are not physically present in Idaho. By removing such restrictions, internet-based entities have less incentive to meet the high regulatory burden imposed by the current Act because a digital presence is more difficult to regulate than a physical presence,<sup>73</sup> especially when the entities are new.<sup>74</sup> Moreover, the relatively small population of Idaho likely dis-incentivizes those entities that might otherwise comply with Idaho's licensing requirements from providing services to the jurisdiction due to the regulatory burden. Further, this regulatory burden may incentivize entities to attempt to operate under the radar of Idaho's Department of Treasury until they have a sufficient customer base to offset the regulatory costs of obtaining a license.<sup>75</sup>

This is especially true when considering the Idaho Act's regulation of prepaid payment mechanisms. As discussed above, new actors are starting to become involved in the issuance of prepaid payment mechanisms because of new technology—in particular, the rise of the internet. As such mechanisms become more important to Idaho's citizens,<sup>76</sup> the redundant regulations imposed by the Idaho Act

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73. These difficulties arise both from jurisdictional problems and from the inability of regulators to punish those who violate the law when they have no assets within the physical territory of the state. See Alan M. Trammell & Derek E. Bambauer, *Personal Jurisdiction and the "Interwebs"*, 100 CORNELL L. REV. 1129, 1188 (2015) (positing the hypothetical difficulties of a U.S. citizen recovering on a judgement from a U.S. court against a hacker in Iran for harm the hacker caused). See generally Teresa Scassa & Robert J. Currie, *New First Principles? Assessing the Internet's Challenges to Jurisdiction*, 42 GEO. J. INT'L L. 1017 (2011) (discussing the challenges posed to establishing jurisdiction across international borders over activities and actors on the internet).

74. See Tim Fernholz, *The Patchwork of Regulation Entangling Square, and Every American Internet Startup that Takes Money*, QUARTZ (Mar. 14, 2013), <https://qz.com/62265/why-square-and-seven-other-finance-start-ups-got-run-out-of-illinois/>.

75. Such evasion has occurred with business that have become very successful, such as Square. See Ingrid Lunden, *Square Fined \$507K In Florida For Operating A Mobile Payment Service Without A Money Transmitter License*, TECHCRUNCH (Aug. 16, 2013), <https://techcrunch.com/2013/08/16/square-fined-507k-in-florida-for-operating-a-mobile-payment-service-without-a-money-transmitter-license/>; see also *General Information Name Search*, DEL. DIV. CORP., <https://icis.corp.delaware.gov/ecorp/entitysearch/NameSearch.aspx> (search "4699855" in the "File Number:" box and then click "SQUARE, INC." under "ENTITY NAME") (last visited Mar. 24, 2019) (indicating that Square was incorporated in 2009).

76. See Sarah Glenn, *More Idahoans Have Bank Accounts, but Underbanked Population Soars*, IDAHO ST. J. (Nov. 1, 2016), [https://infoweb.newsbank.com/apps/news/openurl?ctx\\_ver=z39.88-](https://infoweb.newsbank.com/apps/news/openurl?ctx_ver=z39.88-)

will become an increasingly inconvenient and burdensome barrier to beneficial innovation for Idaho's citizens.

B. Implications of Blockchain-Based Technology Itself and in Conjunction with  
 Artificial Intelligence

As noted above, blockchain-based technologies have already had an impact on the money transmission industry and are poised to have an even greater transformative effect. There are several notable ways that blockchain technologies themselves, or in combination with other technologies, are straining—or are poised to strain—the existing regulatory framework.<sup>77</sup>

One of the most readily apparent effects of blockchain-based technologies is the rise of virtual currencies.<sup>78</sup> As these virtual currencies see greater acceptance, it becomes more likely that they will constitute a substantial asset to a given individual. The result is that the current Act will be less effective at protecting Idaho's citizens' assets that have substantially the same, if not more, value to them as traditional currencies. This diminished effectiveness arises from the Act's failure to regulate transmissions involving only virtual currencies and the more volatile nature of such currencies.<sup>79</sup>

Blockchain technologies present the possibility of radically changing the actors involved in money transmission.<sup>80</sup> The most immediate of these changes to the actors involved is that the intermediaries facilitating money transmission transactions no longer need to be human.<sup>81</sup> Instead, an automated algorithm operating on the blockchain may soon be the only relevant actor involved in the actual transmission.<sup>82</sup> Moreover, such transactions are inherently transparent to anyone on the

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2004&rft\_id=info%3Asid/fofweb.new-bank.com&svc\_dat=AMNEWS&req\_dat=2D945D1F48F94F9BAB3FED5084ADC164&rft\_val\_format=info%3Aofi/fmt%3Akev%3Amtx%3Actx&rft\_dat=document\_id%3Anews%252F1606207177D67AB8/zone%3A.

77. See Iansiti, *supra* note 33, at 120 (noting that blockchain based technologies will require changes to regulation for their full benefit to be realized).

78. See Sean Williams, *supra* note 39; Ken Yagami, *Japan: A Forward Thinking Bitcoin Nation*, FORBES (Nov. 2, 2017, 5:48 AM), <https://www.forbes.com/sites/outofasia/2017/11/02/japan-a-forward-thinking-bitcoin-nation/#1f4aaf4233a3> (discussing how Japan has become the first nation to amend its laws "to allow 'virtual currencies' as a legal form of payment").

79. See Joel Comm, *Coping with BitCoin's Volatility*, FORBES (Nov. 5, 2017, 8:30 AM), <https://www.forbes.com/sites/forbescoachescouncil/2017/11/05/coping-with-bitcoins-volatility/#40a7f20d62ec>.

80. See TEDx Talks, *supra* note 35 (discussing how blockchain removes the need for intermediaries); Christine Lagarde, IMF Managing Dir., *Central Banking and Fintech – A Brave New World?* (Sep. 29, 2017), <https://www.imf.org/en/News/Articles/2017/09/28/sp092917-central-banking-and-fintech-a-brave-new-world>.

81. See TEDx Talks, *supra* note 35 (the automated blockchain algorithm executes transaction without human involvement).

82. See *id.* Recognition must be given to the fact that there is an element of human control since changes can generally be made to the blockchain network protocol with minimal disruption by a consensus of at least 51% of the computing power operating the blockchain. Alyssa Hertig, *Why are Miners Involved in Bitcoin Code Changes Anyway?*, COINDESK (Jul. 28, 2017, 3:05 PM), <https://www.coindesk.com/miners-involved-bitcoin-code-changes-anyway/>. However, this decentralized control effectively regulates those

blockchain network.<sup>83</sup> Thus, by effectively removing the human component while at the same time increasing the transparency of those engaging in money transmission, the risk posed by such transmitters is reduced significantly. An example of a successful implementation of blockchain technology in the financial sector can be found in IBM's use of the technology in their capital financing operation, which is worth \$48 billion a year.<sup>84</sup> Due "to a comprehensive view of operational data from purchase orders to remittances consolidated and distributed to all parties," IBM decreased its dispute amount from \$100 million at a given time to \$30 million and decreased its dispute resolution time by about 75%.<sup>85</sup> The current Act is unable to appropriately respond in a standard way to this very low risk actor, instead imposing the same licensing requirements as are imposed on all transmitters.<sup>86</sup> A separate implication of this technological potential is that the regulatory focus of entities properly employing such technology should switch from the transaction records themselves (since any tampering with those would be easily spotted by a properly developed validation algorithm)<sup>87</sup> to the validation algorithm itself.

Another implication of blockchain technology is that the decentralized and anonymized nature of some implementations of the technology may result in the inability of any one entity to fully report all of the transactions occurring across a network.<sup>88</sup> Individuals may have access to the whole transaction ledger for the chain, but the information identifying specific parties can be anonymized—thereby severely restricting or eliminating the ability of a given individual on a blockchain to tie any particular transaction to any particular individual.<sup>89</sup> The result is that even though the ledgers of the actor are completely transparent, full compliance with the current Act's records requirements may be impracticable.<sup>90</sup>

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seeking to abuse the blockchain because the number of bad actors on the chain would need to constitute at least 51% and, because abuse of the blockchain would likely devalue the currency, there are strong disincentives against malicious abuse. The result is that the risk lies with the entities providing the "wallet" or end-user services because the same difficulties and disincentives do not apply.

83. *What Is Blockchain Technology? A Step-by-Step Guide for Beginners*, BLOCKGEEKS, <https://blockgeeks.com/guides/what-is-blockchain-technology/> (last updated Mar. 1, 2019). Transparent here means that anyone with control over or access to a node on the blockchain performing transaction validation functions (i.e. holding a copy of the distributed ledger and checking transactions against it) will generally be able to see at least the basic information about a given transaction. *See id.*

84. Kamil Gregor, *IBM Wants to Make 2017 the Year of 2017 Blockchain Enterprise Deployment*, IDC 3–4 (April 2017) [https://www.ibm.com/blockchain/in-en/assets/IDC\\_Report\\_\\_IBM\\_wants\\_to\\_make\\_2017\\_the\\_year\\_of\\_BlockChain\\_Enterprise\\_\\_Deployment.pdf](https://www.ibm.com/blockchain/in-en/assets/IDC_Report__IBM_wants_to_make_2017_the_year_of_BlockChain_Enterprise__Deployment.pdf) (discussing IBM's use of blockchain technology in the resolution of financing disputes).

85. *Id.* at 4.

86. *See* IDAHO CODE § 26-2904 (2018) (does not contain exemption for low risk entities); IDAHO CODE § 26-2905(1) (2018) (applying the same net worth requirements for all transmitters as a condition of licensing); IDAHO CODE § 26-2908 (2018) (applying the same bond requirements to all transmitters as a condition of licensing). The net worth requirements may become inapplicable when the only entity engaged in the transaction is the automated algorithm, because it does not need the assets of a traditional business.

87. *See What Is Ethereum? A Step-by-Step Beginners Guide*, BLOCKGEEKS, <https://blockgeeks.com/guides/what-is-ethereum/> (last updated Sept. 12, 2018).

88. *See What Is Cryptocurrency: Everything You Need to Know [Ultimate Guide]*, BLOCKGEEKS, <https://blockgeeks.com/guides/what-is-cryptocurrency/> (last updated Sept. 13, 2018).

89. *Id.*

90. *See* IDAHO CODE § 26-2914(1) (2018).



Blockchain technology also creates the foundation for DAOs, which have the potential to perform money transmission activities requiring a license but lack any clearly identifiable party responsible for obtaining one. Situations could arise where a DAO acts as a payment processor by processing payments from clients to its members or where a DAO issues stored value cards that may be used to purchase goods or services from any of the DAO's members. In either scenario, because the money transmission activity occurs via smart contracts and the only "persons" party to the transaction are end users,<sup>91</sup> it is unlikely that any party in a given transaction would be "controlling" or otherwise liable.<sup>92</sup>

A more radical and more distant possible change built on blockchain technology is the creation of DAO that operates via an AI. Imagine this scenario: A DAO is created to enable P2P transactions, which is governed by an AI who creates the rules of the blockchain supporting the DAO and make changes as necessary to further its goal of enabling P2P transactions. In the course of executing a smart contract between two people, one in State X and the other in State Y to transfer real currency the AI determines that the most efficient routing is via a node in Idaho that a person has put on the network. This person has made his or her computing power available to the network without knowing exactly how it will be used. Assuming the transmission is a violation of the Act, who is responsible for getting the DAO licensed? It was created only to enable P2P transactions but not specifically currency transactions. Further, there is no individual or easily definable group controlling the entity. The current Act does not provide a clear answer, and situations like this may not be that far off in the future.<sup>93</sup>

### C. Implications of the Increase in Incidental Transmitters

One final implication of emerging technology to consider is that the current Idaho Act applies to entities that the drafters of the Act likely would not have intended to cover.<sup>94</sup> Entities like incidental transmitters, which generally present a low risk of loss to consumers,<sup>95</sup> are required to be licensed as money transmitters

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91. See IDAHO CODE § 26-2902(15) (2018) (definition of "person" for the purpose of the Idaho Act).

