

Schulte Roth&Zabel

FinCEN issues final rules relating to money services business (MSB) definitions

Betty Santangelo, Donald J. Mosher, William I. Friedman and Matthew P. Truax
Schulte Roth & Zabel LLP



Reprinted from

Journal of Investment Compliance

Vol. 13 No. 1, 2012, pp. 17-22

© Emerald Group Publishing Limited

ISSN 1528-5812



Reprints
from Emerald

www.emeraldinsight.com/reprints

FinCEN issues final rules relating to money services business (MSB) definitions

Betty Santangelo, Donald J. Mosher, William I. Friedman and Matthew P. Truax

Betty Santangelo and Donald J. Mosher are Partners, William I. Friedman is Special Counsel, and Matthew P. Truax is an Associate, all with Schulte Roth & Zabel LLP, New York, New York, USA.

Abstract

Purpose – *The purpose of the paper is to explain FinCEN's money services business rule (MSB Rule) revising the regulations that apply to MSBs.*

Design/methodology/approach – *The paper details the principal revisions in the new MSB Rule, including an amended definition of an MSB, an activity threshold, and applicability of the rule to foreign-located MSBs, money transmitters, dealers in foreign exchange, check cashiers, and issuers of travelers' checks as defined in the rule.*

Findings – *The final rule clarifies which activities subject a person to the Bank Secrecy Act's rules pertaining to MSBs and subjects certain foreign-located MSBs with a US presence to US rules.*

Originality/value – *The paper provides practical guidance from experienced financial services lawyers.*

Keywords *US Department of the Treasury Financial Crimes Enforcement Network (FinCEN), Bank Secrecy Act, Money services businesses, Banking, Regulation, United States of America*

Paper type *Technical paper*

On July 21, 2011, the US Department of the Treasury's Financial Crimes Enforcement Network ("FinCEN") issued a final rule (the "MSB Rule"), revising the regulations regarding money services businesses ("MSBs"). The final rule clarifies which activities subject a person to the Bank Secrecy Act's ("BSA") rules pertaining to MSBs and subjects certain foreign-located MSBs with a US presence to the BSA rules[1]. In particular, the MSB Rule:

- provides that certain foreign-located persons engaging in MSB activities within the US are subject to the BSA rules;
- updates the MSB definitions to reflect past guidance and administrative rulings, current business operations, evolving technologies and merging lines of business;
- expands the definition of a dealer in foreign exchange to include forex traders, unless they are functionally regulated or examined by the Commodity Futures Trading Commission ("CFTC"); and
- separates the provisions dealing with stored value from those dealing with issuers, sellers, and redeemers of traveler's checks and money orders.

The MSB Rule became effective on September 19, 2011. Compliance with the MSB Rule is required on January 23, 2012.

Separately, on July 29, 2011, FinCEN published a final rule, renaming "stored value" as "prepaid access" and amending the BSA regulations relating to prepaid access (the "Prepaid Access Rule")[2].

Definition of MSBs

The MSB Rule amended the definition of an MSB to include a “person wherever located doing business, whether or not on a regular basis or as an organized or licensed business concern, wholly or in substantial part within the US,” acting in the capacity of certain regulated activities, i.e. a dealer in foreign exchange, check casher, issuer or seller of traveler’s checks or money orders, provider and seller of prepaid access, and/or money transmitter (“Regulated MSB Activity”)[3]. “This includes but is not limited to the maintenance of any agent, agency, branch, or office within the US”[4].

In the preamble to the MSB Rule, FinCEN explains that it amended the definition of an MSB, “to emphasize [its] concern that ‘doing business’ can be misinterpreted to refer to status, not activity”[5]. FinCEN emphasized that “whether a person is subject to regulation as an MSB does not depend on factors such as whether the person is licensed as a business by any state; whether the person has employees; or whether the person is engaged in a for-profit venture”[6]. Rather, it is a person’s activities, and not a person’s formal business status, that would cause a person to be categorized as an MSB. Thus, whether a person engages in Regulated MSB Activity is dependent on all of the facts and circumstances of each case.

The MSB Rule also excludes a natural person who engages in Regulated MSB Activity “on an infrequent basis and not for gain or profit”[7]. However, FinCEN excludes only individuals – not business entities, non-profits, or other legal persons – from the MSB definition. FinCEN intends to limit the exclusion to activity that is rare.