92. See IDAHO CODE § 26-2902(15) (2018) (defining "person" under the Act). See generally Nick Vogel, *The Great Decentralization: How Web 3.0 Will Weaken Copyrights*, 15 J. MARSHALL REV. INTELL. PROP. L. 136, 142 (2015) (discussing the problems with liability for copyright infringement in the context of a decentralized internet).

93. See Falguni Desai, *The Age of Artificial Intelligence in Fintech*, FORBES (June 30, 2016, 10:42 PM), <https://www.forbes.com/sites/falgunidesai/2016/06/30/the-age-of-artificial-intelligence-in-fintech/#181a24335028> (artificial intelligence in financial technologies is becoming increasingly prevalent); Paul Vigna ET AL., *Goldman Sachs Explores a New World: Trading Bitcoin*, WALL STREET J. (Oct. 2, 2017, 8:00 PM), <https://www.wsj.com/articles/goldman-sachs-explores-a-new-world-trading-bitcoin-1506959128> (Goldman Sachs, one of the companies employing AI in fintech, is exploring expansion into blockchain based virtual currencies); Trent McConaghy, *AI DAOs, and Three Paths to Get There*, BIGCHAINDB (June 18, 2016), <https://blog.bigchaindb.com/ai-daos-and-three-paths-to-get-there-cfa0a4cc37b8> (discussing how DAOs operated by AIs may work).

94. See *Fatal Fragments*, supra note 4, at 122.

95. See *id.* (incidental transmitters generally present a lower risk of loss to consumers).

even though their transmission activities are merely incidental to their core business.<sup>96</sup> Companies like Uber and AirBnB fill a need as evidenced by their rapid growth and adoption.<sup>97</sup> However, the benefits provided by such companies may be slower to reach Idaho consumers due to the regulations imposed on such entities and the decreased incentive to serve a state with a smaller population.

## V. OVERVIEW OF IDAHO'S MONEY TRANSMITTERS ACT

With a basic understanding in place of some of the key technologies creating problems for or highlighting existing problems of the Idaho Act, this article now focuses on the provisions of the current Idaho Act implicated by such problems.

### A. Relevant Provisions of the Idaho Money Transmitters Act

#### i. Key Definitions in the Current Act

Several key definitions in the Idaho Money Transmitters Act establish the scope of the Act and provide insight into its drafters' conceptualizations regarding money transmitters and money transmission. Understanding each of these definitions is necessary to understanding the problems with the current Act.

The most problematic definition is how the Idaho Act defines "money transmission." This definition sets the outer bounds of the Act's applicability.<sup>98</sup> The definition has three components: activities, locations, and means.<sup>99</sup> The activities covered are "the sale or issuance of payments systems,"<sup>100</sup> "engaging in the business of receiving money for transmission," and "the business of transmitting money."<sup>101</sup> The locations covered include any origination point within the United States and any destination point in the world.<sup>102</sup> Finally, the definition states that it includes "any and all means."<sup>103</sup> The activities component has revealed itself to be the most problematic in recent years due to the use of the word "money." While the term

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96. See IDAHO CODE §§ 26-2901–2928 (2018) (no exception for incidental transmitters).

97. Brad Stone, *The \$99 Billion Idea: How Uber and Airbnb Fought City Hall, Won Over the People, Outlasted Rivals, and Figured Out the Sharing Economy*, BLOOMBERG (Jan. 26, 2017), <https://www.bloomberg.com/features/2017-uber-airbnb-99-billion-idea/> ("Airbnb and Uber . . . are among the fastest-growing startups in history by sales, market value, and number of employees.").

98. See IDAHO CODE § 26-2903(1) (2018) (only entities engaged in the business of money transmission or engaged in the sale or issuance of prepaid payment mechanisms are required to be licensed under the Act).

99. See IDAHO CODE § 26-2902(11) (2018).

100. *Id.* Payment instruments means "any check, draft, money order, traveler's check or other instrument or written order for the transmission of payment of money, sold or issued . . . [but] does not include any credit card voucher, any letter of credit or any instrument which is redeemable by the issuer in goods or services." IDAHO CODE § 26-2902(13) (2018).

101. IDAHO CODE § 26-2902(11) (2018).

102. *Id.*

103. *Id.*

“money” is not defined in the Act,<sup>104</sup> the Idaho Department of Finance considers only fiat currencies and not virtual currencies to be “money.”<sup>105</sup>

Another key definition limiting the scope of the Idaho Act is the definition of “person,” which delimits the entities that the Act considers.<sup>106</sup> The Act is currently limited in its applicability to traditional entities, such as individuals and partnerships.<sup>107</sup> The Act’s constrained entity conceptualization embodied in its current definition of “person” frames all other aspects of the Act, such as who or what controls the transmitter and who or what is performing the executive functions of the transmitter.<sup>108</sup>

## ii. License Requirements

The current Act requires all entities engaged in an activity covered by the Idaho Act in Idaho to obtain an Idaho license.<sup>109</sup> This may be done through the use of a common license application form filed through the Nationwide Multistate Licensing System & Registry (NMLS), which is accepted by multiple states, or by applying directly to the Idaho Department of Treasury.<sup>110</sup>

The qualifications required to obtain and maintain a license are generally focused on ensuring the solvency and prudent business practices of applicants to protect consumers who might use their services.<sup>111</sup> These qualifications attempt to achieve this goal by imposing minimum net worth and security requirements as direct financial collateral securing the customer funds with which they may be entrusted.<sup>112</sup> Additionally, if the entity issues payment instruments, it must “possess permissible investments having an aggregate market value . . . of not less than the

104. See generally IDAHO CODE §§ 26-2901–2928 (2018).

105. See, e.g., Letter from Jeff Flora, Fin. Exam’r, Idaho Dep’t of Fin., on BitCoin Exchange Licensing Requirement (Oct. 11, 2017) [hereinafter Dep’t Fin. October 2017 Letter], <https://www.finance.idaho.gov/MoneyTransmitter/Documents/NAOP/Digital%20Currency/2017-10-11.pdf>; E-mail from Coleen Hodson, Supervising Investigator, Idaho Dep’t of Fin., on Licensing of Virtual Currency Exchanger (Nov. 08, 2017, 13:28 MST) [hereinafter Dep’t Fin. November 2017 Letter], (<https://www.finance.idaho.gov/MoneyTransmitter/Documents/NAOP/Digital%20Currency/2017-11-08.pdf>).

106. See IDAHO CODE § 26-2902(15) (2018).

107. See *id.* (defining “person”); IDAHO CODE § 26-2903(1) (2018) (licensing requirement is limited only to persons engaged in covered activities).

108. See, e.g., IDAHO CODE § 26-2902(4) (2018) (the only entity the act recognizes that can control a licensee is a “person”); IDAHO CODE § 26-2902(7) (2018) (executive officers are those with the title “and any other person who performs similar functions” (emphasis added)).

109. IDAHO CODE § 26-2903 (2018). However, the Act carves out exclusions for three types of entities: state and federal government entities, banks, and authorized representatives of licensees. IDAHO CODE § 26-2904 (2018).

110. See *States Expand Use of NMLS to New Industries*, NATIONWIDE MULTISTATE LICENSING SYS. & REGISTRY (last updated Jan. 1, 2018), <https://nationwidelicensingsystem.org/searchcenter/pages/results.aspx?k=expansion%20tracking> (spreadsheet identifying the States that accept the common license applications through the NMLS, including Idaho); *Idaho Money Transmitter Section*, *supra* note 14 (providing a license application form for money transmitters not wishing to use the NMLS system).

111. See, e.g., IDAHO CODE § 26-2910(1) (2018) (the applicant’s “financial condition and responsibility, financial and business experience, character and general fitness” are investigated).

112. IDAHO CODE § 26-2905(1) (2018) (minimum net worth requirements for licensees); IDAHO CODE § 26-2908(1) (2018) (security device requirement of at least \$10,000).

aggregate face amount of all outstanding payment instruments issued or sold by the licensee in the United States.”<sup>113</sup> Furthermore, an investigation of the entity itself is performed which, if so desired by the Department of Treasury, may be an on-site investigation “the actual cost of which shall be borne by the applicant.”<sup>114</sup>

Once a license has been granted, the licensee must comply with annual and event-based reporting requirements to maintain the license. The primary reporting requirement is an annual report to the Idaho Department of Treasury containing, among other information, extensive financial information.<sup>115</sup> Furthermore, upon the occurrence of certain events, such as revocation of a transmitter license by another state or an officer of the licensee being convicted of a felony, the event must be reported to the Idaho Department of Treasury within fifteen days.<sup>116</sup> Failing to comply with these reporting or financial requirements or being found as conducting “business in an unsafe or unsound manner” can lead to the suspension or revocation of an entity’s license.<sup>117</sup>

A licensee utilizing authorized representatives must meet more stringent qualifications to obtain a license.<sup>118</sup> In addition to the base net worth requirements, the licensee must maintain an additional \$25,000 in net worth for each authorized representative.<sup>119</sup> Further, each authorized agent must be authorized by express written contract with the licensee.<sup>120</sup> Moreover, the licensee must ensure that the authorized representative complies with certain reporting,<sup>121</sup> further adding to the cost of using authorized representatives.

The sum of these requirements is that they impose a high barrier to entry for those seeking to provide money transmission services or issue payment instruments in Idaho—a barrier that is not necessarily correlated to the actual risk of loss to consumers. The current Idaho Act sacrifices innovation for security. While such a sacrifice may seem to create only a marginal burden on innovation at the micro level, a macro level examination of the Act in light of the larger regulatory landscape reveals the significant regulatory burden to which the Act contributes.

#### B. Entities Covered by the Current Act

While the express wording of the Idaho Act would seem to make it clear who must be licensed, the Act is both more and less inclusive than it first appears. The traditional money transmitters, such as money remitters and money order issuers, easily fall within the scope of the Act.<sup>122</sup> Furthermore, since the definition of

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113. IDAHO CODE § 26-2906 (2018). “Permissible investments” is a defined term in the Idaho Act and includes, among other things, cash, investments securities which are obligations of the United States, and stocks. IDAHO CODE § 26-2902(14) (2018).

114. IDAHO CODE § 26-2910(1) (2018).

115. IDAHO CODE § 26-2911(1) (2018).

116. IDAHO CODE § 26-2912 (2018).

117. IDAHO CODE § 26-2917(4) (2018).

118. See IDAHO CODE § 26-2918 (2018); IDAHO CODE § 26-2905(1) (2018).

119. IDAHO CODE § 26-2905(1) (2018).

120. IDAHO CODE § 26-2918 (2018).

121. IDAHO CODE § 26-2919(5) (2018).

122. *Idaho Money Transmitters Section*, *supra* note 14.