Under the MSB Rule, the term MSB does not include: a bank or foreign bank; or a person registered with, and functionally regulated or examined by, the Securities and Exchange Commission (“SEC”) or the CFTC, or a foreign financial agency that engages in financial activities that, if conducted in the US, would require the foreign financial agency to be registered with the SEC or CFTC[8].

Activity threshold

The MSB regulations currently “apply to persons engaged in specified activities that exceed \$1,000 for any person in any day,” with the exception of money transmitters, which do not have an activity threshold[9]. The \$1,000 threshold remains unchanged by the MSB Rule, although FinCEN has indicated that it will continue to study the issue of the MSB activity thresholds.

Foreign-located MSBs

Recognizing that the internet and other technological advances in the payments industry have made it possible for MSBs located outside of the US to offer MSB services in the US, FinCEN extended the BSA rules to all persons engaging in MSB activities within the US regardless of a person’s physical location.

Under the MSB Rule, a foreign-located person, including a foreign exchange dealer or a money transmitter, will be subject to the BSA as an MSB to the extent that it is doing business “wholly or in substantial part within the US”[10]. Whether or not a foreign-located person’s MSB activities occur within the US depends on all of the facts and circumstances of each case, including whether persons in the US are obtaining MSB services from the foreign-located person, such as sending money to or receiving money from third parties through the foreign-located person. According to FinCEN, merely having a bank account in the US is not enough to render a foreign-located money transmitter or exchange house subject to the BSA.

In the event that a foreign-located MSB is subject to the BSA as an MSB, it will have the same reporting and recordkeeping and registration requirements as MSBs with a physical presence in the US, with respect to their regulated MSB activity in the US[11]. In addition, the foreign-located MSB will be subject to the same civil and criminal penalties as MSBs with a

physical presence in the US, with respect to their failure to comply with regulatory requirements.

In addition, the MSB Rule requires foreign-located MSBs to designate the name and address of a person who resides in the US and is authorized, and has agreed, to be an agent to accept service of legal process. Compliance with this designation of an agent for service of process provision requires a change to FinCEN Form 107 (Registration of Money Services Business)[12]. Accordingly, the rule provides that compliance with the registration requirements set forth in 31 C.F.R. §1022.380 is not required until six months after the date of publication of the rule (January 23, 2012), by which time the revised FinCEN Form 107 is expected to be final[13].

Money transmitter

Under the MSB Rule, a person who provides money transmission services or any other person engaged in the transfer of funds is a money transmitter[14]. The term money transmission services means the acceptance of currency, funds, or other value that substitutes for currency from one person and the transmission of currency, funds, or other value that substitutes for currency to another location or person by any means. The phrase “any means” includes, but is not limited to, “through a financial agency or institution; a Federal Reserve Bank or other facility of one or more Federal Reserve Banks, the Board of Governors of the Federal Reserve System, or both; an electronic funds transfer system network; or an informal value transfer system” (such as a hawala)[15].

Whether a person is a money transmitter is a matter of facts and circumstances[16]. The term money transmitter does not include a person who only:

1. Provides the delivery, communication, or network access services used by a money transmitter to support money transmission services.
2. Acts as a payment processor to facilitate the purchase of, or payment of a bill for, a good or service through a clearance and settlement system by agreement with the creditor or seller.
3. Operates a clearance and settlement system or otherwise acts as an intermediary solely between BSA regulated institutions. This includes but is not limited to the Fedwire system, electronic funds transfer networks, certain registered clearing agencies regulated by the SEC, and derivatives clearing organizations, or other clearinghouse arrangements established by a financial agency or institution[17].
4. Physically transports currency, other monetary instruments, other commercial paper, or other value that substitutes for currency as a person primarily engaged in such business, such as an armored car, from one person to the same person at another location or to an account belonging to the same person at a financial institution, provided that the person engaged in physical transportation has no more than a custodial interest in the currency, other monetary instruments, other commercial paper, or other value at any point during the transportation.
5. Provides stored value (now referred to as prepaid access under the Prepaid Access Rule), whether it is opened or closed loop[18].
6. Accepts and transmits funds only integral to the sale of goods or the provision of services, other than money transmission services, by the person who is accepting and transmitting the funds[19].

Dealer in foreign exchange

In the MSB Rule, FinCEN changed the phrase “currency dealer or exchanger” to “dealer in foreign exchange,” which it defined as including a “person that accepts the currency, or other monetary instruments, funds, or other instruments denominated in the currency, of one or more countries in exchange for the currency, or other monetary instruments, funds, or

other instruments denominated in the currency, of one or more other countries in an amount greater than \$1,000 for any other person on any day in one or more transactions, whether or not for same-day delivery”[20].