“money transmission” explicitly includes the sale of payment instruments,<sup>123</sup> issuers of stored value cards like prepaid gift cards are included.<sup>124</sup> The Act has also been extended to apply to “virtual currency exchangers,” which are entities that act as an intermediary to exchange virtual currencies for legal tender.<sup>125</sup> Moreover, the current Act has been found to apply to payment processors and payroll processors, even when they are only paying out virtual currency.<sup>126</sup>

However, the Idaho Department of Treasury has clearly stated that only exchangers of virtual currencies are regulated.<sup>127</sup> Those who deal exclusively in virtual currency or who exchange virtual currency from their own supply for fiat currencies do not require a license under the current Act.<sup>128</sup> It is only when, by design or in practice, an entity acts like an intermediary between two other parties to exchange fiat legal tender for virtual currency that the entity will be required to obtain a license.<sup>129</sup> The Idaho Department of Treasury has indicated that this is likely to occur in practice when an entity buys virtual currency on the open market and sells it for legal tender at a sufficient volume to effectively be acting like an intermediary between the person from whom they bought the virtual currency and the person to whom they sold it, even though those two parties were not otherwise connected nor had any intention of being so.<sup>130</sup> This position is somewhat incongruent with the Department of Treasury’s stance on payroll processors who receive fiat currency and pay employees virtual currency from their own inventory.<sup>131</sup> The Department has indicated that, even in this scenario, the payroll processor needs to be licensed under the Act.<sup>132</sup>

In addition, incidental transmitters, like bill pay aggregators, potentially fall within the scope of the Act.<sup>133</sup> While these types of entities would seem to clearly fall within the payment processors category, one opinion letter from the Idaho Department of Treasury indicates that certain types of bill pay aggregators may not be

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123. IDAHO CODE § 26-2902(11) (2018).

124. *Idaho Money Transmitters Section*, *supra* note 14.

125. *Id.*

126. *Id.*; see Dep’t Fin. November 2017 Letter, *supra* note 105. The inclusion of payment processors runs counter to FinCEN who excludes payment processors, including online marketplaces. See FINCEN, APPLICATION OF MONEY SERVICES BUSINESS REGULATIONS TO A COMPANY ACTING AS AN INDEPENDENT SALES ORGANIZATION AND PAYMENT PROCESSOR, FIN-2014-R009 (Aug. 27, 2014), <https://perma.cc/B59W-QJE3> [hereinafter FINCEN RULING 2014-R009] (exclusion of payment processors); FINCEN, FINCEN RULING 2003-8 – DEFINITION OF A MONEY TRANSMITTER (MERCHANT PAYMENT PROCESSOR) (Nov. 19, 2003), <https://perma.cc/5ZDK-6TQL> [hereinafter FINCEN RULING 2003-8] (extending payment process exception to online marketplaces). Further, Idaho has failed to include an agent-of-the-payee exemption. See IDAHO CODE §§ 26-2901–2928 (2018); *Fatal Fragments*, *supra* note 4, at 129.

127. Dep’t Fin. November 2017 Letter, *supra* note 105.

128. *Id.*

129. See *id.*; Dep’t Fin. October 2017 Letter, *supra* note 105.

130. See Dep’t Fin. October 2017 Letter, *supra* note 105.

131. *Id.* (stating that the Idaho Department of Treasury requires all payroll processors to obtain a license when responding to an inquiry from an entity that was planning on paying out virtual currencies in its payroll processing capacity, potentially from its own inventory).

132. See *id.*

133. See *id.* These are entities that collect together all of a person’s bills, collects money from that person, and uses that money to pay the bills on the person’s behalf.

required to obtain a license.<sup>134</sup> The Department stated in a letter on January 28, 2016 that credit counselors licensed under the Idaho Collection Agency Act who collected money from their clients and used it to make remittances on the client's behalf to the client's creditors, would not need to obtain a money transmitter license.<sup>135</sup> The Department limited this exception to those remittances made on behalf of clients that were "solely incidental to their credit counselor activities."<sup>136</sup> However, this leniency runs directly counter to the Department's prior stance on the issue.<sup>137</sup>

## VI. ADVANTAGEOUS PROVISIONS IN THE LAWS OF OTHER STATES, THE UNIFORM ACT, AND FEDERAL LAW

### A. Advantageous Money Transmitter Regulation Provisions in Other States

Many states have a similar set of basic provisions in their money transmitter regulations.<sup>138</sup> The provisions that Idaho has in common with many other states include the exclusion of "state and federally chartered depository financial institutions" from regulation,<sup>139</sup> no reciprocity with licensing requirements,<sup>140</sup> bond requirements,<sup>141</sup> and minimum valuations for licensees.<sup>142</sup>

However, other states have seemingly advantageous provisions that are missing from the Idaho Act. One such advantageous provision used by several states is an agent-of-the-payee exemption.<sup>143</sup> This exemption is "meant to exempt businesses that adequately mitigate . . . legislative concerns."<sup>144</sup> It exempts "transaction[s] in which the recipient of the money or other monetary value is an agent of the payee pursuant to a preexisting written contract and delivery of the money or other monetary value to the agent satisfies the payor's obligation to the payee."<sup>145</sup> The transmitters in such transactions present a very low risk to consumers using

134. See Letter from Jim Burns, Sec. Bureau Chief, Idaho Dep't of Fin., on Licensing Requirements for Entities with Licenses Under the Idaho Collection Agency Act (Jan. 28, 2016) (<https://www.finance.idaho.gov/MoneyTransmitter/Documents/NAOP/Licensing%20No-Action/2016-01-28.pdf>) [hereinafter Dep't Fin. January 2016 Letter].

135. *Id.*

136. *Id.*

137. See Letter from James A. Burns, Investigations Chief, Idaho Dep't of Fin., on Licensing Requirements for Entities with Licenses Under the Idaho Collection Agency Act (May 2, 2011) (<https://www.finance.idaho.gov/MoneyTransmitter/Documents/NAOP/Misc/2011-05-02.pdf>) [hereinafter Dep't Fin. May 2011 Letter] (holding that entities licensed under the Idaho Collection Agency Act must obtain a license under the Idaho Money Transmitters Act).

138. See generally 50-STATE SURVEY, *supra* note 27.

139. Judith Rinearson & Kristine M. Andreassen, *Developments in the Regulation of Prepaid Payment Products Under State Money Transmitter Licensing Laws*, 65 BUS. L. 271, 272 (2009); see IDAHO CODE § 26-2904 (2018).

140. See 50-STATE SURVEY, *supra* note 27 (the vast majority of states do not have any reciprocity); IDAHO CODE §§ 26-2901–2928 (2018) (no reciprocity exemption to licensing requirement).

141. See 50-STATE SURVEY, *supra* note 27 (almost every state that regulates money transmitters has a bond requirement).

142. See *id.*

143. *Fatal Fragments*, *supra* note 4, at 129.

144. *Id.*

145. CAL. FIN. CODE § 2010(l) (West 2018); see also WASH. REV. CODE ANN. § 19.230.020(9)(c) (West 2018).

their services because a consumer's obligation to pay is discharged when the consumer provides the money to the transmitter.<sup>146</sup> Such transmitters do not implicate the consumer protection policies underlying the Idaho Act because licensing them does not further protect the consumer.

Another provision used by other states and missing from the Idaho Act is the exclusion of certain payment processors,<sup>147</sup> who are also excluded under federal regulation when certain criteria are met.<sup>148</sup> Certain types of payment processors pose a low risk with respect to both consumers and anti-money laundering concerns. This is especially true for those whose payment processing activities are incidental to their core business, such as AirBnB and Amazon, because such entities are generally transmitting money between "BSA-approved institutions over well-regulated clearing and settlement networks, arguably mitigating anti-money laundering and safety-and-soundness concerns."<sup>149</sup> Moreover, where these entities explicitly adopt the obligation of the consumer to pay their creditors upon accepting the consumer's funds, the risk is decreased further.

An additional provision contained in many other states' money transmitter regulations is one allowing for the modification of monetary licensing requirements.<sup>150</sup> For example, the state of Washington allows the director of its Department of Treasury to determine the net worth requirements for money transmitters, with a statutory minimum of \$10,000 and a statutory maximum of \$3 million.<sup>151</sup> This provision allows for some of the monetary licensing requirements to be tied to the risk of loss to consumers that a given entity represents. Tying the licensing requirements to risk helps alleviate the regulatory burden on entities whose regulation under the default rules would not advance the purposes of imposing such regulation—protecting citizens from financial loss due to fraudulent or from unsound business practices in the state of Idaho.

As another example, Texas has enacted two similar requirement modification provisions pertaining to net worth and permissible investment requirements.<sup>152</sup> Under Texas Financial Code Section 151.307(b), the Texas Banking Commissioner has the power to modify the net worth requirement for an applicant based on the following ten factors:

- (1) the nature and volume of the projected or established business;
- (2) the number of locations at or through which money transmission is or will be conducted;
- (3) the amount, nature, quality, and liquidity of its assets;
- (4) the amount and nature of its liabilities;
- (5) the history of its operations and

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146. See, e.g., CAL. FIN. CODE § 2010(l) (West 2018).

147. See, e.g., WASH. REV. CODE ANN. § 19.230.020(9)(a) (West 2018).

148. See FINCEN RULING 2014-R009, *supra* note 126.

149. *Fatal Fragments*, *supra* note 4, at 128.

150. See, e.g., WASH. REV. CODE ANN. § 19.230.060 (West 2018); TEX. FIN. CODE ANN. § 151.307 (West 2018).

151. WASH. REV. CODE ANN. § 19.230.060 (West 2018).

152. TEX. FIN. CODE ANN. § 151.307(b) (West 2018) (related to net worth requirement); TEX. FIN. CODE ANN. § 151.309(a) (West 2018) (related to permissible investment requirement).

prospects for earning and retaining income; (6) the quality of its operations; (7) the quality of its management; (8) the nature and quality of its principals and persons in control; (9) the history of its compliance with applicable state and federal law; and (10) any other factor the commissioner considers relevant.<sup>153</sup>

Under Texas Financial Code Section 151.309(a), the value of the permissible investments required to be maintained by a licensee depends on the net worth of the licensee.<sup>154</sup> If the licensee's net worth is less than \$5 million, then the aggregate market value of the licensee's permissible investments must be at least equal to "the aggregate face amount of the license holder's average outstanding money transmission obligations."<sup>155</sup> If the licensee's net worth is at least \$5 million, then the aggregate market value of the licensee's permissible investments need only be one half of the aggregate face amount of the licensee's average outstanding money transmission obligations.<sup>156</sup> Both provisions are an attempt to tie the regulatory burden to the risk of loss to consumers posed by a given transmitter. The net worth modification provision attempts to do this by identifying concrete factors for determining the risk posed by a given entity. The permissible investment requirement provision attempts to do this by reducing one monetary requirement when another mean of repaying consumers in the event of loss is available. Both provisions manifest the Texas legislature's recognition that the purposes underlying money transmitter regulation may be better served when the regulatory burden can be modified based on a licensee's unique circumstances.

#### B. Advantageous Provisions of the Uniform Money Services Act

The Uniform Money Services Act ("UMSA") represents one effort to provide a cohesive framework for the regulation of money transmitters and other non-depository providers of financial services.<sup>157</sup> Ten states and two U.S. territories have enacted versions of the UMSA.<sup>158</sup> The UMSA has four notable advantageous provisions related to the regulation of money transmitters that are worth discussing: a reciprocity provision,<sup>159</sup> a more expansive definition of money transmission,<sup>160</sup> a provision allowing for the modification of license monetary requirements,<sup>161</sup> and separate licensing provisions for different money service businesses.<sup>162</sup>

153. TEX. FIN. CODE ANN. §151.307(b) (West 2018).

154. TEX. FIN. CODE ANN. §151.309(a) (West 2018).

155. *Id.*

156. *Id.*

157. UNIF. LAW COMM'N, PURPOSE AND SCOPE OF THE PROPOSED ACT 6 (1997) (though the act is focused on the prevention of money laundering, uniformity in licensing is the means by which this goal is sought).