FinCEN stated that it intended to clarify that “dealing in foreign exchange is not limited to the physical exchange of the currency of one country for the currency of another country,” and that its “current rules and existing body of administrative rulings establish that a person who converts funds denominated in the currency of one country into funds denominated in the currency of another country is an MSB by virtue of that activity”[21]. This amendment to the MSB Rule expands the definition of a dealer in foreign exchange to include forex traders, unless they are functionally regulated or examined by the CFTC.

Additionally, FinCEN noted that it intended to capture those types of payment instruments that do not fall into one of the other categories of Regulated MSB Activity, but nevertheless are readily recognizable as payment instruments. FinCEN further indicated that “a person is not a dealer in foreign exchange to the extent the person exchanges their own money on their own behalf”[22].

Check casher

The definition of a “check casher” includes a person that accepts checks[23] or monetary instruments[24] “in return for currency or a combination of currency and other monetary instruments or other instruments, in an amount greater than \$1,000 for any person on any day in one or more transactions”[25].

Whether a person meets the definition of a “check casher” is a matter of facts and circumstances but the MSB Rule specifically excludes the following persons from the definition of a “check casher”:

- a person who sells stored value (i.e. prepaid access) in exchange for a check, monetary instrument or other instrument;
- a person who solely accepts monetary instruments as payment for goods or services other than check cashing services;
- a person who engages in check cashing for the verified maker of the check who is a customer otherwise buying goods and services;
- a person who redeems its own checks; or
- a person who only holds a customer’s check as collateral for repayment by the customer of a loan[26].

The MSB Rule exempts “the purchase of any type of stored value with a check, monetary instrument, or other instrument from being an activity subject to the check casher definition”[27]. FinCEN clarified that “[e]ntities that accept payment for goods or services with a check and return more than \$1,000 in currency or a combination of currency and other monetary instruments fall under the definition of ‘check casher’ regardless of the value of the goods or services”[28].

Issuer or seller of traveler’s checks or money orders

The MSB Rule combines prior sections of the rule relating to an “issuer of traveler’s checks, money orders, or stored value” and a “seller or redeemer of traveler’s checks, money orders, or stored value”[29], into a new section of the rule concerning an “issuer or seller of traveler’s checks, money orders, or stored value”[30]. The MSB Rule defines an “issuer or seller of traveler’s checks or money orders” as a person who:

- issues traveler’s checks or money orders that are sold in an amount greater than \$1,000 to any person on any day in one or more transactions; or
- sells traveler’s checks or money orders in an amount greater than \$1,000 to any person on any day in one or more transactions[31].

The definition is linked to the aggregate amount at which the traveler's checks or money orders are sold, either directly by the issuer or at the agent level, to a customer in a single day[32]. Nothing in the MSB Rule changes the applicable aggregation requirements.

US Treasury circular 230 notice

Any US federal tax advice included in this communication was not intended or written to be used, and cannot be used, for the purpose of avoiding US federal tax penalties.

This information has been prepared by Schulte Roth & Zabel LLP ("SRZ") for general informational purposes only. It does not constitute legal advice, and is presented without any representation or warranty as to its accuracy, completeness or timeliness. Transmission or receipt of this information does not create an attorney-client relationship with SRZ. Electronic mail or other communications with SRZ cannot be guaranteed to be confidential and will not (without SRZ agreement) create an attorney-client relationship with SRZ. Parties seeking advice should consult with legal counsel familiar with their particular circumstances. The contents of these materials may constitute attorney advertising under the regulations of various jurisdictions.

Notes

1. 76 Fed. Reg. 43,585 (July 21, 2011) (codified at 31 C.F.R. §§1010.100(ff), 1010.605(f), 1021.311(c), 1022.210(d), 1022.380(a)(b) and 1022.410(a)(b) (2011)).
2. See 76 Fed. Reg. 45,403 (July 29, 2011) (codified at 31 C.F.R. §§1010.100(ff), (ww), and (kkk), 1022.210, 1022.320, 1022.380 and 1022.420 (2011)); see also FinCEN Notice 2011-3, "Administrative Relief for Sellers and Providers of Prepaid Access," (Sept. 9, 2011), available at www.fincen.gov/financial_institutions/msb/index.html
3. 31 C.F.R. §1010.100(ff).
4. Id.
5. 76 Fed. Reg. at 43,587.
6. Id.
7. 31 C.F.R. §1010.100(ff)(8)(iii).
8. 31 C.F.R. §1010.100(ff)(8)(i)(ii).
9. 76 Fed. Reg. at 43,588.
10. Id.
11. Id. at 43,589.
12. Id. at 43,594; see 76 Fed. Reg. 62,149 (Oct. 6, 2011), available at: www.gpo.gov/fdsys/pkg/FR-2011-10-06/pdf/2011-25607.pdf (for FinCEN notice and request for comments to a revised Form 107).
13. 76 Fed. Reg. at 43,594.
14. 31 C.F.R. §1010.100(ff)(5)(i)(A)-(B).
15. 31 C.F.R. §1010.100(ff)(5)(i)(A). "An 'informal value transfer system' refers to any system, mechanism, or network of people that receives money for the purpose of making the funds or an equivalent value payable to a third party in another geographic location, whether or not in the same form . . . 'Hawala' is one name for a type of informal value transfer system that operates outside of, or parallel to, 'traditional' banking or financial channels." 76 Fed. Reg. at 43,592, n. 50.
16. 31 C.F.R. §1010.100(ff)(5)(ii).
17. "Persons who solely provide a clearance and settlement system or act as intermediaries between BSA regulated institutions and do not provide other types of money transmission services are mere instrumentalities that the financial institutions use to process their transfers . . . [T]hese instrumentalities, such as the credit card networks, are not included in the definition of 'money transmitter.'" 76 Fed. Reg. at 43,593.

18. FinCEN intends that both entities involved in the sale and management of stored value programs be excluded. "For example, a department store that offers gift cards that only may be used at that department store, a convenience store that sells network branded cards that may be used anywhere like a credit card, or a program manager who organizes a stored value program and facilitates loading the stored value device are not subject to the MSB rules as money transmitters." 76 Fed. Reg. at 43,594.
19. 31 C.F.R. §1010.100(ff)(5)(ii)(A)-(F). FinCEN notes that, similar to circumstance (B), "persons that sell goods or provide services other than money transmission services, and only transmit funds as an integral part of that sale of goods or provision of services, are not money transmitters. For example, brokering the sale of securities, commodity contracts, or similar instruments is not money transmission notwithstanding the fact that the person brokering the sale may move funds back and forth between the buyer and seller to effect the transaction." FinCEN also indicates that a similar limitation would apply to "a debt management company that made payments to creditors as the conduit for a negotiated schedule of payments from the debtor to its creditors." 76 Fed. Reg. at 43,594.
20. 31 C.F.R. §1010.100(ff)(1).
21. 76 Fed. Reg. at 43,589.
22. Id. at 43,590.
23. A check means: (i) a draft, other than a documentary draft, payable on demand and drawn on a bank; or (ii) a cashier's check or teller's check. An instrument may be a check even though it is described on its face by another term, such as "money order." U.C.C. §3-104(f).
24. Monetary instruments include: (i) currency; (ii) traveler's checks in any form; (iii) all negotiable instruments that are either in bearer form, endorsed without restriction, made out to a fictitious payee, or otherwise in such form that title passes upon delivery; (iv) incomplete instruments signed but with the payee's name omitted; and (v) securities or stock in bearer form or otherwise in such form that title thereto passes upon delivery. 31 C.F.R. §1010.100(dd)(1)(ii), (iii), (iv), and (v) (2011).
25. 31 C.F.R. §1010.100(ff)(2)(i).
26. 31 C.F.R. §1010.100(ff)(2)(A)-(E).
27. 76 Fed. Reg. at 43,591.
28. Id.
29. Id.
30. 31 C.F.R. §1010.100(ff)(3)(4).
31. 31 C.F.R. §1010.100(ff)(3)(i)(ii).
32. 76 Fed. Reg. at 43,591.

Corresponding author

Betty Santangelo can be contacted at: betty.santangelo@srz.com

Schulte Roth & Zabel

Schulte Roth & Zabel LLP
919 Third Avenue, New York, NY 10022
212.756.2000 tel | 212.593.5955 fax | www.srz.com
New York | Washington DC | London

To purchase reprints of this article please e-mail: reprints@emeraldinsight.com
Or visit our web site for further details: www.emeraldinsight.com/reprints