158. See *Money Services Act*, <https://www.uniformlaws.org/committees/community-home?CommunityKey=cf8b649a-114c-4bc9-8937-c4ee17148a1b> (last visited Mar. 24, 2019) (map indicating the states and territories that have enacted the Uniform Act).

159. UNIF. MONEY SERVS. ACT § 201(a)(1) (UNIF. LAW COMM'N 2004).

160. UNIF. MONEY SERVS. ACT § 102(14) (UNIF. LAW COMM'N 2004).

161. UNIF. MONEY SERVS. ACT § 204(f) (UNIF. LAW COMM'N 2004).

162. See UNIF. MONEY SERVS. ACT § 201 (UNIF. LAW COMM'N 2004) (money transmitters); UNIF. MONEY SERVS. ACT § 301 (UNIF. LAW COMM'N 2004) (check cashers); UNIF. MONEY SERVS. ACT § 401 (UNIF. LAW COMM'N 2004) (currency exchangers).



The most notable of these provisions is the licensing reciprocity provision. This provision allows an entity licensed to operate as a money transmitter in one state to operate in another state without obtaining another license.<sup>163</sup> Under the UMSA, the transmitter must register with the state,<sup>164</sup> the state will conduct an investigation into the soundness of the transmitter,<sup>165</sup> and the transmitter must comply with reporting and permissible investment requirements of the state as if it had been licensed by the state.<sup>166</sup> This reciprocity scheme simplifies the process and reduces the cost and regulatory burden for a money transmitter expanding its service offerings to other states.<sup>167</sup> The scheme also serves the consumer protection purposes underlying such regulation in two ways. First, these money transmitters are still investigated and tracked by the relevant state agency through the initial investigation and continuous reporting requirements.<sup>168</sup> Second, by lowering the burden of operating legally within the state, entities that may have otherwise not have applied for a license may be more inclined to do so, increasing the visibility of such entities to regulatory authorities.

The next most notable provision is the UMSA's definition of "money transmission,"<sup>169</sup> which is both more and less inclusive than the definition found in the Idaho Act. The definition is more inclusive because "money transmission" is defined to include transmission of "monetary value."<sup>170</sup> The definition is less inclusive since it explicitly excludes "the provision solely of delivery, online or telecommunications services, or network access" and "clearing agents."<sup>171</sup>

The inclusion of transmission of "monetary value" in the UMSA's definition of "money transmission" allows the UMSA to cover transmitters of non-traditional mediums of exchange, including mediums like virtual currency.<sup>172</sup> "Monetary value" is a flexible term meant to allow the UMSA to encompass new and alternative mediums of exchange.<sup>173</sup> The definition is meant to include only those mediums that are "accepted by a community[] larger than the two parties to the exchange."<sup>174</sup> Under this definition, regulators have the discretion to determine when a medium is of sufficient size to fall within the scope of the regulations.<sup>175</sup> The flexibility of the

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163. See UNIF. MONEY SERVS. ACT § 201(a)(1) (UNIF. LAW COMM'N 2004); UNIF. MONEY SERVS. ACT § 203 (UNIF. LAW COMM'N 2004).

164. UNIF. MONEY SERVS. ACT § 203(a)(2) (UNIF. LAW COMM'N 2004).

165. UNIF. MONEY SERVS. ACT § 203(b) (UNIF. LAW COMM'N 2004).

166. UNIF. MONEY SERVS. ACT § 203(d) (UNIF. LAW COMM'N 2004); see UNIF. MONEY SERVS. ACT § 701(a) (UNIF. LAW COMM'N 2004) (licensee must have "permissible investments that have a market value . . . of not less than the aggregate amount of all its outstanding payment instruments and stored value obligations . . . and money transmitted from all states").

167. The principal cost reduction comes from the removal of redundant and non-overlapping security requirements.

168. UNIF. MONEY SERVS. ACT § 203(d) (UNIF. LAW COMM'N 2004).

169. UNIF. MONEY SERVS. ACT § 102(14) (UNIF. LAW COMM'N 2004).

170. *Id.*

171. *Id.*; UNIF. MONEY SERVS. ACT § 102 cmt. 9 (UNIF. LAW COMM'N 2004).

172. See UNIF. MONEY SERVS. ACT § 102(11) (UNIF. LAW COMM'N 2004) (defining "Monetary value").

173. See UNIF. MONEY SERVS. ACT § 102 cmt. 10 (UNIF. LAW COMM'N 2004).

174. *Id.*

175. *Id.*

definition allows regulators to respond to non-traditional mediums of exchange without needing to amend the law or stretch an existing definition beyond its intended scope. However, this flexibility can lead to differences in enforcement of such regulations. For example, Texas, which has enacted a modified version of the UMSA, does not regulate the transmission of virtual currencies,<sup>176</sup> although certain virtual currencies, such as BitCoin, almost certainly fall within the definition of “monetary value.”<sup>177</sup>

Comment 9 to Section 102 of the Uniform Act explains that “entities that simply transfer money between parties as clearing agents . . . fall outside the scope [of the statute];” this section therefore potentially creates an implicit exemption for certain incidental transmitters.<sup>178</sup> The comment contrasts “[i]nternet payment services that hold customer’s funds or monetary value for their own account” with such services that “serve simply as a clearing agent.”<sup>179</sup> The former are included within the definition of money transmission while the latter are not.<sup>180</sup> This exclusion appears to create an inherent exemption for incidental transmitters like online marketplaces that merely serve as a clearing agent to ensure payments are made.

### C. Federal Regulation of Money Transmitters

Federal regulation of money transmitters comes principally from the Bank Secrecy Act (BSA), as enforced by the Financial Crimes Enforcement Network (FinCEN), and is principally focused on the discovery and prevention of money laundering and fraud.<sup>181</sup> The BSA defines a money transmitter as “[a] person that provides money transmission services.”<sup>182</sup> The BSA uses a broad definition of “money transmission services,” defining it as “the acceptance of currency, funds, or other value that substitutes for currency from one person and the transmission . . . to another location or person by any means.”<sup>183</sup> This broad definition, like the one used by the UMSA, allows for transmitters of non-traditional stores of value, such as virtual currencies, to be included within the BSA.<sup>184</sup> FinCEN has indicated that it will treat “convertible” virtual currency like fiat currency for the purposes of defining money transmission.<sup>185</sup>

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176. See Charles G. Cooper, *Regulatory Treatment of Virtual Currencies Under the Texas Money Services Act* (April 3, 2014), <https://www.dob.texas.gov/public/uploads/files/consumer-information/sm1037.pdf>.

177. The Uniform Law Commission has issued a separate act for the regulation of virtual currencies, but the UMSA is still applicable. See *generally* UNIF. REG. OF VIRTUAL-CURRENCY BUS. ACT (UNIF. LAW COMM’N 2017).

178. See UNIF. MONEY SERVS. ACT § 102 cmt. 9 (UNIF. LAW COMM’N 2004).

179. *Id.*

180. *Id.*

181. See *Fatal Fragments*, *supra* note 4, at 113–15; 31 C.F.R. § 1010.100(ff)(5)(i)(A) (2018).

182. 31 C.F.R. § 1010.100(ff)(5)(i)(A) (2018).

183. *Id.*

184. See *Fatal Fragments*, *supra* note 4, at 122.

185. *Application of FinCEN’s Regulations to Persons Administering, Exchanging, or Using Virtual Currencies*, DEP’T TREASURY FIN. CRIMES ENF’T NETWORK (Mar. 18, 2013), <https://www.fincen.gov/sites/default/files/shared/FIN-2013-G001.pdf> [hereinafter *FinCEN Ruling 2013-G001*]. “Convertible” virtual is defined as virtual currency that “either has an equivalent value in real currency, or acts as a substitute for real currency.” *Id.*

Several exemptions exist at the federal level that limit the scope of federally regulated entities.<sup>186</sup> Two noteworthy exemptions are the exemption for certain payment processors and the exemption for entities whose money transmission activities are “integral to the provision of the Company’s service” but are not the service itself.<sup>187</sup> These provisions are noteworthy because they exempt entities that present a low risk of engaging in money laundering.<sup>188</sup>

In addition to the regulation under the BSA, the Consumer Financial Protection Bureau (“CFPB”) has regulated certain prepaid payment mechanisms.<sup>189</sup> These regulations affect certain money transmitters, like Venmo, that provide accounts that store users’ money within their services in addition to issuers of more traditional prepaid payment mechanisms.<sup>190</sup> These regulations are focused principally on protecting the consumers who use such services.<sup>191</sup>

Furthermore, federal courts have determined that virtual currencies, like Bitcoin, are “money” under various federal statutes.<sup>192</sup>

## VII. PROBLEMS WITH THE CURRENT IDAHO ACT AND PROPOSED SOLUTIONS

Now that the relevant technology, statutory provisions, and policies have been explained, the next step is to examine the problems arising from the interaction of these pieces. Based on these problems, this article then suggests solutions to mitigate or resolve them.

### A. Problems with the Idaho’s Money Transmitters Act

The issues with Idaho’s Money Transmitter Act can be attributed to three primary failings: (1) its failure to recognize any meaningful form of licensing reciprocity; (2) its failure to tie the degree of regulation to the degree of risk of loss to the consumer; and (3) its failure to be sufficiently flexible in its applicability. These fail-

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186. See *Fatal Fragments*, *supra* note 4, at 114.

187. See FINCEN RULING 2014-R009, *supra* note 126 (exclusion of payment processors). 31 C.F.R. § 1010.100(ff)(5)(ii)(B) (2018) (excluding payment processors from definition of money transmission); 31 C.F.R. § 1010.100(ff)(5)(ii)(F) (2018) (excluding those who transmit funds only integral to provision of the entity’s services).

188. *Fatal Fragments*, *supra* note 4, at 114.

189. See generally CONSUMER FIN. PROT. BUREAU, PREPAID RULE: SMALL ENTITY COMPLIANCE GUIDE (2017), [https://s3.amazonaws.com/files.consumerfinance.gov/f/documents/201706\\_cfpb\\_prepaid-small-entity-compliance-guide.pdf](https://s3.amazonaws.com/files.consumerfinance.gov/f/documents/201706_cfpb_prepaid-small-entity-compliance-guide.pdf).

190. See *id.*; Gillian B. White, *The New Rules of Digital Cash*, ATLANTIC (Oct. 5, 2016), <https://www.theatlantic.com/business/archive/2016/10/cfpb-prepaid-venmo/503000/>.

191. Gillian B. White, *The New Rules of Digital Cash*, ATLANTIC (Oct. 5, 2016), <https://www.theatlantic.com/business/archive/2016/10/cfpb-prepaid-venmo/503000/>.

192. SEC v. Shavers, No. 4:13-CV-416, 2014 U.S. Dist. LEXIS 194382, at \*21 (E.D. Tex. Aug. 26, 2014). Federal courts have found that such currencies are money within the context of operating an unlicensed money transmission business. See *United States v. Faiella*, 39 F. Supp. 3d 544 (S.D.N.Y. 2014); *United States v. Mansy*, No. 2:15-cr-198-GZS, 2017 U.S. Dist. LEXIS 71786 (D. Me. May 11, 2017) (adopting the reasoning set forth in *Faiella* to find that using virtual currency in the context of a money transmitting business was transmission of “money”).

ures pose the dual problems of stifling innovation and failing to keep up with innovative actors and activities involved in money transmission. The Idaho Act stifles innovation principally through its failures to allow licensing reciprocity and to tie the degree of regulation to the degree of risk of consumer loss. Further, the Idaho Act's rapidly aging conceptualizations are the result of the Act not being updated, in combination with a lack of flexibility built into the Act,<sup>193</sup> the effects of which are exacerbated by the exponential nature of technological development.<sup>194</sup>

The first of these failures, the lack of any licensing reciprocity,<sup>195</sup> contributes to the Balkanized regulatory morass that is the national regulatory landscape governing money transmitters. Idaho is not an outlier with respect to this failure; very few states offer any reciprocity.<sup>196</sup> However, the Idaho Act's failure to include any reciprocity provisions contributes to the problem. Such Balkanization is problematic because most states have their own bond requirements, application information, and entity investigation requirements for money transmitters.<sup>197</sup> The cost and time barriers created by these overlapping requirements can quickly exceed the capacity of a start-up company seeking to provide money transmissions services in more than a few states.<sup>198</sup> For example, if a company based in Idaho wanted to provide money transmission services to Idaho and each state adjoining Idaho, the minimum security amount would be \$115,000.<sup>199</sup> If that company wanted to expand to California, it would be required to pay an additional \$250,000 surety bond or security.<sup>200</sup> Any transmitter that does not already have a robust operation generating strong revenue or significant capital investment would find such costs prohibitive. This redundancy in requirements is an inefficient means of protecting consumers, ultimately harming them by preventing innovative entities from reaching the market and encouraging new transmitters to evade regulation until they are large

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193. The Director has some flexibility to waive requirements, such as those relating to permissible investments and what information is required on the license application, but the Idaho Act is bound too tightly by its statutory definitions and interpretation for such flexibility to be meaningful. IDAHO CODE § 26-2906 (2018) (director can waive permissible investment requirements in certain cases); IDAHO CODE § 26-2907(4) (2018) (power to waive requirement for information on application). *But see* IDAHO CODE § 26-2902(11) (2018) (definition of "money transmission" narrow relative to the Uniform Act and the definition used for federal regulation); Dep't Fin. October 2017 Letter, *supra* note 105 (treating virtual currency as not within the scope of the Idaho Act).

194. See Mohammed Sanduk, *Is the Technology a New Way of Thinking?*, 38 J. TECH. STUD. 105, 110 (2012).

195. IDAHO CODE §§ 26-2903–2928 (2018) (not reciprocity exceptions); *see e.g.*, Letter from James A. Burn, Investigations Chief, Idaho Dep't of Fin., on Licensing of Entities Engaged in Money Transmission with No Physical Presence in Idaho (Apr. 18, 2011) [hereinafter Dep't Fin. April 2011 Letter], <http://www.finance.idaho.gov/MoneyTransmitter/Documents/NAOP/Misc/2011-04-18.pdf>; Letter from James A. Burn, Investigations Chief, Idaho Dep't of Fin., on Licensing of Entities who Accept Fund Transfer Orders from Idaho Residents via the Internet (Dec. 15, 2010) [hereinafter Dep't Fin. December 2010 Letter], <http://www.finance.idaho.gov/MoneyTransmitter/Documents/NAOP/Misc/2010-12-15.pdf>.

196. See 50-STATE SURVEY, *supra* note 27, at 4, 140 (noting that only Alaska and the U.S. Virgin Islands have licensing reciprocity).

197. See generally *id.*

198. *Fatal Fragments*, *supra* note 4, at 131–32.

199. See IDAHO CODE § 26-2908 (2018) (minimum security bond amount is \$10,000); 50-STATE SURVEY, *supra* note 27, at 74, 100, 116, 126, 136 (noting the various minimum-security amounts for NV, OR, UT, WA, and WY. Montana does not regulate money transmitters).

200. 50-STATE SURVEY, *supra* note 27, at 15.

enough to afford the costs of obtaining a license.<sup>201</sup> Idaho has seen examples of such evasion already by transmitters who were licensed in other states.<sup>202</sup> In *State of Idaho v. Quickdiner*, a money transmission business incorporated in Illinois and licensed as a money transmitter in six states agreed to pay a \$5,000 fine for engaging in money transmission in Idaho without a license.<sup>203</sup> The fact that an entity licensed in six other states failed to comply with Idaho's licensing requirements is indicative of the problematic regulatory landscape. While this issue is not isolated to Idaho, the Idaho Act contributes to the problem. The rise of the internet, which has enabled companies to offer their services nationally from the outset, has highlighted this reciprocity issue, but legislatures have been slow to respond.

The second major failure to the current Idaho Act is its failure to adequately tie its degree of regulation to the degree of risk of loss to consumers presented by a given transmitter. This lack of proportionate regulation prevents a regulatory response to new technologies' ability to greatly decrease the risk of loss to consumers,<sup>204</sup> thereby diminishing the benefits realized from these technologies. The monetary and reporting requirements in the current Idaho Act are the source of this failing. While the permissible investment requirement may be waived when "the dollar volume of a licensee's outstanding payment instruments does not exceed the bond or other security devices posted by the licensee,"<sup>205</sup> currently the only other modification to the monetary requirements that could be considered as a proxy for risk of consumer loss is the number of locations or authorized representatives of the licensee.<sup>206</sup> While this may have been a sufficient proxy measurement for such risk when the number and dollar value of transactions a particular transmitter could perform was limited by the number of physical locations, the rise of the internet has rendered this proxy measurement obsolete. A transmitter is no longer limited by physical location and may offer its services to every citizen in Idaho without being physically present in the state at all. Moreover, the reporting requirement has no option for modification, imposing its costly requirements on entities without any attempt to match its regulatory burden to the risk presented by an entity.<sup>207</sup> These requirements together create a relatively high barrier to entry in a state with a relatively small population.<sup>208</sup> Further, the effectiveness of reporting, surety bonds,

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201. *Fatal Fragments*, *supra* note 4, at 132–36.

202. See Agreement and Order 1-3, *State of Idaho v. Quickdiner*, No. 2005-12-1 (Idaho Dep't of Treasury May 20, 2005).

203. See *id.*

204. See generally Kamil Gregor, *IBM Wants to Make 2017 the Year of Blockchain Enterprise Deployment* IDC 3–4, 6 (April 2017), [https://www.ibm.com/blockchain/in-en/assets/IDC\\_Report\\_\\_IBM\\_wants\\_to\\_make\\_2017\\_the\\_year\\_of\\_BlockChain\\_Enterprise\\_\\_Deployment.pdf](https://www.ibm.com/blockchain/in-en/assets/IDC_Report__IBM_wants_to_make_2017_the_year_of_BlockChain_Enterprise__Deployment.pdf) (discussing IBM's use of blockchain technology in the resolution of financing disputes and providing the technology to the Japan Exchange Group to reduce risk, costs, and trade settlement time in security trading).

205. IDAHO CODE § 26-2906 (2018).

206. See IDAHO CODE § 26-2905 (2018); IDAHO CODE § 26-2908 (2018).

207. See IDAHO CODE § 26-2911 (2018).

208. See UNITED STATES CENSUS, ANNUAL ESTIMATES OF THE RESIDENT POPULATION FOR THE UNITED STATES, REGIONS, STATES, AND PUERTO RICO APRIL 1, 2010 TO JULY 1, 2017 (2017), <https://www2.census.gov/programs-surveys/popest/tables/2010-2017/state/totals/nst-est2017-01.xlsx> (listing Idaho as the 39th most populous state as of 2017).

and net worth requirements as consumer protection measures is debatable in the current scheme.<sup>209</sup>

The third major failing of the current Idaho Act, its lack of flexibility, has resulted in narrow conceptualizations of the actors and activities involved in money transmission. These conceptualizations are rapidly antiquating with the exponential progression of technology. The current Act's conceptualization of the actors involved in money transmission that should be regulated has become both over and under-inclusive. Further, the current Act's conceptualization of what constitutes money transmission grows more under-inclusive as alternative mediums of exchange increase in importance. Compared to the first two failings, which err on the side of overprotection of the consumer, the net result of this third failing is to impede the policy of consumer protection underlying the Idaho Act.

The Idaho Act is over-inclusive, because it fails to carve out exclusions for emergent entities that do not present the risks that the Act sought to mitigate. The current Act only requires businesses who sell or issue payment instruments, or engage "in the business of receiving money for transmission or . . . transmitting money" to be licensed.<sup>210</sup> The only exceptions are government entities, banks, and authorized representatives of licensees.<sup>211</sup> The failure to exclude, or modify the requirements for, entities that present a low risk of loss to consumers, but whom the drafters of the Act would be unlikely to consider to be regulatory targets, renders the Act over-inclusive. Moreover, entities that only engage in money transmission incidentally and payment processors dealing exclusively with well-regulated entities present sufficiently low risk of loss to consumers that they should be either excluded from the scope of the Act or subject to a lesser degree of regulation.<sup>212</sup> For these reasons, both types of entities are excluded from federal regulation and from some other states' regulations.<sup>213</sup>

Furthermore, the Idaho Act is under-inclusive because it does not clearly apply to certain types of entities that would arguably be engaging in money transmission. The current definition of money transmission does not clearly apply certain types of new organizations, such as Distributed Autonomous Organizations (DAO), which neither have the centralized control that the Idaho Act seems to envision nor are clearly engaged in the *business* of transmitting money.<sup>214</sup> The first issue, the lack of centralized control, means there may be no identifiable entity to seek a license. Instead, there is only a group of individuals whose only connection to each other is

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209. Aaron Greenspan, *Held Hostage: How the Banking Sector Has Distorted Financial Regulation and Destroyed Technological Progress*, HARV. U. 1, 12–16 (2011), [https://works.bepress.com/aaron\\_green-span/1/](https://works.bepress.com/aaron_green-span/1/) (illustrating how licensing requirements have failed to protect consumers).

210. IDAHO CODE § 26-2902(11) (2018).

211. IDAHO CODE § 26-2904 (2018).

212. "Well-regulated entities" means BSA approved financial institutions in this context. Federal regulators realized that such entities were not necessary to be regulated and updated the BSA to clearly exclude them. Bank Secrecy Act Regulations; Definitions and Other Regulations Relating to Money Services Businesses, 76 Fed. Reg. 43585, 43593 (July 21, 2011) (codified at 31 C.F.R. pt. 1010).

213. 31 C.F.R. § 1010.100(ff)(5)(ii)(C) (2017) (excluding payment processors from BSA regulation); 31 C.F.R. § 1010.100(ff)(5)(ii)(F) (2017) (excluding incidental payment processors from BSA regulation); *Fatal Fragments*, *supra* note 4, at 142 (noting that Illinois does not require third-party payment processors to be licensed as money transmitters).

214. See IDAHO CODE §§ 26-2902(15), 26-2907–2911 (2018) (statutes imposing requirements presumably to be filled out by an individual or representative); IDAHO CODE § 26-2902 (2018) (defining "money transmission" but not "business").

the set of self-executing contracts that constitute the DAO. It is an open question who would be liable under Idaho Code Section 26-2921 for failing to obtain the license if a license were required. It is questionable whether it would be equitable to hold those who implemented the smart contracts responsibly, especially in instances where they were not a party to those contracts. This issue of a centralized management conceptualization is further complicated where all transactional data is anonymized in such a manner that no one person has access to all of the information required to be reported under the current Act. Then there is a further question of whether a DAO is engaging in the *business* of money transmission at all. If the DAO is set up such that it is merely the conduit through which people transmit funds pursuant to smart contracts, and the only remuneration for the service retained by the DAO is a small fee to automatically pay the cost of using the public blockchain on which it operates, it becomes difficult to fairly define the DAO as being in the *business* of money transmission. Note, however, that the calculus might change if there were a third party that facilitated the fund exchange performed by the DAO from whom the DAO collects a fee for arranging the exchange. Under that circumstance, the DAO would arguably be a payment processor, and the Idaho Department of Finance has stated “that all payroll processors are money transmitters and licensure is required.”<sup>215</sup>

The limited conceptualization of the Act can be further demonstrated by taking the above DAO hypothetical a step further and considering how licensing requirements apply when an AI was responsible for the creation and operation of the DAO. The current Act limits its conceptualization of the entities involved in money transmission to “persons,”<sup>216</sup> which does not seem to contemplate AI or other electronic entities.<sup>217</sup>

The other conceptual limitation inherent in the current Idaho Act relates to restrictive conceptualization of money transmission activities. While it is understandable that the Act was not drafted in anticipation of the rise of virtual currencies, the Act’s failure to consider a broader definition of money has resulted in a failure to regulate entities that are handling an increasingly important medium of exchange for Idaho’s citizens.<sup>218</sup> In particular, the limited regulation of virtual currencies is allowing a quickly growing risk of loss for Idaho consumers to go unchecked.<sup>219</sup> The Idaho Department of Treasury does currently require “exchangers”

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215. Dep’t Fin. November 2017 Letter, *supra* note 105

216. Its conceptualization is limited by framing all actions in terms of those performed by a “person” or “persons” as defined by the act. See, e.g., IDAHO CODE § 26-2902(9) (2018) (only a “person” may obtain a license under the Act).

217. See IDAHO CODE § 26-2902(15) (2018).

218. See IDAHO CODE § 26-2902(11) (2018); IDAHO CODE § 26-2902(13) (2018); IDAHO CODE § 26-2902(14) (2018); *Idaho Money Transmitters Section*, *supra* note 14 (stating that only exchangers of virtual currency are regulated money transmitters).

219. See Andrew Arnold, *30% of Millennials Would Rather Invest in Cryptocurrency: Here Are 3 Tips to Help You Do It Smarter*, FORBES (Jan. 7, 2018, 8:01 AM), <https://www.forbes.com/sites/andrewarnold/2018/01/07/30-of-millennials-invest-in-cryptocurrency-here-are-3-tips-to-help-you-do-it-smarter/#21ef3b277861> (noting the large interest from younger demographics in investing in virtual currencies).

of virtual currency, entities who exchange virtual currency for legal tender, to be licensed.<sup>220</sup> However, the protection provided by this requirement is of limited value because companies that exchange their own virtual currency for legal tender are not required to be licensed.<sup>221</sup> Only those facilitating the exchange of virtual currency for legal tender between two other parties need to be licensed.<sup>222</sup> This creates a situation in which the Idaho Act provides no protection from nefarious individuals and organizations using unregulated mechanisms to launder money and defraud consumers. Such money laundering is already a prevalent issue with virtual currencies.<sup>223</sup>

Another issue arising from the limited activity conceptualization is that the Act does not sufficiently consider risk factors arising from the computer systems, which are ubiquitously utilized in money transmission. For example, if a money transmitter's computer systems are hacked, resulting in all customer accounts being drained, it is not required to report the event to the Department of Treasury until its annual report is due.<sup>224</sup> The transmitter is required to report bankruptcy, revocation, or suspension of their license by another state, and a felony indictment or conviction of a key officer within fifteen days of the event,<sup>225</sup> but not a hacking event resulting in the loss of all its customers' money. Furthermore, the reporting requirements do not contain any requirement to provide information on the data security measures being used by the transmitter.<sup>226</sup> With the increase in high-profile data breaches, it is critical that regulated entities provide some confirmation that they are using best practices to protect their systems. In fact, one of the greatest vulnerabilities of blockchain-based virtual currencies is the consumer access point—the digital wallet in which the customer stores the currency in the case of virtual currencies.<sup>227</sup> It is easy to imagine a scenario in which a transmitter leverages a blockchain-based system to securely transmit funds but, due to lackluster security practices, the digital wallet that contain the client's funds is compromised and the currency is stolen before the customer can retrieve it.

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220. *Idaho Money Transmitters Section*, *supra* note 14 (stating that only exchangers of virtual currency are regulated money transmitters).

221. Letter from Jeff Flora, Fin. Exam'r/Investigator, Idaho Dep't of Fin., on Licensing of a Virtual Currency Exchanger Selling its Own Stock of Virtual Currency (July 26, 2016) [hereinafter Dep't Fin. July 2016 Letter], <http://www.finance.idaho.gov/MoneyTransmitter/Documents/NAOP/Digital%20Currency/2016-07-26.pdf>.

222. *Id.*

223. Dan Boylan, *Military, Intelligence Agencies Alarmed by Surge in Bitcoin Value in 'Dark Web' Fight*, WASH. TIMES (Aug. 10, 2017), <http://www.washingtontimes.com/news/2017/aug/10/bitcoin-value-surge-sign-of-criminal-activity/>. See generally *Bitcoin Virtual Currency: Unique Features Present Distinct Challenges for Deterring Illicit Activity*, FBI (Apr. 24, 2012), [https://www.wired.com/images\\_blogs/threat-level/2012/05/Bitcoin-FBI.pdf](https://www.wired.com/images_blogs/threat-level/2012/05/Bitcoin-FBI.pdf).

224. See IDAHO CODE § 26-2912 (2018); IDAHO CODE § 26-2911 (2018); IDAHO CODE § 28-51-105 (2018) (requiring disclosure to Idaho AG and potentially affected Idaho residents).

225. IDAHO CODE § 26-2912 (2018).

226. See IDAHO CODE § 26-2911 (2018).

227. Madhvi Mavadiya, *Blockchain, Bitcoin, and Ethereum Explained*, FORBES (Aug. 22, 2017 9:00 AM), <https://www.forbes.com/sites/madhvimavadiya/2017/08/22/blockchain-bitcoin-ethereum/3/#501f80c8c9fc> (explaining that the underlying technology, the blockchain, is effectively impossible to compromise, so nefarious individuals target the end user instead).



B. Proposed Solutions to the Problems with Idaho's Money Transmitters Act

i. Removing All State Regulatory Authority Over Money Transmitters to the CFPB is the Ideal Solution

The most efficient method of resolving the issues facing Idaho's Money Transmitter Act, and for resolving the fractured regulatory landscape governing money transmitters generally, would be to preempt all current state regulatory power over money transmitters under the Commerce Clause. The CFPB is the appropriate federal agency to take on this regulatory function since its core function is "protecting consumers in the financial marketplace,"<sup>228</sup> which is the policy reason underlying money transmitter regulation in many states.<sup>229</sup> Moreover, the CFPB already regulates international remittance transfers,<sup>230</sup> and the electronic fund transfer regulations it enforces already preempt state law to the extent that the state law is inconsistent.<sup>231</sup> Further, the CFPB already regulates prepaid payment mechanisms for the benefit of consumers, the issuers of which are currently licensed under state money transmitter regulations.<sup>232</sup> The consumer protection focus of money transmitter licensing regulation combined with the CFPB's existing regulatory scope, results in the CFPB being the natural choice of agency in which to consolidate money transmitter licensing authority. Any state regulatory authority relating to anti-money laundering would be removed to FinCEN since that organization already regulates money transmitters for that purpose.

Beyond the natural fit of the CFPB as the central regulatory and licensing authority, there are several benefits to consolidating such authority generally. The foremost benefit of such a change is that it would resolve the Balkanized regulatory landscape by creating a single set of licensing requirements. This would lead to regulatory certainty because case law and advisory opinions would be nationally relevant. Further, it would allow for a more complex gradation of requirements. Moreover, it would consolidate information about money transmitters within a single source. This would have the dual effect of promoting consumer protection and anti-money laundering goals. It would advance consumer protection by providing a single source of information for a consumer to check that a transmitter is licensed and

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228. *The Bureau*, CONSUMER FIN. PROT. BUREAU, <https://www.consumerfinance.gov/about-us/the-bureau/> (last visited Mar. 24, 2019).

229. See, e.g., S.B. 1454, 52d Leg., 2d Reg. Sess. (Idaho 1994), <https://advance.lexis.com/api/permalink/292e36b3-fbdc-4ee2-84b6-372de9b4de58/?context=1000516> (identifying purpose in the Statement of Purpose); *Fatal Fragments*, *supra* note 4, at 117–18 (identifying the policy reasons underpinning similar laws in five of the most populous states).

230. See 12 C.F.R. § 1005.30 (2018).

231. 15 U.S.C. § 1693q (2018); Stephen T. Middlebrook & Sarah Jane Hughes, *Virtual Uncertainty: Developments in the Law of Electronic Payments and Financial Services*, 69 BUS. L. 263, 270 (2013).

232. See *Prepaid Rule: Small Entity Compliance Guide*, CONSUMER FIN. PROT. BUREAU (Jan. 31, 2017), [https://s3.amazonaws.com/files.consumerfinance.gov/f/documents/201706\\_cfpb\\_prepaid-small-entity-compliance-guide.pdf](https://s3.amazonaws.com/files.consumerfinance.gov/f/documents/201706_cfpb_prepaid-small-entity-compliance-guide.pdf) (CFPB regulation of prepaid payment cards); *Idaho Money Transmitter Section*, *supra* note 14 (issuers of stored value instruments are required to be licensed under the Idaho Act).

by ensuring that the license is meaningful.<sup>233</sup> It would advance anti-money laundering goals by concentrating information needed to uncover illegal activity, making it easier for FinCEN as the principal regulatory for preventing money laundering to do its job. The prior point is especially true in the context of cryptocurrencies, where identifying the parties involved requires obtaining as much data as possible to identify patterns.<sup>234</sup> Moreover, it would advance consumer protection and anti-money laundering by encouraging legitimate entities to become licensed by lowering the net regulatory burden, thereby allowing the CFPB and FinCEN to focus on the truly nefarious entities. Lastly, consolidation would provide one entity to be held accountable for ensuring adequate regulation, thereby making issues of regulatory enforcement easier to resolve.

It is unlikely that the states would willingly cede this authority, and thus it would require federal preemption to achieve such centralized control.<sup>235</sup> However, precedent for such federal preemption exists in the related area of financial securities regulation. Called “Blue Sky” laws,<sup>236</sup> each state passed its own laws to protect consumers in their state from increasing levels of securities fraud.<sup>237</sup> However, these laws were ineffective in protecting consumers due to several factors, including the inability of the laws to cross state lines.<sup>238</sup> As a result of the failure of the laws at the state level, federal securities laws were enacted.<sup>239</sup> The explicit reasons given for the enactment of these federal laws included “the fact that securities transactions [were] carried out across state boundaries, are an important part of interstate commerce, involve issuers engaged in interstate commerce, and [that such transactions] affect the financing of activities in interstate commerce.”<sup>240</sup> Congress was also worried about “a race to the bottom” of State level regulation.<sup>241</sup> The transition to federal law occurred gradually over time.<sup>242</sup> The initial federal act did not preempt state laws, but rather supplemented them based on the reasoning that the state laws remained useful.<sup>243</sup> However, in the 1980s federal preemption was made explicit, and in the 1990s the scope of federal preemption was expanded.<sup>244</sup>

Federal preemption of money transmitter regulation, particularly regulation of transmitters operating interstate, could follow a similar path. In addition to efficiency justifications, preemption in this context is justified by many of the same

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233. Cf. Greenspan, *supra* note 209, at 13–14 (enforcement of licensing requirements has been sporadic or nonexistent in some states, rendering a money transmitter license in that state meaningless).

234. See John Bohannon, *Why Criminals Can't Hide Behind Bitcoin*, SCIENCE (Mar. 9, 2016), <http://www.sciencemag.org/news/2016/03/why-criminals-cant-hide-behind-bitcoin>.

235. See *Fatal Fragments*, *supra* note 4, 145–46 (noting that states would likely be resistant to required reciprocity being thrust upon them and instead federal preemption would be required).

236. *Blue Sky Laws*, U.S. SEC. & EXCH. COMM'N, <https://www.sec.gov/fast-answers/answers-blueskyhtm.html> (last updated Oct. 14, 2014).

237. Richard W. Painter, *Responding to a False Alarm: Federal Preemption of State Securities Fraud Causes of Action*, 84 CORNELL L. REV. 1, 21–23 (1998).

238. *Id.* at 22–23.

239. *Id.* at 23.

240. *Id.*

241. *Id.* at 24.

242. *Id.* at 22–24.

243. Painter, *supra* note 237, at 25–26.

244. *Id.* at 29–31.

reasons that federal preemption of the “Blue Sky” laws was justified.<sup>245</sup> The federal government already supplements state regulation of money transmitters to advance anti-money laundering goals,<sup>246</sup> so expanding its regulatory goals to include consumer protection would be possible. However, it is likely that such a federal preemption for consumer protection and regulatory efficiency reasons would result in an accelerated preemption timeline compared to the “Blue Sky” law timeline because the implementation of a federal law related to licensing would likely inherently, if not explicitly, preempt state-level licensing from the outset. This inherent preemption would result from the likelihood that the continued existence of state licensing schemes would frustrate at least the efficiency policy underlying the federal regulation, if not the consumer protection policy as well.<sup>247</sup>

The CFPB’s own regulations could be based on the BSA, and its promulgation by FinCEN, and existing state level regulation. In particular, the CFPB could use the existing regulatory framework at the state level to create its own framework. The CFPB could adopt the basic set of requirements currently used by states, including: net worth, security, permissible investment, applicant information, and reporting requirements. From there, these basic requirements could be modified and scaled in a manner to match the degree of regulation to the degree of risk, like that discussed below in sub-section (b) of this section. In addition to a basic set of regulations, the CFPB could look to adopt advantageous provisions currently enacted only in certain states, such as an agent-of-the-payee exemption<sup>248</sup> and a provision stating that digital actors are agents of their creators.<sup>249</sup> The CFPB could adopt the BSA’s statutory definition of “money transmission services,”<sup>250</sup> the BSA’s statutory exclusion of incidental transmitters,<sup>251</sup> and FinCEN’s interpretations of the BSA provisions.<sup>252</sup> The CFPB could also look to the UMSA, including its broad definition of

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245. The similar policy justification includes a worry about a race to the bottom of regulation. The intentional modification of proposed regulations in California, which as an effort to create a friendly regulatory environment for the virtual currency transmitters that had left New York after the state enacted more stringent regulation, demonstrates that this policy concern is not unfounded. See *Fatal Fragments*, *supra* note 4, at 125–26.

246. *One-hour Money Laundering*, *supra* note 2, at 140 (discussing how federal punishment for operation of money transmission business without the required state license(s) was an enhancement of, and supplement to, state regulation).

247. Francis J. Facciolo & Richard L. Stone, *Avoiding the Inevitable: The Continuing Viability of State Law Claims in the Face of Primary Jurisdiction and Preemption Challenges Under the Securities Exchange Act of 1934*, 1995 COLUM. BUS. L. REV. 525, 531 (1995) (noting that “state action that ‘frustrates policies underlying federal regulation’” are preempted) (quoting Richard J. Pierce Jr., *Regulation, Deregulation, Federalism, and Administrative Law: Agency Power to Preempt State Regulation*, 46 U. PITT. L. REV. 607, 629 (1985)).

248. See, e.g., CAL. FIN. CODE § 2010(l) (West 2018); N.Y. BANKING LAW § 641(1) (McKinney 2018).

249. See, e.g., IDAHO CODE § 28-50-114(1) (2018).

250. 31 C.F.R. § 1010.100(ff)(5)(i)(A) (2017).

251. 31 C.F.R. § 1010.100(ff)(5)(ii)(F) (2017).

252. Interpretations here refers to FinCEN’s administration rulings and other guidance it has issued. See, e.g., FinCEN, *supra* note 185 (“interpretive guidance [clarifying] the applicability of the regulations implementing the Bank Secrecy Act (“BSA”) to persons creating, obtaining, distributing, exchanging, accepting, or transmitting virtual currencies”).

“money transmission” and “monetary value,” to ensure that virtual currency transmitters fall within its regulatory scope.

ii. Proposed Changes to Idaho’s Money Transmitters Act

In the absence of federal preemption of state licensing and regulatory authority, several modifications to the Idaho Act would serve to help alleviate some of the issues that currently exist. The proposed changes are grouped into two categories based on the two overarching issues that they address: (1) those alleviating burdens on innovation, and (2) those recalibrating the Act’s conceptualization of the actors and activities involved in money transmission. These changes would work together to advance the consumer protection policy underlying the Idaho Act while minimizing the regulatory burdens that transmitters face. The difficulty in balancing these two competing interests has caused issues for other states.<sup>253</sup> Therefore, Idaho must proceed carefully. A telling example of the difficulty in achieving the appropriate balance comes from New York’s implementation of its virtual currency regulation. New York implemented a very broad definition of the activities that brought an entity within the scope of their virtual currency transmitter regulation.<sup>254</sup> As a result of the overly broad definition, some virtual currency business ended up leaving New York and terminating services in the state.<sup>255</sup>

a. Suggested Changes to Alleviate Existing Burdens on Innovation

The first category of suggested changes, those designed to alleviate burdens on innovation, is comprised of two types of changes: licensing reciprocity and requirement scaling.

Two levels of licensing reciprocity should be added to the Act: interstate licensing reciprocity and intra-state licensing reciprocity. Interstate licensing reciprocity would entail adding provisions recognizing an entity’s license granted by another state subject to certain conditions. Section 203 of the Uniform Act states requirements that should be sufficient to allow Idaho to ensure that consumers remain protected, while at the same time reducing the regulatory redundancy that currently exists. Section 203 provides that only licenses from states that have substantially similar licensing requirements will be recognized,<sup>256</sup> allows for an investigation of the applicant by Idaho’s regulatory agency<sup>257</sup> and requires that the applicant comply with Idaho’s examination and reporting requirements as if it were licensed by Idaho.<sup>258</sup> However, the Section 203 provision that would require compliance with Idaho’s permissible investment requirements should not be used.<sup>259</sup> In

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253. *Fatal Fragments*, *supra* note 4, at 136.

254. *Fatal Fragments*, *supra* note 4, at 125 (defining regulated activity as “storing, holding, or maintaining custody or control of virtual currency on behalf of others” and “controlling, administering, or issuing a virtual currency” (quoting N.Y. COMP. CODES R. & REGS. tit. 23, § 200.2(q)(2)–(5) (2016)).

255. *Id.*

256. UNIF. MONEY SERVS. ACT § 203(a)(1) (UNIF. LAW COMM’N 2004).

257. UNIF. MONEY SERVS. ACT § 203(b) (UNIF. LAW COMM’N 2004).

258. UNIF. MONEY SERVS. ACT § 203(d) (UNIF. LAW COMM’N 2004).

259. *See id.* (requiring that entities licensed in another state comply with Article 7, which describes permissible investment requirements). This suggestion is predicated on the goal of eliminating redundant

addition to its other inherent benefits, interstate licensing reciprocity would make it more appealing for new and innovative prepaid payment mechanism providers to offer their services in Idaho. With the rising importance of prepaid payment mechanisms,<sup>260</sup> innovative offerings of such financial services are potentially a significant value to Idaho consumers.

The second level of licensing reciprocity should be intrastate licensing reciprocity. The Idaho Department of Treasury has already demonstrated a willingness to allow entities licensed under other Acts that the Department administers to forego obtaining a license under the Money Transmitter Act in certain cases.<sup>261</sup> Building on this willingness, language should be added to the Idaho Act explicitly providing that licenses granted under other acts by Idaho are sufficient; at least when the money transmission activity directly relates to the activities for which an entity has a license and when the additional risk of loss to the consumer is minimal. The reasoning for such intrastate reciprocity is particularly compelling in situations where the other Act's licensing requirements are substantially similar to the licensing requirements in the Idaho Money Transmitter Act.<sup>262</sup>

The next type of suggestion under this category is license requirement scaling based on the risk presented by the applicant/licensee. Two kinds of provisions in the current Idaho Act present opportunities for scaling: monetary requirements and reporting requirements. The method of scaling is similar for both. Statutory provisions should lay out criteria by which the risk presented by a given entity is measured and the baselines from which the requirements are increased or decreased. Other states, such as Texas, have already identified factors that could be used to make such assessments.<sup>263</sup> Idaho could leverage the work done by other states to assemble its own list based on how effective states have found each of their criteria to be. The baselines should be set based on similar criteria to those used in the risk assessments, but the criteria should be objective, such as whether the applicant will have a physical location in Idaho, the number of other states in which the applicant is licensed, the value of surety bonds and other securities that applicant has with other states, how long the applicant has provided money transmission services, the magnitude of the applicant's activities, and the value of the applicant's net assets.

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regulatory burdens. The purpose served by this provision in the Uniform Act, the protection of consumers in the event that a money transmitter becomes unable to repay its obligations to them, is generally otherwise served by the same or similar requirements in the licensing state.

260. *One-hour Money Laundering*, *supra* note 2, at 178. ("[P]repaid cards have emerged as a means of delivering financial services to a large segment of the population that is either not served or underserved by traditional banks.").

261. Dep't Fin. January 2016 Letter, *supra* note 134.

262. For example, the Idaho Collection Agency Act requires much of the same information and a bond requirement to obtain a license under that Act, much like the Money Transmitters Act. *Compare* IDAHO CODE § 26-2224 (2018) (requiring application information for licensing under the Idaho Collection Agency Act) *and* IDAHO CODE § 26-2232 (2018) (requiring bond to be licensed under the Idaho Collection Agency Act), *with* IDAHO CODE § 26-2907 (2018) (requiring information to apply for licensure under the Money Transmitter Act) *and* IDAHO CODE § 26-2908 (2018) (requiring bond to obtain a license under the Money Transmitter Act).

263. *See* TEX. FIN. CODE ANN. § 151.307 (West 2018).

For example, a money transmitter using a blockchain-based financial records system presents a lower risk than one that does not, since such a system makes it almost impossible for an employee of that transmitter to modify the transaction history.<sup>264</sup> Thus, unless the entire business were involved in the fraud, the transmitter would be well-positioned to discover an employee's fraud quickly, thereby decreasing the risk that a given customer will be defrauded by an employee of the transmitter. However, the minimum baseline for the monetary requirements should be set sufficiently high to ensure that a licensee always has sufficient resources available to pay back any money entrusted to it by consumers, and a percentage of that amount should be liquid.

This scaling should apply to the net worth requirements under Section 26-2905(1), the bond requirements under Section 26-2908, and the permissible investment requirements under Section 26-2906. Texas has a rudimentary form of this scaling for its permissible investment requirement, decreasing the requirement permissible investment value when the licensee's net worth reached \$5 million or more.<sup>265</sup>

This scaling should also apply to the reporting requirements and information requirements set forth in Section 26-2907, describing the information that must be provided on the license application and Section 26-2911, describing annual reporting requirements. Based on the identified criteria, the initial information required of an applicant and ongoing reporting requirements, including frequency of reporting, should be modified. Further, a process by which a licensee/applicant can appeal the requirements found applicable to them should be set forth. The goal of such a process should be to avoid litigation over any risk determinations made. This scaling would fundamentally enable at least some regulation of anonymized decentralized transmitters.

Finally, a provision allowing the director to temporarily waive monetary and reporting requirements should be added. As another writer described it, such a waiver provision "would offer time-delimited, carefully-tailored indemnities for 'deserving' business. Whether or not a business deserves temporary relief from licensure depends on the stated goals of the state's money transmitter laws, with specific criteria for such a waiver left to the commissioner's discretion."<sup>266</sup> This waiver, primarily targeted at startups, has become necessary in an age when small companies have the capacity to offer innovative services to the entire world immediately via the internet. Idaho should seek to encourage such entities to obtain the appropriate licensing by shifting the cost/benefit analysis in favor of doing so for legitimate transmitters.

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264. Jun Dai et al., *Why Blockchain Has the Potential to Serve as a Secure Accounting Information System*, CPA J. (Sept. 2017), <https://www.cpajournal.com/2017/09/20/blockchain-potential-serve-secure-accounting-information-system-cpe-season/> ("These characteristics allow blockchain to serve as the foundation of a new accounting information system that prevents accounting records or related electronic documents from being altered or deleted.").

265. TEX. FIN. CODE ANN. § 151.309(a) (West 2018).

266. *Fatal Fragments*, *supra* note 4, at 144.

b. Suggested Changes to Adjust the Idaho Act's Conceptualization of Money  
Transmission Actors and Activities

The second category of suggested changes is focused on adjusting the Idaho Act's conceptualization of the actors and activities involved in money transmission and targeting regulations toward the entities and activities that present a meaningful degree of risk. These changes are intended to provide more flexibility in regulatory enforcement.

The first type of change suggested under this category is the inclusion of certain exemptions. First, the agent-of-the-payee exemption is necessary because many incidental transmitters fall within the scope of the current Idaho Act even though they do not present a significant risk of consumer loss.<sup>267</sup> "Incidental transmission businesses with access to [these exemptions] can agree to assume consumer obligations," thereby presenting a very low risk to consumers.<sup>268</sup> The risk of loss presented by such an entity to consumers is so low that the regulatory burden imposed by requiring the entity be licensed significantly outweighs such risk, even when the licensing requirements are set to their lowest level under the requirement gradation scheme proposed above. This exemption would also exclude certain payment processors, like Square.<sup>269</sup> Second, the Act should exempt transmitters that are merely acting as a clearing agent. These transmitters are excluded from the scope of the UMSA.<sup>270</sup> The comments following Section 102 of the UMSA state that such entities are sufficiently low risk that they need not be included within the scope of a customer protection statute.<sup>271</sup> These clearing agents are more common with the rise of internet marketplaces, and justification for the regulation under the money transmitter regulations is lacking.

The next change proposed under this second category is for Idaho to expand its definition of "money transmission" to include "monetary value" and to adopt the definition of "monetary value" used by the UMSA.<sup>272</sup> The primary difference between the current definition of "money transmission" contained in the Idaho Act and the definition in the UMSA is the UMSA's inclusion of "monetary value" in the definition.<sup>273</sup> This difference limits the flexibility of the Idaho Act to apply to transmitters that convey currency-like substitutes, and the rise of virtual currencies has demonstrated why this limitation has become problematic. Expanding the definition of "money transmission" alone is not sufficient; the newly included term, "monetary value," must be defined to ensure that it encompasses the appropriate

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267. *Id.* at 129.

268. *Id.*

269. *See id.* at 142 (discussing Illinois' exclusion of payment processors like Square over concerns about limiting innovation as a step toward a full-fledged agent-of-the-payee exemption).

270. UNIF. MONEY SERVS. ACT § 102 cmt. 9 (UNIF. LAW COMM'N 2004).

271. *Id.*

272. UNIF. MONEY SERVS. ACT § 102(11) (UNIF. LAW COMM'N 2004). In addition to adopting the definition of "monetary value" contained in the Uniform Act, the comments associated with the definition should also be adopted.

273. *Compare* IDAHO CODE § 26-2902(11) (2018), *with* UNIF. MONEY SERVS. ACT § 102(14) (UNIF. LAW COMM'N 2004).

forms of value. To that end, the UMSA's definition of "monetary value" set forth in Section 102(11), along with the associated Comment 10 following Section 102, provides an appropriately broad definition by which the important forms of value currently popular, like virtual currencies, would be covered as well as forms that may emerge in the future. The definition in Section 102(11) is very broad, but the associated comments clarify that the "mediums of exchange" included within the definition are those accepted by the larger community.<sup>274</sup> Specific exemptions could be added based on legislative priorities, but it is easier to add specific exemptions than specific inclusions. Adopting sufficiently broad definitions would provide the Idaho Act much-needed flexibility to ensure that Idaho consumers are protected.<sup>275</sup>

The next type of proposed change relates to the recognition that most business activity is performed digitally, and the risks created by this are different from those envisioned in the pre-internet proliferation era of the Idaho Act's enactment. The simplest proposed change is that, in addition to current annual reporting requirements under Section 26-2911, a computer system security audit should be provided by the transmitter as well.<sup>276</sup> This requirement would help ensure that one of the largest risks to consumers in this area, a transmitter being hacked and consumer funds being stolen or destroyed, is minimized. Such a reporting requirement might also provide the statutory foundation for validating the algorithms controlling a transmitter's blockchain. The consumer protection policy underlying the Idaho Act cannot be adequately advanced by financial audit reporting alone. In the digital age, good computer security practices play an integral role in protecting consumers, and the failure of a financial services business to engage in appropriate computer security practices is the type of unsound business practice from which the Idaho Act was seemingly designed to protect consumers. Like providing audited financial reports, this requirement would impose a heavy burden, but that burden has become a necessary one in the digital age.<sup>277</sup> Moreover, ensuring that a transmitter is following appropriate computer security principles would facilitate the protection of records that may be required in an examination under Section 26-2914. Finally, two additional requirements naturally flow from this change: (1) the inclusion of a computer system security audit in the initial application information required by Section 26-2907; and (2) the addition of another extraordinary reporting requirement under Section 26-2912, requiring a report in the event the licensee's computer systems are compromised resulting in consumer's funds being lost. The requirement scaling suggested above would apply to the proposed computer system security audit reporting and applicant information requirements.

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274. See UNIF. MONEY SERVS. ACT § 102 cmt. 10 (UNIF. LAW COMM'N 2004).

275. Alternatively, Idaho could seek to enact a separate Act for the regulation of other stores of value. For virtual currency, Idaho could look to enacting something similar to the Regulation of Virtual-Currency Business Act, created by the Uniform Law Commission. However, that would only resolve the issue for virtual currency and does not future-proof the Idaho Act against new mediums of exchange not yet envisioned and falling outside the scope of any kind of virtual currency regulation.

276. A computer system security audit here is meant to include an audit validating the security of any computer code used in proprietary applications, computer network security, and computer security practices (i.e., social engineering prevention, physical security practices, etc.).

277. See U.S. SEC. & EXCH. COMM'N, CF DISCLOSURE GUIDANCE: TOPIC NO. 2 (2011), [https://www.sec.gov/divisions/corpfin/guidance/cfguidance-topic2.htm#\\_ednref1](https://www.sec.gov/divisions/corpfin/guidance/cfguidance-topic2.htm#_ednref1) (noting that disclosure of cybersecurity risks is required in certain cases to register to make a securities offering).



The final change proposed by this article is for the Idaho Act to adopt the electronic agent paradigm as a stopgap measure while the legal and ethical fields regarding artificial intelligences develop. Due to advancements in AI, in the near future humans may be far removed from the creation and operation of money transmitters.<sup>278</sup> However, since we are in the infancy of AI development, attempting to create more targeted regulation is likely to prove folly in hindsight. So instead, this article merely suggests a paradigm under which the actions of an electronic entity are treated as the actions of the electronic entity's creator. Under this paradigm the electronic entity is an agent of its creator.<sup>279</sup> This paradigm could be added to the Idaho Act by expanding the definition of "person" to include "electronic agents," defining "electronic agents" as "digital or virtual entities, applications, programs, or any other form of virtual actor who performs the creation, operation, and/or management functions of a money transmitter business normally performed by an individual,"<sup>280</sup> and specifying that electronic agents are agents of the non-digital entity that created them or their creator or their creator's predecessor. Adopting such a paradigm would allow for a responsible party to be identified if an AI attempts to become licensed in Idaho. Further, such a paradigm would resolve the issue of who is responsible for ensuring that an entity like a DAO has the appropriate licenses by putting the onus on the person who created the smart contracts. However, as noted above, this is merely meant to be a stopgap until the societal consensus regarding the legal and ethical implications of AIs is determinable. As such, Idaho lawmakers should be ready to update the law as necessary once such a determination is possible.

#### VIII. CONCLUSION

The rapid technological progress in the two decades since the original enactment of Idaho's Money Transmitter Act has brought about many beneficial changes, including in the field of money transmission. It has never been easier or cheaper for individuals to take advantage of money transmission services. However, this progress has resulted in changes that were completely unforeseen by those who originally drafted Idaho's Money Transmitter Act, including the rise in importance of virtual currency, the explosion of internet-based markets and services providers, and the proliferation of business entities that transmit money incidentally to their core business. As a result, the current Idaho Act is both over and under-inclusive. Moreover, the sudden ease with which a money transmitter could offer its services in every state due to the proliferation of the internet reveals how the Idaho Act contributes to a larger national regulatory problem.

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278. See Gregory Scopino, *Preparing Financial Regulation for the Second Machine Age: The Need for Oversight of Digital Intermediaries in the Futures Market*, 2015 COLUM. BUS. L. REV. 439, 449–51 (2015) (discussing how artificial digital entities operating in the financial sector will eventually become independent entities and rudimentary forms of AI already impact our life).

279. See IDAHO CODE § 28-50-114(1) (2018) (considering something very similar to this paradigm).

280. The proposed definition of "electronic agent" is meant to be an example. A more precise definition is likely required to ensure that the definition encompasses the intended targets.

In response to these unforeseen changes, this article proposes two principal solutions: the consolidation of licensing and regulatory authority over money transmitters in a single federal entity, the CFPB, and changes to the existing Idaho's Money Transmitter Act. The most efficient solution to many of the problems facing not only Idaho's Act, but money transmitter regulations nationally, would be to consolidate authority within the CFPB. However, it is unlikely that such a transition will occur, particularly in the near future. Thus, Idaho should move to implement the changes suggested in this article to its regulations. Doing so would reduce the barriers to innovative money transmitter services reaching Idaho consumers, provide better protection against fraudulent and unsound business practices for such consumers, and remove one regulatory bramble from the morass that is the national money transmitter regulatory landscape.